ANTIGENICS INC /DE/
Form 10-Q
November 14, 2007
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UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, DC 20549

Form 10-Q

x QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the Quarterly Period Ended September 30, 2007

¨ TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the transition period from _____ to _____

Commission File No. 000-29089

Antigenics Inc.

(Exact Name of Registrant as Specified in its Charter)

Delaware	**06-1562417**
(State of Incorporation)	***(I.R.S. Employer Identification Number)***
162 Fifth Avenue, Suite 900, New York, New York	**10010**
(Address of Principal Executive Offices)	***(Zip Code)***

(212) 994-8200

(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 x No ¨

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

Large accelerated filer ¨ Accelerated filer x Non-accelerated filer ¨

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

Number of shares outstanding of the registrant s Common Stock as of November 1, 2007: 47,551,695 shares.

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Antigenics Inc.

Quarterly Period Ended September 30, 2007

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PART I FINANCIAL INFORMATION

Item 1 *Financial Statements*

ANTIGENICS INC. AND SUBSIDIARIES

CONDENSED CONSOLIDATED BALANCE SHEETS

(Unaudited)

	September 30, 2007	December 31, 2006
ASSETS		
Cash and cash equivalents	$ 21,613,539	$ 24,218,683
Short-term investments	3,249,996	15,876,302
Accounts receivable	323,594	182,493
Inventories	472,901	438,644
Prepaid expenses	1,213,715	1,307,648
Other current assets	249,615	274,652
Total current assets	27,123,360	42,298,422
Plant and equipment, net	15,580,802	18,618,632
Goodwill	2,572,203	2,572,203
Core and developed technology, net	3,810,864	4,641,311
Debt issuance costs, net	1,455,292	1,623,570
Other long-term assets	2,092,986	3,197,403
Total assets	$ 52,635,507	$ 72,951,541
LIABILITIES AND STOCKHOLDERS DEFICIT		
Current portion, long-term debt	$ 146,061	$ 146,061
Accounts payable	986,930	1,089,567
Accrued liabilities	6,570,938	7,586,378
Other current liabilities	670,792	255,735
Total current liabilities	8,374,721	9,077,741
Convertible senior notes	76,346,667	75,333,333
Other long-term liabilities	7,410,167	5,933,935
Commitments and contingencies (Note F)		
STOCKHOLDERS DEFICIT		
Preferred stock, par value $0.01 per share; 25,000,000 shares authorized:		
Series A convertible preferred stock; 31,620 shares designated, issued, and outstanding at September 30, 2007 and December 31, 2006; liquidation value of $31,817,625 at September 30, 2007	316	316
Series B1 convertible preferred stock; 10,000 and 0 shares designated, issued, and outstanding at September 30, 2007 and December 31, 2006, respectively	100	
Series B2 convertible preferred stock; 5,250 and 0 shares designated, issued, and outstanding at September 30, 2007 and December 31, 2006, respectively	53	
Common stock, par value $0.01 per share; 250,000,000 and 100,000,000 shares authorized at September 30, 2007 and December 31, 2006, respectively; 47,550,743 and 45,843,751 shares issued and outstanding at September 30, 2007 and December 31, 2006, respectively	475,507	458,438
Additional paid-in-capital	451,206,985	444,013,527

Accumulated other comprehensive income (loss)	104	(21,853)
Accumulated deficit	(491,179,113)	(461,843,896)
Total stockholders deficit	(39,496,048)	(17,393,468)
Total liabilities and stockholders deficit	$ 52,635,507	$ 72,951,541

See accompanying notes to unaudited condensed consolidated financial statements.

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ANTIGENICS INC. AND SUBSIDIARIES

CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS

(Unaudited)

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2007	2006	2007	2006
Revenue	$ 862,631	$ 216,462	$ 4,659,020	$ 372,399
Operating expenses:				
Research and development	(6,132,653)	(6,251,777)	(18,145,535)	(22,627,949)
General and administrative	(4,579,887)	(4,740,556)	(13,311,193)	(16,023,075)
Restructuring costs				(1,374,293)
Operating loss	(9,849,909)	(10,775,871)	(26,797,708)	(39,652,918)
Other income (expense):				
Non-operating income		120,000		140,528
Interest expense	(1,261,773)	(747,435)	(3,722,254)	(2,222,671)
Interest income	325,386	381,865	1,184,745	1,391,147
Net loss	(10,786,296)	(11,021,441)	(29,335,217)	(40,343,914)
Dividends on convertible preferred stock	(197,625)	(197,625)	(592,875)	(592,875)
Net loss attributable to common stockholders	$ (10,983,921)	$ (11,219,066)	$ (29,928,092)	$ (40,936,789)
Per common share data, basic and diluted:				
Net loss attributable to common stockholders	$ (0.24)	$ (0.24)	$ (0.65)	$ (0.89)
Weighted average number of common shares outstanding, basic and diluted	46,429,973	45,847,666	46,126,316	45,789,401

See accompanying notes to unaudited condensed consolidated financial statements.

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ANTIGENICS INC. AND SUBSIDIARIES

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

(Unaudited)

	Nine Months Ended September 30,	
	2007	**2006**
Cash flows from operating activities:		
Net loss	$ (29,335,217)	$ (40,343,914)
Adjustments to reconcile net loss to net cash used in operating activities:		
Depreciation and amortization	4,094,730	4,252,042
Stock-based compensation	3,248,677	1,762,868
Non-cash interest expense	1,013,334	
Write-down of plant and equipment		645,819
Loss on sale of assets		37,900
Changes in operating assets and liabilities:		
Accounts receivable	(141,101)	(76,186)
Inventories	(34,257)	33,051
Prepaid expenses	93,933	(155,650)
Accounts payable	(112,740)	(380,755)
Increase in deferred revenue	1,477,044	2,901,766
Accrued liabilities and other current liabilities	(858,742)	(4,402,669)
Other operating assets and liabilities	55,283	(212,522)
Net cash used in operating activities	(20,499,056)	(35,938,250)
Cash flows from investing activities:		
Proceeds from maturities of available-for-sale securities	22,750,000	21,050,000
Purchases of available-for-sale securities	(10,101,737)	(1,333,146)
Investment in AGTC	(165,000)	(285,000)
Proceeds from the sale of limited partner interest in AGTC	1,665,000	
Proceeds from sale of equipment		33,257
Purchases of plant and equipment	(8,174)	(108,895)
Decrease in restricted cash		2,814,232
Net cash provided by investing activities	14,140,089	22,170,448
Cash flows from financing activities:		
Net proceeds from sale of equity	4,745,340	
Deferred offering costs	(426,640)	
Proceeds from exercise of stock options		272,109
Proceeds from employee stock purchases	77,998	197,191
Payments of series A convertible preferred stock dividends	(592,875)	(592,875)
Debt issuance costs	(50,000)	
Payments of long-term debt		(3,810,737)
Net cash provided by (used in) financing activities	3,753,823	(3,934,312)
Net decrease in cash and cash equivalents	(2,605,144)	(17,702,114)
Cash and cash equivalents, beginning of period	24,218,683	33,216,876
Cash and cash equivalents, end of period	$ 21,613,539	$ 15,514,762

See accompanying notes to unaudited condensed consolidated financial statements.

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ANTIGENICS INC. AND SUBSIDIARIES

NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

September 30, 2007

Note A Business and Basis of Presentation

Antigenics Inc. (including its subsidiaries, also referred to in this Quarterly Report on Form 10-Q as Antigenics , the Company , we , us , and ou is a biotechnology company developing technologies and product candidates to treat cancers and infectious diseases, primarily based on immunological approaches. Our most advanced product candidate is Oncophage® (vitespen), a patient-specific therapeutic cancer vaccine candidate that has been tested in Phase 3 clinical trials for the treatment of renal cell carcinoma, the most common type of kidney cancer, and for metastatic melanoma. Oncophage has also been tested in Phase 1 and Phase 2 clinical trials in a range of indications and is currently in a Phase 2 clinical trial in recurrent glioma, or brain cancer. Our product candidate portfolio also includes: (1) QS-21 Stimulon® adjuvant (QS-21), which is used in numerous vaccines under development for a variety of diseases, including hepatitis, human immunodeficiency virus (HIV), influenza, cancer, Alzheimer s disease, malaria, and tuberculosis; (2) AG-707, a therapeutic vaccine program in a Phase 1 clinical trial for the treatment of genital herpes; and (3) Aroplatin , a liposomal chemotherapeutic in a Phase 1 clinical trial for the treatment of solid tumors and B-cell lymphomas. Our related business activities include research and development, regulatory and clinical affairs, clinical manufacturing, business development, marketing, and administrative functions that support these activities.

On March 24, 2006, we announced top-line results from part I of our Phase 3 study of Oncophage in renal cell carcinoma patients who are at high risk of recurrence after surgery, indicating that the trial did not meet its primary endpoint. The analysis was triggered based on the number of events (defined as recurrence of disease or death of a patient prior to recurrence) reported by study investigators. However, an independent review by the trial s Clinical Events Committee revealed that substantially fewer events had actually occurred. The analysis showed a trend in favor of Oncophage for recurrence-free survival (RFS the study s primary endpoint), and a trend against Oncophage for overall survival (OS a secondary endpoint); however neither finding was statistically significant. The analysis of the OS endpoint was considered an interim assessment. It was unclear why opposing trends were observed between RFS and OS. Importantly, there was no readily apparent adverse safety signal associated with the vaccine that we believe could be contributing to this finding.

Based on these results, we implemented a restructuring plan in April 2006 that refocused our programs and priorities resulting in the temporary discontinuation of all late-stage clinical programs and concentration on Phase 1 and preclinical programs, including those stated above for Aroplatin and AG-707, and AU-801, a novel preclinical application of our proprietary heat shock protein technology as a treatment for autoimmune disorders. In addition, we terminated part II of our Phase 3 renal cell carcinoma trial and our Phase 2 trial of AG-858 for the treatment of chronic myelogenous leukemia. To match these priorities, we eliminated 42 positions in April 2006. In September 2006, we discontinued activities related to AU-801. We continue to support and develop our QS-21 partnering collaborations, with the goal of generating royalties from this product in the 2010 timeframe.

On June 5, 2006, we announced the updated results from our Phase 3 trial of Oncophage in metastatic melanoma, and on June 7, 2006, we announced the results of an in-depth analysis of the data from part I of our Phase 3 trial of Oncophage in renal cell carcinoma. Based on these results, we decided to continue to collect data from our Phase 3 trial of Oncophage in renal cell carcinoma before making a decision regarding future pivotal clinical trials or seeking registration of Oncophage in the U.S.

On May 21, 2007, we announced additional follow-up results on data collected per the protocol through March 2007. The end-of-study results, which reflect an additional 17 months data collection, showed that in a substantial subset of better-prognosis patients (n = 362) at intermediate risk for disease recurrence, Oncophage demonstrated a clinically significant improvement in RFS of approximately 45 percent (*p* value of less than 0.01 and hazard ratio of 0.55). In addition, updated analysis in this group of intermediate risk patients revealed a trend towards improved OS, the study s secondary endpoint. Furthermore, the positive OS trend observed to date correlates with the RFS improvement demonstrated in previous analyses.

The Eastern Cooperative Oncology Group is currently sponsoring a large adjuvant renal cell carcinoma trial that stratifies patients by certain prognostic risk factors for recurrence, and puts patients into intermediate risk, high risk, and very high risk categories. We are able to apply these definitions to the data generated as part of our Phase 3 trial of Oncophage in renal cell carcinoma and it is in the intermediate risk population where significant improvement over observation is demonstrated.

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NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (continued)

We continue to analyze the data collected to date, and we have also opened a subsequent protocol that will continue to follow patients in the format of a registry in order to collect OS information, as well as investigator reports of disease recurrence. The registry, which is expected to provide additional data on the effectiveness of Oncophage, will follow patients for an additional three years from closure of the initial trial, providing more than five years worth of data collection from the last patient enrolled. This continued data collection and our ongoing analysis is uncertain, and may negatively affect or not affect the acceptability of the overall results of the trial, and even if clinically meaningful, may not meet the requirements of the U.S. Food and Drug Administration (the FDA) or other regulatory authorities for submission and approval of a marketing application or similar ex-U.S. applications for product approval.

Guidance received from past discussions with the FDA indicates that further clinical studies must be conducted to demonstrate to them the efficacy and safety of Oncophage. We intend to seek a meeting with the FDA to discuss the results of the updated analyses utilizing data through March 2007 to determine whether there is an opportunity to file a biologics license application (BLA) on the basis of these results with appropriate commitments to conduct further clinical investigations to support the efficacy of Oncophage in renal cell carcinoma. Because evidence of clinically significant improvement has been observed in a subgroup analysis and was not demonstrated in the pre-specified analysis of the primary and secondary endpoints of the Phase 3 study of Oncophage in renal cell carcinoma, based on existing standards this trial is likely not sufficient to support a BLA for product approval. Furthermore, this trial may not be sufficient to support approval outside of the U.S.

We are exploring the additional steps necessary to seek approval of Oncophage in ex-U.S. markets. This exploration process includes, but is not limited to, formal and informal discussions with international regulatory authorities, key opinion leaders, and consultants with country-specific regulatory experience regarding potential applications for full or conditional marketing approvals and/or named patient programs. In conjunction with this process, on June 25, 2007, we completed the submission of an application for marketing authorization with the Russian Ministry of Public Health for the use of Oncophage in the treatment of kidney cancer patients at intermediate risk for disease recurrence. We cannot predict the outcome of this application.

As detailed in Note G, on July 6, 2006, we entered into expanded license and supply agreements with GlaxoSmithKline Biologicals SA (GSK) for the use of QS-21, an investigational adjuvant used in numerous vaccines under development. In conjunction with our expanded license and supply agreements with GSK, we received a $3.0 million up-front non-refundable payment in July 2006. In February 2007, we achieved a milestone related to the transfer of manufacturing technologies to GSK and received a payment of $2.0 million.

On July 20, 2007, we executed a binding letter of intent (the Letter) with GSK amending the supply agreement to accelerate GSK s commercial grade QS-21 manufacturing rights previously granted in July 2006. As consideration for our entering into the Letter, we received a $2.0 million up-front non-refundable payment from GSK in August 2007, in lieu of a milestone payment that would have otherwise been payable under the supply agreement. In addition, GSK is obligated to pay us $5.25 million over five years for manufacturing profits that were anticipated to have otherwise been payable under the supply agreement. Except as expressly provided in the Letter, all other financial obligations of GSK under the supply agreement, including royalty payments, remain unchanged. The Letter does not affect the rights and obligations of the parties under the July 6, 2006 license agreement.

On September 10, 2007, we issued 1,623,377 shares of our common stock at a price of $3.08 per share to a single institutional investor. In conjunction with this transaction, we also issued to the investor 15,250 shares of our newly created class B convertible preferred stock. Gross proceeds of $5.0 million were received as a result of this transaction. Net proceeds, after deducting the placement agent fees and offering expenses paid by us, were $4.7 million. See Note H for further details on this transaction.

The accompanying condensed consolidated balance sheet as of December 31, 2006, which has been derived from audited consolidated financial statements, and the unaudited interim condensed consolidated financial statements have been prepared in accordance with U.S. generally accepted accounting principles for interim financial information and with the instructions to

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ANTIGENICS INC. AND SUBSIDIARIES

NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (continued)

Article 10 of Regulation S-X. Accordingly, they do not include all of the information and footnotes required by U.S. generally accepted accounting principles for complete annual consolidated financial statements. In the opinion of management, the condensed consolidated financial statements include all normal and recurring adjustments considered necessary for a fair presentation of our consolidated financial position and operating results. All significant intercompany transactions and accounts have been eliminated in consolidation. Certain amounts previously reported have been reclassified in order to conform to the current period s presentation. Operating results for the nine-month period ended September 30, 2007 are not necessarily indicative of the results that may be expected for the year ending December 31, 2007. For further information, refer to our consolidated financial statements and footnotes thereto included in our Annual Report on Form 10-K for the year ended December 31, 2006 filed with the Securities and Exchange Commission (the SEC) on March 16, 2007.

The preparation of consolidated financial statements in conformity with U.S. generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosures of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Management bases its estimates on historical experience and on various assumptions that are believed to be reasonable under the circumstances. Actual results could differ materially from those estimates.

We have incurred annual operating losses since inception and, as a result, at September 30, 2007 we had an accumulated deficit of $491.2 million. Our operations have been funded principally by sales of equity and convertible debt instruments. We believe that, based on our current plans and activities, our working capital resources at September 30, 2007, along with the estimated proceeds from our license, supply, and collaborative agreements, will be sufficient to satisfy our liquidity requirements into 2008. Satisfying our long-term liquidity needs may require the successful commercialization of product candidates and will require additional capital.

Our lead product candidates require clinical trials and approvals from regulatory agencies, as well as acceptance in the marketplace. We are conducting clinical trials in various cancers and in one infectious disease indication. Although we believe our patents, patent rights, and patent applications are valid, the invalidation of our patents or failure of certain of our pending patent applications to issue as patents could have a material adverse effect upon our business. Part of our strategy is to develop and commercialize some of our product candidates by continuing our existing collaborative arrangements with academic and corporate collaborators and licensees and by entering into new collaborations. Our success depends, in part, on the success of these parties in performing research and preclinical and clinical testing. We compete with specialized biotechnology companies, major pharmaceutical companies, universities, and research institutions. Many of these competitors have substantially greater resources than we do.

Note B Net Loss Per Share

Basic loss per common share (EPS) is calculated by dividing the net loss attributable to common stockholders by the weighted average number of common shares outstanding and common shares issuable under our directors deferred compensation plan. Diluted EPS is calculated by dividing the net loss attributable to common stockholders by the weighted average common shares outstanding plus the dilutive effect of outstanding stock options and nonvested shares, our series A convertible preferred stock, our class B convertible preferred stock, our 5.25% convertible senior notes due 2025, and the senior secured convertible notes (the 2006 Notes). Because we have reported a net loss attributable to common stockholders for all periods, diluted loss per common share is the same as basic loss per common share, as the effect of including shares underlying the outstanding stock options and nonvested shares, the series A convertible preferred stock, the class B convertible preferred stock, the 5.25% convertible senior notes due 2025, and the 2006 Notes in the calculation would have reduced the net loss per common share. Therefore, shares underlying the 7,535,061 outstanding stock options and nonvested shares, the 31,620 outstanding shares of series A convertible preferred stock, the 10,000 outstanding shares of series B1 convertible preferred stock, the 5,250 outstanding shares of series B2 convertible preferred stock, and the impact of conversion of the 5.25% convertible senior notes due 2025 and the 2006 Notes are not included in the calculation of diluted net loss per common share.

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ANTIGENICS INC. AND SUBSIDIARIES

NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (continued)

Note C Inventories

Inventories are stated at cost using the first-in, first-out method. The components of inventories are as follows (in thousands).

	September 30, 2007	December 31, 2006
Work in process	$ 425	$ 344
Finished goods	48	95
	$ 473	$ 439

Note D Stock-Based Compensation

Stock-based compensation expense includes compensation expense for all stock-based options granted prior to, but not yet vested as of, January 1, 2006, based on the grant date fair value estimated in accordance with the original provisions of Statement of Financial Accounting Standards (SFAS) No. 123, *Accounting for Stock-Based Compensation*. Stock-based compensation expense also includes compensation expense for all stock-based options granted, modified, or settled after January 1, 2006, based on the grant date fair value estimated in accordance with the provisions of SFAS No. 123R, *Share-Based Payment* (SFAS No. 123R) and the fair market value of shares issued to non-employees for services rendered.

We have applied the provisions of SEC Staff Accounting Bulletin (SAB) No. 107, *Share-Based Payment* (SAB No. 107), in accounting for stock-based compensation in accordance with SFAS No. 123R. SAB No. 107 contains the SEC s guidance on certain aspects of SFAS No. 123R and the valuation of share-based payments for public companies.

Stock options granted to non-employees are accounted for based on the fair-value method of accounting in accordance with SFAS No. 123R and Emerging Issues Task Force (EITF) Issue No. 96-18, *Accounting for Equity Instruments That Are Issued to Other Than Employees for Acquiring, or in Conjunction with Selling, Goods or Services.* As a result, the non-cash charge to operations for non-employee options with vesting or other performance criteria is affected each reporting period, until the non-employee options vest, by changes in the fair value of our common stock. Certain of our fully vested options granted to non-employees are outside the scope of SFAS No. 123R and are subject to EITF Issue No. 00-19, *Accounting for Derivative Financial Instruments Indexed to, and Potentially Settled in, a Company s Own Stock* (EITF Issue No. 00-19), which requires that stock options held by certain non-employee consultants be accounted for as liability-classified awards. The fair value of the award is remeasured at each financial statement date until the award is exercised or expires. As of September 30, 2007, stock options to acquire approximately 788,000 shares of common stock held by non-employee consultants are accounted for as liability-classified awards, and remained unexercised.

We used the Black-Scholes option pricing model to value options for employee populations, as well as our options granted to members of our Board of Directors. The effects of applying SFAS No. 123R, for purposes of recognizing compensation cost under such pronouncement, may not be representative of the effects on our reported results of operations for future years.

All stock option grants have a ten-year term and generally vest ratably over a four-year period. The fair value of each option granted is estimated on the date of grant with the following weighted average assumptions.

	Three Months Ended September 30,	Nine Months Ended September 30,

	2007	2006	2007	2006
Expected volatility	72%	75%	71%	67%
Expected term in years	6	6	6	5
Risk-free interest rate	5%	5%	5%	4%
Dividend yield	0%	0%	0%	0%

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ANTIGENICS INC. AND SUBSIDIARIES

NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (continued)

A summary of option activity for the nine months ended September 30, 2007 is presented below:

	Options	Weighted Average Exercise Price	Weighted Average Remaining Contractual Term (in years)	Aggregate Intrinsic Value
Outstanding at December 31, 2006	5,912,850	$ 7.17		
Granted	1,748,650	2.46		
Forfeited	(531,921)	8.64		
Outstanding at September 30, 2007	7,129,579	$ 5.90	7.03	$ 985,227
Vested or expected to vest at September 30, 2007	6,233,416	$ 6.24	6.74	$ 822,593
Exercisable at September 30, 2007	3,458,490	$ 8.35	4.97	$ 268,758

The weighted average grant-date fair value of options granted during the nine months ended September 30, 2007 and 2006 was $1.57 and $2.15, respectively.

During the first nine months of 2007, all options were granted with exercise prices equal to the fair market value of the underlying shares of common stock on the grant date.

As of September 30, 2007, $5.7 million of total unrecognized compensation cost related to stock options granted to employees and directors is expected to be recognized over a weighted-average period of approximately one year.

As of September 30, 2007, unrecognized expense for options granted to outside advisors for which performance (vesting) has not yet been completed is approximately $425,000.

Certain employees have also been granted nonvested stock. In accordance with SFAS No. 123R, the fair value of nonvested stock is calculated based on the closing sale price of the Company s common stock on the date of issuance.

A summary of nonvested stock activity for the nine months ended September 30, 2007 is presented below:

	Nonvested Shares	Weighted Average

		Grant Date Fair Value
Outstanding at December 31, 2006	52,670	$ 4.60
Granted	406,531	1.83
Vested	(17,102)	4.64
Forfeited	(36,617)	2.07
Outstanding at September 30, 2007	405,482	$ 2.05

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ANTIGENICS INC. AND SUBSIDIARIES

NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (continued)

As of September 30, 2007, there was $573,000 of unrecognized stock-based compensation expense related to these nonvested shares. This cost is expected to be recognized over a weighted-average period of one year.

We issue new shares upon option exercises, purchases under the 1999 Employee Stock Purchase Plan (the 1999 ESPP), vesting of nonvested stock, and under the Director s Deferred Compensation Plan. During the year ended December 31, 2006, 185,660 options were exercised with a weighted average exercise price of $1.47. No options were exercised during the nine months ended September 30, 2007. During the year ended December 31, 2006 and for the nine months ended September 30, 2007, 66,875 shares and 48,813 shares were issued under the 1999 ESPP, respectively. During the nine months ended September 30, 2007, 10,840 shares, net of shares withheld to cover personal income tax withholding, were issued as a result of the vesting of nonvested stock. In addition, during the nine months ended September 30, 2007, 15,629 shares were issued under our Directors Deferred Compensation Plan. No such shares were issued during the year ended December 31, 2006.

The impact on our results of operations from stock-based compensation was as follows (in thousands).

	Three Months Ended		Nine Months Ended	
	September 30,		September 30,	
	2007	2006	2007	2006
Research and development	$ 256	$ 277	$ 1,344	$ (386)
General and administrative	713	680	1,905	2,149
Total stock-based compensation expense	$ 969	$ 957	$ 3,249	$ 1,763

Note E Comprehensive Loss

The following table provides the calculation of comprehensive loss (in thousands).

	Three Months Ended		Nine Months Ended	
	September 30,		September 30,	
	2007	2006	2007	2006
Net loss	$ (10,786)	$ (11,021)	$ (29,335)	$ (40,344)
Other comprehensive income:				
Unrealized gain on available-for-sale securities, net	7	24	22	60
Comprehensive loss	$ (10,779)	$ (10,997)	$ (29,313)	$ (40,284)

Note F Commitments and Contingencies

Antigenics, our Chairman and Chief Executive Officer, Garo H. Armen, Ph.D., and two investment banking firms that served as underwriters in our initial public offering have been named as defendants in a civil class action lawsuit filed on November 5, 2001 in the Federal District Court for the Southern District of New York on behalf of a class of purchasers of our stock between February 3, 2000 and December 6, 2000. Similar complaints were filed against about 300 other issuers, their underwriters, and in many instances their directors and officers. These cases have been coordinated under the caption *In re Initial Public Offering Securities Litigation*, Civ. No. 21 MC 92 (SAS), by order dated August 9, 2001. The suit against Antigenics and Dr. Armen alleges that the brokerage arms of the investment banking firms charged secret excessive

commissions to certain of their customers in return for allocations of our stock in the offering. The suit also alleges that shares of our stock were allocated to certain of the investment banking firms customers based upon agreements by such customers to purchase additional shares of our stock in the secondary market. The complaint alleges that Antigenics is liable under Section 11 of the Securities Act of 1933, as amended (the Securities Act), and Dr. Armen is liable under Sections 11 and 15 of the Securities Act because our registration statement did not disclose these alleged practices. On April 19, 2002, the plaintiffs in this action filed an amended class action complaint, which contains new allegations. Again, similar amended complaints were filed with respect to the other companies. In addition to the claims in the earlier complaint, the amended complaint alleges that Antigenics and Dr. Armen violated Sections 10(b) and 20 of the Securities Exchange Act of 1934, as amended (the Securities Exchange Act) and SEC Rule 10b-5 by making false and misleading statements and/or omissions in order to inflate our stock price and conceal the investment banking firms alleged secret arrangements. The claims against Dr. Armen, in his individual capacity, have been dismissed without prejudice. On July 15, 2002, Antigenics and Dr. Armen joined the Issuer

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ANTIGENICS INC. AND SUBSIDIARIES

NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (continued)

Defendants Motion to Dismiss the Consolidated Amended Complaints. By order of the court, this motion set forth all common issues (i.e., all grounds for dismissal common to all or a significant number of Issuer Defendants). The hearing on the Issuer Defendants Motion to Dismiss and the other Defendants motions to dismiss was held on November 1, 2002. On February 19, 2003, the court issued its opinion and order on the Issuer Defendants Motion to Dismiss. The court granted Antigenics motion to dismiss the Rule 10b-5 and Section 20 claims with leave to amend and denied our motion to dismiss the Section 11 and Section 15 claims. On June 14, 2004, papers formalizing a proposed settlement among the plaintiffs, Issuer Defendants, and insurers were presented to the Federal District Court for the Southern District of New York. On February 15, 2005, the court granted preliminary approval of the settlement. On August 31, 2005, the court issued an order confirming preliminary approval of the settlement. The settlement remained subject to a number of conditions, including final court approval. In December 2006, the appellate court overturned the certification of classes in the six test cases that were selected by the underwriter defendants and plaintiffs in the coordinated proceedings. Class certification was one of the conditions of the settlement. Accordingly, on June 25, 2007, the court entered an order terminating the proposed settlement based on a stipulation among the parties to the settlement. It is uncertain whether there will be any revised or future settlement. To date, the plaintiffs have not asserted a specific amount of damages and, at this time, we cannot make a reliable estimate of possible loss, if any, related to this litigation. Accordingly, no accrual has been recorded at September 30, 2007.

On October 12, 2005, a third party filed a notice of opposition in the European Patent Office to European patent EP 0750513 B1 which has claims relating to AG-702/707 and to which we hold the exclusive license. We have filed a response to this opposition. The opposition division of the European Patent Office has subsequently issued a summons to oral proceedings to be held on January 24, 2008, and has issued a preliminary nonbinding opinion that at least claim 1 of the patent is invalid. We believe this patent claims valid subject matter. However, there is no guarantee that we will continue to defend the opposition, that this patent will not be revoked, or that we may not have to amend the claims.

Antigenics and our Chairman and Chief Executive Officer were named as defendants in a purported shareholder class action complaint filed on June 16, 2006 in Federal District Court in New Mexico by Steven J. Tuckfelt on behalf of himself and all others similarly situated (the Plaintiffs). The complaint alleged that certain of our disclosures in connection with the conduct of the Oncophage Phase 3 renal cell carcinoma trial violated Sections 10(b) and 20(a) of the Securities Exchange Act. The complaint also included purported claims for breach of fiduciary duty. On March 14, 2007, the court dismissed the action without prejudice due to the Plaintiffs failure to prosecute the action. However, there is the possibility the case could be re-filed.

We currently are a party, or may become a party, to other legal proceedings as well. While we currently believe that the ultimate outcome of any of these proceedings will not have a material adverse effect on our financial position, results of operations, or liquidity, litigation is subject to inherent uncertainty. Furthermore, litigation consumes both cash and management attention.

Note G License and Supply Agreements

On July 6, 2006, we entered into expanded license and supply agreements with GSK for the use of QS-21, an investigational adjuvant used in numerous vaccines under development. Under the terms of the agreements, we agreed to supply QS-21 to GSK through 2014. In addition, we agreed to transfer manufacturing technologies under the supply agreement. In conjunction with our expanded license and supply agreements with GSK, we received a $3.0 million up-front non-refundable payment in July 2006. In February 2007, we achieved a milestone related to the transfer of manufacturing technologies to GSK and received a payment of $2.0 million.

On July 20, 2007, we executed the Letter with GSK amending the supply agreement to accelerate GSK s commercial grade QS-21 manufacturing rights previously granted in July 2006. Accordingly, from the effective date of the Letter, GSK has the right to manufacture all of its requirements of commercial grade QS-21. In addition, the parties have amended their purchase and supply obligations with respect to pre-commercial grade QS-21. Also, in accordance with the terms of the Letter, upon our election, GSK is obligated to supply us (or our affiliates, licensees, or customers) certain quantities of commercial grade QS-21 for a stated period of time.

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ANTIGENICS INC. AND SUBSIDIARIES

NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (continued)

As consideration for our entering into the Letter, we received a $2.0 million up-front non-refundable payment from GSK in August 2007, in lieu of a milestone payment that would have otherwise been payable under the supply agreement. In addition, GSK is obligated to pay us $5.25 million over five years for manufacturing profits that were anticipated to have otherwise been payable under the supply agreement. Except as expressly provided in the Letter, all other financial obligations of GSK under the supply agreement, including royalty payments, remain unchanged. The Letter does not affect the rights and obligations of the parties under the July 6, 2006 license agreement.

During the nine months ended September 30, 2007, we recognized revenue of $2.5 million related to these payments. This revenue consisted of a payment in February 2007 of $2.0 million for the achievement of a milestone related to the transfer of manufacturing technologies to GSK and $0.5 million from the amortization of deferred revenue. Deferred revenue of $4.4 million related to our agreement with GSK is included in other long-term liabilities on our balance sheet as of September 30, 2007. Revenue recognized from collaborative agreements like this is based upon the provisions of SAB No. 104, *Revenue Recognition*, and EITF Issue No. 00-21, *Revenue Arrangements with Multiple Deliverables*.

Note H Equity

On September 10, 2007, we issued 1,623,377 shares of our common stock at a price of $3.08 per share to a single institutional investor. In conjunction with this transaction, we also issued to the investor 10,000 shares of our new series B1 convertible preferred stock and 5,250 shares of our new series B2 convertible preferred stock (collectively, our class B convertible preferred stock). Shares of the series B1 convertible preferred stock permit the investor, within one year of the anniversary of closing, to purchase up to an additional $10.0 million of common shares at a purchase price equal to the lesser of $3.08 per share or a price calculated based on the then-prevailing price of our common stock minus $0.30 per share. Shares of the series B2 convertible preferred stock permit the investor to purchase common shares for consideration of up to 35 percent of the total dollar amount previously invested pursuant to the agreement with the investor, including conversions of the series B1 convertible preferred stock, at a purchase price equal to the lesser of $4.16 per common share or a price calculated based on the then-prevailing price of our common stock, and such right expires seven years from the date of issuance. The total number of shares of common stock issued or issuable to the holder of the class B convertible preferred stock cannot exceed 19.9% of our outstanding common stock. No dividends are paid on the class B convertible preferred stock and there are no liquidation preferences.

Gross proceeds of $5.0 million were received as a result of this transaction. Net proceeds, after deducting the placement agent fees and offering expenses paid by us, were $4.7 million. Net proceeds allocated to the class B convertible preferred stock have been recorded as an increase to equity in accordance with our review of SFAS No. 133, *Accounting for Derivative Instruments and Hedging Activities* and EITF Issue No. 00-19.

Note I Recent Accounting Pronouncements

On January 1, 2007, we adopted Financial Accounting Standards Board (FASB) Interpretation No. 48, *Accounting for Uncertainty in Income Taxes* (FIN 48), which is intended to clarify the accounting for income taxes by prescribing a minimum recognition threshold for a tax position before being recognized in the financial statements. FIN 48 also provides guidance on measurement, derecognition, classification, interest and penalties, accounting in interim periods, disclosure, and transition. As of the date of adoption, total uncertain tax positions were immaterial and accordingly, no adjustment to our condensed consolidated financial statements was required. The Company does not anticipate any material changes in the amount of unrecognized tax positions over the next twelve months.

We are subject to taxation in the U.S. and various state, local, and foreign jurisdictions. We remain subject to examination by U.S. Federal, state, local, and foreign tax authorities for tax years 2003 through 2006. With a few exceptions, we are no longer subject to U.S. Federal, state, local, and foreign examinations by tax authorities for the tax year 2002 and prior. However, net operating losses from the tax year 2002 and prior would be subject to examination if and when used in a future tax return to offset taxable income. Our policy is to recognize income tax related penalties and interest, if any, in our provision for income taxes and, to the extent applicable, in the corresponding income tax assets and liabilities, including any amounts for uncertain tax positions.

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ANTIGENICS INC. AND SUBSIDIARIES

NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (continued)

In September 2006, the FASB issued SFAS No. 157, *Fair Value Measurements* (SFAS No. 157). SFAS No. 157 establishes a framework for reporting fair value and expands disclosures about fair value measurements. We are required to adopt SFAS No. 157 as of January 1, 2008. We have not yet determined the impact of adoption of SFAS No. 157 on our consolidated financial statements.

In February 2007, the FASB issued SFAS No. 159, *The Fair Value Option for Financial Assets and Financial Liabilities* (SFAS No. 159). SFAS No. 159 provides companies with the option to measure specified financial instruments and certain other items at fair value. We are required to adopt SFAS No. 159 as of January 1, 2008. We have not yet determined the impact of adoption of SFAS No. 159 on our consolidated financial statements.

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Item 2 ***Management s Discussion and Analysis of Financial Condition and Results of Operations***

Overview

We are currently researching and/or developing technologies and product candidates to treat cancers and infectious diseases. Since our inception in March 1994, our activities have primarily been associated with the development of our heat shock protein technology and our most advanced product candidate, Oncophage® vaccine, a patient-specific therapeutic cancer vaccine. Our business activities have included product research and development, intellectual property prosecution, manufacturing therapeutic vaccines for clinical trials, regulatory and clinical affairs, corporate finance and development activities, marketing, and integration of our acquisitions.

We have incurred significant losses since our inception. As of September 30, 2007, we had an accumulated deficit of $491.2 million. Since our inception, we have financed our operations principally by sales of equity and convertible debt instruments. We believe that, based on our current plans and activities, our working capital resources at September 30, 2007, along with the estimated proceeds from our license, supply, and collaborative agreements, will be sufficient to satisfy our liquidity requirements into 2008. In addition, we expect to attempt to raise additional funds in advance of depleting our current funds. Satisfying long-term liquidity needs may require the successful commercialization of product candidates and will require additional capital.

On March 24, 2006, we announced top-line results from part I of our Phase 3 study of Oncophage in renal cell carcinoma patients who are at high risk of recurrence after surgery, indicating that the trial did not meet its primary endpoint. Based on these results, in April 2006, we implemented a restructuring plan that refocused our programs and priorities resulting in the temporary discontinuation of all late-stage clinical programs and concentration on Phase 1 and preclinical programs, including Aroplatin for the treatment of solid tumors and B-cell lymphomas, AG-707 for the treatment of genital herpes, and AU-801 for autoimmune disorders. In addition, we terminated part II of our Phase 3 renal cell carcinoma trial and our Phase 2 trial of AG-858 for the treatment of chronic myelogenous leukemia (CML). To match these priorities, we eliminated 42 positions in April 2006. In September 2006, we discontinued activities related to AU-801. We continue to support and develop our QS-21 Stimulon® adjuvant (QS-21) partnering collaborations, with the goal of generating royalties from this product in the 2010 timeframe.

We continued to collect data per the protocol through March 2007, and on May 21, 2007, we announced additional follow-up data. The end-of-study results, which reflect an additional 17 months data collection, showed similar trends to that previously reported in June 2006 in the intent-to-treat population where no statistically significant difference was found between the two arms. Further, in the subset of better-prognosis patients (n = 362) at intermediate risk for disease recurrence, patients in the Oncophage arm continued to demonstrate significant improvement in recurrence free survival (RFS the study s primary endpoint) of approximately 45 percent (*p* value of less than 0.01 and hazard ratio of 0.55). In addition, updated analysis in this group of intermediate risk patients revealed a trend towards improved overall survival (OS a secondary endpoint), the study s secondary endpoint. Furthermore, the positive OS trend observed to date correlates with the RFS improvement demonstrated in previous analyses. The results announced in June 2006 reported that a total of 361 patients in the subgroup were defined as having intermediate risk for recurrence of disease. In subsequent follow-up, one patient was recategorized, resulting in an increase in the total number of patients from 361 to 362 in the later analysis.

The Eastern Cooperative Oncology Group (ECOG) is currently sponsoring a large adjuvant renal cell carcinoma trial that stratifies patients by certain prognostic risk factors for recurrence, and puts patients into intermediate risk, high risk, and very high risk categories. We are able to apply these definitions to the data generated as part of our Phase 3 trial of Oncophage in renal cell carcinoma and it is in the intermediate risk population where significant improvement over observation is demonstrated. We continue to analyze the data collected to date, and we have also opened a subsequent protocol that will continue to follow patients in the format of a registry in order to collect OS information, as well as investigator reports of disease recurrence. The registry, which is expected to provide additional data on the effectiveness of Oncophage, will follow patients for an additional three years from closure of the initial trial, providing more than five years worth of data collection from the last patient enrolled. This continued data collection and our ongoing analysis is uncertain, and may negatively affect or not affect the acceptability of the overall results of the trial, and even if clinically meaningful, may not meet the requirements of the U.S. Food and Drug Administration (the FDA) or other regulatory authorities for submission and approval of a marketing application or similar ex-U.S. applications for product approval.

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Guidance received from past discussions with the FDA indicates that further clinical studies must be conducted to demonstrate to them the efficacy and safety of Oncophage. We intend to seek a meeting with the FDA to discuss the results of the updated analyses utilizing data through March 2007 to determine whether there is an opportunity to file a biologics license application (BLA) on the basis of these results with appropriate commitments to conduct further clinical investigations to support the efficacy of Oncophage in renal cell carcinoma. Because evidence of clinically significant improvement has been observed in a subgroup analysis and was not demonstrated in the pre-specified analysis of the primary and secondary endpoints of the Phase 3 study of Oncophage in renal cell carcinoma, based on existing standards this trial is likely not sufficient to support a BLA for product approval. Furthermore, this trial may not be sufficient to support approval outside of the U.S.

We are exploring the additional steps necessary to seek approval of Oncophage in ex-U.S. markets. This exploration process includes, but is not limited to, formal and informal discussions with international regulatory authorities, key opinion leaders, and consultants with country-specific regulatory experience regarding potential applications for full or conditional marketing approvals and/or named patient programs. In conjunction with this process, on June 25, 2007, we completed the submission of an application for marketing authorization with the Russian Ministry of Public Health for the use of Oncophage in the treatment of kidney cancer patients at intermediate risk for disease recurrence. We cannot predict the outcome of this application.

On July 6, 2006, we entered into expanded license and supply agreements with GlaxoSmithKline Biologicals SA (GSK) for the use of QS-21, an investigational adjuvant used in numerous vaccines under development. QS-21 is a component included in several adjuvant systems. A number of vaccine candidates currently under development are formulated with adjuvant systems containing QS-21. Under the terms of the agreements, we agreed to supply QS-21 to GSK through 2014 and to transfer manufacturing technologies under the supply agreement. In conjunction with our expanded license and supply agreements with GSK, we received a $3.0 million up-front non-refundable payment in July 2006. In February 2007, we achieved a milestone related to the transfer of manufacturing technologies to GSK and received a payment of $2.0 million. We are entitled to receive royalties on net sales for a period of at least 10 years after the first commercial sale under the supply agreement.

On July 20, 2007, we executed a binding letter of intent (the Letter) with GSK amending the supply agreement to accelerate GSK s commercial grade QS-21 manufacturing rights previously granted in July 2006. Accordingly, from the effective date of the Letter, GSK has the right to manufacture all of its requirements of commercial grade QS-21. In addition, the parties have amended their purchase and supply obligations with respect to pre-commercial grade QS-21. In accordance with the terms of the Letter, upon our election, GSK is obligated to supply us (or our affiliates, licensees, or customers) certain quantities of commercial grade QS-21 for a stated period of time.

As consideration for our entering into the Letter, we received a $2.0 million up-front non-refundable payment from GSK in August 2007, in lieu of a milestone payment that would have otherwise been payable under the supply agreement. In addition, GSK is obligated to pay us $5.25 million over five years for manufacturing profits that were anticipated to have otherwise been payable under the supply agreement. Except as expressly provided in the Letter, all other financial obligations of GSK under the supply agreement, including royalty payments, remain unchanged. The Letter does not affect the rights and obligations of the parties under the July 6, 2006 license agreement.

On September 10, 2007, we issued 1,623,377 shares of our common stock at a price of $3.08 per share to a single institutional investor. Net proceeds, after deducting offering expenses paid by us, were $4.7 million. In conjunction with this transaction, we also issued to the investor 10,000 shares of our new series B1 convertible preferred stock and 5,250 shares of our new series B2 convertible preferred stock (collectively, our class B convertible preferred stock). Shares of the series B1 convertible preferred stock permit the investor, within one year of the anniversary of closing, to purchase up to an additional $10.0 million of common shares at a purchase price equal to the lesser of $3.08 per share or a price calculated based on the then-prevailing price of our common stock minus $0.30 per share. Shares of the series B2 convertible preferred stock permit the investor to purchase common shares for consideration of up to 35 percent of the total dollar

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amount previously invested pursuant to the agreement with the investor, including conversions of the series B1 convertible preferred stock, at a purchase price equal to the lesser of $4.16 per common share or a price calculated based on the then-prevailing price of our common stock, and such right expires seven years from the date of issuance. The total number of shares of common stock issued or issuable to the holder of the class B convertible preferred stock cannot exceed 19.9% of our outstanding common stock. No dividends are paid on the class B convertible preferred stock and there are no liquidation preferences.

Gross proceeds of $5.0 million were received as a result of this transaction. Net proceeds, after deducting the placement agent fees and offering expenses paid by us, were $4.7 million.

The financial statements in this Quarterly Report on Form 10-Q, unlike those in our earnings release filed on Form 8-K on November 1, 2007, do not attribute $475,000 to dividends on convertible preferred stock, in relation to our September 10, 2007 issuance of preferred stock. This difference results in net loss attributable to common stockholders for the three and nine months ended September 30, 2007, being $0.01 less per share than the amounts reflected in the earnings release.

Forward-Looking Statements

This Quarterly Report on Form 10-Q contains forward-looking statements. Generally, these statements can be identified by the use of terms like believe, expect, anticipate, plan, may, will, could, estimate, potential, opportunity, future, project, and similar terms. Fo include, but are not limited to, statements about generating royalty revenue from QS-21 in the 2010 timeframe, our plans or timelines for performing and completing research, preclinical studies and clinical trials, timelines for releasing data from clinical trials, plans or timelines for initiating new clinical trials, expectations regarding research, preclinical studies, clinical trials and regulatory processes (including additional clinical studies for Oncophage in renal cell carcinoma and our application for marketing approval of Oncophage in Russia), expectations regarding test results, future product research and development activities, the expected effectiveness of therapeutic drugs, vaccines, and combinations in treating diseases, applicability of our heat shock protein technology to multiple cancers and infectious diseases, competitive position, plans for regulatory filings and meetings with regulatory authorities (including potential requests for meetings with the FDA regarding Oncophage clinical studies), the sufficiency of our clinical trials in renal cell carcinoma and melanoma, or subgroup analyses of data from these trials, to support a BLA or foreign marketing application for product approval, possible receipt of future regulatory approvals, the performance of collaborative partners in, and revenue expectations from, our strategic license and partnering collaborations, expected liquidity and cash needs, plans to commence, accelerate, decelerate, postpone, discontinue, or resume clinical programs, and reduction of our net cash burn (cash used in operating activities plus capital expenditures, debt repayments, and dividend payments), plans for sales and marketing, implementation of corporate strategy, increased foreign currency exposure if we commercialize in Russia, and future financial performance. These forward-looking statements involve a number of risks and uncertainties that could cause actual results to differ materially from those suggested by the forward-looking statements. These risks and uncertainties include, among others, that clinical trials may not demonstrate that our products are both safe and more effective than current standards of care; that the subgroup analyses of our Oncophage clinical trials do not predict survival or efficacy of the product in future studies or use of Oncophage; that we may be unable to obtain sufficient funding or the regulatory authorization necessary to conduct additional clinical trials; that we may not be able to enroll sufficient numbers of patients in our clinical trials; that we may be unable to obtain the regulatory review or approval necessary to commercialize our product candidates because the FDA or other regulatory agencies are not satisfied with our trial protocols or the results of our trials; that we may fail to adequately protect our intellectual property or that it is determined that we infringe on the intellectual property of others; our strategic licenses and partnering collaborations may not meet expectations; manufacturing problems may cause product development and launch delays and unanticipated costs; our ability to raise additional capital; our ability to attract and retain employees; changes in financial markets, regulatory requirements, and geopolitical developments; and the solvency of counter parties under material agreements, subleases, and general real estate risks.

We have included more detailed descriptions of these risks and uncertainties and other risks and uncertainties applicable to our business in Part II-Item 1A Risk Factors of this Quarterly Report on Form 10-Q. We encourage you to read those descriptions carefully. We caution investors not to place significant reliance on forward-looking statements contained in this document; such statements need to be evaluated in light of all the information contained in this document. Furthermore, the statements speak only as of the date of this document, and we undertake no obligation to update or revise these statements.

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Historical Results of Operations

Three Months Ended September 30, 2007 Compared to the Three Months Ended September 30, 2006

Revenue: We generated revenue of $863,000 and $216,000 during the three months ended September 30, 2007 and 2006, respectively. Revenue includes revenue earned on shipments of QS-21 to our QS-21 licensees, license fees earned, and, in 2007, royalties earned and milestones achieved.

Research and Development: Research and development expenses include the costs associated with our internal research and development activities, including compensation and benefits, occupancy costs, clinical manufacturing costs, administrative costs, and research and development conducted for us by outside advisors, such as sponsored university-based research partners and clinical research organizations. Research and development expense decreased to $6.1 million for the three months ended September 30, 2007 from $6.3 million for the three months ended September 30, 2006. Fewer ongoing projects and our cost containment efforts resulted in a $669,000 decrease. Payroll and personnel related expenses have decreased $67,000 due to reduced headcount. Partially offsetting these reductions was a $583,000 increase in professional fees related to our efforts to seek approval of Oncophage in markets outside the U.S.

General and Administrative: General and administrative expenses consist primarily of personnel costs, facility expenses, and professional fees. General and administrative expenses decreased to $4.6 million for the three months ended September 30, 2007 from $4.7 million for the three months ended September 30, 2006. This decrease was mainly the result of a $423,000 reduction in facility related costs, which resulted from our ongoing efforts to eliminate excess facility space and the reduced occupancy costs of our new corporate headquarters. In addition, there was a $138,000 reduction in payroll and personnel related expenses reflecting reduced headcount. These decreases were largely offset by a $282,000 increase in professional fees and a $118,000 increase in other expenses, primarily related to our efforts to seek approval of Oncophage in markets outside the U.S.

Non-operating Income: Non-operating income of $120,000 for the three months ended September 30, 2006 represents a lease termination fee received from one of our sublessees.

Interest Expense: Interest expense increased 69% to $1.3 million for the three months ended September 30, 2007 from $747,000 for the three months ended September 30, 2006. This increase relates primarily to interest on our senior secured convertible notes (the 2006 Notes) due 2011 that were sold on October 30, 2006.

Interest Income: Interest income decreased 15% to $325,000 for the three months ended September 30, 2007 from $382,000 for the same period in 2006. This decrease is primarily attributable to a decrease in cash, cash equivalents, and short-term investments, partially offset by a rise in interest rates earned on our cash, cash equivalents, and short-term investments. Our average interest rate earned increased from 5.2% for the three months ended September 30, 2006 to 5.6% for the three months ended September 30, 2007.

Nine Months Ended September 30, 2007 Compared to the Nine Months Ended September 30, 2006

Revenue: We generated revenue of $4.7 million and $372,000 during the nine months ended September 30, 2007 and 2006, respectively. Revenue includes revenue earned on shipments of QS-21 to our QS-21 licensees, license fees earned, and, in 2007, royalties earned and milestones achieved.

Research and Development: Research and development expenses include the costs associated with our internal research and development activities, including compensation and benefits, occupancy costs, clinical manufacturing costs, administrative costs, and research and development conducted for us by outside advisors, such as sponsored university-based research partners and clinical research organizations. Research and development expense decreased 20% to $18.1 million for the nine months ended September 30, 2007 from $22.6 million for the nine months ended September 30, 2006. The decrease was partially due to a $2.2 million reduction in payroll and personnel related expenses due to the workforce reduction in April 2006 and subsequent attrition. There was an additional decrease of $2.0 million in our clinical trial-related expenses due to our restructuring plan and temporary discontinuance of late-stage clinical programs. Other expenses decreased $2.1 million due to fewer ongoing projects and cost containment efforts. These reductions were partially offset by an increase in non-cash, stock-based compensation expense of $1.7 million.

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General and Administrative: General and administrative expenses consist primarily of personnel costs, facility expenses, and professional fees. General and administrative expenses decreased 17% to $13.3 million for the nine months ended September 30, 2007 from $16.0 million for the nine months ended September 30, 2006. This decrease is a reflection of our cost-cutting efforts. Specific cost reductions included a $1.3 million reduction in payroll and personnel related expenses due mainly to the workforce reduction in April 2006, as well as reductions in professional fees of $624,000 and other expenses of $476,000. Non-cash, stock-based compensation expense also decreased $244,000.

Restructuring Costs: In December 2005, we updated our business strategy and refocused our programs and priorities, including the postponement and deceleration of a number of our projects. To match these priorities, we eliminated 65 positions. In addition to severance charges of $990,000 recorded in December 2005 related to the elimination of these positions, we recorded severance charges of $112,000 during the three months ended March 31, 2006. In April 2006, we commenced the implementation of a plan to further restructure, refocusing our programs and priorities with the goal of conserving cash, and eliminated 42 additional positions. We recorded severance charges of $645,000 related to the elimination of these positions during the three months ended June 30, 2006 resulting in total severance charges of $757,000 for the nine months ended September 30, 2006. In addition, during the three months ended March 31, 2006, we wrote-off certain assets that were determined to not be required for our updated business strategy. This resulted in additional restructuring charges of $617,000, for a total of $1.4 million in restructuring charges during the nine months ended September 30, 2006.

Non-operating Income: Non-operating income of $141,000 for the nine months ended September 30, 2006 represents a lease termination fee received from one of our sublessees and proceeds from the sale of certain assets.

Interest Expense: Interest expense increased 67% to $3.7 million for the nine months ended September 30, 2007 from $2.2 million for the nine months ended September 30, 2006. This increase relates primarily to interest on our 2006 Notes due 2011 that were sold on October 30, 2006.

Interest Income: Interest income decreased 15% to $1.2 million for the nine months ended September 30, 2007 from $1.4 million for the same period in 2006. This decrease is primarily attributable to a decrease in cash, cash equivalents, and short-term investments, partially offset by a rise in interest rates earned on our cash, cash equivalents, and short-term investments. Our average interest rate earned increased from 4.7% for the nine months ended September 30, 2006 to 5.3% for the nine months ended September 30, 2007.

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Research and Development Programs

Prior to 2002, we did not track costs on a per project basis, and therefore have estimated the allocation of our total research and development costs to our largest research and development programs. For the nine months ended September 30, 2007, these research and development programs consisted largely of Oncophage, AG-707, Aroplatin, and QS-21, as indicated in the following table (in thousands).

Research and Development Program	Product	Nine Months Ended September 30, 2007	Year Ended December 31, 2006	2005	2004	2003	Prior to 2003	Total
Heat Shock Proteins for Cancer	Oncophage & AG-858	$ 12,344	$ 20,468	$ 37,836	$ 35,462	$ 40,052	$ 91,121	$ 237,283
Heat Shock Proteins for Infectious Diseases	AG-702/707	1,693	1,986	3,001	2,682	2,376	4,068	15,806
Liposomal Cancer Treatments*	Aroplatin	2,594	2,534	3,214	1,112	1,263	3,503	14,220
Vaccine Adjuvant**	QS-21	868	1,856	310	264	301	3,956	7,555
Other Research and Development Programs		647	1,799	2,719	2,198	2,272	7,550	17,185
Total Research and Development Expenses		$ 18,146	$ 28,643	$ 47,080	$ 41,718	$ 46,264	$ 110,198	$ 292,049

* Prior to 2001, costs were incurred by Aronex Pharmaceuticals, Inc., a company we acquired in July 2001.

** Prior to 2000, costs were incurred by Aquila Biopharmaceuticals, Inc., a company we acquired in November 2000.

Research and development program costs include compensation and other direct costs plus an allocation of indirect costs, based on certain assumptions and our review of the status of each program. Our product candidates are in various stages of development as described below. Significant additional expenditures will be required if we start new trials, encounter delays in our trials, apply for regulatory approvals, continue development of our technologies, expand our operations, and bring our product candidates to market. The eventual total cost of each clinical trial is dependent on a number of uncertainties such as trial design, length of the trial, number of clinical sites, and number of patients. The process of obtaining and maintaining regulatory approvals for new therapeutic products is lengthy, expensive, and uncertain. Because the development of our most advanced product candidate, Oncophage, is subject to further evaluation and uncertainty, and because AG-707 and Aroplatin are in early-stage clinical development, we are unable to reliably estimate the cost of completing our research and development programs, the timing of bringing such programs to market, and, therefore, when, if ever, material cash inflows are likely to commence. Our collaborations involving QS-21 depend on our collaborative partners or licensees successfully completing clinical trials, our, or our collaborative partners or licensees, successfully supplying QS-21 to meet demand, and our collaborative partners or licensees obtaining regulatory approvals and successfully commercializing product candidates containing QS-21.

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Product Development Portfolio

Below is a table showing the status of our clinical trials.

Product	Phase 3	Phase 2	Phase 1
Trials Currently Enrolling Patients:			
AG-707			Genital herpes
Aroplatin			Solid tumors and B-cell lymphomas
Oncophage		Glioma (b)	
Trials Closed to Enrollment or Completed:			
Oncophage	Renal cell carcinoma part I (a) Renal cell carcinoma part II (a)(c) Metastatic melanoma (a)	Colorectal cancer Non-Hodgkin s lymphoma (NHL) Gastric cancer Metastatic renal cell carcinoma Lung cancer Metastatic melanoma	Pancreatic cancer Glioma (b)
AG-858		CML (a)(c)	
Aroplatin		Colorectal cancer	Solid tumors

(a) Multicenter trials conducted in the U.S., as well as internationally.