

# PHARMING



Annual Report 2012

## PHARMING ANNUAL REPORT 2012

### 2012 highlights

#### Operational

- Successful completion of the Ruconest®<sup>1</sup> US Phase III pivotal study (Study 1310) followed by receipt of an associated US\$10 million milestone payment from our US partner Santarus.
- Ruconest® continues roll-out across Europe.
  - Roll-out progressing slower than expected as a result of challenging market access conditions in the EU during 2012.
  - To address these issues, our partner Sobi has recently re-aligned their commercial organisation and initiated specific in-market actions.
- First production validation runs completed and initiation of the certification process with the European Medicines Agency (EMA) and Food and Drug Authority (FDA) for the second downstream manufacturing site for the production process of Ruconest®, which will enable significant future reductions in the cost of manufacturing.
- Restructuring to reduce cash-burn initiated in the second half of 2012. Closing and sale of the US facility and the downsizing of the Netherlands organization. The latter is expected to be completed in the first half of 2013.
- Expansion of the geographical coverage for Ruconest® through new agreements with Singapore based Transmedic Pte for Brunei, Indonesia, Malaysia, Philippines, Singapore, as well as Thailand and Seoul based Hypjin Corp for South Korea.
- New data showing that Ruconest® was not observed to have a prothrombotic effect when used to treat acute hereditary angioedema (HAE) attacks. Data derived from a study by Relan et al, published in the peer-reviewed journal Biodrugs (competitive drugs have shown to be prothrombotic).
- Initiated an open-label Phase II clinical study evaluating Ruconest® for the treatment of acute attacks of angioedema in paediatric patients with HAE.
- Data published showing that Ruconest® has been shown to have a protective effect in a preclinical animal model of severe blood loss designed to simulate battlefield injuries.

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<sup>1</sup> Ruconest®, Pharming's recombinant human C1 esterase inhibitor (rhC1INH), previously named Rhucin®, has been developed and European Medicines Agency (EMA) approved for the treatment of acute attacks of HAE.

## Financial

- Revenues and other income from continuing operations increased to €10.9 million (2011: €3.2 million).
- Operating costs from continuing operations excluding cost of sales and inventory impairments increased to €24.1 million (2011: €18.2 million).
- Inventory impairments increased to €3.1 million in 2012 from €1.7 million in 2011.
- Net loss from continuing operations increased to €24.1 million (2011: €17.8 million).
- Raised €13.3 million gross new funds (net €12.4 million, 2011: net €11.6 million).
  - €8.0 million convertible bond (net €7.5 million).
  - €4.9 million Equity Working Capital Facility (net €4.5 million).
  - €0.4 million issue of warrants (net €0.4 million).
- Year-end cash and cash equivalents (including restricted cash) of €6.3 million (2011: €5.1 million).

## About Pharming Group N.V.

Pharming Group N.V. is developing innovative products for the treatment of unmet medical needs. RUCONEST® is a recombinant human C1 inhibitor approved for the treatment of angioedema attacks in patients with HAE in all 27 EU countries plus Norway, Iceland and Liechtenstein, and is distributed in the EU by Swedish Orphan Biovitrum (SOBI). RUCONEST® is partnered with Santarus Inc (NASDAQ: SNTS) in North America where the drug has completed Phase III clinical development. The product is also being evaluated for various follow-on indications. Pharming has a unique GMP compliant, validated rabbit platform for the production of recombinant human proteins that, with the EU approval of RUCONEST®, has proven capable of producing industrial volumes of high quality recombinant human protein in a significantly more economical way through low upfront capital investment and manufacturing costs, compared to current cell based technologies. Pharming plans to utilise this platform for the development of rhFVIII for the treatment of Haemophilia A.

Pharming shares are listed at the NYSE/ Euronext Amsterdam (PHARM). Additional information is available on the Pharming website, [www.pharming.com](http://www.pharming.com).

## **Strategic focus**

### **Pharming's strategic focus is aimed at:**

- Generating value from its lead product Ruconest® for HAE attacks, through:
  - filing the Biological License Application (BLA) in the US in order to initiate the US regulatory approval process for Ruconest®;
  - completing the US regulatory process following BLA filing;
  - preparing for the US commercial launch;
  - generating sales in the other countries covered by our commercial partners; and
  - broadening the application of Ruconest® to other indications in order to grow the potential market for the product.
- Further validating and leveraging the inherent value of its transgenic technology platform, and pro-actively evaluating external opportunities.
- Establishing (international) collaborations with leading academic and research institutions to continue to position Pharming at the forefront of innovative science.

### **Pharming is committed to:**

- Fostering an entrepreneurial culture through appropriate recognition and efficient management of opportunities and risks.
- Communicating in a timely, transparent and consistent manner to all internal and external stakeholders.
- Maintaining a high level of social and corporate responsibility. We operate to high ethical, environmental and animal welfare standards.

## CEO's statement

2012 was another challenging and volatile year for Pharming, largely due to an unforeseen delay in Study 1310 which negatively impacted on our financing. This was shortly followed by the arrangement of an Equity Working Capital Facility for financing and the successful completion of Study 1310, which triggered the payment of the associated US\$10 million milestone by our US partner Santarus, which in turn provided the platform for the January 2013 €16.35 million financing by means of a short term convertible bond and hence a strong ending to the year.

In sharp contrast to some months ago, Pharming is now well prepared and funded to enter the US regulatory review process for the treatment of acute HAE with Ruconest®, which will be a major milestone and thus a trigger for value creation.

In addition, during 2012 we also entered into a strategic review from which it was clear that in order to transform into a profitable company, a more focused and lean organisation had to be urgently created. Although this required difficult decisions impacting on staff, the expected revenues from Ruconest® and the opportunity therefore to be able to extend the exploitation of the transgenic rabbit platform with new partnered product development, made this an urgent requirement. This was subsequently implemented by closing down our US research facilities and the halting of legacy projects and triggered a significant downsizing of both our US and Dutch operations.

Ruconest® is commercialised in Europe, the Balkans, North Africa and the Middle East by our partner, Stockholm based Swedish Orphan Biovitrum International AB (Sobi). The roll out of Ruconest® is progressing slower than anticipated. So far approximately 200 patients have switched to Ruconest®. Sobi have, however, recently re-aligned their commercial organisation and have initiated in-market actions that will lead to acceleration in the acceptance of Ruconest® in the key EU markets during the course of 2013. In addition, (and this is a challenge faced by the entire industry and is not unique to Pharming), the roll-out continues to be hindered by the complex and protracted processes of obtaining national, regional and local market access in all of the EU territories. Nonetheless, Pharming and Sobi anticipate that Ruconest® will be used in all of the major European markets during the course of 2013.

During the early part of 2012, we expanded Ruconest®'s availability to HAE patients in additional territories through a distribution agreement for Brunei, Indonesia, Malaysia, Philippines, Singapore, and Thailand with Singapore based Transmedic Pte, signed in February 2012 and a distribution agreement for the Republic of Korea with Seoul based Hyupjin Corporation, signed in March 2012. Ruconest® is under regulatory review in all these territories.

With regard to the US regulatory approval process, during 2012, we successfully completed the US pivotal Phase III study (Study 1310) that was executed under the Special Protocol Assessment (SPA) process with the FDA.

Whilst first and foremost the focus of Ruconest® development remains on obtaining the US approval for the treatment of acute attacks of HAE, during 2012 we have also been working with thought leaders to understand the potential for the use of C1 inhibitors in HAE prophylaxis. First, we published positive results from Ruconest® open label Phase II trial for HAE prophylaxis in the November 2012 issue of the international peer-reviewed journal, *Allergy*. We have also reviewed the results of various acute and prophylaxis trials of a number of plasma derived C1 inhibitors and concluded that the now decades old paradigm of plasma half-life appears not to be consistent with various (objective) clinical results in both the Ruconest® and plasma derived C1 inhibitor trials. On the basis of the clinical prophylaxis results with Ruconest® and this research we are therefore now preparing to, together with our partner Santarus, further explore the regulatory pathway towards obtaining marketing authorisation for the prophylaxis of HAE as soon as we have the BLA accepted for review with the FDA.

In addition to this work in HAE, during 2013 our partner Santarus intends to initiate clinical research with Ruconest® for the treatment of acute pancreatitis, a large opportunity that leverages Pharming's ability to easily scale up manufacturing, something that is extremely difficult to achieve with plasma-derived products.

**CEO's statement continued**



With regard to leveraging the rabbit transgenic platform, we continued the pilot project with Renova Life Inc (RLI), a biotechnology company based in Maryland, USA. In addition we engaged potential partners in ongoing discussions to set-up new collaborative product development initiatives to develop new recombinant products, including human Factor VIII transgenic rabbits.

The production of validation runs needed for the certification of a second downstream manufacturing site for the production of Ruconest® proceeded and we are on track to receive approval for the up-scaled production process in Europe during the first half of 2013, which will enable significant future reductions in the cost of manufacturing.

Having successfully overcome the deeply challenging issues of 2012, executing on the downsizing of our cost base, and with secure funding throughout the expected US regulatory process which we will be managing closely together with our US partner Santarus, we can now look towards achieving yet another step forwards on our transition from a late-stage development company to an emerging pharmaceutical business, which will

be driven first and foremost by achieving US marketing approval for Ruconest®.

Reflecting on the past year's challenges, particularly the regrettable but unavoidable downsizing which led to the departure of more than a few highly professional and dedicated colleagues, I would like to acknowledge their achievements and the roles that they have played in Pharming's development to date.

I would like to thank all of our employees, investors and partners for their ongoing commitment and support in the continuing transition of Pharming.

Sijmen de Vries

Leiden  
The Netherlands  
29 March 2013

## Management report

### OPERATING REVIEW

The successful completion of the US pivotal Phase III study (Study 1310) in November 2012 represented a major achievement for Pharming, particularly in light of the unforeseen delay in the study, which we announced earlier in the year. The successful completion of the study resulted in a US\$10 million milestone from US partner Santarus and it put us on track to reach the fast growing US HAE market. This market has grown from being virtually non-existent prior to 2008 to more than US\$ 500 million to date, of which more than US\$150 million is accounted for by the acute treatment segment. We firmly believe that entry into the US market, which is also associated with a US\$20 million milestone payment from Santarus will accelerate our transition from a development focused company to a commercially driven organisation. It will also allow us to further broaden the application of Ruconest® and to progress other pipeline projects. The announcement of the collaboration with Renova Life to initiate a Factor VIII feasibility study represented a next step for such new projects and we are actively discussing possible risk and reward sharing structures with potential partners.

The commercialisation of Ruconest® by Sobi in the EU continues to progress; although gaining market access is taking longer than we initially envisaged, primarily as a result of reimbursement negotiations at the national, regional and local level. Pharming remains fully confident in the ability of all of our partners to successfully commercialise Ruconest® across global territories. However, Pharming depends on its commercial partners to market its product in the various territories. Pharming is also indirectly exposed to the risks of its chosen partners. We continue to believe that Ruconest® is a valuable addition to the therapeutic options available to HAE patients and we continue to support our commercialisation partners in their endeavours.

During 2012 our stock price suffered as a result of the additional funding we needed to raise, under difficult stock market circumstances, following the unforeseen delay in Study 1310. However, we have been fortunate in that, during 2012, we continued to attract investors who recognise the potential of Pharming's platform and have been willing to finance Pharming's key development programmes, thereby providing the funds that were required to enable the read out of our US clinical study. This trial was required for the regulatory submission in the US and importantly, is associated with two milestones worth a combined US\$15 million from our US partner, Santarus, of which we received US\$10 million in November 2012. This trial has been agreed by a Special Protocol Assessment (SPA) procedure, whereby the FDA has agreed that the design of the trial, including patient numbers and primary and secondary endpoints are adequate to support licensure of the product Ruconest®.

We have made further progress in achieving our aim of extending the geographical reach of Ruconest®. Early in 2012, distribution agreements were signed with Transmedic Pte. for the markets of Brunei, Indonesia, Malaysia, Philippines, Singapore, and Thailand and Hyupjin Corporation to cover the Republic of Korea.

During 2012, Pharming continued to focus the majority of its resources on Ruconest®, whilst investment in other projects was minimised; mainly aiming at completion of ongoing experiments. The emphasis on cost containment continued and a new more commercially focused pipeline prioritisation process was put in place to evaluate potential new projects.

## ***Management report continued***

### **Operating developments during 2012**

- Successful completion of the Ruconest® US Phase III pivotal study (Study 1310) followed by receipt of an associated US\$10.0 million milestone payment from our US partner Santarus.
- Ruconest® continues roll-out across Europe.
  - Roll-out progressing slower than expected as a result of challenging market access conditions in the EU during 2012.
  - To address these issues, our partner Sobi has recently re-aligned their commercial organization and initiated specific in-market actions.
- First production validation runs completed and initiation of the certification process with the European Medicines Agency (EMA) and Food and Drug Authority (FDA) for new downstream manufacturing site for Ruconest®, which will enable significant future reductions in the cost of manufacturing.
- Restructuring to reduce cash-burn initiated in the second half of 2012; sale of the US facility and the downsizing of the Netherlands organization. The latter is expected to be completed in the first half of 2013.
- New positive data published showing that Ruconest® was not observed to have a prothrombotic effect when used to treat acute HAE attacks.
  - Study published by Relan et al in the peer-reviewed journal Biodrugs.
  - Competitive drugs have shown to be prothrombotic.
- Expansion of the geographical coverage for Ruconest® through new agreements with Singapore based Transmedic Pte for Brunei, Indonesia, Malaysia, Philippines, Singapore, as well as Thailand and Seoul based Hypjin Corp for South Korea.
- Initiated an open-label Phase II clinical study evaluating Ruconest® for the treatment of acute attacks of angioedema in paediatric patients with HAE.
- Data published showing that Ruconest® has a protective effect in a preclinical animal model of severe blood loss designed to simulate battlefield injuries.



**Management report continued**

**Product commercialisation and pipeline**

	Indication	R&D	Pre Clinical	Phase I	Phase II	Phase III	Registration	Market	
<b>Ruconest®</b>									
Ruconest® (rhC1INH) (Europe)	Hereditary Angioedema								
Ruconest® (rhC1INH) (USA)	Hereditary Angioedema								
<b>New Projects</b>									
rhFactor VIII	Haemophilia A								

	Pre Clinical	Clinical (Phase II/III)	Registration	Market
<b>Ruconest® Additional Indications</b>				
Prophylaxis of Hereditary Angioedema				
Acute Pancreatitis				
Delayed Graft Function (Kidney)				
Other IRI Indications				

**Ruconest® for Hereditary Angioedema**

Ruconest® has been developed for the treatment of acute attacks of HAE. HAE is a rare genetic deficiency of C1 inhibitor activity resulting in recurrent attacks of local swelling (edema), which may present as abdominal pains, airway obstruction or swelling of the skin. These attacks are painful and disabling and attacks obstructing the airway can be fatal. Estimates of HAE prevalence vary between 1 in 10,000 and 1 in 50,000. Acute angioedema attacks often begin in childhood or adolescence, but due to the rarity of HAE, the disease is often not correctly diagnosed for many years. The frequency of HAE attacks varies between patients, from extreme cases with several attacks per week, to less severe cases with less than one attack per year, with an estimated average of eight treated attacks per year whilst using steroid prophylaxis. Swelling of the throat can have the most serious complications, since obstruction of the airway can be fatal. Abdominal attacks cause abdominal pain and vomiting, potentially leading to unnecessary surgery in undiagnosed patients, and swelling of the skin leads to disfigurement, disability and pain. Untreated, attacks can last between 48 and 120 hours. Additional information about the disease is available on the international patient association’s website, [www.haei.org](http://www.haei.org).

Administration of C1 inhibitor protein can stop these angioedema attacks. Ruconest® is a recombinant version of the human protein C1 inhibitor (C1INH) which demonstrates best-in-class efficacy (confirmed in Study 1310). It is produced through Pharming’s proprietary technology in milk of transgenic rabbits. Ruconest® offers higher purity and batch consistency compared to plasma derived C1 inhibitors and no risk of human virus transmission. The 50 U/kg dose studied and approved in the EU restores C1INH function to physiological levels and is a highly effective treatment of acute HAE attacks.

## **Management report continued**

### **Ruconest® in Europe**

In 2010 the European Commission granted Marketing Authorisation for the treatment of acute angioedema attacks under the name Ruconest®. Following an April 2010 agreement and an August 2011 extension of territories, Stockholm based Sobi obtained commercialisation rights for all of the EU territories and some North-African and Middle East territories. Under the agreement Sobi paid €8 million (2010) in milestones to Pharming.

- Sobi has continued its roll-out of Ruconest® and the drug is now available in the European territory. To date approximately 400-500 angioedema attacks have been treated with Ruconest® since the launch. It is important to remember that every patient can have several attacks per year. Market share for Ruconest® varies significantly between countries. The highest market share during 2012 was reached in Finland (15%) which is expected to grow to a 30% market share during 2013. We expect a continuous increase in patients using Ruconest® during 2013, especially in Central and Eastern European Countries, which will be made possible by the recently obtained pricing and market access approvals in some of these countries. The market access process continues across European markets using the various country specific procedures to obtain reimbursements and to make the product administratively available under the various national and regional healthcare systems.
- To accelerate acceptance of Ruconest® in the key EU markets during the course of 2013, Sobi have recently re-aligned their commercial organisation and have initiated specific in-market actions. After a slow 2012, we therefore now expect a continuous increase in patients using Ruconest® during 2013.

### **Ruconest® in the USA**

Following a September 2010 agreement, San Diego based Santarus Inc. (SNTS) obtained the commercialisation rights for North America (USA, Canada and Mexico). Under this agreement Santarus has to date paid US\$25 million (2010 and 2012) in milestones to Pharming.

In November 2012, Pharming successfully completed its US pivotal Phase III study (Study 1310) after a delay announced earlier in the year. The FDA had confirmed in August 2011 that the design, clinical endpoints and statistical analysis of the study are adequate to support a BLA filing for Ruconest® in HAE patients. Following discussions with the FDA in an SPA process, Pharming implemented the Agency's recommended changes to the study protocol, including modification of the primary endpoint and an increase in the number of patients to approximately 75. The protocol was also changed to allow the introduction of open-label doses of Ruconest® as a rescue medication. Headline results of the study in November 2012 confirmed the previous encouraging efficacy results and reconfirmed the clean safety profile of Ruconest®; clear immunogenicity results and no findings of any thromboembolic complications in now over 1,000 treatments.

Upon acceptance of the BLA, a further US\$5 million milestone will be payable by Santarus. Additionally, a \$20 million milestone will be payable by Santarus upon the earlier of first commercial sale of Ruconest in the US or 90 days following receipt of FDA approval.

In addition, Santarus will be required to pay one-time performance milestones if they achieve certain aggregate net sales levels of Ruconest.

Furthermore, as consideration for the licenses and rights granted under the license agreement, and as compensation for the commercial supply of Ruconest® Santarus will pay Pharming a tiered supply price based on a percentage of net sales of Ruconest, which starts at 30% of net sales, increasing to a maximum of 40% depending on the amount of net sales. The consideration is subject to reduction in certain events. Under the agreement, the Ruconest® BLA will be transferred to Santarus, no later than at US approval. Both parties also agreed to extend the partnership by exploring certain additional indications, as outlined below.

## ***Management report continued***

In sharp contrast to the EU market, during 2012, the US acute HAE market segment growth accelerated as a result of steady inflow of new patients and the Firazyr market entry late in 2011. Combined 2012 sales (acute HAE segment) grew 179% to US\$156 million (excluding non-reported Berinert sales).

### **Ruconest® commercialisation in other territories**

For the commercialisation of Ruconest®, in other territories as per the date of these financial statements, the Company has four additional commercial agreements in place (in chronological order):

- Istanbul based Eczasibasi Pharma: Turkey, under an agreement closed in April 2008. Ruconest® is under regulatory review in Turkey.
- Tel Aviv based Megapharm: Israel, under an agreement closed in 2011. Ruconest® is under regulatory review in Israel.
- Singapore based Transmedic Pte: Brunei, Indonesia, Malaysia, Philippines, Singapore, and Thailand: signed in February 2012. Ruconest® is under regulatory review in all territories.
- Seoul based Hypjin Corp: South Korea. Ruconest® is under regulatory review for South Korea.

Pharming believes that Ruconest® efficacy and safety profile gives the product a significant competitive advantage over competing treatments and, over time, will result in the product achieving significant market penetration in major global markets. We have partnered with commercially oriented companies that are committed to making Ruconest® a commercial success; in addition, this has brought significant cash milestones to Pharming which have contributed to financing the Company through difficult market conditions. Further potential payments are due upon attaining certain regulatory and commercial milestones in certain of these territories.

Throughout 2012, a number of peer reviewed scientific and academic publications on Ruconest® were published. These are summarized in appendix 1.

### **ADDITIONAL DEVELOPMENT OF RUCONEST®**

#### **HAE in children**

In February 2012, we announced that we had started an open-label Phase II clinical study evaluating the Ruconest® for the treatment of acute attacks of angioedema in paediatric patients with HAE.

The Ruconest® paediatric study has been agreed with the European Medicine Agency's (EMA) Paediatric Committee and will assess the pharmacokinetic, safety, and efficacy profiles of Ruconest® at a dose of 50 U/kg in paediatric HAE patients. The study will support a paediatric indication for the treatment of HAE attacks. Pharming expects to enrol approximately 20 patients, aged from 2 to 13 years. This study, if successful, will broaden the label for Ruconest® in Europe and also has the additional benefit of extending the regulatory exclusivity period, both of which are commercially important. Ruconest® has regulatory exclusivity in Europe until late 2025 and paediatric exclusivity will add another six months, extending the exclusivity period into 2026.

#### **Prophylaxis in HAE**

Ruconest® is currently being developed as treatment for acute HAE. In acute therapy, each individual attack is treated. In prophylaxis therapy, the patient receives the drug on a regular basis with the intention of preventing or reducing the frequency of attacks. In the USA, the market size of prophylactic therapy segment in HAE is significant. Viropharma's Cinryze is only approved for this indication. ViroPharma guided for net revenue from US Cinryze sales in 2013 to be US\$330-350 million.

## **Management report continued**

In November 2012 the encouraging results of our open label exploratory study (OPERA) were published on-line in the international peer reviewed journal *Allergy*, followed by the printed publication in the January 2013 volume.

Following this, together with our partner Santarus, we decided to seek regulatory guidance from the FDA to clarify a path towards obtaining a label for the prophylaxis of HAE.

### **Ischaemia Reperfusion Injury**

Ischaemia Reperfusion Injury (IRI) is a complication arising from lack of oxygen due to an interruption of the blood supply (ischaemia) resulting in tissue damage. This can occur in a transplanted organ, in the brain as a result of stroke, and in the heart in the case of myocardial infarction ('heart attack'). Ruconest® has shown in various pre-clinical models that it can limit the extent of the ischaemia reperfusion injury.

As announced in November 2011, the United States Patent and Trademark Office (USPTO) granted the Company US Patent 8,071,532, covering a method of preventing, reducing or treating IRI by administering Ruconest®. The broad claims in the patent provide protection until 2028. This is Pharming's first patent granted on IRI in the US, and represents a significant milestone in the continuing development of Ruconest® in additional indications associated with IRI such as Delayed Graft Function (DGF) after transplantation. DGF occurs when a lack of oxygen during transplant causes a delayed functioning of the transplanted organ, improper functioning in the longer term and, eventually, in the rejection of the transplanted organ.

As result of the pre-clinical results to date and the granting of the patent, we are evaluating the use of Ruconest® in IRI related indications, including DGF and Acute Myocardial Infarction (AMI). Those indications are commercially attractive markets that are associated with high unmet medical need. Lack of financial resources during 2012 precluded any other activities other than the already initiated pre-clinical activities for these indications.

### **Human lactoferrin, human fibrinogen, human collagen**

Following a strategic review we decided to: terminate the human collagen project; terminate the licensing agreement for human fibrinogen with GTC Biotherapeutics (an LFB Company); finish activities on human lactoferrin, such that the project could potentially be spun out; and abandon all cattle platform related activities. In the course of this we received (i) a consideration of US\$350,000 from GTC Biotherapeutics for the return of the fibrinogen license and transfer of the fibrinogen cattle and other project associated goods, know-how and intellectual property and (ii) a consideration of US\$950,000 for US (Wisconsin) based real estate (cattle research facility).

## **RESEARCH AND TECHNOLOGY**

Pharming is involved in the production, purification and formulation of recombinant protein products. The Company has a large portfolio of patents issued and pending, supporting these technologies and products.

### **Transgenic manufacturing technology**

Pharming's production platform is based on the expression of human proteins in the milk of transgenic mammals. This technology enables the development of complex therapeutic proteins in a cost effective manner.

Pharming develops purification processes to separate the specific human proteins from the other natural components in milk, thereby ensuring competitive yields of high quality and purity. These processes are subsequently transferred to Contract Manufacturing Organisations (CMOs) for large-scale production in accordance with Good Manufacturing Practices (GMP).

## ***Management report continued***

Pharming's production processes are GMP-compliant and have passed inspections by the relevant authorities. To meet sales expectations, Pharming has built up an adequate inventory of finished product and product intermediates and is in the process of scaling up its manufacturing capacity and qualifying a second supplier. During 2012, the first production validation runs were completed and initiation of the certification process with the European Medicines Agency (EMA) for the new downstream manufacturing site for Ruconest® was started, which will enable significant future reductions in the cost of manufacturing.

### **Expanding the pipeline beyond Ruconest®**

With validation secured from the approval of the first product from our transgenic platform, we will now seek to initiate new projects on this platform. Our transgenic platform remains the only technology that to date can deliver recombinant versions of certain complex human proteins in an economically viable way: this is a result of the low cost of capital investment required to start up a suitable founder herd and the fact that the herd is easily scalable. The validation provided by the EU approval of Ruconest® and its manufacture significantly reduces the regulatory risk associated with our transgenic platform.

In 2011, Pharming started a review process to define new projects for this platform. The emphasis of this review was to highlight indications that had a high unmet medical need, required therapeutic intervention using biologics and were assessed to be commercially attractive. The first indication that was reviewed was the production of rhFVIII for the treatment of Haemophilia A.

Haemophilia A is an X chromosome linked hereditary disorder caused by defects in the Factor VIII (FVIII) gene that lead to lower levels of the functional FVIII protein. Lack of functional FVIII diminishes the body's clotting ability, which in turn can lead to damaging or fatal bleeding episodes. The global recombinant human FVIII market was worth over US\$4 billion in 2011 with 90% of sales in the developed markets and very high unmet medical needs in the developing markets, such as China. In addition, only approximately 50% of the world-wide estimated haemophilia market can currently be supplied with appropriate FVIII therapy. Hence, there is still a high unmet medical need in this field and the recombinant human FVIII market is estimated to grow to US\$6.5 billion in 2020.

As the first step in assessing if Pharming can successfully develop such a therapeutic, it has signed a service agreement with Renova Life (RLI). The agreement covers the development and supply of founder transgenic rabbits from RLI to Pharming. The founder rabbits will enable Pharming to start the commercial production breeding process. During 2012 this project continued.

As the next step in this process, various discussions with potential development partners were initiated and continue to date, with a view to develop such future new compounds in a collaboration, rather than as a stand-alone organisation.

In addition, as a result and as part of such discussions, additional potential projects were identified where the transgenic rabbit platform could provide (cost) advantages over cell based production systems and/or where the rabbit based platform could provide opportunities for "fast-follower design-around" analogues of commercially attractive products.

## ***Management report continued***

### **FINANCIAL REVIEW 2012**

The financial objectives for 2012 were focussed on:

- Accessing capital to ensure that the Company had sufficient resources to continue to develop Ruconest® through the readout of Study 1310; and
- Reduction of the future cash burn through restructuring of the Company.

### **Key Financial developments in 2012**

- Revenues and other income from continuing operations increased to €10.9 million (2011: €3.2 million).
- Inventory impairments increased to €3.1 million in 2012 (2011: €1.7 million).
- Operating costs from continuing operations excluding cost of sales and inventory impairments increased to €24.1 million (2011: €18.2 million).
- Net loss from continuing operations increased to €24.1 million (2011: €17.8 million).
  - Included net loss from financial income and expenses of €6.6 million (2011: net profit €0.7 million).
- Raised €13.3 million gross new funds (net €12.4 million, 2011: net €11.6 million).
  - €8.0 million convertible bond (net €7.5 million).
  - €4.9 million Equity Working Capital Facility (net €4.5 million).
  - €0.4 million issue of warrants (net €0.4 million).
- Year-end cash and cash equivalents (including restricted cash) of €6.3 million (2011: €5.1 million).

### **GROSS PROFIT/(LOSS)**

Revenues and other income from continuing operations increased to €10.9 million, from €3.2 million in 2011. The increase mainly stems from the US\$10 million (€7.9 million) milestone from our US partner Santarus following the successful read-out of Study 1310. Other license fee income amounting to €1.9 million reflects the release of accrued deferred license revenues following receipt of in total €20 million upfront and milestone payments in 2010. The 2012 revenues from product supplies to Sobi amounted to €0.8 million (2011: €1.1 million). Cost of product sales in 2012 amounted to €1.1 million (2011: €1.8 million). In 2012 the Company incurred €3.1 million (2011: €1.7 million) of inventory impairments related to ageing of stocks of finished products while the 2011 impairment of €1.7 million followed a one-off production related issue. These inventories were the last remaining of the inventories that were produced ahead of the assumed 2007 EU launch of Ruconest®.

### **OPERATING COSTS**

Operating costs from continuing operations increased to €24.1 million from €18.2 million in 2011. The increase is mainly a result of the costs of Study 1310 and US regulatory costs compared to 2011, as well as impairment charges of €1.2 million following the disposal of the US cattle farm and a restructuring provision expense in relation to the Dutch and US operations of €1.4 million. General and administrative costs decreased to €3.1 million in 2012 from €3.3 million in 2011 and share-based compensation decreased to €0.4 million from €1.0 million in 2011.

## ***Management report continued***

### **FINANCE INCOME AND EXPENSES**

Net loss from financial income and expenses in 2012 amounted to €6.6 million compared to a net profit of €0.7 million in 2011. The 2012 financial expenses were mainly related to the 2012 bonds and comprised interest expenses of €2.4 million and an accounting expense of €2.8 million related to the repayment of the bonds in shares. In addition, following the sale of the US cattle facility, the historical foreign currency translation loss of €1.4 million was transferred from equity to the profit and loss account.

### **NET RESULT**

Net loss from continuing operations increased to €24.1 million (2011 €17.8 million). The overall net loss increased in 2012 to €24.1 million from 17.2 million in 2011. The net loss per share for 2012 amounted to €0.03 (2011: €0.04).

### **CASH FLOWS**

Net cash flows used in operating activities decreased to €10.3 million in 2012 from €16.9 million in 2011. The 2012 operational cash flow included €9.1 million of receipts from license partners, including the US\$10 million milestone from Santarus compared to €0.8 million of receipts of license partners in 2011. Net cash flows from investing activities amounted to €11.6 million in 2012 compared to €12.7 million in 2011.

Year-end cash and cash equivalents (including restricted cash) amounted to €6.3 million (2011: €5.1 million).

### **FINANCING**

In 2012, the Company had proceeds of €8.0 million from the issue of convertible bonds announced in December 2011. Furthermore in 2012, €5.3 million was received, related to the issue of equity and warrants.

### **EQUITY**

Since late 2011, the Company has a negative equity position. This has in itself no immediate impact on the execution of the Pharming's business plan, nor does it imply that the Company is legally required to issue new share capital. However, Pharming is continuously reviewing its financial and liquidity position and continues to work on improving its equity position by hitting (clinical) milestones and raising additional capital. It should be noted that the Company has a significant amount of deferred license fee income (2012: €15.4 million) regarding license fees received in 2010 that, under IFRS, will be recognized in the statement of income over the term of the license agreements involved.

### **OUTLOOK**

In order to strengthen its cash and equity positions, in January 2013, the Company entered into a convertible bond issue that will be amortized in seven equal monthly tranches, in shares or cash at the Company's discretion and implemented a 10:1 reverse share split, all of which were approved by the EGM on 28 February 2013.

The Company's focus will continue to be US regulatory approval process for Ruconest®. The successful readout of the study took place in 2012 and the study will be reported upon sometime during 2013. A pivotal event will be the submission of the BLA to the US FDA in the second quarter of 2013. Upon acceptance of the BLA, a further US\$5 million milestone will be payable by Santarus.

The Company continues to support its partners to market its products in the various territories in order to grow sales as it believes that Ruconest® is a valuable addition to the therapeutic options available to HAE patients.

## ***Management report continued***

Furthermore, Pharming anticipates completion the restructuring in the first half of 2013 in order to reduce the operational burn rate as far as possible.

### **GOING CONCERN**

Pharming's 2012 financial statements have been drawn up on the basis of a going-concern assumption.

The 2012 year-end cash balance of €6.1 million, the net proceeds from the January 2013 convertible bond, amounting to €15.4 million, and the milestone payment of US\$5 million due by our US partner Santarus upon FDA acceptance of the BLA filing for Ruconest®, are expected to fund the Company for at least one year from the date of the report.

However, despite all this, the current financial position may not yet be sufficient to reach a break-even situation without the future inflow of new cash, other than cash from the potential receipt of future milestones from existing collaborations and the proceeds of Ruconest sales by our commercialisation partners, hence the Company may be dependent upon further additional funding.

Pharming has a history of operating losses and anticipates that it will continue to incur losses for the foreseeable future. No assurance can be given both on the timing and size of future profits. In addition, to the extent the Company needs to raise capital by issuing additional shares, shareholders' equity interests will be diluted.

### **Summary of goals for 2013**

- BLA filing of Ruconest® in the US.
- Acceptance for review of the BLA filing by the FDA.
- Increase sales of Ruconest® in Europe and other territories under the EMA product approval.
- Leverage the embedded value of the transgenic technology platform by initiation of new projects.
- Ensure that sufficient funding remains available to extend the Company's runway beyond US regulatory approval.
- Improve the Company's visibility amongst investors and other market participants (both buy- and sell-side analysts and financial press and trade press journalists).

Pharming is not providing guidance for the financial results in 2013.



## ***Management report continued***

### **STATEMENTS OF THE BOARD OF MANAGEMENT**

On the basis of the above and in accordance with best practice II.1.5 of the Dutch corporate governance code effective as of 1 January, 2009, and Article 5:25c of the Financial Markets Supervision Act the Board of Management confirms that internal controls over financial reporting provide a reasonable level of assurance that the financial reporting does not contain any material inaccuracies, and confirms that these controls functioned properly in the year under review. It should be noted that the above does not imply that these systems and procedures provide absolute assurance as to the realisation of operational and strategic business objectives, or that they can prevent all misstatements, inaccuracies, errors, fraud and non-compliances with legislation, rules and regulations.

The Board of Management declares that to the best of their knowledge and in accordance with applicable reporting principles, the consolidated financial statements give a true and fair view of the assets, liabilities, financial position and profit or loss of the group, and the Management Report incorporated in this Annual Report includes a fair review of the development and performance of the business and the position of the group, together with a description of the principal opportunities and certain risks associated with the expected development of the group. For a detailed description of the risk factors, we refer to page 24 of this report.

We would like to thank all our shareholders, research collaborators and partners for their help and support in 2012. We are especially grateful for the continued support from our employees, also in difficult circumstances as a result of the downsizing of the company.

Sincerely,

**The Board of Management**

**The original copy has been signed by the Board of Management**

Leiden,  
The Netherlands,  
29 March 2013

## **Management of the Company**

### **Management Structure**

Pharming has a two-tier board structure, consisting of a Board of Management (Raad van Bestuur) and a Board of Supervisory Directors (Raad van Commissarissen).

### **Management Powers and Function**

The Board of Management is entrusted with the management of the Company and is responsible for the policy and the central management of the Company under the supervision of the Board of Supervisory Directors. The Board of Management is authorised to commit the Company in contractual obligations to third parties. On 22 April, 2005, the Management Board adopted the current management board regulations which provide for certain duties, composition, procedures and decision-making of the Board of Management.

The Board of Supervisory Directors is charged with supervising the policy of the Board of Management and the general course of the Company's affairs and the enterprise connected therewith. The Board of Supervisory Directors assists the Board of Management by rendering advice. In performing their duties, the members of the Board of Management are obliged to act in the best interests of the Company and the enterprise connected therewith. On 14 October, 2004, the Board of Supervisory Directors adopted the current supervisory board regulations, which provide for certain duties, composition, procedures and decision-making of the Board of Supervisory Directors.

The members of the Board of Management and the members of the Board of Supervisory Directors are appointed at a General Meeting of Shareholders from nominations made by the Board of Supervisory Directors. If the nomination comprises two or more persons for each vacancy, the nomination shall be binding. In addition, the Board of Supervisory Directors is authorised to make a non-binding nomination for a vacancy, consisting of one person. If the Board of Supervisory Directors fails to submit the nominations in time, the General Meeting of Shareholders has the authority to appoint any person it chooses. Notwithstanding the foregoing, the General Meeting of Shareholders may at all times, by a resolution adopted by a majority of the votes cast representing more than one third of the Company's issued share capital, deprive the nominations of their binding effect. The General Meeting of Shareholders may adopt or reject a non-binding nomination by a resolution adopted with a majority of the votes cast.

The members of the Board of Management and the members of the Board of Supervisory Directors may at any time be suspended or dismissed by a resolution adopted by a majority of the votes cast representing more than one third of the Company's issued share capital. The members of the Board of Management may also be suspended or dismissed by a resolution of the Board of Supervisory Directors.

If in the aforementioned cases, the quorum of one third of the Company's issued share capital is not met, a new meeting will be convened in which a nomination can be rejected or a dismissal or suspension can be resolved by a majority of the votes cast.

## **Management of the Company continued**

### **Composition board of management**

During 2012, the Board of Management was composed of the following members:

<b>Name</b>	<b>Position</b>	<b>Member since</b>	<b>Term</b>
Mr. Sijmen de Vries	Chief Executive Officer	13 October, 2008	Up to AGM in 2013
Mr. Bruno Giannetti	Chief Operations Officer	1 December, 2006	Up to AGM in 2015
Mr. Rienk Pijpstra	Chief Medical Officer	1 April, 2010	Until 20 June 2012
Mr. Karl Keegan	Chief Financial Officer	1 October, 2010	Until 1 September 2012

#### **Sijmen de Vries, MD MBA (1959)**

Chief Executive Officer

Nationality: Dutch

Date of initial appointment: 13 October, 2008

Other current board positions: Mr. De Vries holds non-executive directorships in two private life science companies, Midatech Group Ltd and Sylus Pharma Ltd.

During 2012, Mr. De Vries was responsible for the overall management of the Company. Following the resignation of the CFO, Mr. Karl Keegan, on 31 August 2012, Mr. De Vries also assumed the (CFO) responsibilities for financing, financial accounting, investor relations and IT. Mr. De Vries has extensive senior level experience in both the pharmaceutical and biotechnology industry. He joined Pharming from Switzerland-based 4-Antibody where he was CEO. Mr. De Vries has also been CEO of Morphochem AG and prior to this he worked at Novartis Pharma and Novartis Ophthalmics and at SmithKline Beecham Pharmaceuticals Plc where he held senior business and commercial positions. Mr. De Vries holds an MD degree from the University of Amsterdam and a MBA in General Management from Ashridge Management College (UK).

#### **Bruno M. L. Giannetti, MD PhD (1952)**

Chief Operations Officer

Nationality: Italian

Date of initial appointment: 1 December, 2006

Other current board positions: Mr. Giannetti is the founder and president of CRM Clinical trials GmbH, a well established European Clinical Research Organisation specialised in international pharmaceutical clinical research.

During 2012, Mr. Giannetti was responsible for the Company's operations including research and development and manufacturing activities. Following the resignation of the CMO, Mr. Rienk Pijpstra, on 19 June 2012, Mr. Giannetti also assumed the (CMO) responsibilities for medical governance and led the non-clinical and clinical development, regulatory affairs, drug safety, and medical information teams. He has more than 25 years of experience in the pharmaceutical and biotech industry. Previously, he was the CEO of AM-Pharma BV (NL) and President and CEO of Verigen AG, Germany. He has served as senior management consultant for pharmaceutical R&D projects at Coopers & Lybrand (in Switzerland and the UK). Mr. Giannetti was also worldwide Vice-President Marketing and Medical Information at Immuno, Austria and Head of Clinical Research at Madaus AG, Germany. Mr. Giannetti holds a PhD in Chemistry and a MD PhD degree in Medicine from the University of Bonn.

## **Management of the Company continued**

### **Rienk R. D. Pijpstra, MD MBA (1961)**

Chief Medical Officer

Nationality: Dutch

Date of initial appointment: 1 April, 2010

Date of resignation: 19 June 2012

Other board positions: Mr. Pijpstra held no other board positions

Until his resignation on 19 June 2012, Mr. Pijpstra was responsible for medical governance at Pharming and led the non-clinical and clinical development, regulatory affairs, drug safety, and medical information teams. Since then, these responsibilities have been assumed by Mr. Bruno Giannetti.

### **Karl D. Keegan, PhD MSc (1967)**

Chief Financial Officer

Nationality: Irish

Date of initial appointment: 1 October, 2010

Date of resignation: 31 August 2012

Other board positions: Mr. Keegan held no other board positions.

Until his resignation on 31 August 2012, Mr. Keegan was responsible for financial accounting, financing activities, investor relations and IT systems. Since then, these responsibilities have been assumed by Mr. Sijmen de Vries.

## **Composition Board of Supervisory Directors**

During 2012, the Board of Supervisory Directors was composed of the following Members:

<b>Name</b>	<b>Position</b>	<b>Member since</b>	<b>Term</b>
Mr. Jaap Blaak	Chairman	23 May, 2007	Up to AGM in 2015
Mr. Juergen Ernst	Vice Chairman	15 April, 2009	Up to AGM in 2013
Mr. Barrie Ward	Member	23 May, 2007	Up to AGM in 2015
Mr. Aad de Winter	Member	15 April, 2009	Up to AGM in 2013

### **Jaap Blaak, MSc (1941)**

Chairman, member of the Remuneration Committee

Nationality: Dutch

Date of initial appointment: 23 May, 2007

Other current board positions: Mr. Blaak holds board positions in non-listed companies in the life science industry, like FlexGen Holding BV and to-BBB Holding BV. He is also a co-founder/shareholder in VenGen Holding BV.

Mr. Blaak has held managerial positions with Hoogovens and Indivers NV and Interturbine Holding BV in the Netherlands, USA, Germany and Singapore. In 1983, he was involved with the foundation of the MIP Equity Fund, one of the largest venture capital groups in Europe, and was appointed CEO in 1986. MIP merged with the ABN-AMRO Venture Capital Group to form AlInvest. Since 1989, Mr. Blaak is president and owner of Tailwind BV, a company investing mainly in early stage life science companies. He has been an advisor to the Dutch Ministry of Economic Affairs for the Biopartner and Technopartner Program and other innovative projects related to Entrepreneurship and Innovation. Mr. Blaak holds a MSc in Physics and Business Economics from the Free University of Amsterdam and followed the Advanced Management Program of the Harvard Business School (AMP '81).

## ***Management of the Company continued***

### **Juergen H.L. Ernst, MBA (1939)**

Vice Chairman, member of the Audit, Corporate Governance and Remuneration Committees

Nationality: German

Date of initial appointment: 15 April, 2009

Other current board positions: Mr. Ernst is chairman of the supervisory board of Aeterna Zentaris Inc

Mr. Ernst has extensive senior level experience in the field of pharmaceutical development and marketing. From 1969 until 1989 he held several positions at Kali-Chemie AG (subsidiary of Solvay SA), including Head of Pharmaceutical Marketing and Head of Pharmaceutical Division. In 1989, Mr. Ernst continued his career at Solvay and held several positions until he retired in 2004. Amongst other, he was member of the board of Pharmaceutical Division, CEO of Health Divisions, General Manager Pharmaceutical Sector and supervisory director and member of the Executive Committee. Mr. Ernst holds an ISMP Degree from Harvard University and an MBA from the University of Cologne.

### **J. Barrie Ward, PhD (1938)**

Member, Chairman of the Corporate Governance and Remuneration Committees and member of the Audit Committee

Nationality: British

Date of initial appointment: 23 May, 2007

Other current board positions: Mr. Ward is chairman of Cellcentric Ltd and board member of BergenBio AS, Cancer Research Technology Ltd and Spirogen sarl.

Mr. Ward has a broad international network and experience in managing and financing biopharmaceutical companies. He has held senior management positions in the UK, USA and Singapore at several pharmaceutical and biotechnology companies, including Glaxo Group Research Ltd, Virus Research Institute Inc, Avant Immunotherapeutics Inc and KuDOS Pharmaceuticals Ltd. His most recent position was CEO of KuDOS Pharmaceuticals Ltd, which was sold to Astra-Zeneca in 2006. Mr. Ward holds a PhD in microbiology from the University of Bath, UK.

### **Aad de Winter, LL.M (1953)**

Member, Chairman of the Audit Committee and member of the Corporate Governance Committee

Nationality: Dutch

Date of initial appointment: 15 April, 2009

Other current board positions: Mr. De Winter holds no other board positions.

Mr. De Winter has extensive financial experience. He started his career at AMRO Bank in 1980. He worked in the areas of capital markets, investment banking and institutional investor relationship management. In 1990, Mr. De Winter became senior Advisor Corporate and Institutional Finance at NIBC (formerly 'De Nationale Investerings Bank'). As of 1998, Mr. De Winter was at NYSE Euronext, Amsterdam responsible for advising and admitting companies to the stock exchange in Amsterdam as Director Listing & Issuer Relations. As of January 2009, Mr. De Winter is an Associate Partner of First Dutch Capital, Amsterdam and since 2008 a member of the China and India working group at the Holland Financial Centre which is, inter alia, focused on attracting Chinese and Indian companies to a (cross) listing on the Euronext Amsterdam. He is also an Associate Partner at Nederlandsche Participatie Exchange (NPEX), an innovative online trading platform for less liquid securities. Mr. De Winter has more than three decades of experience in assisting companies with stock exchange listings for various capital markets instruments. He holds a law degree from Erasmus University, Rotterdam, specialising in corporate law.

## ***Management of the Company continued***

### **Board of Supervisory Directors Committees**

The Board of Supervisory Directors has appointed from among its members an Audit Committee, a Remuneration Committee and a Corporate Governance Committee.

The Audit Committee consists of Mr. De Winter (Chairman), Mr. Ernst, and Mr. Ward. The tasks performed by the Audit Committee include reviewing the scope of internal controls and reviewing the implementation by the Board of Management recommendations made by the auditors of Pharming.

The Remuneration Committee consists of Mr. Ward (Chairman), Mr. Ernst and Mr. Blaak. The Remuneration Committee advises the Board of Supervisory Directors with regard to salaries, grants and awards under incentive plans, benefits and overall compensation for officers of the Company. The Board of Supervisory Directors decides upon remuneration of the Board of Management. The remuneration of each of the members of the Board of Supervisory Directors is determined by the General Meeting of Shareholders.

The Corporate Governance Committee consists of Mr. Ward (Chairman), Mr. Ernst and Mr. De Winter. The Corporate Governance Committee is responsible for monitoring for compliance with the Dutch Corporate Governance Code.

## Corporate governance and risk management

### Corporate Governance

The Board wishes to draw attention to Pharming's compliance with the majority of the provisions in the prevailing Corporate Governance Code. Details of Pharming's position regarding our formal corporate governance statement as required by Dutch Law can be found on our website ([www.pharming.com](http://www.pharming.com)).

### Risk management and control

Pharming's Board of Management is responsible for designing, implementing and operating the Company's internal risk management and control systems. The purpose of these systems is to manage in an effective and efficient manner the significant risks to which the Company is exposed and that provide reasonable assurance that the financial reporting does not contain any errors of material importance. The Company's internal risk management and control systems are designed to provide reasonable assurance that strategic objectives can be met. The Company has developed an internal risk management and control system that is tailored to the risk factors that are relevant to the Company, allowing for its small size. Such systems can never provide absolute assurance regarding achievement of Company objectives, nor can they provide an absolute assurance that material errors, losses, fraud, and the violation of laws or regulations will not occur. A summary of the risks that could prevent Pharming from realising its objectives is included in the section 'Risk Factors' of this report.

Our internal risk management and control systems make use of various measures including:

- Annual objective setting by the Board of Supervisory Directors and evaluation of realized objectives;
- Periodic operational review meetings of the Board of Management with departmental managers;
- Periodical updates to the Board of Supervisory Directors reviewing developments in the areas of operations, finance, research and development, business development, clinical development, and investor relations;
- Quarterly review of the financial position and projections as part of the meetings of the Board of Management with the Board of Supervisory Directors;
- A planning and control cycle consisting of annual, quarterly and monthly procedures, including subsequent follow-up on achievements of targets set; and
- A whistleblowers' procedure, which is published on the Company's website.

An effective system of (internal) controls and procedures is maintained and these include:

- Regular meetings of the Audit Committee with each of the Board of Management and the external auditors to discuss the financial results and the controls and procedures, and
- Audits of internal controls and procedures by the external auditors reported in their Management letters.

The Company maintains records and procedures designed to:

- Ensure the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and disposition of the assets of the Company;
- Provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the Company are being made only by authorised employees in accordance with documented authorisations; and
- Provide reasonable assurance regarding prevention or timely detection of unauthorised acquisition, use or disposition of the Company's assets that could have a material effect on the financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness for future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with policies or procedures may deteriorate. The Board of Management assessed the effectiveness of the Company's internal control over financial reporting as of 31 December, 2012. Based on its assessment and those criteria, they concluded that the Company maintained effective internal control over financial reporting as of 31 December 2012.

## ***Corporate governance and risk management continued***

The complete internal risk management and control systems of the Company are regularly discussed by the Board of Management with the Board of Supervisory Directors, its Audit Committee and Corporate Governance Committee and, in addition, procedures and controls are reviewed and areas requiring improvement are identified in audits from external parties, for example financial and IT experts.

Pharming is subject to many risks and uncertainties that may affect its financial performance. If any of the events or developments described below (see Risk factors) occurs, Pharming's business, financial condition or results of operations could be negatively affected. In that case, the trading price of the Shares could decline, and investors could lose all or part of their investment in the Shares.

The risks listed below do not necessarily comprise all risks faced by the Company, but take into account those which are known to the Company and which the Company considers material. Additional risks and uncertainties not presently known to Pharming or that the Company currently deems immaterial may also have a material adverse effect on its business, results of operations or financial condition and could negatively affect the price of the Shares.

With respect to the financial reporting risks reference is made to the Statements of the Board of Management on page 17 of the Annual Report.

### **RISK FACTORS**

#### **Clinical & Regulatory Risk**

##### **Pharming may not obtain all regulatory approvals for its products**

The process of undertaking and completing pre-clinical studies and clinical trials, and obtaining regulatory approvals, may take several years and requires the expenditure of substantial cash resources. There can be no assurance that applicable regulatory approvals for the Company's products will be granted in a timely manner, or at all. Any failure or delay in commencing or completing clinical trials for our products could severely harm our business.

The regulatory approval process is costly and lengthy and we may not be able to successfully obtain all required regulatory approvals. Negative or inconclusive study results (either pre-clinical or clinical) could result in Pharming stopping the development of a product or technology or requiring additional clinical trials or other testing and could have significant detrimental consequences for Pharming's business, financial position, results of operations, prospects and market price of the Shares.

Once a product receives regulatory approval, such approval can nonetheless be subject to limitations with regard to the indications for which it may be marketed. The approval may also be given subject to conditions, such as additional proof of the product's effectiveness and safety. Even after approval is granted, the product, its manufacturer and the manufacturing facilities are subject to ongoing scrutiny and regular inspections by the relevant agencies. If previously unknown problems are discovered in connection with the product, the manufacturer or the manufacturing facilities, this can result inter alia in restrictions on use and withdrawal of the product from the market and may adversely affect Pharming's business, financial position, results of operations, prospects and market price of the Shares.



## ***Corporate governance and risk management continued***

### **Pharming relies on third parties to conduct pre-clinical and clinical trials**

Pharming does not have the ability to independently conduct pre-clinical and clinical trials for product candidates. Pharming must rely on third parties, such as contract research organisations, medical institutions, clinical investigators and contract laboratories to conduct the pre-clinical and clinical trials. Pharming has entered into agreements with third parties to conduct these trials for and on behalf of Pharming. The Company remains responsible that each of the pre-clinical and clinical trials is conducted in accordance with its general investigation plan and protocol. Moreover, the European Medicines Agency (EMA) and the US Food and Drug Administration (FDA) require the Company to comply with regulations and standards, commonly referred to as good clinical practices, for conducting, recording and reporting the results of pre-clinical and clinical trials to ensure that data and reported results are credible and accurate and that trial participants are adequately protected. The reliance on third parties does not relieve Pharming of these responsibilities and requirements. If these third parties do not successfully carry out their contractual duties or regulatory obligations or meet expected deadlines, or the third parties need to be replaced or if the quality or accuracy of the data they obtain is compromised due to the failure to adhere to our pre-clinical and clinical protocols or regulatory requirements or for other reasons, the pre-clinical or clinical trials may be extended, delayed, suspended or terminated and Pharming may not be able to obtain regulatory approval for, or successfully commercialise, product candidates.

### **Regulatory standards are constantly developing and the failure to comply with applicable regulatory requirements would have serious consequences for the Company**

The industry in which Pharming operates is highly regulated and the applicable regulatory requirements vary considerably in the different geographic markets in which Pharming operates. These regulations are subject to change and development and future regulatory standards relating to, inter alia, biotechnology-derived products may be imposed that are distinct from those currently employed. The Company cannot guarantee that it will be able to meet such standards as they evolve and are implemented.

In addition to changing regulatory requirements, the failure of the Company to comply with applicable regulatory requirements could result in, among other things, injunctions, product recalls, product seizures, fines, and criminal prosecution.

### **The development of Pharming's early stage products face a long product development cycle**

The development of a therapeutic drug up to marketing approval by the competent authority is a lengthy process. During this time a research project must proceed through pre-clinical and several clinical stages of development, as well as the regulatory approval process. The consequence of this lengthy process and the uncertainties in connection with the research and development of pharmaceuticals is that only a small fraction of initial product candidates ultimately receive regulatory approval. In addition to its lead product Ruconest®, Pharming seeks to discover products in a number of long-term research projects for which clinical trials have not been initiated yet. A failure to develop additional products successfully and within a reasonable time frame could have significant detrimental consequences for Pharming's business, financial position, result of operations, prospects and market price of the Shares.

## **Corporate governance and risk management continued**

### **Commercial Risk**

#### **Pharming faces and expects to remain confronted with intense competition in the various markets for its products**

Several other companies develop products for the treatment of Hereditary Angioedema (HAE) attacks. Although Pharming is the sole provider of a recombinant therapy (either on the market or in development), the Company will face competition from these and existing products used to treat HAE attacks. In Europe, three other non-recombinant C1 inhibitor products and one product using another mechanism of action have been approved in the EU, each for the treatment of acute HAE attacks. In the USA one non-recombinant C1 inhibitor product and two products with alternative mechanisms of action have been approved for certain types of acute HAE attacks as well as one non-recombinant C1 inhibitor product for preventive treatment of HAE attacks. As a consequence, Pharming may not obtain a sufficient market penetration with Ruconest® to allow it to become profitable. For its other products under development, Pharming is also exposed to the risk that a competitor may bring a product with similar effects to the market faster than the Company does.

Even if the Company successfully introduces Ruconest® or another of its future products new technologies from competitors can make Ruconest® or any other products under development and Pharming's technology obsolete. Several competitors are active in the market for therapeutic products with more resources and significantly greater experience in, amongst others, obtaining regulatory approvals. The above events may have a material adverse effect on Pharming's business, financial position, and results of operations, prospects and market price of the Shares.

#### **Pharming's future success may depend upon the ability to enter into partnerships with third parties**

Our strategy for the commercialisation of some of our products, in particular those for larger indications, is to partner or out-license such products to third parties. If we are not able to locate, and enter into favourable agreements with, suitable third parties we may have difficult commercialising the relevant products. The process of establishing partnerships is difficult, time-consuming and involves significant uncertainty. Our ability to predict the success of any partnership we may enter into is limited due to (amongst others) the complexity and uncertainty of these arrangements.

#### **Our products may not gain market acceptance**

Sales of medical products depend on physicians' willingness to prescribe the treatment, which is likely to be based on a determination by these physicians that the products are safe and efficacious from a therapeutic and cost perspective relative to competing treatments. We cannot predict whether physicians will make this determination in respect of our products. Even if our products achieve market acceptance, the market may prove not to be large enough to allow us to generate sufficient revenues.

#### **Pharming relies on single source suppliers for the provision of essential materials incorporated in certain product candidates**

For some of the essential materials incorporated into product candidates, Pharming relies on a single supplier. Any disruption in the supply of these materials could adversely affect its ability to successfully complete the clinical trials and other studies of its product candidates, delay submissions of the regulatory applications or adversely affect its ability to commercialise its product candidates in a timely and/or commercially manner, or at all.

#### **The success of Pharming is highly dependent on public, market and governmental acceptance of its transgenic technology, development methods and products**

Development methods and technologies which Pharming uses include, among others, nuclear transfer technology and genetic modification. These and other activities have been, and may in the future be, the subject of debate and negative publicity. In the past, organisations and individuals have tried to stop genetic modification through different ways of putting pressure on companies relating to these activities, including by use of media campaigns. These actions may have a material adverse effect on Pharming's business, financial position, operational performance, prospects and market price of the Shares.

## ***Corporate governance and risk management continued***

Furthermore, the Company needs the market to accept its products in order to be able to commercialise them. Market acceptance is dependent on the opinions of the medical community, partners and competitors about numerous factors including the safety and efficacy of the relevant products. Any failure to obtaining market acceptance may also have a material adverse effect on Pharming's business, financial position, results of operations, prospects and market price of the Shares.

### **Disappointing reimbursements paid by third parties and disappointing cost-effectiveness of Pharming's products once approved for marketing may have a material adverse effect on Pharming's financial results**

Pharming's success is dependent on the reimbursement of the Company's products by third parties like the government health administration authorities, private health insurers and other organisations for the development of the products and/or technology. There is an increasing tendency of health insurers to reduce healthcare cost by limiting both coverage and the level of reimbursement for new therapeutic products and by refusing, in some cases, to provide coverage altogether. Not obtaining, or obtaining insufficient reimbursement from these parties may have an adverse effect on Pharming's business, financial position, results of operations, prospects and market price of the Shares.

In addition to reimbursements from third parties, the Company, if it succeeds in bringing a product to the market, also faces uncertainties about the cost-effectiveness of the product. The prices for the product that health care insurers and/or consumers are willing to pay may be lower than the production costs which may make the product uncompetitive and thereby adversely affect Pharming's business, financial position, results of operations, prospects and market price of the Shares.

### **Pharming is highly dependent on its ability to obtain and hold rights to proprietary technology and to develop its technology and products without infringing the proprietary rights of third parties and to protect its proprietary technology**

Patents, trade secrets and other proprietary rights are critical to Pharming's business. The Company has to protect its products and technology through patenting and licensing and at the same time develop its products without infringing the proprietary rights of third parties. The patent positions of pharmaceutical companies are highly uncertain and involve complex legal and factual questions, and the breadth of claims that will be allowed by patent authorities cannot be predicted with certainty. Pharming has several patent applications pending in the USA, Europe, Japan and in other countries. It is not certain that these pending patent applications will result in patent issues, that these patents will afford adequate protection or that the existing patents will not be challenged. The success of Pharming also depends, in part, on the ability of its licensors to obtain, maintain and enforce their intellectual property rights to the extent required by Pharming to develop and commercialise its products.

The Company seeks protection of its other proprietary know-how through confidentiality and other agreements with employees and third parties. No assurance can be given that these agreements offer an adequate protection or that equivalent or superior know-how is not independently developed by competitors.

## **Corporate governance and risk management continued**

### **Pharming operates in an industry sector that has a relative high risk of facing litigation**

Pharming participates and will participate in an industry that has been subject to significant product liability, intellectual property claims and other litigation. Pharming cannot be certain that it was the first to invent the subject matter of its patent applications and patents, that it was the first to apply for such a patent, or that technologies or products used by Pharming will not infringe third party intellectual property rights or that existing patents remain valid and enforceable. Pharming may face litigation or other legal proceedings concerning its intellectual property. These processes are time consuming and can be very costly. In the event of an unfavourable ruling in patent or intellectual property litigation Pharming could be subject to significant liabilities to third parties, be required to cease developing, manufacturing or selling the affected products or technology or be required to in-license the disputed rights from third parties and thereby adversely affect Pharming's business, financial position, results of operations, prospects and market price of the Shares. Although Pharming does not believe that there is any material litigation or other proceedings pending or threatened, it cannot be excluded that it will face such claims in the future or that such claims, although not considered material, will impose on Pharming considerable costs or will consume significant management resources. In addition it cannot be excluded that Pharming will be confronted with claims which are raised with the main aim of exploiting the nuisance value of publicly raised claims. In order to prevent infringement of third party intellectual property rights, Pharming may need to acquire licenses for patents held by third parties to re-establish or maintain its freedom to operate, possibly on unfavourable terms.

### **Pharming's future supplies of Ruconest® are dependent on third parties**

Pharming has entered into (downstream) manufacturing and supply agreements for the production of rhC1INH, the drug substance of Ruconest®, namely with Sanofi Chimie S.A. (Sanofi) and Merck Sharp & Dohme B.V. (MSD). Pharming may have to develop and/or contract additional (upstream) manufacturing capabilities and may have to contract additional (downstream) manufacturing capacity. It is uncertain whether and to what extent Pharming will be able to develop such capabilities or enter into such partnerships or agreements on a timely basis and on acceptable terms. Even if a partnership or agreement has been concluded, the possibility exists that these partners fail to live up to the agreements made with them or that Pharming is unable to maintain such agreements.

## **Personnel Risk**

### **Pharming is dependent on its ability to recruit and retain management and key employees**

Pharming depends to a large degree on the performance and expertise of its management and technical personnel. Competition for qualified employees is intense in the fields in which Pharming is engaged and there is no guarantee that qualified employees will not leave Pharming. The loss of one or more of these employees could lead to significant delays in product development and thus negatively influence Pharming's business activities. Pharming's continued success depends moreover on recruiting and retaining highly qualified employees in the future, especially in management and in the area of research and development. The loss of individual employees or failure to attract new highly qualified employees could have significant detrimental consequences for Pharming's business and financial position.

## **Financial Risk**

### **The Company is dependent on external funding in the near future**

Pharming does not yet generate sufficient cash from product revenues to meet its current working capital requirements and is, as has been the case since its incorporation, partially dependent on financing arrangements with third parties. The ability of Pharming to attract external funding is (*inter alia*) dependent on the external market conditions (equity and/or debt) and the Company's ability to generate cash inflows from development of sufficient revenues from sales in the European Union (EU) through its commercialisation partners, especially through its main EU partner Sobi and the approval by the FDA of its lead product, the therapeutic protein recombinant human C1 inhibitor (Ruconest®) and subsequent revenues generated from sales through its commercialisation partner Santarus, Inc. (Santarus) for the treatment of acute attacks of HAE for marketing in the United States of America (USA), Canada and Mexico and the ability to leverage its transgenic platform through commercialisation deals.

## ***Corporate governance and risk management continued***

Pharming has a history of operating losses and no assurance can be given both on the timing and size of future profits. We have a history of operating losses and anticipate that we will continue to incur losses for the foreseeable future. We have thus far incurred losses in each year since incorporation. These losses have arisen mainly from costs incurred in research and development of our products and general and administrative expenses.

The amount and timing of any expenditure required to implement our business strategy and continue the development of our products will depend on many factors, some of which are out of our control, including but not limited to:

- scope, rate of progress, results and cost of our pre-clinical and clinical trials and other research and development activities;
- terms and timing of any collaborative, licensing and other arrangements that we may establish;
- higher cost, slower progress than expected to develop products and delays in obtaining regulatory approvals;
- number and characteristics of products that we pursue;
- cost and timing of establishing sales, marketing and distribution capabilities;
- timing, receipt and amount of sales or royalties, if any, from our potential products, or any upfront or milestone payments during their development phase;
- the cost of preparing, filing, prosecuting, defending and enforcing any intellectual property rights; and
- the extent to which we acquire or invest in businesses, products or technologies.

No assurance can be given that we will achieve profitability in the future. Furthermore, if our products fail in clinical trials or do not gain regulatory approval, or if our products do not achieve market acceptance, we may never achieve profitability. Even if we achieve profitability in the future, we may not be able to sustain profitability in subsequent periods.

We expect to need additional funding in the future, which may not be available to us on acceptable terms, or at all, which could force us to delay or impair our ability to develop or commercialise our products. There can be no assurance that additional funds will be available on a timely basis, on favourable terms, or at all, or that such funds, if raised, would be sufficient to enable us to continue to implement our long term business strategy. If we are unable to raise such additional funds through equity or debt financing, we may need to delay, scale back or cease expenditures for some of our longer term research, development and commercialisation programs, or grant rights to develop and market products that we would otherwise prefer to develop and market ourselves, thereby reducing their ultimate value to us. Our inability to obtain additional funds necessary to operate the business could materially and adversely affect the market price of our shares and all or part of an investment in our shares could be lost. In addition, to the extent we raise capital by issuing additional shares, shareholders' equity interests will be diluted.

### **Exchange rate fluctuations could negatively affect our financial condition**

Pharming is based in the Netherlands, but sources materials, products and services from several countries outside the EU-territory which are paid in local currencies. Subject to commercialisation of Ruconest® in the US or in other countries outside the EU and the US, Pharming will also receive payments in US dollar or possibly in other currencies. As a result, Pharming's business and share price will be affected by fluctuations in foreign exchange rates between the euro and these foreign currencies, including the US dollar, which may have a significant impact on Pharming's reported results of operations and cash flows from year to year.

## Board of Supervisory Directors

### REPORT OF THE BOARD OF SUPERVISORY DIRECTORS

The Board of Supervisory Directors, in general, supervises the Board of Management in its duty to manage the Company. It performs its duties and activities in accordance with the Articles of Association of the Company, its regulations, which are posted on the Company's website, the applicable law and the Dutch Corporate Governance Code applicable as of 1 January, 2009 (the "Code"). The supervision of the Board of Management by the Board of Supervisory Directors includes:

- (a) the achievement of the Company's objectives;
- (b) the corporate strategy and the risks inherent in the business activities;
- (c) the structure and operation of the internal risk management and control systems;
- (d) the financial reporting process;
- (e) compliance with primary and secondary regulations;
- (f) the Company-shareholders relationship; and
- (g) corporate social responsibility issues that are relevant to the enterprise.

The Board of Supervisory Directors determines, together with the Board of Management, the corporate governance structure of the Company and ensures compliance with the Code and other (foreign) applicable rules and regulations, assisted by its Corporate Governance Committee. Assisted by its Audit Committee, it supervises the financial reporting process and assisted by its Remuneration Committee, it determines the remuneration of the individual Board of Management members within the remuneration policy adopted by the Annual General Meeting of Shareholders. The report of the Remuneration Committee is presented separately as of page 33.

#### Composition and remuneration

In 2012 the composition of the Board of Supervisory Directors was as follows: Mr. Blaak (Chairman), Mr. Ward, Mr. Ernst and Mr. De Winter.

The remuneration of the members of the Board of Supervisory Directors is determined by the General Meeting of Shareholders. As of 2011 the annual remuneration is based on the position an individual has in the Board of Supervisory Directors, the Audit Committee and the Remuneration Committee, no additional remuneration was agreed for member of the Corporate Governance Committee.

For 2012 the annual compensation was as follows (unchanged from 2011):

- Board of Supervisory Directors: Chairman €44,000 and Member €31,000
- Audit Committee: Chairman €9,000 and Member €3,000
- Remuneration Committee: Chairman €6,000 and Member €3,000
- An additional compensation of €1,000 per day is paid in case of extraordinary activities

No current member of the Board of Supervisory Directors holds shares in the Company. No loans or other financial commitments were made to any member of the Board of Supervisory Directors on behalf of the Company. Pharming does not require its Board of Supervisory Directors members to disclose any holdings in other listed and/or unlisted companies.

## ***Board of Supervisory Directors continued***

### **Activities**

The Board of Supervisory Directors met seven times in 2012. At each of these meetings all Members were present or participating by teleconference. The Board of Management attended these meetings except when the composition, performance, remuneration of the Board of Management and the self-evaluation of the members of the Board of Supervisory Directors and its committees were discussed.

At the meetings of the Board of Supervisory Directors, the Company's financial and operational targets, strategy and accompanying risks were extensively discussed. Amongst other topics, a considerable amount of time was spent on discussing regulatory issues with regard to Ruconest®, the competitive landscape, licensing opportunities, refinancing of the Company, succession planning, corporate governance, the financial performance and structure of the Company, the targets for 2012 and the operational and financial risks to which the Company is exposed.

During its meetings, the Board of Supervisory Directors paid special attention to the following risks:

- The Company's progress on the achievement of certain milestones. There is no certainty that these milestones will actually be achieved.
- The Company does not yet have a positive operational cash flow and therefore will be dependent on financial markets and/or partnership revenues for funding.
- The Company is largely dependent on the development of one key product.
- The key product depends on regulatory filings for all markets. However, the outcome of the registration processes in all markets may be influenced by unpredictable events.
- The Company is dependent on the availability and commitment of key employees.
- The Company is active on a niche market for an orphan drug product with at least three competitors.
- The timely development of the Company's products is dependent on the ability to attract partnerships or capital under attractive conditions.

All these risks have been thoroughly discussed with the Board of Management and, where possible, actions have been undertaken to minimise the Company's exposure. Financial risks are actively monitored by the finance department, whose findings are discussed with the Board of Management on a monthly basis or whenever deemed necessary. The finance department also maintains a close working relationship with the legal officer and company secretary to monitor other corporate and contractual risks. The risks are further described in the corporate governance chapter commencing on page 23.

The quarterly financial statements are circulated to the full Board of Supervisory Directors in advance of every Audit Committee meeting. During the four Audit Committee meetings held in 2012, the financial statements were discussed with a special emphasis on complex transactions and the impact of IFRS related issues. In addition, the audit plan and the audit findings of the external auditor were discussed. The Audit Committee in 2012 consisted of Mr. De Winter (Chairman), Mr. Ernst, and Mr. Ward. All meetings of the Audit Committee were also attended by the other member of the Board of Supervisory Directors, Mr. Blaak, and by the auditors.

The Corporate Governance Committee consisted of Mr. Ward (Chairman), Mr Ernst and Mr. De Winter but did not meet during 2012. However, at every BOSD meeting various topics of Corporate Governance were discussed.

A report of the Remuneration Committee can be found on pages 33-37.

***Board of Supervisory Directors continued***

**Financial statements**

The financial statements of Pharming Group N.V. for 2012, as presented by the Board of Management, have been audited by PricewaterhouseCoopers Accountants N.V. Their report is included in this Annual Report on pages 118-119. The Financial Statements are approved by the Board of Supervisory Directors and all members (as well as the members of the Board of Management) have signed these Statements. The Board of Supervisory Directors recommends the General Meeting of Shareholders to adopt the 2012 Financial Statements and to discharge the Board of Management and Supervisory Board from liability for their management and supervisory activities on behalf of the Company.

**The original copy has been signed by the Board of Supervisory Directors**

Leiden,  
The Netherlands,  
29 March 2013



## **Report of the remuneration committee**

The Remuneration Committee proposes the remuneration policy to the Board of Supervisory Directors as well as the remuneration of the individual members of the Board of Management. The policy includes the remuneration structure, defining the amount of fixed remuneration, shares and/or options to be granted and the variable benefits, pension rights, severance pay and other forms of compensation.

The Remuneration Committee also prepares the remuneration report that accounts for the implementation of the remuneration policy over the past financial year. It includes an overview of the remuneration policy for the next financial year and subsequent years, both in accordance with the Company's current Board of Supervisory Directors Regulations and Remuneration Committee Regulations.

The objectives of the remuneration policy are to attract, motivate and retain good management by means of a competitive policy linked to the Company objectives and the overall performance of the Board of Management and to create a long-term relationship with the Company. The Remuneration Committee recognises that the Company is increasingly competing in an international environment. The policy and its implementation are reviewed by the Remuneration Committee at least annually.

### **2012 Remuneration policy and structure**

The remuneration policy for 2012 was a continuation of the 2011 policy and was approved in the Annual General Meeting of May 2012. The main items of this policy are:

- The remuneration of each member of the Board of Management consists of a fixed salary, an annual bonus as a percentage of the fixed component, short- or long term incentives by way of shares and/or options to shares in the Company and benefits in kind such as health insurance and participation in a pension plan, as further specified in Note 25 to the Financial Statements.
- In general, employment contracts or management contracts, with members of the Board of Management, provide for annual bonuses based on personal and/ or extraordinary performance and/ or the achievement of predetermined objectives. These contracts have included provisions for an individual bonus in cash or shares of up to forty percent, of the member's gross annual salary (including holiday allowance). Other benefits, such as health insurance and pension schemes are in accordance with the applicable staff manual of the Company. Severance pay cannot exceed the member's gross annual salary. The notice period for each Member is two months.
- Members of the Board of Management as well as other key individuals are eligible to participate in the Company's Long Term Incentive Plan (LTIP). Under the plan, participants receive shares in the Company, the number of which is dependent upon the performance of the Company share price, during a three year period, compared to a peer group of European Biotech Companies (see page 36).

### **Meetings and Composition**

During the 2012 financial year the Remuneration Committee consisted of Mr. Ward (Chairman), Mr. Blaak and Mr. Ernst. The Remuneration Committee met twice in 2012. During these meetings the performance of the Board of Management in general and its individual members in particular were reviewed and discussed relative to pre-agreed targets and to define targets for the coming year. The remuneration packages, long term incentive plan and achievements versus 2012 objectives were also discussed and agreed in the last meeting.

## **Report of the remuneration committee continued**

### **Remuneration Report 2012**

Following the recommendations of the Remuneration Committee, the Board of Supervisory Directors (BoSD) decided to grant 6,187,500 of the available 10,550,000 stock options of the Board of Management Option Plan (as approved by the AGM on 14 May, 2012), in line with the achievement of the present target for the Board of Management. The exercise price of these options is €0.0558. The stock options will expire on 13 May, 2017. To Mr. De Vries 3,750,000 stock options were granted, and to Mr. Giannetti 2,437,500 stock options were granted. Initially, options were also issued to Mr. Pijstra (2,437,500 options) and Mr. Keegan (2,812,500), however these were forfeited as they stepped down in the course of the year.

The Remuneration Committee carefully reviewed the performance of the Board of Management against both the corporate and personal objectives that had been set for 2012. The Remuneration Committee recognised that despite continued turbulent times, the BoSD were of the opinion that the Board of Management had met the majority of the corporate and personal objectives set for 2012 and contributed to positioning the Company for the future in particular by the following accomplishments:

- Conclusion of additional regional commercialisation agreements for Ruconest®.
- Succeeded to raise additional funds during the year, under exceptionally challenging circumstances.
- Successfully completed the US pivotal Phase III (1310) Study and recovered from an internal oversight that caused an unplanned delay of almost three months in obtaining the results of the study and in the receipt of the associated milestone payment.
- Leveraging the rabbit platform by initiating a new project eg. (Factor VIII) in haemophilia A.
- Planning and implementing a significant reduction of the cost basis through re- negotiation of existing third party obligations, re- focusing of the Company and the associated downsizing of the company cost structure.
- Increased the Company's visibility with investors.

Especially the acute need for conclusion of an additional financing facility during the summer of 2012, in parallel with the re-negotiation of third party obligations and the initiation of the imperative downsizing of the infrastructure, with at the time, very minimal financial reserves caused by an unplanned delay in the Study 1310, represented a very critical episode from which recovery during the remainder of 2012 was subsequently achieved.

Following the recommendations of the Remuneration Committee, the Board of Supervisory Directors decided therefore that Mr. Giannetti should be granted 75%, and Mr. De Vries 75% of the corporate and personal objectives that had been set to determine their individual bonus pay-out and that in addition to that, Mr. de Vries should be granted an exceptional one-off additional bonus (payable in shares) of 50% of his annual target as recognition for his efforts in successfully securing financing for the Company and positioning it for the future under the abovementioned very critical circumstances.

Following the recommendations of the Remuneration Committee, the Board of Supervisory Directors decided to (i) pay out the regular bonus 50% in cash and 50% in shares (ii) make the pay- out of both the regular bonus payments and 50% of the exceptional bonus payment conditional upon the acceptance of the Ruconest® BLA for review by the FDA and (iii) make the pay-out of the remaining 50% of the exceptional bonus payment conditional upon reaching the first US\$ 1 million of Ruconest® sales in the US market.

The share component of the bonus payments will be valued at the volume weighted average price (VWAP) measured over the 5 trading days prior to 28 February 2012 (€ 0.01821/ €0.182 post reverse share split). A detailed overview of the compensation of the members of the Board of Management can be found in note 25 of the annual report.

The individual remuneration of the members of the Board of Management was reviewed, in the light of certain agreed milestones that were achieved in 2012 and in the light of developments at other listed biotechnology/specialty pharmaceutical companies in Europe. On this basis, the Remuneration Committee advised the Board of Supervisory Directors to not change the fixed salaries of the members of the Board of Management from 1 January, 2013.

## ***Report of the remuneration committee continued***

### **Remuneration Policy 2013 and the future**

To continue to be able to attract and retain top talent in a competitive and global environment and to focus management and staff on creation of sustainable added value, total compensation continues to be significantly driven by variable performance dependent income components and continues to be kept in line with industry standards of companies at a comparable stage of development.

For 2013, the Remuneration Committee will continue to implement the compensation policy approved at the 2010 AGM. All remuneration elements described below are consistent with and covered by the current compensation policy. As usual shareholder approval will be sought at the AGM to be held on 15 May, 2013, for the proposed number of share options to be granted to the Board of Management and for the Staff option pool.

#### **1. Fixed salary determined by the Board of Supervisory Directors.**

#### **2. Target bonus of up to 40% of annual salary in cash and/or in shares.**

The issuance of share based bonus component shall be valued at the VWAP measured over the 20 trading days prior to 31 January, 2013. Payment of the bonus remains dependent on the achievement of pre-defined milestones which are a combination of corporate and personal milestones.

Proposals on the potential award of a bonus, achievement of milestones and an increase of fixed salary is made by the Remuneration Committee towards the end of the year and formally approved by the Board of Supervisory Directors in the first meeting of the next year but in any case before or on the date of approval of the Annual Report.

The Board of Supervisory Directors has defined a mix of corporate and personal milestones that will be used to measure performance and potential award of bonus payments for 2013.

The main corporate objectives for 2013 for the Board of Management can be summarised as follows:

- Increase the value of the Ruconest® franchise through support of our existing partners and through geographical expansion by securing new partnerships.
- Build the C1 Inhibitor franchise by focusing on US regulatory progress and by progressing the development of C1 inhibitor in indications beyond acute HAE attacks.
- Develop the Factor VIII programme according to plan and secure co-funding.
- Leverage the embedded value of the transgenic technology platform by initiation of additional new projects.
- Operate within agreed budgets at the department and company level.
- Create a basis for long term sustainability through rationalization of the current portfolio and concurrently broaden the portfolio with new projects, through a rational process of commercially led asset evaluations.
- Improve the Company's visibility amongst investors and other market participants (both buy- and sell-side analysts and financial press and trade press journalists).

For competitive reasons further details of these milestones and the personal milestones are not publicly disclosed.

## **Report of the remuneration committee continued**

### **3. Share options dependent on defined parameters. The amounts and parameters are outlined below.**

Description of proposed 2013 share option grants to the Board of Management:

	<b>Nr of options</b>	<b>Parameters</b>
Mr. Sijmen de Vries	2,500,000	In service at 1 January, 2014
Mr. Bruno Giannetti	1,625,000	In service at 1 January, 2014

It is proposed to reserve 2,500,000 options for the staff option pool for distribution during 2013.

The strike price of the 2013 share options for the Board of Management shall be equal to the VWAP measured over the 20 trading days prior to the date of the AGM 2013 (15 May, 2013).

### **4. The Long Term Incentive Plan (LTIP)**

Under this LTIP, restricted shares are granted conditionally to the Board of Management and certain eligible managers each year with a target value of 30% of annual salary. These shares will vest after three years provided that the share price has increased (i.e. increased total shareholder value). The number of shares vested will be based on the relative performance of the share price compared to a group of 30 European Small Cap (< €500 million) listed companies active in Life Sciences over the preceding 36 months.

The reference group consists of the following companies:

Ablynx (BE)	Addex (CH)	Allergy Therapeutics (UK)
Ark Therapeutics (UK/Fl)	Basilea (CH)	Bavarian Nordic (DK)
Biotie Therapeutics (Fl)	Collectis (FR)	Cytos (CH)
Evotec (DE)	Exonhit (FR)	Galapagos (BE)
Genmab (DE)	GW Pharma (UK)	Hybrigenics (FR)
ImmuPharma (UK)	Innate Pharma (FR)	Medigene (DE)
Medivir (SE)	Morphosys (DE)	Neurosearch (DK)
Newron (IT)	Oxford Biomedica (UK)	Photocure (NO)
Renovo (UK)	Santhera (CH)	Ti-Genix (BE)
Transgene (FR)	Veloxis Pharmaceuticals (DE)	Vernalis (UK)
Willex (DE)		

The vesting schedule will be as follows:

- Ranking in the top 5% of the group: 100%
- Ranking in the top 5-10 % of the group: 80% of maximum
- Ranking in the top 10-20% of the group: 60% of maximum
- Ranking in the top 20-30% of the group: 50% of maximum
- Ranking in the top 30-50% of the group: 20% of maximum
- Ranking lower than 50% of the group: 0% of maximum

Upon a change of control, all shares will vest automatically.

## ***Report of the remuneration committee continued***

### **LTIP 2010 expired without pay-outs**

At 1 January, 2013, after three years of the three year period of the 2010-LTIP, the Pharming share price has not increased over the period. As a result none of the allocated shares have vested.

The allocations under the 2011 and 2012 LTIP still have one and two years respectively to run.

### **LTIP 2013**

For 2013, the Board of Supervisory Directors, following the recommendation of the Remuneration Committee, has determined that the number of shares (calculated at the closing price of 31 December, 2012 of €0.025, €0.25 after taking into account the 28 February 2013 reverse share split) shall be equal to 30% of each of the Board of Management's 2013 base salaries.

This results in the following allocations:

Mr. S. de Vries 475,200 shares, Mr. B.M.L. Giannetti 318,000 shares. For a selected group of senior managers 400,000 shares are available. A maximum amount of 50,000 shares per senior manager can be allocated.

In the light of the financial position of the Company during 2012, the Board of Supervisory Directors and the Board of Management have decided not to change the Long Term Share based Compensation elements for 2013.

The Corporate Governance chapter of this Annual Report and the Notes to the Financial Statements contain further details with regard to the remuneration of the Board of Supervisory Directors and the Board of Management, as well as the Company's remuneration policy and pension schemes.

## **Corporate social responsibility**

### **Introduction**

Pharming takes its obligation to behave in a sustainable, safe and responsible manner, very seriously. Pharming is aware of its responsibility towards all stakeholders, including employees, shareholders, patients, animals, the environment, as we develop important new therapeutic products to address rare and life threatening human diseases.

### **Medical Need**

Pharming is developing therapeutic products for specific rare diseases (orphan drug development) and other significant medical needs. Through development of the products currently in its pipeline, Pharming can offer alternative treatment options to patients, improve the quality of life and in some cases save lives. As such, we believe that Pharming makes a valuable contribution to society.

### **Patient Safety**

Pharmaceutical products need to be as safe as possible and fully compliant with regulatory guidelines. Therefore, in the development of therapeutics, the evaluation of safety and efficacy of the products is mandatory. Several studies need to be performed, ranging from early research studies in animals to clinical studies in healthy volunteers and patients. These studies are highly regulated and thoroughly monitored, reviewed and evaluated both by Pharming and the regulatory authorities. The risk benefit of the products in each indication under development or marketed is continuously evaluated. Findings, and Pharming's interpretation there-off, are reported to the relevant authorities according to legal timelines, and result in appropriate actions such as updating investigator brochures and product labeling. In the most extreme cases a safety concern can result in suspension of enrolment in a clinical trial or withdrawal of the product from the market.

Clinical studies are carried out in compliance with legal and regulatory requirements and according to Good Clinical Practice (GCP) guidelines. Pharming's laboratories comply with Good Laboratory Practice (GLP) guidelines and all production facilities and processes comply with regulatory Good Manufacturing Practice (GMP) guidelines. Pharming's Quality department conducts internal and external audits of processes, products and facilities on a regular basis. All these processes and guidelines have been implemented to improve and assure the quality of our products.

### **Code of Conduct**

Pharming endeavors to carry out its business fairly and honestly, at the same time taking into account the interests of all those who may in any way be affected by its activities. A good reputation is of major importance to the Company and its stakeholders. In order to achieve success, the members of the Board of Supervisory Directors, Board of Management and employees must comply with a number of behavioral standards which have been stated in a set of general principles referred to as the Code of Conduct. This Code of Conduct has been designed to provide guidance on acting in accordance with the Company's high level of principles and standards as this is of the utmost importance for Pharming's reputation. The Code of Conduct is available on the Company's website.

### **Whistleblowers' procedure**

Pharming has a whistleblowers' policy which can be found on the Company's website. This policy describes the internal reporting procedures of suspected irregularities with regard to a general, operational and financial nature in the Company. The whistleblowers' procedure applies to all Pharming entities. Pharming will not discharge, demote, suspend, threaten, harass, or in any other matter discriminate against an employee in the terms and conditions of employment because of any lawful or other actions by the employee with respect to good faith reporting of complaints or participation in a related investigation.

## ***Corporate social responsibility continued***

### **Animal Care Code of Conduct and Welfare Policy**

Pharming's transgenic technology involves animals and therefore animal safety and welfare are crucial. The Company produces products in animal systems, i.e. in the mammary glands of rabbits. Pharming's specific protein products are purified from the milk of these transgenic animals.

Pharming has an Animal Care Code of Conduct in place, which focuses on the strict regulatory control of transgenic materials and animals in regard to the environment. Our Animal Care Code of Conduct emphasizes the importance of carrying out our activities with transgenic animals in a consistent and safe manner, and in conformity with the laws and regulations in force in the countries of operation. Special attention is given to the strict separation of transgenic and non-transgenic materials and animals. In addition, the Company follows strict procedures to prevent the prohibited release of transgenic animals, their semen or any other reproductive transgenic material into nature.

Pharming is largely dependent on its transgenic animals and highly values animal health and welfare. The Company has an Animal Welfare Policy which amongst others, imposes that Pharming will not develop products with unacceptable adverse effects on animal health and welfare. Accordingly, Pharming carefully and continuously monitors the health and welfare of its animals.

### **Human Resources**

Pharming recognizes that our member of staff represent a key factor to the success of the company. Pharming is committed to attracting, developing and retaining the best talent to fill each and every job in the company.

2012 was largely dominated by the review of strategic options and restructuring. The company undertook a comprehensive review of its strategic options including the implementation of additional cost containment measures.

During the first half of 2012, we started the restructuring process by reviewing all strategic options for the company. As part of a constructive process in cooperation with the Board of Management and the Works Council, a re-organization plan, staffing plan and social plan were developed. Throughout the process we maintained a commitment to clear communication and transparency, our guiding principles in dealing with our employees. To support the process of enabling staff that had been made redundant to re-enter the labor market at the earliest possible opportunity, information on the specific redundancies was provided to all individual members of staff at the earliest moment possible, well ahead of their factual redundancy.

This downsizing led to the closure of Pharming's US based cattle platform research operations including the US farm based research facilities and redundancies for the staff (10 employees) involved in research and maintenance of the company's transgenic cattle herd. This decision reflected the declining importance of transgenic cattle research, and legacy proteins such as fibrinogen, lactoferrin and collagen to Pharming's future strategy and the increasing business development focus on current and new projects.

Pharming did its utmost best to provide all employees with preferred counseling and a respectful redundancy agreement. According to our information, all US employees are re-employed now.

The strategic review also led to a restructuring of the Company's Dutch operations as announced in August 2012. This restructuring is now in the final stage, nearing its completion. Due to the restructuring, 23 employees became redundant. Of the 23 planned redundancies, 3 employees will remain in service, after filling an internal vacancy, and 6 employees, who during the course of the process found new employment, have been compensated in line with the social plan as agreed with the works council in September 2012. For all but one of the 14 remaining redundancies individual amicable termination agreements in line with the Social Plan were agreed. The last case will be settled by the Cantonal Court.

## **Corporate social responsibility continued**

The restructuring has been a difficult, though entirely necessary process. The Company is aware of the tremendous affect this restructuring has had on those individuals who have been made redundant and also on the remaining employees. In recognition of this, the Company has provided several training courses, such as external outplacement trajectory and job application training, to assist its redundant employees in maximizing their employability.

### **Employee Statistics**

As a relatively small company, Pharming employs a diversified team in gender and age.

As per December 31 2012, the majority of personnel are employed at Pharming's headquarters in Leiden; with approximately fifteen employees working at other locations in the Netherlands and in the USA. The Company's business involves specific high-tech processes and technologies and requires the employment of highly skilled personnel. Some of the internal departments are occupied by only one person having specialist knowledge, skills and experience. Therefore, it is important for Pharming to retain and motivate personnel and attract top talent in a competitive and global environment.

During 2012, the Company hired 6 new employees (2011: 5). A total of 24 employees left the Company, of which 13 as result of the restructuring.

As per 31 December, 2012, 61 people were employed (2011: 79), during the first half of 2013, as result of the downsizing, 43 employees (36 FTE) will remain.

The weighted average full time equivalent (FTE) for 2012 was 68 (2011: 76).

<b>Headcount (FTE) per 31 December</b>	<b>2012</b>	<b>2011</b>
G&A	14 (12)	16 (12)
Manufacturing	19 (18)	19 (18)
R&D	28 (25)	44 (39)
Total	61 (55)	79 (69)

### **Diversity**

At the end of 2012, 59% (2011: 56%) of our total workforce was female. 14% of the senior management of the Company was female. There are no female members of the Board of Supervisory Directors. The Company strives for representative senior management and BOSD and therefore, if equally qualified, female members will get preference if new appointments on a senior management or BOSD level occur.

### **Male and female employees (end of 2012)**

Male	in senior management positions	32%
	in other than senior management positions	68%
Female	in senior management positions	5%
	in other than senior management positions	95%



## ***Corporate social responsibility continued***

### **Health, Safety and Environment**

Daily activities at the Company include working with materials that might harm employees and/or our environment. To create a work environment that is as safe as possible, we have created an internal Health and Safety specialist position. Our internal standard operating procedures are designed to protect our people and the environment from any harm. All employees receive safety training and training to deal with work related risks. Our extensive health and safety policy is published on the Intranet and is revised annually. The emergency response teams at our sites are trained to perform first aid, fight small fires and to manage an evacuation. Safety is continuously monitored in everything we do. For that reason we pay significant attention to education and information on all aspects of Safety.

### **Works Council**

The Works Council is the body that by Dutch law represents the employees of the Dutch Pharming companies. Pharming's Board of Management believes in the dialogue with its employees and therefore considers the Works Council to be a valuable partner.

Especially during the very challenging restructuring activities this year, Pharming's Board of Management has experienced constructive cooperation with the Works Council. Extensive meetings were held during which all aspects of the restructuring activities were discussed.

## **Information for Shareholders and Investors**

### **GENERAL**

Pharming's policy is to provide all Shareholders and other parties with timely, equal and simultaneous information about matters that may influence the share price. In addition, we aim to explain our strategy, business developments and financial results.

We communicate with our Shareholders and investors through the publication of the Annual Report, meetings of Shareholders, press releases and our website. Pharming organises analysts and press meetings and/or conference calls, when presenting half year and annual financial results or other significant news. These meetings and/or conference calls are announced in advance by means of press releases and on Pharming's website. Audio and/or web casts of these conference calls and corporate presentations are made available on the website after the meetings. In addition to the scheduled half-yearly and yearly result presentations, we maintain regular contact with financial analysts and institutional investors through meetings and road shows. The Company regularly presents at conferences and corporate and scientific presentations are made available at the Company's website.

Activities in 2012 for shareholders and investors included:

- A full presentation of our annual results to financial journalists and analysts, including audio commentary, Q&A sessions and posting on our website
- Various additional conference calls with analysts, investors and providers of finance
- Regular road show meetings with potential and existing shareholders and sell side analysts
- Timely updates in the Investor Relations section of our website
- A new "in the news" section on our website to provide additional updates aside from press releases

### **SHARE INFORMATION**

Pharming Group N.V.'s shares are listed on NYSE Euronext N.V. Amsterdam (symbol: PHARM) since 1999. The Shares (ISIN Code: NL0010391025) are traded through the book-entry facilities of Euroclear Netherlands, only. The address of Euroclear Netherlands is: Herengracht 459-469, 1017 BS Amsterdam, the Netherlands.

ABN AMRO Bank N.V. is the paying agent with respect to the Shares.

The address of the paying agent is: ABN AMRO Bank N.V., Gustav Mahlerlaan 10, 1000 EA Amsterdam, the Netherlands.

***Information for Shareholders and Investors continued***

**FINANCIAL CALENDAR FOR 2013**

15 May, 2013	Annual General Meeting of Shareholders at the Pharming headquarters in Leiden, the Netherlands at 14.00 CET
16 May, 2013	Publication of first quarter 2013 financial results at 07.00 CET
1 August, 2013	Publication of second quarter 2013 financial results at 07.00 CET
7 November, 2013	Publication of third quarter 2013 financial results at 07.00 CET

## **Glossary**

### **AGM**

Annual General Meeting of Shareholders.

### **AMI**

Acute Myocardial Infarction, commonly known as a heart attack, results from the interruption of blood supply to a part of the heart causing heart cells to die. Heart attacks are the leading cause of death for both men and women worldwide.

### **AMR**

Antibody-mediated rejection occurs when a transplant because of suboptimal histo-compatibility, is perceived by the recipient as a foreign body. The immune system is activated and the foreign body is attacked, which can lead to organ failure and immunological rejection of the organ.

### **BLA**

In the US, pharmaceuticals are approved for marketing under the provisions of the Public Health Service (PHS) Act. The Act requires a firm which manufactures a pharmaceutical for sale in interstate commerce to hold a license for the product. To commercialise a new biological product in the US, the FDA needs to approve a Biologics License Application (BLA). A BLA is a submission that contains specific information on the manufacturing processes, chemistry, pharmacology, clinical pharmacology and the medical affects of the biologic product. If the information provided meets FDA requirements, the application is approved and a license is issued allowing the company to market the pharmaceutical. Biological products include amongst others monoclonal antibodies, growth factors, blood products and proteins intended for therapeutic use. The concerning FDA centre is the Center for Biologics Evaluation and Research (CBER).

### **BOM**

The Board of Management of Pharming Group N.V.

### **C1INH**

C1 esterase inhibitor or C1INH is a serine protease inhibitor protein present in human blood serum. C1INH is involved in the regulation of the first protein in the complement system (C1), which is part of the immune system. Insufficient C1 inhibitor action or amounts can cause inflammation and HAE attacks.

### **CHMP**

The Committee for Medicinal Products for Human Use (CHMP) plays a vital role in the marketing procedures for medicines in the European Union. Amongst others, the CHMP is responsible for preparing the EMA's opinions on all questions concerning medicinal products for human use, in accordance with Regulation (EC) No 726/2004.

### **Clinical trial/studies**

Clinical trials are tests on human individuals, ranging from healthy people to patients, to evaluate safety and efficacy of new pharmaceutical products before they can be approved. Clinical trials typically range from Phase I to Phase IV and even V.

### **CMO**

A Contract Manufacturing Organisation (CMO) is an organisation that provides clients from the pharmaceutical industry with comprehensive services from drug development through manufacture.

## ***Glossary continued***

### **DGF**

DGF or delayed graft function is a common complication affecting all solid organs in the post-transplant period. DGF results in significant morbidity and mortality from early graft dysfunction and from decreased long-term graft survival. The condition also prolongs hospitalisation and requires substitute therapies for these patients, such as dialysis or ventilation support. DGF remains a critical unmet medical need despite improvements in immunosuppression, organ preservation, and surgical technique. C1 inhibitor has been shown in numerous models of organ transplantation to improve early graft function. In the USA alone, over 25,000 solid organs were transplanted in 2005, including kidney, liver, lung and heart transplants.

### **EGM**

Extraordinary General Meeting of Shareholders.

### **EMA**

The European Medicines Agency (EMA) is the regulatory office for pharmaceuticals in the European Union and is responsible for approving new drugs prior to marketing of the product ensuring their safety and efficacy.

### **FDA**

The FDA or Food and Drug Administration is the regulatory office responsible for drug approval in the United States.

### **GMP**

GMP status or Good Manufacturing Practice is a term that is recognised worldwide for the control and management of manufacturing and quality control testing of foods and pharmaceutical products.

### **HAE**

HAE or Hereditary Angioedema is a human genetic disorder caused by insufficient activity of the C1 inhibitor protein. HAE patients suffer from recurrent unpredictable acute attacks of painful and in some cases fatal swelling of soft tissues (edema), including regions of the skin, abdomen and the mouth and throat. Attacks can last up to five days when untreated. In the Western world, approximately 1 in 30,000 individuals suffers from Hereditary Angioedema, having an average of seven acute attacks per year.

### **HAEI**

Hereditary Angioedema International (patient organisation).

### **hLF**

Human lactoferrin is a natural protein that helps to fight and prevent infections. The protein is present in substantial quantities in mother's milk and plays an important role in the defense system of infants. The protein is also present in various body fluids and continues to play an important role against a wide range of bacterial, fungal and viral pathogens in adults. Pharming produces a recombinant version of the natural lactoferrin protein.

### **IFRS, IAS and IASB**

International Financial Reporting Standards (IFRS) along with International Accounting Standards (IAS) are a set of accounting standards issued by the International Accounting Standards Board (IASB).

## ***Glossary continued***

### **IND**

An IND (investigational new drug application) is the vehicle through which a sponsor advances to the next stage of drug development known as clinical trials (human trials).

### **IRI**

Ischaemia Reperfusion Injury (IRI) is a complication arising from lack of oxygen due to an interruption of the blood supply (ischaemia) resulting in tissue damage. This can occur in a transplanted organ, in the brain in case of stroke, and in the heart in case of myocardial infarction ('heart attack').

### **LTIP**

Pharming's Long Term Incentive Plan.

### **MAA**

A Marketing Authorisation Application is a request for market approval in the European Union.

### **Orphan Drug**

A drug being developed to treat a rare disease (affecting less than 200,000 individuals in the USA) can receive Orphan Drug designation from the FDA. This status is granted under the US Orphan Drug Act of 1983, which was established to encourage, support and protect the development of treatment for rare, but serious diseases. Orphan Drug status provides several advantages including market exclusivity for seven years, various financial incentives and a well-defined regulatory approval path. The EMA can grant a similar status to products being developed to treat rare diseases (affecting not more than five in ten thousand persons in Europe), namely Orphan Medicinal Product. This status is granted under European Parliament and Council Regulation (EC) No 141/2000 of 16 December, 1999, on Orphan Medicinal Products, which introduces incentives for Orphan Medicinal Products research, development and marketing, in particular by granting exclusive marketing rights for a ten-year period.

### **POC**

A Proof of Concept (POC) is a study to verify that a concept or theory has the potential of being used.

### **Protein**

Proteins are large organic molecules, like C1 inhibitor, fibrinogen and collagen, and form the basis to all living organisms. They are composed of one or more chains of amino acids joined together by peptide bonds. The sequence of these amino acids is defined by genes, which are present in the DNA.

### **Recombinant**

Recombinant refers to the combination of genetic material (DNA) from different biological sources. Pharming, like all biotechnology firms, uses recombinant technology to produce proteins such as recombinant human C1 inhibitor.

### **rhC1INH**

Recombinant human C1 esterase inhibitor or rhC1INH is the active component of Ruconest®/Rhucin®. Natural C1 inhibitor DNA from a human source is used in Pharming's protein production technology to ensure expression of the C1 inhibitor protein. This product might be useful for certain indications, such as the prevention of complications that sometimes arise after organ transplantation.

## ***Glossary continued***

### **rhFVIII**

Recombinant human Factor VIII is a natural human blood clotting factor and is in early-stage development for treatment of Haemophilia A. Haemophilia A is a hereditary disorder caused by defects in the Factor VIII gene. Lack of functional Factor VIII diminishes the body's clotting ability, which in turn can lead to damaging- or fatal bleeding episodes. On this project, Pharming has a service agreement with Renova Life.

### **Rhucin®**

Rhucin® is the global registered trade mark for Pharming's recombinant human C1 inhibitor and has been renamed **Ruconest®**

### **RLI**

Renova Life, Inc.

### **Ruconest®**

Ruconest® is the global registered trade mark for Pharming's recombinant human C1 inhibitor. Human C1 inhibitor is a protein involved in the regulation of the first protein in the complement system (C1), which is part of the immune system. Insufficient C1 inhibitor action or amounts can cause inflammation and HAE attacks.

### **Sobi**

Swedish Orphan Biovitrum International AB.

### **SPA**

A Special Protocol Assessment (SPA) is a declaration from the FDA that an uncompleted Phase III trial's design, clinical endpoints, and statistical analyses are acceptable for FDA approval.

### **Transgenic**

An organism is called transgenic when its cells carry genetic material from another species in addition to its own genetic material. Pharming produces specific human products in the milk of transgenic rabbits and cows carrying the human recombinant gene responsible for expressing that product.

### **VWAP**

Volume Weighted Average Price of shares.

## Consolidated financial statements



## CONSOLIDATED STATEMENT OF FINANCIAL POSITION

For the year ended December 31

Amounts in €'000	Notes	2012	2011
Intangible assets	4	535	987
Property, plant and equipment	5	7,128	9,567
Restricted cash	6	732	979
<b>Non-current assets</b>		<b>8,395</b>	<b>11,533</b>
Inventories	7	2,101	6,580
Assets held for sale	8	242	-
Trade and other receivables	9	524	2,495
Restricted cash	6	309	309
Cash and cash equivalents	6	5,273	3,777
<b>Current assets</b>		<b>8,449</b>	<b>13,161</b>
<b>Total assets</b>		<b>16,844</b>	<b>24,694</b>
Share capital	10	10,092	20,405
Share premium	10	231,866	224,495
Other reserves	10	14,144	12,325
Accumulated deficit	10	(263,754)	(258,413)
<b>Shareholders' equity</b>		<b>(7,652)</b>	<b>(1,188)</b>
Deferred license fees income	11	13,495	15,431
Finance leases liabilities	12	1,961	2,215
Other liabilities		72	101
<b>Non-current liabilities</b>		<b>15,528</b>	<b>17,747</b>
Deferred license fees income	11	1,936	1,936
Derivative financial liabilities	13	1,215	1,171
Restructuring provision	14	1,232	-
Trade and other payables	15	3,690	3,810
Finance lease liabilities	12	895	1,218
<b>Current liabilities</b>		<b>8,968</b>	<b>8,135</b>
<b>Total equity and liabilities</b>		<b>16,844</b>	<b>24,694</b>

*The notes are an integral part of these financial statements.*

## CONSOLIDATED STATEMENT OF INCOME

For the year ended December 31

Amounts in €'000

	Notes	2012	2011
<b>Continuing operations:</b>			
License fees	16	9,815	1,936
Product sales	16	798	1,063
<b>Revenues</b>		<b>10,613</b>	<b>2,999</b>
Costs of product sales	18	(1,126)	(1,814)
Inventory impairments	18	(3,141)	(1,716)
<b>Gross profit/(loss)</b>		<b>6,346</b>	<b>(531)</b>
Income from grants	17	250	196
<b>Other income</b>		<b>250</b>	<b>196</b>
Research and development	18	(19,350)	(13,830)
General and administrative	18	(3,080)	(3,262)
Impairment charges	19	(1,257)	(35)
Share-based compensation	24	(370)	(1,039)
<b>Costs</b>		<b>(24,057)</b>	<b>(18,166)</b>
<b>Loss from operating activities</b>		<b>(17,461)</b>	<b>(18,501)</b>
Fair value gain derivatives	13	1,283	1,026
<b>Financial income</b>		<b>1,283</b>	<b>1,026</b>
Effective interest convertible bonds	13	(2,353)	-
Settlement convertible bonds	13	(2,757)	-
Result equity working capital facility	10	(673)	-
Recycling equity translation reserve	10	(1,384)	-
Other interest expenses, net	20	(242)	(213)
Foreign currency results	21	(218)	(49)
Other financial expenses	22	(288)	(106)
<b>Financial expenses</b>		<b>(7,915)</b>	<b>(368)</b>
<b>Net loss from continuing operations</b>		<b>(24,093)</b>	<b>(17,843)</b>
Net profit from discontinued operations	23	-	643
<b>Net loss</b>		<b>(24,093)</b>	<b>(17,200)</b>
<b>Attributable to:</b>			
Net loss from continuing operations		(24,093)	(17,843)
Net profit from discontinued operations	23	-	739
<b>Owners of the parent</b>		<b>(24,093)</b>	<b>(17,104)</b>
Net loss from continuing operations		-	-
Net profit from discontinued operations	23	-	(96)
<b>Non-controlling interest</b>		<b>-</b>	<b>(96)</b>
<b>Share information:</b>			
Weighted average shares outstanding	33	72,977,269	47,022,400
<b>Basis loss per share (€), of which:</b>		<b>(0.330)</b>	<b>(0.364)</b>
From continuing operations (€)		(0.330)	(0.379)
From discontinued operations (€)		-	0.015

*The notes are an integral part of these financial statements.*

## CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME

For the year ended December 31

Amounts in €'000	Notes	2012	2011
<b>Net loss for the year</b>		<b>(24,093)</b>	<b>(17,200)</b>
Foreign currency translation	10	65	65
<b>Other comprehensive income, net of tax</b>		<b>65</b>	<b>65</b>
<b>Total recognized income and expense</b>		<b>(24,028)</b>	<b>(17,135)</b>
<b>Attributable to:</b>			
Equity owners of the parent		(24,028)	(17,039)
Non-controlling interest		-	(96)

*The notes are an integral part of these financial statements.*

## CONSOLIDATED STATEMENT OF CASH FLOWS

For the year ended December 31

Amounts in €'000	Notes	2012	2011
Receipts from license partners	6, 11	9,069	814
Receipt of Value Added Tax		1,163	1,162
Interest received		18	1
Receipt of grants		72	384
Other receipts		829	240
Payments of third party fees and expenses, including Value Added Tax		(14,941)	(12,663)
Net compensation paid to (former) board members and (former) employees		(3,285)	(3,790)
Payments of pension premiums, payroll taxes and social securities, net of grants settled		(2,983)	(3,078)
Other payments		(212)	-
<b>Net cash flows used in operating activities</b>	<b>6</b>	<b>(10,270)</b>	<b>(16,930)</b>
Proceeds of sale of assets	5, 6	722	-
Purchase of property, plant and equipment	6	(614)	(1,058)
Deconsolidation of DNage		-	(40)
<b>Net cash flows from/(used in) investing activities</b>	<b>6</b>	<b>108</b>	<b>(1,098)</b>
Proceeds of equity and warrants issued	6, 10	5,340	13,198
Proceeds of convertible bonds issued	6, 10	8,000	-
Receipt from financial lease transaction	6	-	618
Payments of transaction fees and expenses	10	(931)	(369)
Payments of finance lease liabilities	12	(838)	(790)
<b>Net cash flows from financing activities</b>	<b>6</b>	<b>11,571</b>	<b>12,657</b>
<b>Increase/(decrease) of (restricted) cash</b>	<b>6</b>	<b>1,409</b>	<b>(5,371)</b>
Exchange rate effects on (restricted) cash	6	(160)	(42)
(Restricted) cash at January 1	6	5,065	10,478
<b>(Restricted) cash at December 31</b>	<b>6</b>	<b>6,314</b>	<b>5,065</b>

*The notes are an integral part of these financial statements.*

## CONSOLIDATED STATEMENT OF CHANGES IN EQUITY

For the year ended December 31

Amounts in €'000	Notes	Attributable to owners of the parent			
		Number of shares	Share capital	Share premium	Other reserves
<b>Balance at January 1, 2011</b>		<b>436,261,010</b>	<b>17,450</b>	<b>219,220</b>	<b>15,407</b>
Total recognized income and expense		-	-	-	65
Deconsolidation of DNage B.V.	10, 23	-	-	-	-
Share-based compensation	10, 24	-	-	-	1,039
Bonuses settled in shares	10	515,837	21	82	-
Shares/warrants issued for cash	10, 28	29,000,000	1,160	304	-
Warrants exercised	10	24,339,623	974	4,186	(4,186)
Advance shares issued	10, 13	20,000,000	800	703	-
<b>Balance at December 31, 2011</b>		<b>510,116,470</b>	<b>20,405</b>	<b>224,495</b>	<b>12,325</b>
Total recognized income and expense		-	-	-	65
Recycling equity translation reserve	10	-	-	-	1,384
Share-based compensation	10, 24	-	-	-	370
Bonuses settled in shares	10	3,950,211	157	117	-
Bond payments in shares	10, 13	210,181,995	5,432	4,492	-
Shares/warrants issued for cash	10	258,768,453	2,588	2,157	-
Warrants exercised	10, 28	26,171,968	262	605	-
Adjustment nominal value per share	10	-	(18,752)	-	-
<b>Balance at December 31, 2012</b>		<b>1,009,189,097</b>	<b>10,092</b>	<b>231,866</b>	<b>14,144</b>

*The notes are an integral part of these financial statements.*

Amounts in €'000	Attributable to owners of the parent		Non-controlling interest	Total equity
	Accumulated deficit	Total		
<b>Balance at January 1, 2011</b>	<b>(241,213)</b>	<b>10,864</b>	<b>(764)</b>	<b>10,100</b>
Total recognized income and expense	(17,200)	(17,135)	-	(17,135)
Deconsolidation of DNage B.V.	-	-	764	764
Share-based compensation	-	1,039	-	1,039
Bonuses settled in shares	-	103	-	103
Shares/warrants issued for cash	-	1,464	-	1,464
Warrants exercised	-	974	-	974
Advance shares issued	-	1,503	-	1,503
<b>Balance at December 31, 2011</b>	<b>(258,413)</b>	<b>(1,188)</b>	<b>-</b>	<b>(1,188)</b>
Total recognized income and expense	(24,093)	(24,028)	-	(24,028)
Recycling equity translation reserve	-	1,384	-	1,384
Share-based compensation	-	370	-	370
Bonuses settled in shares	-	274	-	274
Bond payments in shares	-	9,924	-	9,924
Shares/warrants issued for cash	-	4,745	-	4,745
Warrants exercised	-	867	-	867
Adjustment nominal value per share	18,752	-	-	-
<b>Balance at December 31, 2012</b>	<b>(263,754)</b>	<b>(7,652)</b>	<b>-</b>	<b>(7,652)</b>

*The notes are an integral part of these financial statements.*

## **Notes to the consolidated financial statements**

For the year ended December 31, 2012

### **1. Corporate information**

The consolidated financial statements of Pharming Group N.V., Leiden for the year ended December 31, 2012 were authorized for issue in accordance with a resolution of the Board of Supervisory Directors on March 29, 2013. The financial statements are subject to approval of the Annual General Meeting of Shareholders, which has been scheduled for May 15, 2013.

Pharming Group N.V. is a limited liability public company which is listed on NYSE Euronext Amsterdam, with its headquarters and registered office located at:

Darwinweg 24  
2333 CR Leiden  
The Netherlands

Pharming focuses on the development, production and commercialization of human therapeutic proteins to be used in highly innovative therapies. The Company's products are aimed at treatments for genetic disorders and surgical and traumatic bleeding. Pharming's technologies include novel transgenic platforms for the production of biopharmaceuticals, as well as technology and processes for the purification and formulation of these biopharmaceuticals.

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

#### **2.1 Basis of preparation**

The consolidated financial statements of the Company have been prepared in accordance with International Financial Reporting Standards (IFRS) for the financial year 2012 issued by the International Accounting Standards Board (IASB) as adopted by the European Union. In conformity with article 402 Book 2 of the Netherlands Civil Code, a condensed statement of income is included in the Pharming Group N.V. accounts.

The principle accounting policies applied in the preparation of these consolidated financial statements are set out below. These policies have been consistently applied to all years presented, unless otherwise stated.

The consolidated financial statements have been prepared under the historical cost convention, unless otherwise stated in this summary of significant accounting policies.

#### **2.2 Basis of consolidation**

The consolidated financial statements include Pharming Group N.V. and its effectively controlled subsidiaries, after the elimination of all intercompany transactions and balances. Subsidiaries are consolidated from the date the acquirer obtains effective control until such time as control ceases.

## **Notes to the consolidated financial statements continued**

An entity is considered effectively controlled if the Company, directly or indirectly, has more than half of the voting power in the entity, unless it can be clearly demonstrated that such ownership does not constitute control. Control also exists when the Company, directly or indirectly, owns half or less of the voting power of an entity but can clearly demonstrate it has power:

- over more than half of the voting rights by virtue of an agreement with other investors;
- to govern the financial and operating policies of the entity under a statute or an agreement;
- to appoint or remove the majority of the Members of the Board of Directors or equivalent governing body and control of the entity is by that board or body; or
- to cast the majority of votes at meetings of the board of directors or equivalent governing body and control of the entity is by that board or body.

Acquisitions of subsidiaries are accounted for using the acquisition method of accounting. The financial statements of the subsidiaries are prepared for the same reporting year as Pharming Group N.V., using the same accounting policies. Intercompany transactions, balances and unrealized gains and losses on transactions between group companies are eliminated.

Investments in companies in which Pharming does not control or have significant influence on the financial and the operational decisions are classified as (available-for-sale) financial assets. In accordance with IAS 39 (Financial instruments), these investments are carried at fair value. Profit or loss and each component of other comprehensive income are attributed to the owners of the parent and to the non-controlling interests. Total comprehensive income is attributed to the owners of the parent and to the non-controlling interests even if this results in the non-controlling interests having a deficit balance.

The following table provides an overview of the investments at December 31, 2012:

<b>Entity</b>	<b>Registered office</b>	<b>Investment %</b>
Pharming B.V.	The Netherlands	100.00
Pharming Intellectual Property B.V.	The Netherlands	100.00
Pharming Technologies B.V.	The Netherlands	100.00
Broekman Instituut B.V.	The Netherlands	100.00
DNage B.V.	The Netherlands	51.00
Pharming Healthcare, Inc.	United States	100.00
ProBio, Inc.	United States	100.00

### **2.3 Significant accounting judgments and estimates**

The preparation of financial statements requires judgments and estimates that affect the reported amounts of assets and liabilities, revenues and expenses, and related disclosure of contingent assets and liabilities at the date of the Financial Statements. The resulting accounting estimates will, by definition, seldom equal the related actual results. The estimates and assumptions that have a significant risk of causing a material adjustment to the carrying amounts of assets and liabilities within the next financial year are addressed below.



## **Notes to the consolidated financial statements continued**

### **Property, plant and equipment**

Pharming at year end 2012 has property, plant and equipment with a carrying value of €7.1 million. These assets are dedicated to the production of Ruconest® inventories (€6.0 million) and other corporate purposes (€1.1 million). It is assumed these asset groups will continue to be used in ongoing production, research and development or general and administrative activities over its anticipated lifetime. The carrying value of these assets may be impaired in 2013 (or the years beyond) in case of a decision to cancel and/or defer certain activities.

### **Inventories**

At year end 2012, the Company has capitalized rhC1INH product and milk with an aggregate carrying value of €2.1 million. The Company has planned for additional inventory investments after the end of the reporting year. These inventories are available for use in commercial, preclinical and clinical activities. Estimates have been made with respect to the ultimate use or sale of the product, taking into account current and expected preclinical and clinical programs for both the HAE project and other indications of the rhC1INH product as well as anticipation of market approval(s). In doing so, best estimates have been made with respect to the timing of such events in view of both the existing and expected lifetimes of the product involved.

Due to the early stage commercialization cycle of Ruconest® the actual cash proceeds from these product sales are currently difficult to predict in terms of volumes, timing and reimbursement amounts. In addition, further inventory investments and execution of preclinical and clinical activities are subject to availability of sufficient financial resources.

### **Derivative financial liabilities**

The Company at year end 2012 has presented derivative financial liabilities with a carrying value of €1.2 million. These liabilities represent the fair values of warrant rights and are based on models using assumptions with respect to, amongst others, the exercise of the warrants on or before maturity dates as well as (historical) volatility. Actual share price developments may trigger exercise of these warrants on a different moment than anticipated in the model and also cause transfer of assets to warrant holders under conditions that are (much) more or (much) less favorable than anticipated at December 31, 2012. As a result, the difference between the value of assets transferred to warrant right holders upon exercise and the carrying value at year end 2012 as charged to the statement of income may be material.

Share price developments may also result in the warrants expiring unexercised while the fair value of warrants unexercised may fluctuate (significantly) until expiration. Fair value changes of warrant rights unexercised between December 31, 2012 and subsequent reporting dates are charged to the statement of income. A sensitivity analysis on the possible effects has been included in Note 32 of these consolidated financial statements.

## **Notes to the consolidated financial statements continued**

### **2.4 Accounting policies**

#### **Foreign currency translation**

Items included in the financial statements of each of the group's entities are measured using the currency of the primary economic environment in which the entity operates ('the functional currency'). The consolidated financial statements are presented in Euros, which is the Company's functional and presentation currency. Non-monetary items that are measured in terms of historical cost in a foreign currency are translated using the exchange rates as at the dates of the initial transactions. Monetary assets and liabilities denominated in foreign currencies are translated to the functional currency (generally Euros) using exchange rates prevailing at the date of the transaction. Transactions executed in foreign currencies are translated at the exchange rate at the date of transaction. The resulting transaction gains or losses are recognized in the statement of income. Assets and liabilities of foreign entities are translated to Euros using year-end spot foreign exchange rates. The statements of income of foreign entities are translated at weighted average exchange rates for the year. The effects of translating these operations are taken directly to other comprehensive income within equity. On disposal of a foreign entity, the accumulated exchange difference is recognized in the statement of income as a component of the gain or loss on disposal. In general, the above-stated translation of foreign entities applies to the entities in the United States. The €/US\$ exchange rates applied at December 31, 2012 amounted to €0.759 (December 31, 2011: €0.773).

#### **Distinction between current and non-current**

An asset is classified as current when it is expected to be realized (settled) within twelve months after the end of the reporting year. Liabilities are classified as current liabilities unless the group has an unconditional right to defer settlement of the liability for at least 12 months after the end of the reporting year.

#### **Intangible assets**

##### **General**

Intangible assets acquired separately are measured on historical cost. The cost of intangible assets acquired in a business combination is recognized and measured at fair value as at the date of acquisition. Following initial recognition, intangible assets are carried at cost less any accumulated amortization and any accumulated impairment losses.

Intangible assets with finite lives are amortized over the useful life and assessed for impairment whenever there is an indication that the intangible assets may be impaired. Changes in the expected useful life or the expected pattern of consumption of future economic benefits embodied in the asset is accounted for by changing the amortization period or method, as appropriate, and treated as changes in accounting estimates. The amortization expense on intangible assets with finite lives is recognized in the statement of income in the relevant expense category consistent with the function of the intangible asset.

Intangible assets with indefinite useful lives are tested for impairment annually either individually or at the cash-generating unit level. Such intangibles are not amortized. The useful life of an intangible asset with an indefinite life is reviewed annually to determine whether indefinite life assessment continues to be supportable. If not, the change in the useful life assessment from indefinite to finite is made on a prospective basis.

## Notes to the consolidated financial statements continued

The remaining amortization periods for intangible assets at December 31, 2012 are:

Category	Description	Remaining amortization period
Transgenic technology	Patents and licenses	2 years
Ruconest® for HAE (EU)	Development costs	8 years
ProBio technology	Patents and licenses	Not applicable*

\* intangible assets with carrying value at December 31, 2012 of €nil

### Research and development costs

Research expenditure is recognized as an expense in the period in which it is incurred. An intangible asset arising from development expenditure on an individual project is recognized only when the Company can demonstrate the technical feasibility of completing the intangible asset so that it will be available for use or sale, its intention to complete and its ability to use or sell the asset, how the asset will generate future economic benefits, the availability of resources to complete and the ability to measure reliably the expenditure during the development. Technical feasibility and ability to use or sell the asset are, in general, considered probable when the Company estimates that obtaining marketing approval is deemed likely.

Following the initial recognition of the development expenditure, the cost model is applied requiring the asset to be carried at cost less any accumulated amortization and accumulated impairment losses. Any expenditure capitalized is amortized over the period of expected useful life of the related patents. The carrying value of development costs is reviewed for impairment annually when the asset is not yet in use or more frequently when an indication of impairment arises during the reporting year.

### Property, plant and equipment

Property, plant and equipment is stated at cost less accumulated depreciation charges and accumulated impairment charges. Generally, depreciation is calculated using a straight-line basis over the estimated useful life of the asset. The carrying values of property, plant and equipment are reviewed for impairment when events or changes in circumstances indicate that the carrying value may not be recoverable.

An item of property, plant and equipment is derecognized upon disposal or when no future economic benefits are expected from its use or disposal. Any gain or loss arising on derecognizing of the asset (calculated as the difference between the net disposal proceeds and the carrying amount of the asset) is included in the statement of income in the year the asset is derecognized. Residual values, useful lives and depreciation methods are reviewed, and adjusted if appropriate, at each financial year-end.

The depreciation periods for property, plant and equipment are:

Land	not depreciated
Land improvements	20 years
Operational facilities	10-20 years
Leasehold improvements	5-10 years
Manufacturing equipment (or less, based on actual use compared to standards)	5-10 years
Assets under construction	not depreciated
Other	3-10 years

## **Notes to the consolidated financial statements continued**

Depreciation charges for manufacturing equipment are based on actual use of the equipment involved, which is expected to take place in a period of no more than five years in view of technical expiration. Assets under construction involves assets not ready for use and thus these are not depreciated until the item is ready for use and reclassified to the applicable category of assets in use. Other property, plant and equipment apply to laboratory and office equipment, furniture, hardware and software.

### **Impairment of assets**

Assets that have an indefinite useful life are not subject to amortization and are tested annually for impairment. Assets that are subject to amortization are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount may not be recoverable. An impairment loss is recognized for the amount by which the asset's carrying amount exceeds its recoverable amount. The recoverable amount is the higher of an asset's fair value less costs to sell and value in use. For the purposes of assessing impairment, assets are grouped at the lowest levels for which there are separately identifiable cash flows (cash-generating units). Non-financial assets that suffered impairment are reviewed for possible reversal of the impairment at each reporting date.

### **Inventories**

Inventories are carried at the lower of cost and net realizable value. The Company has two inventory categories:

- batches rhC1INH. These batches are comprised of therapeutic product available for sales, clinical development and preclinical activities. Initial recognition is at cost, including skimmed milk used, external manufacturing fees and fill and finish costs incurred to bring the product in a saleable or useable position;
- skimmed milk. This item serves as a raw material for the batches rhC1INH. Valuation per unit skimmed milk is based on the total costs of the rabbit facilities and the actual production levels.

Costs are determined applying the weighted average cost formula. Net realizable value is the estimated selling price in the ordinary course of business, less estimated costs of completion and the estimated costs necessary to make the sale. An allowance is provided for inventories if no future use or sale is expected before the expiration date.

### **Financial assets**

Financial assets are classified as financial assets at fair value through profit or loss, held-to-maturity financial assets, loans and receivables, and available-for-sale financial assets, as appropriate. The Company determines the classification of its financial assets at initial recognition. When financial assets are recognized initially, they are measured at fair value, plus, in the case of investments not at fair value through profit or loss, directly attributable transaction costs.

Financial assets include investments in companies other than subsidiaries and associates, financial receivables held for investment purposes and other securities. Purchases and sales of financial assets are recognized using settlement date accounting.

### **Financial assets at fair value through profit or loss**

This category has two subcategories: financial assets held for trading and those designated at fair value through profit or loss at inception. A financial asset is classified in this category if acquired principally for the purpose of selling in the short term or if so designated by the Board of Management.

## **Notes to the consolidated financial statements continued**

### **Loans and receivables**

Loans and receivables are financial assets with fixed or determinable payments not quoted in an active market and created by Pharming by providing money, goods or services directly to a debtor, other than:

- Those Pharming intends to sell immediately or in the short term, which are classified as held for trading; and
- Those for which Pharming may not recover substantially all of its initial investment, other than because of credit deterioration, which are classified as available for sale.

Loans and receivables are carried at amortized cost, or cost if no maturity, less an allowance for uncollectibility. They are included in current assets, except for maturities greater than 12 months after the end of the reporting year.

### **Available-for-sale financial assets**

Available-for-sale financial assets are those non-derivative financial assets that are designated as available-for-sale or are not classified in any of the other three categories (financial assets at fair value through profit or loss; held-to-maturity investments; loans and receivables) in the scope of IAS 39 (Financial instruments: recognition and measurement). After initial recognition, available-for-sale financial assets are measured at fair value with gains or losses being recognized as a separate component of equity until the investment is derecognized or until the investment is determined to be impaired, at which time the accumulated gain or loss previously reported in equity included in the statement of income.

The fair value of investments that are actively traded in organized financial markets is determined by reference to quoted market bid prices at the close of business on the end of the reporting year. For investments where there is no active market, fair value is determined using valuation techniques. Such techniques include using recent arm's length market transactions; reference to the current market value of another instrument, which is substantially the same; discounted cash flow analysis and option pricing models.

### **Impairment of financial assets**

The Company assesses at each end of the reporting year whether there is any objective evidence that a financial asset or a group of financial assets, other than those carried at fair value through profit or loss, is impaired, which is deemed the case if there is objective evidence as a result of one or more events that has occurred after the initial recognition of the asset and that has an impact on the estimated future cash flows of the financial asset or the group of financial assets that can be reliably estimated. For available-for-sale financial assets, objective evidence of impairment includes a significant or prolonged decline in the fair value of the investment below its cost as well as other facts and circumstances such as the financial position of the asset as per (interim) financial information and credit ratings.

### **Trade and other receivables**

Trade and other receivables are initially stated at fair value. Subsequent measurement is at amortized cost using the effective interest method less provision for impairment.

### **Assets held for sale and discontinued operations**

Non-current assets or disposal groups comprising assets and liabilities that are expected to be recovered primarily through a sales transaction rather than through continuing use are classified as assets held for sale. They are stated at the lower of carrying amount and fair value less costs to sell. Impairment losses on initial classification as held for sale are included in the statement of income. The same applies to gains and losses on subsequent measurement. Gains are not recognized in excess of any accumulated impairment loss.

A discontinued operation is a component of Pharming's business that represents a separate major line of business. Classification as a discontinued operation occurs upon disposal or earlier when the operation meets the criteria to be classified as held for sale. When an operation is classified as a discontinued operation, the comparative statement of income is restated as if the operation had been discontinued from the start of the comparative period.

## ***Notes to the consolidated financial statements continued***

Once classified as held for sale, intangible assets and property, plant and equipment are no longer amortized or depreciated.

### **Cash and cash equivalents**

Cash and cash equivalents are defined as cash on hand, demand deposits and short-term, highly liquid investments (maturity less than 3 months) readily convertible to known amounts of cash and subject to insignificant risk of changes in value. Bank overdrafts are shown within borrowings in current liabilities on the statement of financial position. For the purpose of the statement of cash flow, cash and cash equivalents are net of outstanding bank overdrafts.

### **Equity**

The Company only has ordinary shares and these are classified within equity upon issue. Shares transferred in relation to settlement of (convertible) debt and derivative financial liabilities are measured at fair value with fair value based on the closing price of the shares on the trading day prior to the settlement date. Equity is recognized upon the issue of fixed warrants with a fixed exercise price as well as upon the recognition of share-based payment expenses; shares issued upon exercise of such warrants or options are measured at their exercise price.

Transaction costs associated with an equity transaction are accounted for as a deduction from equity to the extent they are incremental costs directly attributable to the equity transaction that otherwise would have been avoided. The costs of an equity transaction that is to be abandoned are recognized as an expense. Transaction costs related to the issue of a compound financial instrument are allocated to the liability and equity components of the instruments in proportion to the allocation of proceeds.

### **Financial liabilities and borrowings**

Financial liabilities within the scope of IAS 39 are classified as either financial liabilities at fair value through profit or loss (derivative financial liabilities) or financial liabilities at amortized cost (borrowings and trade and other payables). All loans and borrowings are initially recognized at the fair value of the consideration received less directly attributable transaction costs; transaction costs related to the issue of a compound financial instrument are allocated to the liability and equity components of the instruments in proportion to the allocation of proceeds. After initial recognition, interest-bearing loans and borrowings are subsequently measured at amortized cost using the effective interest method. Gains and losses are recognized in the statement of income when the liabilities are derecognized as well as through the amortization process. Purchases and sales of financial liabilities are recognized using settlement date accounting.

### **Provisions**

Provisions are recognized when there is a present obligation (legal or constructive) as a result of a past event, it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation and a reliable estimate of the obligation can be made. The expense relating to any provision is presented in the statement of income net of any reimbursement. If the effect of the time value of money is significant, provisions are discounted. When discounting is used, the increase in the provision due to the passage of time is recognized as a financial expense.

### **Derivative financial liabilities**

Derivative financial liabilities are initially recognized at fair value and subsequently measured at fair value through profit or loss with changes in the fair value recognized in the statement of income as they arise.

### **Trade and other payables**

Trade and other payables are initially stated at fair value. Subsequent measurement is at amortized cost using the effective interest method.

## ***Notes to the consolidated financial statements continued***

### **Derecognizing financial assets and liabilities**

#### **Financial assets**

A financial asset (or, where applicable a part of a financial asset or part of a group of similar financial assets) is derecognized where:

- the rights to receive cash flows from the asset have expired;
- the Company retains the right to receive cash flows from the asset, but has assumed an obligation to pay them in full without material delay to a third party under a 'pass-through' arrangement; or
- the Company has transferred its rights to receive cash flows from the asset and either (i) has transferred substantially all the risks and rewards of the asset, or (ii) has neither transferred nor retained substantially all the risks and rewards of the asset, but has transferred control of the asset.

Where the Company has transferred its rights to receive cash flows from an asset and has neither transferred nor retained substantially all the risks and rewards of the asset nor transferred control of the asset, the asset is recognized to the extent of the Company's continuing involvement in the asset. Continuing involvement that takes the form of a guarantee over the transferred asset is measured at the lower of the original carrying amount of the asset and the maximum amount of consideration that the Company could be required to repay.

#### **Financial liabilities**

A financial liability is derecognized when the obligation under the liability is discharged or cancelled or expires. Where an existing financial liability is replaced by another from the same lender on substantially different terms, or the terms of an existing liability are substantially modified, such an exchange or modification is treated as a derecognizing of the original liability and the recognition of a new liability, and the difference in the respective carrying amounts is recognized in the statement of income.

#### **Revenue recognition**

In general, revenue is recognized to the extent that it is probable that the economic benefits will flow to the Company and the amount of revenue and the costs (to be) incurred in the transaction can be measured reliably. Revenue is measured at the fair value of the consideration received excluding discounts, rebates, value added taxes and duties.

#### **License fees and royalties**

Revenue from license agreements is recognized when significant risks and rewards have been transferred to the license fee partner, it is probable that the economic benefits will flow to the Company and the amount of revenue can be measured reliably and no continuing performance obligation exists.

Upfront license fee payments received from third parties under license agreements with a continuing performance obligation are initially recognized as deferred license fee income within the statement of financial position and released to the statement of income in accordance with the substance of the agreement. If no reliable estimate of the Company's performance throughout the remaining license period can be made, the deferred income is equally released as revenues to the statement of income throughout the remaining license period.

## ***Notes to the consolidated financial statements continued***

Certain license agreements provide for additional non-refundable fees to be paid to the Company upon the achievement of (research, development or regulatory) milestones by the Company. These milestones, if deemed substantive (see below), are recognized as revenue when the milestones are achieved and the milestone payments are due and collectible under the terms of the agreement. Milestones are considered substantive if all of the following conditions are met:

- the milestone payments are non-refundable under the terms of the agreement;
- achievement of the milestone involved a degree of risk and was not reasonably assured at the inception of the agreement;
- substantial effort is involved in achieving the milestone;
- the amount of the milestone payment is reasonable in relation to the effort expended or the risk associated with achievement of the milestone; and
- a reasonable amount of time passed between the upfront license fee payment and the first milestone payment as well as between each subsequent milestone payment.

If any of these conditions are not met, the Company recognizes the proportionate amount of the milestone payment upon receipt as revenue that corresponds with the percentage of work already completed. The remaining portion of the milestone payment would be deferred and recognized as revenue as performance obligations are completed.

Royalties on license agreements are recognized on an accrual basis in accordance with the substance of the agreement.

### **Product sales**

Revenues from product sales are recognized when:

- the significant risks and rewards of ownership of the products have been transferred to the buyer;
- the Company does not retain either managerial involvement to the degree usually associated with ownership or effective control over the products sold;
- the amount of revenue and the costs (to be) incurred in the transaction can be measured reliably; and
- it is probable that the economic benefits associated with the transaction will flow to the Company.

Interest income is recognized as interest accrues, using the effective interest method. For the purpose of the consolidated statement of cash flows, interest income derived from cash and cash equivalents have been presented as operating cash flows since the Company considers these interest items as the outcome of working capital management.

### **Other income**

Pharming receives certain grants which support the Company's research efforts in defined research and development projects. These subsidies generally provide for reimbursement of approved costs incurred as defined in various grants. Subsidies are recognized if the Company can demonstrate it has complied with all attached conditions and it is probable that the grant amount will be received.

The Company includes income from grants under 'income from grants' in the statement of income in order to enable comparison of its statement of income with companies in the life sciences sector. Companies in the life sciences sector generally present governmental grants as income since these often are a significant source of income.



## **Notes to the consolidated financial statements continued**

### **Costs**

Costs are expensed as incurred. Costs of research and development cover those activities that are carried out to gain new scientific or technical knowledge and understanding as well as the application of research findings or other knowledge to a plan or design for the production of new or substantially improved products. Costs of a general and administrative nature apply to overhead expenses and expenses incurred to commercialize products.

Interest expense is recognized as interest accrues, using the effective interest method. For the purpose of the consolidated statement of cash flows, interest expense and interest income derived from cash and cash equivalents have been presented as operating cash flows since the Company considers these interest items as a result of working capital management.

### **Short-term employee benefits**

The Company does not provide any benefits based on the statement of income. Bonuses are expensed when there is a present obligation (legal or constructive) as a result of a past event, it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation and a reliable estimate of the obligation can be made.

### **Pension plan**

For all Dutch employees with an indefinite employment contract and who have reached the age of 21 years, the Company participates in defined contribution pension plans with an independent insurance company. Defined contributions are expensed in the year in which the related employee services are rendered.

Employees in the United States are enabled to participate in a 401k plan, which also qualifies as a defined contribution plan. To become an eligible participant, an employee must complete six months of service and attain the age of 21 years. The employer matches 100% of the first 3% the employee contributes to their 401k plan and 50% of any amount over 3% up to 5%. Any employee contribution over 5% is not matched. Costs of the 401k plan are expensed in the year in which the related employee services are rendered.

### **Share-based payment**

The costs of option plans are measured by reference to the fair value of the options on the date on which the options are granted. The fair value is determined using the Black-Scholes model. The costs of these options are recognized in the income statement (share-based compensation) during the vesting period, together with a corresponding increase in equity (other reserves). Share-based payment charges do not affect equity or cash flows in the year of expense since all transactions are equity-settled.

Pharming's employee Option plan states that an employee is entitled to exercise the granted options immediately with a maximum exercise period of five years, but can only transfer the shares acquired upon exercise according to a sliding scale over 48 months: 25% of the options vest one year after date of grant with the remaining 75% vesting in equal parts over the next 36 months. For accounting purposes, the period in which the options become unconditional is defined as the vesting period. As a result of the sliding scale according to which the options become unconditional, graded vesting is applied.

### **Long Term Incentive Plan**

For a limited number of Board Members and officers, performance shares are granted free of charge. A maximum number of predetermined shares vest three years after the grant date, provided that the participant to the Long Term Incentive Plan is still in service (continued employment condition), with actual shares to be transferred based on the relative achievement of Pharming's share price compared to a peer group. The maximum number of shares immediately vests upon a change of control. The fair value is determined using Monte Carlo simulation. The fair value at the grant date includes the market performance condition (relative total shareholder return performance) but excludes the three year service condition.

## ***Notes to the consolidated financial statements continued***

### **Leases**

The determination of whether an arrangement is, or contains a lease is based on the substance of the arrangement and requires an assessment of whether the fulfillment of the arrangement is dependent on the use of a specific asset or assets and the arrangement conveys a right to use the asset.

Finance leases, which transfer to the Company substantially all the risks and benefits incidental to ownership of the leased item, are capitalized at the inception of the lease at the fair value of the leased property or, if lower, at the present value of the minimum lease payments. Lease payments are apportioned between the finance charges and reduction of the lease liability so as to achieve a constant rate of interest on the remaining balance of the liability. Finance charges are charged directly against the statement of income.

Lease agreements in which the lesser effectively retains substantially all the risks and benefits of ownership of the leased item, are classified as operating leases. Operating lease payments are recognized as an expense in the statement of income on a straight-line basis over the lease term.

### **Lease incentives**

In certain lease agreements for property, plant and equipment the lesser funds assets in use and effectively controlled by the Company. Such constructions qualify as a 'lease incentive', in which case the Company fully capitalizes the contribution of the lesser in property, plant and equipment with a corresponding increase in liabilities. The investment is depreciated in accordance with the accounting policies for property, plant and equipment, with the accrued lease incentive released to operational lease charges in the statement of income throughout the lease agreement period and on a straight-line basis. This release in the statement of income therefore matches increased depreciation charges.

### **Taxes**

#### **Current income tax**

Current income tax assets and liabilities for the current and prior periods are measured at the amount expected to be recovered from or paid to the taxation authorities. The income tax rates and income tax laws used to compute the amount are those that enacted or substantively enacted by the end of the reporting year. Current income tax relating to items recognized directly in equity is recognized in equity and not in the statement of income.

Current income tax assets and current income tax liabilities are offset, if a legally enforceable right exists to set off current tax assets against current tax liabilities and the Company intends to either settle on a net basis or to realize the asset and settle the liability simultaneously.

#### **Deferred income tax**

Deferred tax assets and liabilities are recognized for the expected tax consequences of temporary differences between the carrying amounts of assets and liabilities and their tax base. Deferred tax assets and liabilities are measured at the tax rates and under the tax laws that have been enacted or substantially enacted at the end of the reporting year and are expected to apply when the related deferred tax assets are realized or the deferred tax liabilities are settled. Deferred tax assets, including assets arising from losses carried forward, are recognized to the extent that it is probable that future taxable profits will be available against which the deductible temporary differences and unused tax losses can be utilized. Deferred tax assets and liabilities are stated at face value. Deferred income tax relating to items recognized directly in equity is recognized in equity and not in the statement of income.

Deferred tax assets and deferred tax liabilities are offset, if a legally enforceable right exists to set off current tax assets against current tax liabilities and the deferred taxes relate to the same taxable entity and the same taxation authority.

## **Notes to the consolidated financial statements continued**

### **Sales tax**

Revenues, expenses and assets are recognized net of the amount of sales tax, except:

- where the sales tax incurred on a purchase of assets or services is not recoverable from the taxation authority, in which case the sales tax is recognized as part of the cost of acquisition of the asset or as part of the expense item as applicable; and
- receivables and payables that are stated with the amount of sales tax included.

The net amount of sales tax recoverable from, or payable to, the taxation authority is included as part of receivables or payables in the statement of financial position.

### **Cash flow statement**

Operating cash flows in the statement of cash flows are reported using the direct method. Interest income and expense relating to restricted cash, cash and cash equivalents as well as bank overdrafts have been presented as operating cash flows since the Company considers these interest items as the outcome of working capital management. Investing and financing cash flows reflect gross cash receipts and payments with the exception of reclaimable value added tax related to these transactions and which is presented as an operating cash flow.

### **Earnings per share**

Basic earnings per share are calculated based on the weighted average number of ordinary shares outstanding during the period. Diluted earnings per share is computed based on the weighted average number of ordinary shares outstanding including the dilutive effect of shares to be issued in the future under certain arrangements such as option plans, warrants issued and convertible loan agreements.

### **Segment reporting**

Operating segments are reported in a manner consistent with the internal reporting provided to the chief operating decision-maker. The Board of Management, which makes the Company's strategic decisions, has been identified as the chief operating decision-maker responsible for allocating resources and assessing performance of the operating segments.

## **2.5 Effect of new and forthcoming accounting standards**

The IASB and IFRIC have issued new standards, amendments to existing standards and interpretations, some of which are not yet effective or have not yet been endorsed by the European Union. Pharming has introduced standards and interpretations that became effective in 2012. The adoption of these standards and interpretations did not have a material effect on the Company's financial performance or position.

### **Effect of new accounting standards**

No new standards and interpretations became effective as of January 1, 2012 which impact the amounts reported in these consolidated financial statements.

### **Effect of forthcoming accounting standards**

The following new standards and amendments to existing standards are not yet applied by the Company.

The amendments to IAS 1, 'Presentation of Items of Other Comprehensive Income', changes the grouping of items presented in other comprehensive income into items that will be reclassified (or 'recycled') to profit or loss at a future point in time and items that will never be reclassified. The amendment affects presentation only and has no impact on the Company's financial position or performance. It becomes effective for annual periods beginning on or after July 1, 2012 and will therefore be applied from January 1, 2013 onwards.

## **Notes to the consolidated financial statements continued**

Various amendments to IAS 19, 'Employee Benefits', have been introduced, with the most important amendment resulting in elimination of the 'corridor method' under which the recognition of actuarial gains and losses could be deferred. The amendments become effective for annual periods beginning on or after January 1, 2013 and have no impact on the Company's financial position or performance because the Company does not apply defined benefit plans.

IFRS 9, 'Financial Instruments: Classification and Measurement', applies to the classification and measurement of financial assets and financial liabilities as defined in IAS 39. The standard represents the first phase in the work of the IASB to replace IAS 39. Since the standard has not yet been endorsed by the European Union, it is uncertain when it needs to be applied by the Company. The uncertainty with respect to the subsequent phases of the project makes it impossible to quantify the impact of the new standard on the Company's financial position or performance.

IFRS 10, 'Consolidated Financial Statements', establishes a single control model that applies to all entities, including special purpose entities. The standard becomes effective for annual periods beginning on or after January 1, 2013 and has no impact on the Company's financial position or performance.

IFRS 11, 'Joint Arrangements', removes the option to apply proportionate consolidation for joint ventures and mandates the use of the equity method for jointly controlled entities that meet the definition of a joint venture. The introduction of this new standard will not impact Pharming's financial position or performance. The standard becomes effective for annual periods beginning on or after January 1, 2013 and has no impact on the Company's financial position or performance.

IFRS 12, 'Disclosure of Involvement with Other Entities', provides disclosure requirements with respect to interests in subsidiaries, joint arrangements, associates and structured entities. It is the complement of the two new standards discussed in the preceding paragraphs and will become effective for annual periods beginning on or after January 1, 2013; it has no impact on the Company's financial position or performance.

IFRS 13, 'Fair Value Measurement', becomes the single source of guidance in IFRS for all fair value measurements. The standard becomes effective for annual periods beginning on or after January 1, 2013. The impact of this standard on the Company's financial position and performance is not expected to be material because the standard further clarifies requirements that already exist.

New IFRIC interpretations are not expected to have a material effect on the consolidated financial statements.

### **3. Going concern assessment**

The Board of Management of Pharming has, upon preparing and finalizing the 2012 financial statements, assessed the Company's ability to fund its operations for a period of at least one year after the date of signing these financial statements.

Based on the above assessment, the Company has concluded that funding of its operations for a period of at least one year after the date of the signing of these financial statements is realistic and achievable. In arriving at this conclusion, the following main items and assumptions have been taken into account:

- cash and cash equivalents (including restricted cash of €1.0 million), of approximately €19.0 million as per the date of these financial statements; which include the receipt of a net amount of €16.0 million from the issue of convertible short-term bonds, as announced on January 16, 2013;
- the anticipated receipt of US\$5.0 million in cash upon acceptance by the U.S. FDA of the BLA filing. Such acceptance is expected in the third quarter of 2013; and
- the Company's operating cash outflows, its investments in (in)tangible assets as well as its financing payments for one year after the end of the financial statements are expected to be less than €18.0 million. This compares to an outflow of €21.7 million in 2012 (excluding a receipt of €9.1 million from license partners in 2012).

## **Notes to the consolidated financial statements continued**

Pharming has not taken into account other potential sources of cash income, including but not limited to the following:

- under the Equity Working Capital Facility of €10.0 million, the Company has received €4.9 million pursuant to tranches executed in 2012 (see Note 10) and has the ability, if and when needed, to utilize the remaining balance of €5.1 million until expiration of the Equity Working Capital Facility on August 1, 2014. The timing and proceeds from future tranches is subject to various parameters that are partially or entirely beyond control of the Company, including but not limited to (i) the share trading volumes, and (ii) the share price development, and (iii) the calls made by investors subsequent to the issue of draw down shares. However, it is noted that the Company cannot make any draw downs under the Equity Working Capital Facility until the Bonds 2013 (as described in Note 34 of these financial statements) have been fully paid back at the end of the third quarter of 2013;
- proceeds from the exercise of warrants or options outstanding as per the date of these financial statements (see Note 34);
- capital raised by means of an additional capital markets transaction, such as non-dilutive (debt) financing, issuance of equity or a combination thereof. The timing and proceeds from such a transaction are subject to, for instance, market conditions (e.g. the share price in relation to the nominal value per share), availability of assets to secure debt transactions as well as approvals of boards and/or shareholders (e.g. to issue additional shares); and
- receipts from existing or new license partners, other than cash proceeds of US\$5.0 million upon acceptance by the U.S. FDA of the BLA filing as described earlier in this Note.

In addition, the Company may decide to cancel and/or defer certain activities in order to limit cash outflows until sufficient funding is available to resume them. Deferrals substantially relate to the timing of manufacturing-related and/or planned future clinical development activities for additional indications carried out on the initiative of Pharming.

Notwithstanding the above, the Board of Management of the Company emphasizes that the funding of the Company's operations beyond one year after these financial statements is largely affected by its ability to increase product sales and/or license fee payments from both existing and new partnerships to generate positive cash flows in the future.

As per the date of these financial statements, with regards to its ability to generate operating cash flows from product sales and/or license fee payments, the following material uncertainties (individually or combined) have been identified which may cast significant doubt about the Company's future ability to continue as a going concern:

- acceptance by the U.S. FDA of the BLA filing and the subsequent receipt of US\$5.0 million from our US partner Santarus; and/or
- receipt of a US marketing authorization by the U.S. FDA and the subsequent receipt of US\$20.0 million from our US partner Santarus (payment triggered upon the earlier of first commercial sale of Ruconest® in the US or 90 days following receipt of U.S. FDA approval); and/or
- the commercial success of Ruconest® in the US.

Given the dependency of the positive outcome of the factors outlined above there is a material uncertainty which may cast significant doubt about the Company's ability to continue as a going concern.

Overall, based on the outcome of this assessment, these financial statements have been prepared on a going concern basis. Notwithstanding their belief and confidence that Pharming will be able to continue as a going concern, the Board of Management emphasizes that the actual cash flows for various reasons may ultimately (significantly) deviate from their projections. Therefore, in a negative scenario (actual cash inflows less than projected and/or actual cash outflows higher than projected) the going concern of the Company could be at risk.

*Notes to the consolidated financial statements continued*

**4. Intangible assets**

**Movement of intangible assets per category for the financial years 2011 and 2012 was:**

Amounts in €'000	Transgenic technology	Ruconest® for HAE (EU)	ProBio tech- nology	Total
At cost	3,001	528	2,816	6,345
Accumulated:				
Amortization charges	(2,357)	(9)	(1,027)	(3,393)
Impairment charges	-	-	(1,789)	(1,789)
<b>Carrying value at January 1, 2011</b>	<b>644</b>	<b>519</b>	<b>-</b>	<b>1,163</b>
Amortization charges	(123)	(53)	-	(176)
<b>Movement 2011</b>	<b>(123)</b>	<b>(53)</b>	<b>-</b>	<b>(176)</b>
At cost	3,001	528	2,816	6,345
Accumulated:				
Amortization charges	(2,480)	(62)	(1,027)	(3,569)
Impairment charges	-	-	(1,789)	(1,789)
<b>Carrying value at December 31, 2011</b>	<b>521</b>	<b>466</b>	<b>-</b>	<b>987</b>
Amortization charges	(121)	(54)	-	(175)
Impairment charges	(35)	-	-	(35)
Assets held for sale	(242)	-	-	(242)
<b>Movement 2012</b>	<b>(398)</b>	<b>(54)</b>	<b>-</b>	<b>(452)</b>
At cost (*)	2,651	528	2,816	5,995
Accumulated:				
Amortization charges (*)	(2,493)	(116)	(1,027)	(3,636)
Impairment charges	(35)	-	(1,789)	(1,824)
<b>Carrying value at December 31, 2012</b>	<b>123</b>	<b>412</b>	<b>-</b>	<b>535</b>

(\*) the Company in 2012 eliminated assets held for sale at accumulated costs of €350,000 and accumulated depreciation of €108,000

As of year-end 2009 the Company has capitalized development costs in the amount of €48,000 in relation to Ruconest® for HAE in the European Union. In 2010 another €480,000 was capitalized prior to the Marketing Authorization. Following market launch of the product in the fourth quarter of 2010 the amortization of the asset has started and no more development costs have been capitalized.

The carrying value of the ProBio technology is €nil at both year-end 2011 and 2012. The assets involved are maintained and in use with very limited expenses incurred; due to the limited commercial potential the carrying values are in line with future proceeds anticipated.

**Notes to the consolidated financial statements continued**

The Company at year-end 2012 intended the sale of intangible assets with a net carrying value of €242,000. These assets were subsequently presented as assets held of sale (Note 8); the transaction was completed in 2013 for a cash consideration received by the Company of US\$350,000. In addition, Pharming discontinued the use of certain intangible assets linked to the assets to be disposed with a net carrying value of €35,000 and subsequently posted an impairment charge.

**5. Property, plant and equipment**

**Movement of property, plant and equipment for the financial year 2011 was:**

Amounts in €'000	Land and land improvements	Operational facilities	Leasehold improvements	Manufacturing equipment	Assets under construction	Other	Total
At cost	849	5,714	2,524	1,019	2,054	1,339	13,499
Accumulated:							
Depreciation charges	(76)	(2,826)	(1,076)	(304)	-	(933)	(5,215)
Impairment charges	-	-	-	(680)	-	-	(680)
Exchange rate effect	(171)	(708)	-	-	-	(22)	(901)
<b>Carrying value at January 1, 2011</b>	<b>602</b>	<b>2,180</b>	<b>1,448</b>	<b>35</b>	<b>2,054</b>	<b>384</b>	<b>6,702</b>
Investments	-	120	-	-	3,249	288	3,657
Deconsolidation DNage	-	-	-	-	-	(20)	(20)
Depreciation charges	(6)	(269)	(263)	-	-	(257)	(795)
Impairment charges	-	-	-	(35)	-	-	(35)
Exchange rate effect	19	38	-	-	-	-	57
Other movements	-	-	-	5,303	(5,303)	-	-
<b>Movement 2011</b>	<b>13</b>	<b>(111)</b>	<b>(263)</b>	<b>5,268</b>	<b>(2,054)</b>	<b>11</b>	<b>2,865</b>
At cost	849	5,834	2,524	6,322	-	1,607	17,136
Accumulated:							
Depreciation charges	(82)	(3,095)	(1,339)	(304)	-	(1,190)	(6,010)
Impairment charges	-	-	-	(715)	-	-	(715)
Exchange rate effect	(152)	(670)	-	-	-	(22)	(844)
<b>Carrying value at December 31, 2011</b>	<b>615</b>	<b>2,069</b>	<b>1,185</b>	<b>5,303</b>	<b>-</b>	<b>395</b>	<b>9,567</b>

*Notes to the consolidated financial statements continued*

**Movement of property, plant and equipment for the financial year 2012 was:**

Amounts in €'000	Land and land improvements	Operational facilities	Leasehold improvements	Manufacturing equipment	Assets under construction	Other	Total
At cost	849	5,834	2,524	6,322	-	1,607	17,136
Accumulated:							
Depreciation charges	(82)	(3,095)	(1,339)	(304)	-	(1,190)	(6,010)
Impairment charges	-	-	-	(715)	-	-	(715)
Exchange rate effect	(152)	(670)	-	-	-	(22)	(844)
<b>Carrying value at January 1, 2012</b>	<b>615</b>	<b>2,069</b>	<b>1,185</b>	<b>5,303</b>	<b>-</b>	<b>395</b>	<b>9,567</b>
Investments	-	50	-	-	-	45	95
Divestments	(601)	(101)	-	-	-	-	(702)
Depreciation charges	(3)	(223)	(263)	(46)	-	(128)	(663)
Impairment charges	-	(1,198)	-	-	-	(24)	(1,222)
Exchange rate effect	16	36	-	-	-	1	53
<b>Movement 2012</b>	<b>(588)</b>	<b>(1,436)</b>	<b>(263)</b>	<b>(46)</b>	<b>-</b>	<b>(106)</b>	<b>(2,439)</b>
At cost	27	1,882	2,524	6,322	-	1,253	12,008
Accumulated:							
Depreciation charges	-	(1,249)	(1,602)	(350)	-	(964)	(4,165)
Impairment charges	-	-	-	(715)	-	-	(715)
<b>Carrying value at December 31, 2012</b>	<b>27</b>	<b>633</b>	<b>922</b>	<b>5,257</b>	<b>-</b>	<b>289</b>	<b>7,128</b>

Land, land improvements and operational facilities included a Dutch-based rabbit farm and, based in the US and operated through Pharming Healthcare, Inc., cattle farm facilities. At the end of the second quarter of 2012, the Company – following a comprehensive review of its strategic options including cost containment measures – decided to close the cattle facilities and dismiss 10 employees (see Note 14 for a further explanation of termination benefits paid). The Company subsequently sold the cattle facilities for an amount below the net carrying value.

**The effects of the closure of the cattle farm facilities including the sales transaction for each category of property, plant and equipment can be summarized as follows:**

Amounts in €'000	Land and land improvements	Operational facilities	Other	Total
Net carrying value prior to impairment	601	1,299	24	1,924
Impairment charges	(-)	(1,198)	(24)	(1,222)
Net carrying value upon divestment	601	101	-	702
Other movements	(8)	28	-	20
Cash received	593	129	-	722



## **Notes to the consolidated financial statements continued**

Leasehold improvements relate to office and laboratory investments in the Company's leased headquarters. Following the restructuring of the Dutch operations as explained in Note 14 it was ultimately decided to discontinue the future use of certain leasehold improvements and accordingly an amount of €180,000 in impairment charges was incurred.

Manufacturing equipment is dedicated to the purification of rhC1INH with depreciation charges based on actual purification cycles. Assets under construction related to investments in the production capacity with Sanofi Chimie; the equipment in 2011 became available for use and accordingly was reclassified to manufacturing equipment; the net carrying value of previously in use but obsolete manufacturing equipment was fully impaired in 2011 (€35,000).

Depreciation charges on manufacturing equipment of €46,000 in 2012 (2011: €nil) are charged to the value of inventories and accordingly an amount of €617,000 of total 2012 depreciation charges have been charged to the statement of income (2011: €795,000).

Of 2011 investments of €3,657,000, a total of €2,079,000 was covered through various finance lease arrangements and of the remaining €1,578,000 an amount of €1,058,000 was paid in 2011 and presented as an investment cash flow. The unpaid year end 2011 balance of €520,000 was paid in 2012; in addition to the portion of 2012 investments of €94,000 paid in 2012, total 2012 investment cash flows amounted to €614,000.

At year end 2012, the carrying value of the assets hired under a financial lease arrangement – and thus with a restricted title - was €3,860,000 (December 31, 2011: €3,949,000) of which €3,757,000 in relation to manufacturing equipment (December 31, 2011: €3,790,000) and €103,000 related to other property, plant and equipment (December 31, 2011: €159,000).

### **6. Restricted cash, cash and cash equivalents, cash flows**

**The overall net cash position at year-end 2011 and 2012 was as follows:**

<b>Amounts in €'000</b>	<b>2012</b>	<b>2011</b>
Non-current restricted cash	732	979
Current restricted cash	309	309
Cash and cash equivalents	5,273	3,777
<b>Balance at December 31</b>	<b>6,314</b>	<b>5,065</b>
Balance at January 1	5,065	10,478
Exchange rate effects on cash	(160)	(42)
<b>Increase/(decrease) cash</b>	<b>1,409</b>	<b>(5,371)</b>

Restricted cash represent the value of banker's guarantees issued with respect to (potential) commitments towards third parties and are primarily related to finance lease liabilities and rent.

## Notes to the consolidated financial statements continued

The main cash flow statement items for the years 2011 and 2012 are:

Amounts in €'000	2012	2011
Net cash flows used in operating activities	(10,270)	(16,930)
Net cash flows from/(used in) investing activities	108	(1,098)
Net cash flows from financing activities	11,571	12,657
<b>Increase/(decrease) cash</b>	<b>1,409</b>	<b>(5,371)</b>

Pharming's net cash flows used in operating activities decreased from €16.9 million in 2011 to €10.3 million in 2012; the €6.6 million decrease primarily reflects aggregate receipts from license fees of €7.8 million in 2012 versus less than €0.1 million in 2011.

The 2011 net cash flows used in investing activities of €1.1 million primarily reflect payments in relation to manufacturing assets as disclosed in Note 5. The net cash flows from 2012 investing activities of €0.1 million stem from payment of investment in property, plant and equipment of €0.6 million (of which €0.5 million in relation to 2011 investments in manufacturing assets), net of the proceeds of sale of assets in the amount of €0.7 million.

The 2011 net cash flows from financing activities of €12.7 million include the early 2011 receipt of €9.0 million from Socius CG II, Ltd. following a year-end 2010 investment, the subsequent receipt of €1.0 million from the exercise of warrants by Socius CG II, Ltd., the €3.2 million proceeds of an equity issue and €0.6 million received under a finance lease agreement; these receipts were offset with €0.8 million finance lease payments and €0.4 million in transaction fees and expenses in relation to 2011 financing transactions. Net cash flows from financing activities in 2012 of €11.6 million stem from the proceeds of Bonds 2012 issued (€8.0 million), shares issued under the equity working capital facility (€4.9 million), the exercise of warrants (€0.4 million, net of €0.8 million in relation to payment of finance leases and €0.9 million for transaction fees and expenses (of which €0.5 million in relation to the Bonds 2012 described in Note 13 and €0.4 million in relation to the Equity Working Capital Facility described in Note 10).

### 7. Inventories

Inventories include batches rhC1INH and skimmed milk available for production of rhC1INH.

The composition of inventories at year-end 2011 and 2012 was:

Amounts in €'000	2012	2011
Batches rhC1INH	661	4,924
Skimmed milk	1,440	1,656
<b>Balance at December 31</b>	<b>2,101</b>	<b>6,580</b>

In 2011, the Company reversed 2010 impairment charges on batches rhC1INH for a total amount of €1.0 million and subsequently charged €0.7 million of rhC1INH inventories to research and development costs based on use in (pre)clinical activities and €1.8 million as cost of product sales. The Company had entered into commitments to purify skimmed milk batches after 2012; accordingly, the internal costs of these batches were credited to research and development costs in the statement of income 2011 for an amount of €0.9 million.

## **Notes to the consolidated financial statements continued**

Based on the expected use of batches rhC1INH assigned to future preclinical and clinical development, as well as the expiration dates of these inventories, finished product with a carrying value of €0.1 million were written down to the statement of income 2011 and charged to research and development expenses. In addition, the Company in 2011 impaired an amount of €1.7 million due to a one-off event decreasing the value of inventories designated for commercial activities; the amount was charged to cost of revenues in 2011.

The total net carrying value of inventories in 2012 decreased from €6.6 million to €2.1 million. The €4.5 million net decrease reflects investments in new inventories of €1.8 million; these were offset by €6.3 million in expenses, of which €1.1 million for costs of product sales, €3.1 million in inventory impairments of inventories previously carried for the purpose of selling, €1.3 million used in (pre)clinical activities, €0.5 million of inventory impairments for batches rhC1INH designated for use in (pre)clinical activities and €0.3 million of other expenses.

The major portion of inventories at December 31, 2012 has expiration dates starting beyond 2017 and is expected to be sold or used before expiration. Inventories carried at fair value less costs to sell amount to €0.7 million at year end 2012 (2011: €1.8 million).

### **8. Assets held for sale**

Pharming at year-end 2012 intended the sale of intangible assets with a net carrying value of €242,000 (Note 4) and accordingly these assets were presented as assets held of sale. The Company closed a transaction in 2013 and received a cash amount of US\$350,000 or approximately €262,000.

### **9. Trade and other receivables**

**The composition of trade and other receivables at December 31, 2011 and 2012 was:**

<b>Amounts in €'000</b>	<b>2012</b>	<b>2011</b>
Advance payment in shares	-	1,503
Trade receivables	-	353
Prepaid expenses	117	206
Value added tax	36	116
Other receivables	371	317
<b>Balance at December 31</b>	<b>524</b>	<b>2,495</b>

Trade and other receivables at December 31, 2012 are substantially short-term in nature and have largely been settled as per the date of these financial statements. The advance payment in shares at December 31, 2011 has been further described in Note 10 and Note 13.

## **Notes to the consolidated financial statements continued**

### **10. Equity**

The Company's authorized share capital amounts to €13.0 million and is divided into 1,300,000,000 ordinary shares with a nominal value of €0.01 each. All 1,009,189,097 shares outstanding at December 31, 2012 have been fully paid-up.

Other reserves include those reserves related to currency translation, share-based compensation expenses and other equity-settled transactions.

This note further describes the background of the main equity movements in 2011 and 2012.

#### **Adjustment nominal value per share**

On May 14, 2012 the Company's shareholders at an Annual General Meeting of Shareholders approved to reduce the nominal value per share from €0.04 to €0.01 with 625,082,077 shares outstanding as per the date of the adjustment. The reduction is made due to losses incurred and accordingly the amount of share capital has been decreased with €18,752,000 with a corresponding increase of accumulated deficit. The overall effect of the adjustment on shareholders' equity therefore was €nil.

#### **Net loss and Accumulated deficit**

Accumulated deficit at the beginning of 2012 amounted to €258,413,000 and decreased with €18,752,000 to €239,661,000 following the adjustment of the nominal value per share from €0.04 to €0.01 as explained above.

Article 25.1 of the Articles of Association reads as follows: 'The management board shall annually determine, subject to the approval of the Board of Supervisory Directors, the amount of the distributable profit – the surplus on the profit and loss account – to be reserved.' The Board of Management has proposed to forward the net loss for the year 2012 of €24,093,000 to the accumulated deficit. Anticipating the approval of the financial statements by the Shareholders at the AGM, this proposal has already been reflected in the Financial Statements and accordingly accumulated deficit has increased from €239,661,000 to €263,754,000 at year-end 2012.

#### **Deconsolidation of DNage B.V.**

The non-controlling interest of other shareholders in DNage B.V. was 49% and amount to a negative amount of €764,000 at the beginning of 2011. As disclosed in Note 23, the Company due to voluntary liquidation lost control of DNage B.V. as of January 31, 2011 and accordingly the non-controlling interest amount of €764,000 was deconsolidated in 2011.

#### **Recycling equity translation reserve**

Adjustments of the currently translation reserve reflect the effect of translating US operations denominated in US\$ since their functional currency is different from the reporting currency. Subsequent to the Company transferring its US assets in 2012 (see Note 5), Pharming's negative foreign currency translation reserve within equity of €1,384,000 was recycled to the statement of income and charged to financial expenses; overall, this did not have an impact on equity.

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

Share-based compensation within equity includes those transactions with third parties, the Board of Management and employees in which payment is based in shares or options based on current or future performance. For 2011 these transactions were valued at €1,039,000 and for 2012 at €370,000 (see Note 24).

#### **Bonuses settled in shares**

The Company in 2011 issued 515,837 shares to members of the Board of Management and various managers in lieu of bonuses with an aggregate value of €103,000. In 2012 a total of 3,950,211 shares were issued to pay off bonuses of €274,000.

## **Notes to the consolidated financial statements continued**

### **Bond payments in shares**

In February 2012 the Company Pharming issued private bonds ('Bonds 2012', as further explained in Note 13) of €8.4 million carrying 8.5% annual interest. An advance payment of 20 million shares valued at €1,503,000 was made in 2011 (see Advance payment in shares further in this Note). Pharming in 2012 fully redeemed the nominal value plus interest of the Bonds 2012 through the issue of an additional 210,181,995 shares with an aggregate fair value of €9,924,000.

### **Warrants exercised**

In 2011 a total of 24,339,623 warrants with an exercise price of €0.212 or €5,160,000 in total were exercised by Socius CG II, Ltd. The Company received a cash amount of €974,000 representing the nominal value of the shares issued; the remaining balance of €4,186,000 was reclassified from other reserves within equity to share premium since this value had already been paid for in 2010 through the issue of interest-free debt notes Socius CG II, to the Company.

In 2012 a total of 29,259,591 warrants were exercised, of which 24,051,258 warrants were exercised in exchange for the issue of 24,051,258 shares; the Company received a cash amount of €423,000. In addition, a total of 5,208,333 warrants were exercise cashless; a total of 2,120,710 shares with an exercise value of €29,000 were transferred to the warrant holder and in return the warrant holder forfeited the other 3,087,623 warrants with a (profit) value of €29,000.

### **Shares/warrants issued for cash**

Pharming in 2011 issued 29,000,000 shares to investors for an amount of €0.11 per share or €3,190,000 in total and granted the investors the right to receive 20,300,000 warrants with an exercise price of €0.11 per share and subject to shareholder approval; both the number of warrants as well as the exercise price is adjusted subject to various events taking place and accordingly the warrants qualified as a financial instrument, which value including transaction costs allocated to the liability (€1,726,000) was subtracted from the €3,190,000 receipt in order to arrive at the equity portion of the transaction (being €1,464,000). The warrants were formally issued in 2012 (see Note 13 and Note 28).

On August 1, 2012 the Company announced it had secured an Equity Working Capital Facility with institutional investors of up to €10.0 million for a two year term. Pharming has the option to draw in tranches in exchange for ordinary shares in the capital of the Company and retains control of the timing and amount of any funds draw down. Pharming must give notice to the investors (a 'Draw Down Notice') prior to drawing down funds. Each Draw Down Notice will state the number of ordinary shares Pharming wishes to sell to the investors (the 'Draw Down Amount'). The investors have the option to purchase up to 600% of the Draw Down Amount during a 15 trading days pricing period; the total amount of cash paid for such shares to Pharming will depend on the total number of shares called by the investors and the development of the Volume Weighted Average Price ('VWAP') of the shares going forward during this 15 trading days pricing period; the investors subsequently withhold a 12.5% discount on the applicable price. Upon concluding the agreement the investors received 16,500,000 warrants ('initial warrants') with an exercise price of €0.0233; an additional number of warrants ('investment warrants') with an exercise price of €0.0233 are issued if an individual investor has exceeded 25%, 50% and 75% of their proportionate share in the total facility amount of €10.0 million (a maximum of 16,500,000 warrants in total is available for all investors for the 25% as well as the 50% and the 75% threshold).

## Notes to the consolidated financial statements continued

Up to December 31, 2012 the Company has drawn three tranches under the Equity Working Capital Facility. The following table provides an overview of the values paid and received by the Company as well as their recognition in these financial statements:

Number of shares issued		258,768,453
Number of initial warrants issued		16,500,000
Fair value of initial warrants issued (€'000)		198
Number of investment warrants issued		27,505,500
Fair value of investment warrants issued (€'000)		424
	<b>€'000</b>	<b>€'000</b>
Value of shares at applicable VWAP	5,623	
Fair value of shares issued	<u>6,296</u>	6,296
Result charged to statement of income	(673)	
Cash received	4,916	
Value of shares at applicable VWAP	<u>5,623</u>	
Discount 12.5%	(707)	
Fair value of investment warrants issued	(424)	
Other transaction fees and expenses	<u>(420)</u>	
Total items charged to share premium		<u>(1,551)</u>
Directly charged to equity		4,745

The €198,000 fair value of the initial warrants has been capitalized as a prepaid expense and is subsequently amortized within financial expenses (further see Note 22).

### Advance shares issued

On December 23, 2011, the Company announced it had entered into an agreement with various investors under which convertible bonds were issued but subject to an increase of share capital anticipated to take place in 2012. On February 3, 2012 the Company held an Extraordinary General Meeting of Shareholders in which the shareholders approved the increase of authorized share capital from 550 million to 805 million shares. This event triggered the immediately release of €8.0 million in cash to Pharming, which amount was held in escrow by an independent law firm at December 31, 2011. The Company issued the convertible bonds (Bonds 2012) with a nominal value of €8.4 million carrying 8.5 percent interest per annum and to be repaid in six equal monthly tranches of €1.4 million between February and July 2012. The investors have the right to convert outstanding Bonds 2012 at a fixed conversion price of €0.12; the Company has the option to repay in either cash or shares. In addition, the investors received 38,717,484 warrants with an exercise price of €0.12 per warrant.

Following the 2011 agreement, the Company issued 20,000,000 shares to the investors as an advance payment for any future share issue in case of repayment in shares. These shares were valued at the anticipated settlement amount of €1,503,000 in total and posted as a receivable (see Note [9]) with a similar amount posted in equity. In 2012 the advance payment was settled against the outstanding liability of the Bonds 2012 (Note 13).

## **Notes to the consolidated financial statements continued**

### **11. Deferred license fees income**

In 2010, the Company entered into a distribution agreement for Ruconest® with Swedish Orphan Biovitrum International AB under which a €3.0 million upfront payment and a €5.0 million milestone payment were received in cash. The €8.0 million is released to the statement of income in accordance with the remaining lifetime of the agreement following Market Approval for Ruconest® in October 2010 and subsequent start of supplies. An amount of €133,000 in license fees income was released as revenues from license fees in 2010. In both 2011 and 2012 another €800,000 was released from this agreement.

Pharming in 2010 received an upfront payment of US\$15.0 million or €11,692,000 in cash from Santarus, Inc. with respect to a Ruconest® license agreement for recombinant human C1 inhibitor in the US, Canada and Mexico. Since the Company has to perform clinical, regulatory and commercial activities, the amount is released to the statement of income over the full lifetime of the agreement as of its effective date. Accordingly, an amount of €332,000 in license fees income was recognized as revenues from license fees in 2010 and €1,136,000 in both 2011 and 2012.

In 2011 the Company received a license fee amount of €25,000.

<b>Amounts in €'000</b>	<b>2012</b>	<b>2011</b>
<b>Total balance at January 1</b>	<b>17,367</b>	<b>19,278</b>
Receipt of upfront and milestone payments in cash	-	25
Revenues from deferred license fees	(1,936)	(1,936)
<b>Total balance at December 31</b>	<b>15,431</b>	<b>17,367</b>
Current balance at December 31	(1,936)	(1,936)
<b>Non-current balance at December 31</b>	<b>13,495</b>	<b>15,431</b>

Aggregate receipts from license partners in 2012 as per the consolidated statement of cash flows amounted to €9,069,000 (2011: €814,000) of which €nil from upfront and milestone payments recognized as deferred license fees income (2011: €25,000), €7,820,000 of milestone payments immediately recognized as revenues in 2012 (€nil in 2011; the 2012 amount is US\$10,000,000 as per date of actual receipt of the cash), €1,150,000 (2011: €710,000) from product sales and €67,000 (2011: €79,000) from reimbursement of research and development costs and €32,000 from other transactions (2011: €nil).

### **12. Finance lease liabilities**

Certain of the Company's property, plant and equipment items are subject to finance leases. These leases mainly relate to manufacturing equipment in which significant investments were made prior to 2012.

**Notes to the consolidated financial statements continued**

**Movement and composition of the finance lease liabilities for 2011 and 2012 was:**

<b>Amounts in €'000</b>	<b>Note</b>	<b>2012</b>	<b>2011</b>
<b>Total balance at January 1</b>		<b>3,433</b>	<b>77</b>
Initial recognition new finance lease arrangements		-	3,932
Interest expense accrued	20	261	214
Payments of finance lease liabilities	6	(838)	(790)
<b>Total balance at December 31</b>		<b>2,856</b>	<b>3,433</b>
Current balance at December 31		(895)	(1,218)
<b>Non-current balance at December 31</b>		<b>1,961</b>	<b>2,215</b>

Pharming has entered into a number of finance lease arrangements, of which two are material:

- the first arrangement entails a straight-forward financial lease agreement relating to manufacturing and other equipment under which assets valued at €2,059,000 were acquired and for which the Company in 2011 received an amount of €618,000 for investment items under this agreement already paid in 2010. The lease is repaid through a first installment of €261,500 followed by 35 monthly equal installments of €57,700 per month. Ownership of the assets will be transferred to Pharming free of charge after payment of the final installment. In connection with the agreement the Company has issued a banker's guarantee to the lessor that due to payment of monthly installments decreases with €20,500 a month throughout the lifetime of the agreement. At December 31, 2012 the remaining amount of this banker's guarantee is €803,000. The Company pays 7.7% interest per annum; and
- under an existing manufacturing agreement a service provider invested into certain assets exclusively in use by the Company but operated by the service provider. The Company will reimburse the service provider an aggregate amount of €2,814,000 over the lifetime of the agreement through a variable service fee charge based on minimum annual production levels and accordingly the net present value of the investment in the amount of €1,805,000 has been presented as manufacturing equipment with a simultaneous increase of finance liabilities. An estimated 11.0% annual interest charge applies to this agreement. The service provider is and will remain to be the legal owner of the assets in use.

The fair value of the finance lease obligations approximates their carrying amount. No arrangements have been entered into for contingent rental payments.



## Notes to the consolidated financial statements continued

Future minimum lease payments under finance leases as at December 31, 2011 and 2012 are as follows:

Amounts in €'000	2012		2011	
	Minimum pay-ments	Present value of payments	Minimum payments	Present value of payments
Within one year	937	895	1,311	1,218
After one year but not more than five years	1,326	1,321	2,051	1,676
More than five years	825	640	1,120	539
	<b>3,088</b>	<b>2,856</b>	<b>4,482</b>	<b>3,433</b>

At year end 2012, the carrying value of the assets involved as leased was €3,860,000 (2011: €3,949,000) of which €3,757,000 in relation to manufacturing equipment (2011: €3,790,000) and €103,000 related to other property, plant and equipment (2011: €159,000).

### 13. Convertible bonds and derivative financial liabilities

Convertible bonds and derivative financial liabilities relate to financial instruments and include warrants issued in relation to the issue of equity and/or (convertible) bonds as well as conversion rights for holders of convertible bonds.

#### Bonds 2012

Following an announcement in December 2011, the Company in February 2012 issued €8.4 million private convertible bonds ('Bonds 2012') carrying 8.5% annual interest. An advance payment of 20 million shares valued at €1,503,000 was made in 2011; the amount was capitalized within Trade and other receivables at December 31, 2011 and posted within equity (see Note 9 and Note 10) with the advance payment subsequently charged to the Bonds 2012 in 2012.

In connection to the issue of the Bonds 2012 the Company also incurred transaction fees and expenses of €624,000 in total, of which €95,000 had been paid in 2011 and €529,000 was paid in 2012. The amount of €624,000 has been allocated to the derivative financial derivatives and the Bonds 2012 based on their relative weight in the €8.0 million as received and accordingly an amount of €90,000 as charged to the derivative financial liabilities was charged to financial expenses (further see Note 22) with the remaining €534,000 charged to the carrying value of the Bonds 2012.

For accounting purposes, the convertible bond portion was initially recognized at the aggregate value of the value received minus the fair value of the derivative financial liabilities and the portion of transaction fees and expenses allocated to the convertible bond. Pre(payments) of the monthly installment plus interest could take place either in cash or shares; the Company (until maturity in July 2012) decided to pay in shares exclusively and as a result of certain conditions in the agreements this has resulted in transfer of shares for a value higher than if such a repayment had taken place in cash. Accordingly, a transaction loss of €2,757,000 was incurred in 2012.

**Notes to the consolidated financial statements continued**

**Movements of the Bonds 2012 in the financial year 2012 were as follows:**

	Note	€'000
Received in cash	6	8,000
Fair value of warrants issued		(1,045)
Fair value of conversion right		(103)
Transaction fees and expenses		<u>(535)</u>
Carrying value initial recognition		6,317
Effective interest		2,353
Result bond settlements		2,757
Advance payment in shares 2011	9, 10	(1,503)
Fair value of shares issued in 2012	10	<u>(9,924)</u>
Carrying value at December 31, 2012		-

**Derivative financial liabilities**

Derivative financial liabilities at the beginning of 2011 related to 5,208,333 warrants issued before 2011. Pharming in the third quarter of 2011 issued 29,000,000 shares to investors for an amount of €0.11 per share or €3,190,000 in total and granted the investors the right to receive 20,300,000 warrants with an exercise price of €0.11 per share and subject to shareholder approval; both the number of warrants as well as the exercise price is adjusted subject to various events taking place and accordingly the warrant rights qualified as a financial instrument. The fair value upon initial recognition was €1,624,000 and decreased to €1,015,000 at December 31, 2011; the 2011 decrease of €609,000 has been charged to the statement of income (Fair value gain derivatives). Following the involvement of these investors in the fourth quarter December issue of Bonds 2012, the exercise price of the 20,300,000 warrant rights was decreased to €0.06. Shareholder approval was obtained through an Extraordinary General Meeting of Shareholders held on February 3, 2012 so that the warrants were officially granted after the end of the reporting year and thus not included in outstanding warrants at December 31, 2011 (see Note 28).

Derivative financial liabilities recognized in 2012 related to 38,717,484 warrants issued in relation to the Bonds 2012 (see above in this Note 13), 44,005,500 warrants in relation to the Equity Working Capital Facility (Note 10) and conversion rights on Bonds 2012 with the initial fair value of these items upon recognition amounting to €1,045,000, €622,000 and €103,000 or €1,770,000 in total. Following the exercise of in total 29,259,591 warrants in 2012, the Company derecognized their fair values prior to exercise of in total €443,000.

**Movement of derivative financial liabilities for 2011 and 2012 can be summarized as follows:**

Amounts in €'000	2012	2011
<b>Total balance at January 1</b>	<b>1,171</b>	<b>573</b>
Initial recognition upon issue	1,770	1,624
Derecognition fair values upon exercise of warrants	(443)	-
Fair value gains derivatives	(1,283)	(1,026)
<b>Total balance at December 31</b>	<b>1,215</b>	<b>1,171</b>

Fair value gains on derivatives have been presented within financial income.

## Notes to the consolidated financial statements continued

### 14. Restructuring provision

In the second quarter of 2012 Pharming announced the closure and subsequent sale of the US cattle facilities (see Note 5). A total of 7 employees were dismissed with immediate effect and 3 employees involved in the transfer process of the assets were dismissed following completion of the process. Compensation packages for all employees were completely paid off in the second half of 2012 and no remaining liabilities remain at the end of 2012.

The Company on August 2, 2012 announced a restructuring plan involving its Dutch-based operations and which resulted in the intended dismissal of employees in the Netherlands. A social plan was agreed upon with the Company's Works Council that entailed an unconditional payment per employee affected of 20% with another 40% paid upon receipt of the US\$10.0 million milestone from Santarus and another 40% if additional financing of at least €5.0 million was concluded (latter excluded the €10.0 million Equity Working Capital Facility announced on August 1, 2012). Late 2012 the Dutch authorities rejected the request filed for the collective redundancies and therefore Pharming entered into individual agreements, in principle along the terms and conditions of the social plan, with the employees involved; a limited number of employees had already found new employment prior to this phase and these are therefore paid off in accordance with the social plan with some payments already made in 2012. Overall, a very limited number of employees have not agreed to the compensation offered by the Company and these agreements will most likely be solved in court; a provision has been made to settle these issues based on a based estimate per individual case. In addition to compensation offered, the employees involved were also relieved from work for a limited number of months and for which regular compensation benefits are continued to be paid by Pharming. As a result, the Company in 2012 provided for a total amount of €1,242,000 and of which €1,232,000 is scheduled for payment in 2013.

#### Movement of the restructuring provision was as follows:

Amounts in €'000	Note	2012	2011
<b>Total balance at January 1</b>		-	-
Termination benefits restructuring US operations	18	129	-
Termination benefits restructuring Dutch operations	18	954	-
Exempt from work	18	298	-
Other items		24	-
Payments		(173)	-
<b>Total balance at December 31</b>		<b>1,232</b>	-
Current balance at December 31		(1,232)	-
<b>Non-current balance at December 31</b>		-	-

## **Notes to the consolidated financial statements continued**

### **15. Trade and other payables**

Trade and other payables at year-end 2011 and 2012 consist of:

<b>Amounts in €'000</b>	<b>2012</b>	<b>2011</b>
Accounts payable	1,126	2,048
Taxes and social security	207	114
Deferred compensation due to related parties	409	400
Other payables	1,948	1,248
<b>Balance at December 31</b>	<b>3,690</b>	<b>3,810</b>

The amount of deferred compensation due to related parties involves Members of the Board of Management and includes bonuses, holiday allowances and holiday rights.

### **16. Revenues**

Revenues for the financial years 2011 and 2012 can be split as follows:

<b>Amounts in €'000</b>	<b>2012</b>	<b>2011</b>
License fees	9,815	1,936
Product sales	798	1,063
	<b>10,613</b>	<b>2,999</b>

The 2011 income from license fees is related to the portion of deferred license fees income released from upfront and milestone payments of distribution agreements entered into with Swedish Orphan Biovitrum International AB and Santarus, Inc. Further background of the amounts received and the associated release of revenues is provided in Note 11. In 2012 the Company's income from license fees also included an amount of €1,936,000 released; other license fees income of €7,879,000 are largely associated with the receipt of a US\$10.0 million milestone from Santarus, Inc. following successful completion of a clinical study.

Product sales relate to supplies of Ruconest® inventories to Swedish Orphan Biovitrum International AB following Market Approval in the European Union in October 2010. The Company for its 2011 and 2012 product sales revenues was fully dependent on this customer since no market approvals have yet been obtained in territories outside the European Union.

### **17. Other income**

Other income related to grants exclusively and amounted to €196,000 in 2011 and €250,000 in 2012. Grants in both years reflect an annual payroll tax deduction granted by the Dutch government for a range of certain research and development activities. In addition, the Company both in 2011 and 2012 recognized income for a one-time grant from the Dutch government; the grant expired in 2012.

## Notes to the consolidated financial statements continued

### 18. Expenses by nature

Cost of product sales in 2012 amounted to €1.1 million (2011: €1.8 million) and relates to actual supplies as well as anticipated price adjustments on future supply of Ruconest® inventories to Swedish Orphan Biovitrum AB as of October 2010.

Inventory impairments related to inventories designated for commercial activities amounted to €3.1 million in 2012 (2011: €1.7 million). In 2011 the impairments followed from production-related events beyond control of the Company, whereas 2012 impairment charges stem from the write-off of inventories approaching expiration date prior to sale to or by Swedish Orphan Biovitrum AB.

Costs of research and development increased from €13.8 million in 2011 to €19.4 million in 2012. The €5.6 million increase primarily stems from an increase of costs associated with clinical and regulatory activities in relation to the US (plus €3.6 million) and one-time restructuring charges (plus €1.1 million).

Pharming's general and administrative costs decreased from €3.3 million in 2011 to €3.1 million in 2012; the decrease largely stems from a one-time refund from a third party.

This Note further discusses items included in Research and development costs and/or General and administrative costs.

#### Employee benefits for the financial years 2011 and 2012 comprised of:

Amounts in €'000	2012	2011
Salaries	(5,243)	(5,530)
Termination benefits	(1,297)	(101)
Exempt from work	(298)	-
Social security costs	(580)	(559)
Pension costs	(494)	(491)
	<b>(7,912)</b>	<b>(6,681)</b>

Salaries include holiday allowances and cash bonuses. Termination benefit expenses in 2012 include €1,083,000 in relation to the restructuring provision (Note 14) and €177,000 in relation to the termination of the agreement with R.R.D. Pijpstra (Note 25). The amount expensed for exempt from work involves 2012 and 2013 expenses for employees relieved from work (Note 14).

#### The number of employees for 2011 and 2012 per functional category was as follows (at weighted average full time equivalent factor):

	2012	2011
Research and development	54	60
General and administrative	14	15
	<b>68</b>	<b>75</b>

## **Notes to the consolidated financial statements continued**

Employee benefits are charged to Research and development costs or General and administrative costs based on the nature of the services provided.

### **Inventories**

In 2012, the Company expensed an amount of €1.3 million for batches of rhC1INH (2011: €0.1 million) in research and development expense, €0.5 million for impairment charges (2011: €0.8 million) and €0.3 million of other expenses (2011: nil).

### **Depreciation and amortization charges**

The following table shows the composition of depreciation and amortization charges:

<b>Amounts in €'000</b>	<b>Note</b>	<b>2012</b>	<b>2011</b>
Property, plant and equipment	5	(617)	(795)
Intangible assets	4	(175)	(176)
		<b>(792)</b>	<b>(971)</b>

The decrease of depreciation charges of property, plant and equipment in 2012 as compared to 2011 stems from discontinuing such charges following sale of the US cattle facility in the second half of 2012.

Amortization charges of intangible assets have been fully allocated to research and development costs in the statement of income; for property, plant and equipment, in 2012 an amount of €517,000 was charged to research and development costs (2011: €636,000) and €100,000 to general and administrative expenses (2011: €159,000).

### **Operating lease charges**

For the year 2012, the Company charged €0.8 million (2011: €0.7 million) to the statement of income with regard to lease commitments for office rent, equipment, facilities and lease cars. These non-cancellable leases at December 31, 2012 have remaining terms of between one to five years and generally include a clause to enable upward revision of the rental charge on an annual basis according to prevailing market conditions. The expected operating lease charges after the end of the reporting year have been disclosed in Note 31.

Allocations of the operating lease charges to Research and development costs or General and administrative expenses have been based on the nature of the asset in use.

### **Independent auditor fees**

Fees of PricewaterhouseCoopers Accountants N.V. incurred in relation to 2012 audit services were €100,000 (2011: €97,000) with other services and audit-related services amounting to €33,000 (activities related to the issuance of a prospectus) (2011: €nil). Altogether, fees incurred for services of PricewaterhouseCoopers Accountants N.V. were €133,000 in 2012 (2011: €97,000). These items were charged to General and administrative expenses.

## Notes to the consolidated financial statements continued

### 19. Impairment charges

The following table shows the composition of impairment charges:

Amounts in €'000	Note	2012	2011
Property, plant and equipment	5	(1,222)	(35)
Intangible assets	4	(35)	-
		<b>(1,257)</b>	<b>(35)</b>

The 2011 impairment charges of €35,000 related to the carrying value of obsolete manufacturing equipment for which no further use was anticipated. In 2012, Pharming sold its cattle facilities for a cash consideration of €722,000; the Company incurred impairment charges as a result of the net carrying value exceeding the fair value of the assets minus costs to sell by €1,222,000 (€1,198,000 in relation to operational facilities and €24,000 for other items; land was not impaired).

With respect to the 2012 impairment charges on intangible assets of €35,000, the charge followed the use of certain intangible assets linked to other intangible assets to be disposed of.

### 20. Other interest expenses, net

The composition of other net interest expenses in 2011 and 2012 was as follows:

Amounts in €'000	Note	2012	2011
Interest expense financial leases	12	(261)	(214)
Interest income cash and cash equivalents		19	1
		<b>(242)</b>	<b>(213)</b>

Increased interest expenses from financial leases in 2012 compared to 2011 stem from various finance arrangements entered into in the course of 2011.

### 21. Foreign currency results

These results primarily follow from the revaluation of bank balances denominated in foreign currencies and the timing of foreign currency payments against the actual exchange rate as compared to the original exchange rate applied upon the charge of fees or expenses. Net exchange rate losses of €49,000 in 2011 included net losses of €42,000 in relation to revaluation of cash and cash equivalents; in 2012, exchange rate losses amounted to €218,000 of which €160,000 in relation to cash and cash equivalents.

## **Notes to the consolidated financial statements continued**

### **22. Other financial expenses**

The composition of other financial expenses in 2011 and 2012 was as follows:

<b>Amounts in €'000</b>	<b>Note</b>	<b>2012</b>	<b>2011</b>
Costs related to issue of derivative financial liabilities	13	(90)	(106)
Amortization expenses warrants	10	(198)	-
		<b>(288)</b>	<b>(106)</b>

Costs related to issue of derivative financial liabilities include the portion of the total transaction fees of Bonds 2011 and Bonds 2012 allocated to the derivative financial liabilities.

Amortization expense of warrants in 2012 follow from the 16,500,000 warrants issued upon concluding the Equity Working Capital Facility. The fair value of these warrants amounted to €198,000 and these were initially amortized in line with the cash received under the instrument as a percentage of the maximum investment of €10.0 million. The Company accordingly amortized €97,000; the remaining €101,000 was expensed at year-end 2012 following a review of the future use of the Equity Working Capital Facility.

### **23. Net profit from discontinued operations**

On January 31, 2011 the shareholders of DNage B.V., an entity in which Pharming as per that date had a 51% interest, decided to put the company into voluntary liquidation. Due to this decision Pharming effectively lost control and deconsolidated the entity as of that date. The entity until deconsolidation incurred a net loss of €196,000, of which €100,000 was born by Pharming and €96,000 to other shareholders. Following deconsolidation of the negative equity and including minor other movements, a profit of €839,000 was posted as a result from discontinued operations. Altogether, the net profit from discontinued operations amounted to €643,000 of which a net profit of €739,000 was attributable to owners of the parent and a net loss of €96,000 to non-controlling interest.

### **24. Share-based compensation**

The Company has a Long Term Incentive Plan and two option plans in place: one for the Board of Management and one for employees ('the Option plans'). All these plans or arrangements are equity settled. The total expense recognized in 2012 for share based payment plans amounts to €370,000 (2011: €1,039,000).



## ***Notes to the consolidated financial statements continued***

### **Models and assumptions**

The costs of option plans are measured by reference to the fair value of the options at the grant date of the option. IFRS 2 describes a hierarchy of permitted valuation methods for share based payment transactions. If possible, an entity should use market prices at measurement date to determine the fair value of its equity instruments. If market prices are unavailable, as is the case with Pharming's Option plans and Long Term Incentive Plan, the entity shall estimate the fair value of the equity instruments granted. A valuation technique should be used to estimate the value or price of those equity instruments as it would have been at the measurement date in an arm's length transaction between knowledgeable, willing parties. The valuation technique shall be consistent with generally accepted valuation methodologies for pricing financial instruments and shall incorporate all factors and assumptions that knowledgeable market participants would consider in setting the price.

Whatever pricing model is selected, it should, as a minimum, take into account the following elements:

- (a) the exercise price of the option;
- (b) the expected time to maturity of the option;
- (c) the current price of the underlying shares;
- (d) the expected volatility of the share price;
- (e) the dividends expected on the shares;
- (f) the risk-free interest rate for the expected time to maturity of the option.

The six elements above are all incorporated in the Black-Scholes model used to determine the fair value of options. The exercise price of the option and the share price are known at grant date. Volatility is based on the historical end-of-month closing share prices over 5 years prior to the option grant date. It is assumed no dividend payments are expected.

For the Long Term Incentive Plan, the following elements of Pharming and/or the peer group are included in order to determine the fair value of Long Term Incentive Plan share awards, using Monte Carlo Simulation:

- (a) start and end date of performance period;
- (b) the grant date;
- (c) the share prices;
- (d) exchange rates;
- (e) expected volatilities;
- (f) expected correlations;
- (g) expected dividend yields;
- (h) risk-free interest rates.

Volatilities are based on the historical end-of-month closing share prices over the 3 years (Long Term Incentive Plan). Correlations are based on 3 years of historical correlations based on end-of-month closing quotes, taking into account exchange rates. Expected dividend yields for peers and risk-free interest rates (depending on the currency) are obtained from Bloomberg.

### **Long Term Incentive Plan**

At the AGM of April 16, 2008 a Long Term Incentive Plan was approved with an effective date of January 1, 2008. Under the LTIP, restricted shares are granted conditionally each year with shares vesting based on the market condition in which the total shareholder return performance of the Pharming share is compared to the total shareholder return of a peer group of 40 other European biotech companies.

**Notes to the consolidated financial statements continued**

The reference group for the 2010-2012 programs consists of the following 40 companies:

<b>Main location</b>	<b>Number</b>	<b>Company names</b>
Belgium	6	Ablynx, Devgen, Galapagos, Thrombogenics, Ti-Genix, Oncomethylome
Denmark	3	Bavarian Nordic, Lifecycle Pharma, Neurosearch
Finland	1	Biotie Therapeutics
France	4	Exonhit, Hybrigenics, Innate Pharma, Transgene
Germany	6	Cellectis, Evotec, GPC Biotech, Medigene, Morphosys, Wilex
Italy	2	BioXell, Newron
Norway	1	Photocure
The Netherlands	2	AMT, Octopus
Sweden	2	Biovitrum, Medivir
Switzerland	5	Addex, Arpida, Basilea, Cytos, Santhera
United Kingdom	8	Alizyme, Ark Therapeutics, GW Pharma, Oxford Biomedica, Oxford Instruments, Prostrakan, Renovo, Vernalis

The vesting schedule is as follows. Ranking in the top:

- 5% of the index: 100%
- 5-10 % of the index: 80% of maximum
- 10-20% of the index: 60% of maximum
- 20-30% of the index: 50% of maximum
- 30-50% of the index: 20% of maximum

Upon a change of control, all shares will vest automatically.

An overview of the maximum number of LTIP shares granted in 2010-2012 and in total as well as the fair value per share award is as follows:

<b>Participant category</b>	<b>Granted</b>			<b>Total</b>
	<b>2010</b>	<b>2011</b>	<b>2012</b>	
Board of Supervisory Directors	120,000	-	-	120,000
Board of Management	300,000	1,586,954	4,156,097	6,043,051
Senior Managers	400,000	500,000	1,000,000	1,900,000
<b>Total</b>	<b>820,000</b>	<b>2,086,954</b>	<b>5,156,097</b>	<b>8,063,051</b>
Fair value per share award (€)	0.190	0.050	0.013	

## Notes to the consolidated financial statements continued

The following table provides an overview of LTIP shares granted, forfeited or not vested in 2010-2012 as well as the number of LTIP shares reserved at December 31, 2012:

Participant category	Total 2010-2012			Reserved at December 31, 2012
	Granted	Forfeited	Not vested	
Board of Supervisory Directors	120,000	-	(120,000)	-
Board of Management	6,043,051	(2,463,131)	(200,000)	3,379,920
Senior Managers	1,900,000	(120,000)	(280,000)	1,500,000
<b>Total</b>	<b>8,063,051</b>	<b>(2,583,131)</b>	<b>(600,000)</b>	<b>4,879,920</b>

The Company expensed amounts of €132,000 in 2010, €113,000 in 2011 and €99,000 in 2012. The 2010 shares did not vest; LTIP shares reserved at December 31, 2012 relate to the 2011 and 2012 shares available for participants still in service at the end of 2012.

### Main characteristics of the Option plans

The total number of shares with respect to which options may be granted pursuant to the Option plans accumulated, shall be determined by Pharming, but shall not exceed 10% of all issued and outstanding shares of Pharming on a fully diluted basis. Shares transferred or to be transferred, upon exercise of options shall be applied to reduce the maximum number of shares reserved under the plans. Unexercised options can be re-used for granting of options under the Option plans.

Pharming may grant options to a Member of the Board of Management or an employee:

- at the time of a performance review;
- only in relation to an individual: a date within the first month of his or her employment;
- in case of an extraordinary achievement;
- in case of a promotion to a new function within Pharming.

The option exercise price is the price of the Pharming shares on the stock exchange on the trading day prior to the date of grant or on the trading day prior to the meeting of the Board of Supervisory Directors during which it was resolved to grant options. Options can be exercised at any time within five years following the date of grant. Unexercised options shall be deemed cancelled and shall cease to exist automatically after five years. Exercise of options is subject to compliance with laws and regulations in the Netherlands.

### Option plan Board of Management

Article 2.1 of the Option plan for the BOM states: 'The Board of Supervisory Directors may, at its sole discretion, (i) grant Options to any Member (ii) define the conditions attached to the Options which need to be fulfilled before the Options can be exercised (iii) determine the criteria for the granting of the Options. The compensation committee of Pharming will propose (i) the criteria for the granting of Options, (ii) whether the criteria for granting an Option have been met by a potential Participant and (iii) the number of Options to be granted. The Options will at all times be granted under the condition that the granting of such Options will be approved by the general meeting of shareholders of Pharming.' Article 4.4 of the Option plan for the BOM reads as follows: 'In case of the termination of the membership of a Participant of the Board of Management, except for retirement and death, Pharming at its sole discretion is entitled to decide that the Options of the Participant shall lapse if the conditions set out in the Option Granting Letter have not been fulfilled at the time of the termination of the membership of the Board of Management.'

## **Notes to the consolidated financial statements continued**

The Company in its sole discretion may decide to deviate from article 4.4.

At the AGM of May 11, 2011 the four members of the BOM were granted a total of 10,550,000 options with an exercise price of €0.154 and a fair value of €0.08. Vesting of the conditional stock options per individual Member of the Board of Management was based on the requirement to be in service at January 1, 2012; since all Members met this criterion, the Company in 2011 incurred a total expense of €844,000 of which €280,000 for S. de Vries (3,500,000 options), €200,000 for K.D. Keegan (2,500,000 options) and €182,000 (2,275,000 options) for both B.M.L. Giannetti and R.R.D. Pijpstra.

At the AGM of May 14, 2012 the four members of the BOM were granted a total of 11,437,500 options with an exercise price of €0.0558 and a fair value of €0.024. Vesting of the conditional stock options per individual Member of the Board of Management was based on the requirement to be in service at January 1, 2013. K.D. Keegan (2,812,500 options) and R.R.D. Pijpstra (2,437,500 option) both left the Company on September 1, 2012 and accordingly their options did not vest. The options of S. de Vries (3,750,000 options valued at €90,000 in total) and B.M.L. Giannetti (2,437,500 options valued at €59,000 in total) vested on January 1, 2013 and accordingly Pharming in 2012 expensed a total amount of €149,000.

### **Option plan employees**

Article 2.1 of the Option plan for employees states: 'Pharming may grant Options to any Employee. The criteria for the granting of the Options will be determined by the Board of Supervisory Directors of Pharming, at its sole discretion. The Board of Management will propose (i) whether the criteria for granting an Option have been met by a potential Participant and (ii) the number of Options to be granted. Article 4.4 of the employee Option plan deals with the vesting scheme of employee options and reads as follows: 'In case of the termination of the employment of a Participant, except for retirement and death, Pharming at its sole discretion is entitled to decide that the Options of the Participant shall lapse. The following schedule shall apply for the cancellation:

- in the event of termination of employment within one year as of a Date of Grant, all Options shall lapse;
- in the event of termination of employment after the first year as of a Date of Grant, all Options, less 1/4 of the number of Options shall be cancelled. The number of Options to be cancelled decreases for each month that the employment continued for more than one year as of that Date of Grant by 1/48 of the number of Options granted of that Date of Grant.'

The Company in its sole discretion may decide to deviate from article 4.4.

In 2012 the Company granted 422,725 options (2011: 2,862,600 options) to employees with a weighted average exercise price of €0.082 (2011: €0.088); fair values for options granted in 2012 were €0.050 (2011: €0.050 to €0.070).

*Notes to the consolidated financial statements continued*

An overview of activity in the number of options for the years 2011 and 2012 is as follows:

	2012		2011	
	Number	Weighted average exercise price (€)	Number	Weighted average exercise price (€)
<b>Balance at January 1</b>	<b>19,424,643</b>	<b>0.314</b>	<b>6,673,077</b>	<b>0.844</b>
Expired	(495,043)	2.901	(363,175)	3.635
<u>Granted under plan for:</u>				
Board of Management	11,437,500	0.056	10,550,000	0.154
Employees	422,725	0.082	2,862,600	0.088
<u>Forfeited under plan for:</u>				
Board of Management	(5,250,000)	0.056	-	-
Employees	(117,727)	0.159	(297,859)	0.279
<b>Balance at December 31</b>	<b>25,422,098</b>	<b>0.198</b>	<b>19,424,643</b>	<b>0.314</b>

No options have been exercised in 2011 and 2012. All options outstanding at December 31, 2012 are exercisable with the exception of the 6,187,500 options granted to the Board of Management and which vested as per January 1, 2013 and are thus exercisable as of that date. For employees subsequent sale of the shares is subject to the vesting conditions of the option. The weighted average remaining contractual life in years of the outstanding options at December 31, 2012 is 3.3 years.

**Exercise prices of options outstanding at December 31, 2012 and the exercise values are in the following ranges:**

Exercise prices in €	Number	Total range exercise value in €'000
0.056-0.122	9,170,169	603
0.154-0.194	10,903,342	1,690
0.200-0.230	576,125	115
0.350-0.530	3,407,459	1,592
0.550-1.260	1,365,003	1,031
	<b>25,422,098</b>	<b>5,031</b>

## Notes to the consolidated financial statements continued

The following assumptions were used in the Black-Scholes model to determine the fair value of options at grant date:

	2012	2011
Expected time to maturity (employees)	2.5 years	2.5 years
Expected time to maturity (Board of Management)	5 years	5 years
Volatility (employees)	75%	78%
Volatility (Board of Management)	60%	64%
Risk-free interest rate (employees)	1.20%	1.68-1.93%
Risk-free interest rate (Board of Management)	1.06%	2.87%

The range of assumptions used in the Monte Carlo simulation to determine the fair value of Long Term Incentive Plan share awards at grant date were:

	2012	2011
Volatilities	22-167%	28-109%
Risk-free interest rates	0.26-1.43%	0.87-3.67%
Dividend yields	0.00%	0.00%

Share-based compensation

Share-based compensation for 2011 and 2012 can be summarized as follows:

Amounts in €'000	2012	2011
Board of Management options	149	844
Employee options	122	82
Long Term Incentive Plan	99	113
	<b>370</b>	<b>1,039</b>

The decrease of Board of Management options expense in 2012 compared to 2011 results from a lower number of options vested combined with lower fair values per option. The decreased employee option expense reflects the effect of lower number of options granted in 2012. Long Term Incentive Plan expenses primarily decreased due to the effect of lower fair values.

### 25. Board of Management

S. de Vries (Chief Executive Officer) and B.M.L. Giannetti (Chief Operations Officer) have been a member of the Board of Management for the entire year 2011 and 2012. K.D. Keegan (Chief Financial Officer) and R.R.D. Pijpstra (Chief Medical Officer) both were a member of the Board of Management in the entire year 2011 and both stepped down as per September 1, 2012; R.R.D. Pijpstra resigned from the Board of Management as of June 19, 2012. The members of the Board of Management are statutory directors.

Base salary of K.D. Keegan was increased from €213,000 in 2011 to €253,000 in 2012; the base salary of the other members of the Board of Management did not increase in 2012.

*Notes to the consolidated financial statements continued*

Compensation of the Members of the Board of Management for 2011 and 2012 was as follows:

Amounts in €'000	Year	Base salary	Extra tax (i)	Bonus	Share-based payment (ii)	Post-employment benefits	Termination benefits (iii)	Other (iv)	Total
B.M.L. Giannetti	2011	266	-	64	199	64	-	15	608
	2012	266	13	80	77	57	-	15	508
K.D. Keegan	2011	213	-	68	204	20	-	15	520
	2012)	169	4	-	6	14	-	10	203
R.R.D. Pijpstra	2011	221	-	53	193	26	-	18	511
	2012	147	-	-	11	23	177	12	370
S. de Vries	2011	396	-	111	299	64	-	36	906
	2012	396	31	198	113	64	-	36	838
<b>Total</b>	<b>2011</b>	<b>1,096</b>	<b>-</b>	<b>296</b>	<b>895</b>	<b>174</b>	<b>-</b>	<b>84</b>	<b>2,545</b>
	<b>2012</b>	<b>978</b>	<b>48</b>	<b>278</b>	<b>207</b>	<b>158</b>	<b>177</b>	<b>73</b>	<b>1,919</b>

- (a) In 2013, the Company is required to pay an additional one-off amount of tax to the Dutch government. The employer tax due is 16% of the surplus of an individual employee's fiscal income in 2012 over €150,000 based on actual payments in 2012.
- (b) Share-based payments for 2012 relates to options of €149,000 (2011: €844,000) and Long Term Incentive Plan of €58,000 (2011: €51,000).
- (c) Effective June 19, 2012 the Company and R.R.D. Pijpstra entered into an agreement as a result of which he resigned from the Management Board with immediate effect and as an employee as of September 1, 2012; his base salary until such date remained €17,000 gross per month and has been fully reflected in the above table. The agreement entitles Rienk Pijpstra to receive a maximum gross amount of €177,000, of which €29,000 was paid upon termination of the employment as per September 1, 2012 and €74,000 was paid upon receipt of US\$10.0 million from Santarus following achievement of the milestone related to successful completion of Study 1310. In addition, Pharming will pay €74,000 upon receipt of US\$5.0 million from Santarus following acceptance of the BLA for review by the FDA or in the event Pharming is acquired by a third party or enters into a partnership with a third party.
- (d) Includes (lease) car compensation and, for S. de Vries, other expenses.

**Notes to the consolidated financial statements continued**

The following table gives an overview of movements in number of option holdings of the individual members of the Board of Management in 2011 and 2012, the exercise prices and expiration dates:

	January 1, 2011	Granted 2011	Granted 2012	Forfeited/ expired 2012	December 31, 2012	Exercise price (€)	Expiration date
B.M.L. Giannetti	140,000	-	-	(140,000)	-	3.050	May 22, 2012
	41,667	-	-	-	41,667	1.120	April 15, 2013
	250,000	-	-	-	250,000	0.620	October 12, 2013
	250,000	-	-	-	250,000	0.500	April 14, 2014
	250,000	-	-	-	250,000	0.401	May 26, 2015
	-	2,275,000	-	-	2,275,000	0.154	May 10, 2016
	=	=	<u>2,437,500</u>	=	<u>2,437,500</u>	0.056	May 13, 2017
	931,667	2,275,000	2,437,500	(140,000)	5,504,167		
S. de Vries	500,000	-	-	-	500,000	0.620	October 12, 2013
	500,000	-	-	-	500,000	0.500	April 14, 2014
	750,000	-	-	-	750,000	0.401	May 26, 2015
	-	3,500,000	-	-	3,500,000	0.154	May 10, 2016
	=	=	<u>3,750,000</u>	=	<u>3,750,000</u>	0.056	May 13, 2017
	1,750,000	3,500,000	3,750,000	-	9,000,000		
<i>In service at December 31, 2012</i>	<i>2,681,667</i>	<i>5,775,000</i>	<i>6,187,500</i>	<i>(140,000)</i>	<i>14,504,167</i>		
K.D. Keegan	350,000	-	-	-	350,000	0.185	September 30, 2015
	-	2,500,000	-	-	2,500,000	0.154	May 10, 2016
	=	=	<u>2,812,500</u>	<u>(2,812,500)</u>	=	0.056	May 13, 2017
	350,000	2,500,000	2,812,500	(2,812,500)	2,850,000		
R.R.D. Pijpstra	40,000	-	-	(7,500)	32,500	0.600	May 31, 2014
	30,000	-	-	-	30,000	0.530	October 19, 2014
	250,000	-	-	-	250,000	0.376	March 29, 2015
	-	2,275,000	-	-	2,275,000	0.154	May 10, 2016
	=	=	<u>2,437,500</u>	<u>(2,437,500)</u>	=	0.056	May 13, 2017
	320,000	2,275,000	2,437,500	(2,445,000)	2,587,500		
<i>Left in 2012</i>	<i>670,000</i>	<i>4,775,000</i>	<i>5,250,000</i>	<i>(5,257,500)</i>	<i>5,437,500</i>		
<b>Total</b>	<b>3,351,667</b>	<b>10,550,000</b>	<b>11,437,500</b>	<b>(5,397,500)</b>	<b>19,941,667</b>		



## **Notes to the consolidated financial statements continued**

The 70,000 options held by R.R.D. Pijpstra expiring in 2014, and partially forfeited in 2012, were granted under the employee option plan in 2009.

**At December 31, 2012, the members of the Board of Management held the following number of shares:**

	<b>Shares held</b>
B.M.L. Giannetti	771,461
S. de Vries	1,192,638
<b>Total</b>	<b>1,964,099</b>

All shares held by members of the Board of Management are unrestricted.

### **Loans or guarantees**

During the year 2012, no loans or guarantees have been granted to Members of the Board of Management. No loans or guarantees to Members of the Board of Management were outstanding at December 31, 2012.

## **26. Board of Supervisory Directors**

### **Remuneration**

The remuneration is based on the position an individual has in the Board of Supervisory Directors (BOSD), the Audit Committee (AC) and the Remuneration Committee (RC). For both 2011 and 2012 the annual compensation is as follows:

- BOSD: Chairman €44,000 and Member €31,000;
- AC: Chairman €9,000 and Member €3,000; and
- RC: Chairman €6,000 and Member €3,000.

An additional compensation of €1,000 per day is paid in case of extraordinary activities.

The members of the Board of Supervisory Directors no longer participate in the Long Term Incentive Plan from 2011 onwards. The entitlements granted in 2010 (covering the years 2010-2012) have ended in 2012 with no shares issued.

## Notes to the consolidated financial statements continued

Compensation of the Members of the Board of Supervisory Directors for 2011 and 2012 was as follows:

Amounts in €'000	Year	BOSD	AC	RC	Extra-ordinary	Share-based payment	Total
J. Blaak	2011	44	-	3	-	3	50
	2012	44	-	3	-	2	49
J.H.L. Ernst	2011	31	3	3	-	2	39
	2012	31	3	3	3	2	42
J.B. Ward	2011	31	3	6	-	3	43
	2012	31	3	6	-	2	42
A. de Winter	2011	31	9	-	-	2	42
	2012	31	9	-	-	2	42
<b>Total</b>	<b>2011</b>	<b>137</b>	<b>15</b>	<b>12</b>	<b>-</b>	<b>10</b>	<b>174</b>
	<b>2012</b>	<b>137</b>	<b>15</b>	<b>12</b>	<b>3</b>	<b>8</b>	<b>175</b>

### Shares, options and warrants

Members of the Board of Supervisory Directors do not participate in an option plan but are eligible to receive shares under the Long Term Incentive Plan for the year 2010 (covering the years 2010-2012); as of 2011 members of the Board of Supervisory Directors no longer participate in the Long Term Incentive Plan. At year end 2012 none of the Board of Supervisory Directors Members in place held shares, options or warrants in the Company.

### Loans or guarantees

During the year 2012, the Company has not granted loans or guarantees to any Member of the Board of Supervisory Directors. No loans or guarantees to Members of the Board of Supervisory Directors were outstanding at December 31, 2012.

## 27. Income taxes

No current or deferred income taxes applied to the statement of income in both 2011 and 2012 and no other tax items apply to either equity or comprehensive income in both years.

The Dutch fiscal unity at year end 2012 has approximately €192 million of taxable losses that can be offset in the years 2013-2021. The Board of Management has considered the Company's history of losses and concluded that it is not probable that the benefits of these tax loss carry forward will be realized in the near term. Accordingly, the Company did not record a deferred tax asset.

*Notes to the consolidated financial statements continued*

**28. Warrants**

An overview of activity in the number of warrants for the years 2011 and 2012 is as follows:

	2012		2011	
	Number	Weighted average exercise price (€)	Number	Weighted average exercise price (€)
<b>Balance at January 1</b>	<b>5,208,333</b>	<b>0.110</b>	<b>32,697,956</b>	<b>0.337</b>
Issued	103,022,984	0.067	-	-
Exercised	(29,259,591)	0.017	(24,339,623)	0.212
Expired	-	-	(3,150,000)	1.667
Adjustments to exercise price	-	(0.070)	-	(0.010)
<b>Balance at December 31</b>	<b>78,971,726</b>	<b>0.018</b>	<b>5,208,333</b>	<b>0.110</b>

The weighted average remaining contractual life in years of the outstanding warrants at December 31, 2012 is 4.5 years.

Warrants exercised in 2011 relate to 24,339,623 warrants issued to Socius CG II, Ltd. as explained in Note 10. In 2011, the exercise price of the 5,208,333 warrants remaining at year end had been decreased from €0.120 to €0.110 following the 2011 issue of shares at €0.110.

In 2012 the Company formally issued 20,300,000 warrants with an exercise price of €0.06 following a private placement in 2011 (Note 10), 38,717,484 warrants with an exercise price of €0.12 in relation to the Bonds 2012 (Note 13) and 44,005,500 warrants with an exercise price of €0.0233 in relation to the Equity Working Capital Facility (Note 10). Due to issue of shares under the Equity Working Capital Facility at a price of €0.013878, the exercise price of warrants related to other transactions was ultimately adjusted to €0.013878 at December 31, 2012.

Overall, the number of outstanding warrants at December 31, 2012 is comprised of 44,394,226 warrants with an exercise price of €0.013878 and 34,577,500 warrants with an exercise price of €0.0233.

In order to protect the warrant holders from the (potential) effects of dilution, both the number of warrants as well as their exercise prices can be adjusted in the event of issue of new shares or share rights (e.g. warrants) for conditions more favorable than for existing warrant holders (e.g. issue of new shares at a consideration below the existing exercise price); a number of transactions, such as the issue of options to members of the Board of Management and employees, are excluded from these adjustment clauses.

## **Notes to the consolidated financial statements continued**

### **29. Operating segments**

Until January 31, 2011 the Company's operations were set up along two business units, being the recombinant protein business and the DNage business. These units had separate reporting lines and separate financial statements. The recombinant protein business included Pharming Group N.V. as the listed entity of the Pharming Group including the operating companies in the Netherlands and the United States. The DNage business related to the cash-generating unit DNage B.V. Following discontinuation of the DNage operations the consolidated statement of financial position at year end 2011 and year end 2012 exclusively related to the recombinant proteins unit while no investments and no DNage cash flows apply for both 2011 and 2012. The 2011 statement of income included a result of discontinued operations (profit of €643,000) that relate to the DNage entity as discussed in Note 23; the 2012 statement of income did not include any results from the DNage business unit.

#### **Supplemental disclosure operating segments**

The main foreign assets of the Recombinant proteins business unit related to the property, plant and equipment of Pharming Healthcare, Inc. in the United States. The carrying value of these assets at December 31, 2011 amounted to €1,960,000. Following sale of these assets in 2012 the Company received an amount of €722,000 in cash and posted impairment charges of €1,222,000; the carrying value at year-end 2012 amounted to €nil.

### **30. Related party transactions**

Related-parties disclosure relates entirely to the key management of Pharming, being represented by the Members of the Board of Management and the Board of Supervisory Directors.

All direct transactions with Members of the Board of Management and Board of Supervisory Directors have been disclosed in Notes 25 and 26 of these Financial Statements. At December 31, 2012, the Company owed a total amount of €409,000 to Members of the Board of Management with respect to their compensation.

### **31. Commitments and contingencies**

#### **Operating lease commitments**

The Company has entered into operating lease agreements for the rent of office and laboratory facilities, ending in 2016, as well as lease cars for employees (agreements in place at year end 2012 expiring in 2013-2016).

**Future minimum rentals payable under these non-cancellable leases at the end of 2011 and 2012 was as follows:**

<b>Amounts in €'000</b>	<b>2012</b>	<b>2011</b>
Within one year	673	713
After one year but not more than five years	1,648	2,285
More than five years	-	-
	<b>2,321</b>	<b>2,998</b>

## **Notes to the consolidated financial statements continued**

### **Material Agreements**

At end of the reporting year, the Company had entered into several agreements with third parties under which Pharming has to pay cash in case goods or services have been provided or certain performance criteria have been met. In general, these relate to:

- the manufacturing of rhC1INH, including fill and finish activities; and
- milestone payments for research and development activities, including clinical trials.

Total potential liabilities under these agreements are approximately €89 million, of which €10 million is for 2013, €40 million for 2014-2017 and €39 million beyond 2017.

## **32. Financial risk management**

### **General**

Pharming is exposed to several financial risks: market risks (being currency risk and interest rate risk), credit risks and liquidity risks. The Board of Management is responsible for the management of currency, interest, credit and liquidity risks and as such ultimately responsible for decisions taken in this field.

### **Capital risk management**

The Company manages its capital to ensure that it will be able to continue as a going concern. This includes a regular review of cash flow forecasts and, if deemed appropriate, subsequent attraction of funds through execution of equity and/or debt transactions. In doing so, the Board of Management's strategy is to achieve a capital structure which takes into account the best interests of all stakeholders. Pharming's capital structure includes cash and cash equivalents, equity and (convertible) debt. Compared to last year there have been no significant changes in risk management policies.

### **Currency risk**

This is the risk that the fair value of future cash flows of a financial instrument will fluctuate because of changes in foreign exchange rates. Pharming's policy for the management of foreign currency risks is aimed at protecting the operating results and positions held in foreign currencies, in particular of the United States dollar (US\$). The US\$ is used to finance the local operations of US-based entities and make direct payment of US activities carried out through the Dutch entities. If deemed appropriate, taking into account market expectations on the development of the US\$, US\$ are acquired in advance to cover such forecasted US\$ payments. So far, Pharming's foreign currency risk policy for the US\$ has not included derivative agreements.

At December 31, 2012 the Company's cash and cash equivalents, including restricted cash, amounted to €6.3 million. This balance consists of cash assets denominated in € for a total amount of €5.6 million and cash assets in US\$ for a total amount of US\$0.9 million or €0.7 million (applying an exchange rate € to US\$ at December 31, 2012 of 0.759 to 1).

### **Interest rate risk**

Interest rate risk is the risk that the fair value of future cash flows of a financial instrument will fluctuate because of changes in market interest rates. Pharming's interest rate risk policy is aimed at minimizing the interest rate risks associated with the financing of the Company and thus at the same time optimizing the net interest costs. This policy translates into a certain desired profile of fixed-interest and floating interest positions, including those generated by cash and cash equivalents and those paid on finance lease liabilities. The Company performed a sensitivity analysis in which the effect of a 1% interest increase or 1% interest decrease on the carrying value of the financial instruments at year-end 2012 was measured. Pharming concluded that the total effect taking place on the carrying value of these items would be less than €0.1 million.

## **Notes to the consolidated financial statements continued**

### **Credit risk**

Credit risk is defined as the risk that one party to a financial instrument will cause a financial loss for the other party by failing to discharge obligations. Pharming manages credit risk exposure through the selection of financial institutions having a high credit rating, using credit rating reports issued by institutions such as Standard & Poor's and Moody's.

The maximum exposure to credit risk at December 31, 2012 is represented by the carrying amounts of cash and cash equivalents, assets held for sale and trade and other receivables.

The carrying amounts of the cash and cash equivalents (including restricted cash) as per December 31, 2012 amounted to €6.3 million and was held through a financial institution with an A+ rating from Standard & Poor's, an A2 rating from Moody's and an A+ rating from Fitch.

Assets held for sale as per December 31, 2012 of €0.2 million were fully settled in cash in 2013.

Trade and other receivables at December 31, 2012 amounted to €0.5 million. As per the date of these financial statements these amounts have largely been settled, including receipts in cash and receipt of goods and services in exchange of prepaid expense items. Altogether approximately €0.5 million of various items are subject to receipts of cash, goods or services after the end of these financial statements with no indication that such an event will not take place.

Based on the credit ratings of cash and cash equivalents (including restricted cash) as well as the position taken with respect to trade and other receivables, the Company estimates that total maximum exposure to credit risk at the end of 2012 is less than €0.1 million.

### **Liquidity risk**

The liquidity risk refers to the risk that an entity will encounter difficulty in meeting obligations associated with financial liabilities. Pharming's objective is to maintain a minimum level and certain ratio of cash and cash equivalents (including short-term deposits). The strategy of the Company is to repay its obligations through generation of cash income from operating activities such as product sales and licensing agreements. In case such cash flows are insufficient, the Company relies on financing cash flows as provided through the issuance of shares or incurring financial liabilities. Note 2 of these financial statements more extensively describe the Company's going concern assessment.

The following table presents the financial liabilities at year-end 2012, showing the remaining undiscounted contractual amounts due including nominal interest. Liabilities denominated in foreign currency have been converted at the exchange rate at December 31, 2012. Trade and other payables exclude €29,000 non-cash lease incentives released to the statement of income in 2013. The derivative financial liabilities relates to the fair value of warrant rights which can be exercised by warrant holders throughout the remaining lifetime.

<b>Amounts in €'000</b>	<b>2013</b>	<b>2014</b>	<b>2015</b>	<b>2016</b>	<b>2017</b>
Trade and other payables	3,582	-	-	-	-
Derivative financial liabilities	1,215	-	-	-	-
Finance lease liabilities	937	474	292	286	275
Restructuring provision	1,232	-	-	-	-
<b>Total</b>	<b>6,966</b>	<b>474</b>	<b>292</b>	<b>286</b>	<b>275</b>

## Notes to the consolidated financial statements continued

### Fair value estimation

The Company uses the following hierarchy for determining the fair value of financial instruments measured at fair value:

- Quoted prices (unadjusted) in active markets for identical assets or liabilities (level 1);
- Inputs other than quoted prices included within level 1 that are observable for the asset or liability, either directly (that is, as prices) or indirectly (that is, derived from prices) (level 2);
- Inputs for the asset or liability that are not based on observable market data (that is, unobservable inputs) (level 3).

The following table presents the liabilities that are measured at fair value at year-end 2011 and 2012:

Amounts in €'000	2012		2011	
	Level 3	Total	Level 3	Total
Financial liabilities at fair value through profit or loss	1,215	1,215	1,171	1,171
<b>Total liabilities</b>	<b>1,215</b>	<b>1,215</b>	<b>1,171</b>	<b>1,171</b>

The financial liabilities measured at fair value through profit or loss relates to warrants not publicly traded and for which no other observable inputs are available and accordingly the fair value of the warrants has been determined through the Black-Scholes model, applying the following parameters per the end of:

	2012	2011
Expected time to maturity of warrants in issue	4.5 years	1.0 year
Expected time to maturity of warrants to be issued	-	4.5 years
Volatility	70-72%	79%
Risk-free interest rate	0.619-0.720%	1.417%

As per Note 2.3 (Significant accounting judgments and estimates) the Company has performed a sensitivity analysis which demonstrates the potential possible effects in the event that derivative financial liabilities are settled for shares at a fair value price different from the exercise value. The following table provides an overview of the effect on the statement of income assuming the 78,971,726 warrants outstanding at December 31, 2012 with a total fair value of €1,215,000 and an exercise value of €1,422,000 are exercised with the fair value per share upon exercise ranging between €0.030 and €0.100 while applying an interval of €0.010.

*Notes to the consolidated financial statements continued*

Impact on statement of income if 78,971,726 warrants outstanding at year-end 2012 are exercised at an assumed fair value per share between €0.030 and €0.100:

Fair value per share upon exercise in €	Fair value total shares upon exercise in €'000	Exercise value in €'000	Actual fair value warrants in €'000	Fair value warrants at December 31, 2012 in €'000	Additional profit/(loss) in €'000
0.030	2,369	1,422	947	1,215	268
0.040	3,159	1,422	1,737	1,215	(522)
0.050	3,949	1,422	2,527	1,215	(1,312)
0.060	4,738	1,422	3,316	1,215	(2,101)
0.070	5,528	1,422	4,106	1,215	(2,891)
0.080	6,318	1,422	4,896	1,215	(3,681)
0.090	7,107	1,422	5,685	1,215	(4,470)
0.100	7,897	1,422	6,475	1,215	(5,260)

The following table includes carrying values and the estimated fair values of financial instruments:

Amounts in €'000	2012		2011	
	Carrying value	Fair value	Carrying value	Fair value
<b>Assets:</b>				
Cash and cash equivalents, including restricted cash	6,314	6,314	5,065	5,065
Assets held for sale	242	266	-	-
Trade and other receivables	524	524	2,495	2,495
<b>Liabilities:</b>				
Finance lease liabilities	2,856	2,856	3,433	3,433
Trade and other payables	3,690	3,690	3,810	3,810
Derivative financial liabilities	1,215	1,215	1,171	1,171
Restructuring provision	1,232	1,232	-	-

The above fair values of financial instruments are based on internal calculations with the exception of the derivative financial liabilities as calculated by an independent valuator. Cash and cash equivalents, trade and other receivables as well as trade and other payables are stated at carrying amount, which approximates the fair value in view of the short maturity of these instruments. The fair values of finance lease liabilities (both non-current and current portion) are based on arm's length transactions.



## Notes to the consolidated financial statements continued

### 33. Earnings per share and fully-diluted shares

#### Earnings per share

Basic earnings per share is calculated based on the weighted average number of ordinary shares outstanding during the year, being 470,223,995 for 2011 and 729,772,688 for 2012. For the purpose of the basic loss per share as presented in these financial statements, these numbers have been revised to 47,022,400 for 2011 and 72,977,269 for 2012 in order to reflect the 10:1 reverse share split effected on March 5, 2013 (also see Note 34). For 2011 and 2012, the basic loss per share is:

	2012	2011
Net loss attributable to equity owners of the parent (in €'000)	(24,093)	(17,104)
Weighted average shares outstanding	72,977,269	47,022,400
Basic loss per share (in €)	(0.330)	(0.364)

Diluted earnings per share is computed based on the weighted average number of ordinary shares outstanding including the dilutive effect of shares to be issued in the future under certain arrangements such as option plans, warrants issued and convertible loan agreements. There is no difference in basic and diluted net loss per share recorded by the Company because the impact of the arrangements referred to is anti-dilutive in all periods.

#### Fully-diluted shares

The composition of the number of shares and share rights outstanding as well as authorized share capital as per December 31, 2012 and the date of these financial statements are provided in the following tables. The first table provides an overview until March 5, 2013 – on which date a reverse share split was legally effected and authorized share capital was increased (see Note 34) – and the second table provides an overview between the reverse share split and the date of these financial statements.

#### Movements between December 31, 2012 and March 5, 2013:

	December 31, 2012	Shares issued	Other	March 5, 2013
Shares	1,009,189,097	180,000,000	-	1,189,189,097
Warrants	78,971,726	-	-	78,971,726
Options	25,422,098	-	(13,090)	25,409,008
LTIP	4,879,920	-	-	4,879,920
<b>Issued</b>	<b>1,118,462,841</b>	<b>180,000,000</b>	<b>(13,090)</b>	<b>1,298,449,751</b>
Available for issue	181,537,159	(180,000,000)	13,090	1,550,249
<b>Authorized share capital</b>	<b>1,300,000,000</b>	-	-	<b>1,300,000,000</b>

**Notes to the consolidated financial statements continued**

**Movements between March 5, 2013 and the date of these financial statements:**

	<b>Amendments to articles of association on March 5, 2013</b>			
	<b>Prior to amendments</b>	<b>After amendments</b>	<b>Issued</b>	<b>March 29, 2013</b>
Shares	1,189,189,097	118,918,910	13,217,168	132,136,078
Warrants	78,971,726	7,897,173	16,350,000	24,247,173
Options (*)	25,409,008	2,540,901	-	2,540,901
LTIP	4,879,920	487,992	-	487,992
<b>Issued</b>	<b>1,298,462,841</b>	<b>129,844,976</b>	<b>29,567,168</b>	<b>159,412,144</b>
Available for issue	1,537,159	320,155,024	(29,567,168)	290,587,856
<b>Authorized share capital</b>	<b>1,300,000,000</b>	<b>450,000,000</b>	-	<b>450,000,000</b>

(\*) article 5.3 (b) of both the Option plan for the BOM and the Option plan for the employees reads as follows: “ If the Shares are consolidated, each Option shall confer the right to acquire a proportionate amount of one newly emerged share as per the date of the consolidation. It is not possible to acquire a part of a share.” As a result, the number of options subsequent to the reverse share split itself is not adjusted but the number of shares that can be acquired is one-tenth of the number of options; for the purpose of this table the number of options as presented after the amendments of the articles of association have been presented based on the potential number of shares that can be acquired through the exercise of options.

With respect to the 2013 movements of outstanding shares and share rights, further reference is given to Events after the reporting year in Note 34.

**34. Events after the reporting year**

From January 1, 2013 until the date of these financial statements, Pharming did not grant any options whereas 12,250 options expired (all prior to reverse share split) and 840 options were forfeited (all prior to reverse share split); all these option movements took place under the employee option plan.

On January 16, 2013, the Company announced it had entered into a convertible debt financing of €16.35 million (€15.3 million net proceeds after subtraction of transaction fees and a 2% issuers discount); the financing was subject to – among others - shareholder approval of amendments to the Company’s articles of association, as explained below. The Company also issued 180 million shares to the investors as down payment for the first amortization(s). On February 28, 2013, an Extraordinary General Meeting of Shareholders was held and shareholder approval was received to implement (i) a 10:1 reverse share split (authorized share capital decreased from 1,300 million to 130 million shares, while the nominal value per share increased from €0.01 to €0.10), followed by (ii) a reduction of the nominal value of the shares from €0.10 to €0.01, and (iii) an increase of authorized share capital from 130 million to 450 million shares.

### ***Notes to the consolidated financial statements continued***

Following the approval by the shareholders, the Company received a net cash amount of €16.0 million in relation to the transaction; an amount of €0.8 million in fees and expenses are payable by the Company. The convertible bonds carry 8.5% interest per annum, have a fixed conversion price of €0.03 and may be redeemed in cash or shares at the option of the Company in seven monthly tranches between March and September 2013. If the Company elects to pay a tranche in shares, the number of shares to be paid is based on 93.5% of the lowest ten volume weighted average price of the Company's shares over a 20 day pricing period. The bondholders received 16,350,000 warrants with an exercise price of €0.30 (adjustable in the event of certain developments); the warrants are exercisable for five years as of February 28, 2013.

On March 8, 2013 the Company issued 13,217,168 shares to the holders of the above bonds; in addition to the initial number of 180,000,000 shares transferred (which equals 18,000,000 shares following the reverse share split), the first and second installment of in total seven installments has been redeemed as per the date of these financial statements.

Following the above transactions, the exercise price of 3,457,750 warrants (prior to reverse share split equaling 34,577,500 warrants outstanding at December 31, 2012) was adjusted from €0.233 (prior to reverse share split equaling €0.0233) to €0.15754; the exercise price of the other 4,429,423 warrants (prior to reverse share split equaling 44,394,226 warrants outstanding at December 31, 2012) has not changed at €0.13878 (prior to reverse share split: €0.013878).

## Company financial statements

## COMPANY STATEMENT OF FINANCIAL POSITION

For the year ended December 31 (after proposed appropriation of net loss)

Amounts in €'000	Notes	2012	2011
Property, plant and equipment	3	317	404
<b>Non-current assets</b>		<b>317</b>	<b>404</b>
Trade and other receivables	4	213	1,919
Restricted cash	5	62	62
Cash and cash equivalents	5	6,066	4,360
<b>Current assets</b>		<b>6,341</b>	<b>6,341</b>
<b>Total assets</b>		<b>6,658</b>	<b>6,745</b>
Share capital	6	10,092	20,405
Share premium	6	231,866	224,495
Foreign currency translation	6	-	(1,449)
Other reserves	6	14,144	13,774
Accumulated deficit	6	(263,754)	(258,413)
<b>Shareholders' equity</b>		<b>(7,652)</b>	<b>(1,188)</b>
<b>Provision for subsidiaries</b>	7	<b>11,604</b>	<b>5,479</b>
Finance leases liabilities		3	6
<b>Non-current liabilities</b>		<b>3</b>	<b>6</b>
Derivative financial liabilities	8	1,215	1,171
Restructuring provision	9	179	-
Trade and other payables	10	1,306	1,243
Finance lease liabilities		3	34
<b>Current liabilities</b>		<b>2,703</b>	<b>2,448</b>
<b>Total shareholders' equity and liabilities</b>		<b>6,658</b>	<b>6,745</b>

*The notes are an integral part of these financial statements.*

**COMPANY STATEMENT OF INCOME**

For the year ended December 31

<b>Amounts in €'000</b>	<b>Notes</b>	<b>2012</b>	<b>2011</b>
Share in result of investments	7	(12,865)	(12,154)
Other results	11	(11,228)	(5,046)
<b>Net loss</b>		<b>(24,093)</b>	<b>(17,200)</b>

*The notes are an integral part of these financial statements.*

## Notes to the Company financial statements

## Notes to the Company financial statements

For the year ended December 31, 2012

### 1. General

Within the Pharming Group, the entity Pharming Group N.V. acts as a holding company of the operating companies. Its activities are limited to the arrangement of financial transactions with third parties and to provide the operating companies with support in the field of legal, financial, human resources, public relations, IT and other services.

### 2. Summary of significant accounting policies

The company financial statements are prepared in accordance with accounting principles generally accepted in the Netherlands.

Accounting policies applied are substantially the same as those used in the consolidated financial statements in accordance with the provisions of article 362-8 of Book 2 of the Netherlands Civil Code, except for investments in subsidiaries which are accounted for using the equity method. In conformity with article 402 Book 2 of the Netherlands Civil Code, a condensed statement of income is included in the company financial statements of Pharming Group N.V.

### 3. Property, plant and equipment

Property, plant and equipment carried include leasehold improvements relate to office investments in the Company's leased headquarters and other items such as office furniture and equipment as well as hardware and software.

**Movement of property, plant and equipment for the financial years 2011 and 2012 is:**

Amounts in €'000	Leasehold improvements	Other	Total
At cost	747	447	1,194
Accumulated depreciation charges	(325)	(331)	(656)
<b>Carrying value at January 1, 2011</b>	<b>422</b>	<b>116</b>	<b>538</b>
Investments	-	25	25
Depreciation charges	(77)	(82)	(159)
<b>Movement 2011</b>	<b>(77)</b>	<b>(57)</b>	<b>(134)</b>
At cost (*)	747	472	1,219
Accumulated depreciation charges (*)	(402)	(413)	(815)
<b>Carrying value at December 31, 2011</b>	<b>345</b>	<b>59</b>	<b>404</b>
Investments	-	13	13
Depreciation charges	(77)	(23)	(100)
<b>Movement 2012</b>	<b>(77)</b>	<b>(10)</b>	<b>(87)</b>
At cost	747	485	1,232
Accumulated depreciation charges	(479)	(436)	(915)
<b>Carrying value at December 31, 2012</b>	<b>268</b>	<b>49</b>	<b>317</b>

(\*) the Company eliminated fully depreciated assets no longer in use from accumulated costs and accumulated depreciation with an effect of €117,000 in 2011



## Notes to the Company financial statements continued

### 4. Trade and other receivables

Trade and other receivables at year-end 2011 and 2012 comprised:

Amounts in €'000	2012	2011
Advance payment in shares	-	1,503
Prepaid expenses	111	177
Value added tax	36	116
Other receivables	66	123
<b>Balance at December 31</b>	<b>213</b>	<b>1,919</b>

Trade and other receivables at December 31, 2012 are substantially short-term in nature and have largely been settled as per the date of these financial statements. The advance payment in shares at December 31, 2011 has been further described in Note 10 of the consolidated financial statements.

### 5. Restricted cash, cash and cash equivalents

The overall cash position at year-end 2011 and 2012 was as follows:

Amounts in €'000	2012	2011
Current restricted cash	62	62
Cash and cash equivalents	6,066	4,360
<b>Balance at December 31</b>	<b>6,128</b>	<b>4,422</b>

Current restricted cash of €62,000 reflects a bank guarantee issued. This guarantee was, contrary to year end 2011 expectations, not settled in 2012; settlement is now anticipated to take place in 2013. Cash and cash equivalents are defined as cash on hand, demand deposits and short-term, highly liquid investments (maturity less than 3 months) readily convertible to known amounts of cash and subject to insignificant risk of changes in value.

The holding company Pharming Group N.V. has entered into a joint liability agreement with a bank and other group companies. Pursuant to this agreement, the entity at December 31, 2012 is jointly liable for commitments relating to bank guarantees for an aggregate amount of €1,041,000 of which €732,000 with a maturity of more than one year after the end of the reporting year and €309,000 with a maturity of less than one year after the end of the reporting year. Of the total guarantees of €1,041,000, an amount of €62,000 is carried in the company financial statement of position and the remaining €979,000 is accounted for by other group companies.

## **Notes to the Company financial statements continued**

### **6. Shareholders' equity**

The Company's authorized share capital amounts to €13.0 million and is divided into 1,300,000,000 ordinary shares with a nominal value of €0.01 each. All 1,009,189,097 shares outstanding at December 31, 2012 have been fully paid-up.

**Movements in Shareholders' equity for 2011 and 2012 were as follows:**

<b>Amounts in €'000</b>	<b>2012</b>	<b>2011</b>
<b>Balance at January 1</b>	<b>(1,188)</b>	<b>10,864</b>
Net loss	(24,093)	(17,200)
Foreign currency translation	65	65
Recycling equity translation reserve	1,384	-
Share-based compensation	370	1,039
Bonuses settled in shares	274	103
Bond payments in shares	9,924	-
Shares/warrants issued for cash	4,745	1,464
Warrants exercised	867	974
Advance shares issued	-	1,503
<b>Balance at December 31</b>	<b>(7,652)</b>	<b>(1,188)</b>

For a detailed movement schedule of equity for the years 2011 and 2012, please refer to the schedule consolidated statement of changes in equity. The main fluctuations in equity have been described in Note 10 to the consolidated financial statements.

### **7. Provision for subsidiaries**

Investments in subsidiaries are those investments with a positive equity value. In the event the equity value of a group company together with any long-term interests that, in substance, form part of the our net investment in the group company, becomes negative, additional losses are provided for, and a liability is recognized, only to the extent that we have incurred legal or constructive obligations or made payments on behalf of the subsidiary.

**Notes to the Company financial statements continued**

**Movement of financial assets and the provision for subsidiaries for the years 2011 and 2012 was as follows:**

Amounts in €'000	Investments in subsidiaries	Provision for subsidiaries	Net total
<b>Balance at January 1, 2011</b>	<b>282</b>	<b>(177,186)</b>	<b>(176,904)</b>
Share in results of investments	-	(12,154)	(12,154)
Exchange rate effects	(510)	-	(510)
Reclassification	228	(228)	-
<b>Balance at December 31, 2011</b>	<b>-</b>	<b>(189,568)</b>	<b>(189,568)</b>
Share in results of investments	-	(12,865)	(12,865)
Exchange rate effects		340	340
Reclassification			-
<b>Balance at December 31, 2012</b>	<b>-</b>	<b>(202,093)</b>	<b>(202,093)</b>

**At year end 2011 and 2012, the provision for subsidiaries was offset with the following receivable balances from Pharming Group N.V.:**

Amounts in €'000	2012	2011
Provision for subsidiaries	(202,093)	(189,568)
Receivable	190,489	184,089
<b>Net payable</b>	<b>(11,604)</b>	<b>(5,479)</b>
Of which classified as Provision for subsidiaries	(11,604)	(5,479)
<b>Receivable from group companies</b>	<b>-</b>	<b>-</b>

**8. Derivative financial liabilities**

The backgrounds of the derivative financial liabilities have been provided in Note 13 of the consolidated financial statements.

**9. Restructuring provision**

The backgrounds of the restructuring provision have been provided in Note 14 of the consolidated financial statements. The amount presented in the company statement of financial position exclusively relates to the employees in service by the parent entity.

## **Notes to the Company financial statements continued**

### **10. Trade and other payables**

Trade and other payables consist of:

<b>Amounts in €'000</b>	<b>2012</b>	<b>2011</b>
Accounts payable	151	266
Taxes and social security	129	48
Deferred compensation due to related parties	409	400
Other payables	617	529
<b>Balance at December 31</b>	<b>1,306</b>	<b>1,243</b>

The amount of deferred compensation due to related parties involves Members of the Board of Management and includes bonuses, holiday allowances and holiday rights.

### **11. Other results**

Other results in 2011 and 2012 include costs of share-based compensation in the amount of €1,039,000 respective €370,000, as disclosed in Note 24 of the consolidated financial statements. These charges include those related to Members of the Board of Management and employees.

### **12. Employee information**

All employees of Pharming Group N.V. in both 2011 and 2012 were based in the Netherlands. The number of full-time equivalent employees in 2012 was 13 (2011: 12) and the number of employees at December 31, 2012 was 12 (December 31, 2011: 14).

### **13. Related party transactions**

Related-parties disclosure relates entirely to the key management of Pharming, being represented by the Members of the Board of Management and the Board of Supervisory Directors.

All direct transactions with Members of the Board of Management and Board of Supervisory Directors have been disclosed in Notes 25 and 26 of the Consolidated Financial Statements. At December 31, 2012, the Company owed a total amount of €409,000 to Members of the Board of Management with respect to their compensation (see Note 11 of the Company Financial Statements).

## Independent auditor's report

## **Independent auditor's report**

To the General Meeting of Shareholders of Pharming Group N.V.

### **Report on the financial statements**

We have audited the accompanying financial statements 2012 of Pharming Group N.V., Leiden as set out on pages 48 to 116. The financial statements include the consolidated financial statements and the company financial statements. The consolidated financial statements comprise the consolidated statement of financial position as at 31 December 2012, the consolidated statement of income, the consolidated statements of comprehensive income, changes in equity and cash flows for the year then ended and the notes, comprising a summary of significant accounting policies and other explanatory information. The company financial statements comprise the company statement of financial position as at 31 December 2012, the company statement of income for the year then ended and the notes, comprising a summary of accounting policies and other explanatory information.

### **Management's responsibility**

The Board of Management is responsible for the preparation and fair presentation of these financial statements in accordance with International Financial Reporting Standards as adopted by the European Union and with Part 9 of Book 2 of the Dutch Civil Code, and for the preparation of the management report in accordance with Part 9 of Book 2 of the Dutch Civil Code. Furthermore, the Board of Management is responsible for such internal control as it determines is necessary to enable the preparation of the financial statements that are free from material misstatement, whether due to fraud or error.

### **Auditor's responsibility**

Our responsibility is to express an opinion on these financial statements based on our audit. We conducted our audit in accordance with Dutch law, including the Dutch Standards on Auditing. This requires that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the company's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the company's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by the management board, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

### **Opinion with respect to the consolidated financial statements**

In our opinion, the consolidated financial statements give a true and fair view of the financial position of Pharming Group N.V. as at 31 December 2012, and of its result and its cash flows for the year then ended in accordance with International Financial Reporting Standards as adopted by the European Union and with Part 9 of Book 2 of the Dutch Civil Code.

### **Opinion with respect to the company financial statements**

In our opinion, the company financial statements give a true and fair view of the financial position of Pharming Group N.V. as at 31 December 2012, and of its result for the year then ended in accordance with Part 9 of Book 2 of the Dutch Civil Code.

### **Emphasis of uncertainty with respect to the going concern assumption**

We draw attention to Note 3 to the consolidated financial statements, to the net loss incurred of € 24,093,000 during the year ended 31 December 2012 and to the negative shareholders' equity of € 7,652,000 as at 31 December 2012. These conditions indicate the existence of a material uncertainty which may cast significant doubt about the company's ability to continue as a going concern. Our opinion is not qualified in respect of this matter.

***Independent auditor's report continued***

**Report on other legal and regulatory requirements**

Pursuant to the legal requirement under Section 2: 393 sub 5 at e and f of the Dutch Civil Code, we have no deficiencies to report as a result of our examination whether the management report, to the extent we can assess, has been prepared in accordance with Part 9 of Book 2 of this Code, and whether the information as required under Section 2: 392 sub 1 at b-h has been annexed. Further we report that the management report, to the extent we can assess, is consistent with the financial statements as required by Section 2: 391 sub 4 of the Dutch Civil Code.

Utrecht, 29 March 2013

PricewaterhouseCoopers Accountants N.V.

A.C.M. van der Linden RA

## **OTHER FINANCIAL INFORMATION**

### **For the year ended December 31, 2012**

#### **1. Appropriation of result**

Article 25.1 of the Articles of Association reads as follows: 'The management board shall annually determine, subject to the approval of the Board of Supervisory Directors, the amount of the distributable profit – the surplus on the profit and loss account – to be reserved.'

#### **2. Proposed appropriation of net loss**

The Company proposes to forward the net loss for the year 2012 to the accumulated deficit. Anticipating the approval of the Financial Statements by the Shareholders at the Annual General Meeting of Shareholders, this proposal has already been reflected in the Financial Statements.

#### **3. Events after the reporting year**

From January 1, 2013 until the date of these financial statements, Pharming did not grant any options whereas 12,250 options expired (all prior to reverse share split) and 840 options were forfeited (all prior to reverse share split); all these option movements took place under the employee option plan.

On January 16, 2013, the Company announced it had entered into a convertible debt financing of €16.35 million (€15.3 million net proceeds after subtraction of transaction fees and a 2% issuers discount); the financing was subject to – among others - shareholder approval of amendments to the Company's articles of association, as explained below. The Company also issued 180 million shares to the investors as down payment for the first amortization(s). On February 28, 2013, an Extraordinary General Meeting of Shareholders was held and shareholder approval was received to implement (i) a 10:1 reverse share split (authorized share capital decreased from 1,300 million to 130 million shares, while the nominal value per share increased from €0.01 to €0.10), followed by (ii) a reduction of the nominal value of the shares from €0.10 to €0.01, and (iii) an increase of authorized share capital from 130 million to 450 million shares.

Following the approval by the shareholders, the Company received a net cash amount of €16.0 million in relation to the transaction; an amount of €0.8 million in fees and expenses are payable by the Company. The convertible bonds carry 8.5% interest per annum, have a fixed conversion price of €0.03 and may be redeemed in cash or shares at the option of the Company in seven monthly tranches between March and September 2013. If the Company elects to pay a tranche in shares, the number of shares to be paid is based on 93.5% of the lowest ten volume weighted average price of the Company's shares over a 20 day pricing period. The bondholders received 16,350,000 warrants with an exercise price of €0.30 (adjustable in the event of certain developments); the warrants are exercisable for five years as of February 28, 2013.

On March 8, 2013 the Company issued 13,217,168 shares to the holders of the above bonds; in addition to the initial number of 180,000,000 shares transferred (which equals 18,000,000 shares following the reverse share split), the first and second installment of in total seven installments has been redeemed as per the date of these financial statements.

Following the above transactions, the exercise price of 3,457,750 warrants (prior to reverse share split equaling 34,577,500 warrants outstanding at December 31, 2012) was adjusted from €0.233 (prior to reverse share split equaling €0.0233) to €0.15754; the exercise price of the other 4,429,423 warrants (prior to reverse share split equaling 44,394,226 warrants outstanding at December 31, 2012) has not changed at €0.13878 (prior to reverse share split: €0.013878).



## APPENDICES

### Appendix 1 2012 Publications on Ruconest®

Hack CE, Relan A, Baboeram A, Oortwijn B, Versteeg S, van Ree R, Pijpstra R. Immuno-safety of recombinant human C1-inhibitor in hereditary angioedema: no evidence for IgE responses. *Clinical Drug Investigation*. 2013, in press.

van Veen HA, Koiter J, Vogelesang CJ, van Wessel N, van Dam T, Velterop I, van Houdt K, Kupers L, Horbach D, Salaheddine M, Nuijens JH, Manesse ML. Characterization of recombinant human C1 inhibitor secreted in milk of transgenic rabbits. *J Biotechnol*. 2012 Dec;162(2-3):319-26.

Reshef A, Moldovan D, Obtulowicz K, Leibovich I, Mihaly E, Visscher S, Relan A. Recombinant human C1 inhibitor for the prophylaxis of hereditary angioedema attacks: a pilot study. *Allergy*. 2013 Jan;68(1):118-24.

Toubi E, Baker JW, Moldovan D, Levy RJ, Relan A. Safety and efficacy evaluation of rhC1INH for the treatment of HAE attacks in adolescent patients. *Allergy*, 2012 Nov; 67(s96):488.

Hack CE, Manesse M, Baboeram A, Oortwijn B, Relan A. Immunogenicity assessment of recombinant human c1-inhibitor: an integrated analysis of clinical studies. *BioDrugs*. 2012 Oct 1;26(5):303-13.

Plosker GL. Recombinant human c1 inhibitor (conestat alfa): in the treatment of angioedema attacks in hereditary angioedema. *BioDrugs*. 2012 Oct 1;26(5):315-23.

McMillan CV, Speight J, Relan A, Bellizzi L, Haase G, Cicardi M. Content validity of visual analog scales to assess symptom severity of acute angioedema attacks in adults with hereditary angioedema: an interview study. *Patient*. 2012;5(2):113-26.

Relan A, Bakhtiari K, van Amersfoort ES, Meijers JC, Hack CE. Recombinant C1-inhibitor: effects on coagulation and fibrinolysis in patients with hereditary angioedema. *BioDrugs*. 2012 Feb 1;26(1):43-52.

Hack CE, Relan A, van Amersfoort ES, Cicardi M. Target levels of functional C1-inhibitor in hereditary angioedema. *Allergy*. 2012 Jan;67(1):123-30

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