

IMMUNOGEN INC
Form 10-Q
May 02, 2014
[Table of Contents](#)

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

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

For the quarterly period ended March 31, 2014

OR

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

For the transition period from _____ to _____

Commission file number 0-17999

ImmunoGen, Inc.

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Massachusetts
(State or other jurisdiction of incorporation or
organization)

04-2726691
(I.R.S. Employer Identification No.)

830 Winter Street, Waltham, MA 02451

(Address of principal executive offices, including zip code)

(781) 895-0600

(Registrant's telephone number, including area code)

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

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

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

Large accelerated filer

Accelerated filer

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

Smaller reporting company

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

Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date.

Shares of common stock, par value \$.01 per share: 85,813,733 shares outstanding as of April 23, 2014.

Table of Contents

IMMUNOGEN, INC.

FORM 10-Q

FOR THE QUARTER ENDED MARCH 31, 2014

TABLE OF CONTENTS

| Item | | Page Number |
|----------------|---|-------------|
| Part I | | |
| <u>1.</u> | <u>Financial Statements (Unaudited):</u> | |
| <u>1a.</u> | <u>Consolidated Balance Sheets as of March 31, 2014 and June 30, 2013</u> | 3 |
| <u>1b.</u> | <u>Consolidated Statements of Operations and Comprehensive Loss for the three and nine months ended March 31, 2014 and 2013</u> | 4 |
| <u>1c.</u> | <u>Consolidated Statements of Cash Flows for the nine months ended March 31, 2014 and 2013</u> | 5 |
| <u>1d.</u> | <u>Notes to Consolidated Financial Statements</u> | 6 |
| <u>2.</u> | <u>Management's Discussion and Analysis of Financial Condition and Results of Operations</u> | 22 |
| <u>3.</u> | <u>Quantitative and Qualitative Disclosures about Market Risk</u> | 33 |
| <u>4.</u> | <u>Controls and Procedures</u> | 33 |
| Part II | | |
| <u>1A.</u> | <u>Risk Factors</u> | 34 |
| <u>6.</u> | <u>Exhibits</u> | 35 |
| | <u>Signatures</u> | 36 |

Table of Contents**ITEM 1. Financial Statements****IMMUNOGEN, INC.****CONSOLIDATED BALANCE SHEETS****(UNAUDITED)****In thousands, except per share amounts**

| | March 31, 2014 | June 30, 2013 |
|---|---------------------------|--------------------------|
| ASSETS | | |
| Cash and cash equivalents | \$ 164,076 | \$ 194,960 |
| Accounts receivable | 36 | |
| Unbilled revenue | 1,987 | 2,121 |
| Inventory | 2,484 | 703 |
| Restricted cash | 319 | 319 |
| Prepaid and other current assets | 3,442 | 2,581 |
| Total current assets | 172,344 | 200,684 |
| Property and equipment, net of accumulated depreciation | 12,046 | 10,783 |
| Long-term restricted cash | 1,912 | 1,912 |
| Other assets | 392 | 217 |
| Total assets | \$ 186,694 | \$ 213,596 |
| LIABILITIES AND SHAREHOLDERS EQUITY | | |
| Accounts payable | \$ 4,743 | \$ 4,498 |
| Accrued compensation | 6,396 | 6,153 |
| Other accrued liabilities | 7,221 | 6,049 |
| Current portion of deferred lease incentive | 1,016 | 979 |
| Current portion of deferred revenue | 1,821 | 1,494 |
| Total current liabilities | 21,197 | 19,173 |
| Deferred lease incentive, net of current portion | 5,079 | 5,626 |
| Deferred revenue, net of current portion | 59,348 | 63,384 |
| Other long-term liabilities | 3,136 | 3,566 |
| Total liabilities | 88,760 | 91,749 |
| Commitments and contingencies (Note E) | | |
| Shareholders' equity: | | |
| Preferred stock, \$0.01 par value; authorized 5,000 shares; no shares issued and outstanding | | |
| Common stock, \$0.01 par value; authorized 150,000 shares; issued and outstanding 85,807 and 84,725 shares as of March 31, 2014 and June 30, 2013, respectively | 858 | 847 |
| Additional paid-in capital | 718,708 | 697,767 |
| Accumulated deficit | (621,632) | (576,767) |
| Total shareholders' equity | 97,934 | 121,847 |
| Total liabilities and shareholders' equity | \$ 186,694 | \$ 213,596 |

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

Table of Contents

IMMUNOGEN, INC.

CONSOLIDATED STATEMENTS OF OPERATIONS AND COMPREHENSIVE INCOME (LOSS)

(UNAUDITED)

In thousands, except per share amounts

| | Three Months Ended March 31, | | Nine Months Ended March 31, | |
|---|---------------------------------|-------------------|--------------------------------|--------------------|
| | 2014 | 2013 | 2014 | 2013 |
| Revenues: | | | | |
| License and milestone fees | \$ 305 | \$ 22,010 | \$ 39,150 | \$ 23,372 |
| Royalty revenue | 2,558 | | 6,946 | |
| Research and development support | 1,948 | 2,257 | 5,860 | 5,670 |
| Clinical materials revenue | 2,064 | 734 | 2,197 | 2,662 |
| Total revenues | 6,875 | 25,001 | 54,153 | 31,704 |
| Operating Expenses: | | | | |
| Research and development | 38,280 | 21,318 | 81,171 | 66,674 |
| General and administrative | 6,040 | 4,995 | 18,013 | 16,098 |
| Total operating expenses | 44,320 | 26,313 | 99,184 | 82,772 |
| Loss from operations | (37,445) | (1,312) | (45,031) | (51,068) |
| Other (expense) income, net | (7) | (39) | 166 | 132 |
| Net loss | \$ (37,452) | \$ (1,351) | \$ (44,865) | \$ (50,936) |
| Basic and diluted net loss per common share | \$ (0.44) | \$ (0.02) | \$ (0.53) | \$ (0.61) |
| Basic and diluted weighted average common shares outstanding | 85,684 | 84,279 | 85,375 | 83,923 |
| Total comprehensive loss | \$ (37,452) | \$ (1,351) | \$ (44,865) | \$ (50,936) |

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

Table of Contents

IMMUNOGEN, INC.

CONSOLIDATED STATEMENTS OF CASH FLOWS

(UNAUDITED)

In thousands, except per share amounts

| | Nine Months ended March 31, | |
|--|-----------------------------|-------------|
| | 2014 | 2013 |
| Cash flows from operating activities: | | |
| Net loss | \$ (44,865) | \$ (50,936) |
| Adjustments to reconcile net loss to net cash used for operating activities: | | |
| Depreciation and amortization | 3,428 | 3,509 |
| Loss (gain) on sale/disposal of fixed assets | 20 | (22) |
| Gain on forward contracts | (2) | (150) |
| Non-cash licensing fee | 12,830 | |
| Stock and deferred share unit compensation | 12,395 | 9,839 |
| Deferred rent | 92 | (81) |
| Changes in operating assets and liabilities: | | |
| Accounts receivable | (36) | (5,317) |
| Unbilled revenue | 134 | (909) |
| Inventory | (1,781) | 1,176 |
| Prepaid and other current assets | (613) | 777 |
| Other assets | (113) | (9) |
| Accounts payable | 245 | (672) |
| Accrued compensation | 243 | 121 |
| Other accrued liabilities | (84) | 1,088 |
| Deferred revenue, net of non-cash upfront license payment | (16,849) | (7,101) |
| Proceeds from landlord for tenant improvements | 227 | |
| Net cash used for operating activities | (34,729) | (48,687) |
| Cash flows from investing activities: | | |
| Purchases of property and equipment, net | (4,711) | (2,415) |
| Payments (proceeds) from settlement of forward contracts | (1) | 58 |
| Net cash used for investing activities | (4,712) | (2,357) |
| Cash flows from financing activities: | | |
| Proceeds from common stock issuance, net | | 93,991 |
| Proceeds from stock options exercised | 8,557 | 2,218 |
| Net cash provided by financing activities | 8,557 | 96,209 |
| Net change in cash and cash equivalents | (30,884) | 45,165 |
| Cash and cash equivalents, beginning balance | 194,960 | 160,938 |
| Cash and cash equivalents, ending balance | \$ 164,076 | \$ 206,103 |

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

Table of Contents

IMMUNOGEN, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

March 31, 2014

A. Summary of Significant Accounting Policies

Basis of Presentation

The accompanying unaudited consolidated financial statements at March 31, 2014 and June 30, 2013 and for the three and nine months ended March 31, 2014 and 2013 include the accounts of ImmunoGen, Inc., or the Company, and its wholly owned subsidiaries, ImmunoGen Securities Corp. and ImmunoGen Europe Limited. The consolidated financial statements include all of the adjustments, consisting only of normal recurring adjustments, which management considers necessary for a fair presentation of the Company's financial position in accordance with accounting principles generally accepted in the U.S. for interim financial information. Certain information and footnote disclosures normally included in the Company's annual financial statements have been condensed or omitted. The preparation of interim financial statements requires the use of management's estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the interim financial statements and the reported amounts of revenues and expenditures during the reported periods. The results of the interim periods are not necessarily indicative of the results for the entire year. Accordingly, the interim financial statements should be read in conjunction with the audited financial statements and notes thereto included in the Company's Annual Report on Form 10-K for the year ended June 30, 2013.

Subsequent Events

The Company has evaluated all events or transactions that occurred after March 31, 2014 up through the date the Company issued these financial statements. In April 2014, the Company modified its lease agreement at 830 Winter Street, Waltham, MA to extend the lease from 2020 to 2026. The Company may extend the lease for two additional terms of five years. As part of this lease amendment, the Company will receive a construction allowance of approximately \$1.1 million to build out office space to the Company's specifications. The Company did not have any other material recognizable or unrecognizable subsequent events during this period.

Revenue Recognition

The Company enters into licensing and development agreements with collaborative partners for the development of monoclonal antibody-based anticancer therapeutics. The terms of these agreements contain multiple deliverables which may include (i) licenses, or options to obtain licenses, to the Company's antibody-drug conjugate, or ADC, technology, (ii) rights to future technological improvements, (iii) research activities to be performed on behalf of the collaborative partner, (iv) delivery of cytotoxic agents and (v) the manufacture of preclinical or clinical materials for the collaborative partner. Payments to the Company under these agreements may include upfront fees, option fees, exercise fees, payments for research activities, payments for the manufacture of preclinical or clinical materials, payments based upon the achievement of certain milestones and royalties on product sales. The Company follows the provisions of the Financial Accounting Standards Board (FASB)

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Accounting Standards Codification (ASC) Topic 605-25, Revenue Recognition Multiple-Element Arrangements, and ASC Topic 605-28, Revenue Recognition Milestone Method, in accounting for these agreements. In order to account for these agreements, the Company must identify the deliverables included within the agreement and evaluate which deliverables represent separate units of accounting based on whether certain criteria are met, including whether the delivered element has stand-alone value to the collaborator. The consideration received is allocated among the separate units of accounting, and the applicable revenue recognition criteria are applied to each of the separate units.

At March 31, 2014, the Company had the following two types of agreements with the parties identified below:

- Development and commercialization licenses to use the Company's ADC technology and/or certain other intellectual property to develop compounds to a specified target antigen (referred to as development and commercialization licenses, as distinguished from the Company's right-to-test agreements described elsewhere):

Amgen (four exclusive single-target licenses)

Bayer HealthCare (one exclusive single-target license)

Biotest (one exclusive single-target license)

Table of Contents

Lilly (one exclusive single-target license)

Novartis (two exclusive single-target licenses and one license to two related targets: one target on an exclusive basis and the second target on a non-exclusive basis)

Roche, through its Genentech unit (five exclusive single-target licenses)

Sanofi (one exclusive single-target license and one exclusive license to multiple individual targets)

- Option/research agreement for a defined period of time to secure development and commercialization licenses to use the Company's ADC technology to develop anticancer compounds to specified targets on established terms (referred to herein as right-to-test agreements):

Sanofi

Novartis

Lilly

CytomX

There are no performance, cancellation, termination or refund provisions in any of the arrangements that contain material financial consequences to the Company.

Development and Commercialization Licenses

The deliverables under a development and commercialization license agreement generally include the license to the Company's ADC technology with respect to a specified antigen target, and may also include deliverables related to rights to future technological improvements, research activities to be performed on behalf of the collaborative partner and the manufacture of preclinical or clinical materials for the collaborative partner.

Generally, development and commercialization licenses contain non-refundable terms for payments and, depending on the terms of the agreement, provide that the Company will (i) at the collaborator's request, provide research services at negotiated prices which are generally consistent with what other third parties would charge, (ii) at the collaborator's request, manufacture and provide to it preclinical and clinical materials or deliver cytotoxic agents at negotiated prices which are generally consistent with what other third parties would charge, (iii) earn payments upon the achievement of certain milestones and (iv) earn royalty payments, generally until the later of the last applicable patent expiration or 10 to 12 years after product launch. In the case of Roche's Kadcyla®, however, the minimum royalty term is 10 years and the maximum royalty term is 12 years on a country-by-country basis. Royalty rates may vary over the royalty term depending on the Company's intellectual property rights. The Company may provide technical assistance and share any technology improvements with its collaborators during the term of the collaboration agreements. The Company does not directly control when or whether any collaborator will request research or manufacturing services, achieve milestones or become liable for royalty payments. As a result, the Company cannot predict when or if it will recognize revenues in connection with any of the foregoing.

In determining the units of accounting, management evaluates whether the license has stand-alone value from the undelivered elements to the collaborative partner based on the consideration of the relevant facts and circumstances for each arrangement. Factors considered in this determination include the research capabilities of the partner and the availability of ADC technology research expertise in the general marketplace. If the Company concludes that the license has stand-alone value and therefore will be accounted for as a separate unit of accounting, the Company then determines the estimated selling prices of the license and all other units of accounting based on market conditions, similar arrangements entered into by third parties, and entity-specific factors such as the terms of the Company's previous collaborative agreements, recent preclinical and clinical testing results of therapeutic products that use the Company's ADC technology, the Company's pricing practices and pricing objectives, the likelihood that technological improvements will be made, the likelihood that technological improvements made will be used by the Company's collaborators and the nature of the research services to be performed on behalf of its collaborators and market rates for similar services.

Upfront payments on development and commercialization licenses are deferred if facts and circumstances dictate that the license does not have stand-alone value. Prior to the adoption of Accounting Standards Update (ASU) No. 2009-13, Revenue Arrangements with Multiple Deliverables on July 1, 2010, the Company determined that its licenses lacked stand-alone value and were combined with other elements of the arrangement and any amounts associated with the license were deferred and amortized over

Table of Contents

a certain period, which the Company refers to as the Company's period of substantial involvement. The determination of the length of the period over which to defer revenue is subject to judgment and estimation and can have an impact on the amount of revenue recognized in a given period. Historically the Company's involvement with the development of a collaborator's product candidate has been significant at the early stages of development, and lessens as it progresses into clinical trials. Also, as a drug candidate gets closer to commencing pivotal testing the Company's collaborators have sought an alternative site to manufacture their products, as the Company's facility does not produce pivotal or commercial drug product. Accordingly, the Company generally estimates this period of substantial involvement to begin at the inception of the collaboration agreement and conclude at the end of non-pivotal Phase II testing. The Company believes this period of substantial involvement is, depending on the nature of the license, on average six and one-half years. Quarterly, the Company reassesses its periods of substantial involvement over which the Company amortizes its upfront license fees and makes adjustments as appropriate. In the event a collaborator elects to discontinue development of a specific product candidate under a development and commercialization license, but retains its right to use the Company's technology to develop an alternative product candidate to the same target or a target substitute, the Company would cease amortization of any remaining portion of the upfront fee until there is substantial preclinical activity on another product candidate and its remaining period of substantial involvement can be estimated. In the event that a development and commercialization license were to be terminated, the Company would recognize as revenue any portion of the upfront fee that had not previously been recorded as revenue, but was classified as deferred revenue, at the date of such termination.

Subsequent to the adoption of ASU No. 2009-13, the Company determined that its research licenses lack stand-alone value and are considered for aggregation with the other elements of the arrangement and accounted for as one unit of accounting.

Upfront payments on development and commercialization licenses may be recognized upon delivery of the license if facts and circumstances dictate that the license has stand-alone value from the undelivered elements, which generally include rights to future technological improvements, research services, delivery of cytotoxic agents and the manufacture of preclinical and clinical materials.

The Company recognizes revenue related to research services that represent separate units of accounting as they are performed, as long as there is persuasive evidence of an arrangement, the fee is fixed or determinable, and collection of the related receivable is probable. The Company recognizes revenue related to the rights to future technological improvements over the estimated term of the applicable license.

The Company may also provide cytotoxic agents to its collaborators or produce preclinical and clinical materials at negotiated prices which are generally consistent with what other third parties would charge. The Company recognizes revenue on cytotoxic agents and on preclinical and clinical materials when the materials have passed all quality testing required for collaborator acceptance and title and risk of loss have transferred to the collaborator. Arrangement consideration allocated to the manufacture of preclinical and clinical materials in a multiple-deliverable arrangement is below the Company's full cost, and the Company's full cost is not expected to be below its contract selling prices for its existing collaborations for the foreseeable future. During the nine months ended March 31, 2014 and 2013, the difference between the Company's full cost to manufacture preclinical and clinical materials on behalf of its collaborators as compared to total amounts received from collaborators for the manufacture of preclinical and clinical materials was \$1.6 million and \$755,000, respectively. The majority of the Company's costs to produce these preclinical and clinical materials are fixed and then allocated to each batch based on the number of batches produced during the period. Therefore, the Company's costs to produce these materials are significantly impacted by the number of batches produced during the period. The volume of preclinical and clinical materials the Company produces is directly related to the number of clinical trials for which the Company and its collaborators are preparing or currently have underway, the speed of enrollment in those trials, the dosage schedule of each clinical trial and the time period such trials last. Accordingly, the volume of preclinical and clinical materials produced, and therefore the Company's per batch costs to manufacture these preclinical and clinical materials, may vary significantly from period to period.

The Company may also produce research material for potential collaborators under material transfer agreements. Additionally, the Company performs research activities, including developing antibody specific conjugation processes, on behalf of its collaborators and potential

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collaborators during the early evaluation and preclinical testing stages of drug development. The Company records amounts received for research materials produced or services performed as a component of research and development support revenue. The Company also develops conjugation processes for materials for later stage testing and commercialization for certain collaborators. The Company is compensated at negotiated rates and may receive milestone payments for developing these processes which are recorded as a component of research and development support revenue.

The Company's development and commercialization license agreements have milestone payments which for reporting purposes are aggregated into three categories: (i) development milestones, (ii) regulatory milestones, and (iii) sales milestones. Development milestones are typically payable when a product candidate first moves into clinical testing or advances into different clinical trial phases. Regulatory milestones are typically payable upon submission for marketing approval with the U.S. Food and

Table of Contents

Drug Administration, or FDA, or other countries' regulatory authorities or on receipt of actual marketing approvals for the compound or for additional indications. Sales milestones are typically payable when annual sales reach certain levels.

At the inception of each agreement that includes milestone payments, the Company evaluates whether each milestone is substantive and at risk to both parties on the basis of the contingent nature of the milestone. This evaluation includes an assessment of whether (a) the consideration is commensurate with either (1) the entity's performance to achieve the milestone, or (2) the enhancement of the value of the delivered item(s) as a result of a specific outcome resulting from the entity's performance to achieve the milestone, (b) the consideration relates solely to past performance and (c) the consideration is reasonable relative to all of the deliverables and payment terms within the arrangement. The Company evaluates factors such as the scientific, regulatory, commercial and other risks that must be overcome to achieve the respective milestone, the level of effort and investment required to achieve the respective milestone and whether the milestone consideration is reasonable relative to all deliverables and payment terms in the arrangement in making this assessment.

Non-refundable development and regulatory milestones that are expected to be achieved as a result of the Company's efforts during the period of substantial involvement are considered substantive and are recognized as revenue upon the achievement of the milestone, assuming all other revenue recognition criteria are met. Milestones that are not considered substantive because we do not contribute effort to the achievement of such milestones are generally achieved after the period of substantial involvement and are recognized as revenue upon achievement of the milestone, as there are no undelivered elements remaining and no continuing performance obligations, assuming all other revenue recognition criteria are met.

Under the Company's development and commercialization license agreements, the Company receives royalty payments based upon its licensee's net sales of covered products. Generally, under these agreements the Company is to receive royalty reports and payments from its licensee's approximately one quarter in arrears, that is, generally in the second month of the quarter after the licensee has sold the royalty-bearing product or products. The Company recognizes royalty revenues when it can reliably estimate such amounts and collectability is reasonably assured. As such, the Company generally recognizes royalty revenues in the quarter reported to the Company by its licensee's, or one quarter following the quarter in which sales by the Company's licensee's occurred.

Right-to-Test Agreements

The Company's right-to-test agreements generally provide collaborators the right to (a) test the Company's ADC technology for a defined period of time through a research, or right-to-test, license, (b) take options, for a defined period of time, to specified targets and (c) upon exercise of those options, secure or take licenses to develop and commercialize products for the specified targets on established terms. Under these agreements, fees may be due to the Company (i) at the inception of the arrangement (referred to as upfront fees or payments), (ii) upon taking an option with respect to a specific target (referred to as option fees or payments earned, if any, when the option is taken), (iii) upon the exercise of a previously taken option to acquire a development and commercialization license(s) (referred to as exercise fees or payments earned, if any, when the development and commercialization license is taken), or (iv) some combination of all of these fees.

The accounting for right-to-test agreements is dependent on the nature of the options granted to the collaborative partner. Options are considered substantive if, at the inception of a right-to-test agreement, the Company is at risk as to whether the collaborative partner will choose to exercise the options to secure development and commercialization licenses. Factors that are considered in evaluating whether options are substantive include the overall objective of the arrangement, the benefit the collaborator might obtain from the agreement without exercising the options, the cost to exercise the options relative to the total upfront consideration, and the additional financial commitments or economic penalties imposed on the collaborator as a result of exercising the options.

For right-to-test agreements where the options to secure development and commercialization licenses to the Company's ADC technology are considered substantive, the Company does not consider the development and commercialization licenses to be a deliverable at the inception of the agreement. For those right-to-test agreements entered into prior to the adoption of ASU No. 2009-13 where the options to secure development and commercialization licenses are considered substantive, the Company has deferred the upfront payments received and recognizes this revenue over the period during which the collaborator could elect to take options for development and commercialization licenses. These periods are specific to each collaboration agreement. If a collaborator takes an option to acquire a development and commercialization license under these agreements, any substantive option fee is deferred and recognized over the life of the option, generally 12 to 18 months. If a collaborator exercises an option and takes a development and commercialization license to a specific target, the Company attributes the exercise fee to the development and commercialization license. Upon exercise of an option to acquire a development and commercialization license, the Company would also attribute any remaining deferred option fee to the development and commercialization license and apply the multiple-element revenue recognition criteria to the development and commercialization license and any other deliverables to determine the appropriate revenue recognition, which will be consistent with the Company's accounting policy for upfront payments on single-target licenses. In the event a right-to-

Table of Contents

test agreement were to be terminated, the Company would recognize as revenue any portion of the upfront fee that had not previously been recorded as revenue, but was classified as deferred revenue, at the date of such termination. None of the Company's right-to-test agreements entered into subsequent to the adoption of ASU No. 2009-13 has been determined to contain substantive options.

For right-to-test agreements where the options to secure development and commercialization licenses to the Company's ADC technology are not considered substantive, the Company considers the development and commercialization licenses to be a deliverable at the inception of the agreement and applies the multiple-element revenue recognition criteria to determine the appropriate revenue recognition. None of the Company's right-to-test agreements entered into prior to the adoption of ASU No. 2009-13 has been determined to contain non-substantive options.

The Company does not directly control when or if any collaborator will exercise its options for development and commercialization licenses. As a result, the Company cannot predict when or if it will recognize revenues in connection with any of the foregoing.

Fair Value of Financial Instruments

Fair value is defined under ASC Topic 820, Fair Value Measurements and Disclosures, as the exchange price that would be received for an asset or paid to transfer a liability (an exit price) in the principal or most advantageous market for the asset or liability in an orderly transaction between market participants on the measurement date. Valuation techniques used to measure fair value must maximize the use of observable inputs and minimize the use of unobservable inputs. The standard describes a fair value hierarchy to measure fair value which is based on three levels of inputs, of which the first two are considered observable and the last unobservable, as follows:

- Level 1 - Quoted prices in active markets for identical assets or liabilities.

- Level 2 - Inputs other than Level 1 that are observable, either directly or indirectly, such as quoted prices for similar assets or liabilities; quoted prices in markets that are not active; or other inputs that are observable or can be corroborated by observable market data for substantially the full term of the assets or liabilities.

- Level 3 - Unobservable inputs that are supported by little or no market activity and that are significant to the fair value of the assets or liabilities.

As of March 31, 2014, the Company held certain assets that are required to be measured at fair value on a recurring basis. The following table represents the fair value hierarchy for the Company's financial assets measured at fair value on a recurring basis as of March 31, 2014 (in thousands):

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| | Fair Value Measurements at March 31, 2014 Using | | | |
|--|---|---|---|--|
| | Total | Quoted Prices in Active Markets for Identical Assets (Level 1) | Significant Other Observable Inputs (Level 2) | Significant Unobservable Inputs (Level 3) |
| Cash, cash equivalents and restricted cash | \$ 166,307 | \$ 166,307 | \$ | \$ |

As of June 30, 2013, the Company held certain assets that are required to be measured at fair value on a recurring basis. The following table represents the fair value hierarchy for the Company's financial assets measured at fair value on a recurring basis as of June 30, 2013 (in thousands):

| | Fair Value Measurements at June 30, 2013 Using | | | |
|--|--|---|---|--|
| | Total | Quoted Prices in Active Markets for Identical Assets (Level 1) | Significant Other Observable Inputs (Level 2) | Significant Unobservable Inputs (Level 3) |
| Cash, cash equivalents and restricted cash | \$ 197,191 | \$ 197,191 | \$ | \$ |

The fair value of the Company's cash equivalents is based primarily on quoted prices from active markets.

Unbilled Revenue

The majority of the Company's unbilled revenue at March 31, 2014 and June 30, 2013 represents research funding earned prior to those dates based on actual resources utilized under the Company's agreements with various collaborators.

Table of Contents*Inventory*

Inventory costs relate to clinical trial materials being manufactured for sale to the Company's collaborators. Inventory is stated at the lower of cost or market as determined on a first-in, first-out (FIFO) basis.

Inventory at March 31, 2014 and June 30, 2013 is summarized below (in thousands):

| | March 31, 2014 | June 30, 2013 |
|-----------------|---------------------------|--------------------------|
| Raw materials | \$ 547 | \$ 75 |
| Work in process | 1,937 | 628 |
| Total | \$ 2,484 | \$ 703 |

Raw materials inventory consists entirely of DM1 and DM4, proprietary cell-killing agents the Company developed as part of its ADC technology. The Company considers more than a twelve month supply of raw materials that is not supported by firm, fixed orders and/or projections from its collaborators to be excess and establishes a reserve to reduce to zero the value of any such excess raw material inventory with a corresponding charge to research and development expense. In accordance with this policy, the Company recorded \$236,000 and \$798,000 of expense related to excess inventory during the nine-month periods ended March 31, 2014 and 2013, respectively. The Company recorded \$32,000 of expense related to excess inventory during the three-month period ended March 31, 2014. There were no expenses recorded for excess inventory during the same period last year.

Work in process inventory consists of conjugate manufactured for sale to the Company's collaborators to be used in preclinical and clinical studies. All conjugate is made to order at the request of the collaborators and subject to the terms and conditions of respective supply agreements. As such, no reserve for work in process inventory is required.

Computation of Net Loss per Common Share

Basic and diluted net loss per share is calculated based upon the weighted average number of common shares outstanding during the period. During periods of income, participating securities are allocated a proportional share of income determined by dividing total weighted average participating securities by the sum of the total weighted average common shares and participating securities (the two-class method). The Company's restricted stock participates in any dividends declared by the Company and are therefore considered to be participating securities. Participating securities have the effect of diluting both basic and diluted earnings per share during periods of income. During periods of loss, no loss is allocated to participating securities since they have no contractual obligation to share in the losses of the Company. Diluted (loss) income per share is computed after giving consideration to the dilutive effect of stock options that are outstanding during the period, except where such non-participating securities would be anti-dilutive.

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The Company's common stock equivalents, as calculated in accordance with the treasury-stock method, are shown in the following table (in thousands):

| | Three Months Ended March 31, | | Nine Months Ended March 31, | |
|--|---------------------------------|-------|--------------------------------|-------|
| | 2014 | 2013 | 2014 | 2013 |
| Options outstanding to purchase common stock and unvested restricted stock | 8,605 | 7,945 | 8,605 | 7,945 |
| Common stock equivalents under treasury stock method | 1,814 | 2,433 | 1,956 | 2,302 |

The Company's common stock equivalents have not been included in the net loss per share calculation because their effect is anti-dilutive due to the Company's net loss position.

Stock-Based Compensation

As of March 31, 2014, the Company is authorized to grant future awards under one employee share-based compensation plan, which is the ImmunoGen, Inc. 2006 Employee, Director and Consultant Equity Incentive Plan, or the 2006 Plan. At the annual meeting of shareholders on November 13, 2012, an amendment to the 2006 Plan was approved and an additional 3,500,000 shares were authorized for issuance under this plan. As amended, the 2006 Plan provides for the issuance of Stock Grants, the grant of

Table of Contents

Options and the grant of Stock-Based Awards for up to 12,000,000 shares of the Company's common stock, as well as any shares of common stock that are represented by awards granted under the previous stock option plan, the ImmunoGen, Inc. Restated Stock Option Plan, or the Former Plan, that are forfeited, expire or are cancelled without delivery of shares of common stock; provided, however, that no more than 5,900,000 shares shall be added to the 2006 Plan from the Former Plan, pursuant to this provision. Option awards are granted with an exercise price equal to the market price of the Company's stock at the date of grant. Options vest at various periods of up to four years and may be exercised within ten years of the date of grant.

The stock-based awards are accounted for under ASC Topic 718, Compensation - Stock Compensation. Pursuant to Topic 718, the estimated grant date fair value of awards is charged to the statement of operations and comprehensive loss over the requisite service period, which is the vesting period. Such amounts have been reduced by an estimate of forfeitures of all unvested awards. The fair value of each stock option is estimated on the date of grant using the Black-Scholes option-pricing model with the assumptions noted in the following table. As the Company has not paid dividends since inception, nor does it expect to pay any dividends for the foreseeable future, the expected dividend yield assumption is zero. Expected volatility is based exclusively on historical volatility data of the Company's stock. The expected term of stock options granted is based exclusively on historical data and represents the period of time that stock options granted are expected to be outstanding. The expected term is calculated for and applied to one group of stock options as the Company does not expect substantially different exercise or post-vesting termination behavior among its option recipients. The risk-free rate of the stock options is based on the U.S. Treasury rate in effect at the time of grant for the expected term of the stock options.

| | Three Months Ended March 31, | | Nine Months Ended March 31, | |
|-------------------------|---------------------------------|--------|--------------------------------|--------|
| | 2014 | 2013 | 2014 | 2013 |
| Dividend | None | None | None | None |
| Volatility | 60.44% | 60.44% | 60.44% | 60.44% |
| Risk-free interest rate | 1.94% | 1.13% | 1.74% | 0.85% |
| Expected life (years) | 6.3 | 6.3 | 6.3 | 6.3 |

Using the Black-Scholes option-pricing model, the weighted average grant date fair values of options granted during the three months ended March 31, 2014 and 2013 were \$9.52 and \$8.28 per share, respectively, and \$10.54 and \$8.67 per share for options granted during the nine months ended March 31, 2013 and 2012, respectively.

Stock compensation expense related to stock options and restricted stock awards granted under the 2006 Plan was \$3.7 million and \$12.1 million during the three and nine months ended March 31, 2014, respectively, compared to stock compensation expense of \$2.9 million and \$9.6 million for the three and nine months ended March 31, 2013, respectively. As of March 31, 2014, the estimated fair value of unvested employee awards was \$25.5 million, net of estimated forfeitures. The weighted-average remaining vesting period for these awards is approximately two and a quarter years.

During the nine months ended March 31, 2014, holders of options issued under the Company's equity plans exercised their rights to acquire an aggregate of approximately 1.0 million shares of common stock at prices ranging from \$3.19 to \$15.83 per share. The total proceeds to the Company from these option exercises were approximately \$8.6 million.

Financial Instruments and Concentration of Credit Risk

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The Company's cash equivalents consist of money market funds with underlying investments primarily being U.S. Government-issued securities and high quality, short-term commercial paper. All of the Company's cash and cash equivalents are maintained with three financial institutions in the U.S. The Company uses a Euro-denominated bank account to manage the foreign currency exposures that exist as part of our ongoing business operations. Our foreign currency risk management strategy is principally designed to mitigate the future potential financial impact of changes in the value of transactions, anticipated transactions and balances denominated in foreign currency, resulting from changes in foreign currency exchange rates.

Segment Information

During the nine months ended March 31, 2014, the Company continued to operate in one operating segment which is the business of discovery of monoclonal antibody-based anticancer therapeutics.

Table of Contents

The percentages of revenues recognized from significant customers of the Company in the three and nine months ended March 31, 2014 and 2013 are included in the following table:

| Collaborative Partner: | Three Months Ended March 31, | | Nine Months Ended March 31, | |
|------------------------|---------------------------------|------|--------------------------------|------|
| | 2014 | 2013 | 2014 | 2013 |
| Biotest | 13% | 1% | 3% | 5% |
| Lilly | 15% | 1% | 18% | 2% |
| Novartis | 22% | 51% | 40% | 48% |
| Roche | 37% | 42% | 31% | 33% |

There were no other customers of the Company with significant revenues in the three and nine months ended March 31, 2014 and 2013.

Recent Accounting Pronouncements

In July 2013, the FASB issued guidance to address the diversity in practice related to the financial statement presentation of unrecognized tax benefits as either a reduction of a deferred tax asset or a liability when a net operating loss carryforward, a similar tax loss, or a tax credit carryforward exists. This guidance is effective prospectively for fiscal years, and interim periods within those years, beginning after December 15, 2013. The adoption of this guidance is not expected to have a material impact on the Company's consolidated financial statements.

B. Collaborative Agreements*Roche*

In May 2000, the Company granted Genentech, now a unit of Roche, an exclusive license to use the Company's maytansinoid ADC technology with antibodies, such as trastuzumab, or other proteins that target HER2. Under the terms of this agreement, Roche has exclusive worldwide rights to develop and commercialize maytansinoid ADC compounds targeting HER2. In February 2013, the U.S. FDA granted marketing approval to the HER2-targeting ADC compound, Kadcyla. Roche received marketing approval for Kadcyla in Japan and in the European Union (EU) in September 2013 and November 2013, respectively. Roche is responsible for the manufacturing, product development and marketing of Kadcyla and any other products resulting from the agreement. The Company received a \$2 million non-refundable upfront payment from Roche upon execution of the agreement. The Company is also entitled to receive up to a total of \$44 million in milestone payments, plus royalties on the commercial sales of Kadcyla or any other resulting products. Total milestones are categorized as follows: development milestones \$13.5 million; and regulatory milestones \$30.5 million. The Company received two \$5 million regulatory milestone payments in connection with marketing approval of Kadcyla in Japan and in the EU. Based on an evaluation of the effort contributed to the achievement of these milestones, the Company determined these milestones were not substantive. In consideration that there were no undelivered elements remaining, no continuing performance obligations and all other revenue recognition criteria had been met, the Company recognized the \$10 million non-refundable payments as revenue upon achievement of the milestones, which is included in license and milestone fees for the nine months ended March 31, 2014. Through March 31, 2014, the Company has received and recognized \$13.5 million and \$20.5 million in development and regulatory milestone payments, respectively, related to Kadcyla. The next potential milestone the Company will be entitled to receive will be a \$5 million regulatory milestone for marketing approval of Kadcyla for a first extended indication as defined in the agreement.

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Based on an evaluation of the effort contributed towards the achievement of this future milestone, the Company determined this milestone is not substantive.

The Company receives royalty reports and payments related to sales of Kadcyla from Roche one quarter in arrears. In accordance with the Company's revenue recognition policy, \$2.6 million of royalties on net sales of Kadcyla for the three-month period ended December 31, 2013 were recorded and included in royalty revenue for the three months ended March 31, 2014 and \$6.9 million of royalties on net sales of Kadcyla for the nine-month period ended December 31, 2013 is included in royalty revenue for the nine months ended March 31, 2014. No such royalties were recorded in the prior year period.

Amgen

Under a now-expired right-to-test agreement entered into with Abgenix (now Amgen) in December 2000, in September 2009, November 2009 and December 2012, Amgen took three exclusive development and commercialization licenses, for which the Company received an exercise fee of \$1 million for each license taken. Under the same now-expired right-to-test agreement, in May 2013, Amgen took one non-exclusive development and commercialization license, for which the Company received an exercise fee of \$500,000. In October 2013, the non-exclusive license was amended and converted to an exclusive license, for which Amgen paid an additional \$500,000 fee to the Company. For each of these development and commercialization licenses, the Company is entitled to receive up to a total of \$34 million in milestone payments, plus royalties on the commercial sales of any resulting products. The total milestones per development and commercialization license are categorized as follows: development milestones \$9 million;

Table of Contents

regulatory milestones \$20 million; and sales milestones \$5 million. Amgen is responsible for the manufacturing, product development and marketing of any products resulting from the agreement. Amgen no longer has the right to take additional development and commercialization licenses under the agreement.

Since a deliverable to the original right-to-test agreement was determined to be materially modified at the time the non-exclusive license was converted to exclusive in October 2013, the Company accounted for the multiple-element agreement in accordance with ACS 605-25 (as amended by ASU No. 2009-13). As a result, all of the deferred revenue recorded on the date of the modification and the new consideration received as part of the modification was allocated to all of the remaining deliverables at the time of amendment of the right-to-test agreement based on the estimated selling price of each element. The remaining amount represents consideration for previously delivered elements and was recognized upon the execution of the modification.

The outstanding licenses, including the exclusive license delivered upon the signing of the amendment, contain the rights to future technological improvements as well as options to purchase materials and research and development services. The Company concluded that additional materials and research and development services would be paid at a contractual price equal to the estimated selling price based estimated prices that would be charged by third parties for similar services. The estimated selling price of the right to technological improvements is the Company's best estimate of selling price and was determined by estimating the probability that technological improvements will be made and the probability that such technological improvements made will be used by Amgen. In estimating these probabilities, we considered factors such as the technology that is the subject of the development and commercialization licenses, our history of making technological improvements, and when such improvements, if any, were likely to occur relative to the stage of development of any product candidates pursuant to the development and commercialization licenses. The Company's estimate of probability considered the likely period of time that any improvements would be utilized, which was estimated to be ten years following delivery of a commercialization and development license. The value of any technological improvements made available after this ten year period was considered to be *de minimis* due to the significant additional costs that would be incurred to incorporate such technology into any existing product candidates. The estimate of probability was multiplied by the estimated selling price of the development and commercialization licenses and the resulting cash flow was discounted at a rate of 13%, representing the Company's estimate of its cost of capital at the time of amendment of the right-to-test agreement.

The \$430,000 determined to be the estimated selling price of the future technological improvements is being recognized as revenue ratably over the period the Company is obligated to make available any technological improvements, which is equivalent to the estimated term of the agreement. The Company estimates the term of a development and commercialization license to be approximately 25 years, which reflects management's estimate of the time necessary to develop and commercialize products pursuant to the license plus the estimated royalty term. The Company reassesses the estimated term at the end of each reporting period.

After accounting for the undelivered elements at the estimated selling price, the Company had \$2.2 million of remaining allocable consideration which was determined to represent consideration for the previously delivered elements, including the exclusive license that was delivered upon the execution of the modification. This amount was recorded as revenue and is included in license and milestone fees for the nine months ended March 31, 2014.

The next potential milestone the Company will be entitled to receive under the September 2009 and November 2009 development and commercialization licenses will be a development milestone for the first dosing of a patient in a Phase II clinical trial, which will result in a \$3 million payment being due. The next potential milestones the Company will be entitled to receive under the December 2012 and May 2013 development and commercialization licenses will be a development milestone for IND approval which will result in a \$1 million payment being due to the Company. At the time of execution of each of these development and commercialization licenses, there was significant uncertainty as to whether these milestones would be achieved. In consideration of this, as well as the Company's past involvement in the research and manufacturing of these product candidates, these milestones were deemed substantive.

Sanofi

In December 2006, the Company entered into a right-to-test agreement with Sanofi. The agreement provides Sanofi with the right to (a) test the Company's maytansinoid ADC technology with Sanofi's antibodies to targets under a right-to-test, or research, license, (b) take exclusive options, with certain restrictions, to specified targets for specified option periods and (c) upon exercise of those options, take exclusive licenses to use the Company's maytansinoid ADC technology to develop and commercialize products directed to the specified targets on terms agreed upon at the inception of the right-to-test agreement. For each development and commercialization license taken, the Company is entitled to receive an exercise fee of \$2 million and up to a total of \$30 million in milestone payments, plus royalties on the commercial sales of any resulting products. The total milestones are categorized as follows: development milestones \$10 million; and regulatory milestones \$20 million. In December 2013, Sanofi took its first exclusive development and commercialization license under the right-to-test agreement, for which the Company received an exercise fee of \$2 million. The Company has deferred the exercise fee and is recognizing the \$2 million as revenue ratably over the Company's

Table of Contents

estimated period of its substantial involvement. The next payment the Company could receive would either be a \$2 million development milestone payment with the initiation of a Phase I clinical trial under the first development and commercialization license taken, or a \$2 million exercise fee for the execution of a second license. At the time of execution of this agreement, there was significant uncertainty as to whether the milestone related to initiation of a Phase I clinical trial under the first development and commercialization license would be achieved. In consideration of this, as well as the Company's expected involvement in the research and manufacturing of these product candidates, this milestone was deemed substantive. Sanofi is responsible for the manufacturing, product development and marketing of any products resulting from the agreement.

In addition to the \$2 million exercise fee received for the development and commercialization license taken, the Company received upfront payments of \$4 million under the right-to-test agreement, of which \$500,000 was received in December 2006 upon execution of the agreement and \$3.5 million was received in August 2008 upon Sanofi's activation of its rights under the agreement. The right-to-test agreement had a three-year original term from the activation date and was renewed by Sanofi in August 2011 for its final three-year term by payment of a \$2 million fee. The Company has deferred the \$2 million extension fee and is recognizing this amount as revenue over the period during which Sanofi can take additional options for development and commercialization licenses.

Novartis

In October 2010, the Company entered into a three-year right-to-test agreement with Novartis Institutes for BioMedical Research, Inc. (Novartis). The agreement provides Novartis with the right to (a) test the Company's ADC technology with individual antibodies selected by Novartis under a right-to-test, or research, license, (b) take exclusive options, with certain restrictions, to individual targets selected by Novartis for specified option periods and (c) upon exercise of those options, take exclusive licenses to use the Company's ADC technology to develop and commercialize products for a specified number of individual targets on terms agreed upon at the inception of the right-to-test agreement. The initial three-year term of the right-to-test agreement was extended by Novartis in October 2013 for an additional one-year period by payment of a \$5 million fee to the Company. In addition to the one-year extension taken in October 2013, the terms of the right-to-test agreement allow Novartis to extend the research term for one additional one-year period by payment of additional consideration. The terms of the right-to-test agreement require Novartis to exercise its options for the development and commercialization licenses by the end of the term of the research license. The Company received a \$45 million upfront payment in connection with the execution of the right-to-test agreement, and for each development and commercialization license for a specific target, the Company is entitled to receive an exercise fee of \$1 million and up to a total of \$199.5 million in milestone payments, plus royalties on the commercial sales of any resulting products. The total milestones are categorized as follows: development milestones \$22.5 million; regulatory milestones \$77 million; and sales milestones \$100 million. The Company also is entitled to receive payments for research and development activities performed on behalf of Novartis. Novartis is responsible for the manufacturing, product development and marketing of any products resulting from this agreement.

In March 2013, the Company and Novartis amended the right-to-test agreement so that Novartis can take a license to develop and commercialize products directed at two pre-defined and related undisclosed targets, one target licensed on an exclusive basis and the other target initially licensed on a non-exclusive basis. The target licensed on a non-exclusive basis may be converted to an exclusive target by notice and payment to the Company of an agreed-upon fee of at least \$5 million, depending on specific circumstances. The Company received a \$3.5 million fee in connection with the execution of the amendment to the agreement. The Company may be required to credit this fee against future milestone payments if Novartis discontinues the development of a specified product under certain circumstances.

In connection with the amendment, in March 2013, Novartis took the license referenced above under the right-to-test agreement, as amended, enabling it to develop and commercialize products directed at the two targets. The Company received a \$1 million upfront fee with the execution of this license. Additionally, the execution of this license provides the Company the opportunity to receive milestone payments totaling \$199.5 million (development milestones \$22.5 million; regulatory milestones \$77 million; and sales milestones \$100 million) or \$238 million

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(development milestones \$22.5 million; regulatory milestones \$115.5 million; and sales milestones \$100 million), depending on the composition of any resulting products.

In October 2013 and November 2013, Novartis took its second and third exclusive licenses to single targets, each triggering a \$1 million payment to the Company and the opportunity to receive milestone payments totaling \$199.5 million for each license taken, as outlined above, plus royalties on the commercial sales of any resulting products. The next payment the Company could receive would either be a \$5 million development milestone for commencement of a Phase I clinical trial under any of these three licenses, or a \$1 million exercise fee for the execution of a fourth license. At the time of execution of these agreements, there was significant uncertainty as to whether these milestones would be achieved. In consideration of this, as well as the Company's past involvement in the research and manufacturing of these product candidates, these milestones were deemed substantive. Additionally, the Company is entitled to receive royalties on product sales, if any. Novartis also has the right to convert the noted non-exclusive license to an exclusive license, in which case the Company would be entitled to receive, depending on the composition of resultant products, an upward adjustment on milestone payments.

Table of Contents

In accordance with ACS 605-25 (as amended by ASU No. 2009-13), the Company identified all of the deliverables at the inception of the right-to-test agreement and subsequently when amended. The significant deliverables were determined to be the right-to-test, or research, license, the development and commercialization licenses, rights to future technological improvements, and the research services. The options to obtain development and commercialization licenses in the right-to-test agreement were determined not to be substantive and, as a result, the exclusive development and commercialization licenses were considered deliverables at the inception of the right-to-test agreement. Factors that were considered in determining the options were not substantive included (i) the overall objective of the agreement was for Novartis to obtain development and commercialization licenses, (ii) the size of the exercise fee of \$1 million for each development and commercialization license obtained is not significant relative to the \$45 million upfront payment that was due at the inception of the right-to-test agreement, (iii) the limited economic benefit that Novartis could obtain from the right-to-test agreement unless it exercised its options to obtain development and commercialization licenses, and (iv) the lack of economic penalties as a result of exercising the options.

The Company has determined that the research license together with the development and commercialization licenses represent one unit of accounting as the research license does not have stand-alone value from the development and commercialization licenses due to the lack of transferability of the research license and the limited economic benefit Novartis would derive if they did not obtain any development and commercialization licenses. The Company has also determined that this unit of accounting does have stand-alone value from the rights to future technological improvements and the research services. The rights to future technological improvements and the research services are considered separate units of accounting as each of these was determined to have stand-alone value. The rights to future technological improvements have stand-alone value as Novartis would be able to use those items for their intended purpose without the undelivered elements. The research services have stand-alone value as similar services are sold separately by other vendors.

The estimated selling prices for the development and commercialization licenses are the Company's best estimate of selling price and were determined based on market conditions, similar arrangements entered into by third parties, including the Company's understanding of pricing terms offered by its competitors for single-target development and commercialization licenses that utilize ADC technology, and entity-specific factors such as the pricing terms of the Company's previous single-target development and commercialization licenses, recent preclinical and clinical testing results of therapeutic products that use the Company's ADC technology, and the Company's pricing practices and pricing objectives. The estimated selling price of the right to technological improvements is the Company's best estimate of selling price and was determined by estimating the probability that technological improvements will be made and the probability that such technological improvements made will be used by Novartis. In estimating these probabilities, we considered factors such as the technology that is the subject of the development and commercialization licenses, our history of making technological improvements, and when such improvements, if any, were likely to occur relative to the stage of development of any product candidates pursuant to the development and commercialization licenses. The Company's estimate of probability considered the likely period of time that any improvements would be utilized, which was estimated to be ten years following delivery of a commercialization and development license. The value of any technological improvements made available after this ten year period was considered to be *de minimis* due to the significant additional costs that would be incurred to incorporate such technology into any existing product candidates. The estimate of probability was multiplied by the estimated selling price of the development and commercialization licenses and the resulting cash flow was discounted at a rate of 16%, representing the Company's estimate of its cost of capital at the time. The estimated selling price of the research services was based on third-party evidence given the nature of the research services to be performed for Novartis and market rates for similar services.

Upon payment of the extension fee in October 2013, the total arrangement consideration of \$60.2 million (which comprises the \$45 million upfront payment, the amendment fee of \$3.5 million, the \$5 million extension fee, the exercise fee for each license, and the expected fees for the research services to be provided under the remainder of the arrangement) was reallocated to the deliverables based on the relative selling price method as follows: \$55 million to the delivered and undelivered development and commercialization licenses; \$4.5 million to the rights to future technological improvements; and \$710,000 to the research services. The Company recorded \$17.2 million of the \$55 million of the arrangement consideration outlined above for the two development and commercialization licenses taken by Novartis in October 2013 and November 2013, which is included in license and milestone fee revenue for the nine months ended March 31, 2014. The Company also recorded a cumulative catch-up of \$1 million for the license delivered in March 2013 and the delivered portion of the license covering future technological improvements, which is included in license and milestone fee revenue for the nine months ended March 31, 2014.

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Since execution of the first development and commercialization license taken in March 2013, the amount of the total arrangement consideration allocated to future technological improvements is being recognized as revenue ratably over the period the Company is obligated to make available any technological improvements, which is equivalent to the estimated term of the agreement. The Company estimates the term of a development and commercialization license to be approximately 25 years, which reflects management's estimate of the time necessary to develop and commercialize products pursuant to the license plus the estimated royalty term. The Company reassesses the estimated term at the end of each reporting period. The Company does not control when Novartis will exercise its options for development and commercialization licenses. As a result, the Company cannot predict when it will

Table of Contents

recognize the related remaining license revenue except that it will be within the term of the research license. The Company will recognize research services revenue as the related services are delivered.

Lilly

In December 2011, the Company entered into a three-year right-to-test agreement with Eli Lilly and Company (Lilly). The agreement provides Lilly with the right to (a) take exclusive options, with certain restrictions, to individual targets selected by Lilly for specified option periods, (b) test the Company's maytansinoid ADC technology with Lilly's antibodies directed to the optioned targets under a right-to-test, or research, license, and (c) upon exercise of those options, take exclusive licenses to use the Company's maytansinoid ADC technology to develop and commercialize products for a specified number of individual targets on terms agreed upon at the inception of the right-to-test agreement. The terms of the right-to-test agreement require Lilly to exercise its options for the development and commercialization licenses by the end of the term of the research license. In August 2013, Lilly took its first development and commercialization license to a single target.

The Company received a \$20 million upfront payment in connection with the execution of the right-to-test agreement, and for the first development and commercialization license taken in August 2013 and amended in December 2013, the Company received an exercise fee in the amount of \$2 million and is entitled to receive up to a total of \$199 million in milestone payments, plus royalties on the commercial sales of any resulting products. Lilly has the right to elect, at its discretion, which of the two additional development and commercialization licenses it has a right to take under the right-to-test agreement will have no exercise fee and which will have an exercise fee of \$2 million. With respect to any subsequent development and commercialization license taken, if Lilly elects that the \$2 million exercise fee is payable, the Company is entitled to receive, in addition to the exercise fee, up to a total of \$199 million in milestone payments, plus royalties on the commercial sales of any resulting products. If Lilly elects that no exercise fee is payable when it takes a development and commercialization license, the Company is entitled to receive up to a total of \$200.5 million in milestone payments, plus royalties on the commercial sales of any resulting products. The total milestones are categorized as follows: development milestones \$29 million for the development and commercialization licenses with respect to which the \$2 million exercise fee is paid, and \$30.5 million for the development and commercialization license with respect to which no exercise fee is payable; regulatory milestones \$70 million in all cases; and sales milestones \$100 million in all cases. The next payment the Company could receive would either be a \$5 million development milestone payment with the initiation of a Phase I clinical trial under the first development and commercialization license taken, or a \$2 million exercise fee for the execution of an additional license if Lilly elects to pay the exercise fee with respect to such license. At the time of execution of this agreement, there was significant uncertainty as to whether the milestone related to initiation of a Phase I clinical trial under the first development and commercialization license would be achieved. In consideration of this, as well as the Company's expected involvement in the research and manufacturing of these product candidates, this milestone was deemed substantive. The Company also is entitled to receive payments for delivery of cytotoxic agents to Lilly and research and development activities performed on behalf of Lilly. Lilly is responsible for the manufacturing, product development and marketing of any products resulting from this collaboration.

In accordance with ASC 605-25 (as amended by ASU No. 2009-13), the Company identified all of the deliverables at the inception of the right-to-test agreement. The significant deliverables were determined to be the right-to-test, or research, license, the exclusive development and commercialization licenses, rights to future technological improvements, delivery of cytotoxic agents and the research services. The options to obtain development and commercialization licenses in the right-to-test agreement were determined not to be substantive and, as a result, the exclusive development and commercialization licenses were considered deliverables at the inception of the right-to-test agreement. Factors that were considered in determining the options were not substantive included (i) the overall objective of the agreement was for Lilly to obtain development and commercialization licenses, (ii) the size of the exercise fees of \$2 million for each development and commercialization license taken beyond the first license is not significant relative to the \$20 million upfront payment that was due at the inception of the right-to-test agreement, (iii) the limited economic benefit that Lilly could obtain from the right-to-test agreement unless it exercised its options to obtain development and commercialization licenses, and (iv) the lack of economic penalties as a result of exercising the options.

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The Company has determined that the research license together with the development and commercialization licenses represent one unit of accounting as the research license does not have stand-alone value from the development and commercialization licenses due to the lack of transferability of the research license and the limited economic benefit Lilly would derive if they did not obtain any development and commercialization licenses. The Company has also determined that this unit of accounting has stand-alone value from the rights to future technological improvements, the delivery of cytotoxic agents and the research services. The rights to future technological improvements, delivery of cytotoxic agents and the research services are considered separate units of accounting as each of these was determined to have stand-alone value. The rights to future technological improvements have stand-alone value as Lilly would be able to use those items for their intended purpose without the undelivered elements. The research services and cytotoxic agents have stand-alone value as similar services and products are sold separately by other vendors.

Table of Contents

The estimated selling prices for the development and commercialization licenses are the Company's best estimate of selling price and were determined based on market conditions, similar arrangements entered into by third parties, including pricing terms offered by our competitors for single-target development and commercialization licenses that utilize antibody-drug conjugate technology, and entity-specific factors such as the pricing terms of the Company's previous single-target development and commercialization licenses, recent preclinical and clinical testing results of therapeutic products that use the Company's ADC technology, and the Company's pricing practices and pricing objectives. The estimated selling price of the rights to technological improvements is the Company's best estimate of selling price and was determined by estimating the probability that technological improvements will be made, and the probability that technological improvements made will be used by Lilly. In estimating these probabilities, we considered factors such as the technology that is the subject of the development and commercialization licenses, our history of making technological improvements, and when such improvements, if any, were likely to occur relative to the stage of development of any product candidates pursuant to the development and commercialization licenses. The company's estimate of probability considered the likely period of time that any improvements would be utilized, which was estimated to be ten years following delivery of a commercialization and development license. The value of any technological improvements made available after this ten year period was considered to be *de minimis* due to the significant additional costs that would be incurred to incorporate such technology into any existing product candidates. The estimate of probability was multiplied by the estimated selling price of the development and commercialization licenses and the resulting cash flow was discounted at a rate of 16%, representing the Company's estimate of its cost of capital at the time. The estimated selling price of the cytotoxic agent was based on third-party evidence given market rates for the manufacture of such cytotoxic agents. The estimated selling price of the research services was based on third-party evidence given the nature of the research services to be performed for Lilly and market rates for similar services.

The total arrangement consideration of \$28.2 million (which comprises the \$20 million upfront payment, the exercise fee, if any, for each license, the expected fees for the research services to be provided and the cytotoxic agent to be delivered under the arrangement) was allocated to the deliverables based on the relative selling price method as follows: \$23.5 million to the development and commercialization licenses; \$0.6 million to the rights to future technological improvements, \$0.8 million to the sale of cytotoxic agent; and \$3.3 million to the research services. Upon execution of the development and commercialization license taken by Lilly in August 2013, the Company recorded \$7.8 million of the \$23.5 million of the arrangement consideration outlined above, which is included in license and milestone fee revenue for the nine month period ended March 31, 2014. With this first development and commercialization license taken, the amount of the total arrangement consideration allocated to future technological improvements will commence to be recognized as revenue ratably over the period the Company is obligated to make available any technological improvements, which is the equivalent to the estimated term of the license. The Company estimates the term of a development and commercialization license to be approximately 25 years, which reflects management's estimate of the time necessary to develop and commercialize therapeutic products pursuant to the license plus the estimated royalty term. The Company will reassess the estimated term at each subsequent reporting period. The Company will recognize as license revenue an equal amount of the total remaining \$15.7 million of arrangement consideration allocated to the development and commercialization licenses as each individual license is delivered to Lilly upon Lilly's exercise of its remaining options to such licenses. The Company does not control when Lilly will exercise its options for development and commercialization licenses. As a result, the Company cannot predict when it will recognize the related license revenue except that it will be within the term of the research license. The Company will recognize research services revenue and revenue from the delivery of cytotoxic agents as the related services and cytotoxic agents are delivered.

In December 2013, the Company and Lilly amended the right-to-test agreement and the first development and commercialization license. Under these amendments, Lilly now has the right to extend the three-year research period under the right-to-test agreement for up to two nine-month periods by payment to the Company of additional consideration prior to the expiration of both the original term or the first extended term of that agreement. In addition, Lilly retroactively paid the Company an exercise fee of \$2 million for the first development and commercialization license, and has the right to elect, at its discretion, which of the additional development and commercialization licenses, if any, taken under the right-to-test agreement will have no exercise fee and which will have an exercise fee of \$2 million. The application of the \$2 million exercise fee to the first license granted under the arrangement did not impact the total arrangement consideration, only the timing of payment of the consideration. Due to the contingent nature of the extension fees, the lack of overall change in the total consideration for the licenses and the Company's conclusion that there has been no change in the relative selling prices originally used in the allocation of the consideration, there was no accounting impact upon the execution of the amendment.

In January 2014, the Company entered into a reciprocal right-to-test agreement with CytomX Therapeutics, Inc. (CytomX). The agreement provides CytomX with the right to test the Company's ADC technology with CytomX Probodyes to create Probody-drug conjugates (PDCs) directed to a specified number of targets under a right-to-test, or research, license, and to subsequently take an exclusive, worldwide license to use the Company's ADC technology to develop and commercialize PDCs directed to the specified targets on terms agreed upon at the inception of the right-to-test agreement. The Company received no upfront cash payment in connection with the execution of the right-to-test agreement. Instead, the Company received reciprocal rights to CytomX's Probody

Table of Contents

technology whereby the Company was provided the right to test CytomX's Probody technology to create PDCs directed to a specified number of targets and to subsequently take exclusive, worldwide licenses to develop and commercialize PDCs directed to the specified targets on terms agreed upon at the inception of the right-to-test agreement. The terms of the right-to-test agreement require the Company and CytomX to take their respective development and commercialization licenses by the end of the term of the research licenses. In addition, both the Company and CytomX are required to perform specific research activities under the right-to-test agreement on behalf of the other party for no monetary consideration.

With respect to the development and commercialization license that may be taken by CytomX, the Company is entitled to receive up to a total of \$160 million in milestone payments plus royalties on the commercial sales of any resulting product. The total milestones are categorized as follows: development milestones \$10 million; regulatory milestones \$50 million; and sales milestones \$100 million. Assuming no annual maintenance fee is payable as described below, the next payment the Company could receive would be a \$1 million development milestone payment with commencement of a Phase I clinical trial. At the time of execution of the right-to-test agreement, there was significant uncertainty as to whether the milestone related to the Phase I clinical trial would be achieved. In consideration of this, as well as the Company's expected involvement in the research and manufacturing of any product candidate, this milestone was deemed substantive. CytomX is responsible for the manufacturing, product development and marketing of any PDC resulting from the development and commercialization license taken by CytomX under this collaboration.

With respect to any development and commercialization license that may be taken by the Company, the Company will potentially be required to pay up to a total of \$80 million in milestone payments per license, plus royalties on the commercial sales of any resulting product. The total milestones per license are categorized as follows: development milestones \$7 million; regulatory milestones \$23 million; and sales milestones \$50 million. Assuming no annual maintenance fee is payable as described below, the next payment the Company could be required to make is a \$1 million development milestone payment with commencement of a Phase I clinical trial. The Company is responsible for the manufacturing, product development and marketing of any PDC resulting from any development and commercialization license taken by the Company under this collaboration.

In addition, each party may be liable to pay annual maintenance fees to the other party if the licensed PDC product candidate covered under each development and commercialization license has not progressed to a specified stage of development within a specified time frame.

The arrangement was accounted for based on the fair value of the items exchanged. The items to be delivered to CytomX under the arrangement are accounted for under the Company's revenue recognition policy. The items to be received from CytomX are recorded as research and development expenses as incurred.

In accordance with ASC 605-25 (as amended by ASU No. 2009-13), the Company identified all of the deliverables at the inception of the right-to-test agreement. The significant deliverables were determined to be the right-to-test, or research, license, the exclusive development and commercialization license, rights to future technological improvements, and the research services. The research license in the right-to-test agreement was determined not to be substantive and, as a result, the exclusive development and commercialization license was considered a deliverable at the inception of the right-to-test agreement. Factors that were considered in determining the research license was not substantive included (i) the overall objective of the agreement is for CytomX to obtain a development and commercialization license, (ii) there are no exercise fees payable upon taking the development and commercialization license, (iii) the limited economic benefit that CytomX could obtain from the right-to-test agreement unless CytomX was able to take the development and commercialization license, and (iv) the lack of economic penalties as a result of taking the license.

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The Company has determined that the research license from the Company to CytomX together with the development and commercialization license from the Company to CytomX represent one unit of accounting as the research license does not have stand-alone value from the development and commercialization license due to the lack of transferability of the research license and the limited economic benefit CytomX would derive if they did not obtain any development and commercialization license. The Company has also determined that this unit of accounting has stand-alone value from the rights to future technological improvements and the research services. The rights to future technological improvements and the research services are considered separate units of accounting as each of these was determined to have stand-alone value. The rights to future technological improvements have stand-alone value as CytomX would be able to use those items for their intended purpose without the undelivered elements. The research services have stand-alone value as similar services are sold separately by other vendors.

The estimated selling price for the development and commercialization license is the Company's best estimate of selling price and was determined based on market conditions, similar arrangements entered into by third parties, including pricing terms offered by the Company's competitors for single-target development and commercialization licenses that utilize antibody-drug conjugate technology, and entity-specific factors such as the pricing terms of the Company's previous single-target development and commercialization licenses, recent preclinical and clinical testing results of therapeutic products that use the Company's ADC

Table of Contents

technology, and the Company's pricing practices and pricing objectives. In order to determine the best estimate of selling price, the Company determined the overall value of a license by calculating a risk-adjusted net present value of a recent, comparable transaction the Company entered into with another collaborator. This overall value was then decreased by risk-adjusting the net present value of the contingent consideration (the milestones and royalties) payable by CytomX under the development and commercialization license. This amount represents the value that a third party would be willing to pay as an upfront payment for this license to the Company's technology.

The estimated selling price of the rights to technological improvements is the Company's best estimate of selling price and was determined by estimating the probability that technological improvements will be made, and the probability that technological improvements made will be used by CytomX. In estimating these probabilities, the Company considered factors such as the technology that is the subject of the development and commercialization license, the Company's history of making technological improvements, and when such improvements, if any, were likely to occur relative to the stage of development of the product candidate pursuant to the development and commercialization license. The Company's estimate of probability considered the likely period of time that any improvements would be utilized, which was estimated to be ten years following delivery of the commercialization and development license. The value of any technological improvements made available after this ten year period was considered to be *de minimis* due to the significant additional costs that would be incurred to incorporate such technology into any existing product candidate. The estimate of probability was multiplied by the estimated selling price of the development and commercialization license and the resulting cash flow was discounted at a rate of 13%, representing the Company's estimate of its cost of capital at the time.

The estimated selling price of the research services was based on third-party evidence given the nature of the research services to be performed for CytomX and market rates for similar services.

The total allocable consideration of \$13.1 million (which comprises the \$13.0 million that a third party would be willing to pay as an upfront payment for this license to the Company's technology plus \$140,000 for the fair value of fees for the research services to be provided) was allocated to the deliverables based on the relative selling price method as follows: \$12.7 million to the development and commercialization license; \$350,000 to the rights to future technological improvements and \$140,000 million to the research services. The Company will recognize as license revenue the amount of the total allocable consideration allocated to the development and commercialization license when the development and commercialization license is delivered to CytomX. At the time the license is taken, the amount of the total allocable consideration allocated to future technological improvements will commence to be recognized as revenue ratably over the period the Company is obligated to make available any technological improvements, which is the equivalent to the estimated term of the license. The Company estimates the term of a development and commercialization license to be approximately 25 years, which reflects management's estimate of the time necessary to develop and commercialize therapeutic products pursuant to the license plus the estimated royalty term. The Company will be required to reassess the estimated term at each subsequent reporting period. The Company does not control when CytomX will take the development and commercialization license. As a result, the Company cannot predict when it will recognize the related license revenue except that it will be within the term of the research license. The Company will recognize research services revenue as the related services are delivered.

No license fee revenue has been recognized related to this agreement through March 31, 2014 as the research license was not considered to be substantive and the development and commercialization license had not been delivered at this time. Accordingly, \$13.0 million of allocated arrangement consideration is included in long-term deferred revenue at March 31, 2014.

The \$13.1 million of total allocable consideration to be accounted for as revenue described above is also the amount that was used to account for the expense of the licenses and research services the Company received or will receive from CytomX. Based on an estimate of the research services that CytomX will be providing to the Company for no monetary consideration, \$310,000 was allocated to such services and will be expensed over the period the services are provided. The balance of \$12.8 million pertains to technology rights received and these amounts have

been charged to research and development expense during the three months ended March 31, 2014 upon execution of the research agreement.

For additional information related to these agreements, as well as the Company's other significant collaborative agreements, please read Note C, *Agreements* to our consolidated financial statements included within the Company's 2013 Form 10-K.

C. Capital Stock

2001 Non-Employee Director Stock Plan

During the three and nine months ended March 31, 2014, the Company recorded approximately \$2,000 and \$(11,000) in expense and expense reduction, respectively, related to stock units outstanding under the Company's 2001 Non-Employee Director Stock Plan, or the 2001 Plan, compared to \$21,000 and \$(4,000) in expense and expense reduction recorded during the three and nine months ended March 31, 2013, respectively. The value of the stock units are classified as a liability and adjusted to market value at each reporting period as the redemption amount of stock units for this plan will be paid in cash. No stock units have been issued under the 2001 Plan subsequent to June 30, 2004.

Table of Contents

Compensation Policy for Non-Employee Directors

On November 12, 2013, the Board amended the Compensation Policy for Non-Employee Directors to make certain changes to the compensation of its non-employee directors, including an increase in the fees paid in cash to the non-employee directors. Under the terms of the amended policy, the redemption amount of deferred share units issued will continue to be paid in shares of common stock of the Company on the date a director ceases to be a member of the Board. Annual retainers vest quarterly over approximately one year from the date of grant, contingent upon the individual remaining a director of ImmunoGen as of each vesting date. The number of deferred share units awarded is now fixed per the plan on the date of the award and is no longer based on the market price of the Company's common stock on the date of the award. All unvested deferred stock awards will automatically vest immediately prior to the occurrence of a change of control.

In addition to the deferred share units, the Non-Employee Directors are now also entitled to receive a fixed number of stock options instead of a fixed grant date fair value of options, determined using the Black-Scholes option pricing model measured on the date of grant, which would be the date of the annual meeting of shareholders. These options vest quarterly over approximately one year from the date of grant. Any new directors will receive a pro-rated award, depending on their date of election to the Board. The directors received a total of 80,000, 41,805 and 33,187 options in the nine months ended March 31, 2014, and fiscal years ended 2013 and 2012, respectively, and the related compensation expense for the three and nine months ended March 31, 2014 and 2013 is included in the amounts discussed in the Stock-Based Compensation section of footnote A above.

During the three and nine months ended March 31, 2014, the Company recorded approximately \$118,000 and \$315,000 in compensation expense, respectively, related to deferred share units issued and outstanding under the Company's Compensation Policy for Non-Employee Directors, compared to \$98,000 and \$253,000 in compensation expense recorded during the three and nine months ended March 31, 2013, respectively. Pursuant to the Compensation Policy for Non-Employee Directors, in November 2013, the Company issued a retiring director 43,615 shares of common stock of the Company to settle outstanding deferred share units.

D. Cash and Cash Equivalents

As of March 31, 2014 and June 30, 2013, the Company held \$164.1 million and \$195.0 million, respectively, in cash and money market funds consisting principally of U.S. Government-issued securities and high quality, short-term commercial paper which were classified as cash and cash equivalents.

E. Commitments and Contingencies

Leases

Effective July 27, 2007, the Company entered into a lease agreement with Intercontinental Fund III for the rental of approximately 89,000 square feet of laboratory and office space at 830 Winter Street, Waltham, MA through March 2020. The Company uses this space for its corporate headquarters, research and other operations. In December 2013, the Company modified its lease agreement at 830 Winter Street, Waltham, MA

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to include approximately 19,000 square feet of additional office space through 2020, concurrent with the remainder of the original lease term. As part of the lease amendment, the Company will receive a construction allowance of approximately \$746,000 to build out office space to the Company's specifications. The Company obtained physical control of the additional space to begin construction in January 2014. In April, 2014, the Company again modified its lease agreement at this site to extend the lease to 2026. The Company may extend the lease for two additional terms of five years. As part of this lease amendment, the Company will receive a construction allowance of approximately \$1.1 million to build out office space to the Company's specifications. The Company is required to pay certain operating expenses for the leased premises subject to escalation charges for certain expense increases over a base amount. The Company entered into a sublease in December 2009 for 14,100 square feet of this space in Waltham through January 2015, with the sublessee having a conditional option to extend the term for an additional two years. However, the Company has notified the sublessee that it does not intend to allow them to extend the term beyond January 2015.

Effective April 2012, the Company entered into a sublease agreement for the rental of 7,310 square feet of laboratory and office space at 830 Winter Street, Waltham, MA from Histogenics Corporation. The term of the sublease is for three years and the Company is required to pay certain operating expenses for the leased premises subject to escalation charges for certain expense increases over a base amount.

The Company also leases 43,850 square feet of manufacturing and office space at 333 Providence Highway, Norwood, MA under an agreement through 2018 with an option to extend the lease for an additional term of five years. The Company is required to pay certain operating expenses for the leased premises subject to escalation charges for certain expense increases over a base amount.

Table of Contents

Effective April 2013, the Company entered into a lease agreement with River Ridge Limited Partnership for the rental of 7,507 square feet of additional office space at 100 River Ridge Drive, Norwood, MA. The initial term of the lease is for five years and two months commencing in August 2013 with an option for the Company to extend the lease for an additional term of five years. The Company is required to pay certain operating expenses for the leased premises subject to escalation charges for certain expense increases over a base amount.

The minimum rental commitments for the Company's facilities, including real estate taxes and other expenses, for the next five fiscal years and thereafter under the non-cancelable operating lease agreements discussed above are as follows (in thousands):

| | | |
|---|----|--------|
| 2014 (three months remaining) | \$ | 1,537 |
| 2015 | | 7,053 |
| 2016 | | 6,831 |
| 2017 | | 6,848 |
| 2018 | | 6,954 |
| Thereafter | | 12,267 |
| Total minimum lease payments | \$ | 41,490 |
| Total minimum rental payments from sublease | | (573) |
| Total minimum lease payments, net | \$ | 40,917 |

Collaborations

The Company is contractually obligated to make potential future success-based development, regulatory or sales milestone payments in conjunction with certain collaborative agreements. These payments are contingent upon the occurrence of certain future events and, given the nature of these events, it is unclear when, if ever, the Company may be required to pay such amounts. Further, the timing of any future payment is not reasonably estimable. As of March 31, 2014, the maximum amount that may be payable in the future under the Company's current collaborative agreements is \$162 million, \$1.4 million of which is reimbursable by a third party under a separate agreement.

ITEM 2. Management's Discussion and Analysis of Financial Condition and Results of Operations**OVERVIEW**

Since our inception, we have been principally engaged in the development of novel, antibody-drug conjugates, or ADCs, for the treatment of cancer using our expertise in cancer biology, monoclonal antibodies, highly potent cytotoxic, or cell-killing, agents, and the design of linkers that enable these agents to remain stably attached to the antibodies while in the blood stream and released in their fully active form after delivery to a cancer cell. An anticancer compound made using our ADC technology consists of a monoclonal antibody that binds specifically to an antigen target found on the surface of cancer cells with one of our proprietary cell-killing agents attached to the antibody using one of our engineered linkers. An ADC compound's antibody component enables it to bind to cancer cells that express its target antigen, the highly potent cytotoxic agent serves to kill the cancer cell, and the engineered linker controls the release and activation of the cytotoxic agent inside the cancer cell. With some ADC compounds, the antibody component also has anticancer activity of its own. Our ADC technology is designed to enable the creation of highly effective, well-tolerated anticancer products. All of the compounds using our proprietary ADC technology currently in clinical testing contain either DM1 or DM4 as the cytotoxic agent. Both DM1 and DM4, collectively DMx, are our proprietary derivatives of a cytotoxic agent called maytansine. We also have expertise in antibodies and cancer biology to develop naked, or non-conjugated, antibody

anticancer product candidates.

We have used our proprietary ADC technology in conjunction with our in-house antibody expertise to develop our own anticancer product candidates. We have also entered into collaborative agreements that enable companies to use our ADC technology to develop and commercialize product candidates to specified targets. Under the terms of our collaborative agreements, we are generally entitled to upfront fees, milestone payments and royalties on any commercial product sales. In addition, under certain agreements we are compensated for research and development activities performed at our collaborative partner's request at negotiated prices which are generally consistent with what other third parties would charge. We are compensated to manufacture preclinical and clinical materials and deliver cytotoxic agent at negotiated prices which are generally consistent with what other third parties would charge. Currently, our collaborative partners are Amgen, Bayer HealthCare, Biotest, CytomX, Lilly, Novartis, Roche and Sanofi. We expect that substantially all of our revenue for the foreseeable future will result from payments under our collaborative arrangements. Details for some of our collaborative agreements with recent activity follow. Details for our other significant agreements can be found in our 2013 Annual Report on Form 10-K.

Table of Contents

Roche In May 2000, we granted Genentech, now a unit of Roche, an exclusive license to use our maytansinoid ADC technology with antibodies, such as trastuzumab, or other proteins that target HER2. Under the terms of this agreement, Roche has exclusive worldwide rights to develop and commercialize maytansinoid ADC compounds targeting HER2. In February 2013, the US FDA granted marketing approval to the HER2-targeting ADC compound, Kadcyla. Roche received marketing approval for Kadcyla in Japan and in the EU in September 2013 and November 2013, respectively, and with each event, we received a \$5 million regulatory milestone payment. Roche is responsible for the manufacturing, product development and marketing of Kadcyla and any other products resulting from the agreement. We received a \$2 million non-refundable upfront payment from Roche upon execution of the agreement. We are also entitled to receive up to a total of \$44 million in milestone payments, plus royalties on the commercial sales of Kadcyla and any other resulting products. Total milestones are categorized as follows: development milestones \$13.5 million; and regulatory milestones \$30.5 million. Through March 31, 2014, we have received and recognized \$13.5 million and \$20.5 million in development and regulatory milestone payments, respectively, related to Kadcyla. Included in license and milestone fees for the nine months ended March 31, 2014 is \$10 million of milestone payments for marketing approval of Kadcyla in the EU and in Japan.

We receive royalty reports and payments related to sales of Kadcyla from Roche one quarter in arrears. In accordance with our revenue recognition policy, \$2.6 million of royalties on net sales of Kadcyla for the three-month period ended December 31, 2013 were recorded and included in royalty revenue for the three months ended March 31, 2014 and \$6.9 million of royalties on net sales of Kadcyla for the nine-month period ended December 31, 2013 is included in royalty revenue for the nine months ended March 31, 2014. No such royalties were recorded in the prior year periods.

Amgen Under a now-expired right-to-test agreement entered into with Amgen in December 2000, in September 2009, November 2009 and December 2012, Amgen took three exclusive development and commercialization licenses, for which we received an exercise fee of \$1 million for each license taken. In May 2013, Amgen took one non-exclusive development and commercialization license, for which we received an exercise fee of \$500,000. In October 2013, the non-exclusive license was amended and converted to an exclusive license, for which Amgen paid an additional \$500,000 fee to us. For each of these development and commercialization license taken, we are entitled to receive up to a total of \$34 million in milestone payments, plus royalties on the commercial sales of any resulting products. The total milestones per exclusive development and commercialization license are categorized as follows: development milestones \$9 million; regulatory milestones \$20 million; and sales milestones \$5 million. Amgen no longer has the right to take additional options for development and commercialization licenses under the agreement.

Since a deliverable to the original right-to-test agreement was determined to be materially modified at the time the non-exclusive license was converted to exclusive in October 2013, we accounted for the multiple-element agreement in accordance with ACS 605-25 (as amended by ASU No. 2009-13). As a result, all of the deferred revenue recorded on the date of the modification and the new consideration received as part of the modification was allocated to all of the remaining deliverables at the time of amendment of the right-to-test agreement based on the estimated selling price of each element. The remaining amount represents consideration for previously delivered elements and was recognized upon the execution of the modification.

The outstanding licenses, including the exclusive license delivered upon the signing of the amendment, contain the rights to future technological improvements as well as options to purchase materials and research and development services. We concluded that additional materials and research and development services would be paid at a contractual price equal to the estimated selling price based estimated prices that would be charged by third parties for similar services. The estimated selling price of the right to technological improvements is the Company's best estimate of selling price and was determined by estimating the probability that technological improvements will be made and the probability that such technological improvements made will be used by Amgen. The \$430,000 determined to be the estimated selling price of the future technological improvements is being recognized as revenue ratably over the period we are obligated to make available any technological improvements, which is equivalent to the estimated term of the agreement, or 25 years. After accounting for the undelivered elements at the estimated selling price, we had \$2.2 million of remaining allocable consideration which was determined to represent consideration for the previously delivered elements, including the exclusive license that was delivered upon the execution of the modification. This amount was recorded as revenue and is included in license and milestone fees for the nine months ended March 31, 2014.

Sanofi In December 2006, we entered into a right-to-test agreement with Sanofi. The agreement provides Sanofi with the right to (a) test our maytansinoid ADC technology with Sanofi's antibodies to targets under a right-to-test, or research, license, (b) take exclusive options, with certain restrictions, to specified targets for specified option periods and (c) upon exercise of those options, take exclusive licenses to use our maytansinoid ADC technology to develop and commercialize products directed to the specified targets on terms agreed upon at the inception of the right-to-test agreement. For each development and commercialization license taken, we are entitled to receive an exercise fee of \$2 million and up to a total of \$30 million in milestone payments, plus royalties on the commercial sales of any resulting products. The total milestones are categorized as follows: development milestones \$10 million; and regulatory milestones \$20 million. In December 2013, Sanofi took its first exclusive development and

Table of Contents

commercialization license under the right-to-test agreement, for which we received an exercise fee of \$2 million. We have deferred the exercise fee and are recognizing the \$2 million as revenue ratably over our estimated period of substantial involvement.

Novartis In October 2010, we entered into a three-year right-to-test agreement with Novartis. The agreement provides Novartis with the right to (a) test our ADC technology with individual antibodies selected by Novartis under a right-to-test, or research, license, (b) take exclusive options, with certain restrictions, to individual targets selected by Novartis for specified option periods and (c) upon exercise of those options, take exclusive licenses to use our ADC technology to develop and commercialize products for a specified number of individual targets on terms agreed upon at the inception of the right-to-test agreement. The initial three-year term of the right-to-test agreement was extended by Novartis in October 2013 for an additional one-year period by payment of a \$5 million fee to us. In addition to the one-year extension taken in October 2013, the terms of the right-to-test agreement allow Novartis to extend the research term for one additional one-year period by payment of additional consideration. The terms of the right-to-test agreement require Novartis to exercise its options for the development and commercialization licenses by the end of the term of the research license. We received a \$45 million upfront payment in connection with the execution of the right-to-test agreement, and for each development and commercialization license for a specific target, we are entitled to receive an exercise fee of \$1 million and up to a total of \$199.5 million in milestone payments, plus royalties on the commercial sales of any resulting products. The total milestones are categorized as follows: development milestones \$22.5 million; regulatory milestones \$77 million; and sales milestones \$100 million.

In March 2013, we and Novartis amended the right-to-test agreement so that Novartis can take a license to develop and commercialize products directed at two pre-defined and related undisclosed targets, one target licensed on an exclusive basis and the other target initially licensed on a non-exclusive basis. The target licensed on a non-exclusive basis may be converted to an exclusive target by notice and payment to us of an agreed-upon fee of at least \$5 million, depending on specific circumstances. We received a \$3.5 million fee in connection with the execution of the amendment to the agreement. We may be required to credit this fee against future milestone payments if Novartis discontinues the development of a specified product under certain circumstances.

In connection with the amendment, in March 2013, Novartis took the license referenced above under the right-to-test agreement, as amended, enabling it to develop and commercialize products directed at the two targets. We received a \$1 million upfront fee with the execution of this license. Additionally, the execution of this license provides us the opportunity to receive milestone payments totaling \$199.5 million (development milestones \$22.5 million; regulatory milestones \$77 million; and sales milestones \$100 million) or \$238 million (development milestones \$22.5 million; regulatory milestones \$115.5 million; and sales milestones \$100 million), depending on the composition of any resulting products. Additionally, under the license agreements, we are entitled to receive royalties on product sales, if any. Novartis also has the right to convert the noted non-exclusive license to an exclusive license, in which case we would be entitled to receive a conversion fee and, depending on the composition of resultant products, an upward adjustment on milestone payments. In October 2013 and November 2013, Novartis took its second and third exclusive license to a single target, each triggering a \$1 million payment to us and the opportunity to receive milestone payments totaling \$199.5 million for each license taken, as outlined above. In accordance with our revenue recognition policy, upon execution of the development and commercialization licenses taken by Novartis in October 2013 and November 2013 and payment of the one-year extension fee, we recorded \$17.2 million of revenue, which is included in license and milestone fee revenue for the nine months ended March 31, 2014. We also recorded a cumulative catch-up of \$1 million for the license delivered in March 2013 and the delivered portion of the license covering future technological improvements, which is included in license and milestone fee revenue for the nine months ended March 31, 2014.

Lilly In December 2011, we entered into a three-year right-to-test agreement with Lilly. The agreement provides Lilly with the right to (a) take exclusive options, with certain restrictions, to individual targets selected by Lilly for specified option periods, (b) test our maytansinoid ADC technology with Lilly's antibodies directed to the optioned targets under a right-to-test, or research, license, and (c) upon exercise of those options, take exclusive licenses to use our maytansinoid ADC technology to develop and commercialize products for a specified number of individual targets on terms agreed upon at the inception of the right-to-test agreement. The terms of the right-to-test agreement require Lilly to exercise its options for the development and commercialization licenses by the end of the term of the research license. In August 2013, Lilly took its first development and commercialization license to a single target.

We received a \$20 million upfront payment in connection with the execution of the right-to-test agreement. In December 2013, we and Lilly amended the right-to-test agreement and the first development and commercialization license. Under these amendments, Lilly now has the right to extend the three-year research period under the right-to-test agreement for up to two nine-month periods by payment to us of additional consideration prior to the expiration of both the original term or the first extended term of that agreement. In addition, Lilly retroactively paid us an exercise fee of \$2 million for the first development and commercialization license, and has the right to elect, at its discretion, which of the two additional development and commercialization licenses it has a right to take under the right-to-test agreement will have no exercise fee and which will have an exercise fee of \$2 million. The application of the \$2 million exercise fee to the first license granted under the arrangement did not impact the total

Table of Contents

arrangement consideration, only the timing of payment of the consideration. For the first development and commercialization license taken, which occurred in August 2013, we are entitled to receive up to a total of \$199 million in milestone payments, plus royalties on the commercial sales of any resulting products. With respect to any subsequent development and commercialization license taken, if Lilly elects that the \$2 million exercise fee is payable, we are entitled to receive, in addition to the exercise fee, up to a total of \$199 million in milestone payments, plus royalties on the commercial sales of any resulting products. If Lilly elects that no exercise fee is payable when it takes a subsequent development and commercialization license, we are entitled to receive up to a total of 200.5 million in milestone payments, plus royalties on the commercial sales of any resulting products. The total milestones are categorized as follows: development milestones \$29 million for the development and commercialization licenses with respect to which the \$2 million exercise fee is paid, and \$30.5 million for the development and commercialization license with respect to which no exercise fee is payable; regulatory milestones \$70 million in all cases; and sales milestones \$100 million in all cases. In accordance with our revenue recognition policy, upon execution of the development and commercialization license taken by Lilly in August 2013, we recorded \$7.8 million of revenue which is included in license and milestone fee revenue for the nine months ended March 31, 2014.

CytomX In January 2014, we entered into a reciprocal right-to-test agreement with CytomX. The agreement provides CytomX with the right to test our ADC technology with CytomX Probodyes to create Probody-drug conjugates (PDCs) directed to a specified number of targets under a right-to-test, or research, license, and to subsequently take an exclusive, worldwide license to use our ADC technology to develop and commercialize PDCs directed to the specified targets on terms agreed upon at the inception of the right to test agreement. We received no upfront cash payment in connection with the execution of the right to test agreement. Instead, we received reciprocal rights to CytomX's Probody technology whereby we were provided the right to test CytomX's Probody technology to create PDCs directed to a specified number of targets and to subsequently take exclusive licenses to develop and commercialize PDCs directed to the specified targets on terms agreed upon at the inception of the right to test agreement. The terms of the right to test agreement require us and CytomX to take our respective development and commercialization licenses by the end of the term of the research licenses. In addition, both we and CytomX are required to perform specific research activities under the right-to-test agreement on behalf of the other party for no monetary consideration.

With respect to the development and commercialization license that may be taken by CytomX, we are entitled to receive up to a total of \$160 million in milestone payments plus royalties on the commercial sales of any resulting product. The total milestones are categorized as follows: development milestones \$10 million; regulatory milestones \$50 million; and sales milestones \$100 million.

With respect to any development and commercialization license that may be taken by us, we will potentially be required to pay up to a total of \$80 million in milestone payments per license, plus royalties on the commercial sales of any resulting product. The total milestones per license are categorized as follows: development milestones \$7 million; regulatory milestones \$23 million; and sales milestones \$50 million.

The total allocable consideration of \$13.1 million (which comprises the \$13.0 million that a third party would be willing to pay as an upfront payment for this license to our technology plus \$140,000 for the fair value of fees for the research services to be provided) was allocated to the deliverables based on the relative selling price method as follows: \$12.7 million to the development and commercialization license; \$350,000 to the rights to future technological improvements and \$140,000 million to the research services. No license fee revenue has been recognized related to this agreement through March 31, 2014 as the research license was not considered to be substantive and the development and commercialization license had not been delivered. We do not control when, or if, CytomX will exercise its options for development and commercialization licenses. As a result, we cannot predict when we will recognize license fee revenue except that it will be within the term of the research license. Accordingly, \$13.0 million of allocated arrangement consideration is included in long term deferred revenue at March 31, 2014.

The \$13.1 million of total allocable consideration to be accounted for as revenue noted above is also the amount that was used to account for the expense of the licenses and research services we received or will receive from CytomX. Based on an estimate of the research services that

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CytomX will be providing to us for no monetary consideration, \$310,000 was allocated to such services and will be expensed over the period the services are provided. The balance of \$12.8 million pertains to technology rights and these amounts have been charged to research and development expense during the three months ended March 31, 2014 upon execution of the research agreement.

To date, we have not generated revenues from our proprietary commercial product sales and we expect to incur significant operating losses for the foreseeable future. As of March 31, 2014, we had approximately \$164.1 million in cash and cash equivalents compared to \$195.0 million in cash and cash equivalents as of June 30, 2013.

We anticipate that future cash expenditures will be partially offset by collaboration-derived proceeds, including milestone payments, royalties and upfront fees. Accordingly, period-to-period operating results may fluctuate dramatically based upon the

Table of Contents

timing of receipt of the proceeds. We believe that our established collaboration agreements, while subject to specified milestone achievements, will provide funding to assist us in meeting obligations under our collaborative agreements while also providing funding for the development of internal product candidates and technologies. However, we can give no assurances that such collaborative agreement funding will, in fact, be realized in the time frames we expect, or at all. Should we or our partners not meet some or all of the terms and conditions of our various collaboration agreements, we may be required to pursue additional strategic partners, secure alternative financing arrangements, and/or defer or limit some or all of our research, development and/or clinical projects. However, we cannot provide assurance that any such opportunities presented by additional strategic partners or alternative financing arrangements will be entirely available to us, if at all.

Critical Accounting Policies

We prepare our consolidated financial statements in accordance with accounting principles generally accepted in the U.S. The preparation of these financial statements requires us to make estimates and judgments that affect the reported amounts of assets, liabilities, revenues and expenses and related disclosure of contingent assets and liabilities. On an on-going basis, we evaluate our estimates, including those related to our collaborative agreements, inventory and stock-based compensation. We base our estimates on historical experience and various other assumptions that we believe to be reasonable under the circumstances. Actual results may differ from these estimates.

There were no significant changes to our critical accounting policies from those disclosed in our Annual Report on Form 10-K for the fiscal year ended June 30, 2013.

RESULTS OF OPERATIONS

Comparison of Three Months ended March 31, 2014 and 2013

Revenues

Our total revenues for the three months ended March 31, 2014 and 2013 were \$6.9 million and \$25.0 million, respectively. The \$18.1 million decrease in revenues in the three months ended March 31, 2014 from the same period in the prior year is attributable to a decrease in license and milestone fees and research and development support revenue, partially offset by an increase in royalty revenue and clinical materials revenue, all of which are discussed below.

Revenues from license and milestone fees for the three months ended March 31, 2014 decreased \$21.7 million to \$305,000 from \$22.0 million in the same period ended March 31, 2013. Included in license and milestone fees for the three months ended March 31, 2013 is a \$10.5 million regulatory milestone achieved under our collaboration agreement with Roche and \$11.1 million of license fee revenue earned upon the execution of a development and commercialization license by Novartis. The amount of license and milestone fees we earn is directly related to the number of our collaborators, the collaborators' advancement of the product candidates, and the overall success in the clinical trials of the product candidates. As such, the amount of license and milestone fees may vary significantly from quarter to quarter and year to year. Total revenue from license and milestone fees recognized from each of our collaborative partners in the three-month periods ended March 31, 2014 and 2013

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is included in the following table (in thousands):

| License and Milestone Fees | Three Months Ended March 31, | |
|----------------------------|------------------------------|-----------|
| | 2014 | 2013 |
| Collaborative Partner: | | |
| Amgen | \$ 4 | \$ 247 |
| Biotest | 6 | 6 |
| Lilly | 6 | |
| Novartis | 45 | 11,090 |
| Sanofi | 244 | 167 |
| Roche | | 10,500 |
| Total | \$ 305 | \$ 22,010 |

Deferred revenue of \$61.2 million as of March 31, 2014 primarily represents consideration received from our collaborators pursuant to our license agreements, which we have yet to earn pursuant to our revenue recognition policy. Included within this amount is \$13.1 million of non-cash consideration recorded in connection with our arrangement with CytomX.

In February 2013, the U.S. FDA granted marketing approval to Kadcyla, a product resulting from one of our development and commercialization licenses with Roche, through its Genentech unit. We receive royalty reports and payments related to sales of

Table of Contents

Kadcyla from Roche one quarter in arrears. In accordance with our revenue recognition policy, \$2.6 million of royalties on net sales of Kadcyla for the three-month period ended December 31, 2013 were recorded and included in royalty revenue for the three months ended March 31, 2014. No royalty revenue was recorded in the three-month period ended March 31, 2013. We expect royalty revenue to increase in future periods as the underlying net sales of Kadcyla increase.

Research and development support revenue was \$1.9 million for the three months ended March 31, 2014 compared with \$2.3 million for the three months ended March 31, 2013. These amounts primarily represent research funding earned based on actual resources utilized under our agreements with our collaborators shown in the table below. Also included in research and development support revenue are fees for developing antibody-specific conjugation processes on behalf of our collaborators and potential collaborators during the early evaluation and preclinical testing stages of drug development. The amount of research and development support revenue we earn is directly related to the number of our collaborators and potential collaborators, the stage of development of our collaborators' product candidates and the resources our collaborators allocate to the development effort. As such, the amount of research and development support revenue may vary widely from quarter to quarter and year to year. Total revenue recognized from research and development support from each of our collaborative partners in the three-month periods ended March 31, 2014 and 2013 is included in the following table (in thousands):

| Research and Development Support Collaborative Partner: | Three Months Ended March 31, | |
|---|------------------------------|----------|
| | 2014 | 2013 |
| Amgen | \$ 97 | \$ 127 |
| Biotest | 137 | 252 |
| Lilly | 987 | 160 |
| Novartis | 706 | 1,616 |
| Other | 21 | 102 |
| Total | \$ 1,948 | \$ 2,257 |

Clinical materials revenue increased \$1.3 million in the three months ended March 31, 2014 to \$2.1 million from \$734,000 in the three months ended March 31, 2013. We are compensated at negotiated prices which are generally consistent with what other third-parties would charge. The amount of clinical materials revenue we earn, and the related cost of clinical materials charged to research and development expense, is directly related to the number of clinical trials our collaborators who use us to manufacture clinical materials are preparing or have underway, the speed of enrollment in those trials, the dosage schedule of each clinical trial and the time period, if any, during which patients in the trial receive clinical benefit from the clinical materials, and the demand our collaborators have for clinical-grade material for process development and analytical purposes. As such, the amount of clinical materials revenue and the related cost of clinical materials charged to research and development expense may vary significantly from quarter to quarter and year to year.

Research and Development Expenses

Our research and development expenses relate to (i) research to evaluate new targets and to develop and evaluate new antibodies, linkers and cytotoxic agents, (ii) preclinical testing of our own and, in certain instances, our collaborators' product candidates, and the cost of our own clinical trials, (iii) development related to clinical and commercial manufacturing processes and (iv) manufacturing operations which also includes raw materials.

Research and development expense for the three months ended March 31, 2014 increased \$17 million to \$38.3 million from \$21.3 million for the three months ended March 31, 2013. During the current three-month period, we recorded a \$12.8 million non-cash charge to research and

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development expense for technology rights obtained under the collaboration agreement executed with CytomX in January 2014. Salaries and related expenses also increased due to additional headcount, increased incentive compensation and increased stock compensation costs. The number of our research and development personnel increased to 267 as of March 31, 2014 compared to 241 at March 31, 2013. The higher stock compensation is driven by higher stock prices and increases in the number of options granted due to increases in personnel. A more detailed discussion of research and development expense in the period follows.

We are unable to accurately estimate which potential product candidates, if any, will eventually move into our internal preclinical research program. We are unable to reliably estimate the costs to develop these products as a result of the uncertainties related to discovery research efforts as well as preclinical and clinical testing. Our decision to move a product candidate into the clinical development phase is predicated upon the results of preclinical tests. We cannot accurately predict which, if any, of the discovery stage product candidates will advance from preclinical testing and move into our internal clinical development program. The clinical trial and regulatory approval processes for our product candidates that have advanced or that we intend to advance to clinical testing are lengthy, expensive and uncertain in both timing and outcome. As a result, the pace and timing of the clinical

Table of Contents

development of our product candidates is highly uncertain and may not ever result in approved products. Completion dates and development costs will vary significantly for each product candidate and are difficult to predict. A variety of factors, many of which are outside our control, could cause or contribute to the prevention or delay of the successful completion of our clinical trials, or delay or prevent our obtaining necessary regulatory approvals. The costs to take a product through clinical trials are dependent upon, among other factors, the clinical indications, the timing, size and design of each clinical trial, the number of patients enrolled in each trial, and the speed at which patients are enrolled and treated. Product candidates may be found to be ineffective or to cause unacceptable side effects during clinical trials, may take longer to progress through clinical trials than anticipated may fail to receive necessary regulatory approvals or may prove impractical to manufacture in commercial quantities at reasonable cost or with acceptable quality.

The lengthy process of securing FDA approvals for new drugs requires the expenditure of substantial resources. Any failure by us to obtain, or any delay in obtaining regulatory approvals would materially adversely affect our product development efforts and our business overall. Accordingly, we cannot currently estimate, with any degree of certainty, the amount of time or money that we will be required to expend in the future on our product candidates prior to their regulatory approval, if such approval is ever granted. As a result of these uncertainties surrounding the timing and outcome of our clinical trials, we are currently unable to estimate when, if ever, our product candidates that have advanced into clinical testing will generate revenues and cash flows.

We do not track our research and development costs by project. Since we use our research and development resources across multiple research and development projects, we manage our research and development expenses within each of the categories listed in the following table and described in more detail below (in thousands):

| Research and Development Expense | Three Months Ended March 31, | |
|--|------------------------------|-----------|
| | 2014 | 2013 |
| Research | \$ 17,281 | \$ 4,369 |
| Preclinical and Clinical Testing | 8,887 | 6,395 |
| Process and Product Development | 2,113 | 1,938 |
| Manufacturing Operations | 9,999 | 8,616 |
| Total Research and Development Expense | \$ 38,280 | \$ 21,318 |

Research: Research includes expenses primarily associated with activities to identify and evaluate new targets and to develop and evaluate new antibodies, linkers and cytotoxic agents for our products and in support of our collaborators. Such expenses primarily include personnel, contract services, research licensing fees, facilities and lab supplies. Research expenses for the three months ended March 31, 2014 increased \$12.9 million compared to the three months ended March 31, 2013. This increase is primarily due to a \$12.8 million non-cash charge recorded for technology rights obtained under the collaboration agreement executed with CytomX in January 2014. As a result of this non-cash charge, we expect research expenses for fiscal 2014 to be significantly higher than fiscal 2013.

Preclinical and Clinical Testing: Preclinical and clinical testing includes expenses related to preclinical testing of our own and, in certain instances, our collaborators' product candidates, regulatory activities, and the cost of our own clinical trials. Such expenses include personnel, patient enrollment at our clinical testing sites, consultant fees, contract services, and facility expenses. Preclinical and clinical testing expenses for the three months ended March 31, 2014 increased \$2.5 million to \$8.9 million compared to \$6.4 million for the three months ended March 31, 2013. This increase is primarily the result of: (i) higher salaries and related expenses; (ii) an increase in clinical trial costs driven by increased costs associated with the IMG853 401 and IMG289 501 studies, partially offset by decreased costs resulting from the termination of the IMG901 007 Phase II study in November 2013; and (iii) an increase in contract service expense driven primarily by increased study activities related to IMG853 and IMG529. We expect preclinical and clinical testing expenses for fiscal 2014 to be significantly higher than fiscal 2013 due to increased activities to advance our wholly owned product candidates.

Process and Product Development: Process and product development expenses include costs for development of clinical and commercial manufacturing processes for our own and collaborator compounds. Such expenses include the costs of personnel, contract services and facility expenses. For the three months ended March 31, 2014, total development expenses increased \$175,000 compared to the three months ended March 31, 2013. This increase is primarily the result of an increase in salaries and related expenses and an increase in contract service expense driven primarily by development activities for IMG779. We expect process and product development expenses for fiscal 2014 to be marginally higher than fiscal 2013.

Manufacturing Operations: Manufacturing operations expense includes costs to manufacture preclinical and clinical materials for our own and our collaborator s product candidates, and quality control and quality assurance activities and costs to support the operation and maintenance of our conjugate manufacturing facility. Such expenses include personnel, raw materials for our and our collaborators preclinical studies and clinical trials, development costs with contract manufacturing organizations, manufacturing supplies, and facilities expense. For the three months ended March 31, 2014, manufacturing operations expense

Table of Contents

increased \$1.4 million to \$10.0 million compared to \$8.6 million in the same period last year. The increase in the three months ended March 31, 2014 as compared to the three months ended March 31, 2013 is primarily the result of (i) an increase in cost of clinical materials revenue due to timing of orders of such clinical materials from our partners; (ii) an increase in contract service expense driven by increased study activities related to our cytotoxic agents; and (iii) an increase in salaries and related expenses. Partially offsetting these increases, antibody development and supply expense decreased driven primarily by supply required for our IMG853 program and an increase in costs capitalized into inventory due to a greater number of manufactured batches of conjugated materials on behalf of our collaborators during the current period. We expect manufacturing operations expense for fiscal 2014 to be higher than fiscal 2013 due primarily to increased activities to advance our wholly owned product candidates.

General and Administrative Expenses

General and administrative expenses for the three months ended March 31, 2014 increased \$1 million to \$6.0 million compared to \$5.0 million in the same period last year. This increase is primarily due to an increase in salaries and related expenses, as well as an increase in professional service fees, particularly patent expenses. We expect general and administrative expenses for fiscal 2014 to be higher than fiscal 2013 due primarily to increased salaries and related expenses, patent activities and other professional services.

Other (Expense) Income, net

Other (expense) income, net for the three months ended March 31, 2014 and 2013 is included in the following table (in thousands):

| Other (Expense) Income, net | Three Months Ended March 31, | |
|--|-------------------------------------|----------------|
| | 2014 | 2013 |
| Interest Income | \$ 12 | \$ 27 |
| Other (Expense) Income, net | (19) | (66) |
| Total Other (Expense) Income, net | \$ (7) | \$ (39) |

*Comparison of Nine Months ended March 31, 2014 and 2013**Revenues*

Our total revenues for the nine months ended March 31, 2014 and 2013 were \$54.2 million and \$31.7 million, respectively. The \$22.5 million increase in revenues in the nine months ended March 31, 2014 from the same period in the prior year is attributable to an increase in license and milestone fees, royalty revenue and research and development support revenue, partially offset by a decrease in clinical materials revenue, all of which are discussed below.

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Revenues from license and milestone fees for the nine months ended March 31, 2014 increased \$15.8 million to \$39.2 million from \$23.4 million in the same period ended March 31, 2013. Included in license and milestone fees for the nine months ended March 31, 2014 is \$7.8 million of license revenue earned upon the execution of a development and commercialization license by Lilly, two \$5 million regulatory milestones achieved under our collaboration agreement with Roche, \$18.2 million of license revenue earned upon the execution of two development and commercialization licenses and a one-year extension of the original term of the multi-target agreement by Novartis and \$2.2 million of revenue from Amgen related to a modification of an existing arrangement. Included in license and milestone fees for the nine months ended March 31, 2013 is a \$10.5 million regulatory milestone achieved under our collaboration agreement with Roche and \$11.1 million of license revenue earned upon the execution of a development and commercialization license by Novartis. The amount of license and milestone fees we earn is directly related to the number of our collaborators, the collaborators' advancement of the product candidates, and the overall success in the clinical trials of the product candidates. As such, the amount of license and milestone fees may vary significantly from quarter to quarter and year to year. Total revenue from license and milestone fees recognized from each of our collaborative partners in the nine-month periods ended March 31, 2014 and 2013 is included in the following table (in thousands):

| License and Milestone Fees | Nine Months Ended March 31, | |
|-------------------------------|-----------------------------|------------------|
| | 2014 | 2013 |
| Collaborative Partner: | | |
| Amgen | \$ 2,347 | \$ 742 |
| Bayer HealthCare | | 521 |
| Biotest | 19 | 19 |
| Lilly | 7,824 | |
| Novartis | 18,307 | 11,090 |
| Sanofi | 653 | 500 |
| Roche | 10,000 | 10,500 |
| Total | \$ 39,150 | \$ 23,372 |

Table of Contents

In February 2013, the U.S. FDA granted marketing approval to Kadcyła, a product resulting from one of our development and commercialization licenses with Roche, through its Genentech unit. We receive royalty reports and payments related to sales of Kadcyła from Roche one quarter in arrears. In accordance with our revenue recognition policy, \$6.9 million of royalties on net sales of Kadcyła for the nine-month period ended December 31 2013 were recorded and included in royalty revenue for the nine months ended March 31, 2014. No royalty revenue was recorded in the nine-month period ended March 31, 2013. We expect royalty revenue to increase in future periods as the underlying net sales of Kadcyła increase.

Research and development support revenue was \$5.9 million for the nine months ended March 31, 2014 compared with \$5.7 million for the nine months ended March 31, 2013. These amounts primarily represent research funding earned based on actual resources utilized under our agreements with our collaborators shown in the table below. Also included in research and development support revenue are fees for developing antibody-specific conjugation processes on behalf of our collaborators and potential collaborators during the early evaluation and preclinical testing stages of drug development. The amount of research and development support revenue we earn is directly related to the number of our collaborators and potential collaborators, the stage of development of our collaborators' product candidates and the resources our collaborators allocate to the development effort. As such, the amount of research and development support revenue may vary widely from quarter to quarter and year to year. Total revenue recognized from research and development support from each of our collaborative partners in the nine-month periods ended March 31, 2014 and 2013 is included in the following table (in thousands):

| Research and Development Support Collaborative Partner: | Nine Months Ended March 31, | |
|--|-----------------------------|----------|
| | 2014 | 2013 |
| Amgen | \$ 367 | \$ 339 |
| Biotest | 601 | 705 |
| Lilly | 2,127 | 583 |
| Novartis | 2,731 | 3,934 |
| Other | 34 | 109 |
| Total | \$ 5,860 | \$ 5,670 |

Clinical materials revenue decreased \$465,000 in the nine months ended March 31, 2014 to \$2.2 million from \$2.7 million in the nine months ended March 31, 2013. We are compensated at negotiated prices which are generally consistent with what other third-parties would charge. The amount of clinical materials revenue we earn, and the related cost of clinical materials charged to research and development expense, is directly related to the number of clinical trials our collaborators who use us to manufacture clinical materials are preparing or have underway, the speed of enrollment in those trials, the dosage schedule of each clinical trial and the time period, if any, during which patients in the trial receive clinical benefit from the clinical materials, and the demand our collaborators have for clinical-grade material for process development and analytical purposes. As such, the amount of clinical materials revenue and the related cost of clinical materials charged to research and development expense may vary significantly from quarter to quarter and year to year.

Research and Development Expenses

Research and development expense for the nine months ended March 31, 2014 increased \$14.5 million to \$81.2 million from \$66.7 million for the nine months ended March 31, 2013. During the current nine-month period, we recorded a \$12.8 million non-cash charge to research and development expense for technology rights obtained under the collaboration agreement executed with CytomX in January 2014. Salaries and related expenses also increased due to additional headcount, increased incentive compensation and increased stock compensation costs. A more detailed discussion of research and development expense in the period follows.

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We are unable to accurately estimate which potential product candidates, if any, will eventually move into our internal preclinical research program. We are unable to reliably estimate the costs to develop these products as a result of the uncertainties related to discovery research efforts as well as preclinical and clinical testing. Our decision to move a product candidate into the clinical development phase is predicated upon the results of preclinical tests. We cannot accurately predict which, if any, of the discovery stage product candidates will advance from preclinical testing and move into our internal clinical development program. The clinical trial and regulatory approval processes for our product candidates that have advanced or that we intend to advance to clinical testing are lengthy, expensive and uncertain in both timing and outcome. As a result, the pace and timing of the clinical development of our product candidates is highly uncertain and may not ever result in approved products. Completion dates and development costs will vary significantly for each product candidate and are difficult to predict. A variety of factors, many of which are outside our control, could cause or contribute to the prevention or delay of the successful completion of our clinical trials, or delay

Table of Contents

or prevent our obtaining necessary regulatory approvals. The costs to take a product through clinical trials are dependent upon, among other factors, the clinical indications, the timing, size and design of each clinical trial, the number of patients enrolled in each trial, and the speed at which patients are enrolled and treated. Product candidates may be found to be ineffective or to cause unacceptable side effects during clinical trials, may take longer to progress through clinical trials than anticipated, may fail to receive necessary regulatory approvals or may prove impractical to manufacture in commercial quantities at reasonable cost or with acceptable quality.

The lengthy process of securing FDA approvals for new drugs requires the expenditure of substantial resources. Any failure by us to obtain, or any delay in obtaining regulatory approvals would materially adversely affect our product development efforts and our business overall. Accordingly, we cannot currently estimate, with any degree of certainty, the amount of time or money that we will be required to expend in the future on our product candidates prior to their regulatory approval, if such approval is ever granted. As a result of these uncertainties surrounding the timing and outcome of our clinical trials, we are currently unable to estimate when, if ever, our product candidates that have advanced into clinical testing will generate revenues and cash flows.

We do not track our research and development costs by project. Since we use our research and development resources across multiple research and development projects, we manage our research and development expenses within each of the categories listed in the following table and described in more detail below (in thousands):

| Research and Development Expense | Nine Months Ended March 31, | |
|--|-----------------------------|-----------|
| | 2014 | 2013 |
| Research | \$ 25,983 | \$ 12,958 |
| Preclinical and Clinical Testing | 24,819 | 20,244 |
| Process and Product Development | 6,113 | 5,774 |
| Manufacturing Operations | 24,256 | 27,698 |
| Total Research and Development Expense | \$ 81,171 | \$ 66,674 |

Research: Research includes expenses primarily associated with activities to identify and evaluate new targets and to develop and evaluate new antibodies, linkers and cytotoxic agents for our products and in support of our collaborators. Such expenses primarily include personnel, contract services, research licensing fees, facilities and lab supplies. Research expenses for the nine months ended March 31, 2014 increased \$13.0 million compared to the nine months ended March 31, 2013. This increase is primarily due to a \$12.8 million non-cash charge recorded for technology rights obtained under the collaboration agreement executed with CytomX in January 2014. As a result of this non-cash charge, we expect research expenses for fiscal 2014 to be significantly higher than fiscal 2013.

Preclinical and Clinical Testing: Preclinical and clinical testing includes expenses related to preclinical testing of our own and, in certain instances, our collaborators' product candidates, regulatory activities, and the cost of our own clinical trials. Such expenses include personnel, patient enrollment at our clinical testing sites, consultant fees, contract services, and facility expenses. Preclinical and clinical testing expenses for the nine months ended March 31, 2014 increased \$4.6 million to \$24.8 million compared to \$20.2 million for the nine months ended March 31, 2013. This increase is primarily the result of higher salaries and related expenses. We expect preclinical and clinical testing expenses for fiscal 2014 to be significantly higher than fiscal 2013 due to increased activities to advance our wholly owned product candidates.

Process and Product Development: Process and product development expenses include costs for development of clinical and commercial manufacturing processes for our own and collaborator compounds. Such expenses include the costs of personnel, contract services and facility expenses. For the nine months ended March 31, 2014, total development expenses increased \$339,000 compared to the nine months ended March 31, 2013. This increase is primarily the result of an increase in salaries and related expenses and an increase in contract service expense

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driven primarily by development activities for IMGN779. We expect process and product development expenses for fiscal 2014 to be marginally higher than fiscal 2013.

Manufacturing Operations: Manufacturing operations expense includes costs to manufacture preclinical and clinical materials for our own and our collaborator s product candidates, and quality control and quality assurance activities and costs to support the operation and maintenance of our conjugate manufacturing facility. Such expenses include personnel, raw materials for our and our collaborators preclinical studies and clinical trials, development costs with contract manufacturing organizations, manufacturing supplies, and facilities expense. For the nine months ended March 31, 2014, manufacturing operations expense decreased \$3.4 million to \$24.3 million compared to \$27.7 million in the same period last year. The decrease in the nine months ended March 31, 2014 as compared to the nine months ended March 31, 2013 is primarily the result of (i) a decrease in antibody development and supply expense driven primarily by supply required for our IMGN289 program and pivotal activities for our IMGN901 program during the prior period; (ii) a decrease in fill/finish costs due primarily to costs to transfer our internal programs to a new supplier during the prior year period; and (iii) an increase in costs capitalized into inventory due to a greater number of manufactured batches of conjugated materials on behalf of our collaborators. Partially offsetting these decreases, salaries and related

Table of Contents

expenses increased during the current period and contract service expense increased due primarily to increased study activities related to our cytotoxic agents. We expect manufacturing operations expense for fiscal 2014 to be higher than fiscal 2013 due primarily to increased activities to advance our wholly owned product candidates.

General and Administrative Expenses

General and administrative expenses for the nine months ended March 31, 2014 increased \$1.9 million to \$18.0 million compared to \$16.1 million for the nine months ended March 31, 2013. This increase is primarily due to an increase in salaries and related expenses, as well as an increase in professional service fees, particularly consulting fees and patent expenses. We expect general and administrative expenses for fiscal 2014 to be higher than fiscal 2013 due primarily to increased salaries and related expenses, patent activities and other professional services.

Other (Expense) Income, net

Other (expense) income, net for the nine months ended March 31, 2014 and 2013 is included in the following table (in thousands):

| Other (Expense) Income, net | Nine Months Ended March 31, | |
|------------------------------------|------------------------------------|-------------|
| | 2014 | 2013 |
| Interest Income | \$ 33 | \$ 112 |
| Other Income, net | 133 | 20 |
| Total Other (Expense) Income, net | \$ 166 | \$ 132 |

LIQUIDITY AND CAPITAL RESOURCES

| | As of | |
|---------------------------|---------------------------|--------------------------|
| | March 31, 2014 | June 30, 2013 |
| | (In thousands) | |
| Cash and cash equivalents | \$ 164,076 | \$ 194,960 |
| Working capital | 151,147 | 181,511 |
| Shareholders' equity | 97,934 | 121,847 |

| | Nine Months Ended March 31, | |
|---------------------------------------|------------------------------------|-------------|
| | 2014 | 2013 |
| | (In thousands) | |
| Cash used for operating activities | \$ (34,729) | \$ (48,687) |
| Cash used for investing activities | (4,712) | (2,357) |
| Cash provided by financing activities | 8,557 | 96,209 |

Cash Flows

We require cash to fund our operating expenses, including the advancement of our own clinical programs, and to make capital expenditures. Historically, we have funded our cash requirements primarily through equity financings in public markets and payments from our collaborators, including license fees, milestones and research funding. In fiscal year 2013, we also began to receive royalties from one collaborator. As of March 31, 2014, we had approximately \$164.1 million in cash and cash equivalents. Net cash used for operations was \$34.7 million and \$48.7 million for the nine months ended March 31, 2014 and 2013, respectively. The principal use of cash for operating activities for both periods presented was to fund our net loss, adjusted for non-cash items.

Net cash used for investing activities was \$4.7 million and \$2.4 million for the nine months ended March 31, 2014 and 2013, respectively, and primarily represents cash outflows for capital expenditures. Capital expenditures, primarily for the purchase of new equipment and leasehold improvements, were \$4.7 million and \$2.4 million for the nine-month periods ended March 31, 2014 and 2013, respectively.

Net cash provided by financing activities was \$8.6 million and \$96.2 million for the nine months ended March 31, 2014 and 2013, respectively, which represents proceeds from the exercise of approximately 1.0 million and 378,000 stock options, respectively. Also, pursuant to a public offering in the prior year period, we issued and sold 6,250,000 shares of our common stock resulting in net proceeds of \$94.0 million.

Table of Contents

We anticipate that our current capital resources and expected future collaborator payments under existing collaborations will enable us to meet our operational expenses and capital expenditures at least through fiscal year 2015. However, we cannot provide assurance that such future collaborative agreement funding will, in fact, be received. Should we or our partners not meet some or all of the terms and conditions of our various collaboration agreements, we may be required to pursue additional strategic partners, secure alternative financing arrangements, and/or defer or limit some or all of our research, development and/or clinical projects.

Contractual Obligations

There have been no material changes to our contractual obligations during the current period from those disclosed in our Annual Report on Form 10-K for the fiscal year ended June 30, 2013.

Recent Accounting Pronouncements

In July 2013, the FASB issued guidance to address the diversity in practice related to the financial statement presentation of unrecognized tax benefits as either a reduction of a deferred tax asset or a liability when a net operating loss carryforward, a similar tax loss, or a tax credit carryforward exists. This guidance is effective prospectively for fiscal years, and interim periods within those years, beginning after December 15, 2013. The adoption of this guidance is not expected to have a material impact on our consolidated financial statements.

Forward-Looking Statements

This quarterly report includes forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995. These statements relate to analyses and other information which are based on forecasts of future results and estimates of amounts that are not yet determinable. These statements also relate to our future prospects, developments and business strategies.

These forward-looking statements can be identified by their use of terms and phrases, such as anticipate, believe, could, estimate, expect, in, may, plan, predict, project, will and other similar terms and phrases, including references to assumptions. They may also use words such as would, should, could or may. These forward-looking statements involve known and unknown risks, uncertainties and other factors that may cause actual results to be materially different from those contemplated by our forward-looking statements. These known and unknown risks, uncertainties and other factors are described in detail in the Risk Factors section and in other sections of this Annual Report on Form 10-K for the year ended June 30, 2013. We disclaim any intention or obligation to update or revise any forward-looking statements, whether as a result of new information, future events or otherwise.

Kadcyla® is a registered trademark of Genentech, Inc., a member of the Roche Group.

Probody is a trademark of CytomX Therapeutics, Inc.

OFF-BALANCE SHEET ARRANGEMENTS

None.

ITEM 3. *Quantitative and Qualitative Disclosure about Market Risk*

Our market risks, and the ways we manage them, are summarized in Part II, Item 7A, *Quantitative and Qualitative Disclosures About Market Risk* of our Annual Report on Form 10-K for the fiscal year ended June 30, 2013. Since then there have been no material changes to our market risks or to our management of such risks.

ITEM 4. *Controls and Procedures*

(a) *Disclosure Controls and Procedures*

The Company's management, with the participation of its principal executive officer and principal financial officer, has evaluated the effectiveness of the Company's disclosure controls and procedures (as defined in Rules 13a-15(e) or 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 Quarterly Report on Form 10-Q. Based on such evaluation, the Company's principal executive officer and principal financial officer have concluded that, as of the end of such period, the Company's disclosure controls and procedures were adequate and effective.

Table of Contents

(b) *Changes in Internal Controls*

There have not been any changes in the Company's internal control over financial reporting (as such term is defined in Rules 13a-15(f) and 15d-15(f) under the Exchange Act) during the quarter ended March 31, 2014 that have materially affected, or are reasonably likely to materially affect, the Company's internal control over financial reporting.

PART II. OTHER INFORMATION

ITEM 1A. *Risk Factors*

You should carefully review and consider the information regarding certain factors that could materially affect our business, financial condition or future results set forth under Item 1A. (Risk Factors) in our Annual Report on Form 10-K for the fiscal year ended June 30, 2013. There have been no material changes from the factors disclosed in our 2013 Annual Report on Form 10-K, although we may disclose changes to such factors or disclose additional factors from time to time in our future filings with the Securities and Exchange Commission.

Table of Contents

ITEM 6. Exhibits

| Exhibit No. | Description |
|--------------------|--|
| 10.1 | Second Amendment to Lease Agreement dated April 28, 2014 by and between Intercontinental Fund II 830 Winter Street LLC, landlord, and the Registrant |
| 10.2 | Employment offer letter between the Registrant and Ellie Harrison |
| 10.3 | Change in Control Severance Agreement dated as of February 20, 2014 between the Registrant and Ellie Harrison |
| 31.1 | Certification of Principal Executive Officer under Section 302 of the Sarbanes-Oxley Act of 2002. |
| 31.2 | Certification of Principal Financial Officer under Section 302 of the Sarbanes-Oxley Act of 2002. |
| 32 | Certifications of Principal Executive Officer and Principal Financial Officer under Section 906 of the Sarbanes-Oxley Act of 2002. |
| 101.INS | XBRL Instance Document |
| 101.SCH | XBRL Taxonomy Extension Schema |
| 101.CAL | XBRL Taxonomy Extension Calculation Linkbase |
| 101.DEF | XBRL Taxonomy Extension Definition Linkbase |
| 101.LAB | XBRL Taxonomy Extension Label Linkbase |
| 101.PRE | XBRL Taxonomy Extension Presentation Linkbase |

* Portions of this Exhibit were omitted, as indicated by [***], and have been filed separately with the Secretary of the Commission pursuant to the Registrant's application requesting confidential treatment.

Furnished, not filed.

Table of Contents

SIGNATURES

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

ImmunoGen, Inc.

Date: May 2, 2014

By:

/s/ Daniel M. Junius
Daniel M. Junius
President, Chief Executive Officer (Principal
Executive Officer)

Date: May 2, 2014

By:

/s/ David B. Johnston
David B. Johnston
Executive Vice President, Chief Financial Officer
(Principal Financial and Accounting Officer)