

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

**FORM 10-K**

(Mark One)

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

For the fiscal year ended December 31, 2017

OR

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

For the transition period from \_\_\_\_\_ to \_\_\_\_\_  
Commission File Number 001-36292

**NEOS THERAPEUTICS, INC.**

(Exact name of registrant as specified in its charter)

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

**2834**  
(Primary Standard Industrial Classification Code Number)

**27-0395455**  
(I.R.S. Employer Identification Number)

**2940 N. Highway 360**  
**Grand Prairie, TX 75050**  
**(972) 408-1300**

(Address, including zip code, and telephone number, including area code, of registrant's principal executive offices)

**Vipin Garg, President and Chief Executive Officer**

**Neos Therapeutics, Inc.**  
**2940 N. Highway 360**  
**Grand Prairie, TX 75050**  
**(972) 408-1300**

(Name, address, including zip code, and telephone number, including area code, of agent for service)

**Title of each class**

**Name of each exchange on which registered**

Common stock, par value \$0.001 per share

The NASDAQ Global Market

Securities registered pursuant to section 12(b) of the Act: **None**

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act.  Yes  No

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act.  Yes  No

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 if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K (§ 229.405 of this chapter) is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K.

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

Large accelerated filer

Accelerated filer

Non-accelerated filer   
(do not check if 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.

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

The aggregate market value of the registrant's voting and non-voting common stock held by non-affiliates of the registrant (without admitting that any person whose shares are not included in such calculation is an affiliate) computed by reference to the price at which the common stock was last sold on the NASDAQ Global Market on June 30, 2017 was \$194.4 million.

As of March 12, 2018, there were 28,996,956 shares of the registrant's common stock, par value \$0.001 per share, outstanding.

**DOCUMENTS INCORPORATED BY REFERENCE**

Part III incorporates certain information by reference from the registrant's Definitive Proxy Statement to be filed with the Commission pursuant to Regulation 14A in connection with the Registrant's 2018 Annual Meeting of Stockholders. Such Definitive Proxy Statement will be filed with the Commission not later than 120 days after the conclusion of the registrant's fiscal year ended December 31, 2017.

### Special note regarding forward-looking statements

This Annual Report on Form 10-K contains forward-looking statements that involve risks and uncertainties, as well as assumptions that, if they never materialize or prove incorrect, could cause our results to differ materially from those expressed or implied by such forward-looking statements. We make such forward-looking statements pursuant to the safe harbor provisions of the Private Securities Litigation Reform Act of 1995 and other federal securities laws. All statements other than statements of historical facts contained in this Annual Report on Form 10-K are forward-looking statements. In some cases, you can identify forward-looking statements because they contain words such as “may,” “will,” “should,” “expects,” “plans,” “anticipates,” “could,” “intends,” “target,” “projects,” “contemplates,” “believes,” “estimates,” “predicts,” “potential” or “continue” or the negative of these words or other similar terms or expressions that concern our expectations, strategy, plans or intentions. Forward-looking statements contained in this Annual Report on Form 10-K include, but are not limited to, statements about:

- our anticipated cash needs and our estimates regarding our anticipated expenses, capital requirements and our needs for additional financings;
- our ability to commercialize Adzenys XR-ODT, Cotempla XR-ODT and Adzenys ER or develop and commercialize any other future product or product candidate;
- the timing, cost or other aspects of the commercial launch and future sales of Adzenys XR-ODT, Cotempla XR-ODT and Adzenys ER or any other future product or product candidate;
- our ability to increase our manufacturing and distribution capabilities for Adzenys XR-ODT, Cotempla XR-ODT and Adzenys ER or any other future product or product candidate;
- the attention deficit hyperactivity disorder patient market size and market adoption of Adzenys XR-ODT, Cotempla XR-ODT and Adzenys ER by physicians and patients;
- the therapeutic benefits, effectiveness and safety of Adzenys XR-ODT, Cotempla XR-ODT and Adzenys ER or any other future product or product candidate;
- our expectations regarding the commercial supply of our Adzenys XR-ODT, Cotempla XR-ODT and Adzenys ER, or any other future products, or our generic Tussionex;
- our ability to receive, and the timing of any receipt of the U.S. Food and Drug Administration, (“FDA”), approvals, or other regulatory action in the United States and elsewhere, for any future product candidate;
- our expectations regarding federal, state and foreign regulatory requirements;
- our entry into the settlement and licensing agreement with Actavis Laboratories FL, Inc. (“Actavis”) the effect of our agreement with Actavis on its Abbreviated New Drug Application (“ANDA”), with the FDA for a generic version of Adzenys XR-ODT, and the expected timing of the manufacture and marketing of Actavis’s generic version of Adzenys XR-ODT under the ANDA;
- our product research and development activities, including the timing and progress of our clinical trials, and projected expenditures;
- issuance of patents to us by the U.S. Patent and Trademark Office and other governmental patent agencies;
- our ability to achieve profitability;
- our staffing needs; and
- the additional risks, uncertainties and other factors described under the caption “Risk Factors” in this Annual Report on Form 10-K.

We caution you that the foregoing list may not contain all of the forward-looking statements made in this Annual Report on Form 10-K.

You should not rely upon forward-looking statements as predictions of future events. We have based the forward-looking statements contained in this Annual Report on Form 10-K primarily on our current expectations and projections about future events and trends that we believe may affect our business, financial condition, results of operations and prospects. The outcome of the events described in these forward-looking statements is subject to risks, uncertainties and other factors described in “Risk Factors” and elsewhere in this Annual Report on Form 10-K. Moreover, we operate in a very competitive and rapidly changing environment. New risks and uncertainties emerge from time to time, and it is not possible for us to predict all risks and uncertainties that could have an impact on the forward-looking statements contained in this Annual Report on Form 10-K. The results, events and circumstances reflected in the forward-looking statements may not be achieved or occur, and actual results, events or circumstances could differ materially from those described in the forward-looking statements.

The forward-looking statements made in this Annual Report on Form 10-K relate only to events as of the date on which the statements are made. We undertake no obligation to update any forward-looking statements made in this Annual Report on Form 10-K to reflect events or circumstances after the date of this Annual Report on Form 10-K or to reflect new information or the occurrence of unanticipated events, except as required by law. We may not actually achieve the plans, intentions or expectations disclosed in our forward-looking statements and you should not place undue reliance on our forward-looking statements. Our forward-looking statements do not reflect the potential impact of any future acquisitions, mergers, dispositions, joint ventures or investments we may make.

Furthermore, this Annual Report on Form 10-K includes statistical and other industry and market data that we obtained from industry publications and research, surveys and studies conducted by third parties. Industry publications and third party research, surveys and studies generally indicate that their information has been obtained from sources believed to be reliable, although they do not guarantee the accuracy or completeness of such information.

**NEOS THERAPEUTICS, INC.**  
**Annual Report on Form 10-K**  
**For the Fiscal Year Ended December 31, 2017**  
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## PART I

### ITEM 1. Business

#### Overview

We are a pharmaceutical company focused on developing, manufacturing and commercializing products utilizing our proprietary modified-release drug delivery technology platform, which we have already used to develop Adzenys XR-ODT, Cotempla XR-ODT and Adzenys ER oral suspension (“Adzenys ER”), for the treatment of attention deficit hyperactivity disorder (“ADHD”). Our products are extended-release (“XR”), medications in patient-friendly, orally disintegrating tablets (“ODT”) or liquid suspension dosage forms. Our proprietary modified-release drug delivery platform has enabled us to create novel, extended-release ODT and liquid suspension dosage forms. We received approval from the U.S. Food and Drug Administration (“FDA”), for Adzenys XR-ODT, our amphetamine XR-ODT, on January 27, 2016 and launched the commercialization of this product on May 16, 2016. We received approval from the FDA for Cotempla XR-ODT, our methylphenidate XR-ODT for the treatment of ADHD in patients 6 to 17 years old, on June 19, 2017. We initiated an early experience program with limited product availability on September 5, 2017 before launching this product nationwide on October 2, 2017. Also, we received approval from the FDA for Adzenys ER, our amphetamine extended-release liquid suspension, on September 15, 2017, and launched the commercialization of this product on February 26, 2018. We believe Adzenys XR-ODT, Cotempla XR-ODT and Adzenys ER will address an unmet need by providing more patient- and caregiver-friendly dosing options not previously available to patients in the \$9.4 billion market for ADHD-indicated medications.

Our branded products incorporate two of the most commonly prescribed medications for the treatment of ADHD, methylphenidate and amphetamine. Our proprietary modified-release drug delivery platform has enabled us to create novel, extended-release ODT and liquid suspension dosage forms of these medications. We believe Adzenys XR-ODT and Cotempla XR-ODT are the first amphetamine XR-ODT and the first methylphenidate XR-ODT, respectively, for the treatment of ADHD on the market. We expect our patent estate, which we developed internally and which includes composition-of-matter, method-of-manufacture and method-of-use patents and patent applications, some of which are not scheduled to expire until 2032, will provide additional protection for our branded products.

In 2017, 72.7 million prescriptions for medications with ADHD labeling, and principally in extended-release formulations, were written in the United States. The vast majority of currently available dosage forms for ADHD are tablets and capsules. Despite once-daily dosing of these extended-release formulations, we believe there is a significant opportunity to improve compliance rates. Up to 54% of the pediatric population and 40% of the adult population have reported difficulties with swallowing tablets and capsules. We believe that the inability, difficulty or reluctance of many patients to swallow intact tablets and capsules contributes to diminished compliance rates. Such limitations highlight the need for more convenient dosing options such as ODT or liquids. To our knowledge, we are the only company that has succeeded to date in commercializing an XR-ODT formulation of any ADHD medication, even though ODT are among the most preferred dosage forms of pharmaceutical products. We believe, therefore, there is a significant market opportunity to provide two of the most prescribed medications for ADHD, methylphenidate and amphetamine, in two more convenient and patient-friendly dosage forms, ODT and liquid suspension, which we developed using our proprietary technology platform.

We are focusing on commercialization in the United States using our own commercial infrastructure. We currently have a specialty sales force of approximately 125 representatives targeting the highest-volume prescribers of ADHD medication. We manufacture Adzenys XR-ODT, Cotempla XR-ODT and Adzenys ER in our current Good Manufacturing Practice (“cGMP”) and U.S. Drug Enforcement Administration (“DEA”) -registered manufacturing facilities, thereby obtaining our

products at cost without manufacturer's margins and better controlling supply, quality and timing. We also currently use these facilities to manufacture our generic equivalent to the branded product, Tussionex, an XR liquid suspension of hydrocodone and chlorpheniramine indicated for the relief of cough and upper respiratory symptoms of cold.

We believe we can apply our XR-ODT and XR liquid suspension technologies that underlie our branded products and our generic Tussionex to other active pharmaceutical ingredients ("APIs") as well. Our longer-term strategy is to utilize these technologies for the development and approval of additional XR-ODT or XR liquid suspension drug candidates, while leveraging our manufacturing and commercialization experience to reduce costs and effectively reach patients. Patients with central nervous system ("CNS") conditions, such as stroke, Parkinson's disease and Alzheimer's disease often have difficulty swallowing their medication and would benefit from ODT and liquid suspension dosage forms. We have completed feasibility studies on several potential product candidates thus far. After completing feasibility work on approximately a dozen potential product candidates by mid-2018, we plan to select two to three candidates for further clinical development. We intend to utilize the regulatory pathway provided by Section 505(b)(2) of the Federal Food, Drug, and Cosmetic Act (the "505(b)(2) regulatory approval pathway"), for our product candidates using only APIs from approved drug products and incorporating our proprietary drug delivery platform to create branded product candidates. This streamlined development and approval pathway should allow us to initiate clinical trials in approximately 18 months after drug discovery and submit an NDA in as few as 36 months.

Our total revenues increased to \$25.0 million for the year ended December 31, 2017, from \$9.2 million for the year ended December 31, 2016 and \$3.8 million for the year-ended December 31, 2015, all of which was generated in the United States.

## OUR STRATEGY

Our goal is to be a leading pharmaceutical company focused on the development, manufacture and commercialization of pharmaceutical products that utilize our proprietary modified-release drug delivery technology platform. Key elements of our business strategy to achieve this goal are to:

- **Leverage our sales force and commercial infrastructure in the United States for Adzenys XR-ODT, Cotempla XR-ODT and Adzenys ER with any of our other product candidates that we may develop that are FDA approved.**

We believe that we can effectively commercialize Adzenys XR-ODT, Cotempla XR-ODT and Adzenys ER in the United States with a specialty sales force of approximately 125 representatives. We intend to target the highest volume prescribers to address the unmet need for more patient- and caregiver-friendly dosage forms of the two most prescribed medications in the \$9.4 billion market for ADHD-indicated medications. We plan to commercialize our products outside of the United States after receiving the required approvals in those countries through partnerships and collaborations.

- **Manufacture our proprietary products in our cGMP, FDA-inspected and DEA-registered manufacturing facilities.**

We believe our manufacturing facilities and years of manufacturing experience are a competitive advantage. We intend to leverage the economic efficiencies afforded by manufacturing our ADHD products in our cGMP and DEA-registered manufacturing facilities. We believe that we will have sufficient capacity to supply commercial quantities for all of our ADHD products.

- **Utilize our proprietary technology platform to develop additional branded product candidates in CNS and other therapeutic areas with unmet need.**

We intend to expand our branded product portfolio by identifying existing pharmaceutical products that could be improved upon by utilizing our proprietary modified-release drug delivery technology platform. We plan to focus our development efforts on approved drug products for which we believe we can secure composition-of-matter patent protection and utilize the 505(b)(2) regulatory approval pathway. We plan to explore product opportunities in several therapeutic areas, including CNS and gastrointestinal indications.

- **Continue to expand our robust intellectual property portfolio covering our novel modified-release drug delivery technology platform and innovative products.**

We have built a three-tier patent estate consisting of composition-of-matter, method-of-manufacture and method-of-use patents and patent applications. We intend to extend our patent portfolio as we continue to expand upon our drug delivery technologies and identify and develop additional branded product candidates. If issued and listed in the FDA's publication of approved drug products with therapeutic equivalence evaluations (the "Orange Book"), we believe that these patents will provide additional market protection for our FDA-approved products.

## **ADHD**

### **Market and current treatment options**

ADHD is a neurobehavioral disorder characterized by a persistent pattern of inattention and/or hyperactivity/impulsivity that interferes with functioning and/or development. ADHD can have a profound impact on an individual's life, causing disruption at school, work, and home and in relationships. It is one of the most common developmental disorders in children and often persists into adulthood. In 2011, an estimated 11% of children in the United States ages 4 to 17 had previously received an ADHD diagnosis. A 2006 study estimated 4.4% of adults in the United States experience ADHD symptoms. Current ADHD treatment guidelines recommend a multi-faceted approach that uses medications in conjunction with behavioral interventions.

In 2017, 72.7 million prescriptions for medications with ADHD labeling were written in the United States and generated \$9.4 billion in sales. Approximately 92% of these prescriptions were for stimulant medications, such as methylphenidate and amphetamine, which have been the standard of care for several decades. Methylphenidate and amphetamine prescriptions generated \$3.2 billion and \$5.4 billion in sales, respectively, in 2017 in the United States. A few non-stimulant medications are also available, but evidence of their efficacy for treating ADHD symptoms is less compelling. The market for ADHD medications outside of the United States is less developed, but we believe it will continue to grow as recognition and awareness of the disorder increase.

### **Limitations of existing treatment options**

Extended-release, or long acting, dosage forms of stimulant medications are the standard of care for treating ADHD, making up approximately 55% of ADHD prescriptions. Most of these extended-release dosage forms allow for once-daily dosing in the morning, which eliminates the need to re-dose during the day. However, even with once-daily dosing, there is great potential for improvement. The vast majority of currently available dosage forms for ADHD are tablets and capsules. We believe that the inability, difficulty or reluctance of many patients to swallow intact tablets and capsules contributes to diminished compliance rates.

Up to 54% of the pediatric population has difficulty swallowing tablets and capsules, and this can be especially problematic in children with ADHD. For many of these patients, swallowing difficulties can persist into adolescence and adulthood, with 40% of adults reporting pill-swallowing difficulties that

result in skipping doses or discontinuing their medication altogether. In addition, ADHD medications are typically administered in the morning, which is often the busiest and most chaotic period for families.

Some extended-release products do offer alternative dosing options, such as opening the capsule to sprinkle contents over food, but labeling for these products generally includes a caveat that such manipulation may impair the efficacy and/or safety of the product. These alternatives may also be difficult or inconvenient for the caregiver and disruptive to an already difficult and chaotic morning routine. Thus, a significant need remains for more patient- and caregiver-friendly dosage forms of ADHD medications in once-daily dosing forms.

### **Market receptivity to novel dosage forms for the treatment of ADHD**

The most prescribed extended-release medications for ADHD, Concerta® and Adderall XR® (and each of their generic equivalents), are long-acting versions of previously short-acting methylphenidate and amphetamine medications, respectively. While these products address the need for once-daily dosing, Concerta and Adderall XR are only available as tablets and capsules, respectively, and may be difficult for some patients to swallow.

This limitation led to the development of a transdermal methylphenidate patch, Daytrana®. While the methylphenidate transdermal patch offered a non-oral delivery method, it created additional issues related to dose variability, patch placement and premature patch removal. Adverse events such as skin irritation and accidental exposure from discarded patches also deterred Daytrana's utilization. Despite these shortcomings, Daytrana achieved approximately a 3% share of the overall methylphenidate extended-release market in 2014.

In January 2013, an extended-release liquid formulation of methylphenidate, Quillivant XR™, was launched by Pfizer, providing a new dosing option. In April 2016, Pfizer launched Quillichew ER™, an extended-release chewable formulation of methylphenidate and Tris Pharmaceuticals launched an extended-release liquid formulation of amphetamine, Dyanavel XR™. In 2017, Quillivant XR had approximately 627,000 prescriptions and gross sales of approximately \$193.3 million. Quillivant XR had captured a 0.9% share of the ADHD market in the fourth quarter of 2017 prior to a drug shortage issue at the end of year.

We launched commercialization of our amphetamine extended-release ODT, Adzenys XR-ODT, on May 16, 2016 and initiated an early experience program with Cotelma XR-ODT with limited product availability on September 5, 2017 and launched this product nationwide on October 2, 2017. We had 187,685 and 12,721 total equivalent unit prescriptions for Adzenys XR-ODT and Cotelma XR-ODT, respectively, generating \$55.2 million and \$4.1 million in gross sales, respectively, in 2017, including Adzenys XR-ODT gross sales of \$18.5 million in the fourth quarter of 2017. From the launch of Adzenys XR-ODT in May 2016 through December 31, 2016, we had 30,339 equivalent unit prescriptions, generating \$8.2 million in gross sales. Adzenys XR-ODT captured a 0.3% share of the ADHD market in the fourth quarter of 2017.

The market acceptance of these novel formulations, despite their limitations, further demonstrates the significant unmet need and opportunity for novel, patient- and caregiver-friendly dosage forms in the treatment of ADHD. We believe that XR-ODT and XR liquid suspension would be preferred and clinically beneficial dosage forms for the treatment of ADHD patients with swallowing aversion. In a survey commissioned by us, when asked to project their next 100 dextroamphetamine/amphetamine prescriptions, a sample of 51 pediatricians and psychiatrists said they would prescribe a once-daily controlled-release ODT dextroamphetamine/amphetamine four times as often as they would prescribe a once-daily controlled-release liquid dextroamphetamine/amphetamine (13.3 vs. 3.4 out of their next 100 ADHD patients receiving dextroamphetamine/amphetamine). In a study of adult patients with a CNS disorder, 61% of patients chose an ODT, in comparison with 27% who chose a conventional



tablet and 12% who were indifferent. However, to our knowledge, we are the first company to date to commercialize an XR-ODT formulation of any ADHD medication. We believe there is a significant market opportunity to provide the two most prescribed medications for ADHD, methylphenidate and amphetamine, in two patient-friendly dosage forms, ODT and liquid suspension.

### **Our product and product candidates address an unmet need for ADHD patients**

Our proprietary modified-release drug delivery technology platform has enabled us to create XR-ODT and XR liquid suspension formulations of methylphenidate and amphetamine. We have achieved this by combining two key drug delivery attributes in each of our products:

- An extended-release profile, which allows for once daily dosing; and
- An ODT or liquid suspension dosage form, which allows for easier administration and ingestion.

We have developed two XR-ODT products and an XR liquid suspension product, each of which addresses an unmet need. Adzenys XR-ODT and Cotempla XR-ODT are the first XR-ODT products for the treatment of ADHD. We believe that our XR-ODT products have unique attributes to improve compliance and could offer significant advantages over other solid oral dosage forms that can help simplify the morning routine in households with ADHD-diagnosed children. These advantages include:

- Ease of administration and ingestion because they disintegrate rapidly in the mouth and may be taken without water;
- Taste-masking of bitter ADHD medications, with flavoring options;
- Prevention of “cheeking”, the practice of hiding medication in the mouth and later spitting it out rather than swallowing it; and
- Convenient single-unit blister-packaging, which is both portable and discrete.

Adzenys ER is a ready-to-use, XR liquid suspension that does not require reconstitution or refrigeration, and offers an attractive dosing option for younger children who prefer to ingest liquid medicine.

We believe that an XR-ODT, such as Adzenys XR-ODT and Cotempla XR-ODT, and an XR liquid suspension, such as Adzenys ER, may solve the swallowing issue that undermines compliance with tablet and capsule medication regimens.

### **OUR CURRENTLY MARKETED PRODUCTS**

Utilizing our proprietary modified-release drug delivery technology platform, we currently manufacture and market our Adzenys XR-ODT, Cotempla XR-ODT, Adzenys ER and our generic Tussionex. We are in the early stages of discovering and developing future product candidates for which we intend to seek FDA approval in accordance with Section 505(b)(2). The table below summarizes our pipeline of currently marketed products.

<b>Product</b>	<b>Active Drug and Indication</b>	<b>Formulation</b>	<b>Status</b>
Adzenys XR-ODT	Amphetamine for ADHD	XR-ODT	Approved and marketed
Cotempla XR-ODT	Methylphenidate for ADHD	XR-ODT	Approved and marketed
Adzenys ER	Amphetamine for ADHD	XR Liquid Suspension	Approved and marketed
Generic Tussionex	Hydrocodone and chlorpheniramine for cough and upper respiratory symptoms of a cold	XR Liquid Suspension	Approved and marketed

The 505(b)(2) regulatory approval pathway allows for a potentially streamlined and targeted clinical development program. During the development process, we communicated with the FDA on

several occasions and received feedback on our clinical development plans for our currently marketed products. In general, our clinical development program for our branded products comprised single-dose clinical pharmacology studies, each designed to evaluate the bioequivalence and bioavailability of these dosage forms under different test conditions. Each product was studied in adult volunteers and children with ADHD. In addition, a clinical efficacy and safety trial in children with ADHD was conducted for Cotempla XR-ODT, our methylphenidate XR-ODT. During each phase of the clinical trials, safety and tolerability were systematically assessed. A summary of each program is presented below. For the purposes of our clinical trials, unless otherwise indicated, we refer to children as individuals ages 6 to 12, adolescents as individuals ages 13 to 17, and adults as individuals 18 and older.

### **Adzenys XR-ODT: Amphetamine XR-ODT for the treatment of ADHD**

We received approval from the FDA for Adzenys XR-ODT, our amphetamine XR-ODT, on January 27, 2016. We believe Adzenys XR-ODT is the first amphetamine XR-ODT for the treatment of ADHD. Our NDA for Adzenys XR-ODT relies on the efficacy and safety data that formed the basis of FDA approval for the listed drug, Adderall XR, 30 mg, together with bioequivalence, bioavailability and aggregate safety data from our Adzenys XR-ODT clinical program.

Adzenys XR-ODT contains amphetamine loaded onto a mixture of immediate-release and polymer-coated delayed-release resin particles, which are formulated and compressed into an ODT along with other typical tableting excipients using our patented RDIM technology. The result is amphetamine with an *in vivo* extended-release profile delivered through a tablet that quickly disintegrates in the mouth without the need for water. We offer Adzenys XR-ODT in 30-day supply, child-resistant blister packs. We have composition-of-matter patents for Adzenys XR-ODT that are scheduled to expire in 2026 and 2032. These patents are listed in the Orange Book, which we believe will provide additional protection for Adzenys XR-ODT. In addition, we entered into a Settlement Agreement and a Licensing Agreement (collectively, the “Agreement”) with Actavis Laboratories FL, Inc. (“Actavis”) which resolves all ongoing litigation involving our Adzenys XR-ODT patents and Actavis’s Abbreviated New Drug Application (“ANDA”) with the FDA for a generic version of Adzenys XR-ODT. Under the Agreement, we granted Actavis the right to manufacture and market its generic version of Adzenys XR-ODT under the ANDA beginning on September 1, 2025, or earlier under certain circumstances.

### **Adzenys XR-ODT commercialization**

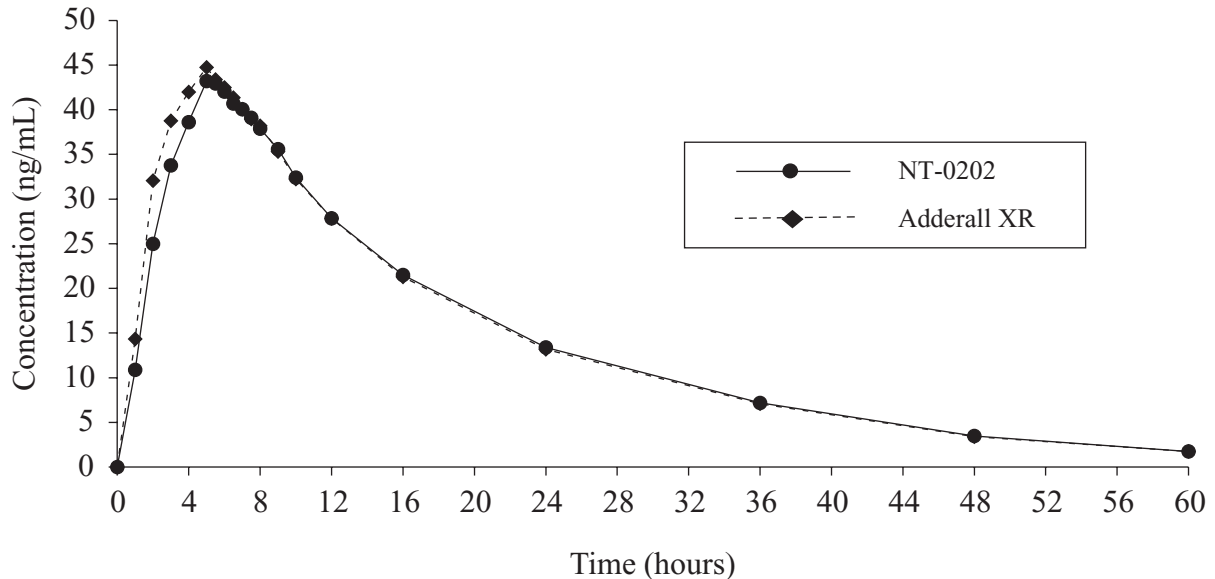
We launched the commercialization of Adzenys XR-ODT on May 16, 2016 and are commercializing this product in the United States with our own infrastructure. We are using a dedicated contract specialty sales force in approximately 125 territories targeting approximately 12,500 physicians who prescribe approximately 40% of all ADHD prescriptions. Through December 2017, we had 218,024 total prescriptions, including 187,685 prescriptions in 2017. The number of prescribers of Adzenys XR-ODT continues to grow, and as of December 31, 2017, 10,870 health care providers had written prescriptions for the product.

### **Adzenys XR-ODT clinical program**

The clinical program for Adzenys XR-ODT consisted of five Phase 1 single-dose human pharmacokinetic studies under fasted and/or fed conditions. Four of the five single-dose clinical studies were submitted to the FDA with the original NDA in December 2012. The fifth study was conducted using commercial-scale material, and was included in our resubmission to the FDA. The four original studies were a Phase 1 bioequivalence study versus Adderall XR, 30 mg, in healthy adult volunteers under fasted conditions; a Phase 1 bioavailability study in healthy adult volunteers under both fed and fasted conditions; a Phase 1 study to determine the impact of alcohol on the bioavailability of Adzenys XR-ODT; and a bioavailability study in children with ADHD under fasted conditions.

The data from the pilot-scale bioequivalence study versus Adderall XR, 30 mg, is shown in Figure 1 and shows that Adzenys XR-ODT is bioequivalent to the listed drug, Adderall XR, 30 mg, under fasted conditions.

**Figure 1: Bioequivalence Study of Adzenys XR-ODT versus Adderall XR, 30 mg, in Healthy Adult Volunteers under Fasted Conditions**



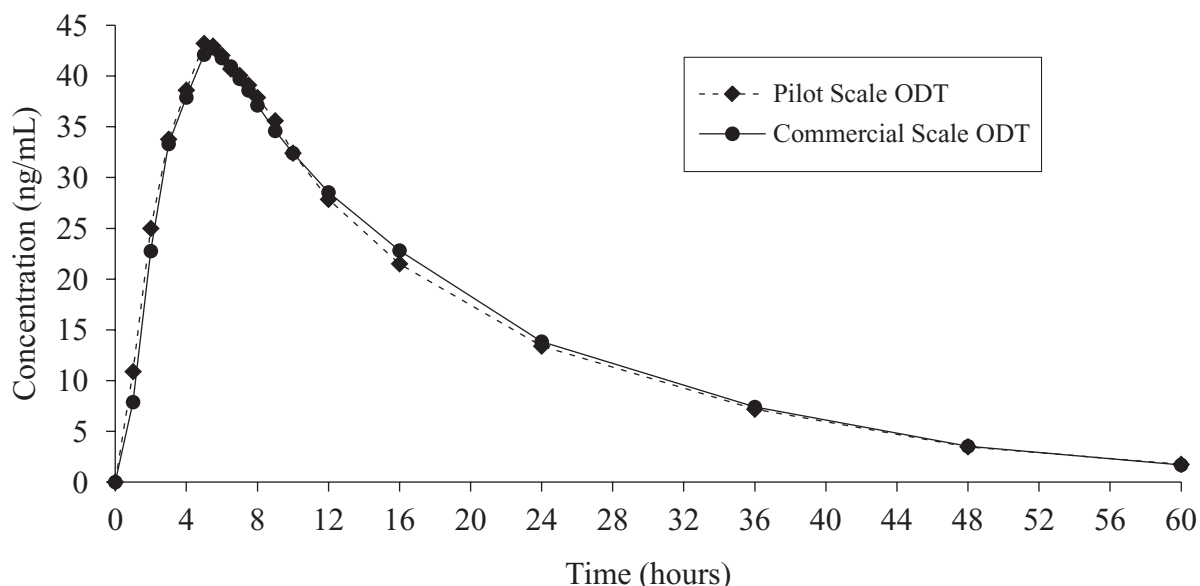
Other key observations from our original clinical program for Adzenys XR-ODT included:

- *No alcohol dose-dumping:* The extended-release properties of Adzenys XR-ODT were maintained in the presence of varying concentrations of alcohol, indicating that Adzenys XR-ODT is a “rugged” formulation that does not cause premature and intentional release of the drug product, or dose-dump, in the presence of alcohol.
- *Similar exposure rate:* Consistent with the listed drug, there was a higher mean amphetamine exposure in children, which decreased with increasing age.
- *Safety and Tolerability:* There were no unexpected adverse events, serious adverse events, deaths or other safety signals. The aggregate data suggested that Adzenys XR-ODT has a similar safety profile to that of the listed drug and is well-tolerated.

Following the receipt of a Complete Response Letter, we received feedback from the FDA on the design of an additional bioequivalence and bioavailability study of Adzenys XR-ODT produced at commercial scale to support the NDA resubmission. This study was designed to compare the pharmacokinetic profile of the commercial-scale product to the listed drug in adult volunteers under fasted conditions; compare the pilot-scale manufacturing batches to the commercial-scale batches; and evaluate the oral bioavailability of Adzenys XR-ODT under fed and fasted conditions in adult volunteers.

The bioequivalence data for the commercial-scale product demonstrated that Adzenys XR-ODT has a similar pharmacokinetic profile to the listed drug under fasted conditions, meeting bioequivalence criteria for key exposure parameters ( $AUC_{5-t}$ ,  $C_{max}$ ,  $AUC_{last}$ , and  $AUC_{inf}$ ). The lower 90% confidence interval for early exposure ( $AUC_{0-5}$ ) of Adzenys XR-ODT produced at commercial scale fell just below the 80% lower criterion when compared to the listed drug. However, the concentration-time profiles for Adzenys XR-ODT produced at commercial scale and pilot scale are virtually identical, as shown in Figure 2, indicating that scale-up of the Adzenys XR-ODT process did not affect the rate and extent of absorption of amphetamine.

**Figure 2: Comparison of Adzenys XR-ODT Pilot Scale versus Adzenys XR-ODT Commercial Scale**



Our settlement agreement with Shire Pharmaceuticals (“Shire”), the producer of Adderall XR, precluded the possibility of a 30-month stay of approval under the Drug Price Competition and Patent Term Restoration Act of 1984, commonly known as the Hatch-Waxman Amendments.

We have committed to the FDA to conduct the following three trials as a post-marketing requirement after approval of the Adzenys XR-ODT NDA: 1) a single-dose, open-label, randomized pharmacokinetic study of Adzenys XR-ODT (amphetamine extended-release orally disintegrating tablets), in male and female children (4 to less than 6 years of age) with ADHD; 2) a randomized, double-blind, placebo-controlled, flexible-dose titration study of Adzenys XR-ODT (amphetamine extended-release orally disintegrating tablets), in children ages 4 to 5 years diagnosed with ADHD; and 3) a one year Pediatric Open-Label Safety Study of patients age 4 to 5 years (at the time of entry into the second study, or at the time of enrollment if directly enrolled into this study) diagnosed with ADHD treated with Adzenys XR-ODT (amphetamine extended-release orally disintegrating tablets). We met with FDA officials in January 2017 to further clarify the design of the protocols required to conduct these studies. We commenced the program beginning with the pharmacokinetics trial in 2017.

#### **Cotempla XR-ODT: Methylphenidate XR-ODT for the treatment of ADHD**

We received approval from the FDA for Cotempla XR-ODT, our methylphenidate XR-ODT for the treatment of ADHD in patients 6 to 17 years old, on June 19, 2017. We believe Cotempla XR-ODT is the first methylphenidate XR-ODT for the treatment of ADHD, providing onset-of-effect within one hour and a 12-hour duration. Our Cotempla XR-ODT NDA relies on the efficacy and safety data that formed the basis of FDA approval for the listed drug, Metadate CD®, together with bioavailability/bioequivalence data and efficacy/safety data from our Cotempla XR-ODT clinical program.

Cotempla XR-ODT contains methylphenidate loaded onto a mixture of immediate-release and polymer-coated delayed-release resin particles, which are formulated and compressed into an ODT along with other typical tableting excipients using our patented rapidly disintegrating ionic masking, or RDIM, technology. The result is methylphenidate with an *in vivo* extended-release profile delivered through a tablet that quickly disintegrates in the mouth. We offer Cotempla XR-ODT in 30-day supply, child-resistant blister packs. We have composition-of-matter patents in the U.S. which we expect will

provide Cotempla XR-ODT intellectual property protection until 2032. These patents are listed in the Orange Book, which we believe will provide additional market protection for Cotempla XR-ODT. In addition, Cotempla XR-ODT has an FDA marketing exclusivity period of three years which bars approval of an ANDA.

### **Cotempla XR-ODT commercialization**

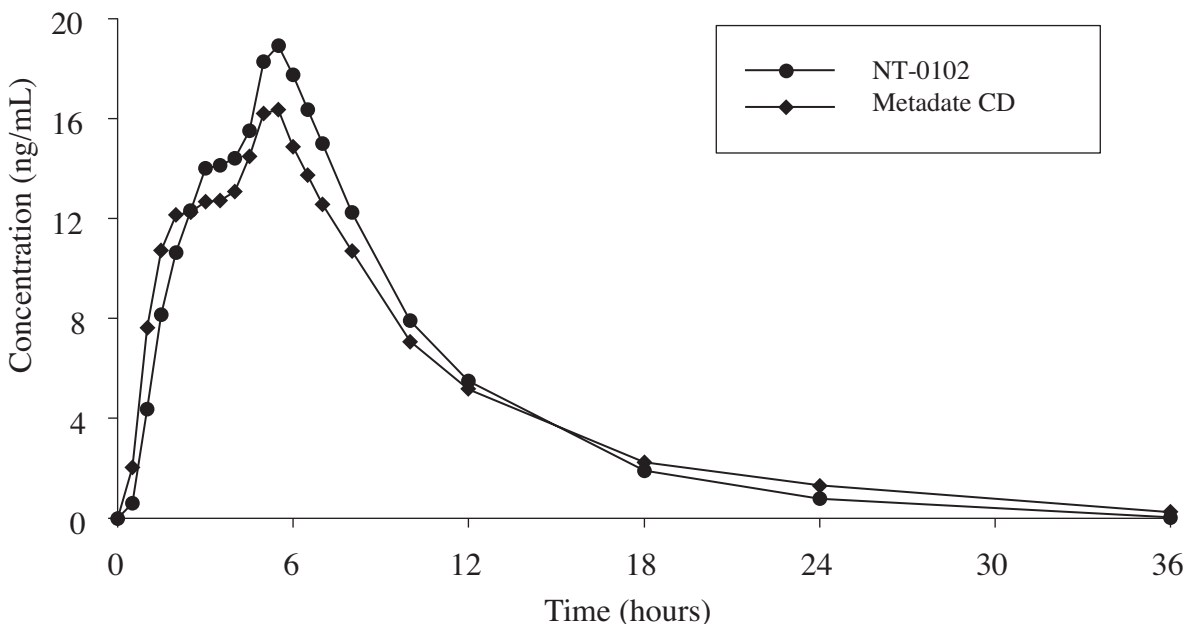
We initiated an early experience program with limited product availability for Cotempla XR-ODT on September 5, 2017 before launching this product nationwide on October 2, 2017 and are commercializing this product in the United States with our own infrastructure. We are using the same dedicated contract specialty sales force that we are using for our commercialization of Adzenys XR-ODT, and have sales professionals in approximately 125 territories targeting approximately 12,500 physicians who prescribe approximately 40% of all ADHD prescriptions. Through December 2017, we had 12,721 total prescriptions. The number of prescribers of Cotempla XR-ODT continues to grow, and as of December 31, 2017, 1,949 health care providers had written prescriptions for the product.

### **Cotempla XR-ODT Clinical Program**

The clinical program for Cotempla XR-ODT consists of four Phase 1 clinical pharmacology studies and a Phase 3 clinical efficacy and safety trial. Three of the clinical pharmacology studies were previously completed. They were single-dose pharmacokinetic studies conducted under fasted and/or fed conditions: a Phase 1 bioequivalence study versus Metadate CD in healthy adult volunteers under fasted conditions; a Phase 1 bioavailability study in healthy adult volunteers under both fed and fasted conditions; and a Phase 1 bioavailability study in children and adolescents with ADHD under fasted conditions. A fourth clinical pharmacology study, which was designed to be a Phase 1 bioequivalence study, demonstrated equivalence between our clinical trial formulation and our to-be-marketed formulation in healthy adult volunteers under fed and fasted conditions and was completed in July 2016. On July 28, 2016, we announced that we had completed the bridging study demonstrating that the Cotempla XR-ODT to-be-marketed drug product met all of the primary and secondary endpoints for establishing bioequivalence under fasted conditions. The NDA includes results from our Phase 3 clinical efficacy and safety study that showed a statistically significant improvement in ADHD symptom control compared to placebo across the classroom day. Onset of effect was observed within one hour post-dose and persisted through 12 hours. No serious adverse events were reported during the study and the adverse event profile was consistent with the drug's mechanism of action. In addition, data from a pharmacokinetic study in children with ADHD was submitted.

The data from our bioequivalence study versus Metadate CD is presented in Figure 3, and shows that Cotempla XR-ODT has a similar plasma concentration-time profile to the listed product, Metadate CD, with a peak exposure that is about 25% higher. The potential efficacy benefits of this increased maximum exposure, as well as any impact on safety parameters, were evaluated in a clinical efficacy and safety trial.

**Figure 3: Bioequivalence Study of Cotempla XR-ODT versus Metadate CD, 60 mg, in Healthy Adult Volunteers under Fasted Conditions**



Other key observations from the Cotempla XR-ODT clinical pharmacology program included:

- *No formulation-related food effect:* The pharmacokinetic profile of Cotempla XR-ODT was similar under fed and fasted conditions.
- *Similar exposure rate:* There was higher mean methylphenidate exposure in children, which decreased with increasing age.
- *Safety and tolerability:* There were no unexpected adverse events, serious adverse events, deaths or other safety signals. The aggregate data suggested that Cotempla XR-ODT has a similar safety profile to that of the listed drug and is well-tolerated.

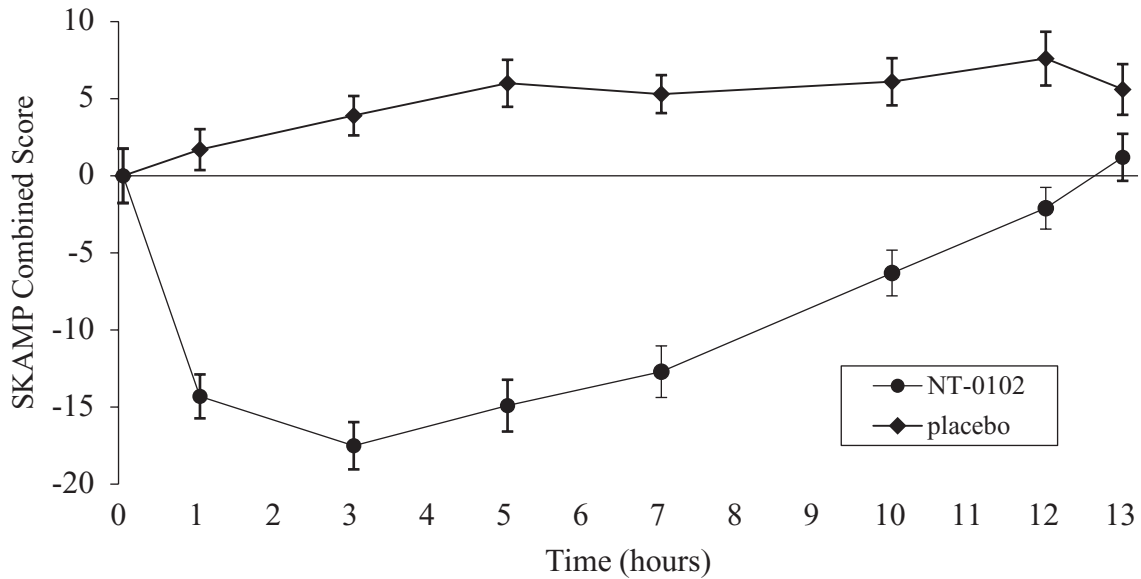
### **Cotempla XR-ODT Phase 3 classroom efficacy and safety trial**

The efficacy, safety and tolerability of Cotempla XR-ODT were evaluated in a multicenter, double-blind, placebo-controlled laboratory classroom trial in 87 children with ADHD. The laboratory classroom was a controlled study environment designed to model the community school classroom setting while allowing detailed assessments of behavior over time by trained observers. The primary efficacy variable was the Swanson, Kotkin, Agler, M-Flynn and Pelham, or SKAMP, Combined Score, a validated rating of attention and behavior, averaged over the test day, with higher scores indicating a higher degree of functional impairment. Time to onset and duration of effect were also evaluated as key secondary endpoints. Additional secondary efficacy endpoints included the Permanent Product Measure of Performance, or PERMP, a ten-minute, level-adjusted math test that measures the child's ability to focus on written schoolwork by determining the number of problems attempted and the number answered correctly.

Cotempla XR-ODT met the primary and key secondary efficacy endpoints, showing statistically significant improvement versus placebo on the SKAMP ( $p < 0.0001$ ). Statistical significance expresses the probability that the results of a particular study could have occurred purely by chance. Results are said to be statistically significant when the p-value obtained is less than the pre-established significance level,

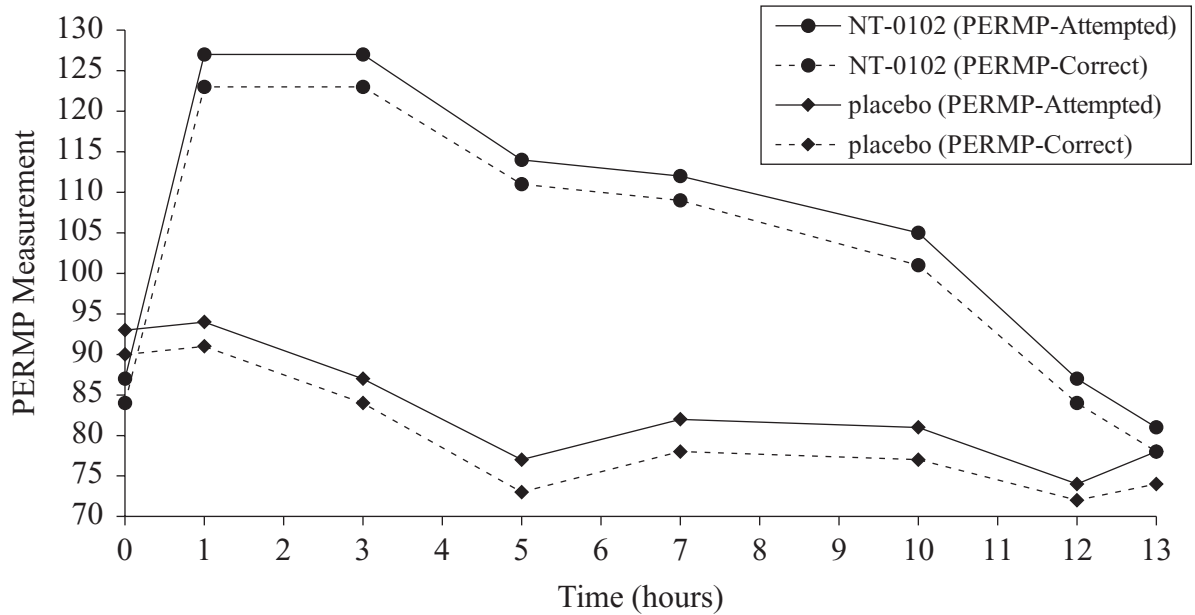
which in this case was  $p < 0.05$  for the primary efficacy endpoint. The SKAMP-Combined score averaged over the classroom testing day was 25.3 for the placebo group and 14.3 in the Cotempla XR-ODT group indicating greater symptom severity in the placebo group. The least squares mean difference was  $-11.04$ . Figure 4 shows SKAMP-Combined Scores for Cotempla XR-ODT versus placebo over the classroom day from our Phase 3 efficacy trial. Time to onset was observed within one hour, with a 12-hour duration of effect.

**Figure 4: Change from Baseline in Mean SKAMP Score During the Test Day**



Statistically significant improvement versus placebo was also observed on both attempted and correct PERMP scales ( $p < 0.0001$ ). Figure 5 shows PERMP scores for Cotempla XR-ODT versus placebo from our Phase 3 classroom efficacy trial. Taken together, the data demonstrate clinically meaningful differences on both the rater-evaluated assessment of attentiveness and behavior and the objective measure of sustained attention.

**Figure 5: Mean Profiles for PERMP Measurements During the Test Day**



All of the other secondary endpoints were also statistically significant, indicating a robust effect of the drug, as well as internal consistency in the study results. There was no impact on safety parameters as Cotempla XR-ODT was well-tolerated with no unexpected adverse events, serious adverse events, deaths or other safety signals.

**Bridging Study: Bioequivalence Between Clinical Trial Formulation and Commercial Formulation**

The objective of this study was to compare the rate of absorption and oral bioavailability of the previously studied clinical trial formulation of Cotempla XR-ODT 60 mg (2 × 30 mg) under fasted conditions to the commercial scale formulation of Cotempla XR-ODT 60 mg (2 × 30 mg) under fasted conditions. Additionally, the rate of absorption and oral bioavailability of the commercial scale formulation of Cotempla XR-ODT 60 mg (2 × 30 mg) under fed and fasted conditions was compared.

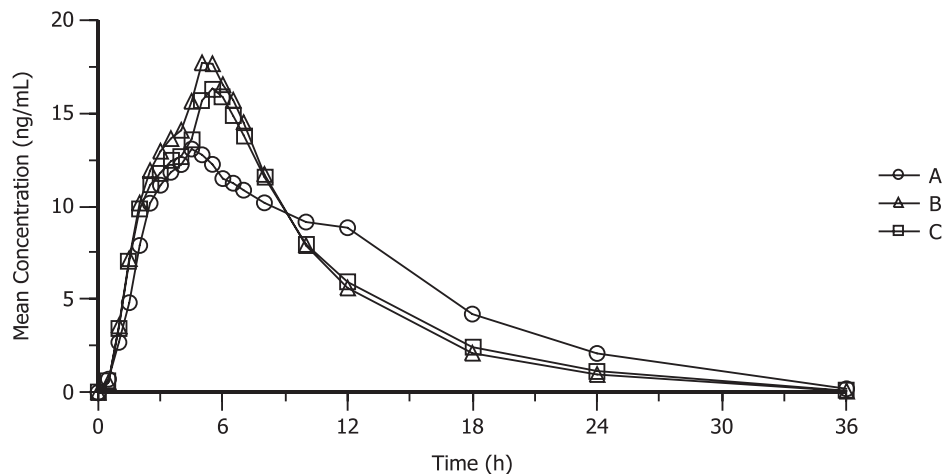
The results from the bioequivalence study bridging the clinical trial lot used in the Cotempla XR-ODT clinical trial program and the commercial lot are presented in Figure 6 below. Key findings from this study are:

- The clinical trial formulation of Cotempla XR-ODT is bioequivalent to the commercial formulation of Cotempla XR-ODT under fasted conditions.
- Peak exposure is decreased slightly (approximately 23%) in the presence of a high-fat meal; however, overall systemic.



**Fig. 6 Bioequivalence Study of Cotempla XR-ODT Clinical vs. Commercial Scale Lot in Healthy Adult Volunteers**

Analyte=DMETH+LMETH



*Treatment A = Cotempla XR-ODT Commercial Scale Lot (Fed); Treatment B = Cotempla XR-ODT Commercial Scale Lot (Fasted); Treatment C = Cotempla XR-ODT Clinical Scale Lot (Fasted)*

Our 505(b)(2) application for Cotempla XR-ODT referenced the FDA's previous findings of safety and effectiveness for Metadate CD. The NDA submission included a Paragraph IV certification notification to UCB, Inc., or UCB, the NDA holder of Metadate CD, in accordance with the Hatch-Waxman Amendments. UCB has acknowledged that they will not initiate a suit against us, and the 45-day period following Paragraph IV notification has since passed which precluded the possibility of a 30-month stay of approval under the Hatch-Waxman Amendments.

We have committed to the FDA to conduct the following three trials as a post-marketing requirement after approval of the Cotempla XR-ODT NDA: 1) a single-dose, open-label, randomized pharmacokinetic study of Cotempla XR-ODT (methylphenidate extended-release orally disintegrating tablets), in male and female children (4 to less than 6 years of age) with ADHD; 2) a randomized, double-blind, placebo-controlled, flexible-dose titration study of Cotempla XR-ODT (methylphenidate extended-release orally disintegrating tablets), in children ages 4 to 5 years diagnosed with ADHD; and 3) a 6-month Pediatric Open-Label Safety Study of patients age 4 to 5 years (at the time of entry into the second study, or at the time of enrollment if directly enrolled into this study) diagnosed with ADHD treated with Cotempla XR-ODT (methylphenidate extended-release orally disintegrating tablets). We expect to commence with the pharmacokinetics trial in 2018.

#### **Adzenys ER: Amphetamine XR liquid suspension for the treatment of ADHD**

We received approval from the FDA for Adzenys ER, our amphetamine extended-release liquid suspension, on September 15, 2017. There are no post-marketing requirements for this product.

In addition to the clinical trial program outlined below, we conducted two additional bioequivalence studies for Adzenys ER, in support of the NDA: a bridging study of our clinical trial material and our to-be-marketed drug material, which examined the effect of a high-fat meal on the commercial formulation, and a bioequivalence study of the commercial formulation versus Adderall XR 30 mg.

Adzenys ER contains amphetamine loaded onto a mixture of immediate-release and polymer coated delayed-release resin particles, and using our patented dynamic time release suspension, or DTRS, technology, we are able to create an amphetamine XR liquid suspension. Adzenys ER is designed to be shelf stable for 24 months, without requiring refrigeration or reconstitution. We have composition-of-matter patents for Adzenys ER that are scheduled to expire in 2032. These patents are listed in the Orange Book, which we believe will provide additional market protection for Adzenys ER.

### Adzenys ER commercialization

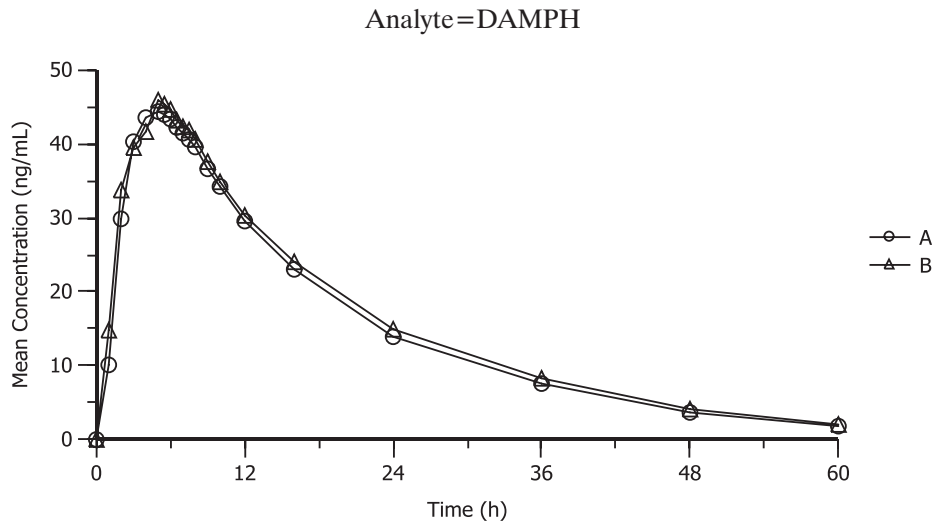
We launched the commercialization of Adzenys ER on February 26, 2018 and are commercializing this product in the United States with our own infrastructure. We are using the same dedicated contract specialty sales force that we are using for our commercialization of Adzenys XR-ODT and Cotempla XR-ODT, and have sales professionals in approximately 125 territories targeting approximately 12,500 physicians who prescribe approximately 40% of all ADHD prescriptions.

### Adzenys ER clinical program

The bioavailability/bioequivalence of Adzenys ER has been characterized in five Phase 1 clinical studies: a Phase 1 study investigating the bioavailability and bioequivalence of three test formulations of Adzenys ER in healthy adults; a Phase 1 study comparing the pharmacokinetic, or PK, profile of the commercial scale formulation of Adzenys ER to Adderall XR 30 mg capsules; a Phase 1 food effect study of Adzenys ER in healthy adults; a Phase 1 study comparing the commercial scale and clinical trial formulations of Adzenys ER under fasted conditions, as well as the effect of food on the PK profile of the commercial scale formulation of Adzenys ER; and a Phase 1 PK study of Adzenys ER in children with ADHD.

The data from our most recent bioequivalence study versus Adderall XR is shown in Figure 7 and shows that the commercial scale formulation of Adzenys ER is bioequivalent to the listed drug, Adderall XR, 30 mg, under fasted conditions.

**Figure 7: Mean *d*-amphetamine Concentration-Time Profiles after Administration of AMP XR OS (Treatment A) and Adderall XR 30 mg (Treatment B)**



*Treatment A = Adzenys ER (30 mg/15 mL); Treatment B = Adderall XR 30 mg capsule*

Other key observations from our clinical program for Adzenys ER included:

- *No significant food effects:* When administered under fasted and fed conditions, no significant food effects were observed for Adzenys ER, and the observed food effects of Adzenys ER were less than those for the listed drug.
- *Similar exposure rate:* Consistent with the listed drug, there was a higher mean amphetamine exposure in children, which decreased with increasing age.
- *Safety and Tolerability:* There were no unexpected adverse events, serious adverse events, deaths or other safety signals. The aggregate data suggested that Adzenys ER has a similar safety profile to that of the listed drug and is well-tolerated.

We included a Paragraph IV certification in the NDA submission, which required a Paragraph IV certification notification to the producer of Adderall XR, Shire Pharmaceuticals, in accordance with the Hatch-Waxman Amendments. On March 6, 2017, we entered into a license agreement with Shire, pursuant to which Shire granted us a non-exclusive license to certain patents owned by Shire for certain activities with respect to Adzenys ER. Under the terms of the agreement, we paid a lump sum, non-refundable license fee of an amount less than \$1.0 million due no later than thirty days after receiving regulatory approval by the FDA of our NDA for Adzenys ER. We will also pay a single digit royalty on net sales of the Adzenys ER during the life of the relevant Shire patents. Additionally, the license agreement contains a covenant from Shire not to file a patent infringement suit against us alleging that Adzenys ER infringes the Shire patents.

### **Generic Tussionex**

We manufacture and market a generic equivalent to the branded product Tussionex. Our generic Tussionex is a hydrocodone polistirex and chlorpheniramine polistirex XR liquid suspension that is a Schedule II narcotic, antitussive and antihistamine combination. This product is indicated for the relief of cough and upper respiratory symptoms associated with allergies or colds in adults and children six years of age and older.

Since its launch in September 2013, we have manufactured and utilized our DTRS technology in the production of our generic Tussionex at our facilities in Grand Prairie, Texas. In August 2014, we acquired all commercialization and profit rights to this formulation of the generic Tussionex product from Cornerstone BioPharma, Inc. and Coating Place, Inc. We have an exclusive supply agreement (the "Supply Agreement"), with Coating Place, Inc., or CPI, which expires in August 2021, pursuant to which CPI (i) is the exclusive supplier of the active ingredient complexes in our generic Tussionex and (ii) has agreed to not supply anyone else engaged in the production of generic Tussionex with such active ingredient complexes. Under the terms of the Supply Agreement, we must deliver a 24-month rolling forecast, or Forecast, of our expected product requirements to CPI on a quarterly basis; however, only the first calendar quarter commencing on or after the 90<sup>th</sup> day after the delivery of a Forecast constitutes a binding purchase commitment with respect to the products listed in such Forecast. In October 2014, we re-launched the product under our own label. We sell our product to drug wholesalers in the United States. We have also established indirect contracts with drug, food and mass retailers that order and receive our product through wholesalers. We have obtained required state licenses, set up distribution channels and established trade relations in order to commercialize our generic Tussionex.

### **Commercialization**

We are commercializing Adzenys XR-ODT, Cotempla XR-ODT and Adzenys ER, in the United States using our existing commercial infrastructure. We sell our Adzenys XR-ODT, Cotempla XR-ODT

and Adzenys ER products to drug wholesalers in the United States, and we have obtained required state licenses and set up distribution channels.

In the United States, approximately 12,500 physicians prescribe approximately 40% of all ADHD prescriptions. We are using a specialty sales force of approximately 125 sales representatives primarily targeting the highest-volume prescribers of ADHD medication. The sales force is divided into 13 regions, each managed by a regional sales manager. Furthermore, since our target physicians tend to prescribe both methylphenidate and amphetamine, we leverage our sales force by promoting all three of our ADHD products to the same audience.

Our commercialization efforts are focused on delivering the right message for each of our three ADHD products. Data indicates that ADHD-indicated extended-release methylphenidate and extended-release amphetamine products are widely prescribed. Based on this, our messaging can focus on anticipated benefits of our XR-ODT and ER liquid suspension dosage forms. We use multi-channel tactics to reach physicians, payers, patients and patient caregivers with the right frequency to drive behavior. In addition to personal promotion, we intend to reach physicians through medical education, direct marketing, journal advertising and electronic health record communication.

Advocacy groups, patients and caregivers are extremely active and vocal in the ADHD space. The period from initial diagnosis to symptom control is difficult, and caregivers actively seek and pass on useful information. Our direct-to-patient and direct-to-consumer plan is designed to provide useful educational materials and tools to help caregivers and patients successfully manage ADHD treatment.

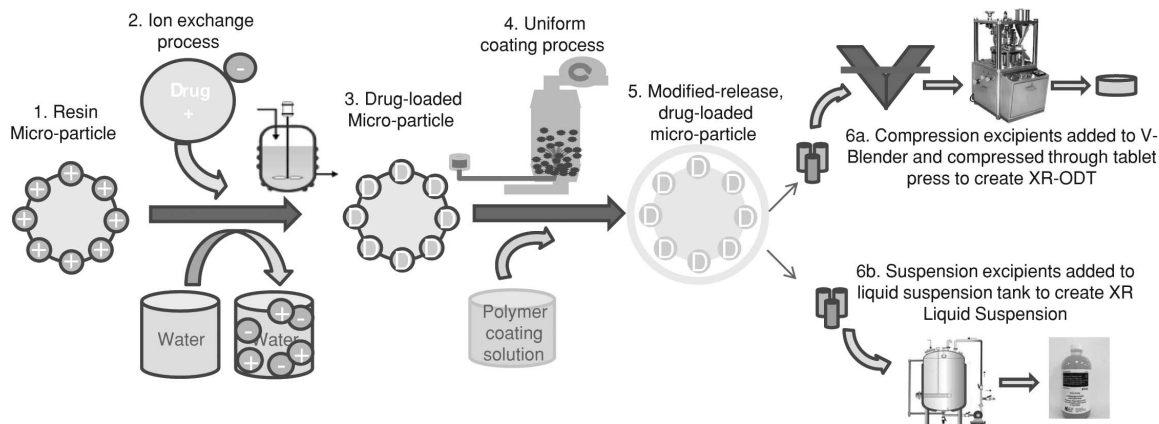
We launched Adzenys XR-ODT, our amphetamine XR-ODT, on May 16, 2016. We initiated an early experience program with limited product availability for Cotempla XR-ODT, our methylphenidate XR-ODT, on September 5, 2017 before launching this product nationwide on October 2, 2017. We launched Adzenys ER, our amphetamine extended-release liquid suspension, on February 26, 2018.

### **Our proprietary technology platform**

We believe that we can apply the XR-ODT and XR liquid suspension technologies that underlie Adzenys XR-ODT, Cotempla XR-ODT, Adzenys ER and generic Tussionex to other active pharmaceutical ingredients, or APIs. This would allow us to offer more patient- and caregiver-friendly dosage forms, potentially improving compliance rates due to difficulty swallowing and providing other clinical advantages. We have the ability to produce drug-loaded micro-particles with complex release profiles, which allows us to develop ODT or liquid suspension formulations that mimic or improve existing therapies not otherwise available in XR-ODT or XR liquid suspension form.

Our proprietary modified-release drug delivery technology platform, as illustrated below in Figure 8, allows us to produce drug-loaded micro-particles through an ion exchange process that creates new salt forms of existing drug compounds that have been proven safe and effective. By applying a uniform modified-release coating to these drug-loaded micro-particles and avoiding agglomeration, or clumping, we are able to create particle structures that can withstand compression and osmotic forces without rupturing, sloughing or leaking. This allows us to compress the modified-release micro-particles into ODT or suspend them in a liquid formulation without destroying their integrity or causing dose-dumping. By applying different types of coatings, we can modify the drug release characteristics of a micro-particle. Additionally, by mixing combinations of these micro-particles, each of which has its own release profile, we are able to produce complex drug release profiles. These micro-particles are further blended with excipients to form a final drug product, which we incorporate into a patient-friendly dosage form such as an ODT or liquid suspension. We are also able to utilize this technology to achieve tamper-resistant formulations and taste-masking.

**Figure 8: Our Proprietary Modified-Release Drug Delivery Technology Platform**



We believe our technology platform is able to deliver a proprietary portfolio of commercially available drugs in highly desirable dosage forms.

### **Our XR-ODT Technology: Rapidly Disintegrating Ionic Masking**

Our Rapidly Disintegrating Ionic Masking (“RDIM”) technology utilizes an orally disintegrating, modified-release, taste-masked pharmaceutical composition that can withstand compression forces associated with standard tableting technology, allowing for a drug to be incorporated into the ODT dosage form using ion resin technology. This technology not only provides extended-release and controlled-release properties, it masks the unpleasant taste of the active drug. Flavor and coloring can also be added to the compression blend to further enhance the pharmaceutical elegance of the finished XR-ODT. The finished product is then packaged in blister packs making them extremely portable, child resistant and stable for 24 months. Our RDIM technology is protected by a U.S. patent that is scheduled to expire in 2026.

ODT are one of the most preferred solid oral dosage forms in the market. We believe Adzenys XR-ODT and Cotempla XR-ODT, using our patented XR-ODT technology, are the first amphetamine XR-ODT and the first methylphenidate XR-ODT, respectively, for the treatment of ADHD on the market.

### **Our XR Liquid Suspension Technology: Dynamic Time Release Suspension**

Our Dynamic Time Release Suspension (“DTRS”) technology encompasses a set of process technologies and know-how to manufacture and test modified-release liquid suspension products that are shelf-stable. By matching the specific gravity, osmotic and ionic characteristics of the drug resin particle to that of the suspension, we are able to obtain shelf-stable liquids with a 24-month shelf life that do not require reconstitution or refrigeration.

XR liquid suspension provides a patient-friendly dosage form for patients who find swallowing an intact tablet or capsule to be difficult, or for whom more precise dose-titration may be preferred or required. Our DTRS technology not only provides for an extended-release, ready-to-use Liquid Suspension but also provides excellent taste-masking of the drug itself. Our DTRS technology is protected by a series of patents and patent applications.

## **Our Tamper Resistant Technology: Kinetically Controlled Tamper Protection**

Ion resin drug products inherently deter some forms of abuse, such as inhalation, smoking and injection; however, the most common form of abuse for many drugs is to induce dose-dumping by crushing, chewing or extraction. Our Kinetically Controlled Tamper Protection (“KCTP”) technology is designed to prevent abuse by altering the kinetics of the drug product and can be used in conjunction with both our XR-ODT and XR liquid suspension dosage forms. KCTP is designed to discourage common methods of tampering associated with certain classes of medications which can be abused and misused. KCTP utilizes an additional ion resin particle with an aversive agent bound to it. The aversive resin complex is then coated so that it passes through the body without material release. If an attempt is made to tamper with the XR-ODT or XR liquid suspension to cause dose-dumping, the aversive agent will also be released and block or disrupt the properties of the active drug product.

We believe that our KCTP technology may be especially useful for opioid-based pain products or other DEA scheduled drug products for which abuse and dose dumping are known problems. Our KCTP technology is the subject of a patent application and, if granted, this patent will provide protection until 2032.

## **Our product pipeline potential**

Beyond our initial focus on ADHD, our strategy is to apply our proprietary drug delivery technology platform for the development of additional drug candidates where patients may benefit from either XR-ODT or XR liquid suspension dosage forms of existing extended-release medications. Difficulty and inability to swallow tablets and capsules are not limited to ADHD medications. Patients with CNS conditions, such as stroke, Parkinson’s disease and Alzheimer’s, and gastrointestinal conditions, such as nausea and vomiting, often have difficulty swallowing their medication and would benefit from ODT and liquid suspension dosage forms.

In addition, our technology can be applied to existing drugs that are currently not optimized for their kinetic delivery. We believe that our technology is capable of overcoming some of the common issues in oral drug delivery, such as high peak to trough ratios, blood level spikes that induce unwanted side effects, wide variations in fed-fasted effect, suboptimal onset of action, suboptimal duration of effect, dose-dumping and single point failures of the delivery system, while providing an oral dosage form that is preferred by patients, caregivers and physicians.

We have an active development pipeline that includes product candidates in complementary therapeutic areas such as psychiatry and neurology, along with additional novel treatment options for ADHD. We have completed feasibility studies on several of these potential product candidates thus far. We believe several of these potential product candidates will be synergistic to our existing commercial infrastructure and the others would allow us to expand into adjacent therapeutic categories. After completing feasibility work on several potential product candidates by mid-2018, we plan to select two to three candidates for further clinical development.

Our screening criteria for future potential product candidates to initially assess technical feasibility include whether the target drug compound can be ionized and bound to a resin micro-particle. We are assessing drug loading efficiency and coating polymers and conducting initial coating work to determine whether the desired release profile can be achieved for a particular drug resin micro-particle.

We are also assessing regulatory criteria to minimize regulatory approval risk. We intend to continue to use the 505(b)(2) regulatory approval pathway in an effort to mitigate approval risk, and also simplify the clinical development program. We intend to address clinical study design, study endpoints and labeling advantages early in the development process so that we can tailor a given clinical program that produces a product candidate with attributes that allow for the optimal strategic positioning, if approved.

Finally, we are evaluating criteria when systematically choosing a potential product candidate for our pipeline. We have looked for product candidates that we believe have a market potential in excess of \$50.0 million, a concentrated specialty physician prescribing base, in the case of complementary candidates, and a patent landscape that can be navigated and protected through the lifespan of our potential product candidate.

We have designed our development process to be targeted and relatively efficient. If we are able to effectively execute our development process, we may be able to initiate clinical trials in approximately 18 months, and submit our NDA in as few as 36 months, after identifying a potential product candidate. We believe we have identified several potential product candidates that fit our screening criteria and that are attractive candidates for our branded product portfolio.

## **OUR MANUFACTURING CAPABILITIES**

### **Overview**

We lease one manufacturing site in Grand Prairie, Texas that handles the development, production, quality control testing and packaging of our products. This facility has 77,112 square feet of manufacturing and laboratory space, and contains dedicated cGMP manufacturing suites for both XR-ODT and XR liquid suspension. We hold DEA manufacturing and analytical licenses, and maintain storage and use of Schedule II through IV controlled substances. The manufacture of our products is subject to extensive cGMP regulations, which impose various procedural and documentation requirements and govern all areas of record keeping, production processes and controls, personnel and quality control. We have operated and maintained these facilities dating back to when we operated as a contract manufacturer by our predecessor corporation, PharmaFab, Inc., or PharmaFab.

In April 2007, the FDA announced entry of a Consent Decree of Permanent Injunction, or the Consent Decree, against PharmaFab, one of its subsidiaries and two of its officials, including Mark Tengler, our former Chief Technology Officer, who was, at the time, PharmaFab's president and Russ McMahan, our Senior Vice President of Scientific Affairs, who held a similar position at the time with PharmaFab, or jointly, the Defendants. The Consent Decree arose out of several perceived cGMP deficiencies related to the manufacture of unapproved drugs or Drug Efficacy Study Implementation, or DESI, drugs that we no longer manufacture. Pursuant to the Consent Decree, the Defendants were permanently restrained and enjoined from directly or indirectly manufacturing, processing, packing, labeling, holding or distributing any prescription drugs that are not the subject of an NDA or an abbreviated NDA. Among other things, the Consent Decree also granted the FDA the ability to, without prior notice, inspect PharmaFab's place of business and take any other measures necessary to monitor and ensure continuing compliance with the terms of the Consent Decree. The FDA has inspected the Grand Prairie facility several times since the Consent Decree was entered, and we have been able to manufacture and ship our generic Tussionex, Adzenys XR-ODT, Cotempla XR-ODT, Adzenys ER for commercial distribution and drug products for our clinical trials. We have also concluded the required annual audit program as prescribed by the Consent Decree. For our most recent annual audit by a cGMP expert in November 2014, the cGMP expert concluded our corrective actions satisfactorily addressed the observations noted by the cGMP expert in its audit report. However, on May 22, 2015, the FDA's Dallas District Office identified three ongoing cGMP deviations based on our response to the audit report related to batch failure investigations, quality control unit procedures, and in-process specifications. We implemented corrective actions and submitted additional information in our response to the FDA pursuant to the Consent Decree and the FDA closed the matter. To date, the consent decree has had no material impact on our current business operations or our ability to pursue approval of our product candidates.

We are currently producing Adzenys XR-ODT, Cotempla XR-ODT, Adzenys ER and our generic Tussionex for commercial distribution. We believe that our current facilities have the manufacturing

capacity for commercial production of Adzenys XR-ODT, Cotempla XR-ODT, Adzenys ER and generic Tussionex in quantities sufficient to meet what we believe will be our commercial needs, and to accommodate the manufacturing of materials for future clinical trials of other potential product candidates that we may identify for our product pipeline. We believe that maintaining our internal manufacturing capabilities enables us to obtain our products at-cost without manufacturer's margins and to better control supply quality and timing.

### **Drug substances**

We currently purchase the APIs used in Adzenys XR-ODT and Adzenys ER (amphetamine), and Cotempla XR-ODT (methylphenidate), anionic resins, excipients and other materials from third-party providers, on a purchase order basis from manufacturers based outside and within the United States. We have entered into commercial supply agreements, with several of these manufacturers, and anticipate entering into commercial supply agreements with additional manufacturers at a later date.

Both amphetamine and methylphenidate are classified as controlled substances under U.S. federal law. Adzenys XR-ODT, Cotempla XR-ODT and Adzenys ER are classified by the DEA as Schedule II controlled substances, meaning that these drug products have a high potential for abuse and dependence among drugs that are recognized as having an accepted medical use. Consequently, the procurement, manufacturing, shipping, dispensing and storing of our products and product candidates will be subject to a high degree of regulation, as described in more detail under the caption "Governmental Regulation—DEA Regulation" included elsewhere in this Annual Report on Form 10-K.

## **INTELLECTUAL PROPERTY**

### **Proprietary protection**

Our commercial success depends in part on our ability to obtain and maintain proprietary protection for our drug candidates, manufacturing and process discoveries and other know-how, to operate without infringing the proprietary rights of others, and to prevent others from infringing on our proprietary rights. We have been building and continue to build our intellectual property portfolio relating to our ADHD products, our generic Tussionex and our technology platform. Our policy is to seek to protect our proprietary position by, among other methods, filing U.S. and certain foreign patent applications related to our proprietary technology, inventions and improvements that are important to the development and implementation of our business. We also intend to rely on trade secrets, know-how, continuing technological innovation, and potential in-licensing opportunities to develop and maintain our proprietary position. We cannot be sure that patents will be granted with respect to any of our pending patent applications or with respect to any patent applications filed by us in the future, nor can we be sure that any of our existing patents or any patents that may be granted to us in the future will be commercially useful in protecting our technology.

### **Patent rights**

Our intellectual property portfolio consists of 13 patents and 8 patent applications in the United States, including 1 provisional application, and 4 patents and 2 patent applications in foreign countries and regions, and 1 international (PCT) patent application. Our intellectual property strategy emphasizes specific drug products, product groups, and technology platforms. Our patents and patent applications covering specific drug products include claims to the drug products and to methods of using those products. Our patents and patent applications covering technology platforms include claims to methods of making products as well as claims to the products made by those methods. Certain of these patents and patent applications cover more than one product.



Our XR-ODT product Adzenys XR-ODT patent portfolio includes five granted U.S. patents and three pending U.S. non-provisional applications. The issued patents contain pharmaceutical composition-of-matter claims covering controlled-release direct compression ODT with drug-resin particles and, among other things, composition of matter for Adzenys XR-ODT. The composition-of-matter patents are scheduled to expire in 2026 and 2032.

Our XR-ODT product Cotempla XR-ODT patent portfolio includes three granted U.S. patents, including pharmaceutical composition-of-matter claims covering controlled-release direct compression ODT with drug-resin particles and, among other things, composition of matter for Cotempla XR-ODT. These patents are scheduled to expire in 2026 and 2032, respectively. This portfolio also includes four other pending U.S. non-provisional applications and one international (PCT) patent application.

Our XR liquid suspension product Adzenys ER patent portfolio contains nine granted U.S. patents and three other pending U.S. non-provisional applications. These patents contain claims directed to, among other things, compositions of matter, as well as methods of preparing liquid controlled-release formulations and for predicting bioequivalence for liquid suspension. The longest-term composition-of-matter patent is scheduled to expire in 2032, and the method patents are scheduled to expire in 2025, 2029 and 2031, respectively.

Our generic Tussionex is covered by six of our granted U.S. patents which include claims directed to, among other things, a composition-of-matter, as well as methods-of-making, and for predicting bioequivalence for liquid suspension. Our generic Tussionex is also covered by one other pending non-provisional applications. The composition-of-matter patent is scheduled to expire in 2031. We expect protection under certain other granted patents and/or a patent granted on the pending application to also extend until 2031.

Both applicable platform patents and relevant specific drug patents for Adzenys XR-ODT, Cotempla XR-ODT and Adzenys ER are listed in the Orange Book. We own all of the above patents and pending applications.

On July 25, 2016, we received a Paragraph IV certification from Actavis advising us that Actavis has filed an ANDA with the FDA for a generic version of Adzenys XR-ODT. The certification notice alleges that the four U.S. patents listed in the FDA's Orange Book for Adzenys XR-ODT, one with an expiration date in April 2026 and three with expiration dates in June 2032, will not be infringed by Actavis's proposed product, are invalid and/or are unenforceable. On September 1, 2016, we filed a patent infringement lawsuit in federal district court in the District of Delaware against Actavis that automatically stayed, or barred, the FDA from approving Actavis's ANDA for 30 months or until a district court decision that is adverse to the asserted patents is rendered, whichever is earlier. On October 17, 2017, we entered into the Agreement with Actavis, which resolves all ongoing litigation involving our Adzenys XR-ODT patents and Actavis's ANDA. Under the Agreement, we have granted Actavis the right to manufacture and market its generic version of Adzenys XR-ODT under the ANDA beginning on September 1, 2025, or earlier under certain circumstances. A stipulation and order of dismissal was entered by the U.S. District Court for the District of Delaware. The Agreement has been submitted to the applicable governmental agencies.

On October 31, 2017, we received a paragraph IV certification from Teva Pharmaceuticals USA, Inc. ("Teva") advising us that Teva has filed an ANDA with the FDA for a generic version of Cotempla XR-ODT, in connection with seeking to market its product prior to the expiration of patents covering Cotempla XR-ODT. On December 13, 2017, we filed a patent infringement lawsuit in federal district court in the District of Delaware against Teva. This case alleged that Teva infringed our Cotempla XR-ODT patents by submitting to the FDA an ANDA seeking to market a generic version of Cotempla XR-ODT prior to the expiration of our patents. This lawsuit automatically stayed, or barred, the FDA from approving Teva's ANDA for 30 months or until a district court decision that is adverse to the asserted patents is rendered, whichever is earlier.

Adzenys XR-ODT and Cotempla XR-ODT are not currently protected by patents outside of the United States and our generic Tussionex and Adzenys ER are currently protected by method patents only in the United States, Australia, Canada and Mexico. As such, competitors may be free to sell products that incorporate the same or similar technologies that are used in our products in countries in which the relevant product does not have patent protection.

Patent life determination depends on the date of filing of the application and other factors as promulgated under the patent laws. In most countries, including the United States, the patent term is generally 20 years from the earliest claimed filing date of a non-provisional patent application in the applicable country.

### **Trade secret and other protection**

In addition to patented intellectual property, we also rely on trade secrets and proprietary know-how to protect our technology and maintain our competitive position, especially when we do not believe that patent protection is appropriate or can be obtained. Our policy is to require each of our employees, consultants and advisors to execute a confidentiality and inventions assignment agreement before beginning their employment, consulting or advisory relationship with us. The agreements generally provide that the individual must keep confidential and not disclose to other parties any confidential information developed or learned by the individual during the course of the individual's relationship with us except in limited circumstances. These agreements generally also provide that we shall own all inventions conceived by the individual in the course of rendering services to us.

### **Other intellectual property rights**

We seek trademark protection in the United States when appropriate. We have filed for trademark protection for the Neos Therapeutics mark, which we use with our pharmaceutical research and development as well as products, as well as trade names that could be used with our potential products. We currently have registered trademarks for Neos Therapeutics, Adzenys and Adzenys XR-ODT in the United States as well as for our DTRS technology.

From time to time, we may find it necessary or prudent to obtain licenses from third party intellectual property holders.

## **RESEARCH AND DEVELOPMENT**

For the years ended December 31, 2017, December 31, 2016 and December 31, 2015, our research and development expenses were \$9.0 million, \$12.2 million and \$11.7 million, respectively.

## **COMPETITION**

Our industry is characterized by rapidly advancing technologies, intense competition and a strong emphasis on proprietary products. We face competition and potential competition from a number of sources, including pharmaceutical and biotechnology companies, generic drug companies, drug delivery companies and academic and research institutions. We believe the key competitive factors that will affect the development and commercial success of our product candidates include ease of administration and convenience of dosing, therapeutic efficacy, safety and tolerability profiles and cost. Many of our potential competitors have substantially greater financial, technical and human resources than we do, as well as more experience in the development of product candidates, obtaining FDA and other regulatory approvals of products, and the commercialization of those products. Consequently, our competitors may develop modified-release products for the treatment of ADHD or for other indications we may pursue in the future, and such competitors' products may be more effective, better tolerated and less costly than our product candidates. Our competitors may also be more successful in manufacturing and marketing their products than we are. We will also face competition in recruiting

and retaining qualified personnel and establishing clinical trial sites and patient enrollment in clinical trials.

Adzenys XR-ODT, Cotempla XR-ODT and Adzenys ER also face competition from commercially available generic and branded medications currently produced by companies that are promoting products in the ADHD market, including Shire (Vyvanse, Adderall XR, Mydayis), Janssen (Concerta), Pfizer (Quillivant XR and QuilliChew ER), Novartis (Focalin XR and Ritalin LA), Tris Pharmaceuticals (Dyanavel XR), Rhodes Pharmaceuticals (Aptensio XR) and related generics. We are also aware of efforts by several pharmaceutical companies with ADHD medications in clinical development, including Sunovion, Kem Pharm and Neurovance. Tris Pharmaceuticals is also working in this space to reformulate existing methylphenidate and amphetamine medications.

The FDA recently issued revised guidance for bioequivalence testing of extended-release methylphenidate, which makes it more difficult to seek approval on the basis of bioequivalence for new generic products. We believe this will result in limited competition for the generic Concerta market and a new branded, extended-release methylphenidate drug with 12-hour duration of effect, such as Cotempla XR-ODT would benefit from the lack of competition. In light of these developments, we believe that along with Concerta and Aptensio XR, Cotempla XR-ODT is positioned to be one of only three branded solid oral dosage formulations of extended-release methylphenidate with 12-hour coverage, and its ODT formulation would offer a unique and patient- and caregiver-friendly dosage form. While several generic versions of Concerta have recently been approved by the FDA, two additional generic manufacturers launched generic versions of Concerta, Mallinckrodt in 2011 and KUDCO in 2013, both have lost their AB-rating, are now BX-rated, and may no longer be substituted for Concerta. This results in a market with a higher barrier to entry.

## **GOVERNMENT REGULATION**

Government authorities in the United States at the federal, state and local levels and in other countries regulate, among other things, the research, development, testing, manufacture, quality control, approval, labeling, packaging, storage, record-keeping, promotion, advertising, distribution, post-approval monitoring and reporting, marketing and export and import of drug products. Generally, before a new drug can be marketed, considerable data demonstrating its quality, safety and efficacy must be obtained, organized into a format specific for each regulatory authority, submitted for review and ultimately approved by the applicable regulatory authority.

### **U.S. drug development**

In the United States, the FDA regulates drugs under the Federal Food, Drug, and Cosmetic Act, or FDCA, and its' implementing regulations. Drugs are also subject to other federal, state and local statutes and regulations. The process of obtaining regulatory approval and maintaining subsequent compliance with applicable federal, state and local statutes and regulations require the expenditure of substantial time and financial resources. Failure to comply with the applicable U.S. requirements at any time during product development, the approval process or after approval may subject an applicant to administrative or judicial sanctions. These sanctions could include, among other actions, the FDA's refusal to approve pending applications, withdrawal of an approval, a clinical hold, untitled or warning letters, voluntary product recalls or market withdrawals, product seizures, total or partial suspension of production or distribution injunctions, fines, consent decrees, refusals of government contracts, restitution, disgorgement or civil and criminal penalties. Any agency or judicial enforcement action could have a material adverse effect on us. For a description of a consent decree our predecessor corporation entered into with the FDA and to which we remain subject, see "Our manufacturing capabilities—Overview" and "Risk factors—Risks related to commercialization."

If we fail to manufacture Adzenys XR-ODT, Cotempla XR-ODT or Adzenys ER in sufficient quantities and at acceptable quality and pricing levels, or fail to obtain adequate DEA quotas for controlled substances, or to fully comply with cGMP regulations, we may face delays in the commercialization of this product candidate or be unable to meet market demand, and may be unable to generate potential revenues.

Our product candidates must be approved by the FDA through the NDA process before they may be legally marketed in the United States. We intend to submit our NDAs under the 505(b)(2) regulatory approval pathway. Development and approval of drugs generally involves the following:

- Submission to the FDA of an IND, which must become effective before clinical trials involving humans may begin;
- Approval by an independent institutional review board, or IRB, or ethics committee at each clinical trial site before a trial may be initiated at that site;
- Performance of adequate and well-controlled human clinical trials in accordance with applicable IND regulations and other good clinical practices, or GCPs;
- Submission of an NDA to the FDA;
- The FDA's decision within 60 days of its receipt of an NDA to accept it for filing and review;
- Satisfactory completion of an FDA pre-approval inspection of the manufacturing facility or facilities where the drug is produced to assess compliance with cGMPs and assure that the facilities, methods and controls are adequate to preserve the drug's identity, strength, quality and purity;
- Possible FDA audit of the clinical trial sites that generated the data in support of the NDA; and
- FDA review and approval of the NDA.

The nonclinical testing, clinical trials and review process requires substantial time, effort and financial resources, and we cannot be certain that any approvals for our product candidates will be granted on a timely basis, if at all. The data required to support an NDA are generated in two distinct developmental stages: nonclinical and clinical. The nonclinical development stage generally involves synthesizing the active component, developing the formulation and control procedures and determining the manufacturing process, as well as carrying out non-human toxicology, pharmacology and drug metabolism studies in the laboratory, which may support subsequent clinical testing in humans. In the case of documentation to support a 505(b)(2) NDA, this nonclinical data may be referenced in literature or the FDA's previous findings of safety and efficacy for a listed drug. The sponsor must submit the results of the nonclinical studies, together with manufacturing information, analytical data, any available clinical data or literature and a proposed clinical protocol, to the FDA as part of the IND. An IND is a request for authorization from the FDA to administer an investigational drug product to humans, and must become effective before clinical trials may begin. An IND automatically becomes effective 30 days after receipt by the FDA, unless before that time the FDA raises concerns or questions related to one or more proposed clinical trials and places the IND on clinical hold. In such a case, the IND sponsor and the FDA must resolve any outstanding concerns before the clinical trial can begin. As a result, submission of an IND may not result in the FDA allowing clinical trials to commence.

The clinical stage of development involves the administration of the product candidate to healthy volunteers and patients under the supervision of qualified investigators, generally physicians not employed by or under the sponsor's control, in accordance with GCPs, which include the requirement that all research subjects provide their informed consent for their participation in any clinical trial. Clinical trials are conducted under protocols detailing, among other things, the objectives of the trial,

dosing procedures, subject selection and exclusion criteria and the parameters to be used to monitor subject safety and assess efficacy. Each protocol, and any subsequent amendments to the protocol, must be submitted to the FDA as part of the IND. Further, each clinical trial must be reviewed and approved by an independent IRB for each institution where the trial will be conducted to ensure that the risks to individuals participating in the clinical trials are minimized and are reasonable in relation to anticipated benefits. The IRB also approves the informed consent form that must be provided to each subject or his or her legal representative and must monitor the clinical trial until completed.

### **Clinical trials**

Clinical trials are generally conducted in three sequential phases, known as Phase 1, Phase 2 and Phase 3, and may overlap.

- Phase 1 clinical trials generally involve a small number of healthy volunteers who are initially exposed to a single dose and then multiple doses of the product candidate. The primary purpose of these clinical trials is to assess the metabolism, pharmacology, side effect tolerability and safety of the drug.
- Phase 2 clinical trials typically involve studies in disease-affected patients to determine the dose required to produce the desired benefits. At the same time, safety and further pharmacokinetic and pharmacodynamics information is collected, possible adverse effects and safety risks are identified and a preliminary evaluation of efficacy is conducted.
- Phase 3 clinical trials generally involve large numbers of patients at multiple sites and are designed to provide the data necessary to demonstrate the product candidate's safety and effectiveness for its intended use, establish its overall benefit/risk relationship, and provide an adequate basis for approval.

By following the 505(b)(2) regulatory approval pathway, the applicant may reduce some of the burdens of developing a full clinical program by relying on investigations not conducted by the applicant and for which the applicant has not obtained a right of reference, such as prior investigations involving the listed drug. In such cases, some clinical trials may not be required or may be otherwise limited.

Post-approval trials, sometimes referred to as Phase 4, may be conducted after initial marketing approval. These trials are used to gain additional experience from the treatment of patients in the intended therapeutic indication. In certain instances, the FDA may mandate the performance of Phase 4 clinical trials as a condition of approval of an NDA.

Before approval, progress reports detailing the results of the clinical trials, among other information, must be submitted at least annually to the FDA, and written IND safety reports must be submitted to the FDA and investigators for serious and unexpected suspected adverse events, findings from other studies suggesting a significant risk to humans exposed to the same or similar drugs, findings from animal or *in vitro* testing suggesting a significant risk to humans, and any clinically important rate increase of a serious suspected adverse reaction compared to that listed in the protocol or investigator brochure. Phase 1, Phase 2 and Phase 3 clinical trials may not be completed successfully within any specified period, if at all. The FDA or the sponsor may suspend or terminate a clinical trial at any time on various grounds, including a finding that the research subjects are being exposed to an unacceptable health risk. Similarly, an IRB can suspend or terminate approval of a clinical trial at its institution if the trial is not being conducted in accordance with the IRB's requirements or the use of the drug raises any safety concerns. Additionally, some clinical trials are overseen by an independent group of qualified experts organized by the sponsor, known as a data safety monitoring board or committee. Depending on its charter, this group may determine whether a trial may move forward at designated check points based on access to certain data from the trial.

There are also requirements governing the reporting of ongoing clinical trials and completed trial results to public registries. Sponsors of certain clinical trials of FDA-regulated products are required to register and disclose specified clinical trial information, which is publicly available at [www.clinicaltrials.gov](http://www.clinicaltrials.gov). Information related to the product, patient population, phase of investigation, study sites and investigators and other aspects of the clinical trial is then made public as part of the registration. Sponsors are also obligated to discuss the results of their clinical trials after completion. Disclosure of the results of these trials can be delayed until the new product or new indication being studied has been approved. However, there are evolving rules and increasing requirements for publication of all trial-related information, and it is possible that data and other information from trials involving drugs that never garner approval could require disclosure in the future.

Concurrent with clinical trials, companies usually develop additional information about the chemistry and physical characteristics of the drug as well as finalize a process for manufacturing it in commercial quantities in accordance with cGMP requirements. The manufacturing process must be capable of consistently producing quality batches of the product candidate, and, among other things, a drug manufacturer must develop methods for testing the identity, strength, quality and purity of the final drug product. Appropriate packaging must be selected and tested, and stability studies must be conducted to demonstrate that the product candidate does not undergo unacceptable deterioration over its shelf life.

### **NDA and FDA review process**

The results of nonclinical studies and clinical trials, together with other detailed information, including extensive information on manufacturing and drug composition and proposed labeling, are submitted to the FDA in the form of an NDA requesting approval to market the drug for one or more specified indications. The FDA reviews an NDA to determine, among other things, whether a drug is safe and effective for its intended use and whether the product is being manufactured in accordance with cGMPs to assure and preserve the product's identity, strength, quality and purity. FDA approval of an NDA must be obtained before a drug may be legally marketed in the United States.

Under the Prescription Drug User Fee Act, as amended (the "PDUFA"), each NDA must be accompanied by a user fee. The FDA adjusts the PDUFA user fees on an annual basis. According to the FDA's fee schedule, effective through September 30, 2018, the user fee for an application requiring clinical data, such as an NDA, is \$2,421,495. Clinical data, as interpreted by the FDA to assess fees under PDUFA, include (1) study reports or literature reports of what are explicitly or implicitly represented by the applicant to be adequate and well-controlled trials for safety or effectiveness or (2) reports of comparative activity (other than bioequivalence and bioavailability studies), immunogenicity, or efficacy, where those reports are necessary to support a claim of comparable clinical effect. The term does not include bioequivalence and bioavailability studies submitted in support of an NDA. NDAs for which clinical data are not required to demonstrate safety and effectiveness are reduced to half of the amount of the prescribed user fee, or \$1,210,748 for 2018. PDUFA also imposes an annual program fee for human drugs (\$304,162 per product up to a maximum of five fees for a fiscal year for prescription drug products identified in a single approved application). Fee waivers or reductions are available in certain circumstances, including waiver of the application fee for the first application filed by a small business.

The FDA reviews submitted NDAs before it accepts them for filing, and may request additional information rather than accepting the applications. The FDA must make a decision on accepting an NDA for filing within 60 days of receipt. Once the submission is accepted for filing, the FDA begins an in-depth review of the NDA. Under the goals and policies agreed to by the FDA under PDUFA, the FDA has ten months from the filing date in which to complete its initial review of a standard NDA and respond to the applicant, and six months from the filing date for an NDA designated for priority review. The FDA does not always meet its PDUFA goal dates for standard and priority NDAs, and the

review process is often significantly extended by FDA requests for additional information or clarification.

Before approving an NDA, the FDA will conduct a pre-approval inspection of the manufacturing facilities for the new product to determine whether they comply with cGMPs. The FDA will not approve the product unless it determines that the manufacturing processes and facilities are in compliance with cGMP requirements and adequate to assure consistent production of the product to specifications. The FDA may also audit data from clinical trials to ensure compliance with GCP requirements. Additionally, the FDA may refer applications for novel drug products or drug products which present difficult questions of safety or efficacy to an advisory committee, typically a panel that includes clinicians and other experts, for review, evaluation and a recommendation regarding whether the application should be approved and, if so, under what conditions. The FDA is not bound by the recommendations of an advisory committee, but it considers them carefully when making decisions. NDAs submitted under Section 505(b)(2) are typically not referred to an Advisory Panel for consideration unless new safety information is revealed in the review cycle. The FDA likely will re-analyze the clinical trial data, which could result in extensive discussions between the FDA and the applicant during the review process. The review and evaluation of an NDA by the FDA is extensive and time consuming and may take longer than originally planned to complete, and we may not receive a timely approval, if at all.

After the FDA evaluates an NDA, it will issue an approval letter or a Complete Response Letter. An approval letter authorizes commercial marketing of the drug with prescribing information for specific indications. A Complete Response Letter indicates that the review cycle of the application is complete and the application will not be approved in its present form. A Complete Response Letter usually describes the specific deficiencies in the NDA identified by the FDA, and may require additional clinical data, such as an additional pivotal Phase 3 clinical trial, and other significant and time-consuming requirements related to clinical trials, nonclinical studies or manufacturing. If a Complete Response Letter is issued, the applicant may resubmit the NDA, addressing all of the deficiencies identified in the letter, or withdraw the application. Even if such data and information are submitted, the FDA may decide that the NDA does not satisfy the criteria for approval. Data obtained from clinical trials are not always conclusive, and the FDA may interpret data differently than the sponsor interprets the same data.

There is no assurance that the FDA will approve a product candidate for marketing, and the sponsor may encounter significant difficulties or costs during the review process. If a product receives marketing approval, the approval may be significantly limited to specific diseases and dosages or the indications for use may otherwise be limited, which could restrict the commercial value of the product. Further, the FDA may require that certain contraindications, warnings or precautions be included in the product labeling, or it may condition approval on changes to the proposed labeling. The FDA also may condition approval on the development of adequate controls and specifications for manufacturing and a commitment to conduct post-marketing testing and surveillance to monitor the potential effects of approved products. For example, the FDA may require Phase 4 trials designed to further assess a drug's safety and efficacy.

The FDA may also place other conditions on approval including the requirement for a risk evaluation and mitigation strategy, or REMS, to assure the safe use of the drug. If the FDA concludes a REMS is needed, the sponsor of the NDA must submit a proposed REMS. The FDA will not approve the NDA without an approved REMS, if required. A REMS could include medication guides, physician communication plans or elements to assure safe use, such as restricted distribution methods, patient registries and other risk minimization tools. Any of these limitations on approval or marketing could restrict the commercial promotion, distribution, prescription or dispensing of products. Marketing approval may be withdrawn for non-compliance with regulatory requirements or if problems occur following initial marketing.

## **Section 505(b)(2) regulatory approval pathway**

Section 505(b)(2) of the FDCA provides an alternate regulatory pathway for approval of a new drug by allowing the FDA to rely on data not developed by the applicant. Specifically, Section 505(b)(2) permits the submission of an NDA where one or more of the investigations relied upon by the applicant for approval was not conducted by or for the applicant and for which the applicant has not obtained a right of reference. The applicant may rely upon published literature and/or the FDA's findings of safety and effectiveness for an approved drug already on the market. Approval or submission of a 505(b)(2) application, like those for abbreviated new drugs, or ANDAs, may be delayed because of patent and/or exclusivity rights that apply to the previously approved drug.

A 505(b)(2) application may be submitted for a new chemical entity, or NCE, when some part of the data necessary for approval is derived from studies not conducted by or for the applicant and when the applicant has not obtained a right of reference. Such data are typically derived from published studies, rather than FDA's previous findings of safety and effectiveness of a previously approved drug. For changes to a previously approved drug however, an applicant may rely on the FDA's finding of safety and effectiveness of the approved drug, coupled with information needed to support the change from the approved drug, such as new studies conducted by the applicant or published data. When based on an approved drug, the 505(b)(2) drug may be approved for all of the indications permitted for the approved drug, as well as any other indication supported by additional data.

Section 505(b)(2) applications also may be entitled to marketing exclusivity if supported by appropriate data and information. As discussed in more detail below, three-year new data exclusivity may be granted to the 505(b)(2) application if one or more clinical investigations conducted in support of the application, other than bioavailability/bioequivalence studies, were essential to the approval and conducted or sponsored by the applicant. Five years of marketing exclusivity may be granted if the application is for an NCE, and pediatric exclusivity is likewise available.

## **Orange Book listing and Paragraph IV certification**

For NDA submissions, including those under Section 505(b)(2), applicants are required to list with the FDA certain patents with claims that cover the applicant's product. Upon approval, each of the patents listed in the application is published in *Approved Drug Products with Therapeutic Equivalence Evaluations*, commonly referred to as the Orange Book. Any applicant who subsequently files an ANDA or 505(b)(2) NDA that references a drug listed in the Orange Book must certify to the FDA that (1) no patent information on the drug product that is the subject of the application has been submitted to the FDA; (2) such patent has expired; (3) the date on which such patent expires; or (4) such patent is invalid or will not be infringed upon by the manufacture, use or sale of the drug product for which the application is submitted. This last certification is known as a Paragraph IV certification.

If an applicant has provided a Paragraph IV certification to the FDA, the applicant must also send notice of the Paragraph IV certification to the holder of the NDA for the approved drug and the patent owner once the application has been accepted for filing by the FDA. The NDA holder or patent owner may then initiate a patent infringement lawsuit in response to notice of the Paragraph IV certification. The filing of a patent infringement lawsuit within 45 days of the receipt of a Paragraph IV certification prevents the FDA from approving the ANDA or 505(b)(2) application until the earlier of 30 months from the date of the lawsuit, the applicant's successful defense of the suit, or expiration of the patent.

Pursuant to our settlement agreements with Shire, we stipulated that Shire's two Orange Book-listed patents covering Adderall XR were valid, enforceable and infringed by our 505(b)(2) NDAs covering Adzenys XR-ODT and Adzenys ER. The agreements with Shire applies solely with respect to Adzenys XR-ODT and Adzenys ER.



## **Pediatric information**

Under the Pediatric Research Equity Act, or PREA, an NDA or supplement to an NDA must contain data to assess the safety and efficacy of the drug for the claimed indications in all relevant pediatric subpopulations and to support dosing and administration for each pediatric subpopulation in which the product is safe and effective. The FDA may grant deferrals for submission of pediatric data or full or partial waivers.

The Food and Drug Administration Safety and Innovation Act, or FDASIA, which was signed into law on July 9, 2012, amended the FDCA to require that a sponsor who is planning to submit an NDA for a new active ingredient, new indication, new dosage form, new dosing regimen or new route of administration submit an initial Pediatric Study Plan, or PSP, within 60 days of an end-of-Phase 2 meeting or, if there is no such meeting, as early as practicable before the initiation of the Phase 3 or Phase 2/3 trial. The initial PSP must include an outline of the pediatric trial(s) that the sponsor plans to conduct, including objectives and design, age groups, relevant endpoints and statistical approach, or a justification for not including such information and any request for a deferral of pediatric assessments or a full or partial waiver of the requirement to provide data from pediatric trials. The FDA and the sponsor must reach an agreement on the PSP, but the sponsor can submit amendments to an agreed-upon initial PSP at any time if changes to the pediatric plan need to be considered based on data collected from nonclinical studies, early phase clinical trials and other clinical development programs.

## **Post-marketing requirements**

Following approval, the company and the new product are subject to continuing regulation by the FDA, which include monitoring and recordkeeping activities, reporting of adverse experiences and complying with promotion and advertising requirements, which include prohibitions on the promotion of the drugs for unapproved, or “off-label” uses. Although physicians may prescribe legally available drugs for off-label treatments, manufacturers may not promote such non-FDA approved uses. Prescription drug promotional materials must be submitted to the FDA in conjunction with their first use on an on-going basis. Further, if there are any modifications to the drug, including changes to indications, labeling, or manufacturing processes or facilities, the applicant may be required to submit and obtain FDA approval of a supplemental NDA or new NDA, which may require the applicant to develop additional data or conduct additional nonclinical studies or clinical trials.

The FDA regulations require that products be manufactured in specific approved facilities and in accordance with cGMPs. These regulations require, among other things, quality control and quality assurance, the maintenance of records and documentation and the obligation to investigate and correct any deviations from cGMPs. Drug manufacturers and other entities involved in the manufacture and distribution of approved drugs are required to register their establishments with the FDA and certain state agencies, and are subject to periodic, unannounced inspections by the FDA and certain state agencies for compliance with cGMPs and other laws. Accordingly, manufacturers must continue to expend time, money and effort in the area of production and quality control to maintain compliance with cGMPs. The discovery of violative conditions, including failure to conform to cGMPs, could result in enforcement actions, and the discovery of problems with a product after approval may result in restrictions on a product, manufacturer or holder of an approved NDA, including voluntary recalls and product seizures.

Discovery of previously unknown problems with a product or the failure to comply with applicable FDA requirements can have negative consequences, including adverse publicity, judicial or administrative enforcement, untitled or warning letters from the FDA, mandated corrections to advertising or communications to doctors and civil or criminal penalties, among others. Newly discovered or developed safety or effectiveness data may require changes to a product’s approved

labeling, including the addition of new warnings and contraindications, and also may require the implementation of other risk management measures. New government requirements, including those resulting from new legislation, may be established, or the FDA's policies may change, which could delay or prevent regulatory approval of our products under development.

As a condition of approval for Adzenys XR-ODT and Cotempla XR-ODT, we committed to three post-marketing requirements to evaluate the pharmacokinetic, efficacy and safety of the product in children ages 4 to 5 years of age. We met with FDA officials in January 2017 to further clarify the design of the protocols required to conduct these studies for Adzenys XR-ODT. We commenced with the pharmacokinetic trial for Adzenys XR-ODT in 2017. We expect to commence with the pharmacokinetic trial for Cotempla XR-ODT in 2018.

### **U.S. marketing exclusivity**

The FDCA provides three years of marketing exclusivity for an NDA, or supplement to an existing NDA, for a drug product that contains a previously approved NCE if new clinical investigations, other than bioavailability/bioequivalence studies, were essential to the application's approval (*e.g.*, for new indications, dosages or strengths of an existing drug). This three-year exclusivity for new data covers only the modification for which the drug received approval on the basis of the new clinical investigations and does not prohibit the FDA from approving ANDAs for drugs containing the active agent for the original indication. Furthermore, this exclusivity will not delay the submission or approval of a full NDA. However, an applicant submitting a full NDA would be required to conduct or obtain a right of reference to all of the nonclinical studies and adequate and well-controlled clinical trials necessary to demonstrate safety and efficacy.

Pediatric exclusivity is another type of regulatory market exclusivity in the United States, which, if granted, adds six months to existing exclusivity periods and patent terms. This six-month exclusivity, which runs from the end of other exclusivity protections or patent term, may be granted based on the voluntary completion of a pediatric trial in accordance with a FDA-issued "Written Request." The FDA issues a written request for pediatric clinical trials before approval of an NDA only where it determines that information relating to the use of a drug in a pediatric population, or part of the pediatric population, may produce health benefits in that population.

### **DEA regulation**

Because our products and product candidates are subject to the Controlled Substances Act, or CSA, we must comply with various requirements set forth by that legislation, as amended, its implementing regulations and as enforced by the DEA. The CSA imposes various registration, record-keeping and reporting requirements, procurement and manufacturing quotas, labeling and packaging requirements, security controls, prescription and order form requirements and restrictions on prescription refills for certain kinds of pharmaceutical products. A principal factor for determining the particular requirements of the CSA applicable to a product, if any, is its actual or potential abuse profile. A product may be listed as a Schedule I, II, III, IV or V controlled substance, with Schedule I presenting the highest perceived risk of abuse and Schedule V presenting the least. For example, Schedule I controlled substances have no currently accepted medical use in treatment in the United States and a lack of accepted safety for use under medical supervision. The active ingredients in our products, hydrocodone, amphetamine and methylphenidate, are Schedule II controlled substances and under various restrictions, including, but not limited to, mandatory written prescriptions and the prohibition of refills.

Annual registration is required for any facility that manufactures, distributes, dispenses, imports or exports any controlled substance. The registration is specific to the particular location, activity and controlled substance schedule. For example, separate registrations are needed for import and

manufacturing, and each registration will specify which schedules of controlled substances are authorized. Similarly, separate registrations are also required for separate facilities.

The DEA typically inspects a facility to review its security measures prior to issuing a registration and on a periodic basis. Security requirements vary by controlled substance schedule, with the most stringent requirements applying to Schedule I and Schedule II controlled substances. Required security measures include background checks on employees and physical control of inventory through measures such as vaults and inventory reconciliations. Records must be maintained for the handling of all controlled substances, and periodic reports made to the DEA, for example distribution reports for Schedule I and II controlled substances. Reports must also be made for thefts or losses of any controlled substance, and to obtain authorization to destroy any controlled substance.

In addition, a DEA quota system controls and limits the availability and production of controlled substances in Schedule I or II. Distributions of any Schedule I or II controlled substance must also be accompanied by special order forms, with copies provided to the DEA. Because our products are, and our product candidates are expected to be, regulated as Schedule II controlled substances, they will be subject to the DEA's production and procurement quota scheme. The DEA establishes annually an aggregate quota for how much of a controlled substance may be produced in total in the United States based on the DEA's estimate of the quantity needed to meet legitimate scientific and medicinal needs. The limited aggregate amount that the DEA allows to be produced in the United States each year is allocated among individual companies, which must submit applications annually to the DEA for individual production and procurement quotas. We must receive an annual quota from the DEA in order to produce or procure any Schedule I or Schedule II controlled substance for use in manufacturing of our product and product candidates. The DEA may adjust aggregate production quotas and individual production and procurement quotas from time to time during the year, although the DEA has substantial discretion in whether or not to make such adjustments.

To enforce these requirements, the DEA conducts periodic inspections of registered establishments that handle controlled substances. Failure to maintain compliance with applicable requirements, particularly as manifested in loss or diversion, can result in administrative, civil or criminal enforcement action. The DEA may seek civil penalties, refuse to renew necessary registrations or initiate administrative proceedings to revoke those registrations. In some circumstances, violations could result in criminal proceedings.

In addition to federal scheduling, some drugs may be subject to state-controlled substance regulation and thus more extensive requirements than those determined by the DEA and FDA.

### **Pharmaceutical coverage, pricing and reimbursement**

Sales of our products will depend, in part, on the extent to which our products will be covered by third-party payors, such as government health programs, commercial insurance and managed healthcare organizations. In the United States no uniform policy of coverage and reimbursement for drug products exists. Accordingly, decisions regarding the extent of coverage and amount of reimbursement to be provided for any of our products will be made on a payor by payor basis. As a result, the coverage determination process is often a time-consuming and costly process that will require us to provide scientific and clinical support for the use of our product candidates to each payor separately, with no assurance that coverage and adequate reimbursement will be obtained.

Third-party payors are increasingly challenging the price and examining the medical necessity and cost-effectiveness of medical products and services, in addition to their safety and efficacy. In order to obtain coverage and reimbursement for any product that might be approved, we may need to conduct expensive pharmacoeconomic studies in order to demonstrate the medical necessity and cost-effectiveness of any products, in addition to the costs required to obtain regulatory approvals. Our product candidates may not be considered medically necessary or cost-effective. If third-party payors do

not consider a product to be cost-effective compared to other available therapies, they may not cover the product after approval as a benefit under their plans or, if they do, the level of payment may not be sufficient to allow a company to sell its products at a profit.

The U.S. government and state legislatures have shown significant interest in implementing cost containment programs to limit the growth of government-paid health care costs, including price controls, restrictions on reimbursement and requirements for substitution of generic products for brand-named prescription drugs. For example, the Patient Protection and Affordable Care Act, as amended by the Health Care and Education Reconciliation Act of 2010, or collectively the ACA, contains provisions that may reduce the profitability of drug products, including, for example, increased rebates for drugs reimbursed by Medicaid programs, extension of Medicaid rebates to Medicaid managed care plans, mandatory discounts for certain Medicare Part D beneficiaries and annual fees based on pharmaceutical companies' share of sales to federal health care programs. Adoption of government controls and measures, and tightening of restrictive policies in jurisdictions with existing controls and measures, could limit payments for pharmaceuticals.

As noted above, even if we are able to secure regulatory approval, sales of any of our products may suffer if the government and third-party payors fail to provide adequate coverage and reimbursement. An increasing emphasis on cost containment measures in the United States has increased, and we expect this sentiment will continue to increase the pressure on drug pricing. Coverage policies and third-party reimbursement rates may change at any time. Even if favorable coverage and reimbursement status is attained for one or more products for which we receive regulatory approval, less favorable coverage policies and reimbursement rates may be implemented in the future.

#### **Other healthcare laws and compliance requirements**

Manufacturing, sales, promotion and other activities following product approval are also subject to regulation by numerous regulatory authorities in addition to the FDA, including the Centers for Medicare & Medicaid Services, other divisions of the Department of Health and Human Services, the U.S. Department of Justice, the DEA, the Consumer Product Safety Commission, the Federal Trade Commission, the Occupational Safety & Health Administration, the Environmental Protection Agency and state and local governments.

We also are subject to various federal and state laws targeting fraud and abuse in the healthcare industry. These laws may impact, among other things, our proposed sales, marketing and educational programs. In addition, we may be subject to patient privacy regulation by both the federal government and the states in which we conduct our business. The laws that may affect our ability to operate include:

- The federal Anti-Kickback Statute, which prohibits, among other things, persons from knowingly and willfully soliciting, receiving, offering or paying remuneration, directly or indirectly, in cash or in kind, to induce or reward, or in return for, either (1) the referral of an individual to a person for furnishing any item or service for which payment is available under a federal health care program, or (2) the purchase, lease, order or recommendation thereof of any good, facility, service or item for which payment is available under a federal health care program;
- The False Claims Act and civil monetary penalty laws, which prohibit, among other things, individuals or entities from knowingly presenting, or causing to be presented, false or fraudulent claims for payment from the federal government or making or using, or causing to be made or used, a false record or statement material to a false or fraudulent claim;
- The federal Health Insurance Portability and Accountability Act of 1996, or HIPAA, which created new federal criminal statutes that prohibit executing a scheme to defraud any healthcare

benefit program, obtaining money or property of the health care benefit program through false representations or knowingly and willingly falsifying, concealing or covering up a material fact, making false statements or using or making any false or fraudulent document in connection with the delivery of, or payment for, health care benefits or services;

- HIPAA, as amended by the Health Information Technology for Economic and Clinical Health Act, or HITECH, and its implementing regulations, which imposes certain requirements relating to the privacy, security and transmission of individually identifiable health information;
- The provision under the ACA commonly referred to as the Sunshine Act, which requires applicable manufacturers of covered drugs, devices, biologics and medical supplies to track and annually report to CMS payments and other transfers of value provided to physicians and teaching hospitals and certain ownership and investment interests held by physicians or their immediate family members in applicable manufacturers and group purchasing organizations; and
- State law equivalents of each of the above federal laws, such as the Anti-Kickback Statute and False Claims Act, and state laws concerning security and privacy of health care information, which may differ in substance and application from state-to-state thereby complicating compliance efforts.

The ACA broadened the reach of the fraud and abuse laws by, among other things, amending the intent requirement of the federal Anti-Kickback Statute and the applicable criminal healthcare fraud statutes contained within 42 U.S.C. Section 1320a-7b. Pursuant to the statutory amendment, a person or entity no longer needs to have actual knowledge of this statute or specific intent to violate it in order to have committed a violation. In addition, the ACA provides that the government may assert that a claim including items or services resulting from a violation of the federal Anti-Kickback Statute constitutes a false or fraudulent claim for purposes of the civil False Claims Act or the civil monetary penalties statute. Many states have adopted laws similar to the federal Anti-Kickback Statute, some of which apply to the referral of patients for healthcare items or services reimbursed by any source, not only the Medicare and Medicaid programs.

As noted above, the federal False Claims Act prohibits anyone from, among other things, knowingly presenting, or causing to be presented, false or fraudulent claims for payment from federal programs, including Medicare and Medicaid. Although we would not submit claims directly to payors, manufacturers can be held liable under these laws if they are deemed to “cause” the submission of false or fraudulent claims by, for example, providing inaccurate billing or coding information to customers. In addition, our future activities relating to the reporting of wholesaler or estimated retail prices for our products, the reporting of prices used to calculate Medicaid rebate information and other information affecting federal, state, and third-party reimbursement for our products, and the sale and marketing of our products are subject to scrutiny under this law. For example, pharmaceutical companies have been prosecuted under the federal False Claims Act in connection with their off-label promotion of drugs. Penalties for such violations could include three times the actual damages sustained by the government, mandatory civil penalties between \$5,500 and \$11,000 for each separate false claim, exclusion from participation in federal healthcare programs, and the potential implication of various federal criminal statutes. Private individuals also have the ability to bring actions under the federal False Claims Act, or *qui tam* actions, and certain states have enacted laws based on the federal False Claims Act.

## **EMPLOYEES**

As of December 31, 2017, we employed 138 full-time employees.

## AVAILABLE INFORMATION

Our website address is [www.neostx.com](http://www.neostx.com). Our Annual Reports on Form 10-K, Quarterly Reports on Form 10-Q, Current Reports on Form 8-K and amendments to those reports filed or furnished pursuant to Section 13(a) or 15(d) of the Securities Exchange Act of 1934 are available free of charge through the investor relations page of our internet website as soon as reasonably practicable after we electronically file such material with, or furnish it to, the Securities and Exchange Commission. Alternatively, these reports may be accessed at the SEC's website at [www.sec.gov](http://www.sec.gov).

## CORPORATE INFORMATION

Our predecessor company was incorporated in Texas on November 30, 1994 as PharmaFab, Inc. and subsequently changed its name to Neostx, Inc. On June 15, 2009, we completed a reorganization pursuant to which substantially all of the capital stock of Neostx, Inc. was acquired by a newly formed Delaware corporation, named Neos Therapeutics, Inc. The remaining capital stock of Neostx, Inc. was acquired by us on June 29, 2015, and Neostx, Inc. was merged with and into Neos Therapeutics, Inc. Our principal executive offices are located at 2940 N. Highway 360, Grand Prairie, Texas, 75050, and our telephone number is (972) 408-1300. We completed our initial public offering of common stock July 2015 and our common stock is listed on the NASDAQ Global Market under the symbol "NEOS."

### Item 1A. Risk factors

*We operate in an industry that involves numerous risks and uncertainties. You should carefully consider the risks and uncertainties described below, together with all of the other information in this Annual Report on Form 10-K, including our consolidated financial statements and the related notes appearing at the end of this Annual Report on Form 10-K, before making a decision to invest in our common stock. If any of the risks actually occur, our business, financial condition, results of operations and prospects could be harmed. In that event, the trading price of our common stock could decline, and you may lose part or all of your investment.*

### RISKS RELATED TO COMMERCIALIZATION

*We are heavily dependent on the success of Adzenys XR-ODT, Cotempla XR-ODT and Adzenys ER. We have not generated substantial revenues from the sales of Adzenys XR-ODT and Cotempla XR-ODT, any sales revenues from Adzenys ER or any of our product candidates, and we may never achieve or maintain profitability.*

Our ability to become profitable depends upon our ability to generate revenues from sales of Adzenys XR-ODT, Cotempla XR-ODT, Adzenys ER and, if approved, any other product candidates that we may develop. We have limited experience in generating revenues from our marketed products, having only generated revenues from the sale of our generic Tussionex since we acquired it in 2014, and Adzenys XR-ODT, which we commenced commercializing in May 2016, and from which we have not generated substantial product sales revenues. We launched Cotempla XR-ODT in September 2017, and as a result have generated minimal sales revenue for this product to date. We have not generated any revenues from product sales of Adzenys ER, which we launched on February 26, 2018, or any other product candidates that we may develop and have incurred significant operating losses.

Our ability to generate product revenues is dependent on our ability to successfully commercialize Adzenys XR-ODT, our amphetamine extended-release orally disintegrating tablet ("XR-ODT"), Cotempla XR-ODT, our methylphenidate XR-ODT, and Adzenys ER, our amphetamine XR liquid suspension, for the treatment of attention deficit hyperactivity disorder, or ADHD, and any other

product candidates that we may identify, develop and obtain approval of. Our ability to successfully commercialize our products and product candidates depends on, among other things, our ability to:

- manufacture commercial quantities of Adzenys XR-ODT, Cotempla XR-ODT, Adzenys ER and, if approved, any other product candidates that we may develop at acceptable cost levels; and
- successfully establish and maintain sales and marketing capabilities to commercialize Adzenys XR-ODT, Cotempla XR-ODT, Adzenys ER and, if approved, any other product candidates that we may develop.

We have incurred and anticipate continuing to incur significant costs associated with commercialization of Adzenys XR-ODT, Cotempla XR-ODT, Adzenys ER and, if approved, any other product candidates that we may develop. It is possible that we will never have sufficient product sales revenues to achieve profitability.

***If our sales and marketing efforts for Adzenys XR-ODT, Cotempla XR-ODT and Adzenys ER are not successful, and if we are unable to establish and maintain sales and marketing capabilities or enter into agreements with third parties to market and sell our other product candidates, if approved, we may be unable to generate significant revenue.***

We have only recently completed building an organization for the sale, marketing and distribution of Adzenys XR-ODT, Cotempla XR-ODT, and Adzenys ER, and there is no guarantee that we will be successful in the commercialization of Adzenys XR-ODT, which we launched in May 2016, Cotempla XR-ODT, which was launched in September 2017, and Adzenys ER, which we launched on February 26, 2018. We currently have a limited sales history for Adzenys XR-ODT and Cotempla XR-ODT and no sales history for Adzenys ER. Additionally, we may need to expand or build additional sales, marketing and distribution capabilities for our products. Although we have established a focused, specialty sales and marketing organization of approximately 125 representatives to promote our approved products in the United States, these commercialization capabilities have only been recently established, and we may need to expand our sales force if we decide to undertake additional commercialization activities on our own, which will be costly and time-consuming. We cannot be certain that we will reap the benefits of our commercialization efforts of Adzenys XR-ODT, Cotempla XR-ODT and Adzenys ER compared to the cost of such efforts. Our prior experience in the marketing, sale and distribution of pharmaceutical products is limited to our generic Tussionex, and, before launching the commercialization of Adzenys XR-ODT, we had no prior experience in marketing, sale and distribution of branded pharmaceutical products. There are significant risks involved in building and managing a sales organization, including our ability to hire, retain and incentivize qualified individuals and in the appropriate numbers, generate sufficient sales leads, provide adequate training to sales and marketing personnel, effectively manage a geographically dispersed sales and marketing team and successfully negotiate with managed care and third-party payors. Any failure or delay in the development of our internal sales, marketing and distribution capabilities would adversely impact the commercialization of these products.

We also intend to enter into strategic partnerships with third parties to commercialize Adzenys XR-ODT, Cotempla XR-ODT, Adzenys ER and our product candidates, if approved, outside of the United States and intend to also enter into strategic partnerships with third parties for certain aspects of our commercialization efforts within the United States. We may have difficulty establishing relationships with third parties on terms that are acceptable to us, or in all of the regions where we wish to commercialize our products, or at all. If we are unable to establish adequate sales, marketing and distribution capabilities, whether independently or with third parties, we may not be able to generate sufficient product revenue and may not become profitable. We will be competing with many companies that currently have extensive and well-funded marketing and sales operations. Without an

internal team or the support of a third party to perform marketing and sales functions, we may be unable to compete successfully against these more established companies.

***Our business is subject to extensive regulatory requirements, and our approved products and any product candidates that obtain approval will be subject to ongoing and continued regulatory review, which may result in significant expense and limit our ability to commercialize such products.***

Even after a product is approved, we will remain subject to ongoing FDA, and other regulatory requirements governing, among other things, the production, labeling, packaging, storage, distribution, safety surveillance, advertising, promotion, import, export, record-keeping and reporting of safety and other post-market information. The holder of an approved new drug application (“NDA”) is obligated to monitor and report adverse events, or AEs, and any failure of a product to meet the specifications in the NDA. The holder of an approved NDA must also submit new or supplemental applications and obtain FDA approval for certain changes to the approved product, product labeling or manufacturing process. In addition, the FDA may impose significant restrictions on the approved indicated uses for which the product may be marketed or on the conditions of approval.

For example, a product’s approval may contain requirements for potentially costly post-approval trials and surveillance to monitor the safety and efficacy of the product or the imposition of a Risk Evaluation and Mitigation Strategy, or REMS, program.

Prescription drug advertising, marketing and promotion are subject to federal, state and foreign regulations, which include requirements for direct-to-consumer advertising and promotional activities involving the Internet and social media. In the United States, prescription drug promotional materials must be submitted to the FDA in conjunction with their first use. The FDA closely regulates the post-approval marketing and promotion of drugs to ensure they are marketed only for their approved indications and in accordance with the provisions of the approved label. Any promotion for uses or in patient populations not described in the approved labeling, known as “off-label” promotion, is impermissible and could subject us to enforcement actions and significant penalties for off-label marketing. The FDA has also provided guidance on industry-sponsored scientific and educational activities to ensure such activities are not promotional.

In addition, manufacturers and their facilities are required to comply with extensive FDA requirements, including ensuring that quality control and manufacturing procedures conform to current Good Manufacturing Practices (“cGMPs”). These cGMP regulations cover all aspects of manufacturing relating to our generic Tussionex, Adzenys XR-ODT, Cotempla XR-ODT and Adzenys ER. As such, we are subject to continual review and periodic inspections to assess compliance with cGMP and must continue to expend time, money and resources in all areas of regulatory compliance, including manufacturing, production and quality control. As a result of the Consent Decree entered into by our predecessor, which is discussed below, we were required to have a cGMP expert conduct an annual audit and submit those audit reports and our responses to the FDA for a period of five years. Although for our most recent and last annual audit by the cGMP expert in November 2014, the expert concluded that our corrective actions satisfactorily addressed the observations noted in its report, on May 22, 2015, the FDA’s Dallas District Office identified three ongoing cGMP deviations in our response to the audit related to batch failure investigations, quality control unit procedures, and in-process specifications. We implemented corrective actions and submitted additional information in our response to the FDA pursuant to the Consent Decree and the FDA closed the matter.

The facilities used by us to manufacture our products and any product candidates that we may develop are subject to inspections, including pre-approval inspections following our submission of any NDAs to the FDA for any product candidates that we may develop. For example, the FDA conducted a cGMP and pre-approval inspection related to our NDA for Cotempla XR-ODT from May 27 to June 4, 2015. At the end of the inspection, the agency issued a Form FDA 483 with one observation



finding that appropriate controls are not exercised over one of our computer systems in order to assure that changes in records are instituted only by authorized personnel. We implemented corrective action related to this observation and responded to the FDA, and the FDA closed the inspection. In addition, in connection with a general cGMP and pre-approval inspection for Adzenys ER from July 11 to July 25, 2017, we received a Form FDA 483 with one observation related to complaint records failing to document the reason and the individual making the decision not to conduct a complaint investigation. We implemented corrective action related to this observation and responded to the FDA.

If we cannot successfully manufacture material that conforms to our specifications and the strict regulatory requirements of the FDA, we will not be able to secure and/or maintain regulatory approval for our product candidates. If the FDA finds deficiencies at our manufacturing facility and does not approve our NDA for any of our future product candidates or if it withdraws any such approval in the future for our products, our ability to develop or market any of our products or any product candidates that we may develop will be impacted.

Manufacturers of drug products and their facilities are subject to continual review and periodic inspections by the FDA and other regulatory authorities for compliance with cGMPs and adherence to commitments made in the NDA. If we or a regulatory agency discovers previously unknown problems with a product, such as AEs of unanticipated severity or frequency, or problems with the facility where the product is manufactured, a regulatory agency may impose restrictions relative to that product or the manufacturing facility, including notice to physicians, withdrawal of the product from the market or suspension of manufacturing. Manufacturers are also subject to annual prescription drug product program fee. If we are unable to generate sales of our product candidates, the user fee requirements could be difficult to pay.

If we fail to comply with applicable regulatory requirements, the FDA may, for example:

- issue untitled or warning letters asserting that we are in violation of the Federal Food, Drug and Cosmetic Act (the “FDCA”);
- impose restrictions on the marketing or manufacturing of any product or product candidate that we may develop;
- seek an injunction or impose civil, criminal and/or administrative penalties, damages, assess monetary fines, or require disgorgement;
- suspend or withdraw regulatory approval;
- suspend any ongoing clinical trials;
- refuse to approve a pending NDA or supplements to an NDA submitted by us with respect to any product candidate that we may develop; or
- seize the product.

Moreover, any violation of these and other laws and regulations could result in exclusion from participation in federal healthcare programs, such as Medicare and Medicaid, require curtailment or restructuring of our operations and prohibit us from entering into government contracts.

Similar requirements may apply in foreign jurisdictions in which we may seek approval of our products. Any government investigation of alleged violations of law could require us to expend significant time and resources in response and could generate negative publicity. The occurrence of any event or penalty described above may inhibit our ability to commercialize our products and generate revenues.

In addition, the FDA’s regulations or policies may change and new or additional statutes or government regulations in the United States and other jurisdictions may be enacted that could prevent

or delay regulatory approval of our product candidates or further restrict or regulate post-approval activities. We cannot predict the likelihood, nature or extent of adverse government regulation that may arise from pending or future legislation or administrative action, either in the United States or abroad. If we are not able to achieve and maintain regulatory compliance, we may not be permitted to market our products and/or product candidates, which would adversely affect our ability to generate revenue and achieve or maintain profitability.

***The commercial success of Adzenys XR-ODT, Cotempla XR-ODT and Adzenys ER depends upon attaining market acceptance by physicians, patients, third-party payors and the medical community.***

To date, we have expended significant time, resources, and effort on the development of Adzenys XR-ODT, Cotempla XR-ODT and Adzenys ER, and a substantial majority of our resources are now focused on the commercialization in the United States of Adzenys XR-ODT, Cotempla XR-ODT and Adzenys ER. Accordingly, our ability to generate significant product revenue will depend almost entirely on our ability to successfully commercialize Adzenys XR-ODT, Cotempla XR-ODT and Adzenys ER.

Our ability to successfully commercialize Adzenys XR-ODT, Cotempla XR-ODT and Adzenys ER will depend on, among other things, our ability to:

- establish relationships with third-party suppliers for the active pharmaceutical ingredient (“API”), in Adzenys XR-ODT, Cotempla XR-ODT and Adzenys ER;
- manufacture and produce, through a validated process, sufficiently large quantities and inventory of Adzenys XR-ODT, Cotempla XR-ODT and Adzenys ER to permit successful commercialization;
- build and maintain a wide variety of internal sales, distribution and marketing capabilities sufficient to build commercial sales of our products;
- establish collaborations with third parties for the commercialization of our products in countries outside the United States, and such collaborators’ ability to obtain regulatory and reimbursement approvals in such countries;
- secure widespread acceptance of our products by physicians, health care payors, patients and the medical community;
- properly price and obtain adequate coverage and reimbursement of the product by governmental authorities, private health insurers, managed care organizations and other third-party payors;
- maintain compliance with ongoing FDA labeling, packaging, storage, advertising, promotion, recordkeeping, safety and other post-market requirements; and
- manage our growth and spending as costs and expenses increase due to commercialization.

There are no guarantees that we will be successful in completing these tasks. Successful commercialization will also depend on whether we can adequately protect against and effectively respond to any claims by holders of patents and other intellectual property rights that our products infringe their rights, whether any unanticipated adverse effects or unfavorable publicity develops in respect of our products, as well as the emergence of new or existing products as competition, which may be proven to be more clinically effective and cost-effective. If we are unable to successfully complete these tasks, we may not be able to commercialize Adzenys XR-ODT, Cotempla XR-ODT and Adzenys ER in a timely manner, or at all, in which case we may be unable to generate sufficient revenues to sustain and grow our business.

In addition, we will need to continue investing substantial financial and management resources to build out our commercial infrastructure and to recruit and train sufficient additional qualified

marketing, sales and other personnel to support the commercialization of Adzenys XR-ODT, Cotempla XR-ODT and Adzenys ER. In addition, we have certain revenue expectations with respect to the sale of Adzenys XR-ODT, Cotempla XR-ODT and Adzenys ER. If we cannot successfully commercialize and achieve those revenue expectations with respect to Adzenys XR-ODT, Cotempla XR-ODT and Adzenys ER, our anticipated revenues and liquidity will be materially adversely impacted.

Moreover, even if we are able to commercialize Adzenys XR-ODT, Cotempla XR-ODT and Adzenys ER, their continued commercial success may be largely dependent on the capability of third-party collaborators. Such third-party collaborators may not deploy the resources we would like them to, and our revenue would then suffer. In addition, we could become embroiled in disputes with these parties regarding the terms of any agreements, their performance or intellectual property rights. Any dispute could disrupt the sales of our products and adversely affect our reputation and revenue. In addition, if any of our manufacturing or collaboration partners fail to effectively perform under our arrangements for any reason, we may not be able to find a suitable replacement partner on a timely basis or on acceptable terms.

***We face significant competition from other biotechnology and pharmaceutical companies, and our operating results will suffer if we fail to compete effectively.***

The biopharmaceutical industries are intensely competitive and subject to rapid and significant technological change. We expect to have competitors both in the United States and internationally, including major multinational pharmaceutical companies, biotechnology companies and universities and other research institutions. For example, amphetamine XR is currently marketed in the United States by Shire under the brand names Adderall XR, Vyvanse and Mydayis and by Tris Pharmaceuticals, or Tris, under the brand name Dyanavel XR, a liquid suspension, and methylphenidate is marketed in the United States by Janssen under the brand name Concerta, by Pfizer under the brand name Quillivant XR, a reconstituted liquid suspension, and QuilliChew ER, a chewable formulation, by Rhodes Pharmaceuticals under the brand name Aptensio XR, a capsule, and by Novartis under the brand names Focalin XR and Ritalin LA. Further, makers of branded drugs could also enhance their own formulations in a manner that competes with our enhancements of these drugs. We are also aware of efforts by several pharmaceutical companies with ADHD medications in clinical development, including Sunovion, Kem Pharm and Neurovance.

Many of our competitors have substantially greater financial, technical and other resources, such as larger research and development staff and more experienced marketing and manufacturing organizations. Mergers and acquisitions in the biotechnology and pharmaceutical industries may result in even more resources being concentrated in our competitors. As a result, these companies may obtain regulatory approval more rapidly than we are able and may be more effective in selling and marketing their products as well. Smaller or early-stage companies may also prove to be significant competitors, particularly through collaborative arrangements with large, established companies. Competition may increase further as a result of advances in the commercial applicability of technologies and greater availability of capital for investment in these industries. Our competitors may succeed in developing, acquiring or licensing on an exclusive basis drug products or drug delivery technologies that are more effective or less costly than our XR-ODT or XR liquid suspension, or any product candidate that we are currently developing or that we may develop. In addition, our competitors may file citizens' petitions with the FDA in an attempt to persuade the FDA that our products, or the nonclinical studies or clinical trials that support their approval, contain deficiencies or that new regulatory requirements be placed on the product candidate or drug class of the product candidate. Such actions by our competitors could delay or even prevent the FDA from approving any NDA that we submit under Section 505(b)(2).

We believe that our ability to successfully compete will depend on, among other things:

- the ability to commercialize and market any of our products and product candidates that receive regulatory approval;
- the price of our products and product candidates that receive regulatory approval, including in comparison to branded or generic competitors;
- the efficacy and safety of our products and product candidates, including as relative to marketed products and product candidates in development by third parties;
- the ability to manufacture on a cost-effective basis and sell commercial quantities of our products and product candidates that receive regulatory approval;
- acceptance of any of our products and product candidates that receive regulatory approval by physicians and other healthcare providers;
- the time it takes for our product candidates to complete clinical development and receive marketing approval;
- the ability to maintain a good relationship with regulatory authorities;
- whether coverage and adequate levels of reimbursement are available under private and governmental health insurance plans, including Medicaid and Medicare; and
- the ability to protect intellectual property rights related to our product and product candidates.

If our competitors market products that are more effective, safer or less expensive than our products or that reach the market sooner than our products we may enter the market too late in the cycle and may not achieve commercial success, or we may have to reduce our price, which would impact our ability to generate revenue and obtain profitability. In addition, the biopharmaceutical industry is characterized by rapid technological change. Because we have limited research and development capabilities, it may be difficult for us to stay abreast of the rapid changes in each technology. If we fail to stay at the forefront of technological change, we may be unable to compete effectively. Technological advances or products developed by our competitors may render our technologies or product candidates obsolete, less competitive or not economical.

***If we are unable to differentiate our products or product candidates from branded drugs or existing generic therapies for similar treatments, or if the FDA or other applicable regulatory authorities approve generic products that compete with any of our products or product candidates, our ability to successfully commercialize such products or product candidates would be adversely affected.***

We expect to compete against branded drugs and to compete with their generic counterparts that will be sold for a lower price. Although we believe that our products and product candidates will be differentiated from branded drugs and their generic counterparts, if any, including through clinical efficacy or through improved patient compliance and ease of administration, it is possible that such differentiation will not impact our market position. If we are unable to achieve significant differentiation for our products and product candidates against other drugs, the opportunity for our products and, if approved, product candidates to achieve premium pricing and be commercialized successfully would be adversely affected.

After an NDA, including a 505(b)(2) application, is approved, the covered product becomes a “listed drug” that, in turn, can be cited by potential competitors in support of approval of an abbreviated new drug application, or ANDA. The FDCA, implementing regulations and other applicable laws provide incentives to manufacturers to create modified, non-infringing versions of a drug to facilitate the approval of an ANDA or other application for generic substitutes. These manufacturers might only be required to conduct a relatively inexpensive study to show that their

product has the same active ingredient(s), dosage form, strength, route of administration, and conditions of use, or labeling as our product candidate and that the generic product is bioequivalent to ours, meaning it is absorbed in the body at the same rate and to the same extent as our product candidate. These generic equivalents, which must meet the same quality standards as the listed drugs, would be significantly less costly than ours to bring to market and companies that produce generic equivalents are generally able to offer their products at lower prices.

Thus, after the introduction of a generic competitor, a significant percentage of the sales of any branded product, such as Adzenys XR-ODT, Cotempla XR-ODT or Adzenys ER can be lost to the generic version. Accordingly, competition from generic equivalents to our product candidates would materially adversely impact our revenues, profitability and cash flows and substantially limit our ability to obtain a return on the investments we have made in our product candidates.

For example, on July 25, 2016, we received a paragraph IV certification from Actavis Laboratories FL, Inc. (“Actavis”) advising us that Actavis had filed an ANDA with the FDA for a generic version of Adzenys XR-ODT. On September 1, 2016, we filed a patent infringement lawsuit in federal district court in the District of Delaware against Actavis, Inc. This case alleged that Actavis infringed our Adzenys XR-ODT patents by submitting to the FDA an ANDA seeking to market a generic version of Adzenys XR-ODT prior to the expiration of our patents. This lawsuit automatically stayed, or barred, the FDA from approving Actavis’s ANDA for 30 months or until a district court decision that is adverse to the asserted patents is rendered, whichever is earlier.

On October 17, 2017, we entered into a Settlement Agreement and a Licensing Agreement (collectively, the “Agreement”) with Actavis. This Agreement resolves all ongoing litigation involving our Adzenys XR-ODT patents and Actavis’s ANDA. Under the Agreement, we have granted Actavis the right to manufacture and market its generic version of Adzenys XR-ODT under the ANDA beginning on September 1, 2025, or earlier under certain circumstances. A stipulation and order of dismissal was entered by the U.S. District Court for the District of Delaware. The Agreement has been submitted to the applicable governmental agencies.

On October 31, 2017, we received a paragraph IV certification from Teva Pharmaceuticals USA, Inc. (“Teva”) advising us that Teva has filed an ANDA with the FDA for a generic version of Cotempla XR-ODT, in connection with seeking to market its product prior to the expiration of patents covering Cotempla XR-ODT. On December 13, 2017, we filed a patent infringement lawsuit in federal district court in the District of Delaware against Teva. This case alleged that Teva infringed our Cotempla XR-ODT patents by submitting to the FDA an ANDA seeking to market a generic version of Cotempla XR-ODT prior to the expiration of our patents. This lawsuit automatically stayed, or barred, the FDA from approving Teva’s ANDA for 30 months or until a district court decision that is adverse to the asserted patents is rendered, whichever is earlier. We intend to vigorously enforce our intellectual property rights relating to Cotempla XR-ODT.

***The design, development, manufacture, supply and distribution of our products and product candidates are highly regulated processes and technically complex.***

We are subject to extensive regulation in connection with the preparation and manufacture of our products, product candidates and potential product candidates for clinical trials and commercial sale. Components of a finished therapeutic product approved for commercial sale or used in late-stage clinical trials must be manufactured in accordance with cGMPs and equivalent foreign standards. These regulations govern manufacturing processes and procedures, including record keeping, and the implementation and operation of quality systems to control and assure the quality of investigational products and products approved for sale. Poor control of production processes can lead to the introduction of adventitious agents or other contaminants, or to inadvertent changes in the properties or stability of our products and product candidates that may not be detectable in final product testing.

The development, manufacture, supply, and distribution of our generic Tussionex, Adzenys XR-ODT, Cotempla XR-ODT and Adzenys ER as well as any of our future potential product candidates, are highly regulated processes and technically complex. We, along with our third-party suppliers, must comply with all applicable regulatory requirements of the FDA and foreign authorities. For instance, because each of Adzenys XR-ODT, Cotempla XR-ODT and Adzenys ER is a regulated drug product and subject to the U.S. Drug Enforcement Administration (“DEA”) regulation, we have had to, and will continue to, need to secure state licenses from each state in which we intend to sell such product allowing us to distribute a regulated drug product in such state.

We must supply all necessary documentation in support of our regulatory filings for our product candidates on a timely basis and must adhere to applicable parts of the FDA’s Good Laboratory Practices, or GLP, and cGMP requirements enforced by the FDA through its facilities inspection program, and the equivalent standards of the regulatory authorities in other countries. Any failure to comply with cGMP requirements or failure to scale-up manufacturing processes, including any failure to deliver sufficient quantities of product candidates in a timely manner, could lead to a delay in, or failure to obtain, regulatory approval of any of our product candidates. Our facilities and quality systems must also pass a pre-approval inspection for compliance with the applicable regulations as a condition of regulatory approval of our product candidates or any of our other potential products. For example, the FDA conducted a cGMP and pre-approval inspection related to our NDA for Cotempla XR-ODT from May 27 to June 4, 2015. At the end of the inspection, the agency issued a Form FDA 483 with one observation finding that appropriate controls are not exercised over one of our computer systems in order to assure that changes in records are instituted only by authorized personnel. We implemented corrective action related to this observation and responded to the FDA, and the FDA closed the inspection. Additionally, in connection with a general cGMP and pre-approval inspection for Adzenys ER from July 11, 2017 to July 25, 2017, we received a Form FDA 483 with one observation related to complaint records failing to document the reason and the individual making the decision not to conduct a complaint investigation. We implemented corrective action related to this observation and responded to the FDA. In addition, the regulatory authorities in any country may, at any time, audit or inspect a manufacturing facility involved with the preparation of our product candidates or our other potential products or the associated quality systems for compliance with the regulations applicable to the activities being conducted. If these facilities and quality systems do not pass a pre-approval plant inspection, FDA approval of our product candidates, or the equivalent approvals in other jurisdictions, will not be granted.

Regulatory authorities also may, at any time following approval of a product for sale, audit our manufacturing facilities. If any such inspection or audit identifies a failure to comply with applicable regulations or if a violation of our product specifications or applicable regulations occurs independent of such an inspection or audit, we or the relevant regulatory authority may require remedial measures that may be costly and/or time-consuming for us to implement and that may include the temporary or permanent suspension of a clinical trial or commercial sales or the temporary or permanent closure of our facility. Any such remedial measures imposed upon us could materially harm our business. If we fail to maintain regulatory compliance, the FDA can impose regulatory sanctions including, among other things, refusal to approve a pending application for a new drug product or revocation of a pre-existing approval. As a result, our business, financial condition and results of operations may be materially harmed.

***For our approved products, we must comply with the requirements of the Drug Supply Chain Security Act, which outlines critical steps to build an electronic, interoperable system to identify and trace certain prescription drugs as they are distributed in the United States.***

For our approved drugs, we must comply with the requirements of the Drug Supply Chain Security Act, including those related to product tracing, verification, and authorized trading partners. Signed

into law on November 27, 2013, the Drug Supply Chain Security Act amended the FSCA and is being implemented over a ten-year period. The law's requirements include the ability to quarantine and promptly investigate suspect product, such as potentially counterfeit, diverted or stolen product, to determine if it is illegitimate, and notify our trading partners and the FDA of any illegitimate product. By November 27, 2017, we were required to place a unique product identifier on prescription drug packages, and such requirement will be enforced beginning November 2018. This identifier consists of the National Drug Code, serial number, lot number and expiration date, in the form of a 2-dimensional data matrix barcode that can be easily read electronically. If our drug products fail to bear this unique product identifier, they would be misbranded under the FDCA and our drug products may not be accepted into the supply chain.

***We rely on limited sources of supply for Adzenys XR-ODT, Cotempla XR-ODT, Adzenys ER and our generic Tussionex, and any disruption in the chain of supply may impact production and sales of Adzenys XR-ODT, Cotempla XR-ODT, Adzenys ER and our generic Tussionex, and cause delays in developing and commercializing our product candidates and currently manufactured and commercialized products.***

Our approved NDAs for Adzenys XR-ODT, Cotempla XR-ODT and Adzenys ER, include our proposed manufacturing process for each product candidate. Any change to our manufacturing process, facilities or suppliers could require that we supplement our approved NDA. Also, because of our proprietary processes for manufacturing our product candidates, we cannot immediately transfer manufacturing activities for Adzenys XR-ODT, Cotempla XR-ODT, Adzenys ER or our generic Tussionex to an alternate supplier, and a change of facilities would be a time-consuming and costly endeavor.

Any changes to our manufacturing process would involve substantial cost and could result in a delay in our desired clinical and commercial timelines. We are also reliant on a limited number of suppliers for resin, drug compounds, coating and other component substances of our final product candidates and products. If any of these single-source suppliers were to breach or terminate its supply agreement, if any, with us or otherwise not supply us, we would need to identify an alternative source for the supply of component substances for our product candidates and products. Identifying an appropriately qualified source of alternative supply for any one or more of the component substances for our product candidates or products could be time consuming, and we may not be able to do so without incurring material delays in the development and commercialization of our approved products or product candidates or a decrease in sales of our generic Tussionex, which could harm our financial position and commercial potential for our product candidates and products. Any alternative vendor would also need to be qualified through an NDA supplement which could result in further delay, including delays related to additional clinical trials. The FDA, DEA, or other regulatory agencies outside of the United States may also require additional studies if we enter into agreements with new suppliers for the manufacture of Adzenys XR-ODT, Cotempla XR-ODT, Adzenys ER and our generic Tussionex that differ from the suppliers used for clinical development of such product candidates.

These factors could cause the delay of clinical trials, regulatory submissions, required approvals or commercialization of our products and product candidates, cause us to incur higher costs and prevent us from commercializing them successfully. Furthermore, if our suppliers fail to deliver the required commercial quantities of components and APIs on a timely basis and at commercially reasonable prices, including if our suppliers did not receive adequate DEA quotas for the supply of certain scheduled components, and we are unable to secure one or more replacement suppliers capable of production at a substantially equivalent cost, commercialization of Adzenys XR-ODT, Cotempla XR-ODT, Adzenys ER, our generic Tussionex and clinical trials of future potential product candidates, may be delayed or we could lose potential revenue and our business, financial condition, results of operation and reputation could be adversely affected.

***If we fail to produce our products or product candidates in the volumes that we require on a timely basis, or fail to comply with stringent regulations applicable to pharmaceutical drug manufacturers, we may face penalties from wholesalers and contracted retailers of our products and delays in the development and commercialization of our product candidates.***

We currently depend on third-party suppliers for the supply of the APIs for our products and product candidates, including drug substance for nonclinical research, clinical trials and commercialization. For Adzenys XR-ODT, Cotempla XR-ODT, Adzenys ER and our generic Tussionex, we currently rely on single suppliers for raw materials including APIs, which we use to manufacture, produce and package final dosage forms. In particular, we have an exclusive supply agreement with Coating Place, Inc. (“CPI”), pursuant to which CPI (i) is the exclusive supplier of the active ingredient complexes in our generic Tussionex and (ii) has agreed to not supply anyone else engaged in the production of generic Tussionex with such active ingredient complexes. Any future curtailment in the availability of raw materials could result in production or other delays with consequent adverse effects on us. In addition, because regulatory authorities must generally approve raw material sources for pharmaceutical products, changes in raw material suppliers may result in production delays or higher raw material costs. We are subject to penalties from wholesalers and contracted retailers if we do not deliver our generic Tussionex in quantities that meet their demand, and in the future we may enter into agreements with similar penalties for Adzenys XR-ODT, Cotempla XR-ODT and Adzenys ER. Any such delays could trigger these penalty provisions, which would have a negative impact on our business.

The manufacture of pharmaceutical products requires significant expertise and capital investment, including the development of advanced manufacturing techniques and process controls. Pharmaceutical companies often encounter difficulties in manufacturing, particularly in scaling up production of their products. These problems include manufacturing difficulties relating to production costs and yields, quality control, including stability of the product and quality assurance testing, shortages of qualified personnel, as well as compliance with federal, state and foreign regulations. If we are unable to demonstrate stability in accordance with commercial requirements, or if our raw material manufacturers were to encounter difficulties or otherwise fail to comply with their obligations to us, our ability to obtain FDA approval and market our products and product candidates would be jeopardized. In addition, any delay or interruption in the supply of clinical trial supplies could delay or prohibit the completion of our bioequivalence and/or clinical trials, increase the costs associated with conducting our bioequivalence and/or clinical trials and, depending upon the period of delay, require us to commence new trials at significant additional expense or to terminate a trial.

Manufacturers of pharmaceutical products need to comply with cGMP requirements enforced by the FDA through their facilities inspection programs. These requirements include, among other things, quality control, quality assurance and the maintenance of records and documentation. We may be unable to comply with these cGMP requirements and with other FDA and foreign regulatory requirements. A failure to comply with these requirements may result in fines and civil penalties, suspension of production, suspension or delay in product approval, product seizure or voluntary recall, or withdrawal of product approval. If the safety of any of our products or product candidates is compromised due to failure to adhere to applicable laws or for other reasons, we may not be able to obtain, or to maintain once obtained, regulatory approval for such products or product candidate or successfully commercialize such products or product candidates, and we may be held liable for any injuries sustained as a result. Any of these factors could cause a delay in clinical development, regulatory submissions, approvals or commercialization of our products or product candidates, entail higher costs or result in our being unable to effectively commercialize our product candidates. The FDA conducted a cGMP and pre-approval inspection related to our NDA for Cotempla XR-ODT from May 27 to June 4, 2015. At the end of the inspection, the agency issued a Form FDA 483 with one observation finding that appropriate controls are not exercised over one of our computer systems in order to assure that changes in records are instituted only by authorized personnel. We implemented



corrective action related to this observation and responded to the FDA, and the FDA closed the inspection. In addition, in connection with a general cGMP and pre-approval inspection for Adzenys ER from July 11 to July 25, 2017, we received a Form FDA 483 with one observation related to complaint records failing to document the reason and the individual making the decision not to conduct a complaint investigation. We implemented corrective action related to this observation and responded to the FDA.

***If we fail to manufacture Adzenys XR-ODT, Cotempla XR-ODT or, Adzenys ER in sufficient quantities and at acceptable quality and pricing levels, or fail to obtain adequate DEA quotas for controlled substances, or to fully comply with cGMP regulations, we may face delays in the commercialization of these products or our product candidates, if approved, or be unable to meet market demand, and may be unable to generate potential revenues.***

The manufacture of pharmaceutical products requires significant expertise and capital investment, including the development of advanced manufacturing techniques and process controls, and the use of specialized processing equipment. In order to meet anticipated demand for Adzenys XR-ODT, Cotempla XR-ODT and Adzenys ER we have installed specialized processing equipment in our Grand Prairie, Texas facilities, which we believe will produce sufficient quantities of our products for commercialization. We purchase raw materials and components from various suppliers in order to manufacture Adzenys XR-ODT, Cotempla XR-ODT and Adzenys ER. If we are unable to source the required raw materials from our suppliers, or if we do not obtain DEA quotas or receive inadequate DEA quotas, we may experience delays in manufacturing Adzenys XR-ODT, Cotempla XR-ODT and Adzenys ER, and may not be able to meet our customers' demands for our products.

In addition, we must comply with federal, state and foreign regulations, including cGMP requirements enforced by the FDA through its facilities inspection program. Any failure to comply with applicable regulations may result in fines and civil penalties, suspension of production, suspension or delay in product approval, product seizure or voluntary recall, or withdrawal of product approval, and would limit the availability of our products. Any manufacturing defect or error discovered after products have been produced and distributed could result in even more significant consequences, including costly recall procedures, re-stocking costs, damage to our reputation and potential for product liability claims.

Our Grand Prairie facility was formerly operated by our predecessor, PharmaFab, Inc., or PharmaFab. In April 2007, the FDA announced entry of a Consent Decree of Permanent Injunction, or the Consent Decree, against PharmaFab, one of its subsidiaries and two of its officials, including Mark Tengler, a former officer of ours who was, at the time, PharmaFab's president, and Russ McMahan, our Senior Vice President of Scientific Affairs, who held a similar position at the time with PharmaFab, or jointly, the Defendants. The Consent Decree arose out of several perceived cGMP deficiencies related to the manufacture of unapproved drugs or Drug Efficacy Study Implementation ("DESI"), drugs that we no longer manufacture. Pursuant to the Consent Decree, the Defendants were permanently restrained and enjoined from directly or indirectly manufacturing, processing, packing, labeling, holding or distributing any prescription drugs that are not the subject of an NDA or an abbreviated NDA. Among other things, the Consent Decree also granted the FDA the ability to, without prior notice, inspect PharmaFab's place of business and take any other measures necessary to monitor and ensure continuing compliance with the terms of the Consent Decree. The FDA has inspected the Grand Prairie facility several times since the Consent Decree was entered, and we have been able to manufacture and ship our generic Tussionex, Adzenys XR-ODT, Cotempla XR-ODT, and Adzenys ER for commercial distribution and drug products for our clinical trials. Although we have concluded the annual audit program prescribed by the Consent Decree entered into by our predecessor, our facilities may be inspected by the FDA at any time as a result of the Consent Decree. Although for our most recent annual audit by the cGMP expert in November 2014, the expert concluded that our corrective

actions satisfactorily addressed the observations noted in its report, on May 22, 2015, the FDA's Dallas District Office identified three ongoing cGMP deviations in our response to the audit related to batch failure investigations, quality control unit procedures, and in-process specifications. We implemented corrective actions and submitted additional information in our response to the FDA pursuant to the Consent Decree and the FDA closed the matter. Although we may apply for relief from the Consent Decree in the future, there is no guarantee that such relief will be granted or that we will be in compliance with the requirements of the Consent Decree.

If we are unable to produce the required commercial quantities of Adzenys XR-ODT, Cotempla XR-ODT or Adzenys ER to meet market demand for Adzenys XR-ODT, Cotempla XR-ODT and Adzenys ER on a timely basis or at all, or if we fail to comply with applicable laws for the manufacturing of Adzenys XR-ODT, Cotempla XR-ODT or Adzenys ER, we will suffer damage to our reputation and commercial prospects and we will be unable to generate potential revenues.

***If we are unable to support demand for Adzenys XR-ODT, Cotempla XR-ODT and Adzenys ER and any future product candidates, including ensuring that we have adequate capacity to meet increased demand, or we are unable to successfully manage the evolution of our drug delivery technology platform, our business could suffer.***

As our volume grows, we will need to continue to increase our workflow capacity for customer service, improve our billing and general process, expand our internal quality assurance program and extend our platform to support product production at a larger scale within expected turnaround times. We may need additional certified laboratory scientists and other scientific and technical personnel to process higher volumes of Adzenys XR-ODT, Cotempla XR-ODT and Adzenys ER. Portions of our process are not automated and will require additional personnel to scale. We may also need to purchase additional equipment, some of which can take several months or more to procure, set up and validate, and increase our software and computing capacity to meet increased demand. There is no assurance that any of these increases in scale, expansion of personnel, equipment, software and computing capacities, or process enhancements will be successfully implemented, or that we will have adequate space in our facilities to accommodate such required expansion.

As additional products, such as Adzenys XR-ODT, Cotempla XR-ODT and Adzenys ER, are commercialized, we will need to incorporate new equipment, implement new technology systems and laboratory processes and hire new personnel with different qualifications. Failure to manage this growth or transition could result in turnaround time delays, higher product costs, declining product quality, deteriorating customer service and slower responses to competitive challenges. A failure in any one of these areas could make it difficult for us to meet market expectations for our products and could damage our reputation and the prospects for our business.

***If our sole facility becomes damaged or inoperable or we are required to vacate our facility, our ability to manufacture Adzenys XR-ODT, Cotempla XR-ODT, Adzenys ER, our generic Tussionex or future potential product candidates for clinical development, may be jeopardized. Our inability to continue manufacturing adequate supplies of our products could adversely affect our ability to generate revenues.***

All of our manufacturing capabilities are housed in our sole manufacturing facility located in Grand Prairie, Texas. Our facility and equipment could be harmed or rendered inoperable by natural or man-made disasters, including war, fire, tornado, power loss, communications failure or terrorism, any of which may render it difficult or impossible for us to operate our drug delivery technology platform and manufacture our product candidates or products for some period of time. The inability to manufacture our products and product candidates if our facility or our equipment is inoperable, for even a short period of time, may result in the loss of customers or harm to our reputation, and we may be unable to regain those customers or repair our reputation in the future. Furthermore, our facility and the equipment we use to manufacture our products and product candidates could become damaged

and time-consuming to repair or replace. It would be difficult, time-consuming and expensive to rebuild our facility or repair or replace our equipment or license or transfer our proprietary technology to a third-party, particularly in light of the requirements for a DEA-registered manufacturing and storage facility like ours. If we are required to change or add a new manufacturer or supplier, the process would likely require prior FDA, DEA and/or equivalent foreign regulatory authority approval, and would be very time consuming. Even in the unlikely event we are able to find a third party with such qualifications to enable us to manufacture our products or product candidates, we may be unable to negotiate commercially reasonable terms.

We carry insurance for damage to our property and the disruption of our business, but this insurance may not cover all of the risks associated with damage or disruption to our business, may not provide coverage in amounts sufficient to cover our potential losses and may not continue to be available to us on acceptable terms, if at all. An inability to continue manufacturing adequate supplies of Adzenys XR-ODT, Cotempla XR-ODT, Adzenys ER or our generic Tussionex at our Grand Prairie, Texas facilities could result in a disruption in the supply of Adzenys XR-ODT, Cotempla XR-ODT, Adzenys ER, or our generic Tussionex to physicians and pharmacies, which would adversely affect our ability to generate revenues.

***If other forms of our products and product candidates are approved and successfully commercialized by other third parties, especially if approved before we can successfully commercialize our products and product candidates, our business would be materially harmed.***

Other third parties may seek approval to manufacture and market their own versions of product candidates in our product pipeline in the United States. If any of these parties obtain FDA approval of such a competitive product before we do, they may be entitled to three years of marketing exclusivity. Such exclusivity would, for example, delay the commercialization of our product candidates and, as a result, we may never achieve significant market share for these products. Consequently, revenues from product sales of these products would be similarly delayed and our business, including our development programs, and growth prospects would suffer. Even if any of our product candidates are approved before a competitor's product candidate, we may not be entitled to any marketing exclusivity and, other than under circumstances in which third parties may infringe or are infringing our patents, we may not be able to prevent the submission or approval of another full NDA for any competitor's product candidate.

***Amphetamine, methylphenidate and hydrocodone are Schedule II controlled substances under the Controlled Substances Act, and any failure to comply with this Act or its state equivalents would have a negative impact on our business.***

Amphetamine, methylphenidate and hydrocodone are listed by the DEA as a Schedule II controlled substance under the Controlled Substances Act ("CSA"). The DEA classifies substances as Schedule I, II, III, IV or V controlled substances, with Schedule I controlled substances considered to present the highest risk of substance abuse and Schedule V controlled substances the lowest risk. Scheduled controlled substances are subject to DEA regulations relating to supply, procurement, manufacturing, storage, distribution and physician prescription procedures. For example, Schedule II controlled substances are subject to various restrictions, including, but not limited to, mandatory written prescriptions and the prohibition of refills. In addition to federal scheduling, some drugs may be subject to state-controlled substance laws and regulations and more extensive requirements than those determined by the DEA and FDA. Though state controlled substances laws often mirror federal law, because the states are separate jurisdictions, they may schedule products separately. While some states automatically schedule a drug when the DEA does so, other states require additional state rulemaking or legislative action, which could delay commercialization. Some state and local governments also

require manufacturers to operate a drug stewardship program that collects, secures, transports and safely disposes of unwanted drugs.

Entities must register annually with the DEA to manufacture, distribute, dispense, import, export and conduct research using controlled substances. In addition, the DEA requires entities handling controlled substances to maintain records and file reports, including those for thefts or losses of any controlled substances, and to obtain authorization to destroy any controlled substances.

Registered entities also must follow specific labeling and packaging requirements, and provide appropriate security measures to control against diversion of controlled substances. Security requirements vary by controlled substance schedule with the most stringent requirements applying to Schedule I and Schedule II controlled substances. Required security measures include background checks on employees and physical control of inventory through measures such as vaults and inventory reconciliations. Failure to follow these requirements can lead to significant civil and/or criminal penalties and possibly even lead to a revocation of a DEA registration. The DEA also has a production and procurement quota system that controls and limits the availability and production of Schedule I or II controlled substances. If we or any of our suppliers of raw materials that are DEA-classified as Schedule I or II controlled substances are unable to receive any quota or a sufficient quota to meet demand for our products, if any, our business would be negatively impacted.

Products containing controlled substances may generate public controversy. As a result, these products may have their marketing approvals withdrawn. Political pressures and adverse publicity could lead to delays in, and increased expenses for, and limit or restrict, the introduction and marketing of our product or product candidates.

***Legislative or regulatory reform of the health care system in the United States may adversely impact our business, operations or financial results.***

Our industry is highly regulated and changes in law may adversely impact our business, operations or financial results. In particular, in March 2010, the Patient Protection and Affordable Care Act, as amended by the Health Care and Education Reconciliation Act of 2010 (collectively the “Affordable Care Act”), was signed into law. This legislation changes the current system of healthcare insurance and benefits intended to broaden coverage and control costs. The law also contains provisions that will affect companies in the pharmaceutical industry and other healthcare related industries by imposing additional costs and changes to business practices. Provisions affecting pharmaceutical companies include the following:

- mandatory rebates for drugs sold into the Medicaid program have been increased, and the rebate requirement has been extended to drugs used in risk-based Medicaid managed care plans.
- the 340B Drug Pricing Program under the Public Health Service Act has been extended to require mandatory discounts for drug products sold to certain critical access hospitals, cancer hospitals and other covered entities.
- pharmaceutical companies are required to offer discounts on branded drugs to patients who fall within the Medicare Part D coverage gap, commonly referred to as the “Donut Hole.”
- pharmaceutical companies are required to pay an annual non-tax deductible fee to the federal government based on each company’s market share of prior year total sales of branded drugs to certain federal healthcare programs, such as Medicare, Medicaid, Department of Veterans Affairs and Department of Defense. The aggregated industry-wide fee is expected to total \$28.0 billion through 2019. Since we expect our branded pharmaceutical sales to constitute a small portion of the total federal health program pharmaceutical market, we do not expect this annual assessment to have a material impact on our financial condition.

Despite initiatives to invalidate the Affordable Care Act, the U.S. Supreme Court has upheld certain key aspects of the legislation, including a tax-based shared responsibility payment imposed on certain individuals who fail to maintain qualifying health coverage for all or part of a year, which is commonly referred to as the “individual mandate”. However, the new presidential administration has indicated that enacting changes to the Affordable Care Act is a legislative priority, and has discussed repealing and replacing the Affordable Care Act or amending the Affordable Care Act. For example, Congress has considered legislation that would repeal or repeal and replace all or part of the ACA. While Congress has not passed repeal legislation, the Tax Cuts and Jobs Act of 2017 includes a provision repealing the individual mandate, effective January 1, 2019. In addition, since January 2017, President Trump has signed two Executive Orders designed to delay the implementation of certain provisions of the ACA or otherwise circumvent some of the requirements for health insurance mandated by the ACA. Further, the Trump administration has concluded that cost-sharing reduction, or CSR, payments to insurance companies required under the ACA have not received necessary appropriations from Congress and announced that it will discontinue these payments immediately until such appropriations are made. The loss of the CSR payments is expected to increase premiums on certain policies issued by qualified health plans under the ACA. A bipartisan bill to appropriate funds for CSR payments was introduced in the Senate, but the future of that bill is uncertain. Several state Attorneys General filed suit to stop the administration from terminating the subsidies, but their request for a restraining order was denied by a federal judge in California on October 25, 2017. In addition, CMS has recently proposed regulations that would give states greater flexibility in setting benchmarks for insurers in the individual and small group marketplaces, which may have the effect of relaxing the essential health benefits required under the ACA for plans sold through such marketplaces. In 2018, Congress may consider other legislation to repeal and replace elements of the Affordable Care Act, and litigation and legislation over the Affordable Care Act are likely to continue, with unpredictable and uncertain results. Changes to the Affordable Care Act or other existing health care regulations could significantly impact our business and the pharmaceutical industry. Although it is too early to determine the effect of legal challenges, pending legislation, and executive action on the Affordable Care Act, the law appears likely to continue the pressure on pharmaceutical pricing, especially under the Medicare program, and may also increase our regulatory burdens and operating costs.

Additionally, other federal health reform measures have been proposed and adopted in the United States since the ACA was enacted:

- The Budget Control Act of 2011, among other things, created measures for spending reductions by Congress. A Joint Select Committee on Deficit Reduction, tasked with recommending a targeted deficit reduction of at least \$1.2 trillion for the years 2013 through 2021, was unable to reach required goals, thereby triggering the legislation’s automatic reduction to several government programs. These changes included aggregate reductions to Medicare payments to providers of up to 2% per fiscal year, which went into effect in April 2013 and will remain in effect through 2025 unless additional Congressional action is taken.
- The American Taxpayer Relief Act of 2012, among other things, reduced Medicare payments to several providers, and increased the statute of limitations period for the government to recover overpayments to providers from three to five years.
- The Middle Class Tax Relief and Job Creation Act of 2012 required that the Centers for Medicare & Medicaid Services reduce the Medicare clinical laboratory fee schedule by 2% in 2013, which served as a base for 2014 and subsequent years. In addition, effective January 1, 2014, CMS also began bundling the Medicare payments for certain laboratory tests ordered while a patient received services in a hospital outpatient setting.

Further, there has been heightened governmental scrutiny over the manner in which manufacturers set prices for their marketed products, which have resulted in several recent Congressional inquiries

and proposed bills designed to, among other things, bring more transparency to product pricing, review the relationship between pricing and manufacturer patient programs, and reform government program reimbursement methodologies for products. In addition, the United States government, state legislatures, and foreign governments have shown significant interest in implementing cost containment programs, including price-controls, restrictions on reimbursement and requirements for substitution of generic products for branded prescription drugs to limit the growth of government paid health care costs. Individual states in the United States have become increasingly aggressive in passing legislation and implementing regulations designed to control pharmaceutical and biological product pricing, including price or patient reimbursement constraints, discounts, restrictions on certain product access and marketing cost disclosure and transparency measures, and, in some cases, designed to encourage importation from other countries and bulk purchasing. We anticipate pricing scrutiny will continue and escalate, including on a global basis. As a result, our business and reputation may be harmed, our stock price may be adversely impacted and experience periods of volatility, and our results of operations may be adversely impacted

In addition, in September 2007, the Food and Drug Administration Amendments Act of 2007 was enacted giving the FDA enhanced post-marketing authority including the authority to require post-marketing studies and clinical trials, labeling changes based on new safety information and compliance with REMS approved by the FDA. The FDA's exercise of this authority could result in delays or increased costs during product development, clinical trials and regulatory review, increased costs to ensure compliance with post-approval regulatory requirements and potential restrictions on the sale and/or distribution of approved products.

Moreover, we cannot predict what healthcare reform initiatives may be adopted in the future. Further federal and state legislative and regulatory developments are likely, and we expect ongoing initiatives in the United States to increase pressure on drug pricing. Such reforms could have an adverse effect on anticipated revenues from product candidates that we may successfully develop and for which we may obtain regulatory approval and may affect our overall financial condition and ability to develop product candidates.

***If we fail to comply with environmental, health and safety laws and regulations, we could become subject to fines or penalties or incur costs that could have a material adverse effect on the success of our business.***

We are subject to numerous environmental, health and safety laws and regulations. Our operations involve the use of hazardous and flammable materials, including chemicals and biological materials. Our operations also produce hazardous waste products. We generally contract with third parties for the disposal of these materials and wastes. We cannot eliminate the risk of contamination or injury from these materials. In the event of contamination or injury resulting from our use of hazardous materials, we could be held liable for any resulting damages, and any liability could exceed our resources. We also could incur significant costs associated with civil or criminal fines and penalties.

Although we maintain workers' compensation insurance to cover us for costs and expenses we may incur due to injuries to our employees resulting from the use of hazardous materials or other work-related injuries, this insurance may not provide adequate coverage against potential liabilities. In addition, we may incur substantial costs in order to comply with current or future environmental, health and safety laws and regulations. These current or future laws and regulations may impair our research, development or production efforts. Failure to comply with these laws and regulations also may result in substantial fines, penalties or other sanctions.

***If we are unable to achieve and maintain adequate levels of coverage and reimbursement for our products or, if approved, product candidates their commercial success may be severely hindered.***

Successful sales of our products and any product candidates that receive regulatory approval depend on the availability of adequate coverage and reimbursement from third-party payors. Patients who are prescribed medications for the treatment of their conditions generally rely on third-party payors to reimburse all or part of the costs associated with their prescription drugs. Adequate coverage and reimbursement from governmental healthcare programs, such as Medicare and Medicaid, and commercial payors is critical to new product acceptance. Coverage decisions may depend upon clinical and economic standards that disfavor new drug products when more established or lower cost therapeutic alternatives are already available or subsequently become available. Assuming we obtain coverage for a given product, the resulting reimbursement payment rates might not be adequate or may require co-payments that patients find unacceptably high. Patients are unlikely to use our products unless coverage is provided and reimbursement is adequate to cover a significant portion of the cost of our products.

In addition, the market for Adzenys XR-ODT, Cotempla XR-ODT and Adzenys ER will depend significantly on access to third-party payors' drug formularies, or lists of medications for which third-party payors provide coverage and reimbursement. The industry competition to be included in such formularies often leads to downward pricing pressures on pharmaceutical companies. Also, third-party payors may refuse to include a particular branded drug in their formularies or otherwise restrict patient access through formulary controls or otherwise to a branded drug when a less costly generic equivalent or other alternative is available.

Third-party payors, whether foreign or domestic, or governmental or commercial, are developing increasingly sophisticated methods of controlling healthcare costs. In addition, in the United States, no uniform policy requirement for coverage and reimbursement for drug products exists among third-party payors. Therefore, coverage and reimbursement for drug products can differ significantly from payor to payor. As a result, the coverage determination process is often a time-consuming and costly process that will require us to provide scientific and clinical support for the use of our products to each payor separately, with no assurance that coverage and adequate reimbursement will be applied consistently or obtained in the first instance.

Further, we believe that future coverage and reimbursement will likely be subject to increased restrictions both in the United States and in international markets. Third party coverage and reimbursement for our product candidates for which we may receive regulatory approval may not be available or adequate in either the United States or international markets, which could have a material adverse effect on our business, results of operations, financial condition and prospects.

***Our relationships with customers, healthcare providers and third-party payors are subject to applicable anti-kickback, fraud and abuse and other healthcare laws and regulations, which could expose us to criminal sanctions, civil penalties, contractual damages, reputational harm and diminished profits and future earnings.***

For our product and any product candidates that obtain regulatory approval and are marketed in the United States, our arrangements with third-party payors, healthcare providers, and customers may expose us to broadly applicable fraud and abuse and other healthcare laws and regulations that may constrain the business or financial arrangements and relationships through which we market, sell and distribute any products for which we obtain marketing approval. In addition, we may be subject to health information privacy and security regulation by U.S. federal and state governments and foreign jurisdictions in which we conduct our business. In the United States, these laws include, without

limitation, state and federal anti-kickback, false claims, physician transparency, and patient data privacy and security laws and regulations, including but not limited to those described below.:

- The federal Anti-Kickback Statute, makes it illegal for any person, including a prescription drug or biologic manufacturer (or a party on its behalf) to knowingly and willfully solicit, receive, offer or pay remuneration, directly or indirectly, in cash or in kind, that is intended to induce or reward referrals, either the referral of an individual, or the purchase, recommendation, order or prescription of a particular item, drug or service for which payment may be made under a federal healthcare program, such as the Medicare and Medicaid programs. Violations of this law are punishable by up to five years in prison, criminal fines, administrative civil money penalties and exclusion from participation in federal healthcare programs. In addition, a person or entity does not need to have actual knowledge of the statute or specific intent to violate it.
- The federal False Claims Act imposes civil penalties, including through civil whistleblower or qui tam actions, against individuals or entities (including manufacturers) for, among other things, knowingly presenting, or causing to be presented false or fraudulent claims for payment by a federal healthcare program or making a false statement or record material to payment of a false claim or avoiding, decreasing or concealing an obligation to pay money to the federal government. Penalties for a False Claims Act violation include three times the actual damages sustained by the government, plus mandatory civil penalties of between \$11,781 and \$22,363 for each separate false claim, the potential for exclusion from participation in federal healthcare programs and the potential implication of various federal criminal statutes. The government may deem manufacturers to have “caused” the submission of false or fraudulent claims by, for example, providing inaccurate billing or coding information to customers or promoting a product off-label. Claims which include items or services resulting from a violation of the federal Anti-Kickback Statute are false or fraudulent claims for purposes of the False Claims Act. Our future marketing and activities relating to the reporting of wholesaler or estimated retail prices for our products, the reporting of prices used to calculate Medicaid rebate information and other information affecting federal, state and third-party reimbursement for our products, and the sale and marketing of our product and any future product candidates, are subject to scrutiny under this law.
- Health Insurance Portability and Accountability Act of 1996 (“HIPAA”), which imposes criminal and civil liability for knowingly and willfully executing, or attempting to execute, a scheme to defraud any healthcare benefit program, including private payors, or falsifying, concealing or covering up a material fact, or making any materially false statements in connection with the delivery of or payment for healthcare benefits, items, or services.
- HIPAA, as amended by the Health Information Technology for Economic and Clinical Health Act of 2009 (“HITECH”), and their respective implementing regulations, which impose, among other things, specified requirements on covered entities and their business associates, relating to the privacy, and security of individually identifiable health information, including mandatory contractual terms and required implementation of technical safeguards of such information. HITECH also created new tiers of civil monetary penalties, amended HIPAA to make civil and criminal penalties applicable to business associates, and gave state attorneys general new authority to file civil actions for damage or injunctions in federal courts to enforce the federal HIPAA laws and seek attorneys’ fees and costs associated with pursuing federal civil actions.
- The Physician Payments Sunshine Act, enacted as part of the Affordable Care Act which imposed new annual reporting requirements for certain manufacturers of drugs, devices, biologics and medical supplies for which payment is available under Medicare, Medicaid or the Children’s Health Insurance Program for certain payments and other “transfers of value”



provided to physicians and teaching hospitals, and ownership and investment interests held by physicians and their immediate family members.

- Analogous state and foreign fraud and abuse laws and regulations, such as state anti-kickback and false claims laws, which may be broader in scope and apply regardless of payor. Such laws are enforced by various state agencies and through private actions. Some state laws require pharmaceutical companies to comply with the pharmaceutical industry's voluntary compliance guidelines and the relevant federal government compliance guidance, require drug manufacturers to report information related to payments and other transfers of value to physicians and other healthcare providers, and restrict marketing practices or require disclosure of marketing expenditures. State and foreign laws also govern the privacy and security of health information in certain circumstances. Such data privacy and security laws may differ from one another in significant ways and often are not preempted by HIPAA, thus complicating compliance efforts.

The scope and enforcement of each of these laws is uncertain and subject to rapid change in the current environment of healthcare reform, especially in light of the lack of applicable precedent and regulations. Federal and state enforcement bodies have recently increased their scrutiny of interactions between healthcare companies and healthcare providers, which has led to a number of investigations, prosecutions, convictions and settlements in the healthcare industry. It is possible that governmental authorities will conclude that our business practices do not comply with current or future statutes, regulations or case law involving applicable fraud and abuse or other healthcare laws and regulations. If our operations are found to be in violation of any of these laws or any other related governmental regulations that may apply to us, we may be subject to significant civil, criminal and administrative penalties, including, without limitation, damages, fines, imprisonment, disgorgement, exclusion from participation in government funded healthcare programs, such as Medicare and Medicaid, reputational harm, additional oversight and reporting obligations if we become subject to a corporate integrity agreement or similar settlement to resolve allegations of non-compliance with these laws and the curtailment or restructuring of our operations. If any of the physicians or other healthcare providers or entities with whom we expect to do business is found to be not in compliance with applicable laws, they may be subject to similar actions, penalties and sanctions. Efforts to ensure that our business arrangements comply with applicable healthcare laws and regulations, as well as responding to possible investigations by government authorities, can be time- and resource-consuming and can divert a company's attention from the business.

***Product liability lawsuits could divert our resources, result in substantial liabilities and reduce the commercial potential of our products.***

The risk that we may be sued on product liability claims is inherent in the development of pharmaceutical products. We face a risk of product liability exposure related to the testing of our product candidates in clinical trials and face even greater risks upon any commercialization by us of our products and product candidates. These lawsuits may divert our management from pursuing our business strategy and may be costly to defend. In addition, if we are held liable in any of these lawsuits, we may incur substantial liabilities and may be forced to limit or forego further commercialization of one or more of our products.

***Our product liability insurance coverage may not be adequate to cover any and all liabilities that we may incur.***

We currently have \$10.0 million in product liability insurance coverage in the aggregate, which may not be adequate to cover any and all liabilities that we may incur. Insurance coverage is increasingly expensive. We may not be able to maintain insurance coverage at a reasonable cost or in an amount adequate to satisfy any liability that may arise. Large judgments have been awarded in class action lawsuits based on drugs that had unanticipated side effects. A successful product liability claim or series

of claims brought against us, particularly if judgments exceed our insurance coverage, could decrease our cash and adversely affect our business. In addition, we may not be able to obtain or maintain sufficient insurance coverage at an acceptable cost or otherwise to protect against potential product liability claims, which could prevent or inhibit the commercial production and sale of our products. For example, we have experienced increasing difficulty in procuring insurance coverage for our products and product candidates due to their status as controlled substances.

## **RISKS RELATED TO THE CLINICAL DEVELOPMENT, REGULATORY REVIEW AND APPROVAL OF OUR PRODUCT CANDIDATES**

*Our failure to successfully identify, develop and market additional product candidates could impair our ability to grow.*

As part of our growth strategy, we intend to identify, develop and market additional product candidates. We are exploring various therapeutic opportunities for our pipeline and proprietary technologies. We may spend several years completing our development of any particular current or future internal product candidates, and failure can occur at any stage. The product candidates to which we allocate our resources may not end up being successful. In addition, because our internal research capabilities are limited, we may be dependent upon pharmaceutical companies, academic scientists and other researchers to sell or license product candidates, approved products or the underlying technology to us. The success of this strategy depends partly upon our ability to identify, select, discover and acquire promising product candidates and products.

The process of proposing, negotiating and implementing a license or acquisition of a product candidate or approved product is lengthy and complex. Other companies, including some with substantially greater financial, marketing and sales resources, may compete with us for the license or acquisition of product candidates and approved products. We have limited resources to identify and execute the acquisition or in-licensing of third-party products, businesses and technologies and integrate them into our current infrastructure. Moreover, we may devote resources to potential acquisitions or in-licensing opportunities that are never completed, or we may fail to realize the anticipated benefits of such efforts. We may not be able to acquire the rights to additional product candidates on terms that we find acceptable, or at all.

In addition, future acquisitions may entail numerous operational and financial risks, including:

- exposure to unknown liabilities;
- disruption of our business and diversion of our management's time and attention to develop acquired products or technologies;
- incurrence of substantial debt, dilutive issuances of securities or depletion of cash to pay for acquisitions;
- higher than expected acquisition and integration costs;
- difficulty in combining the operations and personnel of any acquired businesses with our operations and personnel;
- increased amortization expenses;
- impairment of relationships with key suppliers or customers of any acquired businesses due to changes in management and ownership; and
- inability to motivate key employees of any acquired businesses.

Further, any product candidate that we acquire may require additional development efforts prior to commercial sale, including extensive clinical testing and approval by the FDA and other regulatory authorities.

***Premarket review of our product candidates by the FDA or other regulatory authorities is a lengthy and uncertain process and approval may be delayed, limited or denied, any of which would adversely affect our ability to generate operating revenues.***

The FDA has substantial discretion in the drug approval process, including the ability to delay, limit or deny approval of a product candidate for many reasons. For example, the FDA:

- could determine that we cannot rely on the 505(b)(2) regulatory approval pathway for any future product candidate that we may identify and develop;
- could determine that the information provided by us was inadequate, contained clinical deficiencies or otherwise failed to demonstrate safety and effectiveness of any of our product candidates for any indication;
- may not find the data from bioequivalence studies and/or clinical trials sufficient to support the submission of an NDA or to obtain marketing approval in the United States, including any findings that the safety risks outweigh clinical and other benefits of our product candidates;
- may require us to conduct additional bioequivalence studies to demonstrate that the proposed commercial product is bioequivalent to the batch used in clinical trials;
- may disagree with our trial design or our interpretation of data from nonclinical studies, bioequivalence studies and/or clinical trials, or may change the requirements for approval even after it has reviewed and commented on the design for our trials;
- may determine that we inappropriately relied on a certain listed drug or drugs for our 505(b)(2) NDA or that approval of our applications for any future product candidate is blocked by patent or non-patent exclusivity of the listed drug or drugs;
- may identify deficiencies in the manufacturing processes or facilities of third-party manufacturers with which we enter into agreements for the supply of the API used in our product candidates;
- may identify deficiencies in our own manufacturing processes or our proposed scale-up of the manufacturing processes or facilities for the production of our product candidates;
- may approve our product candidates for fewer or more limited indications than we request, or may grant approval contingent on the performance of costly post-approval clinical trials;
- may change its approval policies or adopt new regulations; or
- may not approve the labeling claims that we believe are necessary or desirable for the successful commercialization of our product candidates.

Notwithstanding the approval of many products by the FDA pursuant to 505(b)(2), over the last few years, some pharmaceutical companies and others have objected to the FDA's interpretation of 505(b)(2). If the FDA changes its interpretation of 505(b)(2), or if the FDA's interpretation is successfully challenged in court, this could delay or even prevent the FDA from approving any 505(b)(2) application that we submit. Any failure to obtain regulatory approval of our product candidates would significantly limit our ability to generate revenues, and any failure to obtain such approval for all of the indications and labeling claims we deem desirable could reduce our potential revenues.

***If the FDA does not conclude that our product candidates satisfy the requirements for the 505(b)(2) regulatory approval pathway, or if the requirements for approval of any of our product candidates under Section 505(b)(2) are not as we expect, the approval pathway for our product candidates will likely take significantly longer, cost significantly more and encounter significantly greater complications and risks than anticipated, and in any case may not be successful.***

We intend to seek FDA approval through the 505(b)(2) regulatory approval pathway for each of our future product candidates in our product pipeline. The Drug Price Competition and Patent Term Restoration Act of 1984, commonly known as the Hatch-Waxman Amendments, added 505(b)(2) to the FDCA. Section 505(b)(2) permits the submission of an NDA where at least some of the information required for approval comes from trials that were not conducted by or for the applicant and for which the applicant does not have a right of reference.

If we cannot pursue the 505(b)(2) regulatory approval pathway for our product candidates as we intend, we may need to conduct additional nonclinical studies or clinical trials, provide additional data and information and meet additional requirements for regulatory approval. If this were to occur, the time and financial resources required to obtain FDA approval for our product candidates likely would increase substantially. Moreover, the inability to pursue the 505(b)(2) regulatory approval pathway could result in new competitive products reaching the market before our product candidates, which could materially adversely impact our competitive position and prospects. Even if we are allowed to pursue the 505(b)(2) regulatory approval pathway for a product candidate, we cannot assure you that we will receive the requisite or timely approvals for commercialization of such product candidate.

In addition, our competitors may file citizen petitions with the FDA in an attempt to persuade the FDA that our product candidates, or the clinical trials that support their approval, contain deficiencies or that new regulatory requirements be placed on the product candidate or drug class of the product candidate. Such actions by our competitors could delay or even prevent the FDA from approving any NDA that we submit under 505(b)(2).

***An NDA submitted under 505(b)(2) may subject us to a patent infringement lawsuit that would delay or prevent the review or approval of our product candidate.***

Our product candidates will be submitted to the FDA for approval under 505(b)(2) of the FDCA. Section 505(b)(2) permits the submission of an NDA where at least some of the information required for approval comes from trials that were not conducted by, or for, the applicant and for which the applicant has not obtained a right of reference. An NDA under 505(b)(2) would enable us to reference published literature and/or the FDA's previous findings of safety and effectiveness for the previously approved drug.

For NDAs submitted under 505(b)(2), the patent certification and related provisions of the Hatch-Waxman Amendments apply. Accordingly, we may be required to include certifications, known as Paragraph IV certifications, that certify that any patents listed in the Approved Drug Products with Therapeutic Equivalence Evaluations (commonly known as "the Orange Book"), with respect to any product referenced in the 505(b)(2) application, are invalid, unenforceable or will not be infringed by the manufacture, use or sale of the product that is the subject of the 505(b)(2) NDA.

Under the Hatch-Waxman Amendments, the holder of patents that the 505(b)(2) application references may file a patent infringement lawsuit after receiving notice of the Paragraph IV certification. Filing of a patent infringement lawsuit against the filer of the 505(b)(2) applicant within 45 days of the patent owner's receipt of notice triggers a one-time, automatic, 30-month stay of the FDA's ability to approve the 505(b)(2) NDA, unless patent litigation is resolved in favor of the Paragraph IV filer or the patent expires before that time. Accordingly, we may invest a significant amount of time and expense in the development of one or more product candidates only to be subject to significant delay and patent litigation before such product candidates may be commercialized, if at all.

In addition, a 505(b)(2) application will not be approved until any non-patent exclusivity, such as exclusivity for obtaining approval of a new chemical entity, or NCE, listed in the Orange Book for the listed drug has expired. The FDA also may require us to perform one or more additional clinical trials or measurements to support the change from the listed drug, which could be time consuming and could substantially delay our achievement of regulatory approval. The FDA also may reject any future 505(b)(2) submissions and require us to submit traditional NDAs under 505(b)(1), which would require extensive data to establish safety and effectiveness of the drug for the proposed use and could cause delay and additional costs. These factors, among others, may limit our ability to commercialize our product candidates successfully.

***Our approved products and product candidates may cause adverse effects or have other properties that could delay or prevent their regulatory approval or limit the scope of any approved label or market acceptance, or result in significant negative consequences following marketing approval, if any.***

As with many pharmaceutical products, treatment with our products or product candidates may produce undesirable side effects or adverse reactions or events. Although our products and product candidates contain active ingredients that have already been approved, meaning that the side effects arising from the use of the active ingredient or class of drug in our product candidates is generally known, our products or product candidates still may cause undesirable side effects. These could be attributed to the active ingredient or class of drug or to our unique formulation of such products or product candidates, or other potentially harmful characteristics. Such characteristics could cause us, institutional review boards, or IRBs, clinical trial sites, the FDA or other regulatory authorities to interrupt, delay or halt clinical trials and could result in a more restrictive label, if the product candidate is approved, or the delay, denial or withdrawal of regulatory approval, which may harm our business, financial condition and prospects significantly.

Further, if any of our products cause serious or unexpected side effects after receiving market approval, a number of potentially significant negative consequences could result, including:

- regulatory authorities may withdraw their approval of the product or impose restrictions on its distribution;
- the FDA may require implementation of a REMS;
- regulatory authorities may require the addition of labeling statements, such as warnings or contraindications;
- we may be required to change the way the product is administered or conduct additional clinical trials;
- we may need to voluntarily recall our products
- we could be sued and held liable for harm caused to patients; or
- our reputation may suffer.

Any of these events could prevent us from achieving or maintaining market acceptance of the affected product or product candidate and could substantially increase the costs of commercializing our products and product candidates.

***We will need to obtain FDA approval of any proposed names for our product candidates that gain marketing approval, and any failure or delay associated with such naming approval may adversely impact our business.***

Any name we intend to use for our product candidates will require approval from the FDA regardless of whether we have secured a formal trademark registration from the U.S. Patent and Trademark Office (“USPTO”). The FDA typically conducts a review of proposed product names, including an evaluation of whether proposed names may be confused with other product names. The FDA may object to any product name we submit if it believes the name inappropriately implies medical claims.

If the FDA objects to any of our proposed product names, we may be required to adopt an alternative name for our product candidates, which could result in further evaluation of proposed names with the potential for additional delays and costs.

***Obtaining and maintaining regulatory approval of our product candidates in one jurisdiction does not mean that we will be successful in obtaining regulatory approval of our product candidates in other jurisdictions.***

Even if we obtain and maintain regulatory approval of our product candidates in one jurisdiction, such approval does not guarantee that we will be able to obtain or maintain regulatory approval in any other jurisdiction, but a failure or delay in obtaining regulatory approval in one jurisdiction may have a negative effect on the regulatory approval process in others. For example, even if the FDA grants marketing approval of a product candidate, comparable regulatory authorities in foreign jurisdictions must also approve the manufacturing, marketing and promotion of the product candidate in those countries. Approval procedures vary among jurisdictions and can involve requirements and administrative review periods different from those in the United States, including additional nonclinical studies or clinical trials as investigations conducted in one jurisdiction may not be accepted by regulatory authorities in other jurisdictions. In many jurisdictions outside the United States, a product candidate must be approved for reimbursement before it can be approved for sale in that jurisdiction. In some cases, the price that we intend to charge for our products is also subject to approval.

Obtaining foreign regulatory approvals and compliance with foreign regulatory requirements could result in significant delays, difficulties and costs for us and could delay or prevent the introduction of our products in certain countries. If we fail to comply with the regulatory requirements in international markets and/or to receive applicable marketing approvals, our target market will be reduced and our ability to realize the full market potential of our product candidates will be harmed.

***We are heavily dependent on the success of our product candidates. We cannot give any assurance that we will receive regulatory approval for our product candidates, which is necessary before they can be commercialized.***

Our business and future success are substantially dependent on our ability to timely obtain regulatory approval for and commercialize any product candidates that we may identify and pursue. We are not permitted to market any of our product candidates in the United States until we receive approval of an NDA from the FDA, or in any foreign jurisdiction until we receive the requisite approvals from such jurisdiction. Satisfaction of regulatory requirements can be protracted, is dependent upon the type, complexity and novelty of the product candidate and requires the expenditure of substantial resources. We cannot predict whether we will obtain regulatory approval to commercialize our product candidates, and we cannot, therefore, predict the timing of any future revenues from these product candidates, if any. Any delay or setback in the regulatory approval or commercialization of any of these product candidates could adversely affect our business.

*The commencement and completion of clinical trials can be delayed or prevented for a number of reasons.*

We intend to identify, develop and market additional product candidates; however, we may not be able to commence or complete the clinical trials that would support the submission of an NDA to the FDA. Drug development is a long, expensive and uncertain process, and delay or failure can occur at any stage of any of our clinical trials. Clinical trials can be delayed or prevented for a number of reasons, including:

- difficulties obtaining regulatory approval to commence a clinical trial or complying with conditions imposed by a regulatory authority regarding the scope or term of a clinical trial;
- delays in reaching or failing to reach agreement on acceptable terms with prospective contract research organizations, or CROs, contract manufacturing organizations, or CMOs, and trial sites, the terms of which can be subject to extensive negotiation and may vary significantly among different CROs and trial sites;
- failure of our third-party contractors, such as CROs and CMOs, or our investigators to comply with regulatory requirements or otherwise meet their contractual obligations in a timely manner;
- insufficient or inadequate supply or quality of a product candidate or other materials necessary to conduct our clinical trials;
- difficulties obtaining IRB approval to conduct a clinical trial at a prospective site;
- the FDA requiring alterations to any of our study designs, our nonclinical strategy or our manufacturing plans;
- challenges recruiting and enrolling subjects to participate in clinical trials for a variety of reasons, including size and nature of subject population, proximity of subjects to clinical sites, eligibility criteria for the trial, nature of trial protocol, the availability of approved effective treatments for the relevant disease and competition from other clinical trial programs for similar indications;
- difficulties maintaining contact with subjects after treatment, which results in incomplete data;
- receipt by a competitor of marketing approval for a product targeting an indication that our product targets;
- governmental or regulatory delays and changes in regulatory requirements, policy and guidelines; and
- varying interpretations of data by the FDA and similar foreign regulatory agencies.

Clinical trials may also be delayed or terminated as a result of ambiguous or negative interim results. In addition, a clinical trial may be suspended or terminated by us, the FDA, the IRBs at the sites where the IRBs are overseeing a trial, or a data safety monitoring board overseeing the clinical trial at issue, or other regulatory authorities due to a number of factors, including:

- failure to conduct the clinical trial in accordance with regulatory requirements or our clinical protocols;
- inspection of the clinical trial operations or trial sites by the FDA or other regulatory authorities;
- unforeseen safety issues, including serious adverse events associated with a product candidate, or lack of effectiveness; and
- lack of adequate funding to continue the clinical trial.

***Positive results in previous nonclinical studies and clinical trials of any of our product candidates may not be replicated in future clinical trials of the same product candidates, which could result in development delays or a failure to obtain marketing approval.***

Positive results in nonclinical studies and clinical trials of any of our product candidates may not be predictive of similar results in future clinical trials. Also, interim results during a clinical trial do not necessarily predict final results. A number of companies in the pharmaceutical and biotechnology industries have suffered significant setbacks in late-stage clinical trials even after achieving promising results in early-stage development. Accordingly, the results from any completed nonclinical studies and clinical trials for any of our product candidates may not be predictive of the results we may obtain in later stage trials. Our clinical trials may produce negative or inconclusive results, and we may decide, or regulators may require us, to conduct additional clinical trials. Moreover, clinical data is often susceptible to varying interpretations and analyses, and many companies that have believed their product candidates performed satisfactorily in nonclinical studies and clinical trials have nonetheless failed to obtain FDA approval for their products.

## **RISKS RELATED TO OUR BUSINESS AND FINANCIAL POSITION**

***We have incurred significant operating losses since our inception and anticipate that we will continue to incur losses for the foreseeable future.***

Our company has limited operating history commercializing branded products. Adzenys XR-ODT and Cotempla XR-ODT require and Adzenys ER will require substantial resources as we implement commercialization strategies to seek to begin generating substantial revenue from product sales. In addition, our product candidates will require substantial additional resources before we will be able to receive regulatory approvals, implement commercialization strategies and begin generating revenue from product sales, if approved. There can be no assurance that any of our product candidates will ever achieve regulatory approval or generate any substantial revenue or revenue at all. We do not anticipate generating substantial revenue from sales of Adzenys XR-ODT, Cotempla XR-ODT, Adzenys ER, if any, or any of our other product candidates in the near term, if ever. We have incurred significant net losses of \$66.2 million, \$83.3 million and \$30.8 million for the years ended December 31, 2017, 2016 and 2015, respectively. As of December 31, 2017, we had an accumulated deficit of \$266.4 million. We have devoted most of our financial resources to implementation of our commercialization strategies, manufacturing operations and product development. To date, we have financed our operations primarily through the sale of equity and debt securities and payments received under collaborative arrangements. The size of our future net losses will depend, in part, on the rate of future expenditures and our ability to generate revenue. Because of the numerous risks and uncertainties associated with pharmaceutical product development, we are unable to fully predict the timing or amount of our increased expenses, but we expect to continue to incur substantial expenses, which we expect will increase as we expand our development activities and operate a specialty sales force and commercialization infrastructure. Our expenses could increase beyond expectations if we are required by the FDA to perform studies in addition to the clinical trials we have already completed. As a result of the foregoing, we expect to continue to incur significant and increasing losses and negative cash flows for the foreseeable future, which may increase compared to past periods. Even if we are able to generate revenue from the sale of any approved products, we may not become profitable and may need to obtain additional funding to continue operations.

***We may need additional funding and may be unable to raise capital when needed, which would force us to delay, reduce or eliminate our product development programs or commercialization efforts.***

Developing future potential product candidates, conducting clinical trials, establishing raw material supplier relationships and manufacturing and marketing drugs are expensive and uncertain processes. Although we believe our cash, cash equivalents and marketable securities and anticipated future



product revenues will be sufficient to allow us to fund the commercialization of Adzenys XR-ODT, Cotempla XR-ODT and Adzenys ER, we may need to obtain additional capital through equity offerings, debt financing, payments under new or existing licensing and research and development collaboration agreements, or any combination thereof, in order to become cash flow positive and to develop and commercialize additional product candidates. If sufficient funds on acceptable terms are not available when needed, we could be required to significantly reduce operating expenses and delay, reduce the scope of, or eliminate one or more of our development programs, which may have a material adverse effect on our business, results of operations and financial condition.

In addition, unforeseen circumstances may arise, or our strategic imperatives could change, causing us to consume capital significantly faster than we currently anticipate, requiring us to seek to raise additional funds sooner than expected. We have no committed external sources of funds.

The amount and timing of our future funding requirements will depend on many factors, including, but not limited to:

- the costs of establishing and operating sales, marketing, distribution and commercial manufacturing capabilities for Adzenys XR-ODT, Cotempla XR-ODT, Adzenys ER and any other potential product candidates;
- our ability to successfully commercialize Adzenys XR-ODT, Cotempla XR-ODT and Adzenys ER, and to continue to increase the level of sales in the marketplace;
- the rate of progress and cost of our trials and other product development programs for our other potential product candidates;
- the costs and timing of in-licensing additional product candidates or acquiring other complementary technologies, assets or companies;
- the actions of our competitors and their success in selling competitive product offerings; and
- the status, terms and timing of any collaborative, licensing, co-promotion or other arrangements.

Additional financing may not be available when we need it or may not be available on terms that are favorable to us. In addition, we may seek additional capital due to favorable market conditions or strategic considerations, even if we believe we have sufficient funds for our current or future operating plans. If adequate funds are not available to us on a timely basis, or at all, we may be required to delay, reduce the scope of or eliminate commercialization efforts for one or more of our product candidates or development programs for future potential product candidates.

***We may sell additional equity or incur debt to fund our operations, which may result in dilution to our stockholders and impose restrictions on our business.***

In order to raise additional funds to support our operations, we may sell additional equity or incur debt, which could adversely impact our stockholders, as well as our business. The sale of additional equity or convertible debt securities would result in the issuance of additional shares of our capital stock and dilution to all of our stockholders. The incurrence of indebtedness would result in increased fixed payment obligations and could also result in certain restrictive covenants, such as limitations on our ability to incur additional debt, limitations on our ability to acquire, sell or license intellectual property rights and other operating restrictions that could adversely impact our ability to conduct our business. We may not have enough available cash or be able to raise additional funds on satisfactory terms, if at all, through equity or debt financings to repay our indebtedness at the time any such repayment is required (causing a default under such indebtedness), which could have a material adverse effect on our business, financial condition and results of operations.

***We may not have cash available to us in an amount sufficient to enable us to make interest or principal payments on our indebtedness when due.***

On May 11, 2016, we entered into a \$60 million senior secured credit facility with Deerfield as lender. Approximately \$33 million of the proceeds was used to repay the existing senior and subordinated debt that was otherwise payable in 2016 and 2017. Principal on the new debt is due in three equal annual installments beginning in May 2019 and continuing through May 2022, with a final payment of principal, interest and all other obligations under the facility due on May 11, 2022. Interest is due quarterly beginning in June 2016, at a rate of 12.95% per year. All obligations under our credit facility are secured by substantially all of our existing property and assets subject to certain exceptions. This debt financing may create additional financial risk for us, particularly if our business or prevailing financial market conditions are not conducive to paying off or refinancing our outstanding debt obligations at maturity. Since our inception, we have had significant operating losses. As of December 31, 2017, we had an accumulated deficit of \$266.4 million. We expect to continue to incur net losses and have negative cash flow from operating activities for the foreseeable future as we continue to develop and seek marketing approval for our product candidates. As a result, we may not have sufficient funds, or may be unable to arrange for additional financing, to pay the amounts due on our outstanding indebtedness under our credit facility with Deerfield. Further, funds from external sources may not be available on economically acceptable terms, if at all. For example, if we raise additional funds through collaboration, licensing or other similar arrangements, it may be necessary to relinquish potentially valuable rights to our product candidates or technologies, or to grant licenses on terms that are not favorable to us. If adequate funds are not available when and if needed, our ability to make interest or principal payments on our debt obligations, finance our operations, our research and development efforts and other general corporate activities would be significantly limited and we may be required to delay, significantly curtail or eliminate one or more of our programs.

Failure to satisfy our current and future debt obligations under our credit facility with Deerfield could result in an event of default and, as a result, our lenders could accelerate all of the amounts due. In the event of an acceleration of amounts due under our credit facility as a result of an event of default, we may not have sufficient funds or may be unable to arrange for additional financing to repay our indebtedness. In addition, our lenders could seek to enforce their security interests in any collateral securing such indebtedness.

***Our quarterly operating results may fluctuate significantly.***

We expect our operating results to be subject to quarterly and annual fluctuations. We expect that any revenues we generate will fluctuate from quarter to quarter and year to year as a result of the timing of our commercialization efforts and seasonal trends with respect to ADHD diagnosis and use of medicinal products in the management of this disorder. Our net loss and other operating results will be affected by numerous factors, including:

- our ability to establish and maintain an effective sales and marketing infrastructure;
- variations in the level of expenses related to our commercialization efforts and the development of additional clinical programs;
- competition from existing products or new products that may emerge;
- the level of market acceptance for any approved product candidates and underlying demand for that product, seasonality in the use of that product by end-users and wholesalers' buying patterns;
- regulatory developments affecting our products and product candidates;
- our dependency on third-party manufacturers to supply components of our product candidates;

- potential side effects of our future products that could delay or prevent commercialization or cause an approved drug to be taken off the market;
- any delays in regulatory review and approval of our product candidates;
- any intellectual property infringement lawsuit in which we may become involved; and
- our execution of any collaborative, licensing or similar arrangements, and the timing of payments we may make or receive under these arrangements.

Due to the various factors mentioned above, and others, the results of any prior quarterly period should not be relied upon as an indication of our future operating performance. If our quarterly operating results fall below the expectations of investors or securities analysts, the price of our common stock could decline substantially. Furthermore, any quarterly fluctuations in our operating results may, in turn, cause the price of our stock to fluctuate substantially.

***Our ability to use our net operating loss carry-forwards and certain other tax attributes may be limited.***

Under Section 382 of the Internal Revenue Code of 1986, as amended (the “Code”), if a corporation undergoes an “ownership change,” generally defined as a greater than 50% change (by value) in its equity ownership over a three year period, the corporation’s ability to use its pre-change net operating loss carry-forwards and other pre-change tax attributes, such as research tax credits, to offset its post-change income may be limited. We have in the past and may experience ownership changes in the future as a result of subsequent shifts in our stock ownership. As a result, if we earn net taxable income, our ability to use our pre-change net operating loss carry-forwards to offset U.S. federal taxable income may be subject to limitations, which could potentially result in increased future tax liability to us. In addition, pursuant to the Tax Cuts and Jobs Act of 2017 we may not use net operating loss carry-forwards to reduce our taxable income in any year by more than 80% and we may not carry back any net operating losses to prior years. These new rules apply regardless of the occurrence of an “ownership change.”

***Our future success depends on our ability to retain key executives and to attract, retain and motivate qualified personnel.***

We are highly dependent on the principal members of our executive team, the loss of whose services may adversely impact the achievement of our objectives. Any of our executive officers could leave our employment at any time, as all of our employees are “at will” employees. Recruiting and retaining other qualified employees for our business, including scientific and technical personnel, will also be critical to our success. There is currently a shortage of skilled executives in our industry, which is likely to continue. As a result, competition for skilled personnel is intense and the turnover rate can be high. We may not be able to attract and retain personnel on acceptable terms given the competition among numerous pharmaceutical companies for individuals with similar skill sets. In addition, failure to succeed in clinical trials or to receive regulatory approval for our product candidates may make it more challenging to recruit and retain qualified personnel. The inability to recruit key executives or the loss of the services of any executive or key employee might impede the progress of our development and commercialization objectives.

***If we fail to maintain an effective system of internal control over financial reporting, we may not be able to accurately report our financial results or prevent fraud. As a result, stockholders could lose confidence in our financial and other public reporting, which would harm our business and the trading price of our common stock.***

Effective internal controls over financial reporting are necessary for us to provide reliable financial reports and, together with adequate disclosure controls and procedures, are designed to prevent fraud.

Any failure to implement required new or improved controls, or difficulties encountered in their implementation, could cause us to fail to meet our reporting obligations. We have established an annual SOX Risk Assessment and Control Effectiveness Test Cycle that is designed to timely identify deficiencies to management for remediation to comply with Section 404 of the SOX. We may discover additional deficiencies in our internal controls over financial reporting, including those identified through testing conducted by us in connection with Section 404 of the SOX. Such deficiencies may be deemed to be significant deficiencies or material weaknesses that may require prospective or retroactive changes to our consolidated financial statements or identify other areas for further remedial action. Failures of internal controls could also cause investors to lose confidence in our reported financial information, which could have a negative effect on the trading price of our common stock.

***Our business and operations would suffer in the event of system failures.***

We utilize information technology, or IT, systems and networks to process, transmit and store electronic information in connection with our business activities. As use of digital technologies has increased, cyber incidents, including deliberate attacks and attempts to gain unauthorized access to computer systems and networks, have increased in frequency and sophistication. These threats pose a risk to the security of our systems and networks and the confidentiality, availability and integrity of our data. There can be no assurance that we will be successful in preventing cyber-attacks or successfully mitigating their effects.

Despite the implementation of security measures, our internal computer systems and those of our contractors and consultants are vulnerable to damage from such cyber attacks, including computer viruses, unauthorized access, natural disasters, terrorism, war and telecommunication and electrical failures. Such an event could cause interruption of our operations. For example, the loss of data from completed clinical trials for our product candidates could result in delays in our regulatory approval efforts and significantly increase our costs. To the extent that any disruption or security breach were to result in a loss of or damage to our data, or inappropriate disclosure of confidential or proprietary information, we could suffer reputational harm or face litigation or adverse regulatory action and the development of our product candidates could be delayed.

***We may rely on third parties to perform many essential services for any products that we commercialize, including distribution, customer service, accounts receivable management, cash collection and adverse event reporting. If these third parties fail to perform as expected or to comply with legal and regulatory requirements, our ability to commercialize Adzenys XR-ODT, Cotempla XR-ODT or Adzenys ER will be significantly impacted and we may be subject to regulatory sanctions.***

We may retain third-party service providers to perform a variety of functions related to the sale and distribution of Adzenys XR-ODT, Cotempla XR-ODT and Adzenys ER, key aspects of which will be out of our direct control. These service providers may provide key services related to distribution, customer service, accounts receivable management and cash collection. We would substantially rely on these third-party providers to perform services for us. If these third-party service providers fail to comply with applicable laws and regulations, fail to meet expected deadlines, or otherwise do not carry out their contractual duties to us, our ability to deliver product to meet commercial demand may be significantly impaired. In addition, we may engage third parties to perform various other services for us relating to adverse event reporting, safety database management, fulfillment of requests for medical information regarding our product candidates and related services. If the quality or accuracy of the data maintained by these service providers is insufficient or if they fail to comply with various requirements, we could be subject to regulatory sanctions.

## RISKS RELATED TO OUR INTELLECTUAL PROPERTY

*If our intellectual property related to our products or product candidates is not adequate, we may not be able to compete effectively in our market.*

We rely upon a combination of patents, trade secret protection and confidentiality agreements to protect the intellectual property related to our products, product candidates and technology. Any disclosure to or misappropriation by third parties of our confidential or proprietary information could enable competitors to duplicate or surpass our technological achievements, thus eroding our competitive position in our market.

Due to legal standards relating to patentability, validity, enforceability and scope of claim, patents covering pharmaceutical and biotechnology inventions involve complex legal, scientific and factual questions. Formulation of drug products such as ours with complex release profiles is an area of intense research, publishing and patenting, which limits the scope of any new patent applications. As a result, our ability to obtain, maintain and enforce patents is uncertain and any rights under any existing patents, or any patents we might obtain or license, may not provide us with sufficient protection for our products and product candidates to afford a commercial advantage against competitive products or processes. The patent applications that we own may fail to result in issued patents in the United States or in foreign countries. Even if patents do successfully issue, third parties may challenge their patentability, validity (e.g., by discovering previously unidentified prior art, or a patent-barring event such as a prior public disclosure, use, sale or offer for sale of the invention), enforceability or scope, which may result in such patents being narrowed, invalidated or held unenforceable. For example, U.S. patents may be challenged by third parties via *inter partes* review, post grant review, derivation or interference proceedings at the USPTO, and European patents may be challenged via an opposition proceeding at the European Patent Office. Furthermore, if we were to assert our patent rights against a competitor, the competitor could challenge the validity and/or enforceability of the asserted patent rights. Although a granted U.S. patent is entitled to a statutory presumption of validity, its issuance is not conclusive as to its validity or its enforceability, and it may not provide us with adequate proprietary protection or competitive advantages against competitors with similar products.

If the breadth or strength of protection provided by the patents and patent applications we hold or pursue with respect to our products and product candidates is successfully challenged, we may face unexpected competition that could have a material adverse impact on our business. Even if they are unchallenged, our patents and patent applications may not adequately protect our intellectual property or prevent others from designing around our claims. For example, a third party may develop a competitive product that provides therapeutic benefits similar to our products or product candidates, but is sufficiently different to fall outside the scope of our patent protection.

Furthermore, if we encounter delays in our clinical trials or entry onto the market in a particular jurisdiction, the period of time during which we could market a particular product under patent protection would be reduced.

Even where laws provide protection, costly and time-consuming litigation could be necessary to enforce and determine the scope of our proprietary rights, and the outcome of such litigation would be uncertain. If we or one of our future collaborators were to initiate legal proceedings against a third party to enforce a patent covering a product or our technology, the defendant could counterclaim that our patent is invalid and/or unenforceable. In patent litigation in the United States, defendant counterclaims alleging invalidity and/or unenforceability are commonplace. Grounds for a validity challenge could be an alleged failure to meet any of several statutory requirements, including lack of novelty, obviousness, lack of written description, non-enablement or a patent-barring event, such as a public disclosure, use or sale of the invention more than a year before the filing date of the application. Grounds for an unenforceability assertion could, for example, be an allegation that someone connected with prosecution of the patent withheld material information from the USPTO, or made a misleading

statement, during prosecution. The outcome following legal assertions of invalidity and unenforceability is unpredictable. With respect to validity, for example, we cannot be certain that there is no invalidating prior art, of which we and the patent examiner were unaware during prosecution, or that a third party challenging one of our patents would not assert that a patent-barring event had occurred. If a plaintiff or a defendant were to prevail on a legal assertion of invalidity and/or unenforceability against one or more of our patents, we would lose at least part, and perhaps all, of the patent protection for one or more of our products or product candidates. Such a loss of patent protection could have a material adverse impact on our business.

For example, on July 25, 2016, we received a paragraph IV certification from Actavis advising us that Actavis has filed an ANDA with the FDA for a generic version of Adzenys XR-ODT. On September 1, 2016, we filed a patent infringement lawsuit in federal district court in the District of Delaware against Actavis, Inc. This case alleged that Actavis infringed our Adzenys XR-ODT patents by submitting to the FDA an ANDA seeking to market a generic version of Adzenys XR-ODT prior to the expiration of our patents. This lawsuit automatically stayed, or barred, the FDA from approving Actavis's ANDA for 30 months or until a district court decision that is adverse to the asserted patents is rendered, whichever is earlier.

On October 17, 2017, we entered into a Settlement Agreement (the "Agreement") with Actavis. This Agreement resolves all ongoing litigation involving our Adzenys XR-ODT patents and Actavis's ANDA. Under the Agreement, we have granted Actavis the right to manufacture and market its generic version of Adzenys XR-ODT under the ANDA beginning on September 1, 2025, or earlier under certain circumstances. A stipulation and order of dismissal was entered by the U.S. District Court for the District of Delaware. The Agreement has been submitted to the applicable governmental agencies. There can be no assurance that the Agreement will be approved by such agencies. In addition, there can be no assurance that we would not face future litigation regarding Adzenys XR-ODT, Cotempla XR-ODT, Adzenys ER or any future product candidates.

For example, on October 31, 2017, we received a paragraph IV certification from Teva advising us that Teva has filed an ANDA with the FDA for a generic version of Cotempla XR-ODT, in connection with seeking to market its product prior to the expiration of patents covering Cotempla XR-ODT. A paragraph IV certification is a certification by a generic applicant that in the opinion of that applicant, the patent(s) listed in the Orange Book for a branded product are invalid, unenforceable, and/or will not be infringed by the manufacture, use or sale of the generic product. On December 13, 2017, we filed a patent infringement lawsuit in federal district court in the District of Delaware against Teva. This case alleged that Teva infringed our Cotempla XR-ODT patents by submitting to the FDA an ANDA seeking to market a generic version of Cotempla XR-ODT prior to the expiration of our patents. This lawsuit automatically stayed, or barred, the FDA from approving Teva's ANDA for 30 months or until a district court decision that is adverse to the asserted patents is rendered, whichever is earlier. Such litigation is often time-consuming and costly and its outcome would be unpredictable, however, we intend to vigorously enforce our intellectual property rights relating to Cotempla XR-ODT. We would expect to face generic competition for our Cotempla XR-ODT product if such patents are not upheld or if Teva is found not to infringe such patents. The resulting loss of exclusivity would impact pricing and our sales of Cotempla XR-ODT, which could have a material adverse impact on our business.

Moreover, we may be subject to a third-party pre-issuance submission of prior art to the USPTO, or become involved in reexamination, *inter partes* review, or interference proceedings challenging our patent rights. Patents based on applications that we file in the future may also be subject to derivation and/or post-grant review proceedings. An adverse determination in any such submission, proceeding or litigation could reduce the scope of, or invalidate, our patent rights and allow third parties to commercialize our technology or products and compete directly with us. In addition, if the breadth or strength of protection provided by our patents and patent applications is threatened, it could dissuade

companies from collaborating with us to license, develop or commercialize current or future product candidates.

***We may not seek to protect our intellectual property rights in all jurisdictions throughout the world, and we may not be able to adequately enforce our intellectual property rights even in the jurisdictions where we seek protection.***

Filing, prosecuting and defending patents on product candidates in all countries and jurisdictions throughout the world would be prohibitively expensive, and our intellectual property rights in some countries outside the United States are less extensive than in the United States. In addition, the laws of some foreign countries do not protect intellectual property rights to the same extent as federal and state laws in the United States. Consequently, even where we do elect to pursue patent rights outside the United States, we may not be able to obtain relevant claims and/or we may not be able to prevent third parties from practicing our inventions in all countries outside the United States, or from selling or importing products made using our inventions in and into the United States or other jurisdictions.

Competitors may use our technologies in jurisdictions where we do not pursue and obtain patent protection to develop their own products and further, may possibly export otherwise infringing products to territories where we have patent protection, but enforcement is not as strong as that in the United States. These products may compete with our products and our patents or other intellectual property rights may not be effective or sufficient to prevent them from competing. Even if we pursue and obtain issued patents in particular jurisdictions, our patent claims or other intellectual property rights may not be effective or sufficient to prevent third parties from competing with us.

The laws of some foreign countries do not protect intellectual property rights to the same extent as the laws of the United States. Many companies have encountered significant problems in protecting and defending intellectual property rights in certain foreign jurisdictions. The legal systems of some countries, particularly developing countries, do not favor the enforcement of patents and other intellectual property protection. This could make it difficult for us to stop the infringement of our patents, if obtained, or the misappropriation of our other intellectual property rights. For example, many foreign countries have compulsory licensing laws under which a patent owner must grant licenses to third parties. In addition, many countries limit the enforceability of patents against third parties, including government agencies or government contractors. In these countries, patents may provide limited or no benefit.

Patent protection must ultimately be sought on a country-by-country basis, which is an expensive and time-consuming process with uncertain outcomes. Accordingly, we have, and may in the future, choose not to seek patent protection in certain countries. Furthermore, while we intend to protect our intellectual property rights in certain markets for our products, we cannot ensure that we will be able to initiate or maintain similar efforts in all jurisdictions in which we may wish to market our products. Accordingly, our efforts to protect our intellectual property rights in such countries may be inadequate.

***Obtaining and maintaining our patent protection depends on compliance with various procedural, document submission, fee payment and other requirements imposed by governmental patent agencies, and our patent protection could be reduced or eliminated for non-compliance with these requirements.***

The USPTO and various foreign governmental patent agencies require compliance with a number of procedural, documentary, fee payment and other provisions during the patent process. There are situations in which noncompliance can result in abandonment or lapse of a patent or patent application, resulting in partial or complete loss of patent rights in the relevant jurisdiction. In such an event, competitors might be able to enter the market earlier than would otherwise have been the case.

*If we are sued for infringing intellectual property rights of third parties, it will be costly and time consuming, and an unfavorable outcome in that litigation would have a material adverse effect on our business.*

Our commercial success depends upon our ability and the ability of our collaborators to develop, manufacture, market and sell our and their approved products and use our proprietary technologies without infringing the proprietary rights of third parties. Numerous U.S. and foreign issued patents and pending patent applications, which are owned by third parties, exist in the fields in which we are developing product candidates. As the pharmaceutical industry expands and more patents are issued, the risk increases that our products and product candidates may give rise to claims of infringement of the patent rights of others. There may, for example, be issued patents of third parties of which we are currently unaware, that may be infringed by our products or product candidates, which could prevent us from being able to commercialize our products or product candidates, respectively. Because patent applications can take many years to issue, there may be currently pending applications which may later result in issued patents that our products or product candidates may infringe.

The pharmaceutical industry is rife with patent litigation between patent holders and producers of follow-on drug products. The possibility of blocking FDA approval of a competitor's product for up to 30 months provides added incentive to litigate over Orange Book patents, but suits involving non-Orange Book patents are also common in the ADHD space. There have been multiple patent litigations involving nearly all of the medications for treatment of ADHD. This trend may continue and, as a result, we may become party to legal matters and claims arising in the ordinary course of business.

We may be exposed to, or threatened with, future litigation by third parties alleging that our products or product candidates infringe their intellectual property rights. If one of our products or product candidates is found to infringe the intellectual property rights of a third party, we or our collaborators could be enjoined by a court and required to pay damages and could be unable to commercialize the applicable approved products and product candidates unless we obtain a license to the patent. A license may not be available to us on acceptable terms, if at all. In addition, during litigation, the patent holder could obtain a preliminary injunction or other equitable relief which could prohibit us from making, using or selling our approved products, pending a trial on the merits, which may not occur for several years.

There is a substantial amount of litigation involving patent and other intellectual property rights in the pharmaceutical industry generally. If a third party claims that we or our collaborators infringe its intellectual property rights, we may face a number of issues, including, but not limited to:

- infringement and other intellectual property claims which, regardless of merit, may be expensive and time-consuming to litigate and may divert our management's attention from our core business;
- third parties bringing claims against us may have more resources than us to litigate claims against us;
- substantial damages for infringement, which we may have to pay if a court decides that the product at issue infringes on or violates the third party's rights, and, if the court finds that the infringement was willful, we could be ordered to pay treble damages and the patent owner's attorneys' fees;
- a court prohibiting us from selling our product or any product candidate approved in the future, if any, unless the third party licenses its rights to us, which it is not required to do;
- if a license is available from a third party, we may have to pay substantial royalties, fees or grant cross-licenses to our intellectual property rights; and



- redesigning any of our products and product candidates so they do not infringe, which may not be possible or may require substantial monetary expenditures and time.

***Our drug development strategy relies heavily upon the 505(b)(2) regulatory approval pathway, which requires us to certify that we do not infringe upon third-party patents covering approved drugs. Such certifications typically result in third-party claims of intellectual property infringement, the defense of which would be costly and time consuming, and an unfavorable outcome in any litigation may prevent or delay our development and commercialization efforts which would harm our business.***

Our commercial success depends in large part on our avoiding infringement of the patents and proprietary rights of third parties for existing approved drug products. Because we utilize the 505(b)(2) regulatory approval pathway for the approval of our products and product candidates, we rely in whole or in part on studies conducted by third parties related to those approved drug products. As a result, upon filing with the FDA for approval of our product candidates, we will be required to certify to the FDA that either: (1) there is no patent information listed in the FDA's Orange Book with respect to our NDA; (2) the patents listed in the Orange Book have expired; (3) the listed patents have not expired, but will expire on a particular date and approval is sought after patent expiration; or (4) the listed patents are invalid or will not be infringed by the manufacture, use or sale of our proposed drug product. If we certify to the FDA that a patent is invalid or not infringed, or a Paragraph IV certification, a notice of the Paragraph IV certification must also be sent to the patent owner once our 505(b)(2) NDA is accepted for filing by the FDA. The third party may then initiate a lawsuit against us asserting infringement of the patents identified in the notice. The filing of a patent infringement lawsuit within 45 days of receipt of the notice automatically prevents the FDA from approving our NDA until the earliest of 30 months or the date on which the patent expires, the lawsuit is settled, or the court reaches a decision in the infringement lawsuit in our favor. If the third party does not file a patent infringement lawsuit within the required 45-day period, our NDA will not be subject to the 30-month stay. However, even if the third party does not sue within the 45-day time limit, thereby invoking the 30-month stay, it may still challenge our right to market our product upon FDA approval; therefore, some risk of an infringement suit remains even after the expiry of the 45-day limit. By way of example, when we initially submitted our Adzenys XR-ODT NDA in December 2012 and in response to our Paragraph IV certification, Shire initiated a lawsuit against us claiming patent infringement against certain of Shire's patents. We settled with Shire in July 2014. As part of our settlement, among other things, we stipulated that the commercial manufacture, use, selling, offering for sale or importing of Adzenys XR-ODT would infringe on certain Shire patents and that such patent claims are valid and enforceable with respect to our Adzenys XR-ODT NDA, but that such stipulations do not preclude us from filing new regulatory applications containing a Paragraph IV certification citing such patents. We also entered into a non-exclusive License Agreement (the "2014 License Agreement") with Shire for certain of Shire's patents with respect to our Adzenys XR-ODT NDA. Under the terms of the 2014 License Agreement, upon obtaining FDA approval of our Adzenys XR-ODT NDA, we were required to pay a lump-sum, non-refundable license fee no later than thirty days after receiving such approval and are required to pay a single-digit royalty on net sales of Adzenys XR-ODT during the life of Shire's patents. In addition, on January 26, 2017, we sent a letter to Shire, notifying Shire that we have made a Paragraph IV certification to the FDA that in our opinion and to the best of our knowledge, the patents owned by Shire that purportedly cover our Adzenys ER are invalid, unenforceable and/or will not be infringed by the commercial manufacture, use or sale of Adzenys ER. On March 6, 2017, we entered into a License Agreement (the "2017 License Agreement") with Shire, pursuant to which Shire granted us a non-exclusive license to certain patents owned by Shire for certain activities with respect to Adzenys ER. Under the terms of the 2017 License Agreement, we were required to pay a lump sum, non-refundable license fee no later than thirty days after receiving regulatory approval and are required to pay a single digit royalty on net sales of the Adzenys ER during the life of the relevant Shire patents. Additionally, each of the 2014 and 2017 License Agreements contains a covenant from

Shire not to file a patent infringement suit against us alleging that Adzenys XR-ODT or Adzenys ER, respectively, infringes the Shire patents.

***We may be unable to adequately prevent disclosure of trade secrets and other proprietary information.***

We rely on trade secrets to protect our proprietary know-how and technological advances, especially where we do not believe patent protection is appropriate or obtainable. However, trade secrets are difficult to protect. We rely in part on confidentiality agreements with our employees, consultants, outside scientific collaborators, sponsored researchers and other advisors to protect our trade secrets and other proprietary information. These agreements may not effectively prevent disclosure of confidential information and may not provide an adequate remedy in the event of unauthorized disclosure of confidential information. In addition, others may independently discover our trade secrets and proprietary information. Costly and time-consuming litigation could be necessary to enforce and determine the scope of our proprietary rights. Failure to obtain or maintain trade secret protection could enable competitors to use our proprietary information to develop products that compete with our products or cause additional, material adverse effects upon our competitive business position.

***We may be subject to claims by third parties asserting that our employees or we have misappropriated their intellectual property, or claiming ownership of what we regard as our own intellectual property.***

Some of our employees were previously employed at other companies, including actual or potential competitors. We may also engage advisors and consultants who are concurrently employed at other organizations or who perform services for other entities. Although we try to ensure that our employees, advisors and consultants do not use the proprietary information or know-how of others in their work for us, we may be subject to claims that we or our employees, advisors, or consultants have used or disclosed intellectual property, including trade secrets or other proprietary information, of any such party's former employer or in violation of an agreement with or legal obligation in favor of another party. Litigation may be necessary to defend against these claims.

In addition, while we generally require our employees, consultants, advisors and contractors who may be involved in the development of intellectual property to execute agreements assigning such intellectual property to us, we may be unsuccessful in executing such an agreement with each party who in fact develops intellectual property that we regard as our own. Our and their assignment agreements may not be self-executing or may be breached, and we may be forced to bring claims against third parties, or defend claims they may bring against us, to determine the ownership of what we regard as our intellectual property. Similarly, we may be subject to claims that an employee, advisor or consultant performed work for us that conflicts with that person's obligations to a third party, such as an employer or former employer, and thus, that the third party has an ownership interest in the intellectual property arising out of work performed for us. Litigation may be necessary to defend against these claims.

If we fail in prosecuting or defending any such claims, in addition to paying monetary damages, we may lose valuable intellectual property rights or personnel. Even if we are successful in prosecuting or defending against such claims, litigation could result in substantial costs and be a distraction to management.

## **RISKS RELATED TO OUR COMMON STOCK**

***The market price of our common stock may be highly volatile and investors in our common stock could incur substantial losses.***

The trading price of our common stock is likely to be volatile. Since shares of our common stock were sold in our initial public offering ("IPO"), in July 2015 at a price of \$15.00 per share, our stock

price has ranged from \$4.85 to \$28.99, through March 12, 2018. Our stock price could be subject to wide fluctuations in response to a variety of factors, including the following:

- failure to successfully execute our commercialization strategy with respect to Adzenys XR-ODT, Cotempla XR-ODT, Adzenys ER, or any other approved potential product candidate in the future;
- any delay in filing an NDA for any of our product candidates and any adverse development or perceived adverse development with respect to the FDA's review of that NDA;
- adverse results or delays in clinical trials, if any;
- significant lawsuits, including patent or stockholder litigation;
- inability to obtain additional funding;
- failure to successfully develop and commercialize our product candidates;
- changes in laws or regulations applicable to our product candidates;
- inability to manufacture adequate amounts of product supply or obtain adequate amounts of components of our product supply for our product candidates, or the inability to do so at acceptable prices;
- unanticipated serious safety concerns related to the use of our generic Tussionex, Adzenys XR-ODT, Cotempla XR-ODT, Adzenys ER or any future potential product candidates;
- adverse regulatory decisions;
- introduction of new products or technologies by our competitors;
- failure to meet or exceed product development or financial projections we provide to the public;
- failure to meet or exceed the estimates and projections of the investment community;
- the perception of the pharmaceutical industry by the public, legislatures, regulators and the investment community;
- announcements of significant acquisitions, strategic partnerships, joint ventures or capital commitments by us or our competitors, or perceptions regarding unsolicited public acquisition proposals of our company;
- disputes or other developments relating to proprietary rights, including patents, litigation matters and our ability to obtain patent protection for our technologies;
- additions or departures of key scientific or management personnel;
- changes in the market valuations of similar companies;
- sales of our common stock by us or our stockholders in the future; and
- trading volume of our common stock.

In addition, the stock market in general, and the NASDAQ Global Market ("NASDAQ"), in particular, has experienced extreme price and volume fluctuations that have often been unrelated or disproportionate to the operating performance of these listed companies. Broad market and industry factors may negatively affect the market price of our common stock, regardless of our actual operating performance.

***Our principal stockholders and management own a significant percentage of our shares and will be able to exert significant control over matters subject to stockholder approval.***

As of December 31, 2017, our executive officers, directors, 5% or greater stockholders and their affiliates beneficially owned approximately 34% of our outstanding voting stock. These stockholders may be able to determine all matters requiring stockholder approval. For example, these stockholders, acting together, may be able to control elections of directors, amendments of our organizational documents or approval of any merger, sale of assets or other major corporate transaction. This may prevent or discourage unsolicited acquisition proposals or offers for our common stock that you may believe are in your best interest as one of our stockholders.

***Sales of a substantial number of shares of our common stock in the public market by our existing stockholders could cause our stock price to fall.***

Sales of a substantial number of shares of our common stock by our existing stockholders in the public market or the perception that these sales might occur, could depress the market price of our common stock and could impair our ability to raise capital through the sale of additional equity securities. We are unable to predict the effect that such sales may have on the prevailing market price of our common stock. Shares held by our affiliates will be subject to volume limitations and other conditions pursuant to Rule 144 of the Securities Act. Sales of stock by these stockholders could have a material adverse effect on the trading price of our common stock.

***Potential uncertainty resulting from unsolicited acquisition proposals and related matters may adversely affect our business.***

In the past we have received, and in the future we may receive, unsolicited proposals to acquire our company or our assets. For example, in June 2017 and in October 2017, the Board of Directors received an unsolicited non-binding proposal for the acquisition of all of our stock. The review and consideration of acquisition proposals and related matters could require the expenditure of significant management time and personnel resources. Such proposals may also create uncertainty for our employees, customers and vendors. Any such uncertainty could make it more difficult for us to retain key employees and hire new talent, and could cause our customers and vendors to not enter into new arrangements with us or to terminate existing arrangements. Additionally, we and members of our Board of Directors could be subject to future lawsuits related to unsolicited proposals to acquire us. Any such future lawsuits could become time consuming and expensive.

***We will continue to incur significant increased costs as a result of operating as a public company, and our management will be required to devote substantial time to new compliance initiatives.***

As a public company, we will continue to incur significant legal, accounting and other expenses. In addition, the SOX Act, as well as rules subsequently implemented by the Securities and Exchange Commission (the "SEC") and NASDAQ, have imposed various requirements on public companies. In July 2010, the Dodd-Frank Wall Street Reform and Consumer Protection Act (the "Dodd-Frank Act"), was enacted. There are significant corporate governance and executive compensation related provisions in the Dodd-Frank Act that required the SEC to adopt additional rules and regulations in these areas such as "say on pay" and proxy access. Stockholder activism, the current political environment and the current high level of government intervention and regulatory reform may lead to substantial new regulations and disclosure obligations, which may lead to additional compliance costs and impact (in ways we cannot currently anticipate) the manner in which we operate our business. Our management and other personnel will need to devote a substantial amount of time to these compliance initiatives. Moreover, these rules and regulations will increase our legal and financial compliance costs and will make some activities more time-consuming and costly. For example, we expect these rules and regulations to make it more difficult and more expensive for us to obtain director and officer liability

insurance and we may be required to incur substantial costs to maintain our current levels of such coverage.

***We are an “emerging growth company,” and we cannot be certain if the reduced reporting requirements applicable to emerging growth companies will make our common stock less attractive to investors.***

We are an “emerging growth company,” as defined in the Jumpstart Our Business Startups Act (the “JOBS Act”). For as long as we continue to be an emerging growth company, we may take advantage of exemptions from various reporting requirements that are applicable to other public companies that are not “emerging growth companies,” including exemption from compliance with the auditor attestation requirements of Section 404 of the SOX Act and reduced disclosure obligations regarding executive compensation in the Annual Report on Form 10-K and our periodic reports and proxy statements, and exemptions from the requirements of holding a non-binding advisory vote on executive compensation. We will remain an emerging growth company until the earlier of (1) the last day of the fiscal year (a) in 2020, (b) in which we have total annual gross revenue of at least \$1.07 billion (as inflation-adjusted by the SEC from time to time), or (c) in which we are deemed to be a large accelerated filer, which means the market value of our common stock that is held by non-affiliates exceeds \$700 million as of the prior March 31st, and (2) the date on which we have issued more than \$1 billion in non-convertible debt during the prior three-year period.

Even after we no longer qualify as an emerging growth company, we may still qualify as a “smaller reporting company,” which would allow us to take advantage of many of the same exemptions from disclosure requirements including exemption from compliance with the auditor attestation requirements of Section 404 of the SOX Act and reduced disclosure obligations regarding executive compensation in our periodic reports and proxy statements. We cannot predict if investors will find our common stock less attractive because we may rely on these exemptions. If some investors find our common stock less attractive as a result, there may be a less active trading market for our common stock and our stock price may be more volatile.

Under the JOBS Act, emerging growth companies can also delay adopting new or revised accounting standards until such time as those standards apply to private companies. We have irrevocably elected not to avail ourselves of this exemption from new or revised accounting standards and, therefore, will be subject to the same new or revised accounting standards as other public companies that are not emerging growth companies.

***We do not intend to pay dividends on our common stock and, consequently, your ability to achieve a return on your investment will depend on appreciation in the price of our common stock.***

We have never declared or paid any cash dividend on our common stock and do not currently intend to do so in the foreseeable future. We currently anticipate that we will retain future earnings for the development, operation and expansion of our business and do not anticipate declaring or paying any cash dividends in the foreseeable future. Therefore, the success of an investment in shares of our common stock will depend upon any future appreciation in their value. There is no guarantee that shares of our common stock will appreciate in value or even maintain the price at which you purchased them.

***Provisions in our amended and restated certificate of incorporation and bylaws, as well as provisions of Delaware law, could make it more difficult for a third party to acquire us or increase the cost of acquiring us, even if doing so would benefit our stockholders or remove our current management.***

Some provisions of our charter documents and Delaware law may have anti-takeover effects that could discourage an acquisition of us by others, even if an acquisition would be beneficial to our

stockholders and may prevent attempts by our stockholders to replace or remove our current management. These provisions include:

- authorizing the issuance of “blank check” preferred stock, the terms of which may be established and shares of which may be issued without stockholder approval;
- limiting the removal of directors by the stockholders;
- creating a classified board of directors;
- prohibiting stockholder action by written consent, thereby requiring all stockholder actions to be taken at a meeting of our stockholders;
- eliminating the ability of stockholders to call a special meeting of stockholders; and
- establishing advance notice requirements for nominations for election to the board of directors or for proposing matters that can be acted upon at stockholder meetings.

These provisions may frustrate or prevent any attempts by our stockholders to replace or remove our current management by making it more difficult for stockholders to replace members of our board of directors, which is responsible for appointing the members of our management. In addition, we are subject to Section 203 of the Delaware General Corporation Law, which generally prohibits a Delaware corporation from engaging in any of a broad range of business combinations with an interested stockholder for a period of three years following the date on which the stockholder became an interested stockholder, unless such transactions are approved by our board of directors. This provision could have the effect of delaying or preventing a change of control, whether or not it is desired by or beneficial to our stockholders. Further, other provisions of Delaware law may also discourage, delay or prevent someone from acquiring us or merging with us.

*Our amended and restated certificate of incorporation provides that the Court of Chancery of the State of Delaware is the exclusive forum for certain litigation that may be initiated by our stockholders, which could limit our stockholders' ability to obtain a favorable judicial forum for disputes with us or our directors, officers or employees.*

Our amended and restated certificate of incorporation, as currently in effect, provides that the Court of Chancery of the State of Delaware is the exclusive forum for (i) any derivative action or proceeding brought on our behalf, (ii) any action asserting a claim for breach of a fiduciary duty owed by any of our directors, officers or other employees to us or our stockholders, (iii) any action asserting a claim arising pursuant to any provision of the Delaware General Corporation Law, our amended and restated certificate of incorporation or our amended and restated bylaws, or (iv) any action asserting a claim governed by the internal affairs doctrine. The choice of forum provision may limit a stockholder's ability to bring a claim in a judicial forum that it finds favorable for disputes with us or our directors, officers or other employees, which may discourage such lawsuits against us and our directors, officers and other employees. Alternatively, if a court were to find the choice of forum provision contained in our amended and restated certificate of incorporation and amended and restated bylaws to be inapplicable or unenforceable in an action, we may incur additional costs associated with resolving such action in other jurisdictions, which could adversely affect our business and financial condition.

#### **ITEM 1B. Unresolved Staff Comments**

None.

#### **ITEM 2. Properties**

Our corporate headquarters are located in Grand Prairie, Texas, where we lease approximately 97,282 square feet of office, laboratory and manufacturing space. Our lease expires on December 31,

2024, with an option to extend. We believe our current office, laboratory and manufacturing space is sufficient to meet our needs until the expiration of the lease. In addition, we executed a 60-month lease for 6,078 square feet of office space in Blue Bell, Pennsylvania for our commercial operations which commenced on May 1, 2016 and which has an option to extend for 60 months. We may seek to negotiate new leases or evaluate additional or alternate space to accommodate operations relating to commercialization. We believe that appropriate alternative space is readily available on commercially reasonable terms.

### **ITEM 3. Legal Proceedings**

From time to time, we may be subject to various legal proceedings and claims that arise in the ordinary course of our business activities. Although the results of litigation and claims cannot be predicted with certainty, we do not believe we are party to any claim or litigation the outcome of which, if determined adversely to us, would individually or in the aggregate be reasonably expected to have a material adverse effect on our business. We may file infringement claims against third parties for the infringement of our patents, such as the lawsuit discussed below. Regardless of the outcome, litigation can have an adverse impact on us because of defense and settlement costs, diversion of management resources and other factors.

On July 25, 2016, we received a paragraph IV certification from Actavis advising us that Actavis has filed an ANDA with the FDA for a generic version of Adzenys XR-ODT. On September 1, 2016, we filed a patent infringement lawsuit in federal district court in the District of Delaware against Actavis, Inc. alleging that Actavis infringed our Adzenys XR-ODT patents by submitting to the FDA an ANDA seeking to market a generic version of Adzenys XR-ODT prior to the expiration of our patents.

On October 17, 2017, we entered into the Agreement with Actavis, which resolves all ongoing litigation involving our Adzenys XR-ODT patents and Actavis's ANDA. Under the Agreement, we granted Actavis the right to manufacture and market its generic version of Adzenys XR-ODT under the ANDA beginning on September 1, 2025, or earlier under certain circumstances. A stipulation and order of dismissal was entered by the U.S. District Court for the District of Delaware. The Agreement has been submitted to the applicable governmental agencies.

On October 31, 2017, we received a paragraph IV certification from Teva advising us that Teva has filed an ANDA with the FDA for a generic version of Cotempla XR-ODT. We have new product exclusivity for a three-year period from the date of approval for Cotempla XR-ODT. The certification notice alleges that the three U.S. patents listed in the FDA's Orange Book for Cotempla XR-ODT, one with an expiration date in April 2026 and two with expiration dates in June 2032, will not be infringed by Teva's proposed product, are invalid and/or are unenforceable. On December 13, 2017, we filed a patent infringement lawsuit in federal district court in the District of Delaware against Teva alleging that Teva infringed our Cotempla XR-ODT patents by submitting to the FDA an ANDA seeking to market a generic version of Cotempla XR-ODT prior to the expiration of our patents. This lawsuit automatically stayed, or barred, the FDA from approving Teva's ANDA for 30 months or until a district court decision that is adverse to the asserted patents is rendered, whichever is earlier. We intend to vigorously enforce our intellectual property rights relating to Cotempla XR-ODT. We cannot predict the timing or outcome of these proceedings.

On March 7, 2018, we received a citation advising us that the County of Harris, Texas (the "County") filed a lawsuit on December 13, 2017 against us and various other alleged manufacturers, promoters, sellers and distributors of opioid pharmaceutical products. Through this lawsuit, the County seeks to recoup as damages some of the expenses it allegedly has incurred to combat opioid use and addiction. The County also seeks punitive damages, disgorgement of profits and attorneys' fees. While we believe that the lawsuit is without merit and intend to vigorously defend against it, we are not able to predict at this time whether this proceeding will have a material impact on our results of operations.

**ITEM 4. Mine Safety Disclosures**

Not applicable.

**ITEM 5. Market for Registrant’s Common Equity, Related Stockholder Matters and Issuer Purchases of Equity Securities****Market Information for our Common Stock**

Our common stock has been listed on the NASDAQ Global Market under the symbol “NEOS” since July 23, 2015. Our initial public offering was priced at \$15.00 per share on July 22, 2015. The following table sets forth for each quarter in 2017 and 2016 the high and low sales prices per share of our common stock as reported on the NASDAQ Global Market:

	<u>High</u>	<u>Low</u>
First Quarter (from January 1, 2017 to March 31, 2017) . . . . .	\$ 7.90	\$4.85
Second Quarter (from April 1, 2017 to June 30, 2017) . . . . .	\$ 9.60	\$6.60
Third Quarter (from July 23, 2017 to September 30, 2017) . . . . .	\$ 9.40	\$6.30
Fourth Quarter (from October 1, 2017 to December 31, 2017) . . . . .	\$13.15	\$7.25
First Quarter (from January 1, 2016 to March 31, 2016) . . . . .	\$15.20	\$7.57
Second Quarter (from April 1, 2016 to June 30, 2016) . . . . .	\$11.40	\$7.15
Third Quarter (from July 1, 2016 to September 30, 2016) . . . . .	\$ 9.99	\$6.33
Fourth Quarter (from October 1, 2016 to December 31, 2016) . . . . .	\$ 9.23	\$5.30

On December 29, 2017, the last trading day of 2017, the last reported sale price of our common stock on the NASDAQ Global Market was \$10.20 per share. As of March 12, 2018, there were 28,996,956 shares of common stock outstanding, held by approximately 56 holders of record of our common stock. The actual number of shareholders is greater than this number of record holders, and includes shareholders who are beneficial owners, but whose shares are held in street name by brokers and other nominees. This number of holders of record also does not include shareholders whose shares may be held in trust by other entities.

**Dividends**

We have never declared or paid any dividends on our capital stock. We currently intend to retain all available funds and any future earnings, if any, to fund the development and expansion of our business, and we do not anticipate paying any cash dividends in the foreseeable future. Any future determination to pay dividends will be made at the discretion of our board of directors. Our ability to pay dividends on our common stock is limited by restrictions under the terms of our credit facility with Deerfield Private Design Fund III, L.P. and Deerfield Special Situations Fund, L.P. In addition, any future indebtedness that we may incur could preclude us from paying dividends. Investors should not purchase our common stock with the expectation of receiving cash dividends.

**Securities Authorized for Issuance under Equity Compensation Plans**

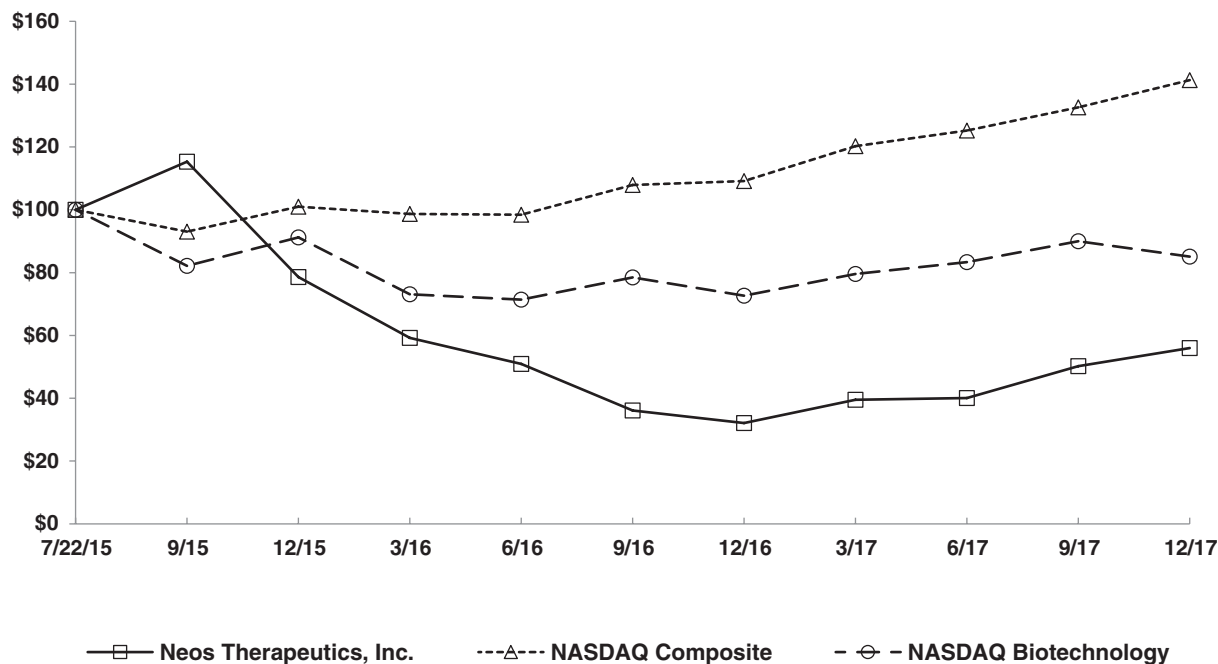
Information about our equity compensation plans is included in Item 11 of Part III of this Annual Report on Form 10-K.

**Performance Graph**

The following stock performance graph illustrates a comparison of the total cumulative stockholder return on our common stock to two indices; the NASDAQ Composite Index and the NASDAQ Biotechnology Index since July 23, 2015, which is the date our common stock first began trading on the NASDAQ Global Market. The graph assumes an initial investment of \$100 at the initial public offering price to the public for Neos stock of \$15 on July 23, 2015 or at June 30, 2015 if invested in the indices, and all dividends, if any, were reinvested. No cash dividends have been declared or paid on our common stock. Stockholder return over the indicated period should not be considered indicative of future stockholder returns.



**COMPARISON OF 29 MONTH CUMULATIVE TOTAL RETURN\***  
Among Neos Therapeutics, Inc., the NASDAQ Composite Index  
and the NASDAQ Biotechnology Index



\*\$100 invested on 7/22/15 in stock or 6/30/15 in index, including reinvestment of dividends.  
Fiscal year ending December 31.

**Recent Sales of Unregistered Securities**

None.

**Purchases of Equity Securities by the Issuer and Affiliated Purchasers**

There was no share purchase in the first three quarters in 2017. Shares purchased in the fourth quarter of 2017 are as follows:

<u>Period</u>	<u>Total Number of Shares Purchased(1)</u>	<u>Average Price Paid per Share</u>
October 1, 2017 to October 31, 2017 . . . . .	14,895	\$8.00
November 1, 2017 to November 30, 2017 . . . . .	—	—
December 1, 2017 to December 31, 2017 . . . . .	—	—
<b>Total . . . . .</b>	<u>14,895</u>	<u>\$8.00</u>

(1) Represents shares withheld to satisfy tax withholding amounts due from an employee related to the vesting of restricted stock.

## ITEM 6. Selected Consolidated Financial Data

The following selected consolidated statements of operations data for the years ended December 31, 2017, 2016, and 2015, and the balance sheet data as of December 31, 2017 and 2016 are derived from our audited financial statements appearing elsewhere in this Annual Report on Form 10-K. The selected historical financial data for the year ended December 31, 2014 and 2013 and as of December 31, 2015, 2014 and 2013 have been derived from our audited consolidated financial statements not included in this Annual Report on Form 10-K. You should read this data together with our financial statements and related notes included elsewhere in this Annual Report on Form 10-K and the information under the caption “Item 7. Management’s Discussion and Analysis of Financial Condition and Results of Operations.” Our historical results for any prior period are not necessarily indicative of results to be expected in any future period.

### Consolidated Statements of Operations Data:

	Year ended December 31,				
	2017	2016	2015	2014	2013
	(in thousands, except per share data)				
Total Revenue(1) . . . . .	\$ 25,018	\$ 9,154	\$ 3,792	\$ 758	\$ 1,044
Cost of Goods Sold . . . . .	12,391	11,437	5,929	3,391	2,534
Research and Development Expenses . . . . .	8,957	12,207	11,691	10,574	9,974
Selling and Marketing Expenses(1) . . . . .	46,881	49,291	5,672	229	153
General and Administrative Expenses . . . . .	13,805	12,625	7,078	5,036	5,471
Interest and Other Expense . . . . .	9,231	6,927	4,203	2,377	1,512
Net Loss from Continuing Operations(1) . . . .	\$ (66,247)	\$ (83,333)	\$ (30,781)	\$ (20,849)	\$ (18,600)
Loss from Discontinued Operations . . . . .	—	—	—	—	(437)
Net Loss(1) . . . . .	\$ (66,247)	\$ (83,333)	\$ (30,781)	\$ (20,849)	\$ (19,037)
Preferred Stock Accretion to Redemption					
Value . . . . .	—	—	(1,169)	(1,118)	(1,227)
Preferred Stock Dividends . . . . .	—	—	(1,221)	(2,185)	(2,185)
Net Loss Attributable to Common Stock . . . .	\$ (66,247)	\$ (83,333)	\$ (33,171)	\$ (24,152)	\$ (22,449)
Net Loss per Share—Basic and Diluted(2) . . .	\$ (2.68)	\$ (5.19)	\$ (4.38)	\$ (27.56)	\$ (28.45)
Shares Used to Compute Net Loss per					
Share—Basic and Diluted(2) . . . . .	24,751,091	16,052,390	7,581,881	876,318	788,964

(1) We began marketing Adzenys XR-ODT on May 16, 2016 and initiated an early experience program with limited product availability for Cotempla XR-ODT on September 5, 2017 before launching this product nationwide on October 2, 2017 and have determined that at this time it cannot reliably estimate expected returns of the product at the time of shipment to wholesalers. Accordingly, we defer recognition of revenue and related cost of goods sold on product shipments of Adzenys XR-ODT and Cotempla XR-ODT until the right of return no longer exists, which occurs at the earlier of the time Adzenys XR-ODT and Cotempla XR-ODT units are dispensed through patient prescriptions or expiration of the right of return. Thus, the amounts included in Total Revenue and Net Loss from Continuing Operations for Adzenys XR-ODT and Cotempla XR-ODT reflect only patient prescriptions dispensed to date. Also, the Selling and Marketing Expenses and Net Loss amounts in 2017 and 2016 reflect the sales and marketing expenses associated with the commercialization of Adzenys XR-ODT and Cotempla XR-ODT.

- (2) See Note 3 to the notes to our consolidated financial statements included elsewhere in this Annual Report on Form 10-K for an explanation of the calculations of our basic and diluted net loss per common share.

**Consolidated Balance Sheet Data:**

	December 31,				
	2017	2016	2015	2014	2013
	(in thousands)				
Cash and Cash Equivalents . . . . .	\$ 31,969	\$24,352	\$ 90,763	\$ 13,343	\$ 11,947
Short-Term Investments . . . . .	18,448	15,430	—	3,000	7,497
Working Capital . . . . .	45,038	33,624	82,306	13,380	14,303
Total Assets . . . . .	107,353	80,142	122,510	45,230	41,878
Long Term Debt, net of Current Portion(1) . . . .	58,938	58,599	26,271	23,121	16,454
Redeemable Convertible Preferred Stock(2) . . . .	—	—	—	90,149	70,836
Stockholders' Equity (Deficit) . . . . .	7,890	(1,548)	78,374	(78,782)	(54,844)

- (1) On May 11, 2016, we entered into a \$60 million senior secured credit facility (“Facility”) with Deerfield Private Design Fund III, L.P. (66⅔% of Facility) and Deerfield Special Situations Fund, L.P. (33⅓% of Facility) (collectively, “Deerfield”), as lenders. See Note 11 to the notes to our consolidated financial statements included elsewhere in this Annual Report on Form 10-K for further details.
- (2) On the closing of the IPO, all outstanding shares of redeemable preferred stock converted into 9,217,983 shares of common stock and all remaining outstanding Series C warrants issued in conjunction with purchases of Series C preferred stock were net exercised at the IPO price for 78,926 shares of common stock. Upon the closing of our IPO, all of the shares of our redeemable convertible preferred stock were retired and cancelled and shall not be reissued as shares of such series, and all rights and preferences of those shares of redeemable convertible preferred stock were cancelled, including the right to receive undeclared accumulated dividends.

**ITEM 7. Management’s Discussion and Analysis of Financial Condition and Results of Operations**

*You should read the following discussion and analysis of our financial condition and results of operations together with the “Item 6. Selected Consolidated Financial Data” and the consolidated financial statements and related notes that are included elsewhere in this Annual Report on Form 10-K. This discussion contains forward-looking statements based upon current expectations that involve risks and uncertainties. Our actual results may differ materially from those anticipated in these forward-looking statements as a result of various factors, including those set forth under “Item 1A. Risk Factors” or in other parts of this Annual Report on Form 10-K.*

**OVERVIEW**

We are a pharmaceutical company focused on developing, manufacturing and commercializing products utilizing our proprietary modified-release drug delivery technology platform, which we have already used to develop Adzenys XR-ODT, Cotempla XR-ODT and Adzenys ER oral suspension (“Adzenys ER”), for the treatment of attention deficit hyperactivity disorder (“ADHD”). Our products and product candidates are extended-release (“XR”), medications in patient-friendly, orally disintegrating tablets (“ODT”) or liquid suspension dosage forms. Our proprietary modified-release drug delivery platform has enabled us to create novel, extended-release ODT and liquid suspension dosage forms. We received approval from the U.S. Food and Drug Administration (“FDA”), for Adzenys XR-ODT, our amphetamine XR-ODT, on January 27, 2016 and launched the commercialization of this product on May 16, 2016. We received approval from the FDA for Cotempla

XR-ODT, our methylphenidate XR-ODT for the treatment of ADHD in patients 6 to 17 years old, on June 19, 2017. We initiated an early experience program with limited product availability on September 5, 2017 before launching this product nationwide on October 2, 2017. Also, we received approval from the FDA for Adzenys ER, our amphetamine extended-release liquid suspension, on September 15, 2017, and launched the commercialization of this product on February 26, 2018. We believe Adzenys XR-ODT and Cotempla XR-ODT are the first amphetamine XR-ODT and the first methylphenidate XR-ODT, respectively, for the treatment of ADHD on the market.

We are commercializing Adzenys XR-ODT, Cotempla XR-ODT and Adzenys ER in the United States using our own commercial infrastructure. We are manufacturing Adzenys XR-ODT, Cotempla XR-ODT and Adzenys ER in our current Good Manufacturing Practice (“cGMP”) and U.S. Drug Enforcement Administration (“DEA”)-registered manufacturing facilities, thereby obtaining our products at cost without manufacturer’s margins and better controlling supply quality and timing. We also currently use these facilities to manufacture our generic equivalent to the branded product, Tussionex, an XR liquid suspension of hydrocodone and chlorpheniramine indicated for the relief of cough and upper respiratory symptoms of a cold (“generic Tussionex”).

On July 25, 2016, we received a paragraph IV certification from Actavis Laboratories FL, Inc. (“Actavis”) advising us that Actavis has filed an Abbreviated New Drug Application (“ANDA”) with the FDA for a generic version of Adzenys XR-ODT. On September 1, 2016, we filed a patent infringement lawsuit in federal district court in the District of Delaware against Actavis, Inc. alleging that Actavis infringed our Adzenys XR-ODT patents by submitting to the FDA an ANDA seeking to market a generic version of Adzenys XR-ODT prior to the expiration of our patents. On October 17, 2017, we entered into a Settlement Agreement and a Licensing Agreement (collectively, the “Agreement”) with Actavis. The Agreement resolves all ongoing litigation involving our Adzenys XR-ODT patents and Actavis’s ANDA. Under the Agreement, we have granted Actavis the right to manufacture and market its generic version of Adzenys XR-ODT under the ANDA beginning on September 1, 2025, or earlier under certain circumstances. A stipulation and order of dismissal was entered by the U.S. District Court for the District of Delaware. The Agreement has been submitted to the applicable governmental agencies.

On October 31, 2017, we received a paragraph IV certification from Teva Pharmaceuticals USA, Inc. (“Teva”) advising us that Teva has filed an ANDA with the FDA for a generic version of Cotempla XR-ODT. We have new product exclusivity for a three-year period from the date of approval for Cotempla XR-ODT. The certification notice alleges that the three U.S. patents listed in the FDA’s Orange Book for Cotempla XR-ODT, one with an expiration date in April 2026 and two with expiration dates in June 2032, will not be infringed by Teva’s proposed product, are invalid and/or are unenforceable. On December 13, 2017, we filed a patent infringement lawsuit in federal district court in the District of Delaware against Teva alleging that Teva infringed our Cotempla XR-ODT patents by submitting to the FDA an ANDA seeking to market a generic version of Cotempla XR-ODT prior to the expiration of our patents. This lawsuit automatically stayed, or barred, the FDA from approving Teva’s ANDA for 30 months or until a district court decision that is adverse to the asserted patents is rendered, whichever is earlier. We intend to vigorously enforce our intellectual property rights relating to Cotempla XR-ODT. We are unable to predict the timing or outcome of these proceedings at this time. We anticipate incurring increasing amounts of legal fees in the enforcement of our intellectual property rights.

Our predecessor company was incorporated in Texas on November 30, 1994 as PharmaFab, Inc. and subsequently changed its name to Neostx, Inc. On June 15, 2009, we completed a reorganization pursuant to which substantially all of the capital stock of Neostx, Inc. was acquired by a newly formed Delaware corporation, named Neos Therapeutics, Inc. The remaining capital stock of Neostx, Inc. was acquired by us on June 29, 2015, and Neostx, Inc. was merged with and into Neos Therapeutics, Inc. Historically, we were primarily engaged in the development and contract manufacturing of unapproved

or Drug Efficacy Study Implementation (“DESI”), pharmaceuticals and, to a lesser extent, nutraceuticals for third parties. The unapproved or DESI pharmaceuticals contract business was discontinued in 2007, and the manufacture of nutraceuticals for third parties was discontinued in March 2013.

Since our reorganization in 2009, we have devoted substantially all of our resources to funding our manufacturing operations and to our commercial products and product candidates which consist of implementation of our commercialization strategies, research and development activities, clinical trials for our product candidates, the general and administrative support of these operations and intellectual property protection and maintenance. Prior to our initial public offering of our common stock in July 2015, we funded our operations principally through private placements of our common stock, redeemable convertible preferred stock, bank and other lender financings and through payments received under collaborative arrangements.

On August 28, 2014, we completed an acquisition of all of the rights to the Tussionex Abbreviated New Drug Application (“Tussionex ANDA”), which include the rights to produce, develop, market and sell, as well as all the profits from such selling activities, our generic Tussionex, which we previously owned the rights to manufacture, but which was marketed and sold by the generic drug division of Cornerstone Biopharma, Inc. (“Cornerstone”). These rights were acquired from the collaboration of the Company, Cornerstone and Coating Place, Inc. Prior to the acquisition, we shared profits generated by the sale and manufacture of the product under a development and manufacturing agreement with those companies.

We have incurred significant losses in each year since our reorganization in 2009. Our net losses were \$66.2 million for the year ended December 31, 2017. As of December 31, 2017, we had an accumulated deficit of approximately \$266.4 million. We expect to continue to incur significant expenses and increasing operating losses in the near term. We expect our expenses will increase substantially in connection with our ongoing activities, as we:

- operate commercial infrastructure to support sales and marketing for Adzenys XR-ODT, Cotempla XR-ODT, and Adzenys ER;
- continue research and development activities for new product candidates;
- conduct post-marketing approval research activities for our approved products;
- manufacture supplies for our preclinical studies and clinical trials;
- continue to enforce our intellectual property rights; and
- operate as a public company.

On July 28, 2015, we closed our initial public offering (“IPO”), whereby we sold 5,520,000 shares of common stock, at a public offering price of \$15.00 per share, which includes 720,000 shares of our common stock resulting from the underwriters’ exercise of their over-allotment option at the IPO price on July 23, 2015. The net proceeds from our IPO, after deducting underwriting discounts and commissions and other offering expenses payable by us, were approximately \$75.0 million. The securities described above were offered by us pursuant to a registration statement on Form S-1 declared effective by the SEC on July 22, 2015.

On May 11, 2016, we entered into a \$60 million senior secured credit facility (“Facility”) with Deerfield Private Design Fund III, L.P. (66 $\frac{2}{3}$ % of Facility) and Deerfield Special Situations Fund, L.P. (33 $\frac{1}{3}$ % of Facility) (collectively, “Deerfield”), as lenders. Approximately \$33 million of the proceeds was used to prepay the existing senior and subordinated debt (the “Note”) that was otherwise payable in 2016 and 2017. Principal on the new debt is due in three equal annual installments beginning in May 2019 and continuing through May 2021, with a final payment of principal, interest and all other

obligations under the facility due May 11, 2022. Interest is due quarterly beginning in June 2016, at a rate of 12.95% per year. We had an option, which we exercised, to defer payment of each of the first four interest payments, adding such amounts to the outstanding loan principal. The aggregate \$6.6 million in deferred interest payments (“Accrued Interest”) was to be paid in cash on June 1, 2017.

On June 1, 2017 (the “Amendment Date”), we entered into a First Amendment (the “Amendment”) with Deerfield to the Facility which extended the date to repay the Accrued Interest under the Facility to June 1, 2018 (the “PIK Maturity Date”), which may have been extended to June 1, 2019 at our election if certain conditions had been met as specified in the Amendment. The right to payment of the Accrued Interest was memorialized in the form of Senior Secured Convertible Notes (the “Convertible Notes”) issued to Deerfield on the Amendment Date. Interest is due quarterly at a rate of 12.95% per year. The \$6.6 million of Convertible Notes were convertible into shares of our common stock at the noteholder’s option at any time up to the close of business on the date that is five days prior to the PIK Maturity Date.

On October 26, 2017, Deerfield provided a conversion notice electing to convert the entire \$6.6 million of Convertible Notes into shares of our common stock at a conversion price of \$7.08 per share. The conversion price was based on 95% of the average of the volume weighted average prices per share of the Company’s common stock on the NASDAQ Global Market for the three trading day period immediately preceding such conversion. This resulted in issuing 929,967 shares of our common stock to Deerfield on this date and the Convertible Notes were cancelled.

On August 1, 2016, we filed a shelf registration statement on Form S-3 with the SEC, which covers the offering, issuance and sale by us of up to an aggregate of \$125.0 million of its common stock, preferred stock, debt securities, warrants and/or units (the “Shelf”). We simultaneously entered into a Sales Agreement with Cowen and Company, LLC, as sales agent, to provide for the offering, issuance and sale by us of up to \$40.0 million of its common stock from time to time in “at-the-market” offerings under the Shelf (the “Sales Agreement”). The Shelf was declared effective by the SEC on August 12, 2016. During the year ended December 31, 2016, we did not make any sales under the Sales Agreement. We made common stock offerings in February 2017 and June 2017 pursuant to the Shelf.

In February 2017, we closed an underwritten public offering of 5,750,000 shares of our common stock at a public offering price of \$5.00 per share, which included 750,000 shares of our common stock resulting from the underwriters’ exercise of their over-allotment option on February 17, 2017. Deerfield, our senior lender, participated in the purchase our common shares as part of this public offering, and as a result, is now classified as a related party. The net proceeds to us from this offering, after deducting underwriting discounts and commissions and other offering expenses payable by us, were approximately \$26.7 million.

On June 30, 2017, we closed an underwritten public offering of 4,800,000 shares of our common stock at a public offering price of \$6.25 per share for total proceeds of \$30.0 million before estimated offering costs of \$0.2 million. We also granted the underwriters a 30-day option to purchase up to an additional 720,000 shares of our common stock which was exercised in full on July 26, 2017. The net proceeds to us through July 26, 2017 from this offering, after deducting offering expenses payable by us, were approximately \$34.3 million.

During the year ended December 31, 2017, we sold an aggregate 749,639 shares of common stock under the Sales Agreement, at an average sale price of approximately \$5.01 per share in February 2017 for gross proceeds of \$3.7 million and net proceeds of \$3.6 million and paying total compensation to the sales agent of approximately \$0.1 million.

We may continue to seek private or public equity and debt financing to meet our capital requirements. There can be no assurance that such funds will be available on terms favorable to us, if at all, or that we will be able to successfully commercialize our product candidates. In addition, we may not be profitable even if we succeed in commercializing Adzenys XR-ODT, Cotempla XR-ODT, Adzenys ER, and, if approved, any of our product candidates that we may develop.

## **FINANCIAL OPERATIONS OVERVIEW**

### **Revenue**

During 2015 and 2016, our revenue was generated primarily from product sales of our generic Tussionex recorded on a net sales basis. Sales of our generic Tussionex are seasonal and correlate with the cough and cold season. We launched commercialization of Adzenys XR-ODT on May 16, 2016 and initiated an early experience program with Cotempla XR-ODT with limited product availability on September 5, 2017 before launching this product nationwide on October 2, 2017. We sell our products to drug wholesalers in the United States. We have also established indirect contracts with drug, food and mass retailers that order and receive our generic Tussionex product through wholesalers. As a result of our acquisition of all of the rights to commercialize and derive future profits from the Tussionex ANDA, the continuing commercialization of Adzenys XR-ODT and Cotempla XR-ODT, and the commercial launch of Adzenys ER, we expect our future revenue to increase from historical levels.

We expect the number of prescriptions filled for Adzenys XR-ODT and Cotempla XR-ODT to continue to increase. Data from IMS shows 187,685 and 12,721 equivalent unit prescriptions for Adzenys XR-ODT and Cotempla XR-ODT, respectively, for the year ended December 31, 2017. From the launch of Adzenys XR-ODT in May 2016 through December 31, 2016, data from IMS showed 30,339 equivalent unit prescriptions.

In the future, we will seek to generate additional revenue from product sales of Adzenys XR-ODT, Cotempla XR-ODT and Adzenys ER. We have little Adzenys XR-ODT and Cotempla XR-ODT sales history and have determined that at this time we cannot reliably estimate expected returns of the products at the time of shipment to wholesalers. Accordingly, we defer recognition of revenue on product shipments of Adzenys XR-ODT and Cotempla XR-ODT until the right of return no longer exists, which occurs at the earlier of the time Adzenys XR-ODT and Cotempla XR-ODT units are dispensed through patient prescriptions or expiration of the right of return. We calculate patient prescriptions of Adzenys XR-ODT and Cotempla XR-ODT dispensed using an analysis of third-party information. If we fail to successfully market Adzenys XR-ODT and Cotempla XR-ODT or successfully launch and market Adzenys ER, our inability to generate future revenue from product sales may adversely affect our results of operations and financial position.

### **Research and development**

We expense research and development costs as they are incurred. Research and development expenses consist of costs incurred in the discovery and development of our product candidates, and primarily include:

- expenses, including salaries and benefits, which includes share-based compensation expense, of employees engaged in research and development activities;
- expenses incurred under third party agreements with contract research organizations (“CROs”), and investigative sites that conduct our clinical trials and a portion of our pre-clinical activities;
- cost of raw materials, as well as manufacturing cost of our materials used in clinical trials and other development testing;
- cost of facilities, depreciation and other allocated expenses;
- fees paid to regulatory authorities for review and approval of our product candidates; and
- expenses associated with obtaining and maintaining patents.

Direct development expenses associated with our research and development activities are allocated to our product candidates. Indirect costs related to our research and development activities that are not

allocated to a product candidate are included in “Other Research and Development Activities” in the table below.

Prior to 2016, the largest component of our total operating expenses has been our investment in research and development activities including the clinical development of our product candidates. The following table summarizes our research and development expenses for the periods indicated:

	<b>December 31,</b>		
	<u>2017</u>	<u>2016</u>	<u>2015</u>
	(in thousands)		
NT-0102 Cotempla XR-ODT . . . . .	\$2,034	\$ 1,613	\$ 3,232
NT-0201 Adzenys ER . . . . .	155	2,403	237
NT-0202 Adzenys XR-ODT . . . . .	760	650	330
Other Research and Development Activities(1) . . . . .	<u>6,008</u>	<u>7,541</u>	<u>7,892</u>
	<u>\$8,957</u>	<u>\$12,207</u>	<u>\$11,691</u>

(1) Includes unallocated product development cost, salaries and wages, occupancy and depreciation and amortization.

During the third quarter of 2016, we reclassified our approved product and facility regulatory fees out of research and development expense and into cost of sales commensurate with the commercial launch of Adzenys XR-ODT. We have reclassified all such applicable regulatory fees for prior quarters and prior years out of research and development expense and into cost of goods sold in accordance with this approach.

We expect that our research and development expenses will fluctuate over time as we explore new product candidates, but will decrease as a percentage of revenue if Adzenys XR-ODT and Cotempla XR-ODT are commercially successful, if Adzenys ER is successfully launched and commercialized or if any of our product candidates are approved and are commercially successful. We expect to fund our research and development expenses from our current cash and cash equivalents, a portion of the net proceeds from our public offerings of common stock and debt financing and revenues, if any, from Adzenys XR-ODT, Cotempla XR-ODT and Adzenys ER and, if approved, our product candidates that we may develop.

The process of conducting clinical trials necessary to obtain regulatory approval is costly and time consuming. We may never succeed in achieving marketing approval for our product candidates. The probability of success of our product candidates may be affected by numerous factors, including clinical data, competition, manufacturing capability and commercial viability. As a result, we are unable to determine the duration and completion costs of our research and development projects or when and to what extent we will generate revenue from the commercialization and sale of any of our product candidates.

### **Selling and marketing**

Selling and marketing expenses consist primarily of salaries and related costs for personnel, including share-based compensation expense, commercialization activities for Adzenys XR-ODT and Cotempla XR-ODT and pre-commercialization activities for Adzenys ER, commercial sales organization costs incurred in the preparation for and in the commercialization of Adzenys XR-ODT and Cotempla XR-ODT, and in the preparation for the launch and commercialization of Adzenys ER and trade sales expenses for our generic Tussionex. Other selling and marketing expenses include market research, brand development, advertising agency and other public relations costs, managed care relations, medical marketing, sales support tools, sales planning and market data and analysis.



We believe that our selling and marketing expenses may continue at these levels with the continuing commercialization of Adzenys XR-ODT, and the launch and commercialization of Cotempla XR-ODT and Adzenys ER in the United States.

### **General and administrative**

General and administrative expenses consist primarily of salaries and related costs for personnel, including share-based compensation expense, for our employees in executive, finance, information technology and human resources functions. Other general and administrative expenses include facility-related costs not otherwise included in research and development expenses or cost of goods sold, and professional fees for business development, accounting, tax and legal services. Beginning in July 2016, we began recording stock compensation expense in the same income statement line as the cash compensation of the employee with the associated stock option in accordance with Staff Accounting Bulletin (“SAB”) Topic 14 due to the increased number and amount of stock options and option compensation. We have reclassified all prior quarters’ and prior years’ amounts that relate to personnel not classified as general and administrative employees out of general and administrative expense to the appropriate income statement line in accordance with this approach.

We anticipate that our general and administrative expenses will increase due to increased expenses associated with being a public company, including costs for audit, legal, regulatory and tax-related services, director and officer insurance premiums and investor relations costs, as well as accounting and compliance costs to support the commercialization of our products, and, if approved, our product candidates. In addition, as a result of our Paragraph IV litigation costs, we have incurred increasing amounts of legal fees in the enforcement of our intellectual property rights.

### **Interest expense, net**

On May 11, 2016, we entered into the Facility with Deerfield. Deerfield participated in the purchase of our common shares as part of our February 2017 public offering, and as a result, is now classified as a related party. Approximately \$33.0 million of the Facility proceeds were used to prepay the existing senior Loan and Security Agreement (“LSA”) with Hercules Technology III, L.P. (“Hercules”) and the 10% related party subordinated debt (the “Note”) that was otherwise payable in 2016 and 2017. We entered into the Amendment to the Facility on June 1, 2017, which provided a one-year deferral, with an option for a second year of deferral, of payment of the first year accrued interest of \$6.6 million, provided that we met certain sales revenue targets and obtain FDA approval of certain of our product candidates on or before the Prescription Drug User Fee Act (the “PDUFA”) goal date. Before the Amendment, this accrued interest had been deferred until June 1, 2017 per the terms of the Facility. The right to payment of the \$6.6 million of accrued interest was memorialized in the form of the Convertible Notes issued to Deerfield on the Amendment Date. Interest is due quarterly at a rate of 12.95% per year. Deerfield had an option to convert these notes into our common stock. On October 26, 2017, Deerfield provided a conversion notice electing to convert the entire \$6.6 million of Convertible Notes into shares of our common stock at a conversion price of \$7.08 per share. This resulted in issuing 929,967 shares of our common stock to Deerfield on this date and the Convertible Notes were cancelled.

Interest expense to date has consisted primarily of interest expense on senior debt, including the amortization of debt discounts, the Note and the capitalized leases from a related party resulting from the sale-leaseback transactions of our existing and newly-acquired property and equipment. We amortize debt issuance costs over the life of the notes which are reported as interest expense in our consolidated statements of operations.

## Other income (expense), net

Other income and expense to date has primarily consisted of amortization of the net gain recorded on the sale-leaseback of our property and equipment. The first sale-leaseback financings occurred in five separate transactions in 2013 and 2014, each with a 42-month lease term. The gains on the transactions were recognized on a straight-line basis over the respective 42-month lease term. In February 2017, we entered into an additional agreement for the sale-leaseback of newly acquired assets of up to \$5.0 million to finance our capital expenditures. Under this agreement, we entered into leases and sold assets with a total capitalized cost of \$481,000 and \$2,742,000 at effective interest rates of 14.3% and 14.9% on February 13, 2017 and June 30, 2017, respectively. The February sale resulted in a net gain of \$14,000 which has been deferred and is being amortized over the 36-month term of the lease. There was no gain or loss on the June 2017 sale. (See Notes 11 and 17 to the notes to our consolidated financial statements included elsewhere in this Annual Report on Form 10-K for additional details). Other income and expense also includes interest earned, accretion and gains on our cash and cash equivalents and short-term investments and changes resulting from the remeasurement of the fair value of our earnout and derivative liabilities. The primary objective of our investment policy is liquidity and capital preservation.

## RESULTS OF OPERATIONS

### *Year ended December 31, 2017 compared to the year ended December 31, 2016*

#### Revenues

The following table summarizes our revenues for the year ended December 31, 2017 and 2016:

	Year Ended December 31,		Increase (Decrease)	% Increase (Decrease)
	2017	2016		
	(in thousands)			
Product . . . . .	\$25,018	\$9,154	\$15,864	173.3%

Total product revenues were \$25.0 million for the year ended December 31, 2017, an increase of \$15.9 million or 173.3% from the \$9.2 million for the year ended December 31, 2016. The increase was primarily due to a \$16.0 million increase in net sales of Adzenys XR-ODT which launched on May 16, 2016 from \$19.0 million of net sales for the year ended December 31, 2017 versus approximately \$3.0 million for the year ended December 31, 2016. Net sales of Cotempla XR-ODT which commenced on September 5, 2017 were \$0.9 million. The increase was partially offset by an approximately \$1.1 million decline in net sales of our generic Tussionex to \$5.1 million for the year ended December 31, 2017 from \$6.2 million for the year ended December 31, 2016 primarily due to competitive pricing pressures for this product.

#### Cost of goods sold

The following table summarizes our cost of goods sold for the year ended December 31, 2017 and 2016:

	Year Ended December 31,		Increase (Decrease)	% Increase (Decrease)
	2017	2016		
	(in thousands)			
Cost of Goods Sold . . . . .	\$12,391	\$11,437	\$954	8.3%

Total cost of goods sold was \$12.4 million for the year ended December 31, 2017, an increase of \$1.0 million or 8.3%, from the \$11.4 million for the year ended December 31, 2016. This increase was

primarily from a \$3.9 million increase in product costs and an associated increase of \$1.7 million of royalty fees, freight and logistics costs relating to the increased sales of Adzenys XR-ODT in 2017 which launched on May 16, 2016 and sales from Cotempla XR-ODT which commenced on September 5, 2017. Partially offsetting these increased costs were lower production cost of \$4.6 million relating to efficiencies from increased production to meet sales demand, manufacturing costs for the production of Cotempla XR-ODT being capitalized into inventory after June 30, 2017, following the FDA approval date of June 19, 2017 and manufacturing costs for the production of Adzenys ER being capitalized into inventory after September 30, 2017, following the FDA approval date of September 15, 2017.

### Research and development expenses

The following table summarizes our research and development expenses for year ended December 31, 2017 and 2016:

	Year Ended December 31,		Increase (Decrease)	% Increase (Decrease)
	2017	2016		
	(in thousands)			
Research & Development Expenses . . . . .	\$8,957	\$12,207	\$(3,250)	(26.6)%

Research and development expenses were \$9.0 million for the year ended December 31, 2017, a decrease of approximately \$3.3 million or 26.6%, from the \$12.2 million for the year ended December 31, 2016. This decrease was primarily due to a \$1.4 million decrease in clinical expenses and a \$1.0 million decrease in FDA filing fees associated with Adzenys ER and Cotempla XR-ODT, which completed in 2016. Additionally, development cost for materials, professional fees, employee and related administrative expenses declined \$0.9 million.

### Selling and marketing expenses

The following table summarizes our selling and marketing expenses for the year ended December 31, 2017 and 2016:

	Year Ended December 31,		Increase (Decrease)	% Increase (Decrease)
	2017	2016		
	(in thousands)			
Sales and Marketing Expenses . . . . .	\$46,881	\$49,291	\$(2,410)	(4.9)%

The total selling and marketing expenses were \$46.9 million for the year ended December 31, 2017, a decrease of \$2.4 million or 4.9%, from the \$49.3 million for the year ended December 31, 2016. The decrease was primarily due to a decrease of \$7.0 million in advertising expenses, \$0.4 million in media management and creative design and \$2.0 million in commercial team training activities associated with the launch of our initial branded product, Adzenys XR-ODT, in 2016. These decreases were partially offset by \$6.4 million increase in the commercial sales organization salesforce costs and \$0.6 million increase in salaries and benefits, as this salesforce and support organization was in place for the full year of 2017, whereas in 2016, we were in the process of building out this operation in anticipation of the May 2016 launch of our initial branded product.

## General and administrative expenses

The following table summarizes our general and administrative expenses for the year ended December 31, 2017 and 2016:

	Year Ended December 31,		Increase (Decrease)	% Increase (Decrease)
	2017	2016		
	(in thousands)			
General and Administrative Expenses . . . .	\$13,805	\$12,625	\$1,180	9.3%

The total general and administrative expenses were \$13.8 million for the year ended December 31, 2017, an increase of \$1.2 million or 9.3%, from the \$12.6 million for the year ended December 31, 2016. Salaries and benefits expense increased \$0.6 million primarily due to additional corporate personnel supporting increased compliance requirements. Legal cost for patent defense increased \$1.0 million, partially offset by a \$0.5 million decrease in business development and office supplies.

## Interest expense

The following table summarizes interest expense and loss on debt extinguishment for the year ended December 31, 2017 and 2016:

	Year Ended December 31,		Increase (Decrease)	% Increase (Decrease)
	2017	2016		
	(in thousands)			
Interest Expense . . . . .	<u>\$(10,085)</u>	<u>\$(8,124)</u>	<u>\$1,961</u>	24.1%

The total interest expense was \$10.1 million for the year ended December 31, 2017, an increase of \$2.0 million or 24.1%, from the \$8.1 million for the year ended December 31, 2016. Interest on debt was \$3.1 million higher due to the higher debt balance in 2017 and interest expense related to the additional debt discounts recorded in June 2017 as a result of the modification of the Facility (see Note 11 to the notes to our consolidated financial statements included elsewhere in this Annual Report on Form 10-K for additional details).

Partially offsetting increased senior debt interest expense was the early prepayment of the LSA in 2016 which resulted in a \$1.2 million loss on debt extinguishment due to recording the \$0.2 million LSA prepayment charge, writing off the \$0.5 million of unamortized LSA end of term charge and the \$0.5 million of unamortized LSA loan discount.

## Other income, net

The following table summarizes our other income for the year ended December 31, 2017 and 2016:

	Year Ended December 31,		Increase (Decrease)	% Increase (Decrease)
	2017	2016		
	(in thousands)			
Other income, net . . . . .	\$854	\$1,197	\$(343)	(28.7)%

Other income, net was \$0.9 million for the year ended December 31, 2017, a decrease of \$0.3 million or 28.7%, from \$1.2 million for the year ended December 31, 2016. Other income, net in 2017 consisted of changes in fair value of the Deerfield debt derivative and the Tussionex earn-out liability amounting to \$0.5 million, interest income of \$0.3 million and amortized gain on the sale-leasebacks of \$0.1 million. Other income, net in 2016 consisted of \$0.5 million of amortization of

the gain on the sale-leasebacks, \$0.4 million gain on the auction sale of certain fully depreciated property and equipment, and interest income of \$0.3 million.

**Year ended December 31, 2016 compared to the year ended December 31, 2015**

**Revenues**

The following table summarizes our revenues for the year ended December 31, 2016 and 2015:

	<b>Year Ended December 31,</b>		<b>Increase (Decrease)</b>	<b>% Increase (Decrease)</b>
	<b>2016</b>	<b>2015</b>		
	(in thousands)			
Product . . . . .	\$9,154	\$3,792	\$5,362	141.4%

Total product revenues were \$9.2 million for the year ended December 31, 2016, an increase of \$5.4 million or 141.4% from the \$3.8 million for the year ended December 31, 2015. Net sales of our generic Tussionex increased approximately \$2.5 million to \$6.3 million from the \$3.8 million for the year ended December 31, 2015 due to increased sales volume. Also included in product revenues for the period from May 16, 2016 through year end 2016 were \$2.9 million of net sales of dispensed patient prescriptions of our Adzenys XR-ODT which was launched May 16, 2016.

**Cost of goods sold**

The following table summarizes our cost of goods sold for the year ended December 31, 2016 and 2015:

	<b>Year Ended December 31,</b>		<b>Increase (Decrease)</b>	<b>% Increase (Decrease)</b>
	<b>2016</b>	<b>2015</b>		
	(in thousands)			
Cost of Goods Sold . . . . .	\$11,437	\$5,929	\$5,508	92.9%

The total cost of goods sold was \$11.4 million for the year ended December 31, 2016, an increase of \$5.5 million or 92.9%, from the \$5.9 million for the year ended December 31, 2015. This increase was primarily due to a \$1.9 million increase in product costs, a \$0.7 million increase in labor costs and a \$1.0 million increase in other production costs associated with the increased unit sales of our generic Tussionex and initial sales of Adzenys XR-ODT. Other cost of goods sold also increased, principally due to a \$1.5 million accrual of the product and facility regulatory fees for Adzenys XR-ODT, \$0.3 million of increased services of outside firms including outside lab testing, a \$0.3 million increase in third party logistics provider (“3PL”) freight and service fees and \$0.2 million of increased lab and manufacturing supplies. These increases were partially offset by a \$0.3 million decrease in facility costs and a \$0.1 million decrease in depreciation due to capitalized depreciation costs associated with the Adzenys XR-ODT inventory build.

**Research and development expenses**

The following table summarizes our research and development expenses for the year ended December 31, 2016 and 2015:

	<b>Year Ended December 31,</b>		<b>Increase (Decrease)</b>	<b>% Increase (Decrease)</b>
	<b>2016</b>	<b>2015</b>		
	(in thousands)			
Research & Development Expenses . . . . .	\$12,207	\$11,691	\$516	4.4%

Research and development expenses were \$12.2 million for the year ended December 31, 2016, an increase of approximately \$0.5 million or 4.4%, from the \$11.7 million for the year ended December 31, 2015. This increase was primarily due to a \$2.5 million increase in professional services principally for clinical studies for our product candidates, partially offset by a \$1.3 million net decrease in regulatory fees as the \$2.3 million FDA filing fee for the NDA for Cotempla XR-ODT submitted in 2015 was partially offset by the \$1.0 million FDA filing fee for the NDA for Adzenys ER in 2016, a \$0.4 million decrease in depreciation expense as certain capital lease assets became fully depreciated in July 2016, a \$0.2 million decrease in services of outside firms and a \$0.1 million decrease in facility and related costs due principally to reduced equipment repairs.

### Selling and marketing expenses

The following table summarizes our selling and marketing expenses for the year ended December 31, 2016 and 2015:

	Year Ended December 31,		Increase (Decrease)	% Increase (Decrease)
	2016	2015		
	(in thousands)			
Sales and Marketing Expenses . . . . .	\$49,291	\$5,672	\$43,619	769.0%

The total selling and marketing expenses were \$49.3 million for the year ended December 31, 2016, an increase of approximately \$43.6 million or 769.0%, from the \$5.7 million for the year ended December 31, 2015. Commercial sales organization salesforce and sales support costs increased \$18.5 million in support of the launch of Adzenys XR-ODT. Selling and marketing professional services associated with the launch of Adzenys XR-ODT, exclusive of commercial sales organization costs, increased by \$19.3 million due to advertising agency, marketing materials, commercial team training and other meeting costs, managed care, pharmacy and patient assistance program management, purchases of sales data, convention costs and public relations costs incurred in 2016. Additionally, salary and compensation expense increased \$4.6 million and recruiting fees increased \$0.1 million for the build out of our sales and marketing management. Selling and marketing travel and entertainment expenses increased \$0.9 million and the marketing office facility cost increased \$0.2 million.

### General and administrative expenses

The following table summarizes our general and administrative expenses for the year ended December 31, 2016 and 2015:

	Year Ended December 31,		Increase (Decrease)	% Increase (Decrease)
	2016	2015		
	(in thousands)			
General and Administrative Expenses . . . .	\$12,625	\$7,078	\$5,547	78.4%

The total general and administrative expenses were \$12.6 million for the year ended December 31, 2016, an increase of \$5.5 million or 78.4%, from the \$7.1 million for the year ended December 31, 2015. Salary and compensation expense increased \$2.7 million in the year ended December 31, 2016, primarily due a \$1.3 million increase in compensation related to share-based payments and a \$1.4 million increase, principally due to the addition of personnel for administrative and compliance functions. Also, professional fees increased \$2.1 million in 2016 primarily for legal, public filing, SOX compliance, business development and information technology services. In addition, general and administrative expenses increased by \$0.4 million in 2016 for a full year of the public company directors and officers insurance policy premium, \$0.1 million for board of directors fees and expenses, \$0.1 million for facility costs and \$0.1 million for depreciation.

## Interest expense

The following table summarizes interest expense and loss on debt extinguishment for the year ended December 31, 2016 and 2015:

	Year Ended December 31,		Increase (Decrease)	% Increase (Decrease)
	2016	2015		
	(in thousands)			
Interest Expense . . . . .	\$ (8,124)	\$ (3,721)	\$ (4,403)	118.3%

Interest expense was \$8.1 million for the year ended December 31, 2016, an increase of \$4.4 million or 118.3%, from the \$3.7 million for the year ended December 31, 2015. Of this increase, the early prepayment of the LSA resulted in a \$1.2 million loss on debt extinguishment due to recording the \$0.2 million LSA prepayment charge, writing off the \$0.5 million of unamortized LSA end of term charge and the \$0.5 million of unamortized LSA loan discount. Additionally, interest on senior debt was \$3.8 million higher due to the increased balance of debt. These increases were partially offset by a \$0.3 million reduction in capital lease interest due to the reduced capital lease balances resulting from ongoing lease payments and \$0.3 million lower interest on the subordinated debt due to the prepayment of the \$5.9 million of principal and \$1.3 million of interest on the 10% Note.

## Other income (expense), net

The following table summarizes our other income (expense) for the year ended December 31, 2016 and 2015:

	Year Ended December 31,		Increase (Decrease)	% Increase (Decrease)
	2016	2015		
	(in thousands)			
Other income (expense), net . . . . .	\$ 1,197	\$ (482)	\$ 1,679	(348.3)%

Other income, net was \$1.2 million of net income for the year ended December 31, 2016, an absolute increase of \$1.7 million or 348.3%, from the \$0.5 million of net expense for the year ended December 31, 2015. The 2016 other income, net included \$0.5 million of amortization of the gain on the sale-leasebacks, \$0.4 million gain on the auction sale of certain fully depreciated property and equipment, and \$0.3 million of investment accretion and interest income. The \$0.5 million of net expense in 2015 was primarily due to \$1.3 million 2015 year-to-date net expense effect of the remeasurements of the fair values of the warrant and earnout liabilities, which was partially offset by the \$0.8 million amortization of the gain on the sale-leasebacks. In 2016, as a result of our IPO, the warrants are no longer being revalued at each balance sheet date (see Note 2—*Warrants* to the notes to our consolidated financial statements).

## LIQUIDITY AND CAPITAL RESOURCES

### Sources of liquidity

Since our reorganization in 2009 until our initial public offering (“IPO”), we financed our operations primarily through private placements of common stock and redeemable convertible preferred stock and bank and other lender financing. On July 28, 2015, we closed our IPO whereby we sold 5,520,000 shares of our common stock, at a public offering price of \$15.00 per share, which includes 720,000 shares of our common stock resulting from the underwriters’ exercise of their over-allotment option at the IPO price on July 23, 2015. We received aggregate net proceeds of \$75.0 million from the offering, after deducting underwriting discounts and commissions of \$5.8 million and offering expenses of approximately \$2.0 million. The securities described above were offered by us pursuant to a registration statement on Form S-1 declared effective by the SEC on July 22, 2015.

On May 11, 2016, we entered into the \$60 million Facility with Deerfield. Approximately \$33 million of the \$60 million Facility proceeds was used to prepay the existing \$24.3 million principal and \$0.1 million of accrued interest related to the LSA, the \$1.1 million LSA end of term fee, an LSA prepayment charge of \$243,000 and the \$5.9 million of principal and \$1.3 million of interest on the 10% amended and restated subordinated note (the “Note”) that was issued by us to Essex Capital Corporation (“Essex”) which was to mature in March 2017, which were otherwise payable in 2016 and 2017. Principal on the Facility is due in three equal annual installments beginning in May 2019 and continuing through May 2021, with a final payment of principal, interest and all other obligations under the Facility due May 11, 2022. Interest is due quarterly beginning in June 2016, at a rate of 12.95% per year. We had an option, which we exercised, to defer payment of each of the first four interest payments under the Facility, adding such amounts to the outstanding loan principal. The aggregate \$6.6 million Accrued Interest was to be paid in cash on June 1, 2017.

On June 1, 2017 (the “Amendment Date”), we entered into the First Amendment (the “Amendment”) to the Facility with Deerfield which extended the date to repay the Accrued Interest under the Facility to June 1, 2018 (the “PIK Maturity Date”), which may have been extended to June 1, 2019 at our election if certain conditions had been met as specified in the Amendment. The right to payment of the Accrued Interest was memorialized in the Convertible Notes issued to Deerfield on the Amendment Date. Interest is due quarterly at a rate of 12.95% per year.

The \$6.6 million of Convertible Notes were convertible into shares of our common stock at the noteholder’s option at any time up to the close of business on the date that is five days prior to the PIK Maturity Date. The per share conversion price was to be the greater of (A) 95% of the average of the volume weighted average prices per share of our common stock on the NASDAQ Global Market for the three trading day period immediately preceding such conversion, and (B) \$7.00. On June 30, 2017, we filed a registration statement on form S-3 with the SEC registering 940,924 shares of our common stock that may be offered from time to time by Deerfield, the maximum number of shares of our common stock which would be issued upon conversion of the Convertible Notes assuming the lowest possible conversion price of \$7.00 per share, and such registration statement was declared effective by the SEC on July 11, 2017. On October 26, 2017, Deerfield provided a conversion notice electing to convert the entire \$6.6 million of Convertible Notes into shares of the Company’s common stock at a conversion price of \$7.08 per share. The conversion price was based on 95% of the average of the volume weighted average prices per share of the Company’s common stock on the NASDAQ Global Market for the three trading day period immediately preceding such conversion. This resulted in issuing 929,967 shares of the Company’s common stock to Deerfield on this date and the Convertible Notes were cancelled.

In February 2017, we entered into an agreement with a related party for the sale-leaseback of newly acquired assets of up to \$5.0 million to finance our capital expenditures. Each lease under this master agreement will be for an initial term of 36 months and will have a bargain purchase option at the end of the respective lease. Under this agreement, we entered into leases and sold assets with a total capitalized cost of \$481,000 and \$2,742,000 at effective interest rates of 14.3% and 14.9% on February 13, 2017 and June 30, 2017, respectively.

In February 2017, we closed an underwritten public offering of 5,750,000 shares of our common stock at a public offering price of \$5.00 per share, which includes 750,000 shares of our common stock resulting from the underwriters’ exercise of their over-allotment option at the public offering price on February 17, 2017. Deerfield, our senior lender, participated in the purchase of our common shares as part of this public offering, and as a result, is now classified as a related party. The net proceeds to us from this offering, after deducting underwriting discounts and commissions and other offering expenses payable by us were approximately \$26.7 million.



On June 30, 2017, we closed an underwritten public offering of 4,800,000 shares of our common stock at a price of \$6.25 per share for total proceeds of \$30.0 million before estimated offering costs of \$0.2 million. We also granted the underwriters a 30-day option to purchase up to an additional 720,000 shares of our common stock which the underwriters exercised in full on July 26, 2017. The net proceeds to us from this offering, after deducting offering expenses payable by us, were approximately \$34.3 million.

The shares of common stock for both the June 2017 and February 2017 offerings were offered pursuant to a shelf registration statement on Form S-3, including a base prospectus, filed by us on August 1, 2016, and declared effective by the SEC on August 12, 2016. This shelf registration statement covers the offering, issuance and sale by us of up to an aggregate of \$125.0 million of our common stock, preferred stock, debt securities, warrants and/or units (the “Shelf”). We simultaneously entered into a sales agreement with Cowen and Company, LLC, as sales agent, to provide for the offering, issuance and sale by us of up to \$40.0 million of our common stock from time to time in “at-the-market” offerings under the Shelf (the “Sales Agreement”). During the year ended December 31, 2017, we sold an aggregate 749,639 shares of common stock under the Sales Agreement, at an average sale price of approximately \$5.01 per share for gross proceeds of \$3.7 million and net proceeds of \$3.6 million after paying compensation to the sales agent of \$0.1 million.

Our policy is to invest any cash in excess of our immediate requirements in investments designed to preserve the principal balance and provide liquidity. Accordingly, our cash equivalents and short-term investments are invested in bank deposits, money market funds, financials and corporate debt securities, all of which are currently providing only minimal returns.

As of December 31, 2017, we had \$32.0 million in cash and cash equivalents and \$18.4 million in short-term investments. We believe that our existing cash and cash equivalents and short-term investments will be sufficient to fund our operations for at least the next 12 months after filing this Annual Report on Form 10-K.

We may continue to seek private or public equity and debt financing to meet our capital requirements. There can be no assurance that such funds will be available on terms favorable to us, if at all, or that we will be able to successfully commercialize our product candidates. In addition, we may not be profitable even if we succeed in commercializing Adzenys XR-ODT, Cotempla XR-ODT and Adzenys ER.

## Cash flows

The following table sets forth the primary sources and uses of cash for the periods indicated:

	Year Ended December 31,		Increase (Decrease)	Year Ended December 31,		Increase (Decrease)
	2017	2016		2016	2015	
	(in thousands)					
<b>Net Cash (used in) provided by:</b>						
Net Cash used in operating activities . . . . .	\$(53,261)	\$(70,646)	\$17,385	\$(70,646)	\$(25,867)	\$ (44,779)
Net Cash (used in) provided by investing activities . . . . .	(2,533)	(19,322)	\$16,789	(19,322)	1,977	\$ (21,299)
Net Cash provided by financing activities . . . . .	63,411	23,557	\$39,854	23,557	101,310	\$ (77,753)
Net increase (decrease) in cash and cash equivalents . . . . .	<u>\$ 7,617</u>	<u>\$(66,411)</u>	<u>\$74,028</u>	<u>\$(66,411)</u>	<u>\$ 77,420</u>	<u>\$(143,831)</u>

### **Cash used in operating activities**

Net cash used in operating activities during these periods primarily reflected our net losses, partially offset by changes in working capital and non-cash charges including deferred interest on debt, share-based compensation expense, depreciation expense, amortization of patents and other intangible assets and amortization of senior debt fees.

Net cash used in operating activities was \$53.3 million and \$70.6 million for the years ended December 31, 2017 and 2016, respectively. The \$17.4 million decrease in net cash used from operating activities was due to the \$17.1 million decrease in our net losses, as discussed in “Results of Operations” above, a \$2.0 million decrease in noncash items and a \$2.3 million increase in the provision of cash from working capital. The increase in cash provided by working capital changes resulted primarily from the following: \$7.4 million from the increase in deferred revenue from Adzenys XR-ODT and Cotempla XR-ODT, \$0.8 million increase from the deferred commercial sales organization costs as the ongoing operations contract commenced in March 2016 and \$3.8 million decreased cash usage for accounts payable and accrued expenses due to the timing of vendor invoicing and payments. These increases were partially offset by \$5.3 million for accounts receivable mainly due to increased sales in Adzenys XR-ODT and Cotempla XR-ODT in 2017 and \$4.4 million from increased inventories due to increased production volume for Adzenys XR-ODT and Cotempla XR-ODT. The decrease in noncash items was principally due to a \$2.6 million decrease in deferred interest on debt, a \$0.9 million decrease resulting from the 2016 loss on debt extinguishment due to the early repayment of the Facility and the Note, a \$0.5 million decrease in the fair value change of earnout and derivative liabilities and a \$0.2 million decrease in depreciation and amortization expense, partially offset by a \$0.6 million increase in share-based compensation expense, a \$0.9 million increase in amortization of senior debt fees and a \$0.9 million decrease in deferred gain on sale of equipment primarily due to the expiration of the 2013 and 2014 sale-leasebacks.

Net cash used in operating activities was \$70.6 million and \$25.9 million for the years ended December 31, 2016 and 2015, respectively. The \$44.8 million increase in net cash used from operating activities was due to the \$52.5 million increase in our net losses, as discussed in “Results of Operations” above, partially offset by a \$5.7 million increase in noncash items and a \$2.0 million increase in cash from working capital. The increase of cash from working capital changes primarily resulted from a \$1.3 million decrease in accounts receivable as customers made payments to bring their accounts current, a \$0.5 million increase in accrued expenses and accounts payable due to the timing of vendor invoicing and costs related to sales of Adzenys XR-ODT which are deferred until the revenue associated with those fees is recognized and a \$3.7 million increase in deferred revenue related to Adzenys XR-ODT, partially offset by increased cash usage from a \$2.8 million increase in inventories in anticipation of forecasted increased sales of our generic Tussionex and Adzenys XR-ODT and a \$0.6 million increase in other assets. The increase in noncash items was principally due to a \$4.2 million of deferred interest on the Facility and the Note, a \$2.3 million increase in share-based compensation expense, a \$0.9 million loss on debt extinguishment related to unamortized debt discount, partially offset by a \$1.3 million decrease in the change in the fair value of the warrant and earnout liabilities since 2015 and a net \$0.4 million decrease in all other noncash items.

### **Cash (used in) provided by investing activities**

Net cash used in investing activities is generally due to investments of cash in excess of our operating needs as well as purchase of equipment to support our research and development and manufacturing activities.

Net cash used in investing activities was \$2.5 million for the year ended December 31, 2017 primarily due to the \$48.0 million purchase of short-term investments and \$2.5 million of capital expenditures principally for production equipment, partially offset by the \$45.1 million of sales and

maturities of short-term investments and \$3.2 million of proceeds from the sale-leaseback of equipment.

Net cash used by investing activities was \$19.3 million for the year ended December 31, 2016 primarily due to the \$66.1 million purchase of short-term investments partially offset by the \$50.8 million sales of short-term investments, \$3.6 million of capital expenditures principally for equipment and systems to be used in the production and testing of Adzenys XR-ODT and our other product candidates and a new Enterprise Resource Planning System (“ERP”).

Net cash provided by investing activities of \$2.0 million for the year ended December 31, 2015 was primarily due to the net sale of \$3.0 million of short-term investments, partially offset by a \$1.0 million of capital expenditures in 2015 primarily in association with the expansion of our controlled substances vault.

### **Cash provided by financing activities**

Net cash provided by financing activities of \$63.4 million in the year ended December 31, 2017 principally included \$64.6 million of proceeds from the issuance of common stock net of related underwriting discounts, commissions and issuance costs and partially offset by \$1.0 million of principal payments under the sales-leasebacks.

Net cash provided by financing activities of \$23.6 million in the year ended December 31, 2016 primarily resulted from proceeds of \$60.0 million from the issuance of notes to Deerfield, partially offset by a \$1.4 yield enhancement fee paid to Deerfield and \$0.2 million of legal fees, the full repayment of the \$25.0 million of principal and a \$1.1 million end of term charge payment under the LSA, a \$7.3 million of principal and interest payment under the 10% Note, and \$1.9 million of principal payments under the sales leasebacks partially offset by \$0.4 million of proceeds from the sale of related equipment.

Net cash provided by financing activities of \$101.3 million in the year ended December 31, 2015 primarily resulted from net cash proceeds of \$77.0 million from our IPO reduced by \$2.0 million of cash public offering costs; \$13.0 million, net of issuance costs, received from the sale of 2,624,936 shares of our Series C preferred stock and the issuance of Series C warrants for 1,197,218 shares of Series C preferred stock; proceeds of \$10.0 million from additional drawdowns under our notes to our senior lender; \$5.0 million from the exercise of 1,000,000 of Series C warrants and \$0.1 million from the exercise of stock options, partially offset by \$1.6 million of principal payments under the sales leasebacks and \$0.2 million of payments made to purchase treasury stock.

### **Credit facilities**

On May 11, 2016, we entered into a \$60 million Facility with Deerfield. Approximately \$33 million of the proceeds was used to repay the existing \$24.3 million principal and \$0.1 million of accrued interest related to the LSA, the \$1.1 million LSA end of term fee, an LSA prepayment charge of \$243,000 and the \$5.9 million of principal and \$1.3 million of interest on the Note that was issued by us to Essex which was to mature in March 2017, which were otherwise payable in 2016 and 2017. Principal on the Facility is due in three equal annual installments beginning in May 2019 and continuing through May 2021, with a final payment of principal, interest and all other obligations under the Facility due May 11, 2022. Interest is due quarterly beginning in June 2016, at a rate of 12.95% per year. In connection with the Facility, we paid a \$1,350,000 yield enhancement fee to Deerfield and approximately \$0.2 million of legal fees. Borrowings under the Facility are collateralized by substantially all of our assets, except the assets under capital lease, and we will maintain cash on deposit of not less than \$5.0 million.

We had an option, which we exercised, to defer payment of each of the first four interest payments, adding such amounts to the outstanding loan principal. The aggregate \$6.6 million Accrued Interest was to be paid in cash on June 1, 2017.

On June 1, 2017, we entered into the Amendment to the Facility which extended the PIK Maturity Date to June 1, 2018, which may have been extended to June 1, 2019 at our election if certain conditions had been met as specified in the Amendment. The right to payment of the Accrued Interest was memorialized in the Convertible Notes issued to Deerfield on the Amendment Date. Interest is due quarterly at a rate of 12.95% per year.

The \$6.6 million of Convertible Notes were convertible into shares of our common stock at Deerfield's option at any time up to the close of business on the date that is five days prior to the PIK Maturity Date. The per share conversion price was to be the greater of (A) 95% of the average of the volume weighted average prices per share of our common stock on the NASDAQ Global Market for the three trading day period immediately preceding such conversion, and (B) \$7.00. On June 30, 2017, we filed a registration statement on form S-3 with the SEC registering 940,924 shares of our common stock that may be offered from time to time by Deerfield, the maximum number of shares of our common stock which would be issued upon conversion of the Convertible Notes assuming the lowest possible conversion price of \$7.00 per share, and such registration was declared effective by the SEC on July 11, 2017. Deerfield cannot own more than 9.985% of our outstanding shares at any one time, and the aggregate conversion could not exceed 19.9% of our outstanding common stock as of June 1, 2017.

The principal amount of the Convertible Notes issued under the Amendment and all accrued and unpaid interest thereon was to become due and payable upon written notice from the Deerfield, and if either (a) we did not meet certain quarterly sales milestones specified in the Amendment or (b) we did not receive and publicly announce FDA approval of the new drug applications on or before the applicable PDUFA goal date as set forth on the schedules to Amendment. Per the Amendment, we will prepay all of the outstanding obligations under the Facility and the Convertible Notes upon the occurrence of a change in control or a sale of substantially all of our assets and liabilities. The Amendment increased the staggered prepayment fees for prepayments due upon a change of control or any other prepayment made or required to be made by us by 300 basis points from June 1, 2017 through the period ending prior to May 11, 2020 for the change in control prepayment fees and through the period ending prior to May 11, 2022 for any other prepayments, respectively (the "Prepayment Premiums"). Such Prepayment Premiums, as amended, range from 12.75% to 2%.

On October 26, 2017, Deerfield elected to convert the entire \$6.6 million of Convertible Notes into shares of the Company's common stock at a conversion price of \$7.08 per share. This resulted in issuing 929,967 shares of the Company's common stock to Deerfield on this date and the Convertible Notes were cancelled.

Borrowings under the Facility are collateralized by substantially all of our assets, except the assets under capital lease, and we will maintain cash on deposit of not less than \$5.0 million. The Facility also contains certain customary nonfinancial covenants, including limitations on our ability to transfer assets, engage in a change of control, merge or acquire with or into another entity, incur additional indebtedness and distribute assets to shareholders. Upon an event of default, the lender may declare all outstanding obligations accrued under the Facility to be immediately due and payable, and exercise its security interests and other rights. As of December 31, 2017, we were in compliance with the covenants under the Facility.

We had a Note in the aggregate principal amount of \$5.9 million that was issued by us to Essex which was to mature in March 2017. Interest was to be accrued and added to the principal balance until such time as we achieved positive EBITDA for three consecutive months. The \$5.9 million Note and the related \$1.3 million of accrued interest were repaid on May 11, 2016 with proceeds from the Facility as mentioned above.

During the years ended December 31, 2017, 2014 and 2013, we entered into agreements with Essex for the sale-leaseback of existing and newly acquired assets with a total capitalized cost of \$3.2 million, \$795,000 and \$5.5 million, respectively, with bargain purchase options at the end of each respective lease, all of which are classified as capital leases. The two February 2013 leases for a total of \$3.5 million of assets expired in July 2016, the July 2013 lease for a total of \$1.0 million of assets expired in December 2016, the November 2013 lease for a total of \$1.0 million of assets expired in April 2017, the March 2014 lease for a total of \$795,000 of assets expired in September 2017, and all lease buy-out liabilities were satisfied. The approximate imputed interest rate on these leases is 14.9%, 14.5% and 14.5%, respectively. See “Contractual Commitments and Obligations” below for future payments under these leases.

### **Capital resources and funding requirements**

On August 1, 2016, we filed a shelf registration statement on Form S-3 with the SEC, which covers the offering, issuance and sale by us of up to an aggregate of \$125.0 million of our common stock, preferred stock, debt securities, warrants and/or units. We simultaneously entered into a Sales Agreement with Cowen and Company, LLC, as sales agent, to provide for the offering, issuance and sale by us of up to \$40.0 million of our common stock from time to time in “at-the-market” offerings under the Shelf. The Shelf was declared effective by the SEC on August 12, 2016.

In February 2017, pursuant to the Shelf, we closed an underwritten public offering of 5,750,000 shares of our common stock at a public offering price of \$5.00 per share, which includes 750,000 shares of our common stock resulting from the underwriters’ exercise of their over-allotment option at the public offering price on February 17, 2017. The net proceeds to us from this offering, after deducting underwriting discounts and commissions and other offering expenses payable by us were approximately \$26.7 million.

On June 30, 2017, pursuant to the Shelf, we closed an underwritten public offering of 4,800,000 shares of our common stock at a price of \$6.25 per share for total proceeds of \$30.0 million before estimated offering costs of \$0.2 million. We also granted the underwriters a 30-day option to purchase up to an additional 720,000 shares of our common stock which the underwriters exercised in full on July 26, 2017. The net proceeds to us from this offering, after deducting offering expenses payable by us, were approximately \$34.3 million.

During the year ended December 31, 2017, we sold an aggregate 749,639 shares of common stock under the Sales Agreement at an average sale price of approximately \$5.01 per share. As of December 31, 2017, \$58.0 million of our common stock, preferred stock, debt securities, warrants and/or units remained available to be sold pursuant to the Shelf, including \$36.2 million of common stock which remained available to be sold under the Sales Agreement, subject to certain conditions specified therein.

We may continue to seek private or public equity and debt financing to meet our capital requirements. There can be no assurance that such funds will be available on terms favorable to us, if at all, or that we will be able to successfully commercialize Adzenys XR-ODT, Cotempla XR-ODT, Adzenys ER or, if approved, our new product candidates. In addition, we may not be profitable even if we succeed in commercializing Adzenys XR-ODT, Cotempla XR-ODT, Adzenys ER or, if approved, any of our new product candidates. We expect to continue to incur operating losses over the next several years as we seek regulatory approval for our product candidates and build and operate commercial infrastructure to support sales and marketing of Adzenys XR-ODT, Cotempla XR-ODT, Adzenys ER and, if approved, our product candidates that we may develop. We believe that our existing cash and cash equivalents and short-term investments will be sufficient to fund our anticipated operating requirements for at least the next twelve months. We have based this estimate on assumptions that may prove to be wrong, resulting in the use of our available capital resources sooner

than we currently expect. Because of the numerous risks and uncertainties associated with the development and commercialization of our products and product candidates, we are unable to estimate the amount of increased capital required to become profitable. Our future funding requirements will depend on many factors, including:

- the costs of operating our sales, marketing and distribution capabilities;
- the market acceptance of our products and, if approved, product candidates and related success in commercializing and generating sales from our products and, if approved, product candidates, that we may develop;
- the costs of our manufacturing capabilities to support our commercialization activities, including any costs associated with adding new capabilities;
- the costs and timing involved in obtaining regulatory approvals for our new product candidates;
- the timing and number of product candidates for which we obtain regulatory approval;
- the costs of maintaining, expanding and protecting our intellectual property portfolio, including potential litigation costs and liabilities;
- the number and characteristics of new product candidates that we pursue; and
- our ability to hire qualified employees at salary levels consistent with our estimates to support our growth and development, including additional general and administrative personnel as a result of becoming a public company, and sales and marketing personnel to commercialize our approved products.

We may not generate a sufficient amount of product revenues from sales of Adzenys XR-ODT, Cotempla XR-ODT and Adzenys ER to finance our cash requirements. Until we obtain regulatory approval to market our new product candidates, if ever, we cannot generate revenues from sales of those products. Even if we are able to sell our products, including Adzenys XR-ODT, Cotempla XR-ODT and Adzenys ER, we may not generate a sufficient amount of product revenues to finance our cash requirements. Accordingly, we may need to obtain additional financing in the future which may include public or private debt and equity financings and/or entrance into product and technology collaboration agreements or licenses and asset sales. There can be no assurance that additional capital will be available when needed on acceptable terms, or at all. The issuance of equity securities may result in dilution to stockholders. If we raise additional funds through the issuance of debt securities, these securities may have rights, preferences and privileges senior to those of our common stock and the terms of the debt securities could impose significant restrictions on our operations. If we raise additional funds through collaborations and licensing arrangements, we might be required to relinquish significant rights to our technologies or products, or grant licenses on terms that are not favorable to us. If adequate funds are not available, we may have to scale back our commercial operations or limit our research and development activities, which would have a material adverse impact on our business prospects and results of operations.

## **CRITICAL ACCOUNTING POLICIES AND SIGNIFICANT JUDGMENTS AND ESTIMATES**

Our management's discussion and analysis of financial condition and results of operations is based on our financial statements, which have been prepared in accordance with accounting principles generally accepted in the United States ("GAAP"). The preparation of our financial statements requires us to make estimates and judgments that affect the reported amounts of assets and liabilities and the disclosure of any contingent assets and liabilities at the date of the financial statements, as well as reported revenue and expenses during the reporting periods. On an ongoing basis, we evaluate our estimates and judgments. We base our estimates on our historical experience and on various other assumptions that we believe to be reasonable under the circumstances. These estimates and

assumptions form the basis for making judgments about the carrying values of assets and liabilities that are not readily apparent from other sources. Our actual results may differ materially from these estimates under different assumptions or conditions.

While our significant accounting policies are described in more detail in Note 2 to the notes to our audited financial statements included elsewhere in this Annual Report on Form 10-K, we believe the following accounting policies to be critical to the judgments and estimates used in the preparation of our consolidated financial statements.

### Revenue recognition

Revenue is generated from product sales, recorded on a net sales basis in consideration of savings offers, prompt pay discounts, product returns, rebates, wholesaler fees and chargebacks, each of which is described in more detail below. Product revenue is recognized when all of the following criteria are met: persuasive evidence of an arrangement exists; delivery has occurred or services have been rendered; price to the buyer is fixed and determinable; and collectability is reasonably assured. Revenue from sales transactions where the buyer has the right to return the product is recognized at the time of sale only if the price to the buyer is substantially fixed or determinable at the date of sale, the buyer has paid for the product, or the buyer is obligated to pay for the product and the obligation is not contingent on resale of the product, the buyer's obligation to pay would not be changed in the event of theft or physical destruction or damage of the product, the buyer acquiring the product for resale has economic substance apart from that provided by us, we do not have significant obligations for future performance to directly bring about resale of the product by the buyer and the amount of future returns can be reasonably estimated.

We have a limited sales history for Adzenys XR-ODT and Cotempla XR-ODT and no sales history for Adzenys ER, and have determined that at this time we cannot reliably estimate expected returns of the product at the time of shipment to wholesalers. Accordingly, we defer recognition of revenue on product shipments of Adzenys XR-ODT and Cotempla XR-ODT until the right of return no longer exists, which occurs at the earlier of the time Adzenys XR-ODT and Cotempla XR-ODT units are dispensed through patient prescriptions or expiration of the right of return. We calculate patient prescriptions of Adzenys XR-ODT and Cotempla XR-ODT dispensed using an analysis of third-party information.

We sell our generic Tussionex, Adzenys XR-ODT and Cotempla XR-ODT to a limited number of pharmaceutical wholesalers. Pharmaceutical wholesalers buy drug products directly from manufacturers. Title to the product passes upon delivery to the wholesalers, when the risks and rewards of ownership are assumed by the wholesaler. These wholesalers then resell the product to retail customers such as food, drug and mass merchandisers.

Revenues for Adzenys XR-ODT, Cotempla XR-ODT and generic Tussionex for the years ended December 31, 2017, 2016 and 2015, respectively, are as follows:

	<b>Year Ended December 31,</b>		
	<b>2017</b>	<b>2016</b>	<b>2015</b>
	<b>(in thousands)</b>		
Adzenys XR-ODT . . . . .	\$18,959	\$2,924	\$ —
Cotempla XR-ODT . . . . .	894	—	—
Generic Tussionex . . . . .	5,165	6,230	3,792
	<u>\$25,018</u>	<u>\$9,154</u>	<u>\$3,792</u>

### *Net branded product sales*

Net product sales for our branded Adzenys XR-ODT and Cotempla XR-ODT products represent total gross product sales less gross to net sales adjustments. Gross to net sales adjustments include savings offers, prompt payment discounts, wholesaler fees and estimated rebates to be incurred on the selling price of the respective product sales. We recognize branded total gross product sales less gross to net sales adjustments as revenue based on information from third-party providers.

### *Savings offers*

We offer savings programs for Adzenys XR-ODT and Cotempla XR-ODT to patients covered under commercial payor plans in which the cost of a prescription to such patients is discounted. We record the amount of redeemed savings offers based on information from third-party providers and recognize the discount as a reduction of revenue in the same period the related revenue is recognized.

### *Prompt payment discounts*

Prompt payment discounts are based on standard programs with wholesalers and are recorded as a discount allowance against accounts receivable and as a deferred discount reduction of deferred revenue. The deferred discounts are subsequently recorded within net product sales when the deferred revenue is recognized into revenue based on units dispensed through patient prescriptions.

### *Wholesale distribution fees*

Wholesale distribution fees are based on definitive contractual agreements for the management of our products by wholesalers and are recorded as deferred wholesale distribution fees in other current assets. The deferred wholesale distribution fees are subsequently recorded within net product sales when the deferred revenue is recognized into revenue based on units are dispensed through patient prescriptions.

### *Rebates*

Our products are subject to commercial managed care and government-managed Medicare and Medicaid programs whereby discounts and rebates are provided to participating managed care organizations and federal and/or state governments. Calculations related to these rebate accruals are estimated based on information from third-party providers. Estimated rebates payable under such programs are recorded as a reduction of revenue at the time revenues are recorded. Historical trends of estimated rebates will be continually monitored and may result in future adjustments to such estimates.

The following table presents our gross to net sales deductions for our Adzenys XR-ODT which we launched commercially on May 16, 2016 and for our Cotempla XR-ODT which we initiated an early



experience program with limited product availability on September 5, 2017 and launched nationwide on October 2, 2017:

	<u>Cash Discounts</u>	<u>Sales Offers</u>	<u>Wholesaler Fees</u>	<u>Government Rebates</u>	<u>Total Gross to Net Sales Deductions</u>
	(in thousands)				
<b>Balance at December 31, 2015</b> . . . . .	\$ —	\$ —	\$ —	\$ —	\$ —
<b>Provision, net</b> . . . . .	384	3,746	1,082	444	5,656
<b>Payments / credits</b> . . . . .	(311)	(3,746)	(766)	(61)	(4,884)
<b>Due to (paid to) third party and deferred until sales recognized</b> . . . . .	(13)	—	144	—	131
<b>Balance at December 31, 2016</b> . . . . .	\$ 60	\$ —	\$ 460	\$ 383	\$ 903
<b>Provision, net</b> . . . . .	1,468	25,880	6,834	6,596	40,778
<b>Payments / credits</b> . . . . .	(1,242)	(25,880)	(5,732)	(4,355)	(37,209)
<b>Due to (paid to) third party and deferred until sales recognized</b> . . . . .	(47)	—	684	—	637
<b>Balance at December 31, 2017</b> . . . . .	\$ 239	\$ —	\$ 2,246	\$ 2,624	\$ 5,109

Total items deducted from gross product sales were \$39,450 and \$5,627, or 66.5% and 64.3% as a percentage of gross product sales, for the years ended December 31, 2017 and 2016, respectively, due principally to the savings offers being made to penetrate the ADHD market.

*Net generic product sales*

Net product sales for our generic Tussionex product represent total gross product sales less gross to net sales adjustments. Gross to net sales adjustments include prompt payment discounts, estimated allowances for product returns, wholesaler fees, estimated government rebates and estimated chargebacks to be incurred on the selling price of generic Tussionex related to the respective product sales. We recognize generic Tussionex total gross product sales less gross to net sales adjustments as revenue based on shipments from our 3PL's to our wholesaler customers.

*Prompt payment discounts*

Prompt payment discounts are based on standard programs with wholesalers and are recorded as a discount allowance against accounts receivable and as a gross to net sales adjustments at the time revenue is recognized.

*Product returns*

Wholesalers' contractual return rights are limited to defective product, product that was shipped in error, product ordered by customer in error, product returned due to overstock, product returned due to dating or product returned due to recall or other changes in regulatory guidelines. The return policy for expired product allows the wholesaler to return such product starting six months prior to expiry date to twelve months post expiry date.

Estimated returns are recorded as accrued expenses and as a gross to net sales adjustments at the time revenue is recognized. During 2017, generic Tussionex product returns were estimated based upon return data available from sales of our generic Tussionex product over the past three years. Prior to 2017, generic Tussionex product returns were estimated based upon data available from sales of our generic Tussionex product provided by our former commercialization partner.

### Wholesale distribution fees

Wholesale distribution fees are based on definitive contractual agreements for the management of our products by wholesalers and are recorded as accrued expenses and as a gross to net sales adjustments at the time revenue is recognized.

### Rebates

Our generic Tussionex product is subject to state government-managed Medicaid programs whereby discounts and rebates are provided to participating state governments. Estimated government rebates are recorded as accrued expenses and as a gross to net sales adjustments at the time revenue is recognized. During 2017, generic Tussionex government rebates were estimated based upon rebate payment data available from sales of our generic Tussionex product over the past three years. Prior to 2017, Generic Tussionex government rebates were estimated based on information from third-party providers. Historical trend of such rebates will be continually monitored and may result in future adjustments to such estimates.

### Wholesaler Chargebacks

Our products are subject to certain programs with wholesalers whereby pricing on products is discounted below wholesaler list price to participating entities. These entities purchase products through wholesalers at the discounted price, and the wholesalers charge the difference between their acquisition cost and the discounted price back to us. Estimated chargebacks are recorded as a discount allowance against accounts receivable and as a gross to net sales adjustments at the time revenue is recognized based on information provided by third parties.

Due to estimates and assumptions inherent in determining the amount of returns, rebates and chargebacks, the actual amount of returns and claims for rebates and chargebacks may be different from the estimates, at which time reserves would be adjusted accordingly. Wholesale distribution fees and the allowance for prompt pay discounts are recorded at the time of shipment and such fees and allowances and all other accruals are recorded in the same period that the related revenue is recognized.

The following table presents our gross to net sales deductions for our generic Tussionex since we acquired the rights to the Tussionex ANDA on August 28, 2014 and began to derive revenue directly from sales made by us:

	<u>Chargebacks</u>	<u>Cash Discounts</u>	<u>Wholesaler Fees</u>	<u>Returns</u>	<u>Government Rebates</u>	<u>Total Gross to Net Sales Deductions</u>
			(in thousands)			
<b>Balance at December 31, 2014</b> . .	190	14	117	212	9	542
<b>Provision, net</b> . . . . .	5,359	194	914	242	103	6,812
<b>Payments / credits</b> . . . . .	(4,609)	(109)	(670)	(25)	(2)	(5,415)
<b>Balance at December 31, 2015</b> . .	940	99	361	429	110	1,939
<b>Provision, net</b> . . . . .	10,504	388	1,756	491	(48)	13,091
<b>Payments / credits</b> . . . . .	(10,665)	(376)	(2,068)	(36)	(24)	(13,169)
<b>Balance at December 31, 2016</b> . .	\$ 779	\$ 111	\$ 49	\$ 884	\$ 38	\$ 1,861
<b>Provision, net</b> . . . . .	10,146	346	1,452	167	43	12,154
<b>Payments / credits</b> . . . . .	(10,109)	(359)	(1,360)	(158)	(18)	(12,004)
<b>Balance at December 31, 2017</b> . .	\$ 816	\$ 98	\$ 141	\$ 893	\$ 63	\$ 2,011

Total items deducted from gross product sales were \$12,154, \$13,091 and \$6,812, or 70.2%, 67.8% and 64.2% as a percentage of gross product sales, for the years ended December 31, 2017, 2016 and 2015, respectively. The increase in the gross to net sales deduction percentage resulted from a higher proportion of the sales being made to a major pharmacy chain that receives volume pricing concessions.

### **Inventories**

Inventories are stated at the lower of cost (first in, first out) or market in 2016 and, effective January 1, 2017, inventory is now required to be measured at the lower of cost (first in, first out) or net realizable value. The change to stating inventories at the lower of cost or net realizable value in 2017 was adopted prospectively and did not have a significant effect on our ongoing financial reporting as valuing inventory at the lower of cost or net realizable value approximated the prior policy of valuing inventory at the lower of cost or market. Inventories have been reduced by an allowance for excess and obsolete inventories. Cost elements include material, labor and manufacturing overhead. Inventories consist of raw materials, work in process, finished goods and deferred cost of goods sold. The cost of sales associated with the deferred product revenues are recorded as deferred costs of goods sold that are released from inventory into cost of goods sold as the deferred revenue is recognized into revenue.

Until objective and persuasive evidence exists that regulatory approval has been received and future economic benefit is probable, pre-launch inventories are expensed into research and development. Manufacturing costs for the production of Adzenys XR-ODT incurred after the January 27, 2016 FDA approval date are being capitalized into inventory, for the production of Cotempla XR-ODT incurred after June 30, 2017, following the FDA approval date of June 19, 2017, and for the production of Adzenys ER incurred after September 30, 2017, following the FDA approval date of September 15, 2017, are being capitalized into inventory.

### **Research and development expenses**

Research and development expenses include costs incurred in performing research and development activities, personnel related expenses, laboratory and clinical supplies, facilities expenses, overhead expenses, fees for contractual services, including preclinical studies, clinical trials and raw materials. We estimate clinical trial expenses based on the services received pursuant to contracts with research institutions and CROs which conduct and manage clinical trials on our behalf. We accrue service fees based on work performed, which relies on estimates of total costs incurred based on milestones achieved, patient enrollment and other events. The majority of our service providers invoice us in arrears, and to the extent that amounts invoiced differ from our estimates of expenses incurred, we accrue for additional costs. The financial terms of these agreements vary from contract to contract and may result in uneven expenses and cash flows. To date, we have not experienced any events requiring us to make material adjustments to our accruals for service fees. If we do not identify costs that we incurred or if we underestimate or overestimate the level of services performed, our actual expenses could differ from our estimates which could materially affect our results of operations. Adjustments to our accruals are recorded as changes in estimates become evident. In addition to accruing for expenses incurred, we may also record payments made to service providers as prepaid expenses that we will recognize as expense in future periods as services are rendered.

### **Share-based compensation expense**

Share-based compensation awards, including grants of employee stock options and restricted stock and modifications to existing stock options, are recognized in the statement of operations based on their fair values. Compensation expense related to awards to employees is recognized on a straight-line basis, based on the grant date fair value, over the requisite service period of the award, which is generally the vesting term. The fair value of our share-based awards to employees and directors is

estimated using the Black-Scholes option pricing model, which requires the input of subjective assumptions, including (1) the expected stock price volatility, (2) the expected term of the award, (3) the risk-free interest rate and (4) expected dividends. Due to the previous lack of a public market for the trading of our common stock and a lack of company-specific historical and implied volatility data, prior to the IPO, we have historically utilized third party valuation analyses to determine the fair value.

Under new guidance for accounting for share-based payments, we have elected to continue estimating forfeitures at the time of grant and, if necessary, revise the estimate in subsequent periods if actual forfeitures differ from those estimates. Ultimately, the actual expense recognized over the vesting period will only be for those options that vest. The adoption of this standard in 2017 did not have a material impact on our business, financial position, results of operations or liquidity.

We calculated the fair value of share-based compensation awards using the Black-Scholes option-pricing model. The Black-Scholes option-pricing model requires the input of subjective assumptions, including stock price volatility and the expected life of stock options. The application of this valuation model involves assumptions that are highly subjective, judgmental and sensitive in the determination of compensation cost. As a formerly private company, we do not have sufficient history to estimate the volatility of our common stock price or the expected life of our options. We have not paid and do not anticipate paying cash dividends. Therefore, the expected dividend rate is assumed to be 0%. The expected stock price volatility for stock option awards was based on a blended volatility rate of prior studies of historical volatility from a representative peer group of comparable companies' selected using publicly-available industry and market capitalization data and 30 months of the Company's stock price volatility. The risk-free rate was based on the U.S. Treasury yield curve in effect commensurate with the expected life assumption. The average expected life of stock options was determined according to the "simplified method" as described in SAB Topic 110, which is the midpoint between the vesting date and the end of the contractual term. The risk-free interest rate was determined by reference to implied yields available from U.S. Treasury securities with a remaining term equal to the expected life assumed at the date of grant. We estimate forfeitures based on our historical analysis of actual stock option forfeitures. We estimate the fair value of all stock option awards on the grant date by applying the Black-Scholes option pricing valuation model. Given the absence of an active market for our common stock prior to our IPO, our board of directors was required to estimate the fair value of our common stock at the time of each option grant primarily based upon valuations performed by a third party valuation firm. After the closing of our IPO, our board of directors has determined the fair value of each share of underlying common stock based on the closing price of our common stock as reported by the NASDAQ Global Market on the date of grant.

There is a high degree of subjectivity involved when using option-pricing models to estimate share-based compensation. There is currently no market-based mechanism or other practical application to verify the reliability and accuracy of the estimates stemming from these valuation models, nor is there a means to compare and adjust the estimates to actual values. Although the fair value of employee stock-based awards is determined using an option-pricing model, such a model value may not be indicative of the fair value that would be observed in a market transaction between a willing buyer and willing seller. If factors change and we employ different assumptions when valuing our options, the compensation expense that we record in the future may differ significantly from what we have historically reported.

### **Derivative liabilities**

We evaluate our debt and equity issuances to determine if those contracts or embedded components of those contracts qualify as derivatives requiring separate recognition in our financial statements. The result of this accounting treatment is that the fair value of the embedded derivative is marked-to-market each balance sheet date and recorded as a liability and the change in fair value is recorded in other income (expense) in the consolidated results of operations. In circumstances where

the embedded conversion option in a convertible instrument is required to be bifurcated and there are also other embedded derivative instruments in the convertible instrument that are required to be bifurcated, the bifurcated derivative instruments are accounted for as a single, compound derivative instrument. The classification of derivative instruments, including whether such instruments should be recorded as liabilities or as equity, is reassessed at the end of each reporting period. Equity instruments that are initially classified as equity that become subject to reclassification are reclassified to liability at the fair value of the instrument on the reclassification date. Derivative instrument liabilities are classified in the balance sheet as current or non-current based on whether or not net-cash settlement of the derivative instrument is expected within twelve months of the balance sheet date.

When we have determined that the embedded conversion options should not be bifurcated from their host instruments, we record, when necessary, discounts to convertible notes for the intrinsic value of conversion options embedded in debt instruments based upon the differences between the fair value of the underlying common stock at the commitment date of the note transaction and the effective conversion price embedded in the note. Debt discounts under these arrangements are amortized over the term of the related debt to their stated date of redemption and recorded in interest expense in the consolidated financial statements.

### Intangible assets

Intangible assets subject to amortization, which principally include our proprietary modified-release drug delivery technology, the costs to acquire the rights to Tussionex ANDA and patents, are recorded at cost and are amortized over the estimated lives of the assets, which primarily range from 10 to 20 years.

### CONTRACTUAL COMMITMENTS AND OBLIGATIONS

The following table reflects a summary of our estimates of future material contractual obligations as of December 31, 2017. Future events could cause actual payments to differ from these estimates.

	<u>Total</u>	<u>&lt; 1 Yr</u>	<u>1 - 3 Yrs.</u>	<u>3 - 5 Yrs</u>	<u>Thereafter</u>
	(In thousands)				
Deerfield senior secured facility . . . . .	\$83,186	\$ 7,878	\$41,601	\$33,707	—
Capital leases for equipment . . . . .	3,246	1,235	2,011	—	—
Earnout liability . . . . .	170	—	—	—	170
Texas facility operating lease . . . . .	7,138	955	1,961	2,060	2,162
Pennsylvania office space lease . . . . .	510	149	308	53	—
Equipment operating leases . . . . .	185	73	107	5	—
	<u>\$94,435</u>	<u>\$10,290</u>	<u>\$45,988</u>	<u>\$35,825</u>	<u>\$2,332</u>

We had borrowed all \$60.0 million under the Deerfield Facility as of December 31, 2017. The payments above are inclusive of related interest amounts as of December 31, 2017.

In addition to the commitments shown above, in response to a lawsuit brought against us by Shire LLC (“Shire”) for infringement of certain of Shire’s patents, we entered into a Settlement Agreement and an associated License Agreement (the “2014 License Agreement”) with Shire for a non-exclusive license to certain patents for certain activities with respect to our New Drug Application (the “NDA”) No. 204326 for an extended-release orally disintegrating amphetamine polistirex tablet in July 2014. Under the terms of the license agreement, after receiving regulatory approval by the FDA of our NDA for Adzenys XR-ODT, in the first quarter of 2016, we paid a lump sum, non-refundable license fee of an amount less than \$1.0 million. This license fee was capitalized and is being amortized over the life of the longest associated patent. We are paying a single digit royalty on net sales of Adzenys XR-ODT during the life of the patents.

On March 6, 2017, after our NDA submission for Adzenys ER requiring a Paragraph IV certification notification to the producer of Adderall XR, Shire Pharmaceuticals, in accordance with the Hatch-Waxman Amendments, we entered into a License Agreement (the “2017 License Agreement”) with Shire. Pursuant to this agreement, Shire granted us a non-exclusive license to certain patents owned by Shire for certain activities with respect to our NDA No. 204325 for an extended-release amphetamine liquid suspension. Under the terms of the agreement, after receiving regulatory approval by the FDA of our NDA for Adzenys ER, in October 2017, we paid a lump sum, non-refundable license fee of an amount less than \$1.0 million. This license fee was capitalized and is being amortized over the life of the longest associated patent. We will also pay a single digit royalty on net sales of the Adzenys ER during the life of the relevant Shire patents.

Due to the uncertainty of when these royalty payments will be made for Adzenys XR-ODT and Adzenys ER, they are not presented in the table above. The license fees are paid and recorded as an intangible asset and amortized over the term of the license. The royalties are being recorded as cost of goods sold in the same period as the net sales upon which they are calculated.

#### **OFF-BALANCE SHEET ARRANGEMENTS**

We did not have during the periods presented, and we do not currently have, any off-balance sheet arrangements, as defined in the rules and regulations of the SEC, including any relationships with unconsolidated entities or financial partnerships, such as entities referred to as structured finance or special purpose entities, which are established for the purpose of facilitating off-balance sheet arrangements or other contractually narrow or limited purposes.

#### **RECENT ACCOUNTING PRONOUNCEMENTS**

See Note 2 to the notes to our consolidated financial statements included elsewhere in this Annual Report on Form 10-K for further discussion of recent accounting pronouncements.

#### **ITEM 7A. Qualitative and Quantitative Disclosures About Market Risk**

##### **Market risk**

We are exposed to market risk related to changes in interest rates as it impacts our interest income. As of December 31, 2017, we had cash and cash equivalents of \$32.0 million and short-term investments of \$18.4 million. Our primary exposure to market risk is interest income sensitivity, which is affected by changes in the general level of U.S. interest rates as our cash equivalents are invested in interest-bearing money market funds. The goals of our investment policy are liquidity and capital preservation to fund our operations. Due to the short-term duration and low risk profile of our cash equivalents portfolio, a 10% change in interest rates would not have a material effect on interest income we recognize or the fair market value of our investments. Accordingly, we would not expect our operating results or cash flows to be affected to any significant degree by the effect of a sudden change in market interest rates.

##### **Interest risk**

The interest rates on our notes payable are fixed. Therefore, we are not exposed to market risk from changes in interest rates as it relates to these interest-bearing obligations.

##### **Effects of Inflation**

We do not believe that inflation and changing prices had a significant impact on our results of operations for any periods presented herein.

## **JOBS ACT**

In April 2012, the Jumpstart Our Business Startups Act, or the JOBS Act, was enacted in the United States. Section 107 of the JOBS Act provides that an “emerging growth company” can take advantage of the extended transition period provided in Section 7(a)(2)(B) of the Securities Act of 1933, as amended, for complying with new or revised accounting standards. Thus, an emerging growth company can delay the adoption of certain accounting standards until those standards would otherwise apply to private companies. We have irrevocably elected not to avail ourselves of this extended transition period and, as a result, we will adopt new or revised accounting standards on the relevant dates on which adoption of such standards is required for non-emerging growth companies.

### **ITEM 8. Financial Statements and Supplementary Data**

The financial statements required to be filed pursuant to this Item 8 are appended to this report. An index of those financial statements is found in Item 15.

### **ITEM 9. Changes in and Disagreements with Accountants on Accounting and Financial Disclosure**

None.

### **ITEM 9A. Controls and Procedures**

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

Our management, with the participation of our principal executive officer and principal financial officer, has evaluated the effectiveness of our disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934, as amended (the “Exchange Act”)), as of the end of the period covered by this Annual Report on Form 10-K. Based on such evaluation, our principal executive officer and principal financial officer have concluded that as of such date, our disclosure controls and procedures were effective.

#### **Management’s Report on Internal Control Over Financial Reporting and Attestation Report of the Registered Public Accounting Firm**

Our management is responsible for establishing and maintaining adequate internal control over financial reporting for our company. Internal control over financial reporting is defined in Rule 13a-15(f) or 15d-15(f) promulgated under the Exchange Act as a process designed by, or under the supervision of, the company’s principal executive and principal financial officer and effected by the company’s board of preparation of financial statements for external purposes in accordance with GAAP and directors, management and other personnel, to provide reasonable assurance regarding the reliability of financial reporting and the includes those policies and procedures that: (i) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; (ii) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of our company are being made only in accordance with authorizations of management and directors of the company; and (iii) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of our company’s assets that could have a material effect on the financial statements.

Internal control over financial reporting is designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements prepared for external purposes in accordance with generally accepted accounting principles. Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

Our management, with the participation of our principal executive and principal financial officer, assessed the effectiveness of our internal control over financial reporting as of December 31, 2017, based on criteria for effective internal control over financial reporting established in Internal Control—Integrated Framework (2013), issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO). Based on its assessment, management concluded that our internal control over financial reporting was effective as of December 31, 2017, based on those criteria.

#### **Inherent Limitations of Internal Controls**

Our management, including our Chief Executive Officer and Chief Financial Officer, does not expect that our disclosure controls and procedures or our internal controls will prevent all errors and all fraud. 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 the inherent limitations in all control systems, no evaluation of controls can provide absolute assurance that all control issues and instances of fraud, if any, within the Company have been detected. These inherent limitations include the realities that judgments in decision-making can be faulty, and that breakdowns can occur because of a simple error or mistake. Additionally, controls can be circumvented by the individual acts of some persons, by collusion of two or more people, or by management override of the control. The design of any system of controls also is based in part upon certain assumptions about the likelihood of future events, and there can be no assurance that any design will succeed in achieving its stated goals under all potential future conditions. Over time, controls may become inadequate because of changes in conditions, or the degree of compliance with the policies or procedures may deteriorate. Because of the inherent limitations in a cost-effective control system, misstatements due to error or fraud may occur and not be detected.

#### **Changes in Internal Control over Financial Reporting**

There have been no changes in our internal control over financial reporting during our most recent fiscal quarter that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

#### **ITEM 9B. *Other Information***

None.

### **PART III**

#### **ITEM 10. *Directors, Executive Officers and Corporate Governance***

Except as set forth below, information required by this item will be included under the captions *Elections of Directors, Information Regarding the Board of Directors and Corporate Governance, Executive Compensation and Other Information*, and *Section 16(a) Beneficial Ownership Reporting Compliance* contained in our definitive Proxy Statement to be filed with the Commission within 120 days after the conclusion of our year ended December 31, 2017 (the “Proxy Statement”) pursuant to General Instructions G(3) of Form 10-K and is incorporated herein by reference.

We have adopted a code of business conduct and ethics that applies to all of our employees, officers and directors, including those officers responsible for financial reporting. Our code of business conduct and ethics is available on our website, which is located at [www.neostx.com](http://www.neostx.com). We intend to disclose any amendments to the code, or any waivers of its requirements, on our website, or in a current report on Form 8-K as may be required by law or applicable NASDAQ rules.



**ITEM 11. *Executive Compensation***

We maintain an employee compensation program and benefit plans in which our executive officers are participants. Copies of these plans and programs are set forth or incorporated by reference as Exhibits to this report. The information required by this item will be included in our Proxy Statement under the caption *Executive Compensation and Other* and is incorporated herein by reference.

**ITEM 12. *Security Ownership of Certain Beneficial Owners and Management and Related Stockholder Matters***

Information required by this item will be included under the captions *Security Ownership of Certain Beneficial Owners and Management* and *Executive Compensation* contained in our Proxy Statement and is incorporated herein by reference.

**ITEM 13. *Certain Relationships and Related Party Transactions, and Director Independence***

Information required by this item will be included under the captions *Certain Relationships and Related Transactions* and *Information Regarding the Board of Directors* contained in our Proxy Statement and is incorporated herein by reference.

**ITEM 14. *Principal Accounting Fees and Services***

Information required by this item will be included under the captions *Selection of Independent Registered Public Accounting Firm* contained in our Proxy Statement and is incorporated herein by reference.

## PART IV

### ITEM 15. Exhibits and Financial Statement Schedules

(a) Documents filed as part of this report:

- (1) *Financial Statements.* The following financial statements of Neos Therapeutics, Inc., together with the report thereon of RSM US LLP, required to be filed pursuant to Part II, Item 8 of this Annual Report on Form 10-K, are included on pages **F-2** through **F-41**, as follows:

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Report of Independent Registered Public Accounting Firm . . . . .	F-2
Consolidated Balance Sheets at December 31, 2017 and 2016 . . . . .	F-3
Consolidated Statements of Operations for the years ended December 31, 2017, 2016 and 2015 . .	F-4
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- (2) *Financial Statement Schedule.*

Schedule II—Valuation and Qualifying Accounts

- (3) The exhibits required by Items 601 of Regulation S-K are listed in the Exhibit Index immediately preceding the exhibits and are incorporated herein.

(b) Exhibits:

<u>Exhibit number</u>	<u>Description of exhibit</u>
3.1	Fourth Amended and Restated Certificate of Incorporation of the Registrant, as amended and currently in effect (Filed as an Exhibit to the Registrant's quarterly report on Form 10-Q (001-37508), filed with the SEC on September 4, 2015, incorporated herein by reference).
3.2	Amended and Restated Bylaws of the Registrant, as amended and currently in effect (Filed as an Exhibit to the Registrant's quarterly report on Form 10-Q (001-37508), filed with the SEC on September 4, 2015, incorporated herein by reference).
4.1	Form of common stock certificate (Filed as an Exhibit to the Registrant's registration statement on Form S-1 (333-205106), filed with the SEC on July 13, 2015, incorporated herein by reference).
4.2	Form of warrant to purchase common stock (Filed as an Exhibit to the Registrant's registration statement on Form S-1 (333-205106), filed with the SEC on June 19, 2015, incorporated herein by reference).
10.1	Amended and Restated Investors' Rights Agreement, dated as of June 9, 2015 (Filed as an Exhibit to the Registrant's registration statement on Form S-1 (333-205106), filed with the SEC on June 19, 2015, incorporated herein by reference).

Exhibit number	Description of exhibit
10.2	Amendment and Waiver, dated as of February 5, 2016, amending the Amended and Restated Investors' Rights Agreement of the Registrant (Filed as an Exhibit to the Registrant's annual report on Form 10-K (001-37508), filed with the SEC on March 18, 2016, incorporated herein by reference).
10.3+	Neos Therapeutics, Inc. 2009 Equity Plan (Filed as an Exhibit to the Registrant's registration statement on Form S-1 (333-205106), filed with the SEC on June 19, 2015, incorporated herein by reference).
10.4+	Form of option agreements under 2009 Equity Plan (Filed as an Exhibit to the Registrant's registration statement on Form S-1 (333-205106), filed with the SEC on June 19, 2015, incorporated herein by reference).
10.5+	Neos Therapeutics, Inc. 2015 Stock Option and Incentive Plan and forms of option agreements thereunder (Filed as an Exhibit to the Registrant's registration statement on Form S-1 (333-205106), filed with the SEC on July 13, 2015, incorporated herein by reference).
10.6+	Senior Executive Cash Incentive Bonus Plan (Filed as an Exhibit to the Registrant's quarterly report on Form 10-Q (001-37508), filed with the SEC on November 13, 2015, incorporated herein by reference).
10.7+	Form of Indemnification Agreement between the Registrant and each of its executive officers and directors (Filed as an Exhibit to the Registrant's registration statement on Form S-1 (333-205106), filed with the SEC on July 13, 2015, incorporated herein by reference).
10.8	Third Amended and Restated Subordinated Promissory Note, dated as of December 31, 2013, issued to Essex Capital Corporation, as amended (Filed as an Exhibit to the Registrant's registration statement on Form S-1 (333-205106), filed with the SEC on June 19, 2015, incorporated herein by reference).
10.9†	Loan and Security Agreement, by and between the Registrant, Hercules Technology III, L.P. and Hercules Technology Growth Capital, Inc., in its capacity as administrative agent for itself and Hercules Technology III, L.P. dated as of March 28, 2014, as amended (Filed as an Exhibit to the Registrant's registration statement on Form S-1 (333-205106), filed with the SEC on June 19, 2015, incorporated herein by reference).
10.10†	Settlement Agreement, by and between the Registrant and Shire LLC, dated as of July 23, 2014 (Filed as an Exhibit to the Registrant's registration statement on Form S-1 (333-205106), filed with the SEC on June 19, 2015, incorporated herein by reference).
10.11†	License Agreement, by and between the Registrant and Shire LLC, dated as of July 23, 2014 (Filed as an Exhibit to the Registrant's registration statement on Form S-1 (333-205106), filed with the SEC on June 19, 2015, incorporated herein by reference).
10.12	Commercial Lease Agreement, by and between Riverside Business Green, L.P., and Neos Therapeutics, LP, dated as of June 29, 1999, as amended (Filed as an Exhibit to the Registrant's registration statement on Form S-1 (333-205106), filed with the SEC on June 19, 2015, incorporated herein by reference).

Exhibit number	Description of exhibit
10.13†	Supply Agreement, by and between the Registrant and Coating Place, Inc., dated as of August 28, 2014 (Filed as an Exhibit to the Registrant's registration statement on Form S-1 (333-205106), filed with the SEC on June 26, 2015, incorporated herein by reference).
10.14†	Asset Purchase Agreement, by and between the Registrant and Cornerstone BioPharma, Inc., dated as of August 28, 2014 (Filed as an Exhibit to the Registrant's registration statement on Form S-1 (333-205106), filed with the SEC on June 19, 2015, incorporated herein by reference).
10.15+	Amended and Restated Employment Agreement, by and between the Registrant and Vipin Garg, dated as of July 10, 2015 (Filed as an Exhibit to the Registrant's registration statement on Form S-1 (333-205106), filed with the SEC on July 13, 2015, incorporated herein by reference).
10.16+	Amended and Restated Employment Agreement, by and between the Registrant and Richard Eisenstadt, dated as of July 10, 2015 (Filed as an Exhibit to the Registrant's registration statement on Form S-1 (333-205106), filed with the SEC on July 13, 2015, incorporated herein by reference).
10.17+	Amended and Restated Employment Agreement, by and between the Registrant and Thomas McDonnell, dated as of July 10, 2015 (Filed as an Exhibit to the Registrant's registration statement on Form S-1 (333-205106), filed with the SEC on July 13, 2015, incorporated herein by reference).
10.18†	License Agreement by and among the Registrant and Shire LLC, dated as of March 6, 2017. (Filed as an Exhibit to the Registrant's quarterly report on Form 10-Q (001-37508), filed with the SEC on May 10, 2017, incorporated herein by reference).
10.19	First Amendment to Facility Agreement, dated as of June 1, 2017, by and among Neos Therapeutics, Inc., Deerfield Private Design Fund III, L.P. and Deerfield Special Situation Fund, L.P. (including schedules and exhibits thereto). (Filed as an Exhibit to the Registrant's current report on Form 8-K, filed with the SEC on June 5, 2017, incorporated herein by reference).
10.20	Registration Rights Agreement, dated June 1, 2017, by and among Neos Therapeutics, Inc., Deerfield Private Design Fund III, L.P. and Deerfield Special Situation Fund, L.P. (Filed as an Exhibit to the Registrant's current report on Form 8-K, filed with the SEC on June 5, 2017, incorporated herein by reference).
10.21*†	Settlement Agreement, by and between the Registrant and Actavis Laboratoris FL, Inc., dated as of October 17, 2017.
21.1*	Subsidiaries of the Registrant.
23.1*	Consent of RSM US LLP.
24.1*	Power of Attorney (included on signature page).
31.1*	Certification of Principal Executive Officer pursuant to Rule 13a-14(a) or Rule 15d-14(a) of the Securities Exchange Act of 1934, as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
31.2*	Certification of Principal Financial Officer pursuant to Rule 13a-14(a) or Rule 15d-14(a) of the Securities Exchange Act of 1934, as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.

Exhibit number	Description of exhibit
32.1**	Certification of Principal Executive Officer and Principal Financial Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
101.INS*	XBRL Instance Document.
101.SCH*	XBRL Taxonomy Extension Schema Document.
101.CAL*	XBRL Taxonomy Extension Calculation Document.
101.DEF*	XBRL Taxonomy Extension Definition Linkbase Document.
101.LAB*	XBRL Taxonomy Extension Labels Linkbase Document.
101.PRE*	XBRL Taxonomy Extension Presentation Link Document.

\* Filed herewith.

\*\* The certifications furnished in Exhibit 32.1 hereto are deemed to accompany this Annual Report on Form 10-K and will not be deemed “filed” for purposes of Section 18 of the Securities Exchange Act of 1934, as amended. Such certifications will not be deemed to be incorporated by reference into any filings under the Securities Act of 1933, as amended, or the Securities Act of 1934, as amended, except to the extent that the Registrant specifically incorporates it by reference.

† Portions of this exhibit (indicated by asterisks) have been omitted pursuant to a request for confidential treatment and this exhibit has been submitted separately to the SEC.

+ Indicates a management contract or compensatory plan.

**ITEM 16. Form 10-K Summary**

None.

**Neos Therapeutics, Inc.**

**Index to Consolidated Financial Statements**

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## **Report of Independent Registered Public Accounting Firm**

To the Board of Directors and Stockholders  
Neos Therapeutics, Inc.

### **Opinion on the Financial Statements**

We have audited the accompanying consolidated balance sheets of Neos Therapeutics, Inc. and Subsidiaries (the “Company”) as of December 31, 2017 and 2016, and the related consolidated statements of operations, comprehensive loss, stockholders’ equity (deficit), and cash flows for each of the three years in the period ended December 31, 2017 and the related notes to the consolidated financial statements and schedule (collectively, the financial statements). In our opinion, the financial statements present fairly, in all material respects, the financial position of the Company as of December 31, 2017 and 2016, and the results of its operations and its cash flows for each of the three years in the period ended December 31, 2017, in conformity with accounting principles generally accepted in the United States of America.

### **Basis for Opinion**

These financial statements are the responsibility of the Company’s management. Our responsibility is to express an opinion on the Company’s financial statements based on our audits. We are a public accounting firm registered with the Public Company Accounting Oversight Board (United States) (PCAOB) and are required to be independent with respect to the Company in accordance with U.S. federal securities laws and the applicable rules and regulations of the Securities and Exchange Commission and the PCAOB.

We conducted our audits in accordance with the standards of the PCAOB. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement, whether due to error or fraud. The Company is not required to have, nor were we engaged to perform, an audit of its internal control over financial reporting. As part of our audits we are required to obtain an understanding of internal control over financial reporting but not for the purpose of expressing an opinion on the effectiveness of the Company’s internal control over financial reporting. Accordingly, we express no such opinion.

Our audits included performing procedures to assess the risks of material misstatement of the financial statements, whether due to error or fraud, and performing procedures that respond to those risks. Such procedures included examining, on a test basis, evidence regarding the amounts and disclosures in the financial statements. Our audits also included evaluating the accounting principles used and significant estimates made by management, as well as evaluating the overall presentation of the financial statements. We believe that our audits provide a reasonable basis for our opinion.

/s/ RSM US LLP

We have served as the Company’s auditor since 2010.

New York, New York  
March 16, 2018

**Neos Therapeutics, Inc. and Subsidiaries**  
**CONSOLIDATED BALANCE SHEETS**  
(In thousands, except share and per share data)

	December 31,	
	2017	2016
<b>ASSETS</b>		
Current Assets:		
Cash and cash equivalents . . . . .	\$ 31,969	\$ 24,352
Short-term investments . . . . .	18,448	15,430
Accounts receivable, net of allowances for chargebacks and cash discounts of \$1,154 and \$950, respectively . . . . .	13,671	6,135
Inventories . . . . .	13,459	5,767
Deferred contract sales organization fees . . . . .	—	720
Other current assets . . . . .	5,093	2,865
<b>Total current assets</b> . . . . .	<b>82,640</b>	<b>55,269</b>
Property and equipment, net . . . . .	8,203	7,076
Intangible assets, net . . . . .	16,348	17,647
Other assets . . . . .	162	150
<b>Total assets</b> . . . . .	<b>\$ 107,353</b>	<b>\$ 80,142</b>
<b>LIABILITIES AND STOCKHOLDERS' EQUITY (DEFICIT)</b>		
Current Liabilities:		
Accounts payable . . . . .	\$ 11,460	\$ 7,798
Accrued expenses . . . . .	10,570	5,264
Deferred revenue . . . . .	14,676	3,662
Current portion of long-term debt . . . . .	896	4,921
<b>Total current liabilities</b> . . . . .	<b>37,602</b>	<b>21,645</b>
Long-Term Liabilities:		
Long-term debt, net of current portion . . . . .	58,938	58,599
Derivative liability . . . . .	1,660	—
Deferred rent . . . . .	1,083	1,174
Other long-term liabilities . . . . .	180	272
<b>Total long-term liabilities</b> . . . . .	<b>61,861</b>	<b>60,045</b>
Stockholders' Equity (Deficit):		
Preferred stock, \$0.001 par value, 5,000,000 shares authorized, no shares issued or outstanding at December 31, 2017 and December 31, 2016 . . . . .	—	—
Common stock, \$0.001 par value, 100,000,000 authorized at December 31, 2017 and December 31, 2016; 29,030,757 and 28,996,956 issued and outstanding, respectively, at December 31, 2017; 16,079,902 and 16,060,996 issued and outstanding, respectively, at December 31, 2016 . . . . .	29	16
Treasury stock, at cost, 33,801 shares at December 31, 2017 and 18,906 shares at December 31, 2016 . . . . .	(352)	(232)
Additional paid-in capital . . . . .	274,584	198,787
Accumulated deficit . . . . .	(266,365)	(200,118)
Accumulated other comprehensive loss . . . . .	(6)	(1)
<b>Total stockholders' equity (deficit)</b> . . . . .	<b>7,890</b>	<b>(1,548)</b>
<b>Total liabilities and stockholders' equity (deficit)</b> . . . . .	<b>\$ 107,353</b>	<b>\$ 80,142</b>

See notes to consolidated financial statements.



**Neos Therapeutics, Inc. and Subsidiaries**  
**CONSOLIDATED STATEMENTS OF OPERATIONS**  
(In thousands, except share and per share data)

	Year Ended December 31,		
	2017	2016	2015
Revenues:			
Net product sales . . . . .	\$ 25,018	\$ 9,154	\$ 3,792
Cost of goods sold . . . . .	12,391	11,437	5,929
<b>Gross profit (loss)</b> . . . . .	<u>12,627</u>	<u>(2,283)</u>	<u>(2,137)</u>
Research and development expenses . . . . .	8,957	12,207	11,691
Selling and marketing expenses . . . . .	46,881	49,291	5,672
General and administrative expenses . . . . .	13,805	12,625	7,078
<b>Loss from operations</b> . . . . .	<u>(57,016)</u>	<u>(76,406)</u>	<u>(26,578)</u>
Interest expense . . . . .	(10,085)	(6,937)	(3,721)
Loss on debt extinguishment . . . . .	—	(1,187)	—
Other income (loss), net . . . . .	854	1,197	(482)
<b>Net loss</b> . . . . .	<u>\$ (66,247)</u>	<u>\$ (83,333)</u>	<u>\$ (30,781)</u>
Preferred stock accretion to redemption value . . . . .	—	—	(1,169)
Preferred stock dividends . . . . .	—	—	(1,221)
<b>Net loss attributable to common stock</b> . . . . .	<u>\$ (66,247)</u>	<u>\$ (83,333)</u>	<u>\$ (33,171)</u>
Weighted average common shares outstanding used to compute net loss per share, basic and diluted . . . . .	<u>24,751,091</u>	<u>16,052,390</u>	<u>7,581,881</u>
<b>Net loss per share of common stock, basic and diluted</b> . . . . .	<u>\$ (2.68)</u>	<u>\$ (5.19)</u>	<u>\$ (4.38)</u>

See notes to consolidated financial statements.

**Neos Therapeutics, Inc. and Subsidiaries**  
**CONSOLIDATED STATEMENTS OF COMPREHENSIVE LOSS**  
(In thousands)

	Year Ended December 31,		
	2017	2016	2015
<b>Net loss</b> .....	\$(66,247)	\$(83,333)	\$(30,781)
Other comprehensive loss:			
Net unrealized (loss) gain on short-term investments .....	(5)	2	—
Reclassification of gains included in net loss .....	—	(3)	—
<b>Total other comprehensive loss</b> .....	(5)	(1)	—
<b>Comprehensive loss</b> .....	\$(66,252)	\$(83,334)	\$(30,781)

See notes to consolidated financial statements.

**Neos Therapeutics, Inc. and Subsidiaries**  
**CONSOLIDATED STATEMENTS OF STOCKHOLDERS' EQUITY (DEFICIT)**  
(In thousands, except shares)

	Preferred Stock		Common Stock		Treasury Stock		Additional Paid-in Capital	Accumulated Deficit	Accumulated Other Comprehensive Loss	Total Stockholders' Equity (Deficit)
	Shares	Amount	Shares	Amount	Shares	Amount				
<b>Balance, December 31, 2014</b>	—	\$—	938,859	\$ 1	(55,905)	\$ —	\$ 4,831	\$ (83,614)	\$—	\$ (78,782)
Proceeds from exercise of options and warrants	—	—	325,292	—	—	—	75	—	—	75
Share-based compensation expense	—	—	—	—	—	—	1,181	—	—	1,181
Cancellation of treasury stock	—	—	(55,905)	—	55,905	—	—	—	—	—
Purchase of treasury stock	—	—	—	—	(9,197)	(171)	—	—	—	(171)
Series B Preferred Stock accretion to redemption value	—	—	—	—	—	—	—	(192)	—	(192)
Series B-1 Preferred Stock accretion to redemption value	—	—	—	—	—	—	—	(370)	—	(370)
Series B-1 accrued dividend	—	—	—	—	—	—	—	(1,221)	—	(1,221)
Series C Preferred Stock accretion to redemption value	—	—	—	—	—	—	—	(607)	—	(607)
Conversion of Redeemable Preferred Stock	—	—	9,217,983	9	—	—	110,767	—	—	110,776
Cashless exercise of Series C warrants issued with Series C financing	—	—	78,926	—	—	—	2,842	—	—	2,842
Reclassification of Series C warrants issued with senior debt	—	—	—	—	—	—	611	—	—	611
Net proceeds from issuance of common stock in IPO	—	—	5,520,000	6	—	—	75,007	—	—	75,013
Net loss	—	—	—	—	—	—	—	(30,781)	—	(30,781)
<b>Balance, December 31, 2015</b>	—	\$—	16,025,155	\$16	(9,197)	\$(171)	\$195,314	\$(116,785)	\$—	\$ 78,374
Proceeds from exercise of options and warrants	—	—	54,747	—	—	—	13	—	—	13
Share-based compensation expense	—	—	—	—	—	—	3,460	—	—	3,460
Purchase of treasury stock	—	—	—	—	(9,709)	(61)	—	—	—	(61)
Net unrealized loss on investments	—	—	—	—	—	—	—	—	(1)	(1)
Net loss	—	—	—	—	—	—	—	(83,333)	—	(83,333)
<b>Balance, December 31, 2016</b>	—	\$—	16,079,902	\$16	(18,906)	\$(232)	\$198,787	\$(200,118)	\$(1)	\$ (1,548)
Issuance of common stock, net of issuance costs	—	—	12,019,639	12	—	—	64,548	—	—	64,560
Issuance of common stock upon conversion of convertible notes	—	—	929,967	1	—	—	6,585	—	—	6,586
Shares issued from exercise of stock options	—	—	1,249	—	—	—	—	—	—	—
Purchase of treasury stock	—	—	—	—	(14,895)	(120)	—	—	—	(120)
Share-based compensation expense	—	—	—	—	—	—	4,051	—	—	4,051
Recognition of beneficial conversion feature on convertible notes	—	—	—	—	—	—	613	—	—	613
Net unrealized loss on investments	—	—	—	—	—	—	—	—	(5)	(5)
Net loss	—	—	—	—	—	—	—	(66,247)	—	(66,247)
<b>Balance, December 31, 2017</b>	—	\$—	29,030,757	\$29	(33,801)	\$(352)	\$274,584	\$(266,365)	\$(6)	\$ 7,890

See notes to consolidated financial statements.

**Neos Therapeutics, Inc. and Subsidiaries**  
**CONSOLIDATED STATEMENTS OF CASH FLOWS**  
(In thousands)

	Year Ended December 31,		
	2017	2016	2015
<b>Cash Flows From Operating Activities:</b>			
Net loss	\$(66,247)	\$(83,333)	\$(30,781)
Adjustments to reconcile net loss to net cash used in operating activities:			
Share-based compensation expense	4,051	3,460	1,181
Depreciation and amortization of property and equipment	1,363	1,598	1,724
Amortization of patents and other intangible assets	1,660	1,662	1,518
Changes in fair value of earnout, derivative and warrant liabilities	(509)	18	1,313
Amortization of senior debt discounts	1,316	406	576
Amortization of short-term investment purchase discounts	(126)	(156)	—
Deferred interest on debt	2,111	4,738	548
Loss on debt extinguishment	—	942	—
Gain on sale of equipment	(23)	(922)	(831)
Other adjustments	(91)	5	(23)
Changes in operating assets and liabilities:			
Accounts receivable	(7,536)	(2,232)	(3,536)
Inventories	(7,692)	(3,247)	(489)
Deferred contract sales organization fees	720	(123)	—
Other assets	(1,586)	(1,624)	(1,060)
Accounts payable	3,008	2,377	3,567
Accrued expenses	5,306	2,123	426
Deferred revenue	11,014	3,662	—
<b>Net cash used in operating activities</b>	<b>(53,261)</b>	<b>(70,646)</b>	<b>(25,867)</b>
<b>Cash Flows From Investing Activities:</b>			
Purchases of short-term investments	(48,015)	(66,088)	—
Sales and maturities of short-term investments	45,118	50,816	3,000
Proceeds from sale-leaseback of equipment	3,222	—	—
Capital expenditures	(2,497)	(3,550)	(1,023)
Intangible asset expenditures	(361)	(500)	—
<b>Net cash (used in) provided by investing activities</b>	<b>(2,533)</b>	<b>(19,322)</b>	<b>1,977</b>
<b>Cash Flows From Financing Activities:</b>			
Proceeds from Deerfield debt note, net of fees	—	58,419	—
Proceeds from senior debt note	—	—	10,000
Prepayment of senior debt and fee	—	(26,063)	—
Proceeds from sale of equipment	—	415	—
Proceeds from the issuance of common stock, net of issuance cost	64,560	13	18,122
Proceeds from initial public offering, net of issuance cost	—	—	75,013
Payments made on borrowings	(989)	(9,166)	(1,654)
Payments made to purchase treasury stock	(120)	(61)	(171)
Payments made on behalf of Deerfield	(40)	—	—
<b>Net cash provided by financing activities</b>	<b>63,411</b>	<b>23,557</b>	<b>101,310</b>
<b>Increase (decrease) in cash and cash equivalents</b>	<b>7,617</b>	<b>(66,411)</b>	<b>77,420</b>
<b>Cash and Cash Equivalents:</b>			
Beginning	24,352	90,763	13,343
Ending	<u>\$ 31,969</u>	<u>\$ 24,352</u>	<u>\$ 90,763</u>
<b>Supplemental Disclosure of Noncash Transactions:</b>			
Issuance of senior secured convertible notes in lieu of interest payment	\$ 6,586	\$ —	\$ —
Issuance of common stock upon conversion of senior secured convertible notes	\$ 6,586	\$ —	\$ —
Capital lease liability from sale-leaseback transactions	\$ 3,222	\$ —	\$ —
Derivative Liability incurred in connection with First Amendment to Facility	\$ 2,107	\$ —	\$ —
Prepaid assets included in accounts payable	\$ 654	\$ —	\$ —
Beneficial conversion feature incurred on convertible notes	\$ 613	\$ —	\$ —
Deferred contract sales organization fees	\$ —	\$ 597	\$ —
Issuance of stock warrants	\$ —	\$ —	\$ 2,131
Exercise of Series C warrants for Series C Preferred Stock	\$ —	\$ —	\$ 2,322
Cashless exercise of Series C warrants from Series C financing in IPO closing	\$ —	\$ —	\$ 2,842
Conversion of Redeemable Preferred Stocks into Common Stock	\$ —	\$ —	\$110,776
Reclassification of Series C warrants issued with senior debt upon IPO closing	\$ —	\$ —	\$ 611
Preferred stock accretion	\$ —	\$ —	\$ 1,169
Preferred stock dividend	\$ —	\$ —	\$ 1,221
<b>Supplemental Cash Flow Information:</b>			
Interest paid	<u>\$ 6,769</u>	<u>\$ 2,857</u>	<u>\$ 2,524</u>

See notes to consolidated financial statements.

**Neos Therapeutics, Inc. and Subsidiaries**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**Note 1. Organization and nature of operations**

Neos Therapeutics, Inc., a Delaware corporation, and its subsidiaries (the “Company”) is a fully integrated pharmaceutical company. The Company has developed a broad, proprietary modified-release drug delivery technology that enables the manufacture of single and multiple ingredient extended-release pharmaceuticals in patient- and caregiver-friendly orally disintegrating tablet and liquid suspension dosage forms. The Company has a pipeline of extended-release pharmaceuticals including three approved products for the treatment of attention deficit hyperactivity disorder (“ADHD”). Adzenys XR-ODT was approved by the US Food and Drug Administration (the “FDA”) on January 27, 2016 and launched commercially on May 16, 2016. The Company received approval from the FDA for Cotempla XR-ODT, its methylphenidate XR-ODT for the treatment of ADHD in patients 6 to 17 years old, on June 19, 2017, the Company initiated an early experience program with limited product availability on September 5, 2017 before launching this product nationwide on October 2, 2017. Also, the Company received approval from the FDA for Adzenys ER oral suspension (“Adzenys ER”) on September 15, 2017, and launched this product on February 26, 2018. In addition, the Company manufactures and markets a generic Tussionex (hydrocodone and chlorpheniramine) (“generic Tussionex”), extended-release liquid suspension for the treatment of cough and upper respiratory symptoms of a cold.

**Note 2. Summary of significant accounting policies**

*Basis of Presentation:* The consolidated financial statements are presented in accordance with accounting principles generally accepted in the United States of America (“GAAP”), and with the rules and regulations of the Securities and Exchange Commission (“SEC”).

*Principles of consolidation:* The consolidated financial statements include the accounts of the Company and its four wholly-owned subsidiaries. All significant intercompany transactions have been eliminated.

*Use of estimates:* The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect reported amounts and disclosures. Actual results could differ from those estimates.

*Concentration of credit risk:* Accounts receivable subjects the Company to concentrations of credit risk. Fourteen and thirteen customers accounted for all the revenue and deferred revenue in the year ended December 31, 2017 and 2016, respectively, and accounts receivable at December 31, 2017 and 2016 were due from fourteen and eleven customers, respectively. Three customers accounted for 93% of the net revenue for the year ended December 31, 2017 and two customers accounted for 82% of the net revenue for the year ended December 31, 2016, and three customers accounted for 94% and 98% of the accounts receivable at December 31, 2017 and 2016, respectively. Four customers accounted for substantially all revenue in the year ended December 31 2015.

*Segment information:* Operating segments are defined as components of an enterprise about which separate discrete information is available for evaluation by the chief operating decision maker, or decision-making group, in deciding how to allocate resources and in assessing performance. The Company views its operations and manages its business in one operating segment, which is the development, manufacturing and commercialization of pharmaceuticals.

**Neos Therapeutics, Inc. and Subsidiaries**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

**Note 2. Summary of significant accounting policies (Continued)**

*Reclassifications:* Certain reclassifications have been made to the prior year's consolidated financial statements to conform to the current period's presentation.

*Liquidity:* During 2017, 2016 and 2015, the Company produced operating losses and used cash to fund operations. Management intends to achieve profitability through revenue growth from pharmaceutical products developed with the Company's extended-release technologies. The Company does not anticipate it will be profitable until after the successful commercialization of its approved products, Adzenys XR-ODT, Cotempla XR-ODT and Adzenys ER. Accordingly, management has performed the review required for going concern accounting and believes the Company presently has sufficient liquidity to continue to operate for the next twelve months after the filing of this Report on Form 10-K.

*Cash equivalents:* The Company invests its available cash balances in bank deposits and money market funds. The Company considers highly liquid investments with original maturities of three months or less at the date of purchase to be cash equivalents. The Company maintains deposits in federally insured financial institutions in excess of federally insured limits. Management believes that the Company is not exposed to significant credit risk due to the financial position of the depository institutions in which those deposits are held. The Company's primary objectives for investment of available cash are the preservation of capital and the maintenance of liquidity.

*Short-term investments:* Short-term investments consist of debt securities that have original maturities greater than three months but less than or equal to one year and are classified as available-for-sale securities. Such securities are carried at estimated fair value, with any unrealized holding gains or losses reported as accumulated other comprehensive loss. Any tax effects are currently and have historically been insignificant. Realized gains and losses, and declines in value judged to be other-than-temporary, if any, are included in other income (expense) in the consolidated results of operations. A decline in the market value of any available-for-sale security below cost that is deemed to be other-than-temporary results in a reduction in fair value charged to earnings in that period, and a new cost basis for the security is established. Dividend and interest income are recognized in other income when earned. The cost of securities sold is calculated using the specific identification method. The Company places all investments with government agencies, or corporate institutions whose debt is rated as investment grade. The Company classifies all available-for-sale marketable securities with maturities greater than one year from the balance sheet date, if any, as non-current assets.

*Allowance for doubtful accounts:* The allowance for doubtful accounts is maintained at a level considered adequate to provide for losses that can be reasonably anticipated. Management determines the adequacy of the allowance based on reviews of individual accounts, historical losses, existing economic conditions and estimates based on management's judgments in specific matters. Accounts are written off as they are deemed uncollectible based on periodic review of the accounts. There is no allowance for doubtful accounts at December 31, 2017 or December 31, 2016, as management believes that all receivables are fully collectible.

*Inventories:* Inventories are stated at the lower of cost (first in, first out) or market in 2016 and, effective January 1, 2017, inventory is now required to be measured at the lower of cost (first in, first out) or net realizable value. The change to stating inventories at the lower of cost or net realizable value in 2017 was adopted prospectively and did not have a significant effect on the Company's ongoing financial reporting as valuing inventory at the lower of cost or net realizable value

**Neos Therapeutics, Inc. and Subsidiaries**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

**Note 2. Summary of significant accounting policies (Continued)**

approximated the prior policy of valuing inventory at the lower of cost or market. Inventories have been reduced by an allowance for excess and obsolete inventories. Cost elements include material, labor and manufacturing overhead. Inventories consist of raw materials, work in process, finished goods and deferred cost of goods sold. The cost of sales associated with the deferred product revenues are recorded as deferred costs of goods sold that are released from inventory into cost of goods sold as the deferred revenue is recognized into revenue.

Until objective and persuasive evidence exists that regulatory approval has been received and future economic benefit is probable, pre-launch inventories are expensed into research and development. Manufacturing costs for the production of Adzenys XR-ODT incurred after the January 27, 2016 FDA approval date are being capitalized into inventory, for the production of Cotempla XR-ODT incurred after June 30, 2017, following the FDA approval date of June 19, 2017, and for the production of Adzenys ER incurred after September 30, 2017, following the FDA approval date of September 15, 2017, are being capitalized into inventory.

*Property and equipment:* Property and equipment is recorded at cost less accumulated depreciation. Depreciation is computed using the straight-line method over the estimated useful lives of the assets, ranging from three to ten years. Leasehold improvements are amortized using the straight-line method over the shorter of the respective lease term or the estimated useful lives of the assets.

*Intangible assets:* Intangible assets subject to amortization, which principally include proprietary modified-release drug delivery technology, the costs to acquire the rights to Tussionex ANDA and patents, are recorded at cost and amortized over the estimated lives of the assets, which primarily range from 10 to 20 years. The Company estimates that the patents it has filed have a future beneficial value. Therefore, costs associated with filing for its patents are capitalized. Once the patent is approved and commercial revenue realized, the costs associated with the patent are amortized over the useful life of the patent. If the patent is not approved, the costs will be expensed.

*Impairment of long-lived assets:* Long-lived assets such as property and equipment and intangibles subject to amortization are evaluated for impairment whenever events or changes in circumstances indicate that the carrying value of an asset group may not be recoverable. Such assets are also evaluated for impairment in light of the Company's continuing losses. If the estimated future cash flows (undiscounted and without interest charges) from the use of an asset are less than the carrying value, a write-down would be recorded to reduce the related asset to its estimated fair value. No impairment charges were recorded for the years ended December 31, 2017, 2016 or 2015.

*Derivative liabilities:* The Company evaluates its debt and equity issuances to determine if those contracts or embedded components of those contracts qualify as derivatives requiring separate recognition in the Company's financial statements. The result of this accounting treatment is that the fair value of the embedded derivative is marked-to-market each balance sheet date and recorded as a liability and the change in fair value is recorded in other income (expense) in the consolidated results of operations. In circumstances where the embedded conversion option in a convertible instrument is required to be bifurcated and there are also other embedded derivative instruments in the convertible instrument that are required to be bifurcated, the bifurcated derivative instruments are accounted for as a single, compound derivative instrument. The classification of derivative instruments, including whether such instruments should be recorded as liabilities or as equity, is reassessed at the end of each

**Neos Therapeutics, Inc. and Subsidiaries**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

**Note 2. Summary of significant accounting policies (Continued)**

reporting period. Equity instruments that are initially classified as equity that become subject to reclassification are reclassified to liability at the fair value of the instrument on the reclassification date. Derivative instrument liabilities are classified in the balance sheet as current or non-current based on whether or not net-cash settlement of the derivative instrument is expected within twelve months of the balance sheet date.

When the Company has determined that the embedded conversion options should not be bifurcated from their host instruments, the Company records, when necessary, discounts to convertible notes for the intrinsic value of conversion options embedded in debt instruments based upon the differences between the fair value of the underlying common stock at the commitment date of the note transaction and the effective conversion price embedded in the note. Debt discounts under these arrangements are amortized over the term of the related debt to their stated date of redemption and are classified in interest expense in the consolidated results of operations.

*Revenue recognition:* Revenue is generated from product sales, recorded on a net sales basis. Product revenue is recognized when all of the following criteria are met: (1) persuasive evidence of an arrangement exists; (2) delivery has occurred or services have been rendered; (3) price to the buyer is fixed and determinable; and (4) collectability is reasonably assured. Revenue from sales transactions where the buyer has the right to return the product is recognized at the time of sale only if (1) the price to the buyer is substantially fixed or determinable at the date of sale, (2) the buyer has paid for the product, or the buyer is obligated to pay for the product and the obligation is not contingent on resale of the product, (3) the buyer's obligation to pay would not be changed in the event of theft or physical destruction or damage of the product, (4) the buyer acquiring the product for resale has economic substance apart from that provided by the Company, (5) the Company does not have significant obligations for future performance to directly bring about resale of the product by the buyer, and (6) the amount of future returns can be reasonably estimated.

The Company sells its commercial products to a limited number of pharmaceutical wholesalers, all subject to rights of return. Pharmaceutical wholesalers buy drug products directly from manufacturers. Title to the product passes upon delivery to the wholesalers, when the risks and rewards of ownership are assumed by the wholesaler (freight on board destination). These wholesalers then resell the product to retail customers such as food, drug and mass merchandisers.

The Company has a limited sales history for Adzenys XR-ODT and Cotempla XR-ODT, and no sales history for Adzenys ER, and has been unable to reliably estimate expected returns of the product at the time of shipment to wholesalers. Accordingly, the Company defers recognition of revenue on product shipments of Adzenys XR-ODT, Cotempla XR-ODT and Adzenys ER, respectively, until the right of return no longer exists, which occurs at the earlier of the time Adzenys XR-ODT, Cotempla XR-ODT and Adzenys ER units are dispensed through patient prescriptions or expiration of the right of return. The Company calculates and expects to calculate patient prescriptions dispensed of Adzenys XR-ODT, Cotempla XR-ODT and Adzenys ER, respectively, using an analysis of third-party information.



**Neos Therapeutics, Inc. and Subsidiaries**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

**Note 2. Summary of significant accounting policies (Continued)**

Revenues for Adzenys XR-ODT, Cotempla XR-ODT and generic Tussionex for the years ended December 31, 2017, 2016 and 2015, respectively, are as follows:

	Year Ended December 31,		
	2017	2016	2015
	(in thousands)		
Adzenys XR-ODT .....	\$18,959	\$2,924	\$ —
Cotempla XR-ODT .....	894	—	—
Generic Tussionex .....	5,165	6,230	3,792
	\$25,018	\$9,154	\$3,792

*Net branded product sales*

Net product sales for branded Adzenys XR-ODT and Cotempla XR-ODT products represent total gross product sales less gross to net sales adjustments. Gross to net sales adjustments include savings offers, prompt payment discounts, wholesaler fees and estimated rebates to be incurred on the selling price of the respective product sales. The Company recognizes branded total gross product sales less gross to net sales adjustments as revenue based on information from third-party providers.

*Savings offers*

The Company offers savings programs for Adzenys XR-ODT and Cotempla XR-ODT to patients covered under commercial payor plans in which the cost of a prescription to such patients is discounted. The Company records the amount of redeemed savings offers based on information from third-party providers and recognizes the discount as a reduction of revenue in the same period the related revenue is recognized.

*Prompt payment discounts*

Prompt payment discounts are based on standard programs with wholesalers and are recorded as a discount allowance against accounts receivable and as a deferred discount reduction of deferred revenue. The deferred discounts are subsequently recorded within net product sales when the deferred revenue is recognized into revenue based on units dispensed through patient prescriptions.

*Wholesale distribution fees*

Wholesale distribution fees are based on definitive contractual agreements for the management of the Company's products by wholesalers and are recorded as deferred wholesale distribution fees in other current assets. The deferred wholesale distribution fees are subsequently recorded as a reduction of net product sales when the deferred revenue is recognized into revenue based on units dispensed through patient prescriptions.

*Rebates*

The Company's products are subject to commercial managed care and government-managed Medicare and Medicaid programs whereby discounts and rebates are provided to participating managed care organizations and federal and/or state governments. Calculations related to these rebate accruals

**Neos Therapeutics, Inc. and Subsidiaries**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

**Note 2. Summary of significant accounting policies (Continued)**

are estimated based on information from third-party providers. Estimated rebates payable under such programs are recorded as a reduction of revenue at the time revenues are recorded. Historical trends of estimated rebates will be continually monitored and may result in future adjustments to such estimates.

*Net generic product sales*

Net product sales for generic Tussionex product represent total gross product sales less gross to net sales adjustments. Gross to net sales adjustments include prompt payment discounts, estimated allowances for product returns, wholesaler fees, estimated government rebates and estimated chargebacks to be incurred on the selling price of generic Tussionex related to the respective product sales. The Company recognizes generic Tussionex total gross product sales less gross to net sales adjustments as revenue based on shipments from 3PL's to the Company's wholesaler customers.

*Prompt payment discounts*

Prompt payment discounts are based on standard programs with wholesalers and are recorded as a discount allowance against accounts receivable and as a gross to net sales adjustments at the time revenue is recognized.

*Product returns*

Wholesalers' contractual return rights are limited to defective product, product that was shipped in error, product ordered by customer in error, product returned due to overstock, product returned due to dating or product returned due to recall or other changes in regulatory guidelines. The return policy for expired product allows the wholesaler to return such product starting six months prior to expiry date to twelve months post expiry date.

Estimated returns are recorded as accrued expenses and as a gross to net sales adjustments at the time revenue is recognized. During 2017, generic Tussionex product returns were estimated based upon return data available from sales of the Company's generic Tussionex product over the past three years. Prior to 2017, generic Tussionex product returns were estimated based upon data available from sales of the Company's generic Tussionex product provided by its former commercialization partner.

*Wholesale distribution fees*

Wholesale distribution fees are based on definitive contractual agreements for the management of the Company's product by wholesalers and are recorded as accrued expenses and as a gross to net sales adjustments at the time revenue is recognized.

*Rebates*

The Company's generic Tussionex product is subject to state government-managed Medicaid programs whereby discounts and rebates are provided to participating state governments. Estimated government rebates are recorded as accrued expenses and as a gross to net sales adjustments at the time revenue is recognized. During 2017, generic Tussionex government rebates were estimated based upon rebate payment data available from sales of the Company's generic Tussionex product over the past three years. Prior to 2017, Generic Tussionex government rebates were estimated based on

**Neos Therapeutics, Inc. and Subsidiaries**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

**Note 2. Summary of significant accounting policies (Continued)**

information from third-party providers. Historical trends of such rebates will be continually monitored and may result in future adjustments to such estimates.

*Wholesaler Chargebacks*

The Company's generic Tussionex products are subject to certain programs with wholesalers whereby pricing on products is discounted below wholesaler list price to participating entities. These entities purchase products through wholesalers at the discounted price, and the wholesalers charge the difference between their acquisition cost and the discounted price back to the Company. Estimated chargebacks are recorded as a discount allowance against accounts receivable and as a gross to net sales adjustments at the time revenue is recognized based on information provided by third parties.

Due to estimates and assumptions inherent in determining the amount of generic Tussionex returns, rebates and chargebacks, the actual amount of returns, claims for rebates and chargebacks may be different from the estimates, at which time reserves would be adjusted accordingly. Wholesale distribution fees and the allowance for prompt pay discounts are recorded at the time of shipment and such fees and allowances are recorded in the same period that the related revenue is recognized.

*Research and development costs:* Research and development costs are charged to operations when incurred and include salaries and benefits, facilities costs, overhead costs, raw materials, laboratory and clinical supplies, clinical trial costs, contract services, fees paid to regulatory authorities for review and approval of the Company's product candidates and other related costs. During the third quarter of 2016, the Company reclassified its approved product and facility regulatory fees out of research and development expense and into cost of sales commensurate with the commercial launch of Adzenys XR-ODT. The Company has reclassified all such applicable regulatory fees for prior quarters and prior years out of research and development expense and into cost of goods sold in accordance with this approach.

*Distribution expenses:* Costs invoiced to the Company by its third party logistics firm are classified as cost of goods sold in the consolidated statements of operations.

*Shipping and handling costs:* Amounts billed to customers for shipping and handling fees for the delivery of goods are classified as cost of goods sold in the consolidated statements of operations.

*Advertising costs:* Advertising costs are comprised of print and electronic media placements that are expensed as incurred. The Company recognized advertising costs of \$0.4 million and \$7.4 million during the years ended December 31, 2017 and 2016, respectively. There was no advertising costs incurred during the year ended December 31, 2015.

*Share-based compensation:* Share-based compensation awards, including grants of employee stock options, restricted stock, restricted stock units ("RSUs") and modifications to existing stock options, are recognized in the statement of operations based on their fair values. Compensation expense related to awards to employees is recognized on a straight-line basis, based on the grant date fair value, over the requisite service period of the award, which is generally the vesting term. The fair value of the Company's stock-based awards to employees and directors is estimated using the Black-Scholes option pricing model, which requires the input of subjective assumptions, including (1) the expected stock price volatility, (2) the expected term of the award, (3) the risk-free interest rate and (4) expected dividends.

**Neos Therapeutics, Inc. and Subsidiaries**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

**Note 2. Summary of significant accounting policies (Continued)**

Due to the previous lack of a public market for the trading of its common stock and a lack of company-specific historical and implied volatility data, the Company had, prior to the IPO, historically utilized third party valuation analyses to determine the fair value. After the closing of the Company's IPO, the Company's board of directors has determined the fair value of each share of underlying common stock based on the closing price of the Company's common stock as reported by the NASDAQ Global Market on the date of grant.

Under new guidance for accounting for share-based payments, the Company has elected to continue estimating forfeitures at the time of grant and, if necessary, revise the estimate in subsequent periods if actual forfeitures differ from those estimates. Ultimately, the actual expense recognized over the vesting period will only be for those options that vest. The adoption of this standard in 2017 did not have a material impact on the Company's business, financial position, results of operations or liquidity.

Beginning in July 2016, the Company began recording stock compensation expense in the same income statement line as the cash compensation of the employee with the option in accordance with Staff Accounting Bulletin ("SAB") Topic 14 due to the increased number and amount of options and option compensation. The Company has reclassified all prior quarters' amounts out of general and administrative expense to the appropriate income statement line in accordance with this approach.

*Paragraph IV Litigation Costs:* Legal costs incurred by the Company in the enforcement of the Company's intellectual property rights are charged to expense as incurred.

*Income taxes:* Income taxes are accounted for using the liability method, under which deferred taxes are determined based on differences between the financial reporting and tax basis of assets and liabilities and are measured using the enacted tax laws that will be in effect when the differences are expected to reverse.

Management evaluates the Company's tax positions in accordance with guidance on accounting for uncertainty in income taxes. Using that guidance, tax positions initially need to be recognized in the financial statements when it is more likely than not that the position will be sustained upon examination. As of December 31, 2017 and 2016, the Company has unrecognized tax benefits associated with uncertain tax positions in the consolidated financial statements. These uncertain tax positions were netted against net operating losses (NOL's) with no separate reserve for uncertain tax positions required.

Deferred tax assets should be reduced by a valuation allowance if current evidence indicates that it is considered more likely than not that these benefits will not be realized. In evaluating the objective evidence that historical results provide, the Company considered that three years of cumulative operating losses was significant negative evidence outweighing projections for future taxable income. Therefore, at December 31, 2017 and 2016, the Company has determined that it is more likely than not that the deferred tax assets will not be realized. Accordingly, the Company has recorded a valuation allowance to reduce deferred tax assets to zero. The Company may not ever be able to realize the benefit of some or all of the federal and state loss carryforwards, either due to ongoing operating losses or due to ownership changes, which limit the usefulness of the loss carryforwards.

*Warrants:* The Company accounts for its warrants and other derivative financial instruments as either equity or liabilities based upon the characteristics and provisions of each instrument. Warrants

**Neos Therapeutics, Inc. and Subsidiaries**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

**Note 2. Summary of significant accounting policies (Continued)**

classified as derivative liabilities are recorded on the Company's balance sheet at their fair value on the date of issuance and prior to completion of the Company's IPO were revalued at each subsequent balance sheet date, with fair value changes recognized as increases or reductions to other income (expense) in the statements of operations. The Company estimates the fair value of its derivative liabilities using third party valuation analysis that utilizes option pricing models and assumptions that are based on the individual characteristics of the warrants or instruments on the valuation date, as well as assumptions for expected volatility, expected life, yield, and risk-free interest rate. Prior to the closing of the IPO, the Company's Series C warrants were determined to be derivative liabilities and they were revalued at each subsequent balance sheet date. Upon closing the IPO, the warrants issued in conjunction with the Series C financing were exchanged in a cashless exercise for 947,185 shares of Series C which converted into 78,926 shares of the Company's common stock. The remaining Series C warrants issued with the senior debt to purchase 170,000 pre-split shares of Series C ("Hercules Warrants") were converted into warrants to purchase 70,833 shares of the Company's common stock and the warrant liability was reclassified to Additional Paid in Capital within Stockholders' Equity (Deficit).

*Recent accounting pronouncements:* In May 2017, the Financial Accounting Standards Board (the "FASB") issued Accounting Standards Update ("ASU") No. 2017-09, *Compensation—Stock Compensation (Topic 718): Scope of Modification Accounting*. This ASU clarifies when to account for a change to the terms or conditions of a share-based payment award as a modification. Under the new guidance, modification accounting is required only if the fair value, the vesting conditions, or the classification of the award changes as a result of the modification. The guidance is effective for annual periods beginning after December 15, 2017, including interim periods within those periods. This standard became effective for the Company on January 1, 2018. The adoption of this standard is not expected to have a material impact on the Company's consolidated results of operations or financial position.

In August 2016, the FASB issued ASU No. 2016-15, *Statement of Cash Flows (Topic 230): Classification of Certain Cash Receipts and Cash Payments*. This ASU was designed to reduce the diversity in practice of how the eight specified items are presented and classified in the statement of cash flows, including debt prepayment or debt extinguishment costs. The amendments are effective for public companies for fiscal years beginning after December 15, 2017, including interim periods within those years. The Company believes the amendments will not have a significant effect on its ongoing financial reporting as the Company has classified its debt prepayment and debt extinguishment costs in the Consolidated Statements of Cash Flows in accordance with the amendments.

In March 2016, the FASB issued ASU No. 2016-09, *Compensation—Stock Compensation—Improvements to Employee Share-Based Payment Accounting (Topic 718)*. For public companies, areas of accounting for share-based payment that this ASU was designed to simplify include: the income tax consequences, the accounting policy for forfeitures, the classification of awards as either equity or liabilities and the classification on the statement of cash flows. The amendments in this ASU are effective for public companies for fiscal years beginning after December 15, 2016, including interim periods within those years. The adoption of this standard does not have a material impact on the Company's business, financial position, results of operations or liquidity.

In February 2016, the FASB issued ASU No. 2016-02, *Leases (Topic 842)*. Under the new guidance, lessees will be required to recognize the following for all leases (with the exception of short-term

**Neos Therapeutics, Inc. and Subsidiaries**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

**Note 2. Summary of significant accounting policies (Continued)**

leases) at the commencement date: 1) a lease liability, which is a lessee's obligation to make lease payments arising from a lease, measured on a discounted basis; and 2) a right-of-use asset, which is an asset that represents the lessee's right to use, or control the use of, a specified asset for the lease term. The new lease guidance simplified the accounting for sale and leaseback transactions primarily because lessees must recognize lease assets and lease liabilities. The amendments in this ASU are effective for fiscal years beginning after December 15, 2018, including interim periods within those years. The new standard must be adopted using a modified retrospective transition and requires application of the new guidance at the beginning of the earliest comparative period presented. The Company is evaluating the effect that the standard will have on its consolidated financial statements and related disclosures and has not determined the expected impact at this time.

In May 2014, the FASB issued ASU No. 2014-09, *Revenue from Contracts with Customers (Topic 606)* (the "New Revenue Standard"). The New Revenue Standard replaces transaction-and industry-specific revenue recognition guidance under current U.S. GAAP with a principles-based approach for determining revenue recognition. The New Revenue Standard requires an entity to recognize the amount of revenue based on the value of transferred goods or services to customers. There is also additional disclosure about the nature, amount, timing and uncertainty of revenue and cash flows arising from contracts with customer. The New Revenue Standard became effective for the Company on January 1, 2018.

The New Revenue Standard permits the use of either a fully retrospective or cumulative effect transition method. For purposes of providing comparable periods upon adoption, the Company will apply the fully retrospective transition method. The impact of the New Revenue Standard relates to the Company's accounting for branded net product sales. There are no changes to the net product sales of generic Tussionex revenue since we have estimated product returns since inception of recognizing revenue in August 2014.

As a result, the Company will revise its results for branded net product sales revenue which commenced in May 2016 with the launch of Adzenys XR-ODT for the years ended December 31, 2016 and 2017 and applicable interim periods within those years, as if the New Revenue Standard had been effective for those periods. No revisions are required for the year ended December 31, 2015 with the adoption of the New Revenue Standard.

In preparation for adoption of the New Revenue Standard, we have implemented internal controls and key system functionality to enable the preparation of financial information and have reached conclusions on key accounting assessments related to the New Revenue Standard, including management's assessment that the impact of accounting for costs incurred to obtain a contract is immaterial.

Under current GAAP, revenue recognition of branded net product sales is deferred until the transaction price is fixed or determinable. The Company has a limited sales history for branded products Adzenys XR-ODT and Cotempla XR-ODT and no sales history for Adzenys ER. Under ASC 605 it was determined that management cannot reliably estimate historical returns of the product at the time of delivery to wholesalers, when title to the asset transfers and the customer is invoiced. Accordingly, the Company defers recognition of revenue on branded product shipments of Adzenys XR-ODT and Cotempla XR-ODT, respectively, until the right of return no longer exists, which occurs at the earlier of the time Adzenys XR-ODT and Cotempla XR-ODT units are dispensed through

**Neos Therapeutics, Inc. and Subsidiaries**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

**Note 2. Summary of significant accounting policies (Continued)**

patient prescriptions or expiration of the right of return. The Company calculates patient prescriptions dispensed of Adzenys XR-ODT and Cotempla XR-ODT using an analysis of third-party information.

Under the New Revenue Standard, an entity recognizes revenue when its customer obtains control of promised goods or services, in an amount that reflects the consideration which the entity expects to receive in exchange for those good or services. Therefore, the Company will be required to make estimates of the net sales price, including estimates of variable consideration (e.g., savings offers, prompt payment discounts, product returns, wholesaler fees and estimated rebates) to be incurred on the selling price of the respective branded product sales, and recognize the estimated amount as revenue, when it transfers control of the product to its customers (e.g., upon shipment or delivery). Variable consideration must be determined using either an expected value or most likely amount method. The estimate of variable consideration is also subject to a constraint such that some or all of the estimated amount of variable consideration will only be included in the transaction price to the extent that it is probable that a significant reversal of revenue (in the context of the contract) will not occur when the uncertainty associated with the variable consideration is subsequently resolved. Estimating variable consideration and the related constraint will require the use of significant management judgment and other market data. To implement the New Revenue Standard, the Company analyzed recent branded product return history and other market data obtained from its 3PLs to determine a reliable return rate. Additionally, management analyzed historical savings offers, prompt payment discounts, wholesaler fees and rebates payments based on patient prescriptions dispensed of Adzenys XR-ODT, Cotempla XR-ODT and information obtained from third-party providers to determine these respective variable considerations. Management has concluded that estimates of the above variable considerations are reasonably constrained, and estimates can be used for recognizing branded total gross product sales less gross to net sales adjustments as revenue beginning January 1, 2018.

Adoption of the New Revenue Standard will result in the recognition of additional net branded product sales revenue of \$2.1 million and \$0.9 million for years ended December 31, 2017 and 2016, respectively partially offset by associated increased cost of goods sold of \$1.6 million and \$0.3 million, respectively. As a result, the net loss reported will be reduced by \$0.5 million and \$0.6 million reflecting the gross profit from the accelerated revenue and associated cost of goods sold for years ended December 31, 2017 and 2016, respectively. The net loss per share of common stock, basic and diluted reported will be improved by \$0.02 and \$0.03 per share for December 31, 2017 and 2016, respectively. The adoption of the New Revenue Standard will reduce the net operating loss carry forward for 2017 and 2016, respectively; however, there is no impact to the provision for income taxes because the Company's deferred tax asset benefits are fully reserved for December 31, 2017 and 2016, respectively. In addition, adoption of the New Revenue Standard will result in a decrease in reported total current assets by \$3.2 million and \$0.6 million as of December 31, 2017 and 2016, respectively, due to the elimination of deferred cost of goods sold and wholesaler fees. Reported total current liabilities will decrease by \$4.3 million and \$1.2 million as of December 31, 2017 and 2016, respectively, due to the elimination of deferred revenue partially offset by increases in accrued expenses for contract obligations related to savings offers, product returns and rebates. See Expected Impacts to Reported Results below for the impact of adoption of the New Revenue Standard on the Company's consolidated financial statements.

**Neos Therapeutics, Inc. and Subsidiaries**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

**Note 2. Summary of significant accounting policies (Continued)**

**Expected impacts to reported results**

Adoption of the new revenue standard is expected to impact the Company's reported results as follows:

	Year Ended December, 31					
	2017			2016		
	As Reported	New Revenue Standard Adjustment	As Adjusted	As Reported	New Revenue Standard Adjustment	As Adjusted
(In thousands, except per share data)						
<b>Condensed consolidated statements of operations:</b>						
Revenue: net product sales . . . . .	\$ 25,018	\$2,114	\$ 27,132	\$ 9,154	\$ 879	\$ 10,033
Cost of goods sold . . . . .	12,391	1,639	14,030	11,437	297	11,734
Gross profit (loss) . . . . .	12,627	475	13,102	(2,283)	582	(1,701)
Net loss attributable to common stock . . . .	(66,247)	475	(65,772)	(83,333)	582	(82,751)
Net loss per share of common stock, basic and diluted . . . . .	(2.68)	0.02	(2.66)	(5.19)	0.03	(5.16)

	December 31,					
	2017			2016		
	As Reported	New Revenue Standard Adjustment	As Adjusted	As Reported	New Revenue Standard Adjustment	As Adjusted
(In thousands)						
<b>Condensed consolidated statements of balance sheet:</b>						
Inventories . . . . .	\$ 13,459	\$ (1,727)	\$ 11,732	\$ 5,767	\$ (225)	\$ 5,542
Other current assets . . . . .	5,093	(1,518)	3,575	2,865	(346)	2,519
Total current assets . . . . .	82,640	(3,245)	79,395	55,269	(571)	54,698
Accrued expenses . . . . .	10,570	10,374	20,944	5,264	2,509	7,773
Deferred revenue . . . . .	14,676	(14,676)	—	3,662	(3,662)	—
Total current liabilities . . . . .	37,602	(4,302)	33,300	21,645	(1,153)	20,492
Accumulated deficit . . . . .	(266,365)	1,057	(265,308)	(200,118)	582	(199,536)
Total liabilities and stockholder's equity	107,353	(3,245)	104,108	80,142	(571)	79,571

Adoption of the New Revenue Standard had no impact to cash from or used in operating, financing, or investing on the Company's consolidated statements of cash flows.

**Note 3. Net loss per share**

Basic net loss per share is calculated by dividing the net loss by the weighted average number of common shares outstanding during the period. Diluted net loss per share is computed by dividing the net loss by the weighted average number of common shares and common share equivalents outstanding for the period. Common stock equivalents are only included when their effect is dilutive. Potentially dilutive securities, which include warrants, outstanding stock options under the stock option plan and shares issuable in future periods, such as RSU awards, have been excluded from the computation of diluted net loss per share as they would be anti-dilutive. For all periods presented, there is no difference in the number of shares used to compute basic and diluted shares outstanding due to the Company's net loss position. Restricted stock is considered legally issued and outstanding on the grant



**Neos Therapeutics, Inc. and Subsidiaries**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

**Note 3. Net loss per share (Continued)**

date, while RSUs are not considered legally issued and outstanding until the RSUs vest. Once the RSUs are vested, equivalent common shares will be issued or issuable to the grantee and therefore the RSUs are not considered for inclusion in total common shares issued and outstanding until vested.

The following potentially dilutive securities outstanding were excluded from consideration in the computation of diluted net loss per share of common stock for the years ended December 31, 2017, 2016 and 2015, respectively, because including them would have been anti-dilutive:

	December 31,		
	2017	2016	2015
Series C Redeemable Convertible Preferred Stock			
Warrants (as converted) . . . . .	70,833	70,833	70,833
Common Stock Warrants . . . . .	—	—	50,158
Stock options outstanding . . . . .	2,454,973	2,107,344	1,352,283
RSU's granted, not issued or outstanding . . . . .	85,000	—	—

**Note 4. Fair value of financial instruments**

The Company records financial assets and liabilities at fair value. The carrying amounts of certain financial assets and liabilities including cash and cash equivalents, accounts receivable, other current assets, accounts payable, accrued liabilities and deferred revenue, approximated their fair value due to their short maturities. The remaining financial instruments were reported on the Company's consolidated balance sheets at amounts that approximate current fair values based on market based assumptions and inputs.

As a basis for categorizing inputs, the Company uses a three tier fair value hierarchy, which prioritizes the inputs used to measure fair value from market based assumptions to entity specific assumptions as follows:

- Level 1:* Unadjusted quoted prices for identical assets in an active market.
- Level 2:* Quoted prices in markets that are not active or inputs that are observable either directly or indirectly for substantially the full-term of the asset.
- Level 3:* Prices or valuation techniques that require inputs that are both unobservable and significant to the overall fair value measurement. They reflect management's own assumptions about the assumptions a market participant would use in pricing the asset.

The following table presents the hierarchy for the Company's financial instruments measured at fair value on a recurring basis for the indicated dates:

	Fair Value as of December 31, 2017			
	Level 1	Level 2	Level 3	Total
	(in thousands)			
Cash and cash equivalents . . . . .	\$31,969	\$ —	\$ —	\$31,969
Short-term investments . . . . .	—	18,448	—	18,448
Earnout liability . . . . .	—	—	170	170
Derivative liability (see Note 11) . . . . .	—	—	1,660	1,660
	\$31,969	\$18,448	\$1,830	\$52,247

**Neos Therapeutics, Inc. and Subsidiaries**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

**Note 4. Fair value of financial instruments (Continued)**

	Fair Value as of December 31, 2016			
	Level 1	Level 2	Level 3	Total
	(in thousands)			
Cash and cash equivalents . . . . .	\$17,917	\$ 6,435	\$ —	\$24,352
Short-term investments . . . . .	—	15,430	—	15,430
Earnout liability . . . . .	—	—	232	232
	\$17,917	\$21,865	\$232	\$40,014

The Company's Level 1 assets included bank deposits, certificates of deposit and actively traded money market funds with a maturity of 90 days or less at December 31, 2017 and 2016. Asset values were considered to approximate fair value due to their short-term nature.

The Company's Level 2 assets included commercial paper and corporate bonds with maturities of less than one year that are not actively traded which were classified as available for sale securities. The estimated fair values of these securities were determined by third parties using valuation techniques that incorporate standard observable inputs and assumptions such as quoted prices for similar assets, benchmark yields, reported trades, broker/dealer quotes, issuer spreads, benchmark securities, bids/offers and other pertinent reference data.

The Company's cash and cash equivalents and short-term investments had quoted prices at December 31, 2017 and 2016 as shown below:

	December 31, 2017		
	Amortized Cost	Unrealized Loss	Market Value
	(in thousands)		
Bank deposits and money market funds . . . . .	\$31,969	\$—	\$31,969
Financial and corporate debt securities . . . . .	18,454	(6)	18,448
	\$50,423	\$(6)	\$50,417

	December 31, 2016		
	Amortized Cost	Unrealized Loss	Market Value
	(in thousands)		
Bank deposits and money market funds . . . . .	\$17,917	\$—	\$17,917
Financial and corporate debt securities . . . . .	21,866	(1)	21,865
	\$39,783	\$(1)	\$39,782

The Company's Level 3 liability included the fair value of the earnout liability at December 31, 2017 and 2016 and the fair value of the Deerfield derivative liability at December 31, 2017.

The fair value of the earnout liability was determined after taking into consideration valuations using the Monte Carlo method based on assumptions at December 31, 2016 and revised at December 31, 2017. These revisions were primarily due to an updated revenue forecast for the Company's generic Tussionex and the use of a directly-calculated revenue volatility of 42% based on data for potential comparable publicly-traded companies in the generic drug manufacturing space including the Company, whereas previously an unlevered equity volatility of 50% had been selected.

**Neos Therapeutics, Inc. and Subsidiaries**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

**Note 4. Fair value of financial instruments (Continued)**

Significant changes to these assumptions would result in increases/decreases to the fair value of the earnout liability. The methodologies and significant inputs used in the determination of the fair value of the earnout liability were as follows:

	<u>Initial Valuation Earnout Liability</u>	<u>December 31, 2015 Earnout Liability</u>	<u>December 31, 2016 Earnout Liability</u>	<u>December 31, 2017 Earnout Liability</u>
<b>Date of Valuation</b> . . . . .	<b>8/28/2014</b>	<b>12/31/2015</b>	<b>12/31/2016</b>	<b>12/31/2017</b>
<b>Valuation Method</b> . . . . .	Monte Carlo	Monte Carlo	Monte Carlo	Monte Carlo
<b>Volatility (annual)</b> . . . . .	50%	50%	50%	42%
<b>Risk-free rate (annual)</b> . . . . .	.03% - 3.56%	.56% - 3.31%	.74% - 3.42%	1.62% - 2.88%
<b>Time period from valuation until end of earnout</b> . . . . .	.1708 - 9.8417	.5 - 9.5	.5 - 9.5	.5 - 9.5
<b>Earnout Target 1 (thousands)</b> . . . . .	\$13,700	\$13,700	\$13,700	\$13,700
<b>Earnout Target 2 (thousands)</b> . . . . .	\$18,200	\$18,200	\$18,200	\$18,200
<b>Discount rate</b> . . . . .	8.03% - 10.51%	8.11% - 10.86%	12.02% - 14.70%	14.72% - 15.98%
<b>Fair value of liability at valuation date (thousands)</b>	<u>\$589</u>	<u>\$214</u>	<u>\$232</u>	<u>\$170</u>

The fair value of the derivative liability was determined after taking into consideration valuations using the Monte Carlo method based on assumptions at June 1, 2017 and December 31, 2017. The methodologies and significant inputs used in the determination of the fair value of the debt derivative liability were as follows:

	<u>Derivative Liability</u>	<u>Initial Valuation Derivative Liability</u>
Date of Valuation . . . . .	12/31/2017	6/1/2017
Valuation Method . . . . .	Monte Carlo	Monte Carlo
Volatility (annual) . . . . .	N/A	76.4%
Time period from valuation until maturity of debt (yrs.) . . . . .	4.360	4.943
Cumulative probability of a change in control prepayment implied by model . . . . .	27%	28%
Cumulative probability of other accelerated prepayments implied by model . . . . .	17%	17%
Discount rate . . . . .	16.20%	15.87%
<b>Fair value of liability at valuation date (thousands)</b> . . . . .	<u>\$1,660</u>	<u>\$2,107</u>

Significant changes to these assumptions in the preceding valuation tables would result in increases/decreases to the fair value of the earnout liability and derivative liability.

**Neos Therapeutics, Inc. and Subsidiaries**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

**Note 4. Fair value of financial instruments (Continued)**

Changes in Level 3 liabilities measured at fair value for the periods indicated were as follows:

	<u>Level 3 Liabilities</u> (in thousands)
Balance at December 31, 2015 . . . . .	\$ 214
Change in fair value . . . . .	18
Balance at December 31, 2016 . . . . .	232
Addition of Deerfield derivative liability . . . . .	2,107
Change in fair value . . . . .	(509)
Balance at December 31, 2017 . . . . .	<u>\$1,830</u>

**Note 5. Inventories**

Inventories at the indicated dates consist of the following:

	<u>December 31,</u>	
	<u>2017</u>	<u>2016</u>
	(in thousands)	
Raw materials . . . . .	\$ 3,476	\$1,672
Work in progress . . . . .	6,156	2,546
Finished goods . . . . .	2,470	2,060
Deferred cost of goods sold . . . . .	1,726	225
Inventory at cost . . . . .	13,828	6,503
Inventory reserve . . . . .	(369)	(736)
	<u>\$13,459</u>	<u>\$5,767</u>

The deferred cost of goods sold relates to the cost of shipments of Adzenys XR-ODT and Cotempla XR-ODT to distributors where the related revenue has been deferred. Such amounts are charged to cost of goods sold when the associated revenue is recognized.

**Note 6. Property and equipment**

Property and equipment, net at the indicated dates consists of the following:

	<u>December 31,</u>	
	<u>2017</u>	<u>2016</u>
	(in thousands)	
Assets under capital lease . . . . .	\$ 3,222	\$ 1,793
Leasehold improvements . . . . .	4,195	3,757
Manufacturing, packaging and lab equipment . . . . .	5,300	4,376
Office furniture and equipment . . . . .	1,656	1,788
Assets under construction . . . . .	1,056	2,066
	<u>15,429</u>	<u>13,780</u>
Accumulated depreciation and amortization (including \$157 and \$762 at December 31, 2017 and 2016, respectively, applicable to capital leases) . . . . .	<u>(7,226)</u>	<u>(6,704)</u>
	<u>\$ 8,203</u>	<u>\$ 7,076</u>

**Neos Therapeutics, Inc. and Subsidiaries**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

**Note 6. Property and equipment (Continued)**

Depreciation and amortization expense related to property and equipment was \$1,363,000, \$1,598,000 and \$1,724,000 for the years ended December 31, 2017, 2016 and 2015, respectively. Depreciation and amortization expense is recorded in cost of goods sold, research and development, or general and administrative expenses in the accompanying consolidated statements of operations. As noted in Note 7, the Company sold and leased back a substantial portion of its operating assets in a series of capital lease transactions.

On October 20, 2016, the Company utilized a third party auctioneer to conduct an auction of certain fully-depreciated equipment assets, resulting in net proceeds of approximately \$415,000 which were paid during the fourth quarter of 2016 and were recorded as a gain on sale and included in other income (loss) in the Company's consolidated statement of operations.

**Note 7. Sale-leaseback transaction**

The Company accounts for the sale and leaseback transactions discussed below as capital leases under the provisions of Accounting Standards Codification ("ASC") Topic 840-40, *Leases—Sale Leaseback Transactions*. Accordingly, the leased assets are recorded in property and equipment and the capitalized lease obligations are included in long-term liabilities at the present value of the future lease payments in accordance with the terms of the lease (see Note 11). Lease payments are applied using the effective interest rate inherent in the leases. Depreciation of the property and equipment is included within depreciation and amortization in the consolidated statements of operations and consolidated statements of cash flows.

In 2012, the Company negotiated financing arrangements with a related party which provided for the sale-leaseback of up to \$6.5 million of the Company's property and equipment with a bargain purchase option at the end of the respective lease. These financing arrangements were executed in five separate tranches that occurred in February, July and November 2013, and March 2014. In the aggregate, the Company sold groups of assets for \$795,000 and \$5.5 million, which resulted in a net gains of approximately \$116,000 and \$2.7 million, in the years ended December 31, 2014 and 2013, respectively, and executed capital leases for these assets with repurchase options at the end of each respective lease term. Gains on the transactions are recognized on a straight-line basis over each respective 42-month lease term. The two February 2013 and the November 2013 leases for a total of \$3.5 million and \$1.0 million of assets expired in July 2016 and April 2017, respectively, and the related \$2.6 million and \$161,000 gains, respectively, were fully amortized at that time and the \$385,000 and \$100,000 lease buy-out option liabilities, respectively, were fully satisfied. The July 2013 lease for a total of \$1.0 million of assets expired in December 2016 and the related \$0.1 million loss had been recorded at inception of the lease and the \$100,000 lease buy-out option liability was fully satisfied. The March 2014 lease for \$795,000 of asset expired in September 2017 and the related \$116,000 gain was fully amortized at that time and the lease buy-out option liability of \$79,000 was fully satisfied.

In February 2017, the Company entered into an agreement with a related party for the sale-leaseback of newly acquired assets of up to \$5.0 million to finance its capital expenditures. Each lease under this master agreement will be for an initial term of 36 months and will have an option to purchase the equipment at the end of the respective lease that management considers to be a bargain purchase option. Under this agreement, the Company entered into leases and sold assets with a total capitalized cost of \$481,000 and \$2,742,000 at effective interest rates of 14.3% and 14.9% on February 13, 2017 and June 30, 2017, respectively. The February sale resulted in net gains of \$14,000

**Neos Therapeutics, Inc. and Subsidiaries**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

**Note 7. Sale-leaseback transaction (Continued)**

which has been deferred and is being amortized over the 36-month term of the lease. There was no gain or loss on the June 2017 sale.

For the years ended December 31, 2017, 2016 and 2015, approximately \$44,000, \$507,000 and \$831,000, respectively, of the net gain on sale-leasebacks was recognized in other income on the condensed consolidated statements of operations.

**Note 8. Intangible assets**

Intangible assets, net at the indicated dates consist of the following:

	December 31,	
	2017	2016
	(in thousands)	
Proprietary modified-release drug delivery technology . . . . .	\$15,600	\$15,600
Tussionex ANDA . . . . .	4,829	4,829
CPI profit sharing . . . . .	2,043	2,043
Patents . . . . .	2,302	2,191
Other . . . . .	1,035	785
	25,809	25,448
Accumulated amortization . . . . .	(9,461)	(7,801)
	\$16,348	\$17,647

As part of the June 15, 2009 reorganization of the Company as Neos Therapeutics, Inc., the Company performed a purchase price allocation analysis. The proprietary modified-release drug delivery technology was valued at \$15.6 million based on projected cash flows expected to be generated from this technology. The \$15.6 million is being amortized over 20 years. Amortization expense of \$780,000 was recorded in each of the years ended December 31, 2017, 2016 and 2015.

On August 28, 2014, the Company completed an acquisition of the rights to Tussionex ANDA from Cornerstone and CPI which was accounted for as an asset acquisition. Prior to the acquisition, the Company, Cornerstone and Coating Place, Inc. (“CPI”) shared profits generated by the sale and manufacture of the product under a development and manufacturing agreement, and Cornerstone had commercialization rights to the product. The Company paid \$4.2 million to Cornerstone to buy out their rights to commercialize and derive future profits from the product and entered into an agreement whereby Cornerstone transferred certain assets associated with the product to the Company. Legal fees of \$90,000 associated with this buyout agreement have been capitalized as part of the purchase price. Additional estimated earnout costs due to Cornerstone of \$589,000, recorded at fair value by the Company based upon a valuation provided by a third party valuation firm, were capitalized as part of the purchase price of this intangible asset. This earnout amount was revalued at December 31, 2017, 2016 and 2015, resulting in a \$62,000 decrease, an \$18,000 increase and a \$542,000 decrease in the estimated fair value of the earnout, respectively, which is recorded in other income (expense), net in the Company’s consolidated statements of operations. The 2015 net decrease resulted primarily from new information regarding the projected impact of the DEA’s reclassification of Tussionex from a Schedule III controlled substance to a Schedule II controlled substance. In addition, the Company paid \$2.0 million to CPI to buy out their rights to future profits from the collaboration and entered into an

**Neos Therapeutics, Inc. and Subsidiaries**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

**Note 8. Intangible assets (Continued)**

agreement whereby CPI will continue to supply a component of the product. Legal fees of \$43,000 associated with this buyout agreement have been capitalized as part of the purchase price of this intangible asset. These two intangible assets have an expected life of ten years and are being amortized on a straight-line basis beginning September 2014. Total amortization expense related to these intangible assets was \$687,000 for each of the years ended December 31, 2017, 2016 and 2015. Aggregate amortization of intangible assets for each of the next five years and thereafter is as follows:

<u>Year ending</u>	<u>December 31,</u> <u>(in thousands)</u>
2018 . . . . .	\$ 1,604
2019 . . . . .	1,604
2020 . . . . .	1,604
2021 . . . . .	1,604
2022 . . . . .	1,604
Thereafter . . . . .	<u>6,237</u>
	<u>\$14,257</u>

Patents utilized in the manufacturing of the Company’s generic Tussionex product which total \$352,000 are being amortized over their expected useful life of 10 years. Patents utilized in the manufacturing of Adzenys XR-ODT which total \$599,000 are being amortized over their expected useful life, including \$535,000 being amortized for approximately 16 years beginning with the approval of Adzenys XR-ODT on January 27, 2016 and \$64,000 being amortized for approximately 15 years beginning in December 2017. Patents utilized in the manufacturing of Cotempla XR-ODT which total \$83,000 are being amortized over their expected useful life of approximately 15 years, beginning with the approval of Cotempla XR-ODT on June 19, 2017. Patents utilized in the manufacturing of Adzenys ER which total \$451,000 are being amortized over their expected useful life of approximately 15 years, beginning with the approval of Adzenys ER on September 15, 2017. For the years ended December 31, 2017, 2016 and 2015, \$88,000, \$69,000 and \$23,000 of patent amortization expense was recorded, respectively.

**Note 9. Income taxes**

The Company applies FASB ASC topic 740, “Income Taxes” or ASC 740 which addresses the determination of whether tax benefits claimed, or expected to be claimed on a tax return should be recorded in the financial statements. Under ASC 740, the Company may recognize the tax benefit from an uncertain tax position only if it is more likely than not that the tax position will be sustained on examination by the taxing authorities, based on the technical merits of the position. The tax benefits recognized in the financial statements from such a position should be measured based on the largest benefit that has a greater than 50% likelihood of being realized upon ultimate settlement. ASC 740 also provides guidance on derecognition, classification, interest and penalties on income taxes, accounting in interim periods and requires increased disclosures.

The Company is generally subject to tax examination for a period of three years after tax returns are filed. Therefore, the statute of limitations remains open for tax years 2014 and forward. However, when a company has net operating loss carryovers, those tax years remain open until three years after the net operating losses are utilized. Therefore, the tax years remain open back to 2004.

**Neos Therapeutics, Inc. and Subsidiaries**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

**Note 9. Income taxes (Continued)**

On December 22, 2017, the President of the United States signed into law the Tax Cuts and Jobs Act of 2017. The legislation significantly changes U.S. tax law by, among other things, lowering the U.S. corporate income tax rate from a maximum of 35% to a flat 21% rate, effective January 1, 2018.

Deferred tax assets and liabilities are determined based on the differences between the financial reporting and tax bases of assets and liabilities. Deferred tax assets and liabilities are measured using enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to reverse. As a result of the reduction in the U.S. corporate income tax rate from 35% to 21% under the Tax Cuts and Jobs Act of 2017, the Company revalued its ending net deferred tax assets at December 31, 2017 and recognized a reduction of \$20.5 million in deferred tax assets with a corresponding reduction in the valuation allowance.

The significant components of deferred income tax assets and liabilities consist of the following:

	December 31,	
	2017	2016
	(in thousands)	
Deferred Tax Assets:		
Net operating loss . . . . .	\$32,193	\$ 65,532
Deferred revenue . . . . .	3,145	—
Share-based compensation . . . . .	1,340	1,562
R&D tax credit . . . . .	1,696	1,792
Other reserves . . . . .	1,069	1,064
Capital lease liability . . . . .	562	151
State deferreds . . . . .	464	16
Inventory . . . . .	466	—
Other . . . . .	980	1,595
Total deferred tax assets . . . . .	41,915	71,712
Deferred Tax Liabilities:		
Intangible assets . . . . .	(1,846)	(3,371)
Property and equipment . . . . .	(747)	(124)
Total deferred tax liabilities . . . . .	(2,593)	(3,495)
Valuation allowance . . . . .	(39,322)	(68,217)
Net deferred tax asset (liability) . . . . .	\$ —	\$ —

At December 31, 2017, and 2016, the Company has gross federal net operating loss carry-forwards of \$247,493,000 and \$200,170,000 and research and development credits of \$2,275,000 and \$2,179,000, respectively, which begin to expire in 2024. The Company has tax effected state net operating loss carry-forwards of \$2,620,000 and \$1,835,000 at December 31, 2017 and 2016, respectively. Utilization of the net operating loss carry-forwards and credits may be subject to a substantial annual limitation due to the ownership change limitations provided by the Internal Revenue Code of 1986, as amended and similar state provisions. The Company has performed an analysis to determine the impact of any ownership change(s) under Section 382 of the Internal Revenue Code. Due to an ownership change in 2017, the amount of federal net operating loss that will expire unused due to the Section 382 limitation is \$101,744,000. The amount of federal research and development credit that will expire unused is



**Neos Therapeutics, Inc. and Subsidiaries**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

**Note 9. Income taxes (Continued)**

\$350,000. The deferred tax assets and related valuation allowances for both carryforwards have been reduced accordingly.

The Company recognizes interest and penalties related to uncertain tax positions in income tax expense. The Company has no accrued interest related to its uncertain tax positions as they all relate to timing differences that would adjust the Company's net operating loss carryforward and do not require recognition. As a result of these timing differences, at December 31, 2017 and December 31, 2016, the Company had gross unrecognized tax benefits related to uncertain tax positions of \$7,261,000 and \$5,081,000, respectively. The Company has no other tax positions taken or expected to be taken that would significantly increase or decrease unrecognized tax benefits within 12 months of the reporting date. Changes in unrecognized benefits in any given year are recorded as a component of deferred tax expense. A tabular rollforward of the Company's gross unrecognized tax benefits is below:

	December 31,	
	2017	2016
	(in thousands)	
Beginning Balance . . . . .	\$5,081	\$4,355
Increase based on tax positions taken during a current period . . . .	2,180	726
Ending Balance . . . . .	\$7,261	\$5,081

The Company has recorded a valuation allowance of \$39,322,000 at December 31, 2017 and \$68,217,000 at December 31, 2016 to fully reserve its net deferred tax assets. The Company has assessed the likelihood that the deferred tax assets will be realized and determined that it is more likely than not that all of the deferred tax assets will not be realized. The ultimate realization of deferred tax assets is dependent upon the generation of future taxable income during the periods in which those temporary differences become deductible. The Company considers the scheduled reversal of deferred tax liabilities, projected future taxable income and tax planning strategies in making this assessment. Due to the uncertainty of realizing the deferred tax asset, the Company has placed a valuation allowance against the entire deferred tax asset. The Company may not ever be able to realize the benefit of some or all of the federal and state loss carryforwards, either due to ongoing operating losses or due to ownership changes, which limit the usefulness of the loss carryforwards. The change in the valuation allowance was a decrease of 28,895,000 and an increase of \$29,886,000 for the years ended December 31, 2017 and December 2016, respectively. As a result of the TCJA reduction in the U.S. corporate income tax rate, the Company reduced its deferred tax assets by \$20,547,000 with a corresponding reduction in the valuation allowance.

**Neos Therapeutics, Inc. and Subsidiaries**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

**Note 9. Income taxes (Continued)**

A reconciliation of the Company's Federal statutory tax rate of 34% to the Company's effective income tax rate is as follows:

	<b>Year Ended December 31,</b>	
	<b>2017</b>	<b>2016</b>
U.S. Statutory Tax Rate . . . . .	34%	34%
Change in Valuation Allowance . . . . .	44%	(36)%
Deferred Tax Adjustments . . . . .	(47)%	1%
Federal Rate Change . . . . .	(31)%	—
State tax expense, net . . . . .	2%	2%
Provision to Return and Other Adjustments . . . . .	(2)%	(1)%
Tax Expense / (Benefit) . . . . .	<u>0%</u>	<u>0%</u>

The deferred tax adjustments are primarily attributable to the amount of federal net operating loss that will expire unused due to the Section 382 limitation.

**Note 10. Accrued expenses**

Accrued expenses as of December 31, 2017 and 2016 consist of the following:

	<b>December 31,</b>	
	<b>2017</b>	<b>2016</b>
Reserve for rebates . . . . .	\$ 2,687	\$ 421
Accrued payroll and benefits . . . . .	2,534	2,085
Reserve for wholesaler fees . . . . .	2,387	509
Other accrued expenses . . . . .	2,962	2,249
Total accrued expenses . . . . .	<u>\$10,570</u>	<u>\$5,264</u>

**Note 11. Long-term debt**

Long-term debt at the indicated dates consists of the following:

	<b>December 31,</b>	
	<b>2017</b>	<b>2016</b>
	<b>(in thousands)</b>	
Deerfield senior secured credit facility, net of discount of \$2,843 and \$1,401, respectively . . . . .	\$57,156	\$63,075
Capital leases, maturing through May 2020 . . . . .	2,678	445
	59,834	63,520
Less current portion . . . . .	(896)	(4,921)
Long-term debt . . . . .	<u>\$58,938</u>	<u>\$58,599</u>

**Neos Therapeutics, Inc. and Subsidiaries**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

**Note 11. Long-term debt (Continued)**

*Senior secured credit facility:* On May 11, 2016, the Company entered into a \$60.0 million senior secured credit facility (“Facility”) with Deerfield Private Design Fund III, L.P. (66⅔% of Facility) and Deerfield Special Situations Fund, L.P. (33⅓% of Facility) (collectively, “Deerfield”), as lenders. In February 2017, the Company closed an underwritten public offering of 5,750,000 shares of its common stock at a public offering price of \$5.00 per share (see Note 12). Deerfield, the Company’s senior lender, participated in the purchase of the Company’s common shares as part of this public offering, and as a result, is now classified as a related party.

Approximately \$33 million of the \$60 million Facility proceeds was used to prepay the existing \$24.3 million principal and \$0.1 million of accrued interest related to the senior Loan and Security Agreement (“LSA”) with Hercules Technology III, L.P., (“Hercules”), the \$1.1 million LSA end of term fee, an LSA prepayment charge of \$243,000 and the \$5.9 million of principal and \$1.3 million of interest on the 10% related party amended and restated subordinated note (“Note”) that was issued by the Company to Essex Capital Corporation (“Essex”), which were otherwise payable in 2016 and 2017. Principal on the Facility is due in three equal annual installments beginning in May 2019 and continuing through May 2021, with a final payment of principal, interest and all other obligations under the Facility due May 11, 2022. Interest is due quarterly beginning in June 2016, at a rate of 12.95% per year. The Company had an option, which it exercised, to defer payment of each of the first four interest payments, adding such amounts to the outstanding loan principal. The aggregate \$6.6 million in deferred interest payments (“Accrued Interest”) was due and payable on June 1, 2017. Borrowings under the Facility are collateralized by substantially all of the Company’s assets, except the assets under capital lease, and the Company will maintain cash on deposit of not less than \$5.0 million.

On June 1, 2017 (the “Amendment Date”), the Company and Deerfield entered into a First Amendment (the “Amendment”) to the Facility which extended the date to repay the Accrued Interest under the Facility to June 1, 2018 (the “PIK Maturity Date”), which may be extended to June 1, 2019 at the election of the Company if certain conditions have been met as specified in the Amendment.

The right to payment of the Accrued Interest was memorialized in the form of senior secured convertible notes (the “Convertible Notes”) issued to Deerfield on the Amendment Date. Interest is due quarterly at a rate of 12.95% per year. The principal amount of the Convertible Notes issued under the Amendment and all accrued and unpaid interest thereon shall become due and payable upon written notice from Deerfield, and if either (a) the Company does not meet certain quarterly sales milestones specified in the Amendment or (b) the Company has not received and publicly announced FDA approval of the new drug applications on or before the applicable Prescription Drug User Fee Act (the “PDUFA”) goal date as set forth on the schedules to Amendment. Per the Amendment, the Company will prepay all of the outstanding obligations under the Facility and the Convertible Notes upon the occurrence of a change in control or a sale of substantially all of the Company’s assets and liabilities. The Amendment increased the staggered prepayment fees for prepayments due upon a change of control or any other prepayment made or required to be made by the Company by 300 basis points from June 1, 2017 through the period ending prior to May 11, 2020 for the change in control prepayment fees and through the period ending prior to May 11, 2022 for any other prepayments, respectively (the “Prepayment Premiums”). Such Prepayment Premiums, as amended, range from 12.75% to 2%.

**Neos Therapeutics, Inc. and Subsidiaries**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

**Note 11. Long-term debt (Continued)**

The \$6.6 million of Convertible Notes was convertible into shares of the Company's common stock at the noteholder's option at any time up to the close of business on the date that is five days prior to the PIK Maturity Date. The per share conversion price was the greater of (a) 95% of the average of the volume weighted average prices per share of the Company's common stock on the NASDAQ Global Market for the three trading day period immediately preceding such conversion, and (b) \$7.00. Deerfield cannot own more than 9.985% of the Company's outstanding shares at any one time, and the aggregate conversion cannot exceed 19.9% of the Company's outstanding common stock as of June 1, 2017.

On October 26, 2017, Deerfield provided a conversion notice electing to convert the entire \$6.6 million of Convertible Notes into shares of the Company's common stock at a conversion price of \$7.08 per share. The conversion price was based on 95% of the average of the volume weighted average prices per share of the Company's common stock on the NASDAQ Global Market for the three trading day period immediately preceding such conversion. This resulted in issuing 929,967 shares of the Company's common stock to Deerfield on this date and the Convertible Notes were cancelled.

In conjunction with the Amendment to the Facility and the related issuance of the Convertible Notes, the Company entered into a Registration Rights Agreement ("Registration Agreement") which required the Company to file a registration statement with the SEC to register the shares of common stock issued or issuable upon conversion of the Convertible Notes ("Conversion Shares") (subject to certain adjustment for stock split, dividend or other distribution, recapitalization or similar events, "Registrable Securities") within 30 days from June 1, 2017, which was to become effective per the SEC no later than 75 days thereafter. The Company filed a registration statement on Form S-3 to comply with the Registration Agreement on June 30, 2017, which became effective on July 11, 2017. This filing covered 940,924 shares, which is the number of shares that would be issued at the floor conversion rate of \$7.00 per share. The Company is also required to, among other things, maintain the effectiveness of such registration statement, continue to file the required SEC filings on a timely basis, use its best efforts to ensure that the registered securities are listed on each securities exchange on which securities of the same class or series as issued by the Company are then listed and comply with any Financial Industry Regulatory Authority ("FINRA") requests. The Company's obligations with respect to each registration end at the date which is the earlier of (a) when all of the Registrable Securities covered by such registration have been sold or (b) when Deerfield or any of its transferee or assignee under the Registration Agreement cease to hold any Registrable Securities. For each registration, the Company shall bear all reasonable expenses, other than underwriting discounts and commissions, and shall reimburse Deerfield or any assignee or transferee for up to \$25,000 in legal fees. The Company currently expects to satisfy all of its obligations under this Registration Agreement and does not expect to pay any damages pursuant to this agreement; therefore, no liability has been recorded (see Note 15).

The Company has accounted for the Amendment as a debt modification as the instruments were not substantially different; therefore, the remaining debt discount on the original Facility is being amortized using the effective interest method over the remaining term of the modified debt. The Company evaluated the Amendment together with the Convertible Notes to determine if those contracts or embedded components of those contracts qualified as derivatives requiring separate recognition. This evaluation identified a derivative liability of \$2.1 million for the fair value of the change in control and other accelerated payment features as the prepayment fees resulted in premiums that were greater than 10% (see Note 4). As the change in control and other accelerated payments terms, including the prepayment fees, were applied to the entire debt per the terms of the amended

**Neos Therapeutics, Inc. and Subsidiaries**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

**Note 11. Long-term debt (Continued)**

Facility, the corresponding debt discount will be amortized using the effective interest method over the remaining term of the Facility. The fees paid to or on behalf of the creditor for the debt modification totaled \$40,000 and were recorded as additional debt discount on the amended Facility to be amortized to interest expense using the effective interest method over the term of the Facility. The Company's evaluation also determined that the embedded conversion options should not be bifurcated as derivatives from the Convertible Notes host instruments. Therefore, the Company recorded a \$0.6 million discount to the convertible notes for the intrinsic value of the embedded conversion option based upon the difference between the fair value of the underlying common stock on June 1, 2017 and the effective conversion price embedded in the Convertible Notes, which will be amortized using the effective interest method to interest expense over the one-year term of the Convertible Notes. The Company recorded a \$0.6 million corresponding credit to a beneficial conversion feature classified as additional paid in capital in stockholders' equity (deficit) in the Company's financial statements.

In connection with the initial Facility, the Company paid a \$1,350,000 yield enhancement fee to Deerfield, approximately \$173,000 of legal costs to the Company's attorneys and \$58,000 of legal costs on behalf of Deerfield's attorneys, all of which were recorded as debt discount and amortized over the six-year term of the Facility, using the effective interest method. Borrowings under the Facility are collateralized by substantially all of the Company's assets, except the Company's assets under capital lease, and the Company will maintain cash on deposit of not less than \$5.0 million.

Pursuant to the Convertible Notes, if the Company had failed to provide the number of conversion shares, then the Company would have paid damages to Deerfield or subsequent holder or any designee ("Holder") for each day after the third business day after receipt of notice of conversion ("Share Delivery Date") that such conversion was not timely effected. The Facility also contains certain customary nonfinancial covenants, including limitations on the Company's ability to transfer assets, engage in a change of control, merge or acquire with or into another entity, incur additional indebtedness and distribute assets to shareholders. Upon an event of default, the lenders may declare all outstanding obligations accrued under the Facility to be immediately due and payable, and exercise its security interests and other rights. As of December 31, 2017, the Company was in compliance with the covenants under the Facility.

Debt discount amortization for the Facility, including the Amendment after June 1, 2017, was calculated using the effective interest rates of 15.03% on the original facility debt and 25.35% on the Convertible Notes, charged to interest expense and totaled \$1,316,000 and \$181,000 for the years ended December 31, 2017 and 2016, respectively.

*Senior debt:* In March 2014, the Company entered into the LSA, which was subsequently amended in August 2014, September 2014, December 2014 and June 2015. As amended, the LSA provided a total commitment of \$25.0 million, available in four draws. Borrowings under the LSA were collateralized by substantially all of the Company's assets, except the Company's intellectual property and assets under capital lease. The first draw of \$10.0 million, ("Tranche 1"), was issued during March 2014 and was used in its entirety to repay outstanding principal under a previous credit facility. The second draw of \$5.0 million, ("Tranche 2"), was issued during September 2014. The third draw ("Tranche 3") in the amount of \$5.0 million was issued in March 2015, and the fourth and final draw ("Tranche 4") in the amount of \$5.0 million was issued in June 2015.

**Neos Therapeutics, Inc. and Subsidiaries**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

**Note 11. Long-term debt (Continued)**

Each draw was to be repaid in monthly installments, comprised of interest-only monthly payments until May 2016, when installments of interest and principal calculated over a thirty-month amortization period commenced. A balloon payment of the entire principal balance outstanding on October 1, 2017 and all accrued but unpaid interest thereunder was due and payable on October 1, 2017. The interest rate was 9% per annum for Tranche 1 and Tranche 4 and 10.5% per annum for Tranche 2 and Tranche 3. An end of term charge of \$1.1 million was payable at the earliest to occur of (1) October 1, 2017, (2) the date the Company prepaid its outstanding Secured Obligations, as defined therein, or (3) the date the Secured Obligations became due and payable. As such, the end of term charge of \$1.1 million was paid on May 11, 2016 when the Company prepaid its outstanding Secured Obligations, as defined therein.

In connection with the LSA, the Company issued the Hercules Warrants which consisted of 60,000 Series C warrants in March 2014 and 110,000 Series C warrants in September 2014 at the then current price of \$5.00 per share. The Hercules Warrants became warrants with a term of five years for the purchase of 70,833 shares of common stock at a price of \$12.00 per share upon the closing of the Company's IPO and were therefore reclassified from warrant liability to Additional Paid in Capital within Stockholders' Equity at July 22, 2015.

LSA end of term charge amortization totaled \$121,000 and \$311,000 for the years ended December 31, 2016 and 2015, respectively. LSA debt discount amortization charged to interest expense totaled \$104,000 and \$265,000 for the years ended December 30, 2016 and 2015, respectively.

The early prepayment of the LSA with some of the proceeds from the Facility resulted in a \$1,187,000 loss on debt extinguishment which is separately shown in the consolidated statement of operations for the year ended December 31, 2016.

*10% subordinated related party note:* The Company had a Note in the aggregate principal amount of \$5.9 million that was issued by the Company to Essex which was to mature in March 2017. Interest was to be accrued and added to the principal balance until such time as the Company achieved positive EBITDA for three consecutive months. During the year ended December 31, 2016, interest expense of \$263,000 was accrued. On May 11, 2016, the Company prepaid the \$5.9 million outstanding aggregate principal and \$1.3 million in accrued and unpaid interest.

*Capital lease obligations to related party:* As described in Notes 7 and 17, during the years ended December 31, 2017, 2014 and 2013, the Company entered into agreements with Essex for the sale-leaseback of existing and newly acquired assets with a total capitalized cost of \$3.2 million, \$795,000 and \$5.5 million, respectively, which are classified as capital leases. The approximate imputed interest rate on these leases is 14.9%, 14.5% and 14.5%, respectively. Interest expense on these leases was \$263,000, \$204,000 and 467,000 for the years ended December 31, 2017, 2016 and 2015 respectively.

**Neos Therapeutics, Inc. and Subsidiaries**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

**Note 11. Long-term debt (Continued)**

Future minimum capital lease payments through the years ending December 31, 2020 are as follows:

<u>Year ending:</u>	<u>December 31,</u> <u>(in thousands)</u>
2018 . . . . .	\$1,235
2019 . . . . .	1,235
2020 . . . . .	<u>776</u>
Total minimum lease payments . . . . .	\$3,246
Less amount representing interest . . . . .	<u>568</u>
Future minimum lease payments . . . . .	<u>\$2,678</u>

Future principal payments of long-term debt, including capital leases, are as follows:

<u>Year ending:</u>	<u>December 31,</u> <u>(in thousands)</u>
2018 . . . . .	\$ 896
2019 . . . . .	16,039
2020 . . . . .	15,742
2021 . . . . .	15,000
2022 . . . . .	15,000
Thereafter . . . . .	<u>—</u>
Future principal payments . . . . .	\$62,677
Less unamortized debt discount . . . . .	(2,843)
Less current portion of long-term debt . . . . .	<u>(896)</u>
Total long-term debt . . . . .	<u>\$58,938</u>

**Note 12. Common stock**

On July 28, 2015, the Company closed its initial public offering (“IPO”) whereby the Company sold 5,520,000 shares of common stock, at a public offering price of \$15.00 per share, which includes 720,000 shares of common stock resulting from the underwriters’ exercise of their over-allotment option at the IPO price on July 23, 2015. Proceeds from the Company’s IPO, net of underwriting discounts and commissions and other offering costs, were \$75.0 million.

In connection with the IPO, the Company’s Board of Directors approved a 1-for-2.4 reverse stock split of the Company’s common stock which also resulted in a proportional adjustment to the conversion ratios of the preferred stock and the preferred stock warrants. All references to common stock and per share amounts in these condensed financial statements and accompanying footnotes have been retroactively adjusted for all periods presented to give effect to this reverse stock split.

In February 2017, the Company closed an underwritten public offering of 5,750,000 shares of its common stock at a public offering price of \$5.00 per share, which included 750,000 shares of its common stock resulting from the underwriters’ exercise of their over-allotment option on February 17, 2017. Deerfield, the Company’s senior lender, participated in the purchase of the Company’s common shares as part of this public offering, and as a result, is now classified as a related party. The net

**Neos Therapeutics, Inc. and Subsidiaries**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

**Note 12. Common stock (Continued)**

proceeds to the Company from this offering, after deducting underwriting discounts and commissions and other offering expenses payable by the Company, were approximately \$26.7 million.

On June 30, 2017, the Company closed an underwritten public offering of 4,800,000 shares of the its common stock at a public offering price of \$6.25 per share for total proceeds of \$30.0 million before estimated offering costs of \$0.2 million. The Company also granted the underwriters a 30-day option to purchase up to an additional 720,000 shares of its common stock which was exercised in full on July 26, 2017. The net proceeds to the Company through July 26, 2017 from this offering, after deducting offering expenses payable by the Company, were approximately \$34.3 million.

The shares of common stock for both the June 2017 and February 2017 offerings were offered pursuant to a shelf registration statement on Form S-3, including a base prospectus, filed by us on August 1, 2016, and declared effective by the SEC, on August 12, 2016. This shelf registration statement covers the offering, issuance and sale by the Company of up to an aggregate of \$125.0 million of its common stock, preferred stock, debt securities, warrants and/or units (the “Shelf”). The Company simultaneously entered into a sales agreement with Cowen and Company, LLC, as sales agent, to provide for the offering, issuance and sale by the Company of up to \$40.0 million of its common stock from time to time in “at-the-market” offerings under the Shelf (the “Sales Agreement”).

During the year ended December 31, 2017, the Company sold an aggregate 749,639 shares of common stock under the Sales Agreement in February 2017, at an average sale price of approximately \$5.01 per share for gross proceeds of \$3.7 million and net proceeds of \$3.6 million and paying total compensation to the sales agent of approximately \$0.1 million. As of December 31, 2017, \$58.0 million of the Company’s common stock, preferred stock, debt securities, warrants and/or units remained available to be sold pursuant to the Shelf, including \$36.2 million of the Company’s common stock which remained available to be sold under the Sales Agreement, subject to certain conditions specified therein.

On October 26, 2017, Deerfield provided a conversion notice electing to convert the entire \$6.6 million of Convertible Notes into shares of the Company’s common stock at a conversion price of \$7.08 per share. The conversion price was based on 95% of the average of the volume weighted average prices per share of the Company’s common stock on the NASDAQ Global Market for the three trading day period immediately preceding such conversion. This resulted in issuing 929,967 shares of the Company’s common stock to Deerfield on this date and the Convertible Notes were cancelled.

The Company never declared or paid any dividends on its capital stock. The Company currently intends to retain all available funds and any future earnings, if any, to fund the development and expansion of its business, and the Company does not anticipate paying any cash dividends in the foreseeable future. Any future determination to pay dividends will be made at the discretion of our board of directors. The Company’s ability to pay dividends on its common stock is limited by restrictions under the terms of our credit facility with Deerfield. In addition, any future indebtedness that the Company may incur could preclude it from paying dividends.

**Note 13. Share-based Compensation**

*Share-based Compensation Plans*

In July 2015, the Company adopted the Neos Therapeutics, Inc. 2015 Stock Option and Incentive Plan (“2015 Plan”) which became effective immediately prior to the closing of the IPO and initially had



**Neos Therapeutics, Inc. and Subsidiaries**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

**Note 13. Share-based Compensation (Continued)**

767,330 shares of common stock reserved for issuance. On January 1, 2016 and each January 1 thereafter, the number of shares of common stock reserved and available for issuance under the 2015 Plan shall be cumulatively increased by five percent of the number of shares of stock issued and outstanding on the immediately preceding December 31 or such lesser number of shares determined by the administrator of the 2015 Plan. Accordingly, on January 1, 2018 and 2017, the Company added 1,449,847 shares and 803,049 shares, respectively, to the option pool. The 2015 Plan superseded the Neos Therapeutics, Inc. 2009 Equity Plan (“2009 Plan”), originally adopted in November 2009 and which had 1,375,037 shares reserved and available for issuance. Effective upon closing of the IPO, the Company’s board of directors determined not to grant any further awards under the 2009 Plan.

The shares of common stock underlying any awards that are forfeited, canceled, reacquired by the Company prior to vesting, satisfied without the issuance of stock or otherwise terminated (other than by exercise) under the 2009 Plan will be added to the shares of common stock available under the 2015 Plan. This number is subject to adjustment in the event of a stock split, stock dividend or other change in the Company’s capitalization. The 2015 Plan is administered by the Company’s compensation committee. The Company’s compensation committee has full power to select, from among the individuals eligible for awards, the individuals to whom awards will be granted, to make any combination of awards to participants and to determine the specific terms and conditions of each award, subject to the provisions of the 2015 Plan. The Company’s compensation committee may delegate authority to grant certain awards to the Company’s chief executive officer. Through December 31, 2017, the Company has granted options, restricted stock and RSUs. The exercise price per share for the stock covered by a stock award granted shall be determined by the administrator at the time of grant but shall not be less than 100 percent of the fair market value on the date of grant. Unexercised stock awards under the 2015 Plan expire after the earlier of 10 years or termination of employment, except in the case of any unexercised vested options, which generally expire 90 days after termination of employment.

The 2009 Plan allowed the Company to grant options to purchase shares of the Company’s common stock and to grant restricted stock awards to members of its management and selected members of the Company’s board of directors. Restricted stock awards are recorded as deferred compensation and amortized into compensation expense, on a straight-line basis over a defined vesting period ranging from 1 to 48 months. Options were granted to officers, employees, nonemployee directors and consultants, and independent contractors of the Company. The Company also granted performance based awards to selected management. The performance options vested over a three-year period based on achieving certain operational milestones and the remaining options vest in equal increments over periods ranging from two to four years. Unexercised options under the 2009 Plan expire after the earlier of 10 years or termination of employment, except in the case of any unexercised vested options, which generally expire 90 days after termination of employment. All terminated options are available for reissuance under the 2015 Plan. Since the inception of the 2015 Plan through December 31, 2017, 9,304 shares related to forfeited 2009 Plan options and 33,801 shares related to the surrender of restricted stock were added to the shares available under the 2015 Plan. During year ended December 31, 2017, 1,804 shares related to forfeited 2009 Plan options and 14,895 shares related to the surrender of restricted stock were added to the shares available under the 2015 Plan. As of December 31, 2017, 594,665 shares of common stock remain available for grant under the 2015 Plan.

**Neos Therapeutics, Inc. and Subsidiaries**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

**Note 13. Share-based Compensation (Continued)**

*Share-based Compensation Expense*

The Company has reported share-based compensation expense for the years ended December 31, 2017, 2016 and 2015, respectively, in its condensed consolidated statements of operations as follows:

	<b>Year Ended December 31,</b>		
	<b>2017</b>	<b>2016</b>	<b>2015</b>
	<i>(in thousands)</i>		
Cost of goods sold . . . . .	\$ 390	\$ 311	\$ 112
Research and development . . . . .	394	304	73
Selling and marketing . . . . .	913	723	211
General and administrative . . . . .	2,354	2,122	785
	<u>\$4,051</u>	<u>\$3,460</u>	<u>\$1,181</u>

The total share based compensation expense included in the table above is attributable to stock options, RSUs and restricted stock of \$3.9 million, \$86,000 and \$71,000, respectively, for the year ended December 31, 2017. The total share based compensation expense included in the table above is attributable to stock options and restricted stock of \$3.4 million and \$91,000, respectively, for the year ended December 31, 2016. The total share based compensation expense included in the table above is attributable to stock options and restricted stock of \$1.1 million and \$94,000, respectively, for the year ended December 31, 2015.

As of December 31, 2017, there was \$6.5 million of compensation costs adjusted for any estimated forfeitures, related to non-vested stock options and RSUs granted under the Company's equity incentive plans not yet recognized in the Company's financial statements. The unrecognized compensation cost is expected to be recognized over a weighted average period of 2.0 years for stock options and 3.4 years for RSUs. There is no unrecognized compensation cost associated with grants of restricted stock.

*Stock Options*

During the year ended December 31, 2017, the Company's board of directors granted 570,432 options.

The Company estimates the fair value of all stock options on the grant date by applying the Black-Scholes option pricing valuation model. The application of this valuation model involves assumptions that are highly subjective, judgmental and sensitive in the determination of compensation cost. Prior to the IPO, given the absence of an active market for the Company's common stock prior to its IPO, the Company's board of directors was required to estimate the fair value of its common stock at the time of each option grant primarily based upon valuations performed by a third-party valuation firm.

**Neos Therapeutics, Inc. and Subsidiaries**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

**Note 13. Share-based Compensation (Continued)**

The weighted-average key assumptions used in determining the fair value of options granted during the period indicated are as follows:

	Year Ended December 31,		
	2017	2016	2015
Estimated dividend yield . . . . .	0%	0%	0%
Expected stock price volatility . . . . .	60%	60%	60%
Weighted-average risk-free interest rate . . . . .	2.01%	1.18%	1.60%
Expected life of option in years . . . . .	6.06	6.15	5.00
Weighted-average option fair value at grant . . . . .	\$4.090	\$5.800	\$9.723

A summary of outstanding and exercisable options as of December 31, 2017, 2016 and 2015, and the activity from December 31, 2014 through December 31, 2017, is presented below:

	Number of Options	Weighted-Average Exercise Price	Intrinsic Value  (in thousands)
Outstanding at December 31, 2014 . . . . .	511,775	\$ 3.684	\$2,883
Exercisable at December 31, 2014 . . . . .	150,109	\$ 1.467	\$1,179
Granted . . . . .	883,537	18.789	
Exercised . . . . .	(38,307)	1.928	
Expired, forfeited or cancelled . . . . .	(4,722)	2.547	
Outstanding at December 31, 2015 . . . . .	1,352,283	\$13.607	\$ 964
Exercisable at December 31, 2015 . . . . .	229,000	\$ 3.385	\$2,504
Granted . . . . .	859,257	10.385	
Exercised . . . . .	(10,886)	1.231	
Expired, forfeited or cancelled . . . . .	(93,310)	17.780	
Outstanding at December 31, 2016 . . . . .	2,107,344	\$12.173	\$1,128
Exercisable at December 31, 2016 . . . . .	595,424	\$ 9.715	\$ 881
Granted . . . . .	570,432	7.220	
Exercised . . . . .	(1,249)	0.223	
Expired, forfeited or cancelled . . . . .	(221,554)	10.325	
Outstanding at December 31, 2017 . . . . .	2,454,973	\$11.195	\$4,764
Exercisable at December 31, 2017 . . . . .	1,137,766	\$10.919	\$2,890

The weighted-average remaining contractual life of options outstanding and exercisable on December 31, 2017 was 7.9 and 7.2 years, respectively. The option exercise price for all options granted in the year ended December 31, 2017 ranged from \$7.00 to \$9.10 per share.

*Restricted Stock Units*

On May 1, 2017, the Company granted 78,750 RSUs to members of its management which vest in four equal annual installments, beginning May 1, 2018. On October 2, 2017, the Company granted

**Neos Therapeutics, Inc. and Subsidiaries**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

**Note 13. Share-based Compensation (Continued)**

6,250 RSUs to a member of its management which vest in four equal annual installments, beginning October 2, 2018. The Company had not issued any RSUs previously.

A summary of outstanding RSUs as of December 31, 2017 and 2016 and the activity from December 31, 2016 through December 31, 2017, is presented below:

	Number of RSUs	Weighted-Average Fair Value
Outstanding at December 31, 2016 .....	—	\$ —
Granted .....	85,000	\$7.15
Exercised .....	—	—
Expired, forfeited or cancelled .....	—	—
Outstanding at December 31, 2017 .....	85,000	\$7.15

The weighted-average remaining contractual life of RSUs outstanding on December 31, 2017 was 9.4 years.

*Restricted stock*

The Company did not issue any shares of restricted stock for the years ended December 31, 2017, 2016 and 2015. On October 16, 2017, October 17, 2016 and October 16, 2015, 14,895 shares, 9,709 shares and 9,197 shares, respectively, of restricted stock were surrendered by the holder to the Company to cover taxes associated with vesting of restricted stock. The surrendered shares of restricted stock were added to the shares available under the 2015 Plan.

The Company had no unvested restricted stock as of December 31, 2017, and had 35,513 and 71,025 shares of unvested restricted stock with a weighted average fair value of \$2.55 and \$2.55 as of December 31, 2016 and 2015, respectively. For the years ended December 31, 2017, 2016 and 2015, there were no shares of restricted stock granted or forfeited.

**Note 14. Treasury stock**

The Company has the authority to repurchase common stock from former employees, officers, directors or other persons who performed services for the Company at the lower of the original purchase price or the then-current fair market value. On October 16, 2017, October 17, 2016 and October 16, 2015, 14,895 shares, 9,709 shares and 9,197 shares, respectively, of restricted stock were surrendered by the holder to the Company to cover taxes associated with vesting of restricted stock and such shares were added back into the treasury stock of the Company, increasing total treasury stock to 33,801 shares as of December 31, 2017. On February 19, 2015, the Company's board of directors approved the cancellation of the Company's 55,905 shares of treasury stock which had been repurchased at the original purchase price of \$0.002 in 2013.

**Note 15. Commitments and contingencies**

*Registration Payment Arrangement:* On June 1, 2017, in conjunction with the Amendment to the Facility and the related issuance of the Convertible Notes, the Company entered into the Registration Agreement which required the Company to file a registration statement with the SEC to register the

**Neos Therapeutics, Inc. and Subsidiaries**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

**Note 15. Commitments and contingencies (Continued)**

Registrable Securities (see Note 11) within 30 days from June 1, 2017, which was to become effective per the SEC no later than 75 days thereafter. The Company filed a registration statement on Form S-3 to comply with the Registration Agreement on June 30, 2017, which became effective on July 11, 2017. This filing covered 940,924 shares, which is the number of shares that would be issued at the floor conversion rate of \$7.00 per share. The Company is also required to, among other things, maintain the effectiveness of such registration statement, continue to file the required SEC filings on a timely basis, use its best efforts to ensure that the registered securities are listed on each securities exchange on which securities of the same class or series as issued by the Company are then listed and comply with any FINRA requests. Upon any Registration Failure, the Company shall pay additional damages to the Holder for each 30-day period (prorated for any partial period) after the date of such Registration Failure in an amount in cash equal to two percent of the original principal amount of the Convertible Notes. The Company's obligations with respect to each registration end at the date which is the earlier of (a) when all of the Registrable Securities covered by such registration have been sold or (b) when Deerfield or any of its transferee or assignee under the Registration Agreement cease to hold any of the Registrable Securities. For each registration filing, the Company shall bear all reasonable expenses, other than underwriting discounts and commissions, and shall reimburse Deerfield or any assignee or transferee for up to \$25,000 in legal fees. The Company currently expects to satisfy all of its obligations under the Registration Agreement and does not expect to pay any damages pursuant to this agreement; therefore, no liability has been recorded.

*Patent Infringement Litigation:* On October 31, 2017, the Company received a paragraph IV certification from Teva Pharmaceuticals USA, Inc. ("Teva") advising the Company that Teva has filed an ANDA with the FDA for a generic version of Cotempla XR-ODT, in connection with seeking to market its product prior to the expiration of patents covering Cotempla XR-ODT. The certification notice alleged that the three U.S. patents listed in the FDA's Orange Book for Cotempla XR-ODT, one with an expiration date in April 2026 and two with expiration dates in June 2032, will not be infringed by Teva's proposed product, are invalid and/or are unenforceable. On December 13, 2017, the Company filed a patent infringement lawsuit in federal district court in the District of Delaware against Teva alleging that Teva infringed the Company's Cotempla XR-ODT patents by submitting to the FDA an ANDA seeking to market a generic version of Cotempla XR-ODT prior to the expiration of the Company's patents. This lawsuit automatically stayed, or barred, the FDA from approving Teva's ANDA for 30 months or until a district court decision that is adverse to the asserted patents is rendered, whichever is earlier. The Company intend to vigorously enforce its intellectual property rights relating to Cotempla XR-ODT.

On July 25, 2016, the Company received a paragraph IV certification from Actavis Laboratories FL, Inc. ("Actavis") advising the Company that Actavis had filed an Abbreviated New Drug Application ("ANDA") with the FDA for a generic version of Adzenys XR-ODT. The certification notice alleged that the four U.S. patents listed in the FDA's Orange Book for Adzenys XR-ODT, one with an expiration date in April 2026 and three with expiration dates in June 2032, will not be infringed by Actavis's proposed product, are invalid and/or are unenforceable. On September 1, 2016, the Company filed a patent infringement lawsuit in federal district court against Actavis alleging that Actavis infringed the Company's Adzenys XR-ODT patents by submitting to the FDA an ANDA seeking to market a generic version of Adzenys XR-ODT prior to the expiration of the Company's patents. On October 17, 2017, the Company entered into a Settlement Agreement (the "Settlement Agreement") and a Licensing Agreement (the "Licensing Agreement" and collectively with the Settlement

**Neos Therapeutics, Inc. and Subsidiaries**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

**Note 15. Commitments and contingencies (Continued)**

Agreement, the “Agreement”) with Actavis. The Agreement resolves all ongoing litigation involving our Adzenys XR-ODT patents and Actavis’s ANDA. Under the Agreement, the Company granted Actavis the right to manufacture and market its generic version of Adzenys XR-ODT under the ANDA beginning on September 1, 2025, or earlier under certain circumstances. A stipulation and order of dismissal was entered by the U.S. District Court for the District of Delaware. The Agreement has been submitted to the applicable governmental agencies.

*Other Litigation:* On March 7, 2018, the Company received a citation advising the Company that the County of Harris, Texas (the “County”) filed a lawsuit on December 13, 2017 against the Company and various other alleged manufacturers, promoters, sellers and distributors of opioid pharmaceutical products. Through this lawsuit, the County seeks to recoup as damages some of the expenses it allegedly has incurred to combat opioid use and addiction. The County also seeks punitive damages, disgorgement of profits and attorneys’ fees. While the Company believes that the lawsuit is without merit and intend to vigorously defend against it, the Company is not able to predict at this time whether this proceeding will have a material impact on its results of operations.

*Defined contribution plans:* The Company maintains a defined contribution plan covering substantially all employees under the provisions of Section 401(k) of the Internal Revenue Code (“Code”). As the Company has elected a Safe-Harbor provision for the 401(k) Plan, participants are always fully vested in their employer contributions. Employees may contribute annually up to the lesser of 50% of their compensation or the applicable limit established by the Code. Effective January 1, 2015, the Company amended its 401(k) plan to provide a Company matching contribution on 100% of a participant’s contribution for the first 3% of their salary deferral and 50% of the next 2% of their salary deferral. For the years ended December 31, 2017, 2016 and 2015, the Company recorded \$419,000, \$371,000 and \$186,000, respectively, of expense for 401(k) contributions.

*Operating leases:* The Company leases its Grand Prairie, Texas office space and manufacturing facility under an operating lease which expires in 2024. In addition, the Company has a 60-month lease for office space in Blue Bell, Pennsylvania for its commercial operations which commenced on May 1, 2016. Total future minimum lease payments under these operating leases with noncancelable terms are as follows:

<u>Year ending December 31,</u>	<u>(in thousands)</u>
2018 . . . . .	\$1,104
2019 . . . . .	1,109
2020 . . . . .	1,160
2021 . . . . .	1,058
2022 . . . . .	1,055
Thereafter . . . . .	<u>2,162</u>
Future minimum lease payments . . . . .	<u>\$7,648</u>

The Company accounts for rent expense on long-term operating leases on a straight-line basis over the life of the lease resulting in a deferred rent balance of \$1,083,000 and \$1,174,000 at December 31, 2017 and December 31, 2016, respectively. The Company is also liable for a share of operating expenses for both premises as defined in the lease agreements. The Company’s share of these operating expenses for both locations was \$243,000 and \$230,000 for the years ended December 31, 2017 and

**Neos Therapeutics, Inc. and Subsidiaries**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

**Note 15. Commitments and contingencies (Continued)**

2016. The Company's share of these operating expenses for the Grand Prairie facility was \$237,000 for the years ended December 31, 2015. Rent expense for these leases, excluding the share of operating expenses, was \$1,010,000, \$1,011,000 and \$884,000 for the years ended December 31, 2017, 2016 and 2015, respectively.

*Cash incentive bonus plan:* In July 2015, the Company adopted the Senior Executive Cash Incentive Bonus Plan ("Bonus Plan"). The Bonus Plan provides for cash payments based upon the attainment of performance targets established by the Company's compensation committee. The payment targets will be related to financial and operational measures or objectives with respect to the Company, or corporate performance goals, as well as individual targets. The Company has recorded \$701,000, \$464,000 and \$552,000 of compensation expense for the years ended December 31, 2017, 2016 and 2015, respectively, under the Bonus Plan.

**Note 16. License agreements**

On October 17, 2017, the Company entered into the Agreement with Actavis. Under the Licensing Agreement, the Company granted Actavis a non-exclusive license to certain patents owned by the Company by which Actavis has the right to manufacture and market its generic version of Adzenys XR-ODT under its ANDA beginning on September 1, 2025, or earlier under certain circumstances. The Licensing Agreement has been submitted to the applicable governmental agencies (see Note 15).

On July 23, 2014, the Company entered into a Settlement Agreement and an associated License Agreement (the "2014 License Agreement") with Shire LLC ("Shire") for a non-exclusive license to certain patents for certain activities with respect to the Company's New Drug Application (the "NDA") No. 204326 for an extended-release orally disintegrating amphetamine polistirex tablet. In accordance with the terms of the 2014 License Agreement, following the receipt of the approval from the FDA for Adzenys XR-ODT, the Company paid a lump sum, non-refundable license fee of an amount less than \$1.0 million in February 2016. The Company is paying a single digit royalty on net sales of Adzenys XR-ODT during the life of the patents.

On January 26, 2017, the Company sent a letter to Shire, notifying Shire that the Company has made a Paragraph IV certification to the FDA that in the Company's opinion and to the best of its knowledge, the patents owned by Shire that purportedly cover the Company's Adzenys ER are invalid, unenforceable and/or will not be infringed by the commercial manufacture, use or sale of Adzenys ER. On March 6, 2017, the Company entered into a License Agreement (the "2017 License Agreement") with Shire, pursuant to which Shire granted the Company a non-exclusive license to certain patents owned by Shire for certain activities with respect to the Company's NDA No. 204325 for an extended-release amphetamine liquid suspension. In accordance with the terms of the 2017 License Agreement, following the receipt of the approval from the FDA for Adzenys ER, the Company paid a lump sum, non-refundable license fee of an amount less than \$1.0 million in October 2017. The Company will also pay a single digit royalty on net sales of Adzenys ER during the life of the relevant Shire patents.

Such license fees are capitalized as an intangible asset and are amortized into cost of goods sold over the life of the longest associated patent. The royalties are recorded as cost of goods sold in the same period as the net sales upon which they are calculated.

**Neos Therapeutics, Inc. and Subsidiaries**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

**Note 16. License agreements (Continued)**

Additionally, each of the 2014 and 2017 License Agreements contains a covenant from Shire not to file a patent infringement suit against the Company alleging that Adzenys XR-ODT or Adzenys ER, respectively, infringes the Shire patents.

**Note 17. Related party transactions**

As described in Note 7, in February 2017, the Company entered into an agreement with a related party for the sale-leaseback of newly acquired assets of up to \$5.0 million to finance the Company's capital expenditures. Each lease under this master agreement will be for an initial term of 36 months and will have an option to purchase the equipment at the end of the respective lease that management considers to be bargain purchase option. Under this master agreement, the Company entered into leases and sold assets with a total capitalized cost of \$481,000 and \$2,742,000 at effective interest rates of 14.3% and 14.9% on February 13, 2017 and June 30, 2017, respectively. Also, in 2012, the Company negotiated financing arrangements with the same related party that provided for the sale-leaseback of up to \$6.5 million of the Company's property and equipment. From the 2012 financing arrangements, the Company has no lease obligation remaining at December 31, 2017 and has a lease obligation of \$445,000 at December 31, 2016. The total lease obligation under all related party financing arrangements was \$2,678,000 and \$445,000 at December 31, 2017 and 2016, respectively.

In February 2017, the Company closed an underwritten public offering of 5,750,000 shares of its common stock at a public offering price of \$5.00 per share, which includes 750,000 shares of the Company's common stock resulting from the underwriters' exercise of their over-allotment option at the public offering price on February 17, 2017 (see Note 12). On June 30, 2017, the Company closed an underwritten public offering of 4,800,000 shares of its common stock at a public offering price of \$6.25 per share for total proceeds of \$30.0 million before estimated offering costs of \$0.2 million. The Company also granted the underwriters a 30-day option to purchase up to an additional 720,000 shares of its common stock (see Note 12). Deerfield, the Company's senior lender, participated in the purchase of the Company's common shares as part of both public offerings, and as a result, is now classified as a related party. The Company is obligated under a \$60.0 million senior secured credit Facility that was issued by the Company to Deerfield. On June 1, 2017, the Company and Deerfield entered into an Amendment to the Company's existing Facility with Deerfield which extended the date to repay the Accrued Interest under the Facility to June 1, 2018, which may be extended to June 1, 2019 at the election of the Company if certain conditions have been met as specified in the Amendment. The right to payment of the Accrued Interest was memorialized in the form of Convertible Notes issued to Deerfield on the Amendment Date. On October 26, 2017, Deerfield provided a conversion notice electing to convert the entire \$6.6 million of Convertible Notes into shares of the Company's common stock at a conversion price of \$7.08 per share. The conversion price was based on 95% of the average of the volume weighted average prices per share of the Company's common stock on the NASDAQ Global Market for the three trading day period immediately preceding such conversion. This resulted in issuing 929,967 shares of the Company's common stock to Deerfield on this date and the Convertible Notes were cancelled (see Note 11).

**Note 18. Selected Quarterly Financial Data (Unaudited)**

The following financial information reflects all normal recurring adjustments, which are, in the opinion of management, necessary for a fair statement of the results of the interim periods. Operating results for these periods are not necessarily indicative of the operating results for a full year. Historical



**Neos Therapeutics, Inc. and Subsidiaries**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

**Note 18. Selected Quarterly Financial Data (Unaudited) (Continued)**

results are not necessarily indicative of results to be expected in future periods. Selected quarterly financial data for years ended December 31, 2017 and 2016, are as follows (in thousands, except share and per share amounts):

	Quarter Ended			
	March 31, 2017	June 30, 2017	September 30, 2017	December 31, 2017
Net sales(1) . . . . .	\$ 5,627	\$ 4,909	\$ 6,695	\$ 7,787
Gross profit(1) . . . . .	1,012	2,333	4,273	5,009
<b>Net loss attributable to common stock . .</b>	<b>\$ (17,090)</b>	<b>\$ (18,674)</b>	<b>\$ (16,258)</b>	<b>\$ (14,225)</b>
Weighted average common shares outstanding used to compute net loss per share, basic and diluted(2) . . . . .	19,624,712	22,613,382	27,884,983	28,746,608
<b>Net loss per share of common stock, basic and fully diluted(3): . . . . .</b>	<b>\$ (0.87)</b>	<b>\$ (0.83)</b>	<b>\$ (0.58)</b>	<b>\$ (0.49)</b>

	Quarter Ended			
	March 31, 2016	June 30, 2016	September 30, 2016	December 31, 2016
Net sales(1) . . . . .	\$ 2,583	\$ 1,485	\$ 1,583	\$ 3,503
Gross (loss)(1) . . . . .	(173)	(858)	(735)	(517)
<b>Net loss attributable to common stock . .</b>	<b>\$ (12,614)</b>	<b>\$ (26,539)</b>	<b>\$ (25,806)</b>	<b>\$ (18,374)</b>
Weighted average common shares outstanding used to compute net loss per share, basic and diluted(2) . . . . .	16,025,318	16,050,138	16,070,705	16,062,685
<b>Net loss per share of common stock, basic and fully diluted(3): . . . . .</b>	<b>\$ (0.79)</b>	<b>\$ (1.65)</b>	<b>\$ (1.61)</b>	<b>\$ (1.14)</b>

- (1) The Company began selling Adzenys XR-ODT on May 16, 2016 and initiated an early experience program for Cotempla XR-ODT with limited product availability on September 5, 2017 before launching this product nationwide on October 2, 2017, and has determined that at this time it cannot reliably estimate expected returns of the products at the time of shipment to wholesalers. Accordingly, the Company defers recognition of revenue and related cost of goods sold on product shipments of Adzenys XR-ODT and Cotempla XR-ODT until the right of return no longer exists, which occurs at the earlier of the time Adzenys XR-ODT and Cotempla XR-ODT units are dispensed through patient prescriptions or expiration of the right of return. Thus, the amounts included in Net Sales and Gross profit (loss) for Adzenys XR-ODT and Cotempla XR-ODT reflect only patient prescriptions dispensed to date. Also, the net loss amounts reflect the sales and marketing expenses associated with the commercialization of Adzenys XR-ODT and Cotempla XR-ODT.
- (2) In February 2017, the Company closed an underwritten public offering of 5,750,000 shares of its common stock at a public offering price of \$5.00 per share, which included 750,000 shares of its common stock resulting from the underwriters' exercise of their over-allotment option on February 17, 2017. On June 30, 2017, the Company closed an underwritten public offering of 4,800,000 shares of its common stock at a public offering price of \$6.25 per share for total proceeds of \$30.0 million before estimated offering costs of \$0.2 million. The Company also granted the underwriters a 30-day option to purchase up to an additional 720,000 shares of its

**Neos Therapeutics, Inc. and Subsidiaries**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

**Note 18. Selected Quarterly Financial Data (Unaudited) (Continued)**

common stock which was exercised in full on July 26, 2017. On October 26, 2017, Deerfield provided a conversion notice electing to convert the entire \$6.6 million of Convertible Notes into shares of the Company's common stock at a conversion price of \$7.08 per share. The conversion price was based on 95% of the average of the volume weighted average prices per share of the Company's common stock on the NASDAQ Global Market for the three trading day period immediately preceding such conversion. This resulted in issuing 929,967 shares of the Company's common stock to Deerfield on this date and the Convertible Notes were cancelled. These transactions produced a significant increase in the number of shares outstanding which will impact the year-over-year comparability of the Company's loss per share calculations.

- (3) Loss per share is computed independently for each of the quarters presented. Therefore, the sum of the quarterly loss per share may not necessarily equal the total for the year.

**Note 19. Subsequent event**

On January 1, 2018, in accordance with the Evergreen Provisions of the 2015 Plan, the Company added 1,449,847 shares to the option pool, increasing the total number of shares reserved and available for issuance under the 2015 Plan to 2,044,512 shares.

## Exhibit index

Exhibit number	Description of exhibit
3.1	Fourth Amended and Restated Certificate of Incorporation of the Registrant, as amended and currently in effect (Filed as an Exhibit to the Registrant's quarterly report on Form 10-Q (001-37508), filed with the SEC on September 4, 2015, incorporated herein by reference).
3.2	Amended and Restated Bylaws of the Registrant, as amended and currently in effect (Filed as an Exhibit to the Registrant's quarterly report on Form 10-Q (001-37508), filed with the SEC on September 4, 2015, incorporated herein by reference).
4.1	Form of common stock certificate (Filed as an Exhibit to the Registrant's registration statement on Form S-1 (333-205106), filed with the SEC on July 13, 2015, incorporated herein by reference).
4.2	Form of warrant to purchase common stock (Filed as an Exhibit to the Registrant's registration statement on Form S-1 (333-205106), filed with the SEC on June 19, 2015, incorporated herein by reference).
10.1	Amended and Restated Investors' Rights Agreement, dated as of June 9, 2015 (Filed as an Exhibit to the Registrant's registration statement on Form S-1 (333-205106), filed with the SEC on June 19, 2015, incorporated herein by reference).
10.2	Amendment and Waiver, dated as of February 5, 2016, amending the Amended and Restated Investors' Rights Agreement of the Registrant (Filed as an Exhibit to the Registrant's annual report on Form 10-K (001-37508), filed with the SEC on March 18, 2016, incorporated herein by reference).
10.3+	Neos Therapeutics, Inc. 2009 Equity Plan (Filed as an Exhibit to the Registrant's registration statement on Form S-1 (333-205106), filed with the SEC on June 19, 2015, incorporated herein by reference).
10.4+	Form of option agreements under 2009 Equity Plan (Filed as an Exhibit to the Registrant's registration statement on Form S-1 (333-205106), filed with the SEC on June 19, 2015, incorporated herein by reference).
10.5+	Neos Therapeutics, Inc. 2015 Stock Option and Incentive Plan and forms of option agreements thereunder (Filed as an Exhibit to the Registrant's registration statement on Form S-1 (333-205106), filed with the SEC on July 13, 2015, incorporated herein by reference).
10.6+	Senior Executive Cash Incentive Bonus Plan (Filed as an Exhibit to the Registrant's quarterly report on Form 10-Q (001-37508), filed with the SEC on November 13, 2015, incorporated herein by reference).
10.7+	Form of Indemnification Agreement between the Registrant and each of its executive officers and directors (Filed as an Exhibit to the Registrant's registration statement on Form S-1 (333-205106), filed with the SEC on July 13, 2015, incorporated herein by reference).
10.8	Third Amended and Restated Subordinated Promissory Note, dated as of December 31, 2013, issued to Essex Capital Corporation, as amended (Filed as an Exhibit to the Registrant's registration statement on Form S-1 (333-205106), filed with the SEC on June 19, 2015, incorporated herein by reference).

Exhibit number	Description of exhibit
10.9†	Loan and Security Agreement, by and between the Registrant, Hercules Technology III, L.P. and Hercules Technology Growth Capital, Inc., in its capacity as administrative agent for itself and Hercules Technology III, L.P. dated as of March 28, 2014, as amended (Filed as an Exhibit to the Registrant's registration statement on Form S-1 (333-205106), filed with the SEC on June 19, 2015, incorporated herein by reference).
10.10†	Settlement Agreement, by and between the Registrant and Shire LLC, dated as of July 23, 2014 (Filed as an Exhibit to the Registrant's registration statement on Form S-1 (333-205106), filed with the SEC on June 19, 2015, incorporated herein by reference).
10.11†	License Agreement, by and between the Registrant and Shire LLC, dated as of July 23, 2014 (Filed as an Exhibit to the Registrant's registration statement on Form S-1 (333-205106), filed with the SEC on June 19, 2015, incorporated herein by reference).
10.12	Commercial Lease Agreement, by and between Riverside Business Green, L.P., and Neos Therapeutics, LP, dated as of June 29, 1999, as amended (Filed as an Exhibit to the Registrant's registration statement on Form S-1 (333-205106), filed with the SEC on June 19, 2015, incorporated herein by reference).
10.13†	Supply Agreement, by and between the Registrant and Coating Place, Inc., dated as of August 28, 2014 (Filed as an Exhibit to the Registrant's registration statement on Form S-1 (333-205106), filed with the SEC on June 26, 2015, incorporated herein by reference).
10.14†	Asset Purchase Agreement, by and between the Registrant and Cornerstone BioPharma, Inc., dated as of August 28, 2014 (Filed as an Exhibit to the Registrant's registration statement on Form S-1 (333-205106), filed with the SEC on June 19, 2015, incorporated herein by reference).
10.15+	Amended and Restated Employment Agreement, by and between the Registrant and Vipin Garg, dated as of July 10, 2015 (Filed as an Exhibit to the Registrant's registration statement on Form S-1 (333-205106), filed with the SEC on July 13, 2015, incorporated herein by reference).
10.16+	Amended and Restated Employment Agreement, by and between the Registrant and Richard Eisenstadt, dated as of July 10, 2015 (Filed as an Exhibit to the Registrant's registration statement on Form S-1 (333-205106), filed with the SEC on July 13, 2015, incorporated herein by reference).
10.17+	Amended and Restated Employment Agreement, by and between the Registrant and Thomas McDonnell, dated as of July 10, 2015 (Filed as an Exhibit to the Registrant's registration statement on Form S-1 (333-205106), filed with the SEC on July 13, 2015, incorporated herein by reference).
10.18†	License Agreement by and among the Registrant and Shire LLC, dated as of March 6, 2017. (Filed as an Exhibit to the Registrant's quarterly report on Form 10-Q (001-37508), filed with the SEC on May 10, 2017, incorporated herein by reference).
10.19	First Amendment to Facility Agreement, dated as of June 1, 2017, by and among Neos Therapeutics, Inc., Deerfield Private Design Fund III, L.P. and Deerfield Special Situation Fund, L.P. (including schedules and exhibits thereto). (Filed as an Exhibit to the Registrant's current report on Form 8-K, filed with the SEC on June 5, 2017, incorporated herein by reference).
10.20	Registration Rights Agreement, dated June 1, 2017, by and among Neos Therapeutics, Inc., Deerfield Private Design Fund III, L.P. and Deerfield Special Situation Fund, L.P. (Filed as an Exhibit to the Registrant's current report on Form 8-K, filed with the SEC on June 5, 2017, incorporated herein by reference).

Exhibit number	Description of exhibit
10.21*†	Settlement Agreement, by and between the Registrant and Actavis Laboratoris FL, Inc., dated as of October 17, 2017.
21.1*	Subsidiaries of the Registrant.
23.1*	Consent of RSM US LLP.
24.1*	Power of Attorney (included on signature page).
31.1*	Certification of Principal Executive Officer pursuant to Rule 13a-14(a) or Rule 15d-14(a) of the Securities Exchange Act of 1934, as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
31.2*	Certification of Principal Financial Officer pursuant to Rule 13a-14(a) or Rule 15d-14(a) of the Securities Exchange Act of 1934, as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
32.1**	Certification of Principal Executive Officer and Principal Financial Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
101.INS*	XBRL Instance Document.
101.SCH*	XBRL Taxonomy Extension Schema Document.
101.CAL*	XBRL Taxonomy Extension Calculation Document.
101.DEF*	XBRL Taxonomy Extension Definition Linkbase Document.
101.LAB*	XBRL Taxonomy Extension Labels Linkbase Document.
101.PRE*	XBRL Taxonomy Extension Presentation Link Document.

\* Filed herewith.

\*\* The certifications furnished in Exhibit 32.1 hereto are deemed to accompany this Annual Report on Form 10-K and will not be deemed “filed” for purposes of Section 18 of the Securities Exchange Act of 1934, as amended. Such certifications will not be deemed to be incorporated by reference into any filings under the Securities Act of 1933, as amended, or the Securities Act of 1934, as amended, except to the extent that the Registrant specifically incorporates it by reference.

† Portions of this exhibit (indicated by asterisks) have been omitted pursuant to a request for confidential treatment and this exhibit has been submitted separately to the SEC.

+ Indicates a management contract or compensatory plan.



Signature

Title

Date

\_\_\_\_\_  
/s/ JOHN SCHMID  
John Schmid Director March 16, 2018

\_\_\_\_\_  
/s/ PAUL EDICK  
Paul Edick Director March 16, 2018

**SCHEDULE II**  
**VALUATION AND QUALIFYING ACCOUNTS**  
(in thousands)

		<u>Balance at beginning of period</u>	<u>Additions charged to costs and expenses</u>	<u>Due to (paid to) third party and deferred until sales recognized</u>	<u>Deductions and Payments</u>	<u>Balance at end of period</u>
<b>For the year ended December 31,</b>						
<b>2017</b>						
Allowance for chargebacks . . . .	(1)	\$779	\$10,146	\$ —	\$(10,109)	\$ 816
Allowance for cash discounts . .	(1)	171	1,814	(47)	(1,601)	337
Sales offers . . . . .	(2)	—	25,880	—	(25,880)	—
Reserve for wholesaler fees . . . .	(2)	509	8,286	684	(7,092)	2,387
Reserve for returns . . . . .	(2)	884	167	—	(158)	893
Rebates . . . . .	(2)	421	6,639	—	(4,373)	2,687
<b>For the year ended December 31,</b>						
<b>2016</b>						
Allowance for chargebacks . . . .	(1)	940	10,504	—	(10,665)	779
Allowance for cash discounts . .	(1)	99	772	(13)	(687)	171
Sales offers . . . . .	(2)	—	3,746	—	(3,746)	—
Reserve for wholesaler fees . . . .	(2)	361	2,838	144	(2,834)	509
Reserve for returns . . . . .	(2)	429	491	—	(36)	884
Rebates . . . . .	(2)	110	396	—	(85)	421
<b>For the year ended December 31,</b>						
<b>2015</b>						
Allowance for chargebacks . . . .	(1)	190	5,359	—	(4,609)	940
Allowance for cash discounts . .	(1)	14	194	—	(109)	99
Sales offers . . . . .	(2)	—	—	—	—	—
Reserve for wholesaler fees . . . .	(2)	117	914	—	(670)	361
Reserve for returns . . . . .	(2)	212	242	—	(25)	429
Rebates . . . . .	(2)	9	103	—	(2)	110

- (1) Shown as a reduction of accounts receivable and gross sales or deferred sales as indicated in column heading.
- (2) Shown as accrued expenses and a reduction of gross sales.



**Consent of Independent Registered Public Accounting Firm**

We consent to the incorporation by reference in the Registration Statements on Form S-3 (No. 333-212809 and 333-219108) and Form S-8 (No. 333-2166698, No. 333-210267 and No. 333-205937) of Neos Therapeutics, Inc. of our report dated March 16, 2018, relating to the consolidated financial statements and the financial statement schedule of Neos Therapeutics and subsidiaries appearing in the Annual Report on Form 10-K of Neos Therapeutics, Inc. for the year ended December 31, 2017.

/s/ RSM US LLP  
New York, New York  
March 16, 2018

**CERTIFICATION PURSUANT TO RULE 13a-14(a) OR 15d-14(a) OF  
THE SECURITIES EXCHANGE ACT OF 1934,  
AS ADOPTED PURSUANT TO SECTION 302 OF  
THE SARBANES-OXLEY ACT OF 2002**

I, Vipin Garg, certify that:

1. I have reviewed this Annual Report on Form 10-K of Neos Therapeutics, Inc.;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
  - a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
  - b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
  - c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
  - d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting.
5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
  - a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
  - b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: March 16, 2018

By: /s/ VIPIN GARG

Vipin Garg  
*President and Chief Executive Officer*  
*(Principal Executive Officer)*

**CERTIFICATION PURSUANT TO RULE 13a-14(a) OR 15d-14(a) OF  
THE SECURITIES EXCHANGE ACT OF 1934,  
AS ADOPTED PURSUANT TO SECTION 302 OF  
THE SARBANES-OXLEY ACT OF 2002**

I, Richard Eisenstadt, certify that:

1. I have reviewed this Annual Report on Form 10-K of Neos Therapeutics, Inc.;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
  - a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
  - b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
  - c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
  - d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting.
5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
  - a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
  - b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting

Date: March 16, 2018

By: /s/ RICHARD EISENSTADT

Richard Eisenstadt  
*Chief Financial Officer (Principal Financial Officer)*

**CERTIFICATION OF CHIEF EXECUTIVE OFFICER AND CHIEF FINANCIAL OFFICER  
PURSUANT TO  
18 U.S.C. SECTION 1350,  
AS ADOPTED PURSUANT TO  
SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002**

I, Vipin Garg, certify, pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that, to my knowledge, the Annual Report on Form 10-K of Neos Therapeutics, Inc. for the period ended December 31, 2016 fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934 and that information contained in such Annual Report on Form 10-K fairly presents, in all material respects, the financial condition and results of operations of Neos Therapeutics, Inc.

/s/ VIPIN GARG

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Vipin Garg  
*President and Chief Executive Officer*  
*(Principal Executive Officer)*  
March 16, 2018

I, Richard Eisenstadt, certify, pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that, to my knowledge, the Annual Report on Form 10-K of Neos Therapeutics, Inc. for the period ended December 31, 2016 fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934 and that information contained in such Annual Report on Form 10-K fairly presents, in all material respects, the financial condition and results of operations of Neos Therapeutics, Inc.

/s/ RICHARD EISENSTADT

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Richard Eisenstadt  
*Chief Financial Officer*  
*(Principal Financial Officer)*  
March 16, 2018

*The foregoing certifications are not deemed filed with the Securities and Exchange Commission for purposes of Section 18 of the Securities Exchange Act of 1934, as amended (Exchange Act), and are not to be incorporated by reference into any filing of Neos Therapeutics, Inc. under the Securities Act of 1933, as amended, or the Exchange Act, whether made before or after the date hereof, regardless of any general incorporation language in such filing.*