SPS COMMERCE INC
Form DEF 14A
April 01, 2019
Table of Contents

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

SCHEDULE 14A

Proxy Statement Pursuant to Section 14(a) of the

Securities Exchange Act of 1934

(Amendment No.)

Filed by the Registrant Filed by a Party other than the Registrant

Check the appropriate box:

Preliminary Proxy Statement

Confidential, for Use of the Commission Only (as permitted by Rule 14a-6(e)(2))

Definitive Proxy Statement

Definitive Additional Materials

Soliciting Material Pursuant to §240.14a-12

SPS Commerce, Inc.

(Name of Registrant as Specified In Its Charter)

(Name of Person(s) Filing Proxy Statement, if other than the Registrant)

Payment of Filing Fee (Check the appropriate box):

No fee required.

Fee computed on table below per Exchange Act Rules 14a-6(i)(1) and 0-11.

(1) Title of each class of securities to which transaction applies:

(2) Aggregate number of securities to which transaction applies:

(3) Per unit price or other underlying value of transaction computed pursuant to Exchange Act Rule 0-11 (set forth the amount on which the filing fee is calculated and state how it was determined):

(4) Proposed maximum aggregate value of transaction:

(5) Total fee paid:

Fee paid previously with preliminary materials.

Check box if any part of the fee is offset as provided by Exchange Act Rule 0-11(a)(2) and identify the filing for which the offsetting fee was paid previously. Identify the previous filing by registration statement number, or the Form or Schedule and the date of its filing.

(1) Amount Previously Paid:

(2) Form, Schedule or Registration Statement No.:

(3) Filing Party:

(4) Date Filed:

Table of Contents

333 South Seventh Street, Suite 1000

Minneapolis, Minnesota 55402

(612) 435-9400

April 1, 2019

Dear Stockholders:

You are cordially invited to join us for our 2019 annual meeting of stockholders, which will be held on Tuesday, May 14, 2019, at 8:00 a.m., Central Time, at 2200 Wells Fargo Center, 90 South Seventh Street, Minneapolis, Minnesota 55402. The notice of annual meeting of stockholders and the proxy statement that follow describe the business to be conducted at the meeting. Whether or not you plan to attend the meeting, your vote is important and we encourage you to vote your shares promptly. You may vote your shares using a toll-free telephone number, using the internet or you may sign, date and mail a proxy card which can be requested and mailed to you free of charge. Instructions regarding the three methods of voting are contained in the proxy materials.

We are pleased to take advantage of Securities and Exchange Commission (SEC) rules that allow companies to furnish their proxy materials over the internet. We are mailing to many of our stockholders a Notice of Internet Availability of Proxy Materials (the Notice) instead of a paper copy of our proxy materials and our 2018 Annual Report to Stockholders (the Annual Report). The Notice contains instructions on how to access those documents and to cast your vote via the internet. The Notice also contains instructions on how to request a paper copy of our proxy materials and our Annual Report. All stockholders who do not receive a Notice will receive a paper copy of the proxy materials and the Annual Report by mail. This process allows us to provide our stockholders with the information they need on a more timely basis, while reducing the environmental impact and lowering the costs of printing and distributing our proxy materials.

We look forward to seeing you at the annual meeting.

Sincerely,

Archie C. Black
President and Chief Executive Officer

Table of Contents

SPS Commerce, Inc.

333 South Seventh Street

Minneapolis, Minnesota 55402

Notice of 2019 Annual Meeting of Stockholders

Time and Date	Place
8:00 a.m., Central Daylight Time	2200 Wells Fargo Center
Tuesday, May 14, 2019	90 South Seventh Street
	Minneapolis, MN 55402

Items of Business

1. Election of the seven directors identified in the Proxy Statement, each for a one-year term.

2. Ratification of the selection of KPMG LLP as independent auditor of SPS Commerce, Inc. for the fiscal year ending December 31, 2019.

3. An advisory vote to approve the compensation of our named executive officers as disclosed in the attached proxy statement (a Say-on-Pay vote).

4. An advisory vote regarding the frequency of holding future Say-on-Pay votes.

5. Any other business that may properly be considered at the meeting or any adjournment or postponement of the meeting.

Record Date You may vote at the meeting if you were a stockholder of record at the close of business on March 20, 2019.

Voting by Proxy Whether or not you plan to attend the annual meeting, please vote your shares by proxy to ensure they are represented at the meeting. To submit your proxy vote, you may follow the instructions for voting via telephone or the internet as described in the Notice of Internet Availability of Proxy Materials and the following proxy statement. If you received a paper copy of the proxy card by mail, you may sign, date and mail the proxy card in the

envelope provided. Our vote tabulator is Broadridge Financial Solutions, Inc., and no postage is required if the request for a paper copy of the proxy materials is mailed in the United States.

By Order of the Board of Directors,

Archie C. Black

President and Chief Executive Officer

IMPORTANT NOTICE REGARDING THE AVAILABILITY OF PROXY MATERIALS FOR THE ANNUAL MEETING OF STOCKHOLDERS TO BE HELD ON MAY 14, 2019:

The Notice of Annual Meeting, Proxy Statement, and 2018 Annual Report are available at www.proxyvote.com.

Table of Contents

How to Vote

Whether or not you plan to attend the meeting, please provide your proxy by either using the Internet or telephone as further explained in this proxy statement or filling in, signing, dating, and promptly mailing a proxy card.

BY TELEPHONE

You will need to use a control number that was provided to you by our vote tabulator, Broadridge Financial Solutions.

Call the toll-free number on your Notice or proxy card, 24 hours a day, seven days a week, through 11:59 p.m. (ET) on May 13, 2019 for shares held directly, and through 11:59 p.m. (ET) on May 9, 2019 for shares held in a Plan.

Please have your Notice or proxy card available and follow the additional steps when prompted.

BY INTERNET

Go to the web site at www.proxyvote.com, 24 hours a day, seven days a week, through 11:59 p.m. (ET) on May 13, 2019 for shares held directly, and through 11:59 p.m. (ET) on May 9, 2019 for shares held in a Plan.

Please have your Notice or proxy card available and follow the instructions provided to obtain your records and to create an electronic voting instruction form.

BY MAIL

If you received a Notice, first request a paper copy of the proxy materials as directed in the Notice.

Mark, sign and date your proxy card.

Return it in the postage-paid envelope provided.

If your shares are held in an account at a brokerage firm, bank or similar organization, you will receive voting instructions from the organization holding your account and you must follow those instructions to vote your shares. You will receive a Notice Regarding the Availability of Proxy Materials that will tell you how to access our proxy materials on the Internet and vote your shares over the Internet. It will also tell you how to request a paper or e-mail copy of our proxy materials.

YOUR VOTE IS IMPORTANT. THANK YOU FOR VOTING.

Table of Contents

PROXY STATEMENT

TABLE OF CONTENTS

Table of Contents

PROXY SUMMARY

This summary highlights information contained elsewhere in this proxy statement. We encourage you to review the entire proxy statement. This proxy statement and our Annual Report for the year ended December 31, 2018 are first being mailed to our shareholders on or about April 1, 2019. Website addresses included throughout this proxy statement are for reference only. The information contained on our website is not incorporated by reference into this proxy statement.

Business Results

We are a technology company with $248.2 million in annual revenues. We are a leading provider of cloud-based supply chain management solutions, providing network-proven integrations and comprehensive retail performance analytics to thousands of customers worldwide.

2018 was a year of continued execution for SPS Commerce, in an industry that is in transition. We achieved year-over-year recurring revenue growth, customer growth and wallet share growth and delivered strong revenue and adjusted EBITDA growth in 2018. We also executed two strategic acquisitions and continued to repurchase shares through our buyback program. Additional information regarding our performance in 2018 follows.

We had sequential revenue growth for all four quarters of 2018 and we now have 72 consecutive quarters of sequential revenue growth.

Our revenues of $248.2 million for 2018, compared to $220.1 million for 2017, reflect 13% growth from 2017. Recurring revenue grew 13% from 2017.

Our average recurring revenue per recurring revenue customer increased 4% from 2017, and the number of recurring revenue customers grew 14% from 2017.

We achieved improvements in operational efficiency that produced Adjusted EBITDA of $51.3 million, compared to $34.2 million in 2017, and non-GAAP net income per diluted share of $1.93 in 2018 compared to $1.02 in 2017.[1]

[1.] Adjusted EBITDA, Non-GAAP income and non-GAAP income per diluted share are non-GAAP financial measures. Refer to Appendix A in this proxy statement for a reconciliation of these non-GAAP financial measures to the corresponding GAAP measures.

Table of Contents

Voting Matters and Voting Recommendations

The following proposals are included in this proxy statement and are scheduled to be voted on at the meeting. Our board of directors recommends that you vote your shares as indicated below.

PROPOSALS:	THE BOARD OF DIRECTOR S VOTING RECOMMENDATIONS:	RATIONALE FOR SUPPORT:	FOR FURTHER DETAILS:
1. Election of the seven directors identified in this Proxy Statement, each for a term of one year.	FOR each nominee to the Board	Our nominees are distinguished leaders who bring a mix of skills and qualifications to our board of directors and can represent the interests of all stockholders.	Page 7
2. Ratification of the selection of KPMG LLP (KPMG) as independent auditor of SPS Commerce, Inc. for the fiscal year ending December 31, 2019.	FOR	Based on its assessment of the qualifications and performance of KPMG, the Audit Committee believes that it is in the best interests of the company and its stockholders to retain KPMG.	Page 37
3. An advisory vote to approve the compensation of our named executive officers (a Say-on-Pay vote).	FOR	Our executive compensation program is designed to attract and retain talented and highly experienced executives and to motivate our executives to achieve the goals that are important to the company s growth.	Page 38
4. An advisory vote regarding the frequency of holding future Say-on-Pay votes.	1 YEAR	The board of directors believes holding an annual advisory Say-on-Pay vote is a best practice and is consistent with our current practice.	Page 39

Other than the proposals described in this proxy statement, the board is not aware of any other matters to be presented for a vote at the annual meeting. If you grant a proxy by telephone, internet, or by signing and returning your proxy card, any of the persons appointed by the board as proxy holders will have the discretion to vote your shares on any additional matters properly presented for a vote at the meeting. If any of our nominees is unavailable as a candidate for director, the above-named proxy holders will vote your proxy for another candidate or candidates as may be nominated by the board of directors.

Table of Contents

QUESTIONS AND ANSWERS ABOUT THE ANNUAL MEETING AND VOTING

The board of directors of SPS Commerce, Inc. is soliciting proxies for use at the annual meeting of stockholders to be held on May 14, 2019, and at any adjournment or postponement of the meeting.

Purpose of the Annual Meeting

At our annual meeting, stockholders will act upon the matters outlined in the Notice of Annual Meeting of Stockholders, and management will report on matters of current interest to our stockholders and respond to questions from our stockholders. The matters outlined in the notice include the election of directors, the ratification of the selection of our independent auditor for 2019, an advisory vote to approve the compensation of our named executive officers (a Say-on-Pay vote), and an advisory vote on the frequency of holding future Say-on-Pay votes.

Annual Meeting Voting Rights and Attendance

Who is entitled to vote at the meeting?

The board of directors has set March 20, 2019 as the record date for the annual meeting. If you were a stockholder of record at the close of business on March 20, 2019, you are entitled to vote at the meeting. As of the record date, 17,470,443 shares of common stock, representing all of our voting stock, were issued and outstanding and, therefore, eligible to vote at the meeting.

What are my voting rights?

Holders of our common stock are entitled to one vote per share. Therefore, a total of 17,470,443 votes are entitled to be cast at the meeting. There is no cumulative voting.

How many shares must be present to hold the meeting?

In accordance with our bylaws, shares equal to a majority of the voting power of the outstanding shares of common stock entitled to vote generally in the election of directors as of the record date must be present at the annual meeting in order to hold the meeting and conduct business. This is called a quorum. Shares are counted as present at the meeting if:

- you are present and vote in person at the meeting; or

you have properly and timely submitted your proxy as described below under How do I submit my proxy?

What is the difference between a stockholder of record and a street name holder?

If your shares are registered directly in your name, you are considered the stockholder of record with respect to those shares. If your shares are held in a stock brokerage account or by a bank, trust or other nominee, then the broker, bank, trust or other nominee is considered to be the stockholder of record with respect to those shares, while you are considered the beneficial owner of those shares. In that case, your shares are said to be held in street name. Street name holders generally cannot vote their shares directly and must instead instruct the broker, bank, trust or other nominee how to vote their shares using the method described below under How do I submit my proxy?

Table of Contents

How can I attend the meeting?

All of our stockholders are invited to attend the annual meeting. You may be asked to present valid photo identification, such as a driver s license or passport, before being admitted to the meeting. If you hold your shares in street name, you also may be asked to present proof of ownership to be admitted to the meeting. A brokerage statement or letter from your broker, bank, trust or other nominee are examples of proof of ownership.

Information about the Notice and Proxy Materials

What is a proxy?

It is your designation of another person to vote stock you own. That other person is called a proxy. If you designate someone as your proxy in a written document, that document also is called a proxy or a proxy card. When you designate a proxy, you also may direct the proxy how to vote your shares. We refer to this as your proxy vote. Two executive officers have been designated as proxies for our 2019 annual meeting of stockholders. These executive officers are Archie C. Black and Kimberly K. Nelson.

If I received a one-page Notice of Internet Availability of Proxy Materials, how can I receive a full set of printed proxy materials?

As permitted by SEC rules, we have elected to provide access to our proxy materials over the Internet to record owners and any beneficial owners of our stock who have not previously requested printed proxy materials, which reduces our costs and the environmental impact of our annual meeting. The Notice of Availability contains instructions on how to request a printed set of proxy materials, which we will provide to stockholders upon request at no cost to the requesting stockholder within three business days after receiving the request.

How do I submit my proxy?

If you are a stockholder of record, you can submit a proxy to be voted at the meeting in any of the following ways:

over the internet using www.proxyvote.com,

over the telephone by calling a toll-free number; or

signing, dating and mailing the proxy card in the envelope provided.

To vote by telephone or the internet, you will need to use a control number that was provided to you by our vote tabulator, Broadridge Financial Solutions, and then follow the additional steps when prompted. The steps have been designed to authenticate your identity, allow you to give voting instructions, and confirm that those instructions have been recorded properly. If you hold your shares in street name, you must vote your shares in the manner prescribed by your broker, bank, trust or other nominee, which is similar to the voting procedures for stockholders of record. If you request the proxy materials by mail after receiving a Notice of Internet Availability of Proxy Material, you will receive a voting instruction form (not a proxy card) to use in directing the broker, bank, trust or other nominee how to vote your shares.

What does it mean if I receive more than one printed set of proxy materials?

If you receive more than one Notice of Internet Availability of Proxy Materials or printed set of proxy materials, it means that you hold shares registered in more than one account. To ensure that all of your shares are voted, vote once for each control number you receive as described above under How do I submit my proxy?

Who pays for the cost of proxy preparation and solicitation?

SPS Commerce pays for the cost of proxy preparation and solicitation, including the reasonable charges and expenses of brokerage firms, banks, trusts or other nominees for forwarding proxy materials to street name holders. We are soliciting proxies by mail. In addition, our directors, officers and regular employees may solicit

Table of Contents

proxies personally, telephonically, electronically or by other means of communication. Our directors, officers and regular employees will receive no additional compensation for their services other than their regular compensation.

Voting

How does the board of directors recommend that I vote?

The board of directors recommends a vote:

FOR the election of each of the nominees for director;

FOR the ratification of the selection of KPMG as the independent auditor of SPS Commerce, Inc. for the year ending December 31, 2019;

FOR advisory approval of the compensation of our named executive officers; and

1 YEAR for the advisory vote regarding the frequency of holding future Say-on-Pay votes.

What if I do not specify how I want my shares voted?

If you are a stockholder of record and submit a signed proxy card or submit your proxy by internet or telephone but do not specify how you want to vote your shares on a particular matter, we will vote your shares as follows:

FOR the election of each of the nominees for director;

FOR the ratification of the selection of KPMG as the independent auditor of SPS Commerce, Inc. for the year ending December 31, 2019;

FOR advisory approval of the compensation of our named executive officers; and

1 YEAR for the advisory vote regarding the frequency of holding future Say-on-Pay votes.

Your vote is important. We urge you to vote, or to instruct your broker, bank, trust or other nominee how to vote, on all matters before the annual meeting. If you are a street name holder and fail to instruct the stockholder of record how you want to vote your shares on a particular matter, those shares are considered to be uninstructed. New York Stock Exchange rules determine the circumstances under which member brokers of the New York Stock Exchange may exercise discretion to vote uninstructed shares held by them on behalf of their clients who are street name holders. Other than the ratification of the selection of KPMG as our independent auditor for the year ending December 31, 2019, the rules do *not* permit member brokers to exercise voting discretion as to the uninstructed shares on any matter included in the notice of meeting. With respect to the ratification of the selection of KPMG as our independent auditor for the year ending December 31, 2019, the rules permit member brokers to exercise voting discretion as to the uninstructed shares. For matters with respect to which the broker, bank or other nominee does not have voting discretion or has, but does not exercise, voting discretion, the uninstructed shares will be referred to as a broker non-vote. For more information regarding the effect of broker non-votes on the outcome of the vote, see below under How are votes counted?

Can I change my vote after submitting my proxy?

Yes. You may revoke your proxy and change your vote at any time before your proxy is voted at the annual meeting, in any of the following ways:

by submitting a later-dated proxy by telephone or the internet before 11:59 p.m. Eastern Time on Monday, May 13, 2019 for shares held directly and before 11:59 p.m. Eastern Time on Thursday, May 9, 2019 for shares held in a Plan;

by submitting a later-dated proxy to the Chief Financial Officer of SPS Commerce, Inc., which must be received by us before the time of the annual meeting;

Table of Contents

by sending a written notice of revocation to the Chief Financial Officer of SPS Commerce, Inc., which must be received by us before the time of the annual meeting; or

by voting in person at the meeting.

Can I vote my shares in person at the meeting?

If you are a stockholder of record, you may vote your shares in person at the meeting by completing a ballot at the meeting. Even if you currently plan to attend the meeting, we recommend that you submit your proxy as described above so your vote will be counted if you later decide not to attend the meeting. If you submit your vote by proxy and later decide to vote in person at the annual meeting, the vote you submit at the meeting will override your proxy vote.

If you are a street name holder, you may vote your shares in person at the meeting only if you obtain and bring to the meeting a signed letter or other form of proxy from your broker, bank, trust or other nominee giving you the right to vote the shares at the meeting.

What vote is required to approve each item of business included in the notice of meeting?

A director nominee will be elected if the number of votes cast FOR the nominee exceeds the number of votes cast AGAINST the nominee. Any incumbent director who does not receive a greater number of votes FOR than AGAINST his or her reelection in an uncontested election shall tender his or her resignation to the board of directors, subject to acceptance by the board of directors. The board of directors will determine whether to accept or reject the offer to resign within 90 days of certification of the stockholder vote.

The affirmative vote of the holders of a majority of the outstanding shares of common stock present in person or represented by proxy and entitled to vote at the annual meeting is required to ratify the selection of our independent auditor.

For the advisory vote to approve the executive compensation of our named executive officers and the advisory vote regarding the frequency of future Say-on-Pay votes, there is no minimum approval necessary for either proposal since these are advisory votes; however, the board of directors will consider the results of the advisory votes when considering future decisions related to such proposals.

How are votes counted?

You may vote FOR, AGAINST OR ABSTAIN for each director nominee and on the other proposals other than the proposal regarding the frequency of holding future Say-on-Pay votes. You may vote 1 YEAR, 2 YEARS, 3 YEARS or ABSTAIN on the advisory vote regarding the frequency of holding future Say-on-Pay votes. If you properly submit your proxy but abstain from voting for a director nominee or on these other proposals, your shares will be counted as present at the meeting for the purpose of determining a quorum and for the purpose of calculating the vote on the particular matter(s) with respect to which you abstained from voting. If you do not submit your proxy or voting instructions and also do not vote by ballot at the annual meeting, your shares will not be counted as present at the meeting for the purpose of determining a quorum unless you hold your shares in street name and the broker, bank, trust or other nominee has discretion to vote your shares and does so. For more information regarding discretionary voting, see the information above under What if I do not specify how I want my shares voted?

If you abstain from voting for one or more of the director nominees or you do not vote your shares on this matter (whether by broker non-vote or otherwise), this will have no effect on the outcome of the vote. With respect to the

proposal to ratify the selection of KPMG as our independent auditor, if you abstain from voting, doing so will have the same effect as a vote against the proposal, but if you do not vote your shares (or, for shares held in street name, if you do not submit voting instructions and your broker, bank, trust or other nominee does not or may not vote your shares), this will have no effect on the outcome of the vote. Abstentions and broker non-votes will have no effect on the advisory vote to approve the compensation of our named executive officers or the advisory vote regarding the frequency of holding future Say-on-Pay votes.

Table of Contents

ITEM 1 ELECTION OF DIRECTORS

Our Amended and Restated Bylaws provide that each member of our board of directors is elected annually by a majority of votes cast if the election is uncontested. The number of directors currently serving on our board of directors is nine. Messrs. Keating and McConnell will not be standing for re-election at our annual meeting, and the size of our board of directors will be decreased to seven on the date of the meeting. Upon recommendation of the governance and nominating committee, the board has nominated the seven directors set forth below for election at our annual meeting, and all have agreed to serve as directors if elected. All of the director nominees were elected by our stockholders at our 2018 annual meeting of stockholders.

If, for any reason, any nominee becomes unable to serve before the annual meeting occurs, the persons named as proxies may vote your shares for a substitute nominee selected by our board of directors. The director nominees, if reelected, will serve until our 2020 annual meeting of stockholders or until their successors are elected and qualified.

The board of directors recommends a vote FOR the election of each of the seven director nominees. Proxies will be voted FOR the election of each of the nominees unless otherwise specified.

Set forth below is biographical information for each of the director nominees. The following includes certain information regarding our directors individual experience, qualifications, attributes and skills that led the board of directors to conclude that they should serve as directors.

Nominees for Director

Archie C. Black

President, Chief Executive Officer of SPS Commerce, Inc.

Age	56
Director since	2001
SPS Board committee	Ex-officio member of Finance and Strategy
Independent	No

Professional Highlights

Mr. Black has served as President and Chief Executive Officer of SPS Commerce, Inc. since 2001. Mr. Black joined us in 1998 as our Senior Vice President and Chief Financial Officer and served in those capacities until becoming our President and Chief Executive Officer. Prior to joining us, Mr. Black was a Senior Vice President and Chief Financial Officer at Investment Advisors, Inc. in Minneapolis, Minnesota, where he directed both the Minneapolis and London organizations. Prior to Investment Advisors, he spent three years at Price Waterhouse. Mr. Black serves on the board of directors of Proto Labs, Inc., a publicly traded internet-enabled manufacturer of custom parts.

Nominee Qualifications

Mr. Black s qualifications to serve on our board of directors include, among other skills and qualifications, his extensive management, financial, and operational experience as well as his experience with our company.

Table of Contents

Martin J. Leestma

Chairman of the board of directors of Forthright Solutions

Age	60
Director since	2006
SPS Board committees	Audit; Finance and Strategy
Independent	Yes

Professional Highlights

Mr. Leestma has served as Chairman of the board of directors for Forthright Solutions, a solution provider for regulatory and legal compliance programs, since 2008. He served as Chief Executive Officer of Forthright from 2011 to 2014. Prior to Forthright, Mr. Leestma served as the President, Chief Executive Officer, and a member of the board of directors for Retek Information Systems, a software company, from 2003 to 2005, during which time Retek was a publicly traded company. Prior to joining Retek, Mr. Leestma was Global Managing Partner of Retail Technology at Accenture from 1996 to 1999 and Managing Partner of North American Consumer Goods & Services from 1999 to 2002. He became Global Industry Managing Partner Retail & CG&S Industries in 2002 and served in this role until his departure in 2003. From 2005 to 2008, he served as an independent business consultant. Mr. Leestma also serves on the board of directors for Kipsu, a private texting and digital messaging company, and Xsell Technologies, a private digital dialogue company. Mr. Leestma was Chairman of the board of directors of SPS Commerce from March 2011 to May 2014.

Nominee Qualifications

Mr. Leestma s qualifications to serve on our board of directors include, among other skills and qualifications, his general business experience due to his work as an independent business consultant and his experience with public companies as the Chief Executive Officer of Retek Information Systems from 2003 to 2005.

James B. Ramsey

Co-founder and board member, Vlocity Inc.

Age	46
Director since	2014
SPS Board committees	Compensation; Governance and Nominating
Independent	Yes

Professional Highlights

Mr. Ramsey co-founded and has served as board member of Vlocity Inc., a provider of industry-specific cloud CRM applications, since 2014. Mr. Ramsey also serves on the boards of Ambra Health (formerly DicomGrid), a privately-held company. Previously, Mr. Ramsey served as the Executive Vice President of Worldwide Sales and Distribution at NetSuite Inc., a publicly traded provider of cloud-based business management software, from 2011 to 2013. Prior to his position as Executive Vice President, Mr. Ramsey held several senior executive roles at NetSuite, including Vice President of the Americas and Senior Vice President of Worldwide Sales and Distribution. Prior to

NetSuite Inc., Mr. Ramsey served in various sales management roles at Oracle Corporation.

Nominee Qualifications

Mr. Ramsey s qualifications to serve on our board of directors include, among other skills and qualifications, his experience in software sales and in rapidly scaling sales organizations with NetSuite Inc. and Oracle Corporation.

Table of Contents

Marty M. Reaume

Chief People Officer, Twilio, Inc.

Age	53
Director since	2018
SPS Board committee	Compensation; Governance and Nominating
Independent	Yes

Professional Highlights

Ms. Reaume has served since 2017 as Chief People Officer of Twilio Inc., a publicly traded developer and provider of a cloud-based platform enabling organizations to integrate voice, messaging and video communications capabilities into their software applications. From 2015 to 2017, she served as Chief People Officer of Fitbit, Inc., a publicly traded technology company focused on delivering health solutions that impact health outcomes. Ms. Reaume served as Chief People Officer of NetSuite, Inc., a publicly traded provider of cloud-based business management software, from 2009 to 2014, and served as its head of human resources from 2006 to 2009. Prior to that, Ms. Reaume served as director of human resources at Royal & Sunalliance, a multinational insurance company, from 2001 to 2005.

Nominee Qualifications

Ms. Reaume s qualifications to serve on our board of directors include, among other skills and qualifications, her strong human resources, talent acquisition and talent development expertise.

Tami L. Reller

Executive Vice President and Chief Marketing and Experience Officer at UnitedHealthcare, a division of UnitedHealth Group

Age	54
Director since	2016
SPS Board committee	Finance and Strategy
Independent	Yes

Professional Highlights

Ms. Reller has served as Executive Vice President and Chief Marketing and Experience Officer of UnitedHealthcare, the health benefits platform of UnitedHealth Group, since November 2017. From April 2017 to November 2017, Ms. Reller served as Chief Growth Officer of Optum, and from June 2016 to April 2017 she served as Chief Financial Officer of Optum, the health service platform of UnitedHealth Group. From April 2001 until September 2014, Ms. Reller served in several executive roles with Microsoft Corporation including Executive Vice President of Marketing, Windows Chief Financial Officer and Chief Marketing Officer, Divisional Chief Financial Officer and Corporate Vice President of Dynamics. She was also the Chief Financial Officer of Great Plains Software from 1999 to 2001, until the company was acquired by Microsoft Corporation. Since May of 2018, Ms. Reller has served as Chairwoman of our board of directors.

Nominee Qualifications

Ms. Reller s qualifications to serve on our board of directors include, among other skills and qualifications, her extensive experience steering and managing software companies, her capabilities in financial understanding and auditing review, and her general business knowledge.

Table of Contents

Philip E. Soran

Lead Director, Piper Jaffray Companies; Director, Foodsby; Director, Spineology

Age	62
Director since	2010
SPS Board committees	Audit; Compensation; Finance and Strategy
Independent	Yes

Professional Highlights

Mr. Soran serves as Lead Director on the board of directors of Piper Jaffray Companies, a publicly traded investment bank and asset management firm, on the board of directors for Foodsby, a privately-held food delivery service, and on the board of directors of Spineology, a private medical technology company. Mr. Soran was the Executive Chairman and co-founder of Flipgrid, Inc., a privately-held education technology software company, from January 2015 until its sale to Microsoft in June 2018. Mr. Soran served as President, Chief Executline; FONT-FAMILY: times new roman; FONT-SIZE: 10pt">

Weighted average number of common shares outstanding used in computing basic and diluted net loss per common share

106,609,720 71,669,170

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

Back to Table of Contents

PALATIN TECHNOLOGIES, INC.
and Subsidiary
Consolidated Statements of Cash Flows
(unaudited)

	Three Months Ended September 30,	
	2013	2012
CASH FLOWS FROM OPERATING ACTIVITIES:		
Net loss	$(4,489,182)	$(10,452,979)
Adjustments to reconcile net loss to net cash used in operating activities:		
Depreciation and amortization	27,242	27,467
Accrued interest and amortization on premium/discount	(272)	-
Gain on sale of supplies and equipment	-	(4,620)
Stock-based compensation	203,636	176,103
Increase in fair value of warrants	-	7,069,165
Changes in operating assets and liabilities:		
Accounts receivable	-	(3,806)
Prepaid expenses and other assets	80,770	296,410
Accounts payable	652,172	26,727
Accrued expenses and deferred rent	480,389	(1,863,919)
Unearned revenue	1,000,000	-
Net cash used in operating activities	(2,045,245)	(4,729,452)
CASH FLOWS FROM INVESTING ACTIVITIES:		
Proceeds from sale/maturity of investments	1,500,000	-
Proceeds from sale of supplies and equipment	-	4,620
Purchases of property and equipment	(6,239)	(8,550)
Net cash provided by (used in) investing activities	1,493,761	(3,930)
CASH FLOWS FROM FINANCING ACTIVITIES:		
Payments on capital lease obligations	(5,841)	(5,411)
Payment of withholding taxes related to restricted stock units	(25,214)	(34,785)
Proceeds from sale of common stock units	-	34,407,446
Net cash (used in) provided by financing activities	(31,055)	34,367,250
NET (DECREASE) INCREASE IN CASH AND CASH EQUIVALENTS	(582,539)	29,633,868
CASH AND CASH EQUIVALENTS, beginning of period	19,167,632	3,827,198
CASH AND CASH EQUIVALENTS, end of period	$18,585,093	$33,461,066
SUPPLEMENTAL CASH FLOW INFORMATION:		
Cash paid for interest	$1,851	$2,013

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

Back to Table of Contents

PALATIN TECHNOLOGIES, INC.
and Subsidiary
Notes to Consolidated Financial Statements
(unaudited)

(1) ORGANIZATION:

Nature of Business – Palatin Technologies, Inc. (Palatin or the Company) is a biopharmaceutical company developing targeted, receptor-specific peptide therapeutics for the treatment of diseases with significant unmet medical need and commercial potential. Palatin's programs are based on molecules that modulate the activity of the melanocortin and natriuretic peptide receptor systems. The melanocortin system is involved in a large and diverse number of physiologic functions, and therapeutic agents modulating this system may have the potential to treat a variety of conditions and diseases, including sexual dysfunction, obesity and related disorders, cachexia (wasting syndrome) and inflammation-related diseases. The natriuretic peptide receptor system has numerous cardiovascular functions, and therapeutic agents modulating this system may be useful in treatment of acute asthma, heart failure, hypertension and other cardiovascular diseases.

The Company's primary product in development is bremelanotide for the treatment of female sexual dysfunction (FSD). The Company also has drug candidates or development programs for obesity, erectile dysfunction, pulmonary diseases, cardiovascular diseases, dermatologic diseases and inflammatory diseases. The Company has an exclusive global research collaboration and license agreement with AstraZeneca AB (AstraZeneca) to commercialize compounds that target melanocortin receptors for the treatment of obesity, diabetes and related metabolic syndrome.

Key elements of the Company's business strategy include using its technology and expertise to develop and commercialize therapeutic products; entering into alliances and partnerships with pharmaceutical companies to facilitate the development, manufacture, marketing, sale and distribution of product candidates that the Company is developing; and partially funding its product candidate development programs with the cash flow generated from the Company's license agreements with AstraZeneca and any other companies.

Business Risk and Liquidity – The Company has incurred negative cash flows from operations since its inception, and has expended, and expects to continue to expend in the future, substantial funds to complete its planned product development efforts. As shown in the accompanying consolidated financial statements, the Company has an accumulated deficit as of September 30, 2013 of $264.6 million and incurred a net loss for the three months ended September 30, 2013 of $4.5 million. The Company anticipates incurring additional losses in the future as a result of spending on its development programs. To achieve profitability, the Company, alone or with others, must successfully develop and commercialize its technologies and proposed products, conduct successful preclinical studies and clinical trials, obtain required regulatory approvals and successfully manufacture and market such technologies and proposed products. The time required to reach profitability is highly uncertain, and there can be no assurance that the Company will be able to achieve profitability on a sustained basis, if at all.

As of September 30, 2013, the Company's cash, cash equivalents and short-term investments were $22.3 million. The Company intends to utilize existing capital resources for general corporate purposes and working capital, including preparing for the Phase 3 clinical trial program with bremelanotide for female sexual dysfunction (FSD), preclinical development of its peptide melanocortin receptor-1 program, preclinical and clinical development of its PL-3994 program and preclinical development of other portfolio products. Management believes that the Phase 3 clinical trial program with bremelanotide will cost at least $78.0 million. The Company does not intend to initiate patient enrollment in the Phase 3 program unless the Company has adequate funds, or commitments for adequate funds, to complete the Phase 3 program. The Company intends to seek additional capital to support the Phase 3 program through collaborative arrangements on bremelanotide, public or private equity or debt financings, or other sources.

Management believes that the Company's existing capital resources will be adequate to fund its currently planned operations, including submitting complete protocols for pivotal Phase 3 studies to the U.S. Food and Drug Administration (FDA) but not initiating patient enrollment, through at least calendar year 2014.

Concentrations – Concentrations in the Company's assets and operations subject it to certain related risks. Financial instruments that subject the Company to concentrations of credit risk primarily consist of cash, cash equivalents and short-term investments. The Company's cash and cash equivalents are primarily in one money market fund sponsored by a large financial institution and the Company's short-term investments are invested in U.S. government securities. For the three months ended September 30, 2012, 100% of revenues were from AstraZeneca.

Back to Table of Contents

PALATIN TECHNOLOGIES, INC.
and Subsidiary
Notes to Consolidated Financial Statements
(unaudited)

(2) BASIS OF PRESENTATION:

The accompanying unaudited consolidated financial statements have been prepared in accordance with U.S. generally accepted accounting principles for interim financial information and with the instructions to Form 10-Q. Accordingly, they do not include all of the information and footnote disclosures required to be presented for complete financial statements. In the opinion of management, these consolidated financial statements contain all adjustments (consisting of normal recurring adjustments) considered necessary to present fairly the Company's financial position as of September 30, 2013, and its results of operations and its cash flows for the three months ended September 30, 2013 and 2012. The results of operations for the three months ended September 30, 2013 may not necessarily be indicative of the results of operations expected for the full year, except that the Company expects to incur a significant loss for the fiscal year ending June 30, 2014.

The accompanying consolidated financial statements should be read in conjunction with the audited consolidated financial statements and notes thereto included in the Company's annual report on Form 10-K for the year ended June 30, 2013, filed with the Securities and Exchange Commission (SEC), which includes consolidated financial statements as of June 30, 2013 and 2012 and for each of the fiscal years in the three-year period ended June 30, 2013.

(3) SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES:

Principles of Consolidation – The consolidated financial statements include the accounts of Palatin and its wholly-owned inactive subsidiary. All intercompany accounts and transactions have been eliminated in consolidation.

Use of Estimates – The preparation of consolidated financial statements in conformity with U.S. generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amount of assets and liabilities and disclosure of contingent assets and liabilities at the date of the consolidated financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

Cash and Cash Equivalents – Cash and cash equivalents include cash on hand, cash in banks and all highly liquid investments with a purchased maturity of less than three months. Cash equivalents consist of $15,679,545 in a money market fund at September 30, 2013 and $16,284,184 in a money market fund at June 30, 2013.

Investments – The Company determines the appropriate classification of its investments in debt and equity securities at the time of purchase and reevaluates such determinations at each balance sheet date. Debt securities are classified as held-to-maturity when the Company has the intent and ability to hold the securities to maturity. Debt securities for which the Company does not have the intent or ability to hold to maturity are classified as available-for-sale. Held-to-maturity securities are recorded as either short-term or long-term on the balance sheet, based on the contractual maturity date and are stated at amortized cost. Marketable securities that are bought and held principally for the purpose of selling them in the near term are classified as trading securities and are reported at fair value, with unrealized gains and losses recognized in earnings. Debt and marketable equity securities not classified as held-to-maturity or as trading are classified as available-for-sale and are carried at fair market value, with the unrealized gains and losses, net of tax, included in the determination of comprehensive loss.

The fair value of substantially all securities is determined by quoted market prices. The estimated fair value of securities for which there are no quoted market prices is based on similar types of securities that are traded in the market.

Fair Value of Financial Instruments – The Company's financial instruments consist primarily of cash equivalents, short-term investments, accounts receivable, accounts payable, and capital lease obligations. Management believes that the carrying value of these assets and liabilities are representative of their respective fair values based on quoted market prices for investments and the short-term nature of the other instruments.

Property and Equipment – Property and equipment consists of office and laboratory equipment, office furniture and leasehold improvements and includes assets acquired under capital leases. Property and equipment are recorded at cost. Depreciation is recognized using the straight-line method over the estimated useful lives of the related assets, generally five years for laboratory and computer equipment, seven years for office furniture and equipment and the lesser of the term of the lease or the useful life for leasehold improvements. Amortization of assets acquired under capital leases is included in depreciation expense. Maintenance and repairs are expensed as incurred while expenditures that extend the useful life of an asset are capitalized.

Back to Table of Contents

PALATIN TECHNOLOGIES, INC.
and Subsidiary
Notes to Consolidated Financial Statements
(unaudited)

Impairment of Long-Lived Assets – The Company reviews its long-lived assets for impairment whenever events or changes in circumstances indicate that the carrying amount of the assets may not be fully recoverable. To determine recoverability of a long-lived asset, management evaluates whether the estimated future undiscounted net cash flows from the asset are less than its carrying amount. If impairment is indicated, the long-lived asset would be written down to fair value. Fair value is determined by an evaluation of available price information at which assets could be bought or sold, including quoted market prices if available, or the present value of the estimated future cash flows based on reasonable and supportable assumptions.

Deferred Rent – The Company's operating leases provide for rent increases over the terms of the leases. Deferred rent consists of the difference between periodic rent payments and the amount recognized as rent expense on a straight-line basis, as well as tenant allowances for leasehold improvements. Rent expenses are being recognized ratably over the terms of the leases.

Revenue Recognition – Revenue from corporate collaborations and licensing agreements consists of up-front fees, research and development funding, and milestone payments. Non-refundable up-front fees are deferred and amortized to revenue over the related performance period. The Company estimates the performance period as the period in which it performs certain development activities under the applicable agreement. Reimbursements for research and development activities are recorded in the period that the Company performs the related activities under the terms of the applicable agreements. Revenue resulting from the achievement of milestone events stipulated in the applicable agreements is recognized when the milestone is achieved, provided that such milestone is substantive in nature. Revenue from grants is recognized as the Company provides the services stipulated in the underlying grants based on the time and materials incurred.

During the three months ended September 30, 2013, the Company received a $1.0 million, non-refundable option fee relating to negotiation of a potential future license of bremelanotide in a defined territory outside North America for the treatment of FSD. Subject to certain contingencies, if not exercised, the option expires in the first calendar quarter of 2014. This payment, which is creditable against any upfront or initial license fee in the event of negotiation of a definitive license agreement, was recorded as unearned revenue as of September 30, 2013.

Research and Development Costs – The costs of research and development activities are charged to expense as incurred, including the cost of equipment for which there is no alternative future use.

Accrued Expenses – Third parties perform a significant portion of our development activities. We review the activities performed under significant contracts each quarter and accrue expenses and the amount of any reimbursement to be received from our collaborators based upon the estimated amount of work completed. Estimating the value or stage of completion of certain services requires judgment based on available information.

Stock-Based Compensation – The Company charges to expense the fair value of stock options and other equity awards granted. The Company determines the value of stock options utilizing the Black-Scholes option pricing model. Compensation costs for share-based awards with pro rata vesting are allocated to periods on a straight-line basis.

Income Taxes – The Company and its subsidiary file consolidated federal and separate-company state income tax returns. Income taxes are accounted for under the asset and liability method. Deferred tax assets and liabilities are recognized for the future tax consequences attributable to differences between the financial statement carrying

amounts of assets and liabilities and their respective tax basis and operating loss and tax credit carryforwards. Deferred tax assets and liabilities are measured using enacted tax rates expected to apply to taxable income in the years in which those temporary differences or operating loss and tax credit carryforwards are expected to be recovered or settled. The effect on deferred tax assets and liabilities of a change in tax rates is recognized in the period that includes the enactment date. The Company has recorded a valuation allowance against its deferred tax assets based on the history of losses incurred.

Net Loss per Common Share – Basic and diluted earnings per common share (EPS) are calculated in accordance with the provisions of Financial Accounting Standards Board (FASB) Accounting Standards Codification (ASC) Topic 260, “Earnings per Share,” which includes guidance pertaining to the warrants, issued in connection with the July 3, 2012 private placement offering, that are exercisable for nominal consideration and, therefore, are to be considered in the computation of basic and diluted net loss per common share. The Series A 2012 warrants to purchase up to 31,988,151 shares of common stock were exercisable starting at July 3, 2012 and, therefore, are included in the weighted average number of common shares outstanding used in computing basic and diluted net loss per common share starting on July 3, 2012.

Back to Table of Contents

PALATIN TECHNOLOGIES, INC.
and Subsidiary
Notes to Consolidated Financial Statements
(unaudited)

The Series B 2012 warrants to purchase up to 35,488,380 shares of common stock were considered contingently issuable shares and were not included in computing basic net loss per common share until the Company received stockholder approval for the increase in authorized underlying common stock on September 27, 2012 (see note 6). For diluted EPS, contingently issuable shares are to be included in the calculation as of the beginning of the period in which the conditions were satisfied, unless the effect would be anti-dilutive. The Series B 2012 warrants have been excluded from the calculation of diluted net loss per common share during the period from July 3, 2012 until September 27, 2012 as the impact would be anti-dilutive.

As of September 30, 2013 and 2012, common shares issuable upon conversion of Series A Convertible Preferred Stock, the exercise of outstanding options and warrants (excluding the warrants issued in connection with the July 3, 2013 private placement offering), and the vesting of restricted stock units amounted to an aggregate of 28,677,356 and 27,904,284 shares, respectively. These share amounts have been excluded from the calculation of net loss per share as the impact would be anti-dilutive.

(4) AGREEMENT WITH ASTRAZENECA:

In January 2007, the Company entered into an exclusive global research collaboration and license agreement with AstraZeneca to discover, develop and commercialize compounds that target melanocortin receptors for the treatment of obesity, diabetes and related metabolic syndrome. In June 2008, the license agreement was amended to include additional compounds and associated intellectual property developed by the Company. In December 2008, the license agreement was further amended to include additional compounds and associated intellectual property developed by the Company and extended the research collaboration for an additional year through January 2010. In September 2009, the license agreement was further amended to modify royalty rates and milestone payments. The collaboration is based on the Company’s melanocortin receptor obesity program and includes access to compound libraries, core technologies and expertise in melanocortin receptor drug discovery and development. As part of the September 2009 amendment to the research collaboration and license agreement, the Company agreed to conduct additional studies on the effects of melanocortin receptor specific compounds on food intake, obesity and other metabolic parameters.

In December 2009 and 2008, the Company also entered into clinical trial sponsored research agreements with AstraZeneca, under which the Company agreed to conduct studies of the effects of melanocortin receptor specific compounds on food intake, obesity and other metabolic parameters. Under the terms of these clinical trial agreements, AstraZeneca paid $5,000,000 as of March 31, 2009 upon achieving certain objectives and paid all costs associated with these studies. The Company recognized $3,806 as revenue in the three months ended September 30, 2012 under these clinical trial sponsored research agreements.

The Company received an up-front payment of $10,000,000 from AstraZeneca on execution of the research collaboration and license agreement. Under the September 2009 amendment the Company was paid an additional $5,000,000 in consideration of reduction of future milestones and royalties and providing specific materials to AstraZeneca. The Company is now eligible for milestone payments totaling up to $145,250,000, with up to $85,250,000 contingent on development and regulatory milestones and the balance contingent on achievement of sales targets. In addition, the Company is eligible to receive mid to high single digit royalties on sales of any approved products. AstraZeneca assumed responsibility for product commercialization, product discovery and development costs, with both companies contributing scientific expertise in the research collaboration. The Company provided research services to AstraZeneca through January 2010, the expiration of the research collaboration portion of the

research collaboration and license agreement, at a contractual rate per full-time-equivalent employee.

AstraZeneca has a number of collaboration compounds in various stages of preclinical testing, and is evaluating its program and next steps. No assurance can be given that AstraZeneca will continue to develop compounds that target melanocortin receptors for the treatment of obesity, diabetes and related metabolic syndrome, or that AstraZeneca will be successful in developing any such compound.

Back to Table of Contents

PALATIN TECHNOLOGIES, INC.
and Subsidiary
Notes to Consolidated Financial Statements
(unaudited)

(5) FAIR VALUE MEASUREMENTS:

The fair value of cash equivalents and short-term investments are classified using a hierarchy prioritized based on inputs. Level 1 inputs are quoted prices (unadjusted) in active markets for identical assets or liabilities. Level 2 inputs are quoted prices for similar assets and liabilities in active markets or inputs that are observable for the asset or liability, either directly or indirectly through market corroboration, for substantially the full term of the financial instrument. Level 3 inputs are unobservable inputs based on management's own assumptions used to measure assets and liabilities at fair value. A financial asset or liability's classification within the hierarchy is determined based on the lowest level input that is significant to the fair value measurement.

The following table provides the assets carried at fair value:

	Carrying Value	Quoted prices in active markets (Level 1)	Other quoted/observable inputs (Level 2)	Significant unobservable inputs (Level 3)
September 30, 2013:				
Money Market Fund	$ 15,679,545	$ 15,679,545	$ -	$ -
U.S. Government Securities	3,749,926	3,750,082	-	-
TOTAL	$ 19,429,471	$ 19,429,627	$ -	$ -
June 30, 2013:				
Money Market Fund	$ 16,284,184	$ 16,284,184	$ -	$ -
U.S. Government Securities	5,249,654	5,249,160	-	-
TOTAL	$ 21,533,838	$ 21,533,344	$ -	$ -

(6) STOCKHOLDERS' EQUITY:

Common Stock Transactions – On July 3, 2012, the Company closed on a private placement offering in which the Company sold, for aggregate proceeds of $35.0 million, 3,873,000 shares of its common stock, Series A 2012 warrants to purchase up to 31,988,151 shares of common stock, and Series B 2012 warrants to purchase up to 35,488,380 shares of common stock. These warrants are exercisable at an exercise price of $0.01 per share, and expire ten years from the date of issuance. The holders may exercise the warrants on a cashless basis. The warrants are subject to a blocker provision prohibiting exercise of the warrants if the holder and its affiliates would beneficially own in excess of 9.99% of the total number of shares of common stock of the Company following such exercise (as may be adjusted to the extent set forth in the warrant). The warrants also provide that in the event of a Company Controlled Fundamental Transaction (as defined in the warrants), the Company may, at the election of the warrant holder, be required to redeem all or a portion of the warrants at an amount tied to the greater of the then market price of the Company's common stock or the amount per share paid to any other person.

Because there were not sufficient authorized shares to cover all the outstanding Series B 2012 warrants in the private placement offering as of closing, under ASC 815, "Derivatives and Hedging," the portion of the warrants above the then authorized level of common stock was required to be classified as a liability and carried at fair value on the Company's balance sheet. The fair value, including the initial fair value liability of $16,960,963, was calculated by multiplying

the number of shares underlying the Series B 2012 warrants above the then authorized level of the Company's common stock by the closing price of its common stock less the exercise price of $0.01 per share. The warrants were liability classified through September 27, 2012, at which time the then fair value of the warrant liability was reclassified into stockholders' equity upon stockholder approval of the increase in authorized common stock. The increase in fair value, as a result of the Company's common stock increasing from $0.50 per share at date of issuance to $0.71 per share upon shareholder approval, of $7,069,165 has been recorded as a non-operating expense for the three months ended September 30, 2012.

Back to Table of Contents

PALATIN TECHNOLOGIES, INC.
and Subsidiary
Notes to Consolidated Financial Statements
(unaudited)

The purchase agreement for the private placement provides that the purchasers, funds under the management of QVT Financial LP, have certain rights until July 3, 2018, including rights of first refusal and participation in any subsequent equity or debt financing, provided that the funds own at least 20% of the outstanding common stock of the Company calculated as if warrants held by the funds were exercised. The purchase agreement also contains certain restrictive covenants so long as the funds continue to hold specified amounts of warrants or beneficially own specified amounts of the outstanding shares of common stock.

The net proceeds to the Company were $34.4 million, after deducting offering expenses payable by the Company and excluding the proceeds to the Company, if any, from the exercise of the warrants issued in the offering.

Stock Options – In June 2013, the Company granted 525,000 options to its executive officers, 394,300 options to its employees and 270,000 options to its non-employee directors under the Company's 2011 Stock Incentive Plan. The Company is amortizing the fair value of these options of $287,000, $204,000 and $148,000, respectively, over the 48 month vesting period ending June 2017. The Company recognized $66,198 of stock-based compensation expense related to these options during the three months ended September 30, 2013.

In July 2012, the Company granted 285,000 options to its executive officers, 182,500 options to its employees and 112,500 options to its non-employee directors under the Company's 2011 Stock Incentive Plan. The Company is amortizing the fair value of these options of $182,000, $108,000 and $72,000, respectively, over the 48 month vesting period ending July 2016. The Company recognized $17,140 and $35,188, respectively, of stock-based compensation expense related to these options during the three months ended September 30, 2013 and 2012, respectively.

Restricted Stock Units – In June 2013, the Company granted 420,000 restricted stock units to its executive officers and 115,000 restricted stock units to its employees under the Company's 2011 Stock Incentive Plan. The Company is amortizing the fair value of these restricted stock units of $260,000 and $71,000, respectively, over the 24 month vesting period ending June 2015. The Company recognized $62,194 of stock-based compensation expense related to these restricted stock units during the three months ended September 2013.

In July 2012, the Company granted 222,500 restricted stock units to its executive officers under the Company's 2011 Stock Incentive Plan. The Company is amortizing the fair value of these restricted stock units of $160,000 over the 24 months ending July 2014. The Company recognized $13,673 and $24,547, respectively, of stock-based compensation expense related to these restricted stock units during the three months ended September 30, 2013 and 2012, respectively.

In June 2011, the Company granted 500,000 restricted stock units to its executive management under the Company's 2011 Stock Incentive Plan. The Company amortized the fair value of these restricted stock units of $430,000 over the 24 month vesting period ending June 2013. The Company recognized $26,875 of stock-based compensation expense related to these restricted stock units during the three months ended September 30, 2012.

Stock-based compensation cost for the three months ended September 30, 2013 for stock options and equity-based instruments issued other than the stock options and restricted stock units described above was $44,431, and $89,493 for the three months ended September 30, 2012.

Back to Table of Contents

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

The following discussion and analysis should be read in conjunction with the consolidated financial statements and notes to the consolidated financial statements filed as part of this report and the audited consolidated financial statements and notes thereto included in our annual report on Form 10-K for the year ended June 30, 2013.

Statements in this quarterly report on Form 10-Q, as well as oral statements that may be made by us or by our officers, directors, or employees acting on our behalf, that are not historical facts constitute "forward-looking statements", which are made pursuant to the safe harbor provisions of Section 21E of the Securities Exchange Act of 1934, as amended (the Exchange Act). The forward-looking statements in this quarterly report on Form 10-Q do not constitute guarantees of future performance. Investors are cautioned that statements that are not strictly historical statements contained in this quarterly report on Form 10-Q, including, without limitation, current or future financial performance, management's plans and objectives for future operations, ability to raise capital or repay debt, if required, clinical trials and results, uncertainties associated with product research and development, product plans and performance, management's assessment of market factors, as well as statements regarding our strategy and plans and those of our strategic partners, constitute forward-looking statements. Such forward-looking statements involve known and unknown risks, uncertainties and other factors that could cause our actual results to be materially different from historical results or from any results expressed or implied by such forward-looking statements. Our future operating results are subject to risks and uncertainties and are dependent upon many factors, including, without limitation, the risks identified in this report, in our annual report on Form 10-K for the year ended June 30, 2013, and in our other Securities and Exchange Commission (SEC) filings.

We expect to incur losses in the future as a result of spending on our planned development programs and losses may fluctuate significantly from quarter to quarter.

In this quarterly report on Form 10-Q, references to "we", "our", "us" or "Palatin" means Palatin Technologies, Inc. and its subsidiary.

Critical Accounting Policies and Estimates

Our significant accounting policies, which are described in the notes to our consolidated financial statements included in this report and in our annual report on Form 10-K for the year ended June 30, 2013, have not changed as of September 30, 2013. We believe that our accounting policies and estimates relating to revenue recognition, accrued expenses and stock-based compensation are the most critical.

Overview

We are a biopharmaceutical company developing targeted, receptor-specific peptide therapeutics for the treatment of diseases with significant unmet medical need and commercial potential. Our programs are based on molecules that modulate the activity of the melanocortin and natriuretic peptide receptor systems. Our primary product in clinical development is bremelanotide for the treatment of female sexual dysfunction (FSD). In addition, we have drug candidates or development programs for obesity, erectile dysfunction, pulmonary diseases, cardiovascular diseases, dermatologic diseases and inflammatory diseases.

The following drug development programs are actively under development:

- Bremelanotide, an on-demand subcutaneous injectable peptide melanocortin receptor agonist, for treatment of FSD. Bremelanotide is scheduled to start Phase 3 clinical trials in the first quarter of calendar 2014.

Melanocortin receptor-based compounds for treatment of obesity, under development by AstraZeneca AB (AstraZeneca) pursuant to our research collaboration and license agreement.

PL-3994, a peptide mimetic natriuretic peptide receptor A (NPR-A) agonist, for treatment of cardiovascular and pulmonary indications.

Melanocortin receptor-1 agonist (MC1R) peptides, for treatment of dermatologic and inflammatory disease indications.

Back to Table of Contents

The following chart shows the status of our drug development programs.

We are developing subcutaneously administered bremelanotide for the treatment of FSD in premenopausal women. Bremelanotide, which is a melanocortin agonist (a compound which binds to a cell receptor and activates a response), is a synthetic peptide analog of the naturally occurring hormone alpha-MSH (melanocyte-stimulating hormone). We have completed a Phase 2B clinical trial and end-of-Phase 2 meeting with the U.S. Food and Drug Administration (FDA), and are planning to start pivotal Phase 3 clinical trials in the first quarter of calendar 2014. The Phase 3 clinical study program will be conducted in premenopausal women with hypoactive sexual desire disorder, either with or without arousal difficulties, and will include two pivotal placebo-controlled, randomized parallel group trials each in 600 evaluable patients with two arms, one a fixed bremelanotide dose and one placebo. Hypoactive sexual desire disorder is the single largest specific diagnosis in FSD. We will also conduct open-label safety extension, drug interaction and other ancillary studies. The Phase 3 studies, which will be conducted in North America, will utilize a single-dose autoinjector intended for commercialization. It is anticipated that the Phase 3 program will take at least fifteen to eighteen months from initiation of patient dosing through database lock. Following database lock, clinical trial data will be analyzed and, assuming the data supports approval of bremelanotide for FSD, a New Drug Application (NDA) will be submitted to FDA. There can be no assurance that the Phase 3 data will support approval of bremelanotide for FSD or that the FDA will approve an NDA for bremelanotide.

We have initiated preclinical studies with MC1R peptide drug candidates for a number of indications, primarily dermatologic and inflammatory disease related. The MC1R is implicated in a number of diseases, including inflammatory indications such as inflammatory bowel disease and nephritis, dermatologic indications such as vitiligo and erythropoietic protoporphyria, and ocular indications such as uveitis and dry eye. We are conducting animal studies for a number of different indications, and if these efforts are successful, intend to select one or more clinical development candidates and indications during the current fiscal year. We will then start preclinical toxicology and other studies preparatory to filing an Investigational New Drug (IND) application with FDA.

Key elements of our business strategy include: using our technology and expertise to develop and commercialize innovative therapeutic products; entering into alliances and partnerships with pharmaceutical companies to facilitate the development, manufacture, marketing, sale and distribution of product candidates that we are developing; and, partially funding our product development programs with the cash flow generated from our license agreement with AstraZeneca and any other companies.

We incorporated in Delaware in 1986 and commenced operations in the biopharmaceutical area in 1996. Our corporate offices are located at 4B Cedar Brook Drive, Cranbury, New Jersey 08512 and our telephone number is (609) 495-2200. We maintain an Internet site at http://www.palatin.com, where among other things, we make available free of charge on and through this website our Forms 3, 4 and 5, proxy statements, 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), Section 14A and Section 16 of the Exchange Act as soon as reasonably practicable after we electronically file such material with, or furnish it to, the SEC. Our website and the information contained in it or connected to it are not incorporated into this quarterly report on Form 10-Q.

Results of Operations

Three Months Ended September 30, 2013 Compared to the Three Months Ended September 30, 2012

Revenue – We recognized no revenue for the three months ended September 30, 2013 compared to $3,806 for the three months ended September 30, 2012 pursuant to our license agreement with AstraZeneca. Revenue for the three months ended September 30, 2012 consisted entirely of reimbursement of development costs and per-employee compensation,

earned at the contractual rate.

Back to Table of Contents

Research and Development – Research and development expenses were $3.4 million for the three months ended September 30, 2013 compared to $2.3 million for the three months ended September 30, 2012.

Research and development expenses related to our bremelanotide, PL-3994, peptide melanocortin agonist, obesity and other preclinical programs were $2.8 million for the three months ended September 30, 2013 compared to $1.7 million for the three months ended September 30, 2012. Spending to date has been primarily related to our bremelanotide for the treatment of FSD program. We are currently completing protocols and preparing for initiation of pivotal Phase 3 studies of bremelanotide. The amount of such spending and the nature of future development activities are dependent on a number of factors, including primarily the availability of funds to support future development activities, success of our clinical trials and preclinical and discovery programs, and our ability to progress compounds in addition to bremelanotide and PL-3994 into human clinical trials.

The amounts of project spending above exclude general research and development spending, which consists mainly of compensation and related costs, of $0.6 million for the three months ended September 30, 2013 and September 30, 2012.

Cumulative spending from inception to September 30, 2013 on our bremelanotide, NeutroSpec (a previously marketed imaging product which has been terminated) and other programs (which include PL-3994, other melanocortin receptor agonists, obesity and other discovery programs) amounts to approximately $166.6 million, $55.6 million and $61.4 million, respectively. Due to various risk factors described in our periodic filings with the SEC, including the difficulty in currently estimating the costs and timing of future Phase 1 clinical trials and larger-scale Phase 2 and Phase 3 clinical trials for any product under development, we cannot predict with reasonable certainty when, if ever, a program will advance to the next stage of development or be successfully completed, or when, if ever, net cash inflows will be generated.

General and Administrative – General and administrative expenses, which consists mainly of compensation and related costs, were $1.0 million for the three months ended September 30, 2013 compared to $1.1 million for the three months ended September 30, 2012.

Liquidity and Capital Resources

Since inception, we have incurred net operating losses, primarily related to spending on our research and development programs. We have financed our net operating losses primarily through equity financings and amounts received under collaborative agreements.

Our product candidates are at various stages of development and will require significant further research, development and testing and some may never be successfully developed or commercialized. We may experience uncertainties, delays, difficulties and expenses commonly experienced by early stage biopharmaceutical companies, which may include unanticipated problems and additional costs relating to:

the development and testing of products in animals and humans;

product approval or clearance;

regulatory compliance;

good manufacturing practices (GMPs);

intellectual property rights;

product introduction;

marketing, sales and competition; and

obtaining sufficient capital.

Failure to enter into collaboration agreements and obtain timely regulatory approval for our product candidates and indications would impact our ability to increase revenues and could make it more difficult to attract investment capital for funding our operations. Any of these possibilities could materially and adversely affect our operations and require us to curtail or cease certain programs.

During the three months ended September 30, 2013, we used $2.0 million of cash for our operating activities, compared to $4.7 million used in the three months ended September 30, 2012. Lower net cash outflows from operations in the three months ended September 30, 2013 were primarily the result of the receipt of a $1.0 million, non-refundable option fee relating to negotiation of a potential future license of bremelanotide in a defined territory outside North America for the treatment of FSD and, secondarily, a payment deferral into the second quarter of fiscal 2014. Our accounts payable and accrued expenses increased to $1.0 million and $2.2 million, respectively, as of September 30, 2013 compared to $0.3 million and $1.7 million, respectively, as of June 30, 2013. Our periodic accounts payable and accrued expenses balances will continue to be highly dependent on the timing of our operating costs.

Back to Table of Contents

During the three months ended September 30, 2013, net cash provided by investing activities was $1.5 million, consisting of proceeds from the maturity of short-term investments offset by $6,239 used for capital expenditures. Net cash used in investing activities for the three months ended September 30, 2012 of $3,930 consisted of $4,620 in proceeds from the sale of equipment offset by $8,550 used for capital expenditures.

During the three months ended September 30, 2013, cash used in financing activities of $31,056 consisted of the $25,214 for the payment of withholding taxes related to restricted stock units and payments of $5,841 on capital lease payments. During the three months ended September 30, 2012, cash provided by financing activities consisted of net proceeds from the completion on July 3, 2012 of our private placement of 3,873,000 shares of our common stock, Series A 2012 warrants to purchase up to 31,988,151 shares of our common stock, and Series B 2012 warrants to purchase up to 35,488,380 shares of our common stock. Aggregate gross proceeds to us were $35.0 million, with net proceeds, after deducting offering expenses, of $34.4 million.

As of September 30, 2013, our cash, cash equivalents and short-term investments were $22.3 million and our current liabilities were $4.2 million. We intend to utilize existing capital resources for general corporate purposes and working capital, including preparing for the Phase 3 clinical trial program with bremelanotide for FSD, preclinical development of our peptide MC1R program, preclinical and clinical development of our PL-3994 program and preclinical development of other portfolio products. We believe that the Phase 3 clinical trial program with bremelanotide will cost at least $78.0 million. We do not intend to initiate patient enrollment in the Phase 3 program unless we have adequate funds, or commitments for adequate funds, to complete the Phase 3 program. We intend to seek additional capital to support the Phase 3 program through collaborative arrangements on bremelanotide, public or private equity or debt financings, or other sources.

We believe that our existing capital resources will be adequate to fund our currently planned operations, including submitting complete protocols for pivotal Phase 3 studies to the U.S. Food and Drug Administration (FDA) but not initiating patient enrollment, through at least calendar year 2014.

We anticipate incurring additional losses over at least the next few years. To achieve profitability, if ever, we, alone or with others, must successfully develop and commercialize our technologies and proposed products, conduct preclinical studies and clinical trials, obtain required regulatory approvals and successfully manufacture and market such technologies and proposed products. The time required to reach profitability is highly uncertain, and we do not know whether we will be able to achieve profitability on a sustained basis, if at all.

ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK.

Not required to be provided by smaller reporting companies.

ITEM 4. CONTROLS AND PROCEDURES.

Our management, with the participation of our Chief Executive Officer and Chief Financial Officer, has evaluated the effectiveness of our disclosure controls and procedures, as defined in Exchange Act Rules 13a-15(e) and 15d-15(e), as of the end of the period covered by this report. Based on that evaluation, our Chief Executive Officer and Chief Financial Officer concluded that our disclosure controls and procedures were effective as of September 30, 2013. There were no changes in our internal control over financial reporting that occurred during our most recent fiscal quarter that materially affected, or that are reasonably likely to materially affect, our internal control over financial reporting.

Back to Table of Contents

PART II - OTHER INFORMATION

ITEM 1. LEGAL PROCEEDINGS.

We may be involved, from time to time, in various claims and legal proceedings arising in the ordinary course of our business. We are not currently a party to any claim or legal proceeding.

ITEM 1A. RISK FACTORS.

There have been no material changes to our risk factors disclosed in Part I, Item 1A of our annual report on Form 10-K for the fiscal year ended June 30, 2013.

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

Issuer purchases of equity securities. We have not and do not currently intend to retire or repurchase any of our capital securities other than providing our employees with the option to withhold shares to satisfy tax withholding amounts due from employees upon the vesting of restricted stock units in connection with our 2011 Stock Incentive Plan. The following 36,543 shares were withheld during the three-month period ended September 30, 2013 at the direction of the employees as permitted under the 2011 Stock Incentive Plan in order to pay the minimum amount of tax liability owed by the employee from the vesting of those units:

Period	Total Number of Shares Purchased (1)	Average Price Paid per Share	Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs	Maximum Number of Shares that May Yet be Purchased Under Announced Plans or Programs
July 1-31, 2013	-	$ -	-	-
August 1-31, 2013	-	$ -	-	-
September 1-30, 2013	36,543	$ 0.69	-	-
Total	36,543	$ 0.69	-	-

(1) Consists solely of 36,543 shares that were withheld to satisfy tax withholding amounts due from employees upon the vesting of previously issued restricted stock units.

ITEM 3. DEFAULTS UPON SENIOR SECURITIES.

None.

ITEM 4. MINE SAFETY DISCLOSURES.

Not applicable.

ITEM 5. OTHER INFORMATION.

None.

Back to Table of Contents

ITEM 6. EXHIBITS.

Exhibits filed or furnished with this report:

31.1	Certification of Chief Executive Officer.
31.2	Certification of Chief Financial Officer.
32.1	Certification by Chief Executive Officer pursuant to 18 U.S.C. Section 1350.
32.2	Certification by Chief Financial Officer pursuant to 18 U.S.C. Section 1350.
101.INS	XBRL Instance Document.
101.SCH	XBRL Taxonomy Extension Schema Document.
101.CAL	XBRL Taxonomy Extension Calculation Linkbase Document.
101.LAB	XBRL Taxonomy Extension Label Linkbase Document.
101.PRE	XBRL Taxonomy Extension Presentation Linkbase Document.
101.DEF	XBRL Taxonomy Extension Definition Linkbase Document.

Back to Table of Contents

SIGNATURES

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

Palatin Technologies, Inc.
(Registrant)

Date: November 13, 2013

By: /s/ Carl Spana
Carl Spana, Ph.D.
President and Chief Executive Officer
(Principal Executive Officer)

Date: November 13, 2013

By: /s/ Stephen T. Wills
Stephen T. Wills, CPA, MST
Executive Vice President,
Chief Financial Officer and Chief Operating Officer

Back to Table of Contents

EXHIBIT INDEX

31.1	Certification of Chief Executive Officer.
31.2	Certification of Chief Financial Officer.
32.1	Certification by Chief Executive Officer pursuant to 18 U.S.C. Section 1350.
32.2	Certification by Chief Financial Officer pursuant to 18 U.S.C. Section 1350.
101.INS	XBRL Instance Document.
101.SCH	XBRL Taxonomy Extension Schema Document.
101.CAL	XBRL Taxonomy Extension Calculation Linkbase Document.
101.LAB	XBRL Taxonomy Extension Label Linkbase Document.
101.PRE	XBRL Taxonomy Extension Presentation Linkbase Document.
101.DEF	XBRL Taxonomy Extension Definition Linkbase Document.