XOMA Corp
Form 10-Q
May 08, 2013

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 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 March 31, 2013

or

o 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. 0-14710

XOMA Corporation
(Exact name of registrant as specified in its charter)

Delaware	52-2154066
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)
2910 Seventh Street, Berkeley, California 94710	(510) 204-7200
(Address of principal executive offices, including zip code)	(Telephone Number)

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 o

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

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

Large accelerated filer o	Accelerated filer x	Non-accelerated filer o (Do not check if a smaller reporting company)	Smaller reporting company o

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act of 1934). Yes o No x

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

Class	Outstanding at May 6, 2013
Common Stock, $0.0075 par value	82,893,328

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PART I - FINANCIAL INFORMATION
ITEM 1. CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (unaudited)

XOMA CORPORATION
CONDENSED CONSOLIDATED BALANCE SHEETS
(in thousands, except share and per share amounts)

	March 31, 2013 (unaudited)	December 31, 2012 (Note 1)
ASSETS		
Current assets:		
Cash and cash equivalents	$50,379	$ 45,345
Short-term investments	19,996	39,987
Trade and other receivables, net	6,270	8,249
Prepaid expenses and other current assets	3,062	2,256
Total current assets	79,707	95,837
Property and equipment, net	7,861	8,143
Other assets	1,378	1,696
Total assets	$88,946	$ 105,676
LIABILITIES AND STOCKHOLDERS' (DEFICIT) EQUITY		
Current liabilities:		
Accounts payable	$4,194	$ 3,867
Accrued and other liabilities	5,410	13,045
Deferred revenue	3,756	3,409
Interest bearing obligation – current	4,085	3,391
Accrued Interest on interest bearing obligations – current	1,662	121
Total current liabilities	19,107	23,833
Deferred revenue – long-term	5,857	6,315
Interest bearing obligations – long-term	37,017	37,653
Contingent warrant liabilities	27,841	15,001
Other liabilities - long term	33	1,407
Total liabilities	89,855	84,209
Stockholders' (deficit) equity:		
Common stock, $0.0075 par value, 138,666,666 shares authorized, 82,887,828 and 82,447,274 shares outstanding at March 31, 2013 and December 31, 2012, respectively	618	615
Additional paid-in capital	980,467	977,962
Accumulated comprehensive income	11	8
Accumulated deficit	(982,005)	(957,118)
Total stockholders' (deficit) equity	(909)	21,467
Total liabilities and stockholders' (deficit) equity	$88,946	$ 105,676

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

(Note 1) The condensed consolidated balance sheet as of December 31, 2012 has been derived from the audited consolidated financial statements as of that date included in the Company's Annual Report on Form 10-K for the year ended December 31, 2012.

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XOMA CORPORATION
CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE LOSS
(unaudited)
(in thousands, except per share amounts)

	Three months ended March 31,	
	2013	2012
Revenues:		
License and collaborative fees	$ 399	$ 1,014
Contract and other	8,796	8,844
Net product sales	258	7
Total revenues	9,453	9,865
Operating expenses:		
Research and development	16,590	15,771
Selling, general and administrative	4,124	4,679
Restructuring	17	3,777
Cost of sales	46	-
Total operating expenses	20,777	24,227
Loss from operations	(11,324)	(14,362)
Other income (expense):		
Interest expense	(1,172)	(1,042)
Other income (expense)	449	(664)
Revaluation of contingent warrant liabilities	(12,840)	(14,357)
Net loss	$ (24,887)	$ (30,425)
Basic and diluted net loss per share of common stock	$ (0.30)	$ (0.69)
Shares used in computing basic and diluted net loss per share of common stock	82,595	44,353
Other comprehensive loss:		
Net loss	$ (24,887)	$ (30,425)
Net unrealized gains on available-for-sale securities	3	-
Comprehensive loss	$ (24,884)	$ (30,425)

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

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XOMA CORPORATION
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
(unaudited)
(in thousands)

	Three Months Ended March 31,	
	2013	2012
Cash flows from operating activities:		
Net loss	$ (24,887)	$ (30,425)
Adjustments to reconcile net loss to net cash used in operating activities:		
Depreciation	780	1,265
Common stock contribution to 401(k)	828	1,134
Stock-based compensation expense	1,619	674
Accrued interest on interest bearing obligations	1,542	394
Revaluation of contingent warrant liabilities	12,840	14,357
Restructuring charge related to long-lived assets	-	1,707
Amortization of debt discount, final payment fee on debt, and debt issuance costs	603	467
Unrealized (gain) loss on foreign currency exchange	(440)	376
Unrealized loss (gain) on foreign exchange options	189	276
Other non-cash adjustments	(4)	(43)
Changes in assets and liabilities:		
Trade and other receivables, net	1,997	2,168
Prepaid expenses and other assets	(802)	(1,651)
Accounts payable and accrued liabilities	(7,128)	(3,221)
Deferred revenue	(111)	884
Other liabilities	(1,554)	(37)
Net cash used in operating activities	(14,528)	(11,675)
Cash flows from investing activities:		
Proceeds from maturities of investments	20,000	-
Net purchase of property and equipment	(498)	(548)
Net cash provided by (used in) investing activities	19,502	(548)
Cash flows from financing activities:		
Proceeds from issuance of common stock, net of issuance costs	60	39,480
Principal payments of debt	-	(714)
Net cash provided by financing activities	60	38,766
Net increase in cash and cash equivalents	5,034	26,543
Cash and cash equivalents at the beginning of the period	45,345	48,344
Cash and cash equivalents at the end of the period	$ 50,379	$ 74,887
Supplemental Cash Flow Information:		
Cash paid for:		
Interest	$ 333	$ 195
Non-cash investing and financing activities:		
Issuance of warrants	$ -	$ 6,386
Interest added to principal balances on long-term debt	$ 290	$ 398

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

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XOMA CORPORATION
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(unaudited)

1. Description of Business

XOMA Corporation ("XOMA" or the "Company"), a Delaware corporation combines a portfolio of late-stage clinical programs and research activities to develop innovative therapeutic antibodies with its commercial operations. XOMA focuses its scientific research on allosteric modulation, which offers opportunities for new classes of therapeutic antibodies to treat a wide range of human diseases. XOMA is developing its lead product candidate gevokizumab (IL-1 beta modulating antibody) with Les Laboratoires Servier ("Servier") through a global Phase 3 clinical development program and ongoing proof-of-concept studies in other IL-1-mediated diseases. XOMA's scientific research also has produced the XMet platform, which consists of three classes of preclinical antibodies, including selective insulin receptor modulators that could offer new approaches in the treatment of diabetes. In order to retain significant value from its scientific discoveries, XOMA initiated commercial operations in January 2012 through the licensing of U.S. commercial rights to Servier's ACEON® (perindopril erbumine) and certain U.S. rights to a patent-protected portfolio of fixed dose combination ("FDC") product candidates where perindopril is combined with other active ingredients to treat cardiovascular disease.

2. Basis of Presentation and Significant Accounting Policies

Basis of Presentation

The condensed consolidated financial statements include the accounts of XOMA and its subsidiaries. All intercompany accounts and transactions were eliminated during consolidation. The unaudited financial statements were prepared in accordance with accounting principles generally accepted in the United States for interim financial information and with the instructions to Form 10-Q. These financial statements and related disclosures have been prepared with the assumption that users of the interim financial information have read or have access to the audited financial statements for the preceding fiscal year. Accordingly, these statements should be read in conjunction with the audited consolidated financial statements and related notes included in the Company's Annual Report on Form 10-K for the fiscal year ended December 31, 2012, filed with the U.S. Securities and Exchange Commission ("SEC") on March 12, 2013.

In management's opinion, the unaudited condensed consolidated financial statements include all adjustments, consisting only of normal recurring adjustments, which are necessary to present fairly the Company's consolidated financial position as of March 31, 2013, the consolidated results of the Company's operations and the Company's cash flows for the three months ended March 31, 2013 and 2012. The interim results of operations are not necessarily indicative of the results that may occur for the full fiscal year or future periods.

Use of Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States requires management to make estimates and assumptions that affect the reported amounts of assets, liabilities, revenue and expenses, and related disclosures. On an on-going basis, management evaluates its estimates including, but not limited to, those related to contingent warrant liabilities, revenue recognition, research and development expense, long-lived assets, derivative instruments, stock-based compensation, and restructuring liabilities. The Company bases its estimates on historical experience and on various other market-specific and other relevant assumptions that are believed to be reasonable under the circumstances, the results of which form the basis for making judgments about the carrying values of assets and liabilities that are not readily apparent from other sources. Actual

results may differ significantly from these estimates, such as the Company's billing under government contracts. Under the Company's contracts with the National Institute of Allergy and Infectious Diseases ("NIAID"), a part of the National Institutes of Health ("NIH"), the Company bills using NIH provisional rates and thus are subject to future audits at the discretion of NIAID's contracting office. These audits can result in adjustments to revenues previously reported.

Long-lived Assets

The Company reviews the carrying values and depreciation lives of its long-lived assets whenever events or changes in circumstances indicate that the asset may not be recoverable. An impairment loss is recognized when the estimated future net cash flows expected to result from the use of an asset is less than its carrying amount. Long-lived assets include property and equipment and building and leasehold improvements. During the three months ended March 31, 2012, the Company recorded an impairment loss of $0.8 million and accelerated depreciation of $0.9 million on long-lived assets in connection with the Company's 2012 streamlining plan. See Note 5: Streamlining and Restructuring Charges for additional disclosure on the 2012 streamlining plan.

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Concentration of Risk

Cash equivalents and receivables are financial instruments, which potentially subject the Company to concentrations of credit risk, as well as liquidity risk for certain cash equivalents such as money market funds. The Company has not encountered such issues during the first quarter of 2013.

The Company has not experienced any significant credit losses and does not generally require collateral on receivables. For the three months ended March 31, 2013, two customers represented 79% and 18% of total revenue and 56% and 39% of the accounts receivable balance.

For the three months ended March 31, 2012, these two customers represented 49% and 40% of total revenues. As of December 31, 2012, there were receivables outstanding from these two customers representing 58% and 35% of the accounts receivable balance.

Newly Adopted Accounting Pronouncements

In February 2013, Accounting Standards Codification Topic 220, Comprehensive Income was amended to require companies to report, in one place, information about reclassifications out of accumulated other comprehensive income. Accordingly, a company can present this information on the face of the financial statements, if certain requirements are met, or the information must be presented in the notes to the financial statements. The Company adopted this guidance as of January 1, 2013, on a retrospective basis and the items reclassified out of accumulated other comprehensive income are not material for all periods presented.

3. Condensed Consolidated Financial Statement Detail

Net Loss Per Share of Common Stock

Basic and diluted net loss per share of common stock is based on the weighted average number of shares of common stock outstanding during the period.

Potentially dilutive securities are excluded from the calculation of loss per share if their inclusion is anti-dilutive. The following table shows the total outstanding securities considered anti-dilutive and therefore excluded from the computation of diluted net loss per share (in thousands):

	Three Months Ended March 31,	
	2013	2012
Common stock options and restricted stock units	6,459	5,722
Warrants for common stock	16,176	5,457
Total	22,635	11,179

For the three months ended March 31, 2013 and 2012, all outstanding securities were considered anti-dilutive, and therefore the calculation of basic and diluted net loss per share was the same.

Cash and Cash Equivalents

At March 31, 2013, cash and cash equivalents consisted of demand deposits of $12.4 million and money market funds of $38.0 million with maturities of less than 90 days at the date of purchase. At December 31, 2012, cash and cash equivalents consisted of demand deposits of $7.8 million and money market funds of $37.5 million with maturities of less than 90 days at the date of purchase.

Short-term Investments

At March 31, 2013, short-term investments consisted of U.S. treasury securities of $20.0 million with maturities of greater than 90 days and less than one year from the date of purchase. At December 31, 2012, short-term investments consisted of U.S. treasury securities of $40.0 million with maturities of greater than 90 days and less than one year from the date of purchase.

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Foreign Exchange Options

The Company holds debt and may incur revenue and expenses denominated in foreign currencies, which exposes it to market risk associated with foreign currency exchange rate fluctuations between the U.S. dollar and the Euro. The Company is required in the future to make principal and accrued interest payments in Euros on its €15.0 million loan from Servier (See Note 6: Long-Term Debt and Other Financings). In order to manage its foreign currency exposure related to these payments, in May 2011, the Company entered into two foreign exchange option contracts to buy €1.5 million and €15.0 million in January 2014 and January 2016, respectively. By having these option contracts in place, the Company's foreign exchange rate risk is reduced if the U.S. dollar weakens against the Euro. However, if the U.S. dollar strengthens against the Euro, the Company is not required to exercise these options, but will not receive any refund on premiums paid.

Upfront premiums paid on these foreign exchange option contracts totaled $1.5 million. The fair values of these option contracts are revalued at each reporting period and are estimated based on pricing models using readily observable inputs from actively quoted markets. The fair values of these option contracts are included in other assets on the consolidated balance sheet and changes in fair value on these contracts are included in other income (expense) on the condensed consolidated statements of comprehensive loss.

The foreign exchange options were revalued at March 31, 2013 and had an aggregate fair value of $0.3 million. The Company recognized losses of $0.2 million and $0.3 million related to the revaluation for the three months ended March 31, 2013 and 2012, respectively.

Accrued Liabilities

Accrued liabilities consisted of the following at March 31, 2013 and December 31, 2012 (in thousands):

	March 31, 2013	December 31, 2012
Accrued payroll and other benefits	$ 2,169	$ 2,461
Accrued management incentive compensation	1,086	3,978
Accrued clinical trial costs	746	4,702
Other	1,409	1,904
Total	$ 5,410	$ 13,045

Contingent Warrant Liabilities

In March 2012, in connection with an underwritten offering, the Company issued five-year warrants to purchase 14,834,577 shares of XOMA's common stock at an exercise price of $1.76 per share. These warrants contain provisions that are contingent on the remote occurrence of a change in control, which would conditionally obligate the Company to repurchase the warrants for cash in an amount equal to their fair value using the Black-Scholes Option Pricing Model (the "Black-Scholes Model") on the date of such change in control. The Company believes the likelihood of a change in control prior to the expiration of the warrants is remote; however, due to these provisions, the Company is required to account for the warrants issued in March 2012 as a liability at fair value. In addition, the estimated liability related to the warrants is required to be revalued at each reporting period until the earlier of the exercise of the warrants, at which time the liability will be reclassified to stockholders' equity, or expiration of the warrants. At December 31, 2012, the fair value of the warrant liability was estimated to be $15.0 million using the Black-Scholes Model. The Company revalued the warrant liability at March 31, 2013 using the Black-Scholes Model and recorded the $12.8 million increase in the fair value as a loss in the revaluation of contingent warrant liabilities line of its condensed consolidated statements of comprehensive loss. As of March 31, 2013, 14,265,970 of these warrants were

outstanding and had a fair value of $27.8 million. This increase in liability is due primarily to the increase in the market value of the Company's common stock at March 31, 2013 compared to December 31, 2012.

In February 2010, in connection with an underwritten offering, the Company issued five-year warrants to purchase 1,260,000 shares of XOMA's common stock at an exercise price of $10.50 per share. In June 2009, the Company issued warrants to certain institutional investors as part of a registered direct offering. These warrants represent the right to acquire an aggregate of up to 347,826 shares of XOMA's common stock over a five year period beginning December 11, 2009 at an exercise price of $19.50 per share. These warrants contain provisions that are contingent on the remote occurrence of a change in control, which would conditionally obligate the Company to repurchase the warrants for cash in an amount equal to their fair value using the Black-Scholes Model on the date of such change in control. The Company believes the likelihood of a change in control prior to the expiration of the warrants is remote; however, due to these provisions, the Company is required to account for the warrants issued in February 2010 and June 2009 as liabilities at fair value. As of March 31, 2013, all of these warrants were outstanding and had an aggregate fair value of approximately $33,000.

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4. Fair Value Measurements

Fair value is defined as the price that would be received from selling an asset or the amount that would be paid to transfer a liability in an orderly transaction between market participants at the measurement date. The Company applies ASC 820, which establishes a framework for measuring fair value and a fair value hierarchy that prioritizes the inputs used in valuation techniques. ASC 820 describes a fair value hierarchy based on three levels of inputs, of which the first two are considered observable and the last unobservable, that may be used to measure fair value which are the following:

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

Level 2 – Observable inputs other than quoted prices in active markets for similar assets or liabilities.

Level 3 – Unobservable inputs.

The following tables set forth the Company's fair value hierarchy for its financial assets and liabilities measured at fair value on a recurring basis as of March 31, 2013 and December 31, 2012.

Financial assets and liabilities carried at fair value as of March 31, 2013 and December 31, 2012 were classified as follows (in thousands):

	Fair Value Measurements at March 31, 2013 Using			
	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Total
Assets:				
Money market funds (1)	$ 37,951	$ -	$ -	$37,951
U.S. treasury securities (2)	19,996	-	-	19,996
Foreign exchange options (3)	-	299	-	299
Total	$ 57,947	$ 299	$ -	$58,246
Liabilities:				
Contingent warrant liabilities	$ -	$ -	$ 27,841	$27,841

	Fair Value Measurements at December 31, 2012 Using			
	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Total
Assets:				
Money market funds (1)	$ 37,461	$ -	$ -	$37,461

U.S. treasury securities (2)	39,987	-	-	39,987
Foreign exchange options (3)	-	488	-	488
Total	$ 77,448	$ 488	$ -	$77,936
Liabilities:				
Contingent warrant liabilities	$ -	$ -	$ 15,001	$15,001

(1) Included in cash and cash equivalents
(2) Included in short-term investments
(3) Included in other assets

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The fair value of the foreign exchange options at March 31, 2013 and December 31, 2012 was determined using readily observable market inputs from actively quoted markets obtained from various third-party data providers. These inputs, such as spot rate, forward rate and volatility have been derived from readily observable market data, meeting the criteria for Level 2 in the fair value hierarchy.

The fair value of the contingent warrant liabilities was determined at March 31, 2013 and December 31, 2012 using the Black-Scholes Model, which requires inputs such as the expected term of the warrants, volatility and risk-free interest rate. These inputs are subjective and generally require significant analysis and judgment to develop.

The fair value of the contingent warrant liabilities was estimated using the following range of assumptions at March 31, 2013 and December 31, 2012:

	March 31, 2013	December 31, 2012
Expected volatility	40 %	40 %
Risk-free interest rate	0.3% - 0.4 %	0.3% - 0.7 %
Expected term	1.7 - 3.9 years	1.9 - 4.2 years

The following table provides a summary of changes in the fair value of the Company's Level 3 financial liabilities for the three months ended March 31, 2013 (in thousands):

Contingent warrant liabilities	March 31, 2013
Balance at December 31, 2012	$ 15,001
Net increase in fair value of contingent warrant liabilities upon revaluation	12,840
Balance at March 31, 2013	$ 27,841

The net increase of $12.8 million in the estimated fair value of the contingent warrant liabilities was recognized as a loss in the revaluation of contingent warrant liabilities line of the condensed consolidated statements of comprehensive loss for the three months ended March 31, 2013.

For the three months ended March 31, 2012, the Company recognized a net increase of $14.4 million in the estimated fair value of the contingent warrant liabilities as a loss in the revaluation of contingent warrant liabilities line of the condensed consolidated statements of comprehensive loss.

5. Streamlining and Restructuring Charges

In January 2012, the Company implemented a streamlining of operations, which resulted in a restructuring plan designed to sharpen its focus on value-creating opportunities led by gevokizumab and its unique antibody discovery and development capabilities. The restructuring plan included a reduction of XOMA's personnel by 84 positions, or 34%, of which 52 were eliminated immediately and the remainder eliminated as of April 6, 2012. These staff reductions resulted primarily from the Company's decisions to utilize a contract manufacturing organization for Phase 3 and commercial antibody production, and to eliminate internal research functions that are non-differentiating or that can be obtained cost effectively by contract service providers.

In connection with the streamlining of operations, the Company incurred restructuring charges in the first quarter of 2012 of $2.1 million related to severance, other termination benefits and outplacement services and $1.7 million related to the impairment and accelerated depreciation of various assets and leasehold improvements. The Company

does not expect to incur additional significant restructuring charges during 2013 related to these streamlining activities.

6. Long-Term Debt

Novartis Note

In May 2005, the Company executed a secured note agreement with Novartis (then Chiron Corporation), which is due and payable in full in June 2015. Under the note agreement, the Company borrowed semi-annually to fund up to 75% of the Company's research and development and commercialization costs under its collaboration arrangement with Novartis, not to exceed $50 million in aggregate principal amount. Interest on the principal amount of the loan accrues at six-month LIBOR plus 2%, which was equal to 2.51% at March 31, 2013, and is payable semi-annually in June and December of each year. Additionally, the interest rate resets in June and December of each year. At the Company's election, the semi-annual interest payments can be added to the outstanding principal amount, in lieu of a cash payment, as long as the aggregate principal amount does not exceed $50 million. The Company has made this election for all interest payments thus far. Loans under the note agreement are secured by the Company's interest in its collaboration with Novartis, including any payments owed to it thereunder.

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At March 31, 2013 and December 31, 2012, the outstanding principal balance under this note agreement was $14.4 million. Pursuant to the terms of the arrangement as restructured in November 2008, the Company will not make any additional borrowings under the Novartis note. Due to the structure of the secured note agreement with Novartis and since there is no liquid market for this obligation, there is no practical method to estimate fair value of this long-term debt.

Servier Loan

In December 2010, in connection with the license and collaboration agreement entered into with Servier, the Company executed a loan agreement with Servier (the "Servier Loan Agreement"), which provided for an advance of up to €15.0 million. The loan was fully funded in January 2011, with the proceeds converting to approximately $19.5 million. The loan is secured by an interest in XOMA's intellectual property rights to all gevokizumab indications worldwide, excluding certain rights in the U.S. and Japan. Interest is calculated at a floating rate based on a Euro Inter-Bank Offered Rate ("EURIBOR") and subject to a cap. The interest rate is reset semi-annually in January and July of each year. The interest rate for the initial interest period was 3.22%. The interest rate has been reset to 3.83% for the six-month period from July 2011 through January 2012, 3.54% for the six-month period from January 2012 through July 2012, 2.80% for the six-month period from July 2012 through January 2013, and 2.33% for the six-month period from January 2013 through July 2013. Interest is payable semi-annually; however, the Servier Loan Agreement provides for a deferral of interest payments over a period specified in the agreement. During the deferral period, accrued interest will be added to the outstanding principal amount for the purpose of interest calculation for the next six-month interest period. On the repayment commencement date, all unpaid and accrued interest shall be paid to Servier and thereafter, all accrued and unpaid interest shall be due and payable at the end of each six-month period. The loan matures in 2016; however, after a specified period prior to final maturity, the loan is to be repaid (i) at Servier's option, by applying up to a significant percentage of any milestone or royalty payments owed by Servier under the Company's collaboration agreement and (ii) using a significant percentage of any upfront, milestone or royalty payments the Company receives from any third-party collaboration or development partner for rights to gevokizumab in the U.S. and/or Japan. In addition, the loan becomes immediately due and payable upon certain customary events of default. At March 31, 2013 and December 31, 2012, the outstanding principal balance under this loan was $19.2 million and $19.8 million, respectively, using the Euro to US Dollar exchange rates of 1.2816 and 1.3215, respectively. For the three months ended March 31, 2013 and 2012, the Company recorded an unrealized foreign exchange gain of $0.6 million and an unrealized foreign exchange loss of $0.6 million, respectively, related to the re-measurement of the loan.

The loan has a stated interest rate lower than the market rate based on comparable loans held by similar companies, which represents additional value to the Company. The Company recorded this additional value as a discount to the face value of the loan amount, at its fair value of $8.9 million. The fair value of this discount, which was determined using a discounted cash flow model, represents the differential between the stated terms and rates of the loan, and market rates. Based on the association of the loan with the collaboration arrangement, the Company recorded the offset to this discount as deferred revenue.

The loan discount is amortized under the effective interest method over the expected five-year life of the loan. The Company recorded non-cash interest expense of $0.4 million and $0.3 million in the three months ended March 31, 2013 and 2012, respectively, resulting from the amortization of the loan discount. At March 31, 2013 and December 31, 2012, the net carrying value of the loan was $14.2 million. For the three months ended March 31, 2013 and 2012, the Company recorded unrealized foreign exchange losses of $0.2 million related to the re-measurement of the loan discount.

The Company believes realization of the benefit and the associated deferred revenue is contingent on the loan remaining outstanding over the five-year contractual term of the loan. If the Company were to stop providing service

under the collaboration arrangement and the arrangement is terminated, the maturity date of the loan would be accelerated and a portion of measured benefit would not be realized. As the realization of the benefit is contingent, in part, on the provision of future services, the Company is recognizing the deferred revenue over the expected five-year life of the loan. The deferred revenue is amortized under the effective interest method, and the Company recorded $0.4 million and $0.3 million of related non-cash revenue during the three months ended March 31, 2013 and 2012, respectively.

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General Electric Capital Corporation Term Loan

In December 2011, the Company entered into a loan agreement (the "GECC Loan Agreement") with General Electric Capital Corporation ("GECC"), under which GECC agreed to make a term loan in an aggregate principal amount of $10 million (the "Term Loan") to the Company, and upon execution of the GECC Loan Agreement, GECC funded the Term Loan. As security for its obligations under the GECC Loan Agreement, the Company granted a security interest in substantially all of its existing and after-acquired assets, excluding its intellectual property assets (such as those relating to its gevokizumab and anti-botulism products). The Term Loan accrued interest at a fixed rate of 11.71% per annum and was to be repaid over a period of 42 consecutive equal monthly installments of principal and accrued interest and was due and payable in full on June 15, 2015. The Company incurred debt issuance costs of approximately $1.3 million in connection with the Term Loan and was required to pay a final payment fee equal to $500,000 on the maturity date, or such earlier date as the Term Loan is paid in full. The debt issuance costs and final payment fee were being amortized and accreted, respectively, to interest expense over the term of the Term Loan using the effective interest method.

In connection with the GECC Loan Agreement, the Company issued to GECC unregistered warrants that entitle GECC to purchase up to an aggregate of 263,158 unregistered shares of XOMA common stock at an exercise price equal to $1.14 per share. These warrants are exercisable immediately and have a five-year term. The Company allocated the aggregate proceeds of the GECC Term Loan between the warrants and the debt obligation based on their relative fair values. The fair value of the warrants issued to GECC was determined using the Black-Scholes Model. The warrants' fair value of $0.2 million was recorded as a discount to the debt obligation and was being amortized over the term of the loan using the effective interest method.

In September 2012, The Company entered into an amendment to the GECC Loan Agreement providing for an additional term loan in the amount of $4.6 million, increasing the term loan obligation to $12.5 million (the "Amended Term Loan") and providing for an interest-only monthly repayment period following the effective date of the amendment through March 1, 2013, at a stated interest rate of 10.9% per annum. Thereafter, the Company is obligated to make monthly principal payments of $347,222, plus accrued interest, over a 27-month period commencing on April 1, 2013, and through June 15, 2015, at which time the remaining outstanding principal amount of $3.1 million, plus accrued interest, is due. The Company incurred debt issuance costs of approximately $0.2 million and are required to make a final payment fee in the amount of $875,000 on the date upon which the outstanding principal amount is required to be repaid in full. This final payment fee replaced the original final payment fee of $500,000. The debt issuance costs and final payment fee are being amortized and accreted, respectively, to interest expense over the term of the Amended Term Loan using the effective interest method.

In connection with the amendment, on September 27, 2012 the Company issued to GECC unregistered stock purchase warrants, which entitle GECC to purchase up to an aggregate of 39,346 shares of XOMA common stock at an exercise price equal to $3.54 per share. These warrants are exercisable immediately and have a five-year term. The warrants' fair value of $0.1 million was recorded as a discount to the debt obligation and is being amortized over the term of the loan using the effective interest method. The warrants are classified in permanent equity on the condensed consolidated balance sheets.

The Amended Term Loan does not change the remaining terms of the GECC Loan Agreement. The GECC Loan Agreement contains customary representations and warranties and customary affirmative and negative covenants, including restrictions on the ability to incur indebtedness, grant liens, make investments, dispose of assets, enter into transactions with affiliates and amend existing material agreements, in each case subject to various exceptions. In addition, the GECC Loan Agreement contains customary events of default that entitle GECC to cause any or all of the indebtedness under the GECC Loan Agreement to become immediately due and payable. The events of default include any event of default under a material agreement or certain other indebtedness.

The Company may prepay the Amended Term Loan voluntarily in full, but not in part, and any voluntary and certain mandatory prepayments are subject to a prepayment premium of 3% in the first year after the effective date of the loan amendment, 2% in the second year and 1% thereafter, with certain exceptions. The Company will also be required to pay the $875,000 final payment fee in connection with any voluntary or mandatory prepayment. On the effective date of the loan amendment, the Company paid an accrued final payment fee in the amount of $0.2 million relating to the original final payment fee of $500,000.

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At March 31, 2013 and December 31, 2012, the outstanding principal balance under the Amended Term Loan was $12.5 million.

Interest Expense

Interest expense and amortization of debt issuance costs and discounts, recorded as other expense in the condensed consolidated statements of comprehensive loss for the three months ended March 31, 2013 and 2012 are shown below (in thousands):

	Three Months Ended March 31,	
	2013	2012
Interest expense		
GECC term loan	$ 545	$ 417
Servier loan	525	516
Novartis note	91	99
Other	11	10
Total interest expense	$ 1,172	$ 1,042

7. Income Taxes

The Company did not recognize any income tax expense for the three months ended March 31, 2013 and 2012. The Company's effective tax rate will fluctuate from period to period due to several factors inherent in the nature of the Company's operations and business transactions. The factors that most significantly impact this rate include the variability of licensing transactions in foreign jurisdictions.

8. Stock-based Compensation

In the first quarter of 2013, the Board of Directors of the Company approved grants under the Company's Long Term Incentive Plan for an aggregate of 994,053 stock options and an aggregate of 895,860 restricted stock units ("RSUs") to certain employees of the Company. The stock options vest monthly over four years, and the RSUs vest annually over three years, in equal increments.

The Company recognizes compensation expense for all stock-based payment awards made to the Company's employees, consultants and directors based on estimated fair values. The valuation of stock option awards is determined at the date of grant using the Black-Scholes Model. This model requires inputs such as the expected term of the option, expected volatility and risk-free interest rate. To establish an estimate of expected term, the Company considers the vesting period and contractual period of the award and its historical experience of stock option exercises, post-vesting cancellations and volatility. The estimate of expected volatility is based on the Company's historical volatility. The risk-free rate is based on the yield available on U.S. Treasury zero-coupon issues. The forfeiture rate impacts the amount of aggregate compensation for both stock options and RSUs. To establish an estimate of forfeiture rate, the Company considers its historical experience of option forfeitures and terminations.

The fair value of the stock options granted was estimated based on the following weighted average assumptions for three months ended March 31, 2013 and 2011:

	Three Months Ended March 31,			
	2013		2012	
Dividend yield	0	%	0	%
Expected volatility	92	%	92	%

Risk-free interest rate	0.78	%	1.05	%
Expected term	5.6 years		5.6 years	

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Stock option activity for the three months ended March 31, 2013 was as follows:

	Options	Weighted Average Exercise Price Per Share	Weighted Average Remaining Contractual Life (in years)	Aggregate Intrinsic Value (in thousands)
Options outstanding at December 31, 2012	6,788,383	$8.99	7.36	$1,531
Granted	994,053	2.92		
Exercised	(19,090)	1.97		
Forfeited, expired or cancelled	(54,930)	31.12		
Options outstanding at March 31, 2013	7,708,416	$8.07	7.54	$4,502
Options exercisable at March 31, 2013	4,473,529	$11.70	6.39	$2,245

The valuation of RSUs is determined at the date of grant using the closing stock price. To establish an estimate of forfeiture rate, the Company considers its historical experience of forfeitures and terminations.

Unvested RSU activity for the three months ended March 31, 2013 is summarized below:

	Number of Shares	Weighted-Average Grant-Date Fair Value
Unvested balance at December 31, 2012	1,459,853	$ 2.75
Granted	895,860	2.87
Vested	(164,998)	2.50
Forfeited	(4,835)	2.06
Unvested balance at March 31, 2013	2,185,880	$ 2.65

The following table shows total stock-based compensation expense included in the condensed consolidated statements of comprehensive loss for the three months ended March 31, 2013 and 2012 (in thousands):

	Three Months Ended March 31,	
	2013	2012
Research and development	$ 997	$ 385
Selling, general and administrative	622	289
Total stock-based compensation expense	$ 1,619	$ 674

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

Forward Looking Statements

This Quarterly Report on Form 10-Q contains forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, as amended, or the Securities Act, and Section 21E of the Securities Exchange Act of 1934, as amended, or the Exchange Act, which are subject to the "safe harbor" created by those sections. Forward-looking statements are based on our management's beliefs and assumptions and on information currently available to them. In some cases you can identify forward-looking statements by words such as "may," "will," "should," "could," "would," "expects "plans," "anticipates," "believes," "estimates," "projects," "predicts," "potential" and similar expressions intended to identify forward-looking statements. Examples of these statements include, but are not limited to, statements regarding: the implications of interim or final results of our clinical trials, the progress of our research programs, including clinical testing, the extent to which our issued and pending patents may protect our products and technology, our ability to identify new product candidates, the potential of such product candidates to lead to the development of commercial products, our anticipated timing for initiation or completion of our clinical trials for any of our product candidates, our future operating expenses, our future losses, our future expenditures for research and development, and the sufficiency of our cash resources. Our actual results could differ materially from those anticipated in these forward-looking statements for many reasons, including the risks faced by us and described in Part II, Item 1A of this Quarterly Report on Form 10-Q and our other filings with the SEC. You should not place undue reliance on these forward-looking statements, which apply only as of the date of this Quarterly Report on Form 10-Q. You should read this Quarterly Report on Form 10-Q completely and with the understanding that our actual future results may be materially different from those we expect. Except as required by law, we assume no obligation to update these forward-looking statements, whether as a result of new information, future events or otherwise.

The following discussion and analysis should be read in conjunction with the unaudited financial statements and notes thereto included in Part I, Item 1 of this Quarterly Report on Form 10-Q and with the audited consolidated financial statements and related notes thereto included as part of our Annual Report on Form 10-K for the year ended December 31, 2012.

Overview

We are a leader in the discovery and development of innovative antibody-based therapeutics. Our lead drug candidate, gevokizumab (formerly XOMA 052), is a potent humanized monoclonal antibody with unique allosteric modulating properties. Gevokizumab binds to the inflammatory cytokine interleukin-1 beta ("IL-1 beta"), which is believed to be a primary trigger of pathologic inflammation in multiple diseases. We have entered into a license and collaboration agreement with Les Laboratoires Servier ("Servier") to develop and commercialize gevokizumab in multiple indications. In collaboration with Servier, we have launched the global Phase 3 gevokizumab clinical development program for active and controlled non-infectious uveitis ("NIU") involving the intermediate and/or posterior segment of the eye, and Behçet's uveitis. XOMA is conducting both of the NIU studies, and Servier is sponsoring the study in Behçet's uveitis. The study sites are screening and enrolling patients in these distinct studies.

Separately, we launched a Phase 2 proof-of-concept program for gevokizumab to evaluate additional indications for further development, including a clinical trial in moderate-to-severe inflammatory acne, for which we reported encouraging preliminary top-line results in January 2013; a clinical trial in erosive osteoarthritis of the hand, which was opened for enrollment in June 2012; and a clinical trial in scleritis that is being conducted by the National Eye Institute ("NEI"), a part of the U.S. National Institutes of Health ("NIH"). Servier is expected to institute its own proof-of-concept program for gevokizumab in indications different from ours. In November 2012, Servier began a Phase 2 study to determine gevokizumab's potential to decrease plaque inflammation in patients with atherosclerosis.

Our proprietary preclinical pipeline includes classes of antibodies that activate, sensitize or deactivate the insulin receptor in vivo, which we have named XMet. This portfolio of antibodies represents potential new therapeutic approaches to the treatment of diabetes and several diseases that have insulin involvement, which we believe may be orphan drug opportunities.

We have developed these and other antibodies using some or all of our ADAPT™ antibody discovery and development platform, our ModulX™ technologies for generating allosterically modulating antibodies, and our OptimX™ technologies for optimizing biophysical properties of antibodies, including affinity, immunogenicity, stability and manufacturability.

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Our biodefense initiatives include XOMA 3AB, a biodefense anti-botulism product candidate comprised of a combination of three antibodies. XOMA 3AB is directed against botulinum toxin serotype A and has been developed through funding from the National Institute of Allergy and Infectious Diseases ("NIAID"), a part of the NIH. All volunteers have been enrolled and dosed with XOMA 3AB in a Phase 1 clinical trial sponsored by NIAID. In January 2012, we announced we will complete NIAID biodefense contracts currently in place but will not actively pursue future contracts. Should the government choose to acquire XOMA 3AB or other biodefense products in the future, we expect to be able to produce these antibodies through an outside manufacturer.

We also have developed antibody product candidates with premier pharmaceutical companies including Novartis AG ("Novartis") and Takeda Pharmaceutical Company Limited ("Takeda"). Two antibodies developed with Novartis, LFA102 and HCD122 (lucatumumab), are in Phase 1 and/or Phase 2 clinical development by Novartis for the potential treatment of breast or prostate cancer and hematological malignancies, respectively.

In January 2012, we announced we had acquired certain U.S. rights to a portfolio of antihypertensive products from Servier. The portfolio includes ACEON (perindopril erbumine), a currently marketed angiotensin converting enzyme ("ACE") inhibitor, and three fixed-dose combination ("FDC") product candidates where perindopril is combined with another active ingredient(s). The last to expire proprietary form of perindopril in each FDC product candidate provides patent protection until April 2023. We assumed commercialization activities for ACEON in January 2012. In November 2012, we announced the 837-patient Phase 3 trial for the FDC of perindopril arginine and amlodipine besylate ("FDC1") met its primary endpoint. Partial funding for the trial was provided by Servier. We expect to pay the balance of study expenses, consisting primarily of costs generated by our contract research organization, from the profits generated by our ACEON sales. We are working to identify a third-party organization that could sublicense this FDC and move it forward toward commercialization in the U.S. market.

Significant Developments in the First Quarter of 2013

Gevokizumab

- In January 2013, we announced encouraging preliminary top-line data from an interim analysis of our Phase 2 proof-of-concept study to evaluate the safety and efficacy of gevokizumab for the treatment of moderate-to-severe inflammatory acne. Preliminary data from the 125-patient trial demonstrated clear activity according to the Investigator's Global Assessment ("IGA") parameter. Gevokizumab was well-tolerated in this trial, with no significant differences in adverse events between gevokizumab and placebo and no serious drug-related adverse events were reported.

Management Addition

- On March 18, 2013, the Company announced Tom Klein has joined the Company as Vice President, Chief Commercial Officer, a newly created position reporting to John Varian, Chief Executive Officer.

Results of Operations

Revenues

Total revenues for the three months ended March 31, 2013 and 2012, were as follows (in thousands):

	Three Months Ended March 31,		
	2013	2012	Increase (Decrease)

License and collaborative fees	$399	$1,014	$ (615)
Contract and other	8,796	8,844	(48)
Product sales	258	7	251
Total revenues	$9,453	$9,865	$ (412)

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License and Collaborative Fees

License and collaborative fee revenue includes fees and milestone payments related to the out-licensing of our products and technologies. The decrease in license and collaborative fee revenue for the three months ended March 31, 2013, as compared to the same period of 2012, was due primarily a $0.6 million decrease in licensing fees. The generation of future revenue related to license fees and other collaborative arrangements is dependent on our ability to attract new licensees to our antibody technologies and new collaboration partners. We expect a slight decrease in license and collaboration fee revenue in 2013 compared to 2012 levels.

Contract and Other Revenue

Contract and other revenues include agreements where we provide contracted research and development services to our contract and collaboration partners, including Servier and NIAID. The following table shows the activity in contract and other revenue for the three months ended March 31, 2013 and 2012 (in thousands):

	Three Months Ended March 31,		
	2013	2012	Increase (Decrease)
Servier	$7,027	$3,649	$3,378
NIAID	1,695	4,837	(3,142)
Other	74	358	(284)
Total contract and other	$8,796	$8,844	$(48)

The increase in revenue from Servier is due primarily to an increase in reimbursable clinical development activity under our agreements with Servier. The increase in clinical development activity is partially offset by a decrease in NIAID revenue due primarily to decreased activity under NIAID Contract No. HHSN272200800028C (“NIAID 3”) and the recognition of $2.0 million in revenue during the first quarter of 2012 related to an adjustment to previously-reported revenue from NIAID resulting from an audit by NIAID’s contracting office. This revenue, which was previously deferred, was recognized upon the completion of negotiations with and approval by the NIH in March 2012.

Based on expected levels of revenue generating activity related to our Servier and NIAID contracts, we expect contract and other revenue in 2013 to be comparable to 2012 levels.

Net Product Sales

Net product sales, cost of sales, and product gross margin for the three months ended March 31, 2013 were as follows (in thousands):

	Three Months Ended March 31,				
	2013		2012		Increase (Decrease)
Net product sales (1)	258		7		251
Cost of sales (2)	46		-		46
Product gross margin	82	%	93	%	

(1) Product sales are recorded net of prompt pay discounts, volume rebates and product returns.

(2) Cost of sales includes raw materials, third-party manufacturing and production costs, and royalties payable to Servier for ACEON® sales.

Research and Development Expenses

Biopharmaceutical development includes a series of steps, including in vitro and in vivo preclinical testing, and Phase 1, 2 and 3 clinical studies in humans. Each of these steps is typically more expensive than the previous step, but actual timing and the cost to us depends on the product being tested, the nature of the potential disease indication and the terms of any collaborative or development arrangements with other companies or entities. After successful conclusion of all of these steps, regulatory filings for approval to market the products must be completed, including approval of manufacturing processes and facilities for the product. Our research and development expenses currently include costs of personnel, supplies, facilities and equipment, consultants, third-party costs and other expenses related to preclinical and clinical testing.

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Research and development expenses were $16.6 million for the three months ended March 31, 2013, compared with $15.8 million for the same period of 2012. The increase of $0.8 million for the three months ended March 31, 2013, as compared to the same period in 2012, was due primarily to a $0.6 million increase in stock-based compensation costs. Also contributing to the increase was an increase in external manufacturing costs largely offset by a decrease in internal facility costs due to the 2012 streamlining of operations.

Salaries and related personnel costs are a significant component of research and development expenses. We recorded $7.6 million in research and development salaries and employee-related expenses for the three months ended March 31, 2013, as compared with $7.0 million for the same period of 2012. The increase of $0.6 million was due primarily to a $0.6 million increase in stock-based compensation.

Our research and development activities can be divided into earlier-stage programs and later-stage programs. Earlier-stage programs include molecular biology, process development, pilot-scale production and preclinical testing. Also included in earlier-stage programs are costs related to excess manufacturing capacity, of which we expect to further decrease in 2013 due to our streamlining objective to utilize a contract manufacturing organization, which was implemented in 2012. Later-stage programs include clinical testing, regulatory affairs and manufacturing clinical supplies. The costs associated with these programs approximate the following (in thousands):

	Three Months Ended March 31,	
	2013	2012
Earlier stage programs	$ 9,217	$ 8,333
Later stage programs	7,373	7,438
Total	$ 16,590	$ 15,771

Our research and development activities also can be divided into those related to our internal projects and those projects related to collaborative and contract arrangements. The costs related to internal projects versus collaborative and contract arrangements approximate the following (in thousands):

	Three Months Ended March 31,	
	2013	2012
Internal projects	$ 9,825	$ 6,682
Collaborative and contract arrangements	6,765	9,089
Total	$ 16,590	$ 15,771

For the three months ended March 31, 2013, the gevokizumab program, for which we incurred the largest amount of expense, accounted for more than 40% but less than 50% of our total research and development expenses. A second development program, XMet, accounted for more than 20% but less than 30% of our total research and development expenses and a third development program, NIAID, accounted for more than 10% but less than 20% of our total research and development expenses. All remaining development programs accounted for less than 10% of our total research and development expenses for the three months ended March 31, 2013. For the three months ended March 31, 2012, the gevokizumab program, for which we incurred the largest amount of expense, accounted for more than 40% but less than 50% of our total research and development expenses. A second development program, NIAID, accounted for more than 20% but less than 30% of our total research and development expenses and a third development program, XMet, accounted for more than 10% but less than 20% of our total research and development expenses. All remaining development programs accounted for less than 10% of our total research and development expenses for the three months ended March 31, 2012.

We expect our research and development spending in 2013 will increase due primarily to our ongoing global Phase 3 clinical program for gevokizumab for the NIU indications, under our license and collaboration agreement with

Servier, and our ongoing Phase 2 proof-of-concept program.

Future research and development spending also may be impacted by potential new licensing or collaboration arrangements, as well as the termination of existing agreements. Beyond this, the scope and magnitude of future research and development expenses are difficult to predict at this time.

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Selling, General and Administrative Expenses

Selling, general and administrative expenses include salaries and related personnel costs, facilities costs and professional fees. Selling, general and administrative expenses were $4.1 million for the three months ended March 31, 2013, compared with $4.7 million for the same period of 2012. The $0.6 million decrease for the first quarter of 2013, as compared to the same period of 2012, was due primarily to a $0.9 million decrease in professional services cost, partially offset by a $0.3 million increase in stock-based compensation.

Streamlining and Restructuring Charges

In January 2012, we implemented a streamlining of operations, which resulted in a restructuring plan designed to sharpen our focus on value-creating opportunities led by gevokizumab and its unique antibody discovery and development capabilities. The restructuring plan included a reduction of XOMA's personnel by 84 positions, or 34%, of which 52 were eliminated immediately and the remainder eliminated as of April 6, 2012. These staff reductions resulted primarily from our decision to utilize a contract manufacturing organization for Phase 3 and commercial antibody production and to eliminate internal research functions that are non-differentiating or that can be obtained cost effectively by contract service providers.

In connection with the streamlining of operations, we incurred restructuring charges in the first quarter of 2012 of $2.1 million related to severance, other termination benefits and outplacement services and $1.7 million related to the impairment and accelerated depreciation of various assets and leasehold improvements. We do not expect to incur additional significant restructuring charges during 2013 related to these streamlining activities.

Other Income (Expense)

Interest Expense

Interest expense and amortization of debt issuance costs and discounts are shown below the three months ended March 31, 2013 and 2012 (in thousands):

	Three Months Ended March 31,		
	2013	2012	Increase (Decrease)
Interest expense			
GECC term loan	$545	$417	$128
Servier loan	525	516	9
Novartis note	91	99	(8)
Other	11	10	1
Total interest expense	$1,172	$1,042	$130

The increase of $0.1 million in interest expense in 2013 as compared to 2012 was due primarily to an increase in interest expense under the GECC term loan, amended in September 2012.

Other Expense

Other expense primarily consisted of unrealized and realized (losses) gains. The following table shows the activity in other expense for the three months ended March 31, 2013 and 2012 (in thousands):

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	Three Months Ended March 31,		
	2013	2012	Increase (Decrease)
Other income (expense)			
Unrealized foreign exchange gain (loss) (1)	$515	$(402)	$917
Unrealized loss on foreign exchange options	(189)	(276)	87
Other	123	14	109
Total other income (expense)	$449	$(664)	$1,113

(1) Unrealized foreign exchange gain (loss) for the three months ended March 31, 2013 and 2012 primarily relates to the re-measurement of the €15 million Servier loan.

Revaluation of Contingent Warrant Liabilities

In March 2012, in connection with an underwritten offering, we issued five-year warrants to purchase 14,834,577 shares of XOMA's common stock at an exercise price of $1.76 per share. These warrants contain provisions that are contingent on the remote occurrence of a change in control, which would conditionally obligate us to repurchase the warrants for cash in an amount equal to their fair value using the Black-Scholes Option Pricing Model (the "Black-Scholes Model") on the date of such change in control. We believe the likelihood of a change in control prior to the expiration of the warrants is remote; however, due to these provisions, we are required to account for the warrants issued in March 2012 as a liability at fair value. In addition, the estimated liability related to the warrants is required to be revalued at each reporting period until the earlier of the exercise of the warrants, at which time the liability will be reclassified to stockholders' equity, or expiration of the warrants. At December 31, 2012, the fair value of the warrant liability was estimated to be $15.0 million using the Black-Scholes Model. We revalued the warrant liability at March 31, 2013 using the Black-Scholes Model and recorded the $12.8 million increase in the fair value as a loss in the revaluation of contingent warrant liabilities line of our condensed consolidated statements of comprehensive loss. As of March 31, 2013, 14,265,970 of these warrants were outstanding and had a fair value of $27.8 million. This increase in liability is due primarily to the increase in the market value of our common stock at March 31, 2013 compared to December 31, 2012.

In February 2010, in connection with an underwritten offering, we issued five-year warrants to purchase 1,260,000 shares of XOMA's common stock at an exercise price of $10.50 per share. In June 2009, we issued warrants to certain institutional investors as part of a registered direct offering. These warrants represent the right to acquire an aggregate of up to 347,826 shares of XOMA's common stock over a five year period beginning December 11, 2009, at an exercise price of $19.50 per share. These warrants contain provisions that are contingent on the remote occurrence of a change in control, which would conditionally obligate us to repurchase the warrants for cash in an amount equal to their fair value using the Black-Scholes Model on the date of such change in control. We believe the likelihood of a change in control prior to the expiration of the warrants is remote; however, due to these provisions, we are required to account for the warrants issued in February 2010 and June 2009 as liabilities at fair value. As of March 31, 2013, all of these warrants were outstanding and had an aggregate fair value of approximately $33,000.

The following table provides a summary of the changes in fair value of contingent warrant liabilities for the three months ended March 31, 2013 (in thousands):

Contingent warrant liabilities	March 31, 2013
Balance at December 31, 2012	$ 15,001
Net increase in fair value of contingent warrant liabilities upon revaluation	12,840
Balance at March 31, 2013	$ 27,841

Income Taxes

We did not recognize any income tax expense for the three months ended March 31, 2013 and 2012.

Accounting Standards Codification Topic 740, Income Taxes ("ASC 740") provides for the recognition of deferred tax assets if realization of such assets is more likely than not. Based upon the weight of available evidence, which includes our historical operating performance and carry-back potential, we have determined that total deferred tax assets should be fully offset by a valuation allowance.

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We do not expect the unrecognized tax benefits to change significantly over the next twelve months. We will recognize interest and penalties accrued on any unrecognized tax benefits as a component of income tax expense. As of March 31, 2013, we have not accrued interest or penalties related to uncertain tax positions.

Liquidity and Capital Resources

The following table summarizes our cash and cash equivalents, our working capital and our cash flow activities as of the end of, and for each of, the periods presented (in thousands):

	March 31, 2013	December 31, 2012	Change
Cash and cash equivalents	$ 50,379	$ 45,345	$5,034
Short-term investments	$ 19,996	$ 39,987	$(19,991)
Working Capital	$ 60,600	$ 72,004	$(11,404)

	Three Months Ended March 31,		
	2013	2012	Change
Net cash used in operating activities	$ (14,528)	$ (11,675)	$(2,853)
Net cash provided by (used in) investing activities	19,502	(548)	20,050
Net cash provided by financing activities	60	38,766	(38,706)
Net increase in cash and cash equivalents	$ 5,034	$ 26,543	$(21,509)

Working Capital

The decrease in working capital was due primarily to a $15.0 million decrease in cash, cash equivalents, and short-term investments, partially offset by a $2.5 million reclassification of principal and accrued interest on our interest bearing obligations from long-term to short-term.

Cash Used in Operating Activities

Net cash used in operating activities was $14.5 million for the three months ended March 31, 2013, compared with $11.7 million for the same period in 2012. Net cash used in operating activities was $2.8 million higher in the first quarter of 2013 due primarily to a decrease in accounts payable and other accrued liabilities of $7.1 million during the first quarter of 2013 associated with timing of payments, compared to a $3.2 million decrease during the first quarter of 2012.

Cash Provided by (Used in) Investing Activities

Net cash provided by investing activities was $19.5 million for the three months ended March 31, 2013, compared with net cash used in investing activities of $0.5 million for the same period of 2012. $20.1 million change in cash provided by investing activities was due primarily to the maturity of $20.0 million in short-term investments during the first quarter of 2013. Cash used in investing activities for the three months ended March 31, 2012, primarily consisted of fixed asset purchases.

Cash Provided by Financing Activities

Net cash provided by financing activities was $0.1 million for the three months ended March 31, 2013, compared with $38.8 million for the same period of 2012. Cash provided by financing activities in the first quarter of 2013 related to

net proceeds received from employee stock purchases. Cash provided by financing activities in the first quarter of 2012 related to net proceeds received from the issuance of common stock and warrants of $36.2 million in the March 2012 underwritten public offering and net proceeds of $3.2 million received from the issuance of common stock under the 2011 ATM Agreement, offset by $0.7 million of principal payments on our loan with GECC.

Net proceeds received during the first quarters of 2013 and 2012 were used to continue development of our gevokizumab product candidate and for other working capital and general corporate purposes.

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We have incurred significant operating losses and negative cash flows from operations since our inception. At March 31, 2013, we had cash, cash equivalents, and short-term investments of $70.4 million. During 2013, we expect to continue using our cash, cash equivalents and short-term investments to fund ongoing operations. Additional licensing, antibody discovery and development collaboration agreements, government funding and financing arrangements may positively impact our cash balances. Based on our cash reserves and anticipated spending levels, revenue from collaborations including the gevokizumab license and collaboration agreement with Servier, funding from the loan agreement with GECC, our March 2012 and October 2012 public offerings, biodefense contracts and licensing transactions and other sources of funding that we believe to be available, we estimate we have sufficient cash resources to meet our anticipated net cash needs into late 2014. Any significant revenue shortfalls, increases in planned spending on development programs or more rapid progress of development programs than anticipated, as well as the unavailability of anticipated sources of funding, could shorten this period. If adequate funds are not available, we will be required to delay, reduce the scope of, or eliminate one or more of our product development programs and further reduce personnel-related costs. Progress or setbacks by potentially competing products may also affect our ability to raise new funding on acceptable terms.

Critical Accounting Estimates

Critical accounting estimates are those that require significant judgment and/or estimates by management at the time that the financial statements are prepared such that materially different results might have been reported if other assumptions had been made. We consider certain accounting policies including, but not limited to, revenue recognition, research and development expense, long-lived assets, contingent warrant liabilities, derivative instruments and stock-based compensation to be critical policies. There have been no significant changes in our critical accounting estimates during the three months ended March 31, 2013, as compared with those previously disclosed in our Annual Report on Form 10-K for the fiscal year ended December 31, 2012, filed with the SEC on March 12, 2013.

ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

Interest Rate Risk

We are exposed to market risks in the ordinary course of our business. These risks primarily include risk related to interest rate sensitivities. Our market risks related to interest rate sensitivities at March 31, 2013, have not changed materially from those discussed in Item 7A of our Form 10-K for the year ended December 31, 2012 filed with the SEC.

Foreign Currency Risk

We hold debt, incur expenses, and may be owed milestones denominated in foreign currencies. The amount of debt owed, expenses incurred, or milestones owed to us will be impacted by fluctuations in these foreign currencies. When the U.S. Dollar weakens against foreign currencies, the U.S. Dollar value of the foreign-currency denominated debt, expense, and milestones increases, and when the U.S. Dollar strengthens against these currencies, the U.S. dollar value of the foreign-currency denominated debt, expense, and milestones decreases. Consequently, changes in exchange rates will affect the amount we are required to repay on our €15.0 million loan from Servier and may affect our results of operations. We estimate that a hypothetical 0.01 change the Euro to USD exchange rate could increase or decrease our unrealized gains or losses by approximately $0.1 million.

Our loan from Servier was fully funded in January 2011, with the proceeds converting to approximately $19.5 million using the January 13, 2011 Euro to U.S. dollar exchange rate of 1.3020. At March 31, 2013, the €15.0 million outstanding principal balance under the Servier Loan Agreement would have equaled approximately $19.2 million

using the March 31, 2013 Euro to USD exchange rate of 1.2816. In May 2011, in order to manage our foreign currency exposure relating to our principal and interest payments on our loan from Servier, we entered into two foreign exchange option contracts to buy €1.5 million and €15.0 million in January 2014 and January 2016, respectively. Upfront premiums paid on these foreign exchange option contracts totaled $1.5 million and they had an aggregate fair value of $0.3 million at March 31, 2013. Our use of derivative financial instruments represents risk management; we do not enter into derivative financial contracts for trading purposes.

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ITEM 4. CONTROLS AND PROCEDURES

Evaluation of Controls and Procedures

Under the supervision and with the participation of our management, including our Chief Executive Officer (our principal executive officer) and our Vice President, Finance, Chief Financial Officer and Secretary (our principal financial and principal accounting officer), we conducted an evaluation of our disclosure controls and procedures, as such term is defined under Rule 13a-15(e) promulgated under the Securities Exchange Act of 1934, as amended, as of the end of the period covered by this report. Based on this evaluation, our Chief Executive Officer and our Vice President, Finance, Chief Financial Officer and Secretary concluded that our disclosure controls and procedures are effective as of the end of the period covered by this report in timely alerting them to material information relating to us and our consolidated subsidiaries required to be included in our periodic SEC filings.

Changes in Internal Control

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

PART II – OTHER INFORMATION

ITEM 1. LEGAL PROCEEDINGS

None.

ITEM 1A. RISK FACTORS

This Quarterly Report on Form 10-Q contains forward-looking information based on our current expectations. Because our actual results may differ materially from any forward-looking statements made by or on behalf of us, this section includes a discussion of important factors that could affect our actual future results, including, but not limited to, our revenues, expenses, operating results, cash flows, net loss and loss per share. Additional risks and uncertainties not presently known to us also may impair our business operations. You should carefully consider these risk factors, together with all of the other information included in this Quarterly Report on Form 10-Q as well as our other publicly available filings with the U.S. Securities and Exchange Commission, or SEC.

We have marked with an asterisk (*) those risks described below that reflect substantive changes from, or additions to, the risks described in our Annual Report on Form 10-K for the year ended December 31, 2012.

Because our product candidates are still being developed, we will require substantial funds to continue; we cannot be certain that funds will be available, and if they are not available, we may have to take actions that could adversely affect the price of our common stock and may not be able to continue operations.*

We will need to commit substantial funds to continue development of our product candidates, and we may not be able to obtain sufficient funds on acceptable terms, or at all. If we raise additional funds by issuing equity securities, our stockholders will experience dilution. Any debt financing or additional equity that we raise may contain terms that are not favorable to our stockholders or us. If we raise additional funds through collaboration and licensing arrangements with third parties, we may be required to relinquish some rights to our technologies or our product candidates, grant licenses on terms that are not favorable to us or enter into a collaboration arrangement for a product candidate at an earlier stage of development or for a lesser amount than we might otherwise choose.

Additional funds may not be available when we need them on terms that are acceptable to us, or at all. If adequate funds are not available on a timely basis, we may:

- terminate or delay clinical trials for one or more of our product candidates;
- further reduce our headcount and capital or operating expenditures; or
- curtail our spending on protecting our intellectual property.

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We finance our operations primarily through our multiple revenue streams resulting from discovery and development collaborations, biodefense contracts, the licensing of our antibody technologies, and sales of our common stock. In August 2010, we sold our royalty interest in CIMZIA® for gross proceeds of $4.0 million, including royalty revenue from the second quarter of 2010. As a result, we no longer have a royalty interest in CIMZIA. We received revenue from this royalty interest of $0.5 million in 2010.

Based on our cash, cash equivalents and short-term investments of $70.4 million at March 31, 2013, anticipated spending levels, anticipated cash inflows from collaborations, biodefense contracts and licensing transactions, funding availability including under our loan agreements, and the proceeds from the October 2012 public offering, we believe we have sufficient cash resources to meet our anticipated net cash needs into the fourth quarter of 2014. Any significant revenue shortfalls, increases in planned spending on development programs, more rapid progress of development programs than anticipated, or the initiation of new clinical trials, as well as the unavailability of anticipated sources of funding, could shorten this period or otherwise have a material adverse impact on our ability to finance our continued operations. If adequate funds are not available, we will be required to delay, reduce the scope of, or eliminate one or more of our product development programs and further reduce personnel-related costs. Progress or setbacks by potentially competing products also may affect our ability to raise new funding on acceptable terms. As a result, we do not know when or whether:

- operations will generate meaningful funds;
- additional agreements for product development funding can be reached;
- strategic alliances can be negotiated; or
- adequate additional financing will be available for us to finance our own development on acceptable terms, or at all.

Because all of our product candidates still are being developed, we have sustained losses in the past, and we expect to sustain losses in the future.*

We have experienced significant losses, and as of March 31, 2013, we had an accumulated deficit of $982.0 million.

For the three months ended March 31, 2013, we had a net loss of approximately $24.9 million, or $0.30 per share of common stock (basic and diluted). For the three months ended March 31, 2012, we had a net loss of approximately $30.4 million, or $0.69 per share of common stock (basic and diluted).

Our ability to achieve profitability is dependent in large part on the success of our development programs, obtaining regulatory approval for our product candidates and licensing certain of our preclinical compounds, all of which are uncertain. Our ability to fund our ongoing operations is dependent on the foregoing factors and on our ability to secure additional funds. Because our product candidates still are being developed, we do not know whether we will ever achieve sustained profitability or whether cash flow from future operations will be sufficient to meet our needs.

We are substantially dependent on Servier for the development and commercialization of gevokizumab and for other aspects of our business, and if we are unable to maintain our relationship with Servier, or Servier does not perform under our development and commercialization agreements with Servier, our business would be harmed significantly.

We have a number of agreements with Servier that are material to the conduct of our business, including:

- In December 2010, we entered into a license and collaboration agreement with Servier, to jointly develop and commercialize gevokizumab in multiple indications. Under the terms of the agreement, Servier has worldwide rights to cardiovascular disease and diabetes indications and rights outside the United States and Japan to all other indications, including Behçet's uveitis and other inflammatory and oncology indications. In late 2011, we announced Servier agreed to include the NIU Phase 3 trials under the terms of the collaboration agreement for Behçet's

uveitis. We retain development and commercialization rights for NIU and other inflammatory disease and oncology indications in the United States and Japan and have an option to reacquire rights to cardiovascular disease and diabetes indications from Servier in these territories. Should we exercise this option, we will be required to pay an option fee to Servier and partially reimburse a specified portion of Servier's incurred development expenses. The agreement contains mutual customary termination rights relating to matters, such as material breach by either party. Servier may terminate for safety issues, and we may terminate the agreement, with respect to a particular country or the European Patent Organization ("EPO") member states, for any challenge to our patent rights in that country or any EPO member state, respectively, by Servier. Servier also has a unilateral right to terminate the agreement for the European Union ("EU") or for non-EU countries, on a country-by-country basis, or in its entirety, in each case with six months' notice.

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- In December 2010, we entered into a loan agreement with Servier (the "Servier Loan Agreement"), which provides for an advance of up to €15.0 million and was funded fully in January 2011 with the proceeds converting to approximately $19.5 million at the January 13, 2011, Euro-to-U.S.-dollar exchange rate of 1.3020. This loan is secured by an interest in our intellectual property rights to all gevokizumab indications worldwide, excluding the United States and Japan. The loan has a final maturity date in 2016; however, after a specified period prior to final maturity, the loan is required to be repaid (1) at Servier's option, by applying up to a significant percentage of any milestone or royalty payments owed by Servier under our collaboration agreement and (2) using a significant percentage of any upfront, milestone or royalty payments we receive from any third-party collaboration or development partner for rights to gevokizumab in the United States and/or Japan. In addition, the loan becomes immediately due and payable upon certain customary events of default. At March 31, 2013, the €15.0 million outstanding principal balance under this Servier Loan Agreement would have equaled approximately $19.2 million using the March 31, 2013 Euro-to-U.S.-dollar exchange rate of 1.2816.

- Effective in January 2012, we entered into an amended and restated agreement with Servier for the United States commercialization rights to ACEON and, upon exercise by us of an option with respect to each product, a portfolio of additional FDC product candidates where perindopril is combined with another active ingredient(s), such as a calcium channel blocker. To date we have exercised this option with respect to one FDC product. This agreement, together with a related trademark license agreement, provides us with exclusive U.S. rights to ACEON and FDC1, and options on additional FDCs. The arrangement also provides that Servier will supply to us, and we will purchase exclusively from Servier, the active ingredients in ACEON and the FDCs, in some cases for a limited period. The agreement contains customary termination rights relating to matters, such as material breach by, or insolvency of, either party or, as to particular licensed products, for safety issues arising with respect to such products. Each party also has the right to terminate the arrangement if FDC1 does not receive FDA approval by December 31, 2014. Servier also has the right to terminate the arrangement if certain aspects of our commercialization strategy are not successful and Servier does not consent to an alternative strategy, or as to the FDCs, if we breach our obligations to certain of our service providers. Further, Servier also may terminate the agreement if we fail to achieve certain levels of sales of products and do not make a specified payment in such circumstances to maintain our license, or under certain circumstances upon our change in control, if we fail to take certain actions or make certain payments. We are working to identify a third-party organization that could sublicense this FDC and move it forward toward commercialization in the U.S. market.

Because Servier is an independent third party, it may be subject to different risks than we are and has significant discretion in, and different criteria for, determining the efforts and resources it will apply related to its agreements with us. Even though we have a collaborative relationship with Servier, our relationship could deteriorate or other circumstances may prevent our relationship with Servier from resulting in successful development of marketable products. If we are not able to maintain our working relationship with Servier, or if Servier does not perform under our agreements with Servier, our ability to develop and commercialize gevokizumab and the FDCs would be materially and adversely affected, as would our ability to commercialize ACEON.

We have received negative results from certain of our clinical trials, and we face uncertain results of other clinical trials of our product candidates.

Drug development has inherent risk, and we are required to demonstrate through adequate and well-controlled clinical trials that our product candidates are effective, with a favorable benefit-risk profile for use in their target profiles before we can seek regulatory approvals for their commercial use. It is possible we may never receive regulatory approval for any of our product candidates. Even if a product candidate receives regulatory approval, the resulting product may not gain market acceptance among physicians, patients, healthcare payors and the medical community. In March 2011, we announced our 421-patient Phase 2b trial of gevokizumab in Type 2 diabetes did not achieve the primary endpoint of reduction in hemoglobin A1c ("HbA1c") after six monthly treatments with

gevokizumab compared to placebo. In June 2011, we announced top-line trial results from our six-month 74-patient Phase 2a trial of gevokizumab in Type 2 diabetes, and there were no differences in glycemic control between the drug and placebo groups as measured by HbA1c levels.

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Many of our product candidates, including gevokizumab, XMet, and XOMA 3AB, require significant additional research and development, extensive preclinical studies and clinical trials and regulatory approval prior to any commercial sales. This process is lengthy and expensive, often taking a number of years. As clinical results frequently are susceptible to varying interpretations that may delay, limit or prevent regulatory approvals, the length of time necessary to complete clinical trials and to submit an application for marketing approval for a final decision by a regulatory authority varies significantly. As a result, it is uncertain whether:

- our future filings will be delayed;
- our preclinical and clinical studies will be successful;
- we will be successful in generating viable product candidates to targets;
- we will be able to provide necessary additional data;
- results of future clinical trials will justify further development; or
- we ultimately will achieve regulatory approval for any of these product candidates.

The timing of the commencement, continuation and completion of clinical trials may be subject to significant delays relating to various causes, including completion of preclinical testing and earlier-stage clinical trials in a timely manner, engaging contract research organizations and other service providers, scheduling conflicts with participating clinicians and clinical institutions, difficulties in identifying and enrolling patients who meet trial eligibility criteria, and shortages of available drug supply. Patient enrollment is a function of many factors, including the size of the patient population, the proximity of patients to clinical sites, the eligibility criteria for the trial, the existence of competing clinical trials and the availability of alternative or new treatments. Regardless of the initial size or relative complexity of a clinical trial, the costs of such trial may be higher than expected due to increases in duration or size of the trial, changes in the protocol pursuant to which the trial is being conducted, additional or special requirements of one or more of the healthcare centers where the trial is being conducted, or changes in the regulatory requirements applicable to the trial or in the standards or guidelines for approval of the product candidate being tested or for other unforeseen reasons. In addition, we conduct clinical trials in foreign countries, which may subject us to further delays and expenses as a result of increased drug shipment costs, additional regulatory requirements and the engagement of foreign clinical research organizations, as well as expose us to risks associated with foreign currency transactions insofar as we might desire to use U.S. Dollars to make contract payments denominated in the foreign currency where the trial is being conducted.

All of our product candidates are prone to the risks of failure inherent in drug development. Preclinical studies may not yield results that satisfactorily support the filing of an Investigational New Drug application (“IND”) (or a foreign equivalent) with respect to our product candidates. Even if these applications would be or have been filed with respect to our product candidates, the results of preclinical studies do not necessarily predict the results of clinical trials. Similarly, early stage clinical trials in healthy volunteers do not predict the results of later-stage clinical trials, including the safety and efficacy profiles of any particular product candidates. In addition, there can be no assurance the design of our clinical trials is focused on appropriate indications, patient populations, dosing regimens or other variables that will result in obtaining the desired efficacy data to support regulatory approval to commercialize the drug. Preclinical and clinical data can be interpreted in different ways. Accordingly, FDA officials or officials from foreign regulatory authorities could interpret the data differently than we or our collaboration or development partners do, which could delay, limit or prevent regulatory approval.

Administering any of our products or potential products may produce undesirable side effects, also known as adverse effects. Toxicities and adverse effects that we have observed in preclinical studies for some compounds in a particular research and development program may occur in preclinical studies or clinical trials of other compounds from the same program. Such toxicities or adverse effects could delay or prevent the filing of an IND (or a foreign equivalent) with respect to such products or potential products or cause us to cease clinical trials with respect to any drug candidate. In clinical trials, administering any of our products or product candidates to humans may produce adverse

effects. These adverse effects could interrupt, delay or halt clinical trials of our products and product candidates and could result in the FDA or other regulatory authorities denying approval of our products or product candidates for any or all targeted indications. The FDA, other regulatory authorities, our collaboration or development partners or we may suspend or terminate clinical trials at any time. Even if one or more of our product candidates were approved for sale, the occurrence of even a limited number of toxicities or adverse effects when used in large populations may cause the FDA to impose restrictions on, or stop, the further marketing of such drugs. Indications of potential adverse effects or toxicities that may occur in clinical trials and that we believe are not significant during the course of such clinical trials may actually turn out later to constitute serious adverse effects or toxicities when a drug has been used in large populations or for extended periods of time. Any failure or significant delay in completing preclinical studies or clinical trials for our product candidates, or in receiving and maintaining regulatory approval for the sale of any drugs resulting from our product candidates, may severely harm our reputation and business.

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In June 2011, Novartis announced an advisory committee of the FDA had voted in favor of the overall efficacy but not the overall safety of Ilaris® (canakinumab), a fully human monoclonal antibody that, like gevokizumab, targets IL-1 beta, to treat gouty arthritis attacks in patients who cannot obtain adequate relief with non-steroidal anti-inflammatory drugs or colchicine. Ilaris was initially approved in June 2009 for Cryopyrin-Associated Periodic Syndromes, an orphan indication. Novartis also stated that in two pivotal Phase 3 studies of canakinumab in gouty arthritis patients, a higher percentage of patients had adverse events with canakinumab than with the standard treatment for gouty arthritis, and more serious adverse events were reported by patients treated with canakinumab compared to patients receiving the standard treatment. In August 2011, Novartis announced the FDA had issued a Complete Response Letter requesting additional information, including clinical data to evaluate the benefit risk profile of canakinumab in refractory gouty arthritis patients. We have not yet determined what impact, if any, these developments may have on the development of gevokizumab.

If our therapeutic product candidates do not receive regulatory approval, neither our third-party collaborators, our contract manufacturers nor we will be able to manufacture and market them.

Our product candidates (including gevokizumab, FDC1, XMetA, XMetD, XMetS, and XOMA 3AB) cannot be manufactured and marketed in the United States or any other countries without required regulatory approvals. The United States government and governments of other countries extensively regulate many aspects of our product candidates, including:

- clinical development and testing;
- manufacturing;
- labeling;
- storage;
- record keeping;
- promotion and marketing; and
- importing and exporting.

In the United States, the FDA regulates pharmaceutical products under the Federal Food, Drug, and Cosmetic Act and other laws, including, in the case of biologics, the Public Health Service Act. At the present time, we believe many of our product candidates (including gevokizumab , XMetA, XMetD, XMetS, and XOMA 3AB) will be regulated by the FDA as biologics and some of our product candidates (including FDC1) will be regulated by the FDA as drugs. Initiation of clinical trials requires approval by health authorities. Clinical trials involve the administration of the investigational new drug to healthy volunteers or to patients under the supervision of a qualified principal investigator. Clinical trials must be conducted in accordance with FDA and International Conference on Harmonisation of Technical Requirements for Registration of Pharmaceuticals for Human Use Good Clinical Practices and the European Clinical Trials Directive under protocols that detail the objectives of the study, the parameters to be used to monitor safety and the efficacy criteria to be evaluated. Other national, foreign and local regulations also may apply. The developer of the drug must provide information relating to the characterization and controls of the product before administration to the patients participating in the clinical trials. This requires developing approved assays of the product to test before administration to the patient and during the conduct of the trial. In addition, developers of pharmaceutical products must provide periodic data regarding clinical trials to the FDA and other health authorities, and these health authorities may issue a clinical hold upon a trial if they do not believe, or cannot confirm, that the trial can be conducted without unreasonable risk to the trial participants. We cannot assure you that U.S. and foreign health authorities will not issue a clinical hold with respect to any of our clinical trials in the future.

The results of the preclinical studies and clinical testing, together with chemistry, manufacturing and controls information, are submitted to the FDA and other health authorities in the form of an NDA for a drug, and in the form of a Biologic License Application (“BLA”) for a biological product, requesting approval to commence commercial

sales. In responding to an NDA or BLA, the FDA or foreign health authorities may grant marketing approvals, request additional information or further research, or deny the application if it determines the application does not satisfy its regulatory approval criteria. Regulatory approval of an NDA, BLA, or supplement never is guaranteed, the approval process can take several years, is extremely expensive and can vary substantially based upon the type, complexity, and novelty of the products involved, as well as the target indications. FDA regulations and policies permit applicants to request accelerated or priority review pathways for products intended to treat certain serious or life-threatening illnesses in certain circumstances. If granted by the FDA, these review pathways can provide a shortened timeline to commercialize the product, although the shortened review timeline is often accompanied with additional post-market requirements. Although we may pursue the FDA's accelerated or priority review programs, we cannot guarantee the FDA will permit us to utilize these pathways or the FDA's review of our application will not be delayed. Moreover, even if the FDA agrees to an accelerated or priority review of any of our applications, we may not ultimately be able to obtain approval of our application in a timely fashion or at all. The FDA and foreign health authorities have substantial discretion in the drug and biologics approval processes. Despite the time and expense incurred, failure can occur at any stage, and we could encounter problems that cause us to abandon clinical trials or to repeat or perform additional preclinical, clinical or manufacturing-related studies.

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Changes in the regulatory approval policy during the development period, changes in, or the enactment of additional regulations or statutes, or changes in regulatory review for each submitted product application may cause delays in the approval or rejection of an application. State regulations may also affect our proposed products.

The FDA and other regulatory agencies have substantial discretion in both the product approval process and manufacturing facility approval process, and as a result of this discretion and uncertainties about outcomes of testing, we cannot predict at what point, or whether, the FDA or other regulatory agencies will be satisfied with our or our collaborators' submissions or whether the FDA or other regulatory agencies will raise questions that may be material and delay or preclude product approval or manufacturing facility approval. In light of this discretion and the complexities of the scientific, medical and regulatory environment, our interpretation or understanding of the FDA's or other regulatory agencies' requirements, guidelines or expectations may prove incorrect, which also could delay further or increase the cost of the approval process. As we accumulate additional clinical data, we will submit it to the FDA and other regulatory agencies, as appropriate, and such data may have a material impact on the approval process.

Given that regulatory review is an interactive and continuous process, we maintain a policy of limiting announcements and comments upon the specific details of regulatory review of our product candidates, subject to our obligations under the securities laws, until definitive action is taken.

We rely on third parties to provide services in connection with our product candidate development and manufacturing programs. The inadequate performance by or loss of any of these service providers could affect our product candidate development.

Several third parties provide services in connection with our preclinical and clinical development programs, including in vitro and in vivo studies, assay and reagent development, immunohistochemistry, toxicology, pharmacokinetics, clinical trial support, manufacturing and other outsourced activities. If these service providers do not adequately perform the services for which we have contracted or cease to continue operations and we are not able to find a replacement provider quickly or we lose information or items associated with our product candidates, our development programs may be delayed. In particular, we have a master services agreement with a contract research organization that provides the majority of our clinical trial services with respect to our collaboration with Servier in relation to the FDC products. Under this agreement, which was amended in October 2011, we are obligated to fund the clinical trial services provided by the contract research organization by allocating a specified portion of the revenue received from sales of ACEON. If we do not receive sufficient revenue from sales of ACEON to fund such services, and we do not otherwise pay the contract research organization for these services, certain of our rights under the commercialization agreement with Servier may terminate, unless Servier elects to make such payments on our behalf, in which case we will be required to reimburse Servier for such payments within a specified timeframe. Certain rights under the commercialization agreement with Servier also will terminate if we fail to reimburse Servier within such period.

We may not obtain orphan drug exclusivity, or we may not receive the full benefit of orphan drug exclusivity even if we obtain such exclusivity.

The FDA has awarded orphan drug status to gevokizumab for the treatment of non-infectious, intermediate, posterior or pan uveitis, and chronic non-infectious anterior uveitis and Behçet's uveitis. Under the Orphan Drug Act, the first company to receive FDA approval for gevokizumab for the designated orphan drug indication will obtain seven years of marketing exclusivity, during which time the FDA may not approve another company's application for gevokizumab for the same orphan indication. Even though we have obtained orphan drug designation for certain indications for gevokizumab and even if we obtain orphan drug designation for our future product candidates or other indications, due to the uncertainties associated with developing pharmaceutical products, we may not be the first to obtain marketing approval for any particular orphan indication, or we may not obtain approval for an indication for

which we have obtained orphan drug designation. Further, even if we obtain orphan drug exclusivity for a product, that exclusivity may not protect the product effectively from competition because different drugs can be approved for the same condition. Even after an orphan drug is approved, the FDA can subsequently approve the same drug for the same condition if the FDA concludes that the later drug is safer, more effective or makes a major contribution to patient care. Orphan drug designation neither shortens the development time or regulatory review time of a drug, nor gives the drug any advantage in the regulatory review or approval process.

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Even after FDA approval, a product may be subject to additional testing or significant marketing restrictions, its approval may be withdrawn or it may be removed voluntarily from the market.

Even if we receive regulatory approval for our product candidates, we will be subject to ongoing regulatory oversight and review by the FDA and other regulatory entities. The FDA, the European Commission or another regulatory agency may impose, as a condition of the approval, ongoing requirements for post-approval studies or post-approval obligations, including additional research and development and clinical trials, and the FDA, European Commission or other regulatory agency subsequently may withdraw approval based on these additional trials. As the current holder of the ACEON® NDA, we are required to submit annual reports to the FDA and are responsible for pharmacovigilance activities related to the product.

Even for approved products, the FDA, European Commission or other regulatory agency may impose significant restrictions on the indicated uses, conditions for use, labeling, advertising, promotion, marketing and/or production of such product. In addition, the labeling, packaging, adverse event reporting, storage, advertising, promotion and record-keeping for our products are subject to extensive regulatory requirements.

Furthermore, a marketing approval of a product may be withdrawn by the FDA, the European Commission or another regulatory agency or such a product may be withdrawn voluntarily by the company marketing it based, for example, on subsequently arising safety concerns. In February 2009, the European Medicines Agency ("EMA") announced it had recommended suspension of the marketing authorization of RAPTIVA® in the EU and its Committee for Medicinal Products for Human Use ("CHMP") had concluded the benefits of RAPTIVA no longer outweigh its risks because of safety concerns, including the occurrence of progressive multifocal leukoencephalopathy ("PML") in patients taking the medicine. In the second quarter of 2009, Genentech announced and carried out a phased voluntary withdrawal of RAPTIVA from the U.S. market, based on the association of RAPTIVA with an increased risk of PML. We had participated in the development of RAPTIVA.

The FDA, European Commission and other agencies also may impose various civil or criminal sanctions for failure to comply with regulatory requirements, including withdrawal of product approval.

We may issue additional equity securities and thereby materially and adversely affect the price of our common stock.*

We are authorized to issue, without stockholder approval, 1,000,000 shares of preferred stock, of which none were issued and outstanding as of May 6, 2013, which may give other stockholders dividend, conversion, voting, and liquidation rights, among other rights, which may be superior to the rights of holders of our common stock. In April 2011, the 2,959 Series B convertible preference shares previously issued to Genentech were converted by Genentech into 254,560 shares of common stock. In addition, we are authorized to issue, generally without stockholder approval, up to 138,666,666 shares of common stock, of which 82,893,328 were issued and outstanding as of May 6, 2013. If we issue additional equity securities, the price of our common stock may be materially and adversely affected.

On February 4, 2011, we entered into an At Market Issuance Sales Agreement (the "2011 ATM Agreement") with McNicoll, Lewis & Vlak LLC (now known as MLV & Co. LLC, "MLV"), under which we may sell shares of our common stock from time to time through the MLV, as our agent for the offer and sale of the shares, in an aggregate amount not to exceed the amount that can be sold under our Registration Statement on Form S-3 (File No. 333-172197) filed with the SEC on February 11, 2011, and amended on March 10, 2011, June 3, 2011, and January 3, 2012, which was most recently declared effective by the SEC on January 17, 2012. MLV may sell the shares by any method permitted by law deemed to be an "at the market" offering as defined in Rule 415 of the Securities Act, including without limitation sales made directly on The NASDAQ Global Market, on any other existing trading market for our common stock or to or through a market maker. MLV also may sell the shares in privately negotiated transactions, subject to our prior approval. From the inception of the 2011 ATM Agreement through May 6, 2013, we

sold a total of 7,572,327 shares of common stock under this agreement for aggregate gross proceeds of $14.6 million.

On March 9, 2012, we completed an underwritten public offering of 29,669,154 shares of our common stock, and accompanying warrants to purchase one half of a share of common stock for each share purchased, at a public offering price of $1.32 per share. Total gross proceeds from the offering were approximately $39.2 million, before deducting underwriting discounts and commissions and estimated offering expenses totaling approximately $3.0 million. The warrants, which represent the right to acquire an aggregate of up to 14,834,577 shares of common stock, are exercisable immediately and have a five-year term and an exercise price of $1.76 per share. As of May 6, 2013, 14,265,970 of these warrants were outstanding.

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On October 29, 2012, we completed an underwritten public offering of 13,333,333 shares of our common stock, at a public offering price of $3.00 per share. In addition, we granted the underwriters a 30-day option to purchase up to an additional 1,999,999 shares of common stock on the same terms and conditions, solely to cover over-allotments, which option was not exercised within the 30-day option period. Total gross proceeds from the offering were approximately $40.0 million, before deducting underwriting discounts and commissions and estimated offering expenses totaling approximately $3.0 million.

The financial terms of future collaborative or licensing arrangements could result in dilution of our share value.

Funding from collaboration partners and others has in the past and may in the future involve issuance by us of our shares. We cannot be certain how the purchase price of such shares, the relevant market price or premium, if any, will be determined or when such determinations will be made. Any such issuance could result in dilution in the value of our issued and outstanding shares.

Our share price may be volatile and there may not be an active trading market for our common stock.*

There can be no assurance the market price of our common stock will not decline below its present market price or there will be an active trading market for our common stock. The market prices of biotechnology companies have been and are likely to continue to be highly volatile. Fluctuations in our operating results and general market conditions for biotechnology stocks could have a significant impact on the volatility of our common stock price. We have experienced significant volatility in the price of our common stock. From January 1, 2013, through May 6, 2013, the share price of our common stock has ranged from a high of $3.67 to a low of $2.43. Factors contributing to such volatility include, but are not limited to:

- results of preclinical studies and clinical trials;
- information relating to the safety or efficacy of products or product candidates;
- developments regarding regulatory filings;
- announcements of new collaborations;
- failure to enter into collaborations;
- developments in existing collaborations;
- our funding requirements and the terms of our financing arrangements;
- technological innovations or new indications for our therapeutic products and product candidates;
- introduction of new products or technologies by us or our competitors;
- sales and estimated or forecasted sales of products for which we receive royalties, if any;
- government regulations;
- developments in patent or other proprietary rights;
- the number of shares issued and outstanding;
- the number of shares trading on an average trading day;
- announcements regarding other participants in the biotechnology and pharmaceutical industries; and
- market speculation regarding any of the foregoing.

If we are unable to continue to meet the requirements for continued listing on The NASDAQ Global Market, then we may be de-listed. In March 2010, we received a Staff Determination letter from The NASDAQ Stock Market LLC (“NASDAQ”) indicating we had not regained compliance with the minimum $1.00 per share requirement for continued inclusion on The NASDAQ Global Market, pursuant to NASDAQ Listing Rule 5450(a)(1). On August 18, 2010, we effected a reverse split of our common stock to regain compliance.

We may not be successful in commercializing our products, which could affect our development efforts.

We began commercializing our first product, ACEON, in January 2012, and we have limited experience in the sales, marketing and distribution of pharmaceutical products. There can be no assurance we will be able to maintain the arrangements we have with third-party suppliers, distributors and other service providers that are necessary for us to perform these activities or our efforts will be successful. Maintaining or expanding these arrangements, or developing our own capabilities, may divert attention and resources from or otherwise negatively affect our development programs.

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Our rights to commercialize ACEON are licensed from Servier, and we are obligated to use diligent efforts to develop and commercialize the products covered by our agreement in accordance with the terms and conditions of that agreement. Our ability to satisfy some of these obligations is dependent on factors that are outside of our control. Our agreement with Servier may be terminated by Servier if we materially breach our obligations and fail to cure such breach, for our insolvency, or terminated by either party with respect to any individual licensed product in the event of certain safety issues are presented. Each party also has the right to terminate the agreement if FDC1 does not receive FDA approval by December 31, 2014, and Servier may terminate the agreement if we fail to achieve certain levels of annual net sales of products and do not make a specified payment to maintain our license. Servier also has the right to terminate the agreement if we do not meet specified commercialization objectives and Servier does not consent to an alternative strategy or, as to the FDCs, if we breach our obligations to certain of our service providers. Servier also may terminate under certain circumstances upon our change in control, if we fail to take certain actions or make certain payments. If our agreement is terminated, we would have no further rights to develop and commercialize these products.

Furthermore, because we intend to use revenues generated by sales of ACEON in part to fund development of FDC1, lower than expected revenues from such sales could adversely affect our ability to fund the costs of, and progress, such development.

We are subject to various state and federal healthcare related laws and regulations that may impact the commercialization of ACEON or our product candidates and could subject us to significant fines and penalties.

Our operations may be directly or indirectly subject to various state and federal healthcare laws, including, without limitation, the federal Anti-Kickback Statute, the federal False Claims Act and HIPAA/HITECH. These laws may impact, among other things, the commercial operations for ACEON or any of our product candidates that may be approved for commercial sale.

The federal Anti-Kickback Statute prohibits persons from knowingly and willfully soliciting, offering, receiving or providing remuneration, directly or indirectly, in exchange for or to induce either the referral of an individual, or the furnishing or arranging for a good or service, for which payment may be made under a federal healthcare program, such as the Medicare and Medicaid programs. Several courts have interpreted the statute's intent requirement to mean that if any one purpose of an arrangement involving remuneration is to induce referrals of federal healthcare covered business, the statute has been violated. The Anti-Kickback Statute is broad and prohibits many arrangements and practices that are lawful in businesses outside of the healthcare industry. Penalties for violations of the federal Anti-Kickback Statute include criminal penalties and civil sanctions such as fines, penalties, imprisonment and possible exclusion from Medicare, Medicaid and other federal healthcare programs. Many states also have adopted laws similar to the federal Anti-Kickback Statute, some of which apply to the referral of patients for healthcare items or services reimbursed by any source, not only the Medicare and Medicaid programs. The Physician Payments Sunshine Act also has several state equivalents, which require, and under which the Federal government will require in 2013, disclosure of payments or other transfers of value we make to physicians.

The federal False Claims Act prohibits persons from knowingly filing, or causing to be filed, a false claim to, or the knowing use of false statements to obtain payment from the federal government. Suits filed under the False Claims Act, known as "qui tam" actions, can be brought by any individual on behalf of the government and such individuals, commonly known as "whistleblowers", may share in any amounts paid by the entity to the government in fines or settlement. The filing of qui tam actions has caused a number of pharmaceutical, medical device and other healthcare companies to have to defend a False Claims Act action. When an entity is determined to have violated the False Claims Act, it may be required to pay up to three times the actual damages sustained by the government, plus civil penalties for each separate false claim. Various states also have enacted laws modeled after the federal False Claims Act.

The Federal Health Insurance Portability and Accountability Act of 1996 (“HIPAA”), created new federal criminal statutes that prohibit executing a scheme to defraud any healthcare benefit program and making false statements relating to healthcare matters and was amended by the Health Information Technology and Clinical Health Act (“HITECH”), and its implementing regulations, which imposes certain requirements relating to the privacy, security and transmission of individually identifiable health information. We take our obligation to maintain our compliance with these various laws and regulations seriously. If we are found to be in violation of any of the laws and regulations described above or other applicable state and federal healthcare fraud and abuse laws, we may be subject to penalties, including civil and criminal penalties, damages, fines, exclusion from government healthcare reimbursement programs and the curtailment or restructuring of our operations, all of which could have a material adverse effect on our business and results of operations.

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Certain of our technologies are in-licensed from third parties, so our capabilities using them are restricted and subject to additional risks.

We license technologies from third parties. These technologies include but are not limited to phage display technologies licensed to us in connection with our bacterial cell expression technology licensing program. However, our use of these technologies is limited by certain contractual provisions in the licenses relating to them, and although we have obtained numerous licenses, intellectual property rights in the area of phage display are particularly complex. If the owners of the patent rights underlying the technologies that we license do not properly maintain or enforce those patents, our competitive position and business prospects could be harmed. Our success will depend in part on the ability of our licensors to obtain, maintain and enforce our in-licensed intellectual property. Our licensors may not be successful in prosecuting the patent applications to which we have licenses, or our licensors may fail to maintain existing patents. They may determine not to pursue litigation against other companies that are infringing these patents, or they may pursue such litigation less aggressively than we would. Our licensors also may seek to terminate our license, which could cause us to lose the right to use the licensed intellectual property and adversely affect our ability to commercialize our technologies, products or services.

We do not know whether there will be, or will continue to be, a viable market for the products in which we have an ownership or royalty interest.

Even if products in which we have an interest receive approval in the future, they may not be accepted in the marketplace. In addition, we or our collaborators or licensees may experience difficulties in launching new products, many of which are novel and based on technologies that are unfamiliar to the healthcare community. We have no assurance healthcare providers and patients will accept such products, if developed. For example, physicians and/or patients may not accept a product for a particular indication because it has been biologically derived (and not discovered and developed by more traditional means) or if no biologically derived products are currently in widespread use in that indication. Similarly, physicians may not accept a product if they believe other products to be more effective or more cost effective or are more comfortable prescribing other products.

Safety concerns also may arise in the course of on-going clinical trials or patient treatment as a result of adverse events or reactions. For example, in February 2009, the EMA announced it had recommended suspension of the marketing authorization of RAPTIVA in the EU and EMD Serono Inc., the company that marketed RAPTIVA in Canada (“EMD Serono”) announced that in consultation with Health Canada, the Canadian health authority (“Health Canada”), it would suspend marketing of RAPTIVA in Canada. In March 2009, Merck Serono Australia Pty Ltd, the company that marketed RAPTIVA in Australia (“Merck Serono Australia”), following a recommendation from the Therapeutic Goods Administration, the Australian health authority (“TGA”), announced it was withdrawing RAPTIVA from the Australian market. In the second quarter of 2009, Genentech announced and carried out a phased voluntary withdrawal of RAPTIVA from the U.S. market, based on the association of RAPTIVA with an increased risk of PML, and sales of the product ceased.

Furthermore, government agencies, as well as private organizations involved in healthcare, from time to time publish guidelines or recommendations to healthcare providers and patients. Such guidelines or recommendations can be very influential and may adversely affect product usage directly (for example, by recommending a decreased dosage of a product in conjunction with a concomitant therapy or a government entity withdrawing its recommendation to screen blood donations for certain viruses) or indirectly (for example, by recommending a competitive product over our product). Consequently, we do not know if physicians or patients will adopt or use our products for their approved indications.

Even approved and marketed products are subject to risks relating to changes in the market for such products. Introduction or increased availability of generic versions of products can alter the market acceptance of branded

products, such as ACEON. In addition, unforeseen safety issues may arise at any time, regardless of the length of time a product has been on the market.

Our third-party collaborators, licensees, suppliers or contractors may not have adequate manufacturing capacity sufficient to meet market demand.

Upon approval of any of our product candidates or in the event of increased demand for marketed products, we do not know whether the capacity of the manufacturing facilities of our existing or future third-party collaborators, licensees, suppliers or contractors will be available or can be increased to produce sufficient quantities of our products to meet market demand. Also, if we or our third-party collaborators, licensees, suppliers or contractors need additional manufacturing facilities to meet market demand, we cannot predict that we will successfully obtain those facilities because we do not know whether they will be available on acceptable terms. In addition, any manufacturing facilities acquired or used to meet market demand must meet the FDA’s quality assurance guidelines.

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In addition to our agreements with Servier, our agreements with other third parties, many of which are significant to our business, expose us to numerous risks.

Our financial resources and our marketing experience and expertise are limited. Consequently, our ability to develop products successfully depends, to a large extent, upon securing the financial resources and/or marketing capabilities of third parties other than Servier. For example:

- In March 2004, we announced we had agreed to collaborate with Chiron Corporation (now Novartis) for the development and commercialization of antibody products for the treatment of cancer. In April 2005, we announced the initiation of clinical testing of the first product candidate out of the collaboration, HCD122, an anti-CD40 antibody, in patients with advanced chronic lymphocytic leukemia. In October 2005, we announced the initiation of the second clinical trial of HCD122 in patients with multiple myeloma. In November 2008, we announced the restructuring of this product development collaboration, which involved six development programs including the ongoing HCD122 and LFA102 programs. In exchange for cash and debt reduction on our existing loan facility with Novartis, Novartis has control over the HCD122 and LFA102 programs, as well as the right to expand the development of these programs into additional indications outside of oncology.

- In March 2005, we entered into a contract with the National Institute of Allergy and Infectious Diseases ("NIAID") to produce three monoclonal antibodies designed to protect U.S. citizens against the harmful effects of botulinum neurotoxin used in bioterrorism. In July 2006, we entered into an additional contract with NIAID for the development of an appropriate formulation for human administration of these three antibodies in a single injection. In September 2008, we announced we had been awarded an additional contract with NIAID to support our on-going development of drug candidates toward clinical trials in the treatment of botulism poisoning. In October 2011, we announced we had been awarded an additional contract with NIAID to develop broad-spectrum antitoxins for the treatment of human botulism poisoning.

- In December 2011, we entered into a loan agreement with GECC (the "GECC Loan Agreement"), under which GECC agreed to make a term loan in an aggregate principal amount of $10 million to XOMA (US) LLC, our wholly owned subsidiary, and upon execution of the GECC Loan Agreement, GECC funded the term loan. The term loan is guaranteed by us and our two other principal subsidiaries, XOMA Ireland Limited and XOMA Technology Ltd. As security for our obligations under the GECC Loan Agreement, we, XOMA (US) LLC, XOMA Ireland Limited and XOMA Technology Ltd. each granted a security interest pursuant to a guaranty, pledge and security agreement in substantially all of our existing and after-acquired assets, excluding our intellectual property assets (such as those relating to our gevokizumab and anti-botulism products). We were required to repay the principal amount of the Term Loan over a period of 42 installments of principal and accrued interest, but we amended the GECC Loan Agreement on September 27, 2012, as described below. The GECC Loan Agreement contains customary representations and warranties and customary affirmative and negative covenants, including restrictions on the ability to incur indebtedness, grant liens, make investments, dispose of assets, enter into transactions with affiliates and amend existing material agreements, in each case subject to various exceptions. In addition, the GECC Loan Agreement contains customary events of default that entitle GECC to cause any or all of the indebtedness under the GECC Loan Agreement to become immediately due and payable. The events of default include any event of default under a material agreement or certain other indebtedness. We may prepay the term loan in full voluntarily, but not in part, and any voluntary and certain mandatory prepayments are subject to a prepayment premium of 3% in the first year of the loan, 2% in the second year and 1% thereafter, with certain exceptions. We also will be required to pay the final payment fee in connection with any voluntary or mandatory prepayment. Pursuant to the GECC Loan Agreement, we issued to GECC unregistered stock purchase warrants, which entitle GECC to purchase up to an aggregate of 263,158 unregistered shares of XOMA common stock at an exercise price equal to $1.14 per share, are exercisable immediately and expire

on December 30, 2016.

- On September 27, 2012, we entered into an amendment to the GECC Loan Agreement providing for an additional term loan in the amount of $4.6 million and an interest-only monthly repayment period with respect to the aggregate loan obligation of $12.5 million outstanding following the effective date of the amendment through March 1, 2013, at a stated interest rate of 10.9% per annum. Thereafter, we are obligated to make monthly principal payments of $0.3 million, plus accrued interest, at a stated interest rate of 10.9% per annum, over a 27-month period commencing on April 1, 2013, and through June 15, 2015, at which time the remaining outstanding principal amount of $3.1 million, plus accrued interest, shall be due. A final payment fee in the amount of $0.9 million is payable on the date upon which the outstanding principal amount is required to be repaid in full. Any mandatory or voluntary prepayment of the $12.5 million will accelerate the due date of the final payment fee and trigger a prepayment penalty equal to 3% of the outstanding principal amount being prepaid if prepaid on or before September 27, 2013, 2% if prepaid on or before September 27, 2014, and 1% if prepaid after September 27, 2014, but prior to the maturity date. In connection with the amendment, on September 27, 2012, we issued GE a warrant to purchase up to 39,346 shares of our common stock, which warrant is exercisable immediately, has a five-year term and has an exercise price of $3.54 per share.

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- We have licensed our bacterial cell expression technology, an enabling technology used to discover and screen, as well as develop and manufacture, recombinant antibodies and other proteins for commercial purposes, to over 60 companies. As of May 6, 2013, we were aware of two antibody products manufactured using this technology that have received FDA approval, Genentech's LUCENTIS® (ranibizumab injection) for treatment of neovascular wet age-related macular degeneration and UCB's CIMZIA® (certolizumab pegol) for treatment of Crohn's disease and rheumatoid arthritis. In the third quarter of 2009, we sold our LUCENTIS royalty interest to Genentech. In the third quarter of 2010, we sold our CIMZIA royalty interest.

- On July 24, 2012, Servier and we entered into an agreement with Boehringer Ingelheim to transfer XOMA's technology and processes for the manufacture of gevokizumab to Boehringer lngelheim for Boehringer Ingelheim's implementation and validation in preparation for the commercial manufacture of gevokizumab. Upon the successful completion of the transfer and the establishment of biological comparability, including validation of the XOMA processes as implemented by Boehringer Ingelheim, we intend Boehringer Ingelheim will produce gevokizumab for XOMA's commercial use at its facility in Biberach, Germany. Servier and we retain all rights to the development and commercialization of gevokizumab. Transferring of our technology to Boehringer Ingelheim exposes us to numerous risks, including the possibility that Boehringer Ingelheim may not perform under the agreement as anticipated, and that we will need to successfully conduct a comparability trial demonstrating to the FDA's satisfaction the similarity between XOMA-manufactured and Boehringer Ingelheim-manufactured product.

Because our collaborators, licensees, suppliers and contractors are independent third parties, they may be subject to different risks than we are and have significant discretion in, and different criteria for, determining the efforts and resources they will apply related to their agreements with us. If these collaborators, licensees, suppliers and contractors do not successfully perform the functions for which they are responsible, we may not have the capabilities, resources or rights to do so on our own.

We do not know whether we, our collaborators or licensees will successfully develop and market any of the products that are or may become the subject of any of our collaboration or licensing arrangements. In some cases these arrangements provide for funding solely by our collaborators or licensees, and in other cases, all of the funding for certain projects and a significant portion of the funding for other projects is to be provided by our collaborator or licensee, and we provide the balance of the funding. Even when we have a collaborative relationship, other circumstances may prevent it from resulting in successful development of marketable products. In addition, third-party arrangements such as ours also increase uncertainties in the related decision-making processes and resulting progress under the arrangements, as we and our collaborators or licensees may reach different conclusions, or support different paths forward, based on the same information, particularly when large amounts of technical data are involved. Furthermore, our contracts with NIAID contain numerous standard terms and conditions provided for in the applicable Federal acquisition regulations and customary in many government contracts, some of which could allow the U.S. government to exercise certain rights under the technology developed under these contracts. Uncertainty exists as to whether we will be able to comply with these terms and conditions in a timely manner, if at all. In addition, we are uncertain as to the extent of NIAID's demands and the flexibility that will be granted to us in meeting those demands.

Although we continue to evaluate additional strategic alliances and potential partnerships, we do not know whether or when any such alliances or partnerships will be entered into.

Products and technologies of other companies may render some or all of our products and product candidates noncompetitive or obsolete.

Developments by others may render our products, product candidates, or technologies obsolete or uncompetitive. Technologies developed and utilized by the biotechnology and pharmaceutical industries are changing

continuously and substantially. Competition in antibody-based technologies is intense and is expected to increase in the future as a number of established biotechnology firms and large chemical and pharmaceutical companies advance in these fields. Many of these competitors may be able to develop products and processes competitive with or superior to our own for many reasons, including that they may have:

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- significantly greater financial resources;
- larger research and development and marketing staffs;
- larger production facilities;
- entered into arrangements with, or acquired, biotechnology companies to enhance their capabilities; or
- extensive experience in preclinical testing and human clinical trials.

These factors may enable others to develop products and processes competitive with or superior to our own or those of our collaborators. In addition, a significant amount of research in biotechnology is being carried out in universities and other non-profit research organizations. These entities are becoming increasingly interested in the commercial value of their work and may become more aggressive in seeking patent protection and licensing arrangements. Furthermore, many companies and universities tend not to announce or disclose important discoveries or development programs until their patent position is secure or, for other reasons, later; as a result, we may not be able to track development of competitive products, particularly at the early stages. Positive or negative developments in connection with a potentially competing product may have an adverse impact on our ability to raise additional funding on acceptable terms. For example, if another product is perceived to have a competitive advantage, or another product's failure is perceived to increase the likelihood that our product will fail, then investors may choose not to invest in us on terms we would accept or at all.

The examples below pertain to competitive events in the market that we review quarterly yet are not intended to be representative of all existing competitive events.

Gevokizumab

We, in collaboration with Servier, are developing gevokizumab, a potent monoclonal antibody with unique allosteric modulating properties that binds strongly to interleukin-1 beta (IL-1 beta), a pro-inflammatory cytokine. In binding to IL-1 beta, gevokizumab inhibits the activation of the IL-1 receptor, thereby modulating the cellular signaling events that produce inflammation. Other companies are developing other products based on the same or similar therapeutic targets as gevokizumab, and these products may prove more effective than gevokizumab. We are aware that:

- Novartis markets and is developing Ilaris (canakinumab, ACZ885), a fully human monoclonal antibody that selectively binds to and neutralizes IL-1 beta. Since 2009, canakinumab has been approved in over 50 countries for the treatment of children and adults suffering from Cryopyrin-Associated Periodic Syndrome ("CAPS"). Novartis has filed for regulatory approval of canakinumab in the United States and Europe for the treatment of acute attacks in gouty arthritis. On March 1, 2013, Novartis announced that they received EU approval for Ilaris in patients suffering acute gouty arthritis attacks which cannot gain relief from current treatments. It is administered as a single 150 mg subcutaneous injection. In September 2011, Novartis announced positive results of a pivotal Phase 3 trial of canakinumab in patients with systemic juvenile idiopathic arthritis and it plans to seek regulatory approval for this indication in 2012. Novartis also is pursuing other diseases in which IL-1 beta may play a prominent role, such as systemic secondary prevention of cardiovascular events.

- Eli Lilly and Company ("Lilly") is developing a monoclonal antibody to IL-1 beta in Phase 1 studies for the treatment of cardiovascular disease. In June 2011, Lilly reported results from a Phase 2 study of LY2189102 in 106 patients with Type 2 diabetes, showing a significant ($p<0.05$), early reduction in C reactive protein ("CRP"), moderate reduction in HbA1c and anti-inflammatory effects. We do not know whether LY2189102 remains in development.

- In 2008, Swedish Orphan Biovitrum obtained from Amgen the global exclusive rights to Kineret® (anakinra) for rheumatoid arthritis as currently indicated in its label. In November 2009, the agreement regarding Swedish Orphan Biovitrum's Kineret license was expanded to include certain orphan indications. Kineret is an IL-1 receptor antagonist (IL-1ra) that has been evaluated in multiple IL-1-mediated diseases, including indications we are

considering for gevokizumab. In addition to other on-going studies, a proof-of-concept clinical trial in the United Kingdom investigating Kineret in patients with a certain type of myocardial infarction, or heart attack, has been completed. In August 2010, Biovitrum announced the FDA had granted orphan drug designation to Kineret for the treatment of CAPS, and in January 2013 they obtained FDA approval for NOMID, a severe form of CAPS.

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- In February 2008, Regeneron Pharmaceuticals, Inc. (“Regeneron”), announced it had received marketing approval from the FDA for ARCALYST® (rilonacept) Injection for Subcutaneous Use, an interleukin-1 blocker or IL-1 Trap, for the treatment of CAPS, including Familial Cold Auto-inflammatory Syndrome and Muckle-Wells Syndrome in adults and children 12 and older. In September 2009, Regeneron announced rilonacept was approved in the EU for CAPS. In June 2010 and February 2011, Regeneron announced positive results of two Phase 3 clinical trials of rilonacept in gout. In November 2011, Regeneron announced the FDA had accepted for review Regeneron’s supplemental BLA for ARCALYST for the prevention and treatment of gout. A meeting of an FDA advisory panel to review this supplemental BLA was held in May 2012 with a recommendation against approval of the new use in gout. In July 2012, the FDA issued a Complete Response Letter that states the FDA cannot approve the application in its current form and has requested additional clinical data, as well as additional CMC information related to a proposed new dosage form. Regeneron is reviewing the complete response letter from the FDA and will determine appropriate next steps.

- Amgen has been developing AMG 108, a fully human monoclonal antibody that targets inhibition of the action of IL-1. In April 2008, Amgen discussed results from a Phase 2 study in rheumatoid arthritis. AMG 108 showed statistically significant improvement in the signs and symptoms of rheumatoid arthritis and was well tolerated. In January 2011, MedImmune, the worldwide biologics unit for AstraZeneca PLC, announced Amgen granted it rights to develop AMG 108 worldwide except in Japan.

- In June 2009, Cytos Biotechnology AG announced the initiation of an ascending dose Phase 1/2a study of CYT013-IL1bQb, a therapeutic vaccine targeting IL-1 beta, in Type 2 diabetes. In 2010, this study was extended to include two additional groups of patients.

- The following companies have completed or are conducting or planning Phase 3 clinical trials of the following products for the treatment of noninfectious intermediate, posterior or pan-uveitis: Abbott - HUMIRA® (adalimumab); Lux Biosciences, Inc. – LUVENIQ® (voclosporin); Novartis - Myfortic® (mycophenalate sodium) and Santen Pharmaceutical Co., Ltd. – Sirolimus® (rapamycin).

Perindopril

We currently are selling ACEON, an angiotensin converting enzyme (“ACE”) inhibitor, and developing FDC1, a fixed-dose combination of perindopril arginine and amlodipine besylate, a calcium channel blocker.

The ACE inhibitor market is highly genericized with all options being available generically. We are aware:

- The leading product (based on annual sales) in the United States within the ACE inhibitor category is lisinopril, formerly marketed by Astra-Zeneca Pharmaceuticals LP under the brand ZESTRIL® and by Merck & Co. under the brand Prinivil®.

- There are multiple options in the FDC market combining ACE inhibitors with diuretics, and two options combining an ACE inhibitor with a calcium channel blocker. Current options with a calcium channel blocker are benazepril/amlodipine, formerly marketed by Novartis Pharmaceuticals as Lotrel®, and trandolapril/verapamil, formerly marketed by Abbot Laboratories as Tarka®.

ACE inhibitors are a segment of the larger Renin Angiotensin Aldosterone System (“RAAS”) market. This market is comprised of ACE inhibitors and angiotensin receptor blockers (“ARB”). Both classes act on the RAAS in different ways to control blood pressure. We are aware the most successful of the ARB (in terms of annual sales) is valsartan, trade name Diovan®, which is marketed by Novartis. This compound, along with other ARBs, has been developed in multiple FDC products: with a diuretic, a calcium channel blocker (amlodipine) and as a triple combination of all

three.

Our perindopril franchise will compete directly with FDCs containing an ACE inhibitor and secondarily with fixed-dose combinations containing an ARB or calcium channel blocker.

XOMA 3AB

We also are developing XOMA 3AB, a combination, or cocktail, of antibodies designed to neutralize the most potent of botulinum toxins. Other companies are developing other products targeting botulism poisoning, and these products may prove more effective than XOMA 3AB. We are aware:

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- Cangene Corporation has a contract with the U.S. Department of Health & Human Services, expected to be worth $423.0 million, to manufacture and supply an equine heptavalent botulism anti-toxin; and

- Emergent BioSolutions, Inc., is currently in development of a botulism immunoglobulin candidate that may compete with our anti-botulinum neurotoxin monoclonal antibodies.

Manufacturing risks and inefficiencies may affect adversely our ability to manufacture products for ourselves or others.

To the extent we continue to provide manufacturing services for our own benefit or to third parties, we are subject to manufacturing risks. Additionally, unanticipated fluctuations in customer requirements have led and may continue to lead to manufacturing inefficiencies, which if significant could lead to an impairment on our long-lived assets or restructuring activities. We must utilize our manufacturing operations in compliance with regulatory requirements, in sufficient quantities and on a timely basis, while maintaining acceptable product quality and manufacturing costs. Additional resources and changes in our manufacturing processes may be required for each new product, product modification or customer or to meet changing regulatory or third-party requirements, and this work may not be completed successfully or efficiently.

Manufacturing and quality problems may arise in the future to the extent we continue to perform these manufacturing activities for our own benefit or for third parties. Consequently, our development goals or milestones may not be achieved in a timely manner or at a commercially reasonable cost, or at all. In addition, to the extent we continue to make investments to improve our manufacturing operations, our efforts may not yield the improvements that we expect.

Failure of our products to meet current Good Manufacturing Practices standards may subject us to delays in regulatory approval and penalties for noncompliance.

Our contract manufacturers are required to produce ACEON and our clinical product candidates under current Good Manufacturing Practices (“cGMP”) to meet acceptable standards for use in our clinical trials and for commercial sale, as applicable. If such standards change, the ability of contract manufacturers to produce our product candidates and ACEON on the schedule we require for our clinical trials or to meet commercial requirements may be affected. In addition, contract manufacturers may not perform their obligations under their agreements with us or may discontinue their business before the time required by us to successfully produce clinical and commercial supplies of our product candidates and ACEON.

We and our contract manufacturers are subject to pre-approval inspections and periodic unannounced inspections by the FDA and corresponding state and foreign authorities to ensure strict compliance with cGMP and other applicable government regulations and corresponding foreign standards. We do not have control over a third-party manufacturer’s compliance with these regulations and standards. Any difficulties or delays in our contractors’ manufacturing and supply of our product candidates and ACEON or any failure of our contractors to maintain compliance with the applicable regulations and standards could increase our costs, cause us to lose revenue, make us postpone or cancel clinical trials, prevent or delay regulatory approval by the FDA and corresponding state and foreign authorities, prevent the import and/or export of our product candidates and ACEON, or cause any of our product candidates that may be approved for commercial sale and ACEON to be recalled or withdrawn.

Because many of the companies with which we do business also are in the biotechnology sector, the volatility of that sector can affect us indirectly as well as directly.

As a biotechnology company that collaborates with other biotechnology companies, the same factors that affect us directly also can adversely impact us indirectly by affecting the ability of our collaborators, partners and others with which we do business to meet their obligations to us and reduce our ability to realize the value of the consideration provided to us by these other companies.

For example, in connection with our licensing transactions relating to our bacterial cell expression technology, we have in the past and may in the future agree to accept equity securities of the licensee in payment of license fees. The future value of these or any other shares we receive is subject both to market risks affecting our ability to realize the value of these shares and more generally to the business and other risks to which the issuer of these shares may be subject.

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As we do more business internationally, we will be subject to additional political, economic and regulatory uncertainties.

We may not be able to operate successfully in any foreign market. We believe that because the pharmaceutical industry is global in nature, international activities will be a significant part of our future business activities and when and if we are able to generate income, a substantial portion of that income will be derived from product sales and other activities outside the United States. Foreign regulatory agencies often establish standards different from those in the United States, and an inability to obtain foreign regulatory approvals on a timely basis could put us at a competitive disadvantage or make it uneconomical to proceed with a product or product candidate's development. International operations and sales may be limited or disrupted by:

- imposition of government controls;
- export license requirements;
- political or economic instability;
- trade restrictions;
- changes in tariffs;
- restrictions on repatriating profits;
- exchange rate fluctuations;
- withholding and other taxation; and
- difficulties in staffing and managing international operations.

We are subject to foreign currency exchange rate risks.

We are subject to foreign currency exchange rate risks because substantially all of our revenues and operating expenses are paid in U.S. Dollars, but we pay interest and principal obligations with respect to our loan from Servier in Euros. To the extent the U.S. Dollar declines in value against the Euro, the effective cost of servicing our Euro-denominated debt will be higher. Changes in the exchange rate result in foreign currency gains or losses. Although we have managed some of our exposure to changes in foreign currency exchange rates by entering into foreign exchange option contracts, there can be no assurance foreign currency fluctuations will not have a material adverse effect on our business, financial condition, liquidity or results of operations. In addition, our foreign exchange option contracts are re-valued at each financial reporting period, which also may result in gains or losses from time to time.

If we and our partners are unable to protect our intellectual property, in particular our patent protection for our principal products, product candidates and processes, and prevent its use by third parties, our ability to compete in the market will be harmed, and we may not realize our profit potential.

We rely on patent protection, as well as a combination of copyright, trade secret, and trademark laws to protect our proprietary technology and prevent others from duplicating our products or product candidates. However, these means may afford only limited protection and may not:

- prevent our competitors from duplicating our products;
- prevent our competitors from gaining access to our proprietary information and technology; or
- permit us to gain or maintain a competitive advantage.

Because of the length of time and the expense associated with bringing new products to the marketplace, we and our collaboration and development partners hold and are in the process of applying for a number of patents in the United States and abroad to protect our product candidates and important processes and also have obtained or have the right to obtain exclusive licenses to certain patents and applications filed by others. However, the mere issuance of a patent

is not conclusive as to its validity or its enforceability. The U.S. Federal Courts or equivalent national courts or patent offices elsewhere may invalidate our patents or find them unenforceable. In addition, the laws of foreign countries may not protect our intellectual property rights effectively or to the same extent as the laws of the United States. If our intellectual property rights are not protected adequately, we may not be able to commercialize our technologies, products, or services, and our competitors could commercialize our technologies, which could result in a decrease in our sales and market share that would harm our business and operating results. Specifically, the patent position of biotechnology companies generally is highly uncertain and involves complex legal and factual questions. The legal standards governing the validity of biotechnology patents are in transition, and current defenses as to issued biotechnology patents may not be adequate in the future. Accordingly, there is uncertainty as to:

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- whether any pending or future patent applications held by us will result in an issued patent, or that if patents are issued to us, that such patents will provide meaningful protection against competitors or competitive technologies;
- whether competitors will be able to design around our patents or develop and obtain patent protection for technologies, designs or methods that are more effective than those covered by our patents and patent applications; or
- the extent to which our product candidates could infringe on the intellectual property rights of others, which may lead to costly litigation, result in the payment of substantial damages or royalties, and/or prevent us from using technology that is essential to our business.

We have established a portfolio of patents, both United States and foreign, related to our bacterial cell expression technology, including claims to novel promoter sequences, secretion signal sequences, compositions and methods for expression and secretion of recombinant proteins from bacteria, including immunoglobulin gene products. Most of the more important European patents in our bacterial cell expression patent portfolio expired in July 2008 or earlier.

If certain patents issued to others are upheld or if certain patent applications filed by others issue and are upheld, we may require licenses from others to develop and commercialize certain potential products incorporating our technology or we may become involved in litigation to determine the proprietary rights of others. These licenses, if required, may not be available on acceptable terms, and any such litigation may be costly and may have other adverse effects on our business, such as inhibiting our ability to compete in the marketplace and absorbing significant management time.

Due to the uncertainties regarding biotechnology patents, we also have relied and will continue to rely upon trade secrets, know-how and continuing technological advancement to develop and maintain our competitive position. All of our employees have signed confidentiality agreements under which they have agreed not to use or disclose any of our proprietary information. Research and development contracts and relationships between us and our scientific consultants and potential customers provide access to aspects of our know-how that are protected generally under confidentiality agreements. These confidentiality agreements may be breached or may not be enforced by a court. To the extent proprietary information is divulged to competitors or to the public generally, such disclosure may affect our ability to develop or commercialize our products adversely by giving others a competitive advantage or by undermining our patent position.

Litigation regarding intellectual property can be costly and expose us to risks of counterclaims against us.

We may be required to engage in litigation or other proceedings to protect our intellectual property. The cost to us of this litigation, even if resolved in our favor, could be substantial. Such litigation also could divert management’s attention and resources. In addition, if this litigation is resolved against us, our patents may be declared invalid, and we could be held liable for significant damages. In addition, we may be subject to a claim that we are infringing another party’s patent. If such claim is resolved against us, we or our collaborators may be enjoined from developing, manufacturing, selling or importing products, processes or services unless we obtain a license from the other party.

Such license may not be available on reasonable terms, thus preventing us from using these products, processes or services and adversely affecting our revenue.

We may be unable to price our products effectively or obtain adequate reimbursement for sales of our products, which would prevent our products from becoming profitable.

If we or our third-party collaborators or licensees succeed in bringing our product candidates to the market, they may not be considered cost effective, and reimbursement to the patient may not be available or may not be sufficient to allow us to sell our products on a competitive basis. In both the United States and elsewhere, sales of medical products

and treatments are dependent, in part, on the availability of reimbursement to the patient from third-party payors, such as government and private insurance plans. Third-party payors are increasingly challenging the prices charged for pharmaceutical products and services. Our business is affected by the efforts of government and third-party payors to contain or reduce the cost of healthcare through various means. In the United States, there have been and will continue to be a number of federal and state proposals to implement government controls on pricing.

In addition, the emphasis on managed care in the United States has increased and will continue to increase the pressure on the pricing of pharmaceutical products. We cannot predict whether any legislative or regulatory proposals will be adopted or the effect these proposals or managed care efforts may have on our business.

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Healthcare reform measures and other statutory or regulatory changes could adversely affect our business.

In both the United States and certain foreign jurisdictions, there have been a number of legislative and regulatory proposals to change the healthcare system in ways that could impact our business. In March 2010, the U.S. Congress enacted and President Obama signed into law the Patient Protection and Affordable Care Act, as amended by the Health Care and Education Affordability Reconciliation Act (collectively, "PPACA"), which includes a number of healthcare reform provisions. The reforms imposed by the law are expected to impact the pharmaceutical industry significantly, most likely in the area of pharmaceutical product pricing. While the law may increase the number of patients who have insurance coverage for our products or product candidates, its cost containment measures also could adversely affect reimbursement for our existing or potential products; however, the full effects of this law cannot be known until these provisions are implemented and the relevant Federal and state agencies issue applicable regulations or guidance.

The pharmaceutical and biotechnology industries are subject to extensive regulation, and from time to time, legislative bodies and governmental agencies consider changes to such regulations that could have significant impact on industry participants. For example, in light of certain highly publicized safety issues regarding certain drugs that had received marketing approval, the U.S. Congress has considered various proposals regarding drug safety, including some that would require additional safety studies and monitoring and could make drug development more costly. We are unable to predict what additional legislation or regulation, if any, relating to safety or other aspects of drug development may be enacted in the future or what effect such legislation or regulation would have on our business.

Beginning in 2013, the PPACA also imposes new reporting and disclosure requirements on pharmaceutical manufacturers for payments to healthcare providers and ownership of their stock by healthcare providers. Failure to submit required information may result in civil monetary penalties of up to an aggregate of $150,000 per year (or up to an aggregate of $1 million per year for "knowing failures"), for all payments, transfers of value or ownership or investment interests not reported in an annual submission. On December 14, 2011, CMS released its proposed rule implementing these provisions, providing further clarification to ambiguous or unclear statutory language and providing instructions for manufacturers to comply with such requirements. CMS has not issued a final rule to date.

The business and financial condition of pharmaceutical and biotechnology companies also are affected by the efforts of governments, third-party payors and others to contain or reduce the costs of healthcare to consumers. In the United States and various foreign jurisdictions there have been, and we expect there will continue to be, a number of legislative and regulatory proposals aimed at changing the healthcare system, such as proposals relating to the reimportation of drugs into the United States from other countries (where they are then sold at a lower price) and government control of prescription drug pricing. We expect current health care reform measures, such as PPACA, and those that may be adopted in the future could result in a decrease in the share price of our common stock, limit our ability to raise capital or to obtain strategic collaborations or licenses or successfully commercialize our products.

We are exposed to an increased risk of product liability claims, and a series of related cases is currently pending against us.

The testing, marketing and sales of medical products entails an inherent risk of allegations of product liability. We have been party to a number of product liability claims filed against Genentech Inc., and even though Genentech has agreed to indemnify us in connection with these matters, there can be no assurance these or other products liability lawsuits will not result in liability to us or that our insurance or contractual arrangements will provide us with adequate protection against such liabilities. In the event of one or more large, unforeseen awards of damages against us, our product liability insurance may not provide adequate coverage. A significant product liability claim for which we were not covered by insurance or indemnified by a third party would have to be paid from cash or other assets, which could have an adverse effect on our business and the value of our common stock. To the extent we have

sufficient insurance coverage, such a claim would result in higher subsequent insurance rates. In addition, product liability claims can have various other ramifications, including loss of future sales opportunities, increased costs associated with replacing products, a negative impact on our goodwill and reputation, and divert our management's attention from our business, each of which could also adversely affect our business and operating results.

The loss of key personnel, including our Chief Executive Officer, could delay or prevent achieving our objectives.

Our research, product development and business efforts could be affected adversely by the loss of one or more key members of our scientific or management staff, particularly our executive officers: John Varian, our Chief Executive Officer; Patrick J. Scannon, M.D., Ph.D., our Executive Vice President and Chief Scientific Officer; Fred Kurland, our Vice President, Finance, Chief Financial Officer and Secretary; and Paul D. Rubin, M.D., our Senior Vice President, Research and Development and Chief Medical Officer. We currently do not have key person insurance on any of our employees.

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Our ability to use our net operating loss carry-forwards and other tax attributes will be substantially limited by Section 382 of the U.S. Internal Revenue Code.

Section 382 of the U.S. Internal Revenue Code of 1986, as amended, generally limits the ability of a corporation that undergoes an "ownership change" to utilize its net operating loss carry-forwards ("NOLs") and certain other tax attributes against any taxable income in taxable periods after the ownership change. The amount of taxable income in each taxable year after the ownership change that may be offset by pre-change NOLs and certain other pre-change tax attributes is generally equal to the product of (a) the fair market value of the corporation's outstanding shares (or, in the case of a foreign corporation, the fair market value of items treated as connected with the conduct of a trade or business in the United States) immediately prior to the ownership change and (b) the long-term tax exempt rate (i.e., a rate of interest established by the U.S. Internal Revenue Service ("IRS") that fluctuates from month to month). In general, an "ownership change" occurs whenever the percentage of the shares of a corporation owned, directly or indirectly, by "5-percent shareholders" (within the meaning of Section 382 of the Internal Revenue Code) increases by more than 50 percentage points over the lowest percentage of the shares of such corporation owned, directly or indirectly, by such "5-percent shareholders" at any time over the preceding three years.

Based on an analysis under Section 382 of the Internal Revenue Code (which subjects the amount of pre-change NOLs and certain other pre-change tax attributes that can be utilized to an annual limitation), the Company experienced ownership changes in 2009 and 2012 which substantially limit the future use of our pre-change NOLs and certain other pre-change tax attributes per year. As of March 31, 2013, the Company has excluded the NOLs and R&D credits that will expire as a result of the annual limitations. To the extent that the Company does not utilize its carry-forwards within the applicable statutory carry-forward periods, either because of Section 382 limitations or the lack of sufficient taxable income, the carry-forwards will also expire unused.

We may not realize the expected benefits of our initiatives to reduce costs across our operations, and we may incur significant charges or write-downs as part of these efforts.

We have pursued and may continue to pursue a number of initiatives to reduce costs of our operations. In January 2012, we implemented a workforce reduction of approximately 34% to improve our cost structure. This workforce reduction resulted primarily from our decisions to utilize a contract manufacturing organization for Phase 3 and commercial antibody production and to eliminate internal research functions that are non-differentiating or that can be obtained cost effectively by contract service providers.

We may not realize some or all of the expected benefits of our current and future initiatives to reduce costs. In addition to restructuring or other charges, we may experience disruptions in our operations as a result of these initiatives.

Because we are a relatively small biopharmaceutical company with limited resources, we may not be able to attract and retain qualified personnel.*

Our success in developing marketable products and achieving a competitive position will depend, in part, on our ability to attract and retain qualified scientific and management personnel, particularly in areas requiring specific technical, scientific or medical expertise. We had approximately 167 employees as of May 6, 2013. We may require additional experienced executive, accounting, research and development, legal, administrative and other personnel from time to time in the future. There is intense competition for the services of these personnel, especially in California. Moreover, we expect that the high cost of living in the San Francisco Bay Area, where our headquarters and manufacturing facilities are located, may impair our ability to attract and retain employees in the future. If we do not succeed in attracting new personnel and retaining and motivating existing personnel, our operations may suffer and we may be unable to implement our current initiatives or grow effectively.

Global credit and financial market conditions may reduce our ability to access and maintain capital for our operations.

Traditionally, we have funded a large portion of our research and development expenditures through raising capital in the equity markets. Recent events, including failures and bankruptcies among large commercial and investment banks, have led to considerable declines and uncertainties in these and other capital markets and have led to new regulatory and other restrictions that may have broad effect on the nature of these markets. These circumstances could severely restrict the ability to raise new capital by companies such as us in the future.

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Volatility in the financial markets also has created liquidity problems in investments previously thought to bear a minimal risk. For example, money market fund investors, including us, have in the past been unable to retrieve the full amount of funds, even in highly rated liquid money market accounts, upon maturity. Although as of March 31, 2013, we have received the full amount of proceeds from money market fund investments, an inability to retrieve funds from money market fund investments as they mature in the future could have a material and adverse impact on our business, results of operations and cash flows.

Our cash and cash equivalents are maintained in highly liquid investments with remaining maturities of 90 days or less at the time of purchase. While we are not aware of any downgrades, material losses, or other significant deterioration in the fair value of our cash equivalents since March 31, 2013, no assurance can be given that further deterioration in conditions of the global credit and financial markets would not impact our current portfolio of cash equivalents negatively or our ability to meet our financing objectives.

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

Despite the implementation of security measures, our internal computer systems and those of our current and any future collaborators, licensees, suppliers, contractors and consultants are vulnerable to damage from cyber–attacks, computer viruses, unauthorized access, natural disasters, terrorism, war and telecommunication and electrical failures. We could experience failures in our information systems and computer servers, which could be the result of a cyber–attack and could result in an interruption of our normal business operations and require substantial expenditure of financial and administrative resources to remedy. System failures, accidents or security breaches can cause interruptions in our operations and can result in a material disruption of our development programs, commercialization activities and other business operations. The loss of clinical trial data from completed or future clinical trials could result in delays in our regulatory approval efforts and significantly increase our costs to recover or reproduce the data. Similarly, we rely on third parties to supply components for and manufacture our product and product candidates, conduct clinical trials of our product candidates and warehouse and distribute ACEON, and similar events relating to their computer systems could also have a material adverse effect on our business. To the extent that any disruption or security breach were to result in a loss of, or damage to, our data or applications, or inappropriate disclosure of confidential or proprietary information, we could incur liability and the development of gevokizumab, FDC1 or any of our other product candidates and the commercialization of ACEON could be delayed or otherwise adversely affected.

Calamities, power shortages or power interruptions at our Berkeley headquarters and manufacturing facility could disrupt our business and adversely affect our operations.

Our principal operations are located in Northern California, including our corporate headquarters and manufacturing facility in Berkeley, California. This location is in an area of seismic activity near active earthquake faults. Any earthquake, terrorist attack, fire, power shortage or other calamity affecting our facilities may disrupt our business and could have material adverse effect on our business and results of operations.

We have a significant stockholder, which may limit other stockholders' ability to influence corporate matters and may give rise to conflicts of interest.*

Entities controlled by Felix J. Baker and Julian C. Baker beneficially own approximately 30.8% of our outstanding common stock as of May 6, 2013, which includes warrants to purchase approximately 7.6 million shares of XOMA's common stock at an exercise price of $1.76 per share. On July 19, 2012, our Board of Directors elected Kelvin Neu, M.D., to serve on our Board of Directors. Dr. Neu is a Managing Director at Baker Bros. Advisors, LLC, an entity controlled by Felix J. Baker and Julian C. Baker. Accordingly, these entities may exert significant influence over us and any action requiring the approval of the holders of our stock, including the election of directors and approval of

significant corporate transactions. Furthermore, conflicts of interest could arise in the future between us, on the one hand, and these entities, on the other hand, concerning potential competitive business activities, business opportunities, the issuance of additional securities and other matters.

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Our organizational documents contain provisions that may prevent transactions that could be beneficial to our stockholders and may insulate our management from removal.

Our charter and by-laws:

- require certain procedures to be followed and time periods to be met for any stockholder to propose matters to be considered at annual meetings of stockholders, including nominating directors for election at those meetings; and
- authorize our Board of Directors to issue up to 1,000,000 shares of preferred stock without stockholder approval and to set the rights, preferences and other designations, including voting rights, of those shares as the Board of Directors may determine.

In addition, we are subject to the provisions of Section 203 of the Delaware General Corporation Law (the "DGCL"), that may prohibit large stockholders, in particular those owning 15% or more of our outstanding common stock, from merging or combining with us.

These provisions of our organizational documents and the DGCL, alone or in combination with each other, may discourage transactions involving actual or potential changes of control, including transactions that otherwise could involve payment of a premium over prevailing market prices to holders of common stock, could limit the ability of stockholders to approve transactions that they may deem to be in their best interests, and could make it considerably more difficult for a potential acquirer to replace management.

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

None.

ITEM 3. DEFAULTS UPON SENIOR SECURITIES

None.

ITEM 4. MINE SAFETY DISCLOSURES

Not applicable.

ITEM 5. OTHER INFORMATION

On May 8, 2013, the Company issued a press release announcing the Company's financial results for the first quarter ended March 31, 2013. A copy of the press release is furnished as Exhibit 99.1 to this report.

ITEM 6. EXHIBITS

See Index to Exhibits at the end of this Report, which is incorporated by reference here. The Exhibits listed in the accompanying Index to Exhibits are filed as part of this report.

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SIGNATURES

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

XOMA Corporation

Date: May 8, 2013	By:	/s/ JOHN VARIAN John Varian Chief Executive Officer (principal executive officer) and Director
Date: May 8, 2013	By:	/s/ FRED KURLAND Fred Kurland Vice President, Finance, Chief Financial Officer and Secretary (principal financial and principal accounting officer)

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EXHIBIT INDEX

Exhibit Number	Exhibit Description	Incorporation By Reference Form	SEC File No.	Exhibit	Filing Date
3.1	Certificate of Incorporation of XOMA Corporation	8-K	000-14710	3.1	01/03/2012
3.2	Certificate of Amendment of Certificate of Incorporation of XOMA Corporation	8-K	000-14710	3.1	05/31/2012
3.3	By-laws of XOMA Corporation	8-K	000-14710	3.2	01/03/2012
4.1	Reference is made to Exhibits 3.1, 3.2 and 3.3				
4.2	Specimen of Common Stock Certificate	8-K	000-14710	4.1	01/03/2012
4.3	Form of Certificate of Designations of Series A Preferred Stock	8-K	000-14710	3.1	01/03/2012
4.4	Form of Amended and Restated Warrant (June 2009 Warrants)	8-K	000-14710	10.6	02/02/2010
4.5	Form of Warrant (February 2010 Warrants)	8-K	000-14710	10.2	02/02/2010
4.6	Form of Warrant (December 2011 Warrants)	10-K	000-14710	4.9	03/14/2012
4.7	Form of Warrant (March 2012 Warrants)	8-K	000-14710	4.1	03/07/2012
4.8	Form of Warrant (September 2012 Warrants)	8-K	000-14710	4.10	10/03/2012
10.1+	Officer Employment Agreement by and between XOMA Corporation and Thomas Klein dated March 18, 2013				
31.1+	Certification of Chief Executive Officer, as required by Rule 13a-14(a) or Rule 15d-14(a)				
31.2+	Certification of Chief Financial Officer, as required by Rule 13a-14(a) or Rule 15d-14(a)				
32.1+	Certification of Chief Executive Officer and Chief Financial Officer, as required by Rule 13a-14(b) or Rule 15d-14(b) and Section 1350 of Chapter 63 of Title 18 of the United States Code (18 U.S.C. §1350)(1)				
99.1+	Press Release dated May 8, 2013				

101.INS+	XBRL Instance Document(2)
101.SCH+	XBRL Taxonomy Extension Schema Document(2)
101.CAL+	XBRL Taxonomy Extension Calculation Linkbase Document(2)
101.DEF+	XBRL Taxonomy Extension Definition Linkbase Document(2)

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Exhibit Number	Exhibit Description	Incorporation By Reference Form	SEC File No.	Exhibit	Filing Date
101.LAB+	XBRL Taxonomy Extension Labels Linkbase Document(2)				
101.PRE+	XBRL Taxonomy Extension Presentation Linkbase Document(2)				

+ Filed herewith

(1) This certification accompanies the Form 10-Q to which it relates, is not deemed filed with the Securities and Exchange Commission and is not to be incorporated by reference into any filing of the Registrant under the Securities Act of 1933, as amended, or the Securities Exchange Act of 1934, as amended (whether made before or after the date of the Form 10-Q), irrespective of any general incorporation language contained in such filing.

(2) Pursuant to applicable securities laws and regulations, the Registrant is deemed to have complied with the reporting obligation relating to the submission of interactive data files in such exhibits and is not subject to liability under any anti-fraud provisions of the federal securities laws as long as the Registrant has made a good faith attempt to comply with the submission requirements and promptly amends the interactive data files after becoming aware that the interactive data files fail to comply with the submission requirements. These interactive data files are deemed not filed or part of a registration statement or prospectus for purposes of sections 11 or 12 of the Securities Act of 1933, as amended, are deemed not filed for purposes of section 18 of the Securities Exchange Act of 1934, as amended, and otherwise are not subject to liability under these sections.