CYTOKINETICS INC
Form 10-Q
August 05, 2008

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UNITED STATES SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549
FORM 10-Q

(Mark One)

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

For the quarterly period ended June 30, 2008

or

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

Commission file number: 000-50633

CYTOKINETICS, INCORPORATED

(Exact name of registrant as specified in its charter)

Delaware	**94-3291317**
(State or other jurisdiction of incorporation or organization)	**(I.R.S. Employer Identification Number)**
280 East Grand Avenue South San Francisco, California	**94080**
(Address of principal executive offices)	**(Zip Code)**

Registrant s telephone number, including area code: (650) 624-3000

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

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

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

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

Number of shares of common stock, $0.001 par value, outstanding as of July 31, 2008: 49,412,922.

CYTOKINETICS, INCORPORATED
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FOR THE QUARTER ENDED JUNE 30, 2008

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PART I. FINANCIAL INFORMATION
ITEM 1. FINANCIAL STATEMENTS

CYTOKINETICS, INCORPORATED
(A Development Stage Enterprise)
CONDENSED BALANCE SHEETS
(In thousands, except share and per share data)
(Unaudited)

	June 30, 2008	December 31, 2007 (1)
ASSETS		
Current assets:		
Cash and cash equivalents	$ 86,861	$ 116,564
Short-term investments		3,175
Related party accounts receivable	60	87
Related party notes receivable short-term portion	77	127
Prepaid and other current assets	2,337	2,063
Total current assets	89,335	122,016
Long-term investments	18,749	20,025
Property and equipment, net	6,728	7,728
Related party notes receivable long-term portion	39	99
Restricted cash	4,147	5,167
Other assets	368	335
Total assets	$ 119,366	$ 155,370
LIABILITIES and STOCKHOLDERS EQUITY		
Current liabilities:		
Accounts payable	$ 1,659	$ 1,584
Accrued liabilities	8,024	8,558
Related party payables and accrued liabilities	6	22
Short-term portion of equipment financing lines	3,029	4,050
Short-term portion of deferred revenue	12,234	12,234
Total current liabilities	24,952	26,448
Long-term portion of equipment financing lines	3,576	4,639
Long-term portion of deferred revenue	18,250	24,367
Total liabilities	46,778	55,454
Stockholders equity:		
Common stock, $0.001 par value: Authorized: 170,000,000 shares; Issued and outstanding: 49,399,620 shares at June 30, 2008 and 49,282,362 shares at December 31, 2007	49	49
Additional paid-in capital	382,730	379,730
Deferred stock-based compensation	(124)	(329)
Accumulated other comprehensive loss	(1,276)	(1)

Deficit accumulated during the development stage	(308,791)	(279,533)
Total stockholders equity	72,588	99,916
Total liabilities and stockholders equity	$ 119,366	$ 155,370

(1) The condensed balance sheet at December 31, 2007 has been derived from the audited financial statements at that date but does not include all of the information and footnotes required by accounting principles generally accepted in the United States of America for complete financial statements.

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

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CYTOKINETICS, INCORPORATED
(A Development Stage Enterprise)
CONDENSED STATEMENTS OF OPERATIONS
(In thousands, except per share data)
(Unaudited)

	Three Months Ended		Six Months Ended		Period from August 5, 1997 (date of inception) to June 30, 2008
	June 30, 2008	June 30, 2007	June 30, 2008	June 30, 2007	
Revenues:					
Research and development revenues from related party	$ 16	$ 119	$ 27	$ 265	$ 40,279
Research and development, grant and other revenues					2,955
License revenues from related parties	3,058	3,058	6,117	6,117	32,451
Total revenues	3,074	3,177	6,144	6,382	75,685
Operating expenses:					
Research and development (1)	14,859	13,726	28,961	26,213	312,449
General and administrative (1)	4,252	4,015	8,409	8,497	93,869
Total operating expenses	19,111	17,741	37,370	34,710	406,318
Operating loss	(16,037)	(14,564)	(31,226)	(28,328)	(330,633)
Interest and other income	808	2,122	2,249	4,363	26,992
Interest and other expense	(135)	(186)	(281)	(356)	(5,150)
Net loss	$ (15,364)	$ (12,628)	$ (29,258)	$ (24,321)	$ (308,791)
Net loss per common share basic and diluted	$ (0.31)	$ (0.27)	$ (0.59)	$ (0.52)	
Weighted-average number of shares used in computing net loss per common share basic and diluted	49,366	46,890	49,330	46,826	
(1) Includes the following stock-based compensation charges:					
Research and development	$ 652	$ 684	$ 1,517	$ 1,328	$ 9,829
General and administrative	695	792	1,356	1,308	7,792

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

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CYTOKINETICS, INCORPORATED
(A Development Stage Enterprise)
CONDENSED STATEMENTS OF CASH FLOWS
(In thousands)
(Unaudited)

	Six Months Ended		Period from August 5, 1997 (date of inception) to June 30, 2008
	June 30, 2008	June 30, 2007	
Cash flows from operating activities:			
Net loss	$ (29,258)	$ (24,321)	$ (308,791)
Adjustments to reconcile net loss to net cash provided by (used in) operating activities:			
Depreciation and amortization of property and equipment	1,274	1,500	22,263
Loss on disposal of property and equipment		4	348
Gain on sale of investments			(84)
Allowance for doubtful accounts			191
Non-cash expense related to warrants issued for equipment financing lines and facility lease			41
Non-cash interest expense	46	46	473
Non-cash forgiveness of loan to officer	11	12	375
Stock-based compensation	2,873	2,636	17,621
Other non-cash expenses			27
Changes in operating assets and liabilities:			
Related party accounts receivable	25	42,006	(402)
Prepaid and other assets	(351)	(505)	(2,702)
Accounts payable	384	(47)	1,778
Accrued liabilities	(549)	(780)	7,972
Related party payables and accrued liabilities	(16)	(88)	7
Deferred revenue	(6,117)	817	30,484
Net cash provided by (used in) operating activities	(31,678)	21,280	(230,399)
Cash flows from investing activities:			
Purchases of investments	(9,400)	(39,800)	(654,303)
Proceeds from sales and maturities of investments	12,576	65,720	634,362
Purchases of property and equipment	(567)	(1,947)	(29,459)
Proceeds from sale of property and equipment			50
(Increase) decrease in restricted cash	1,020	(91)	(4,147)
Issuance of related party notes receivable			(1,146)
Proceeds from payments of related party notes receivable	100	99	799
Net cash provided by (used in) investing activities	3,729	23,981	(53,844)
Cash flows from financing activities:			
		26,002	193,934

Proceeds from initial public offering, sale of common stock to related party and public offerings, net of issuance costs			
Proceeds from draw down of Committed Equity Financing Facility, net of issuance costs			32,046
Proceeds from other issuances of common stock	331	686	5,889
Proceeds from issuance of preferred stock, net of issuance costs			133,172
Repurchase of common stock			(68)
Proceeds from equipment financing lines		1,743	23,696
Repayment of equipment financing lines	(2,085)	(1,856)	(17,565)
Net cash provided by (used in) financing activities	(1,754)	26,575	371,104
Net increase (decrease) in cash and cash equivalents	(29,703)	71,836	86,861
Cash and cash equivalents, beginning of period	116,564	39,387	
Cash and cash equivalents, end of period	$ 86,861	$ 111,223	$ 86,861

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

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CYTOKINETICS, INCORPORATED
(A DEVELOPMENT STAGE ENTERPRISE)
NOTES TO UNAUDITED CONDENSED FINANCIAL STATEMENTS

Note 1. Organization and Summary of Significant Accounting Policies

Overview

Cytokinetics, Incorporated (the Company, we or our) was incorporated under the laws of the state of Delaware on August 5, 1997. The Company is focused on developing small molecule therapeutics for the treatment of cardiovascular disease, cancer and other diseases. The Company is a development stage enterprise and has been primarily engaged in conducting research, developing drug candidates and technologies, and raising capital.

The Company has funded its operations primarily through sales of common stock and convertible preferred stock, contract payments under its collaboration agreements, debt financing arrangements, government grants and interest income.

The Company s registration statement for its initial public offering (IPO) was declared effective by the Securities and Exchange Commission (SEC) on April 29, 2004. The Company s common stock commenced trading on the NASDAQ National Market, now the NASDAQ Global Market, on April 29, 2004 under the trading symbol CYTK.

Until it achieves profitable operations, the Company intends to continue to fund operations through the additional sale of equity securities, payments from strategic collaborations, government grant awards and debt financing.

Basis of Presentation

The accompanying unaudited condensed financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America for interim financial information and with instructions to Form 10-Q and Rule 10-01 of Regulation S-X. Accordingly, they do not include all of the information and footnotes required by generally accepted accounting principles for complete financial statements. The financial statements include all adjustments (consisting only of normal recurring adjustments) that management believes are necessary for the fair statement of the balances and results for the periods presented. These interim financial statement results are not necessarily indicative of results to be expected for the full fiscal year or any future interim period.

The balance sheet at December 31, 2007 has been derived from the audited financial statements at that date. The financial statements and related disclosures have been prepared with the presumption that users of the interim financial statements have read or have access to the audited financial statements for the preceding fiscal year. Accordingly, these financial statements should be read in conjunction with the audited financial statements and notes thereto contained in the Company s Form 10-K for the year ended December 31, 2007.

Comprehensive Income (Loss)

Comprehensive loss consists of the net loss and other comprehensive income (loss). Other comprehensive income (loss) (OCI) includes certain changes in stockholder s equity that are excluded from net loss. Comprehensive loss and its components for the three-and six-month periods ended June 30, 2008 and 2007 are as follows (in thousands):

	Three months Ended		Six Months Ended	
	June 30, 2008	June 30, 2007	June 30, 2008	June 30, 2007
Net loss	$ (15,364)	$ (12,628)	$ (29,258)	$ (24,321)
Change in unrealized gain (loss) on investments	(328)	(6)	(1,275)	15
Comprehensive loss	$ (15,692)	$ (12,634)	$ (30,533)	$ (24,306)

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Restricted Cash

In accordance with the terms of the Company s line of credit agreements with General Electric Capital Corporation (GE Capital) to fund certain equipment, the Company is obligated to maintain a certificate of deposit with the lender. The balance of the certificate of deposit, which is classified as restricted cash, was $4.1 million at June 30, 2008 and $5.2 million at December 31, 2007. At July 1, 2008, the restricted cash balance was $2.7 million.

Fair Value of Financial Instruments

In September 2006, the Financial Statement Standard Board (FASB) issued Statement of Financial Accounting Standard (SFAS) No. 157, Fair Value Measurements (SFAS No. 157). SFAS No. 157 established a common definition for fair value, which is to be applied to U.S. generally accepted accounting principles (GAAP) requiring use of fair value, and a framework for measuring fair value, and expanded disclosure about such fair value measurements. This pronouncement applies under the other accounting standards that require or permit fair value measurements. Accordingly, this statement does not require any new fair value measurement. SFAS No. 157 is effective for financial assets and financial liabilities for fiscal years beginning after November 15, 2007. In February 2008, the FASB released a FASB Staff Position (FSP) 157-1, Application of FASB Statement No. 157 to FASB Statement 13 and Other Accounting Pronouncements That Address Fair Value Measurements for Purposes of Lease Classification or Measurement under Statement 13. FSP 157-1 removed leasing transactions accounted for under FASB Statement 13 and related guidance from the scope of SFAS No. 157. FSP 157-2, Partial Deferral of the Effective Date of Statement 157, deferred the effective date of SFAS No. 157 for all nonfinancial assets and nonfinancial liabilities, except those are recognized or disclosed at fair value in the financial statements on a recurring basis (at least annually) to fiscal years beginning after November 15, 2008.

SFAS No. 159, The Fair Value Option for Financial Assets and Financial Liabilities, became effective for the Company on January 1, 2008. SFAS No. 159 includes an amendment of FASB Statement No. 115, Accounting for Certain Investments in Debt and Equity Securities, which permits an entity to measure certain financial assets and financial liabilities at fair value. The objective of SFAS No. 159 is to improve financial reporting by allowing entities to mitigate volatility in reported earnings caused by the measurement of related assets and liabilities using different attributes, without having to apply complex hedge accounting provisions. Under SFAS No. 159, entities that elect the fair value option (by instrument) will report unrealized gains and losses in earnings at each subsequent reporting date. The fair value option election is irrevocable, unless a new election date occurs. SFAS No. 159 establishes presentation and disclosure requirements to help financial statement users understand the effect of the entity s election on its earnings, but does not eliminate disclosure requirements of other accounting standards. Assets and liabilities that are measured at fair value must be displayed on the face of the balance sheet. The Company did not elect the fair value option for its financial assets and liabilities existing at January 1, 2008, nor for its financial assets and liabilities transacted in the six months ended June 30, 2008.

Stock-Based Compensation

Effective January 1, 2006, the Company adopted the provisions of SFAS No. 123R, Share-Based Payment, which establishes accounting for share-based payment awards made to employees and directors, including employee stock options and employee stock purchases. Under the provisions of SFAS No. 123R, stock-based compensation cost is measured at the grant date based on the calculated fair value of the award, and is recognized as an expense on a straight-line basis over the employee s requisite service period, generally the vesting period of the award.

The Company uses the Black-Scholes option pricing model to determine the fair value of stock options and employee stock purchase plan (ESPP) shares, consistent with the provisions of SFAS No. 123R. The key input assumptions used to estimate fair value of these awards include the exercise price of the award, the expected option term, the expected volatility of the Company s stock over the option s expected term, the risk-free interest rate over the option s expected term and the Company s expected dividend yield, if any.

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For employee stock options, the fair value of share-based payments was estimated on the date of grant using the Black-Scholes option pricing model based on the following weighted average assumptions:

	Three Months Ended		Six Months Ended	
	June 30, 2008	June 30, 2007	June 30, 2008	June 30, 2007
Risk-free interest rate	3.50%	4.74%	2.97%	4.52%
Volatility	67%	74%	63%	73%
Expected life (in years)	6.11	5.73	6.08	5.99
Expected dividend yield	0.00%	0.00%	0.00%	0.00%

For the ESPP, the fair value of share-based payments was estimated on the date of grant using the Black-Scholes option pricing model based on the following weighted average assumptions:

	Three Months Ended		Six Months Ended	
	June 30, 2008	June 30, 2007	June 30, 2008	June 30, 2007
Risk-free interest rate	2.23%	4.84%	2.23%	4.84%
Volatility	67%	74%	67%	74%
Expected life (in years)	1.25	1.25	1.25	1.25
Expected dividend yield	0.00%	0.00%	0.00%	0.00%

The risk-free interest rate that the Company uses in the option pricing model is based on the U.S. Treasury zero-coupon issues with remaining terms similar to the expected terms of the options. The Company does not anticipate paying dividends in the foreseeable future and therefore uses an expected dividend yield of zero in the option pricing model. The Company is required to estimate forfeitures at the time of grant and revise those estimates in subsequent periods if actual forfeitures differ from those estimates. Historical data is used to estimate pre-vesting option forfeitures and record stock-based compensation expense only on those awards that are expected to vest.

Under Staff Accounting Bulletin (SAB) No. 107, the Company used the simplified method of estimating the expected term for stock-based compensation from January 1, 2006, the date it adopted SFAS No. 123R, through December 31, 2007. Starting January 1, 2008, the Company ceased to use the simplified method, and now uses its own historical exercise activity and extrapolates the life cycle of options outstanding to arrive at its estimated expected term for new option grants.

From January 1, 2006, the date of adopting SFAS No. 123R, through December 31, 2007, the Company estimated the volatility of its common stock by using an average of historical stock price volatility of comparable companies due to the limited length of trading history. Starting January 1, 2008, the Company has used its own volatility history based on its stock s trading history of approximately four years. Because its outstanding options have an expected term of approximately six years, the Company supplemented its own volatility history by using comparable companies volatility history for approximately two years preceding the Company s IPO.

Note 2. Net Loss Per Share

Basic net loss per common share is computed by dividing the net loss by the weighted-average number of vested common shares outstanding during the period. Diluted net loss per common share is computed by giving effect to all potentially dilutive common shares, including outstanding options, common stock subject to repurchase, warrants and shares issuable under the ESPP. The following is a reconciliation of the numerator and denominator used in the calculation of basic and diluted net loss per common share (in thousands):

	Three Months Ended		Six Months Ended	
	June 30, 2008	June 30, 2007	June 30, 2008	June 30, 2007
Numerator net loss	$ (15,364)	$ (12,628)	$ (29,258)	$ (24,321)

Denominator:				
Weighted-average common shares outstanding	49,366	46,890	49,330	46,827
Less: Weighted-average shares subject to repurchase	( )	( )	( )	(1)
Weighted-average shares used in computing basic and diluted net loss per common share	49,366	46,890	49,330	46,826

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The following outstanding instruments were excluded from the computation of diluted net loss per common share for the periods presented, because their effect would have been antidilutive (in thousands):

	As of June 30,	
	2008	2007
Options to purchase common stock	6,590	5,250
Warrants to purchase common stock	474	244
Shares issuable related to the ESPP	46	38
Total shares	7,110	5,532

Note 3. Supplemental Cash Flow Data

Supplemental cash flow data was as follows (in thousands):

	Six Months Ended		Period from August 5, 1997 (date of inception)
	June 30, 2008	June 30, 2007	June 30, 2008
Significant non-cash investing and financing activities:			
Deferred stock-based compensation	$	$	$ 6,940
Purchases of property and equipment through accounts payable	65	42	65
Purchases of property and equipment through trade in value of disposed property and equipment			258
Penalty on restructuring of equipment financing lines			475
Conversion of convertible preferred stock to common stock			133,172
Unrealized loss on auction rate securities	1,276		1,276

Note 4. Related Party Agreements

Research and Development Arrangements

GlaxoSmithKline (GSK). Pursuant to the collaboration and license agreement between the Company and GSK (the GSK Agreement), the Company received and recorded as research and development revenues from related party, patent expense reimbursements from GSK of $16,000 and $119,000 in the three months ended June 30, 2008 and 2007, respectively. For the six months ended June 30, 2008 and 2007, the Company received and recorded as research and development revenues from related party, patent expense reimbursements from GSK of $27,000 and $265,000, respectively. Related party accounts payable and accrued liabilities payable to GSK for outsourced services under the GSK Agreement were zero and $20,000 at June 30, 2008 and December 31, 2007, respectively.

Amgen Inc. (Amgen). Pursuant to the collaboration and option agreement between the Company and Amgen (the Amgen Agreement), the Company recognized license revenue of $3.1 million and $6.1 million in both the three and six months ended June 30, 2008 and June 30, 2007. At June 30, 2008, deferred revenue related to the Amgen Agreement and its related common stock purchase agreement was $30.5 million.

Other

Board member. Charles J. Homcy, M.D. was a member of the Company s Board of Directors through June 30, 2008 and continues as a consultant to the Company. The Company incurred consulting fees earned by Dr. Homcy of $8,000 and $13,000 in the six months ended June 30, 2008 and 2007, respectively. Related party accounts payable and accrued liabilities payable to Dr. Homcy for his consulting services were $6,300 and $2,500 as of June 30, 2008 and December 31, 2007, respectively.

Related Party Notes Receivable. Effective March 31, 2008, James Sabry voluntarily resigned from his position as Executive Chairman of the Board of Directors of the Company, and on April 1, 2008, assumed his new role as the

non-employee Chairman of the Board of Directors, as well as Chairman of the Company s Scientific Advisory Board and a consultant to the Company. In accordance with the terms of Dr. Sabry s promissory note payable to the Company, the outstanding balance of the note of $100,000 became due, and was repaid in full, on April 30, 2008.

In May 2007, $11,000 of principal and interest on a loan receivable from an officer of the Company was forgiven in accordance with the terms of the loan agreement.

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Note 5. Cash, cash equivalents, and investments

The amortized cost and fair value of cash, cash equivalents and short- and long-term investments at June 30, 2008 and December 31, 2007 were as follows (in thousands):

	June 30, 2008				
	Amortized Cost	Unrealized Gains	Unrealized Losses in accumulated OCI	Fair Value	Investment Maturity Dates
Cash and cash equivalents	$ 86,861			$ 86,861	
Long-term investments:					
Student loan auction rate securities (taxable)	$ 20,025		(1,276)	$ 18,749	6/2036 8/2045
Total long-term investments	$ 20,025	$	$ (1,276)	$ 18,749	

	December 31, 2007				
	Amortized Cost	Unrealized Gains	Unrealized Losses in accumulated OCI	Fair Value	Investment Maturity Dates
Cash and cash equivalents	$ 116,565		$ (1)	$ 116,564	
Short-term investments:					
Student loan auction rate securities (taxable)	$ 3,175			$ 3,175	1/2008
Total short-term investments	$ 3,175	$	$	$ 3,175	
Long-term investments:					
Student loan auction rate securities (taxable)	$ 20,025			$ 20,025	6/2036 8/2045
Total long-term investments	$ 20,025	$	$	$ 20,025	

The Company s student loan auction rate securities (ARS), which had a fair value of $18.7 million as of June 30, 2008 and $23.2 million as of December 31, 2007, are securities that are structured with short-term interest reset dates of less than 30 days, but with maturities generally greater than 20 years. The Company classified $18.7 million and $20.0 million of these ARS as long-term investments as of June 30, 2008 and December 31, 2007, respectively, due to their illiquidity and the Company s inability to use them in its current operations.

These ARS are intended to provide liquidity via an auction process that resets the applicable interest rate at predetermined calendar intervals, allowing investors to either roll over their holdings or gain immediate liquidity by selling such interests at par. As of December 31, 2007, there were no ARS in an unrealized loss position, and there were no failed auctions associated with the Company s ARS through that date. The Company s ARS with auction reset dates prior to February 13, 2008 had successful auctions at which their interest rates were reset. In February 2008, the

Company liquidated $3.2 million of its ARS at par, which were classified as short-term investments as of December 31, 2007. The recent uncertainties in the credit markets have affected all of the Company s holdings in ARS investments and auctions for the Company s investments in these securities have failed to settle on their respective settlement dates since February 2008. Consequently, the investments are not currently liquid, and the Company will not be able to access these funds until a future auction of these investments is successful, the issuer redeems the outstanding securities, the securities mature or a buyer is found outside of the auction process. Maturity dates for these ARS range from 2036 to 2045. All of the ARS are AAA/Aaa rated and were in compliance with the Company s investment policy at the time of acquisition. As of June 30, 2008, the Company held ARS with a par value of $20.0 million, which were classified as long-term investments because of the Company s inability to determine when its investments in these ARS would settle. Typically the fair value of ARS investments approximates par value due to the frequent resets through the auction process. The Company earns interest on its ARS at the contractual rates, however, these investments are not currently trading and accordingly, the estimated fair value of these ARS no longer approximates par value.

The Company used a discounted cash flow (DCF) model to assess the estimated fair value of its investment in ARS as of June 30, 2008. See Footnote 8 for the assumptions used in preparing the DCF model. As of June 30, 2008, the Company determined there was a decline in the fair value of its ARS of $1.3 million and deemed the entire decline temporary. As a result, the Company recorded an unrealized loss of $1.3 million associated with its ARS as a component of stockholders equity as of June 30, 2008. The Company reviews its impairments in accordance with SFAS No. 115, Accounting for Certain Investments in Debt and Equity Securities, and FSP Nos. FASB 115-1 and FASB 124-1, The Meaning of Other-Than-Temporary Impairment and Its Application to Certain Investments, in order to determine the classification of the impairment as temporary or other-than-temporary. A temporary decline in value results

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in an unrealized loss being recorded in the Other Comprehensive Income (Loss) component of stockholders equity. Such an unrealized loss does not affect net income (loss) for the applicable accounting period. An other-than-temporary decline in value is recorded as a realized loss in the condensed statement of operations and reduces net income (loss) for the applicable accounting period. In evaluating the impairment of any individual ARS, the Company classifies such impairment as temporary or other-than-temporary. The differentiating factors between temporary and other-than-temporary impairment are primarily the length of the time and the extent to which the market value has been less than cost, the financial condition and near-term prospects of the issuer and the Company s intent and ability to retain its investment in the issuer for a period of time sufficient to allow for any anticipated recovery in market value. As of June 30, 2008 and December 31, 2007, the Company had not incurred any losses that were other-than-temporary. The Company continues to monitor the ARS market and to consider the impact, if any, on the fair value of its ARS.

Note 6. Equipment Financing Lines

In August 2007, the Company secured a new line of credit with GE Capital of up to $3.0 million to finance certain equipment until September 30, 2008. The line of credit is subject to the Master Security Agreement between the Company and GE Capital, dated February 2001 and amended on March 24, 2005. As of June 30, 2008, the Company has not borrowed any funds under this line.

Note 7. Stockholders Equity

Stock Option Plans

In January 2004, the Board of Directors adopted the 2004 Equity Incentive Plan (the 2004 Plan) which was approved by the stockholders in February 2004. The 2004 Plan provides for the granting of incentive stock options, nonstatutory stock options, restricted stock purchase rights and stock bonuses to employees, directors and consultants. Under the 2004 Plan, the number of authorized shares automatically increases on an annual basis by a number of shares equal to the lesser of (i) 1,500,000 shares, (ii) 3.5% of the outstanding shares on such date, or (iii) an amount determined by the Board of Directors. Accordingly, on January 1, 2008, the number of shares of common stock authorized for issuance under the 2004 Plan was increased by 1,500,000 shares to a total of 2,997,296 shares. At the May 2008 Annual Stockholder Meeting, the number of shares of common stock authorized for issuance under the 2004 Plan was increased by 2,000,000, and approved an amended and restated 2004 Plan which eliminated the automatic increase provision.

Stock option activity for the six months ended June 30, 2008 under the 2004 Plan and the 1997 Stock Option/Stock Issuance Plan was as follows:

	Options Available for Grant	Options Outstanding	Weighted Average Exercise Price per Share
Balance at December 31, 2007	1,497,296	5,060,294	$ 5.80
Increase in authorized shares	3,500,000		
Options granted	(1,708,137)	1,708,137	$ 3.41
Options exercised		(22,400)	$ 1.19
Options cancelled	156,019	(156,019)	$ 4.73
Balance at June 30, 2008	3,445,178	6,590,012	$ 5.22

The weighted average fair value of options granted in the six months ended June 30, 2008 was $2.06 per share.

Note 8 Fair Value Measurements

As stated in Note 1. Organization and Summary of Significant Accounting Policies, on January 1, 2008, the Company adopted the methods of fair value described in SFAS No. 157 to value its financial assets and liabilities. As defined in SFAS No. 157, fair value is the price that would be received for asset when sold or paid to transfer a

liability in an orderly transaction between market participants at the measurement date (exit price). The Company utilizes market data or assumptions that the Company believes market participants would use in pricing the asset or liability, including assumptions about risk and the risks inherent in the inputs to the valuation technique. These inputs can be readily observable, market corroborated or generally unobservable.

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The Company primarily applies the market approach for recurring fair value measurements and endeavors to utilize the best information available to it. Accordingly, the Company utilizes valuation techniques that maximize the use of observable inputs and minimize the use of unobservable inputs to the extent possible, and considers the security issuers and the third-party insurers credit risk in its assessment of fair value.

The Company classifies the determined fair value based on the observability of those inputs. SFAS No. 157 establishes a fair value hierarchy that prioritizes the inputs used to measure fair value. The hierarchy gives the highest priority to unadjusted quoted prices in active markets for identical assets or liabilities (Level 1 measurement) and the lowest priority to unobservable inputs (Level 3 measurement). The three levels of the fair value hierarchy defined by SFAS No. 157 are as follows:

Level 1 Quoted prices are available in active markets for identical assets or liabilities as of the reporting date. Active markets are those in which transactions for the asset or liability occur in sufficient frequency and volume to provide the most reliable pricing information and evidence of fair value on an ongoing basis.

Level 2 Pricing inputs are other than quoted prices in active markets included in Level 1, which are either directly or indirectly observable as of the reporting date. Level 2 includes those financial instruments that are valued using models or other valuation methodologies. These models are primarily industry-standard models that consider various assumptions, including quoted forward prices for commodities, time value, volatility factors, and current market and contractual prices for the underlying instruments, as well as other relevant economic measures. Substantially all of these assumptions are observable in the marketplace throughout the full term of the instrument, can be derived from observable data or are supported by observable levels at which transactions are executed in the marketplace.

Level 3 Pricing inputs include significant inputs that are generally less observable from objective sources. These inputs may be used with internally developed methodologies that result in management s best estimate of fair value from the perspective of a market participant. Instruments subject to Level 3 measurements include those that may be more structured or otherwise tailored to customers needs. At each balance sheet date, the Company performs an analysis of all instruments subject to SFAS No. 157 and includes in Level 3 all of those whose fair value is based on significant unobservable inputs.

Financial assets carried at fair value as of June 30, 2008 are classified in the table below in one of the three categories described above (in thousands):

	Fair Value Measurements Using			Assets At Fair Value
	Level 1	**Level 2**	**Level 3**	
Cash equivalents	$85,923			$ 85,923
Long-term investments ARS			$18,749	$ 18,749
Total	$85,923		$18,749	$ 104,672

The Company chose not to elect the fair value option as prescribed by SFAS No. 159 for its financial assets and liabilities that had not been previously reported at fair value. Therefore, financial assets and liabilities not reported at fair value, such as the Company s accounts receivable, notes receivable, short- and long-term equipment financing lines and accounts payable are still reported at their carrying values.

As of June 30, 2008, the Company applied Level 1 measurements to its holdings of money market funds, which it classified as cash equivalents.

Temporary Impairment of Long-Term Student Loan Auction Rate Securities

The Company s financial assets measured at fair value on a recurring basis using significant Level 3 inputs as of June 30, 2008 consisted solely of ARS. The following table summarizes the Company s fair value measurements using Level 3 inputs, and changes therein, for the six-months period ended June 30, 2008 (in thousands):

		Long-term Investment
Beginning balance as of December 31, 2007	$	
Transfer-in of Level 3 hierarchy measurement from Level 1		20,025
Unrealized losses included in other comprehensive income		(1,276)
Ending balance as of June 30, 2008	$	18,749

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The Company s ARS holdings as of June 30, 2008 and December 31, 2007 consisted entirely of student loan ARS. The unrealized loss of these ARS for the six months ended June 30, 2008 reflected a decrease of fair value of the Company s long-term investments and was reported in its OCI. Due to the lack of observable market quotes on the Company s ARS portfolio, the Company utilized DCF valuation models that relied exclusively on Level 3 inputs including estimates for interest rates, timing and amount of cash flows, credit quality, expected holding periods of the ARS, net loan rate provision and percentage of portfolio guaranteed by the Federal Family and Education Loan Program. The valuation used estimates of observable market data including yields or spreads of trading instruments that the Company believed to be similar or comparable and assumptions that it believed to be reasonable non-observable inputs such as illiquidity premium and likelihood of redemption. The valuation of the Company s ARS is subject to uncertainties that are difficult to predict. Factors that may impact its valuation include changes to credit ratings of the securities and to the underlying assets supporting those securities, rates of default of the underlying assets, underlying collateral value, discount rates and ongoing strength and quality of market credit and liquidity. The Company s ARS, valued using Level 3 inputs, represent 18 percent of assets measured at fair value under the provisions of SFAS 157.

Based on this assessment of fair value, as of June 30, 2008, the Company determined there was a decline in the fair value of its ARS investment of $1,276,000, and deemed the entire decline temporary. The unrealized losses are reported as a component of stockholders equity, except for unrealized losses determined to be other than temporary which are recorded in the Statement of Operations, in accordance with the Company s policy and FSP No. FASB 115-1 and FASB 124-1, The Meaning of Other-Than-Temporary Impairment and Its Application to Certain Investments. As of June 30, 2008 and December 31, 2007, the Company had not incurred any losses that it deemed other-than-temporary. The Company continues to monitor the ARS market and consider its impact, if any, on the fair value of its ARS.

If the current market conditions deteriorate further, or the anticipated recovery in market values does not occur, the Company may be required to record additional unrealized losses in other comprehensive income (loss) or impairment charges in future quarters.

Note 9. Recent Accounting Pronouncements

Recently Adopted Accounting Pronouncements

The Company adopted certain requirements of SFAS No. 157 effective January 1, 2008. See Note 1, Organization and Summary of Significant Accounting Policies *Fair Value of Financial Instruments.*

Effective January 1, 2008, the Company adopted SFAS No. 159. The Company did not elect the fair value option for its financial assets and liabilities existing at January 1, 2008, nor for its financial assets and liabilities transacted in the six months ended June 30, 2008. Therefore, the adoption of SFAS No. 159 had no impact on the Company s financial position or results of operations. See Note 1, Organization and Summary of Significant Accounting Policies *Fair Value of Financial Instruments.*

The Company adopted Emerging Issues Task Force (EITF) Issue No. 07-3, Accounting for Nonrefundable Advance Payments for Goods or Services to Be Used in Future Research and Development Activities, on a prospective basis for new contracts entered into on or after effective January 1, 2008. EITF Issue No. 07-3 states that nonrefundable advance payments for future research and development activities should be deferred and recognized as an expense as the goods are delivered or the related services are performed. Entities should then continue to evaluate whether they expect the goods to be delivered or services to be rendered and, if an entity does not expect the goods to be delivered or services to be rendered, the capitalized advance payment should be charged to expense. The adoption of EITF Issue No. 07-3 did not have a material effect on the Company s financial position or results of operations.

In December 2007, the SEC issued SAB No. 110, which addresses the continued use of the simplified method for estimating the expected term for stock based compensation. Previously, under SAB No. 107, the use of the simplified method was intended to be discontinued after December 31, 2007. Under SAB No. 110, companies may continue to use the simplified method in certain circumstances. The Company used the simplified method of estimating the expected term for stock based compensation from January 1, 2006,

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the date it adopted SFAS No. 123R, through December 31, 2007. Starting January 1, 2008, the Company ceased to use the simplified method under SAB No. 107. Instead, the Company uses its own historical exercise activity and extrapolates the life cycle of options outstanding to arrive at its estimated expected term for new option grants.

Accounting Pronouncements Not Yet Adopted

In November 2007, the EITF issued a consensus on EITF Issue No. 07-01, Accounting for Collaboration Arrangements Related to the Development and Commercialization of Intellectual Property, which is focused on how the parties to a collaborative agreement should account for costs incurred and revenue generated on sales to third parties, how sharing payments pursuant to a collaboration agreement should be presented in the income statement and certain related disclosure questions. EITF Issue No. 07-01 is to be applied retrospectively for collaboration arrangements in fiscal years beginning after December 15, 2008. The Company is currently evaluating the impact on its financial statements of adopting EITF Issue No. 07-1.

In March 2008, the FASB issued SFAS No. 161, Disclosures about Derivative Instruments and Hedging Activities, as an amendment to SFAS No. 133, Accounting for Derivative Instruments and Hedging Activities. SFAS No. 161 requires that the objectives for using derivative instruments be disclosed in terms of underlying risk and accounting designation. The fair value of derivative instruments and their gains and losses will need to be presented in tabular format in order to present a more complete picture of the effects of using derivative instruments. SFAS No. 161 is effective for financial statements issued for fiscal years beginning after November 15, 2008. The Company is currently evaluating the impact of adopting this pronouncement.

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

This discussion and analysis should be read in conjunction with our financial statements and accompanying notes included elsewhere in this report. Operating results are not necessarily indicative of results that may occur in future periods.

This report contains forward-looking statements that are based upon current expectations within the meaning of the Private Securities Litigation Reform Act of 1995. We intend that such statements be protected by the safe harbor created thereby. Forward-looking statements involve risks and uncertainties and our actual results and the timing of events may differ significantly from the results discussed in the forward-looking statements. Examples of such forward-looking statements include, but are not limited to, statements about or relating to:

- the initiation, progress, timing and scope of clinical trials and development for our drug candidates and potential drug candidates by ourselves or GlaxoSmithKline (GSK), including the anticipated dates of data becoming available or being announced or presented from clinical trials;
- guidance concerning revenues, research and development expenses and general and administrative expenses for 2008;
- our and our partners plans or ability for continued research and development of drug candidates, such as CK-1827452, ispinesib, SB-743921 and GSK-923295, and other compounds, such as our skeletal muscle activators and our smooth muscle myosin inhibitors;
- our ability to generate clinical data sufficient to result in Amgen Inc. (Amgen) exercising its option with respect to CK-1827452 or GSK exercising its option with respect to either or both of ispinesib or SB-743921, or to provide such data within our expected timeframes.
- our expected roles in research, development or commercialization under our strategic alliances, such as with Amgen and GSK;
- the potential benefits of our drug candidates and potential drug candidates;
- the scope, conduct and results of our research and development activities and programs;

the utility of our clinical trials programs for our drug candidates in informing future development activities;

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our plans or ability to commercialize drugs with or without a partner, including our intention to develop sales and marketing capabilities;

receipt of milestone payments, royalties and other funds from our partners under strategic alliances, such as with Amgen and GSK;

issuance of shares of our common stock under our committed equity financing facility entered into with Kingsbridge Capital Limited (Kingsbridge) in 2007;

losses, costs, expenses and expenditures;

the sufficiency of existing resources to fund our operations for at least the next 12 months;

capital requirements and our needs for additional financing;

future payments under lease obligations and equipment financing lines;

expected future sources of revenue and capital;

increasing the number of our employees and recruiting additional key personnel; and

expected future amortization of employee stock-based compensation.

Such forward-looking statements involve risks and uncertainties, including, but not limited to, those risks and uncertainties relating to:

difficulties or delays in development, testing, obtaining regulatory approval for, and undertaking production and marketing of our drug candidates, including decisions by the National Cancer Institute (NCI) to postpone or discontinue development activities for ispinesib, or by GSK to postpone or discontinue research or development activities relating to GSK-923295 or to centromere-associated protein E;

difficulties or delays in or slower than anticipated patient enrollment in our or our partners clinical trials;

unexpected adverse side effects or inadequate therapeutic efficacy of our drug candidates that could slow or prevent product approval (including the risk that current and past results of clinical trials or preclinical studies are not indicative of future results of clinical trials);

the possibility that the U.S. Food and Drug Administration (FDA), or foreign regulatory agencies may delay or limit our or our partners ability to conduct clinical trials;

our receipt of funds under our strategic alliances, including those funds dependent upon Amgen s exercise of its option with respect to CK-1827452 and GSK s exercise of its option with respect to either or both of ispinesib and SB-743921;

activities and decisions of, and market conditions affecting, current and future strategic partners;

our ability to obtain additional financing if necessary;

our ability to maintain the effectiveness of our registration statement permitting resale of securities to be issued to Kingsbridge by us under, and in connection with, the 2007 committed equity financing facility;

changing standards of care and the introduction of products by competitors or alternative therapies for the treatment of indications we target;

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the uncertainty of our ability to obtain and maintain protection for our intellectual property, through patents, trade secrets or otherwise; and

our potential infringement or misappropriation of the intellectual property rights of third parties.

In addition such statements are subject to the risks and uncertainties discussed in the Risk Factors section and elsewhere in this document. Operating results are not necessarily indicative of results that may occur in future periods.

When used in this report, unless otherwise indicated, Cytokinetics, the Company, we, our and us refers to Cytokinetics, Incorporated.

CYTOKINETICS, and our logo used alone and with the mark CYTOKINETICS, and CYTOMETRIX are registered service marks and trademarks of Cytokinetics. PUMA is a trademark of Cytokinetics. Other service marks, trademarks and trade names referred to in this report are the property of their respective owners.

Overview

We are a biopharmaceutical company, incorporated in Delaware in 1997, focused on developing small molecule therapeutics for the treatment of cardiovascular diseases, cancer and other diseases. Our current clinical development activities are primarily directed to advancing multiple drug candidates through clinical trials with the objective of determining the intended pharmacodynamic effect or effects in two principal diseases: heart failure and cancer. Our drug development pipeline consists of a drug candidate, CK-1827452, being developed in both an intravenous and oral formulation for the potential treatment of heart failure; three drug candidates, ispinesib, SB-743921 and GSK-923295, each being developed in an intravenous formulation for the potential treatment of cancer; and a potential drug candidate for the potential treatment of skeletal muscle weakness associated with neuromuscular diseases or other conditions. Our drug candidates and potential drug candidate are all novel small molecules that arose from our research activities and are directed toward the cytoskeleton. We believe our understanding of the cytoskeleton enables us to discover novel and potentially safer and more effective therapeutics.

Since our inception in August 1997, we have incurred significant net losses. As of June 30, 2008, we had an accumulated deficit of $308.8 million. We expect to incur substantial and increasing losses for the next several years if and to the extent:

we advance CK-1827452 through clinical development for the treatment of heart failure and Amgen does not exercise its option to conduct later-stage development and commercialization;

Amgen exercises its option to conduct later-stage development and commercialization of CK-1827452 and we then exercise our option to co-fund the development of CK-1827452;

we conduct continued Phase I, Phase II and later-stage development and commercialization of ispinesib, SB-743921 or GSK-923295 under our collaboration and license agreement with GSK, as amended;

we advance ispinesib through clinical development for breast cancer and SB-743921 through clinical development for Hodgkin and non-Hodgkin lymphoma, and GSK does not exercise its option to conduct later-stage development and commercialization for either or both of these drug candidates;

we exercise our option to co-fund the development of GSK-923295 or of any other drug candidate being developed by GSK under our strategic alliance;

we exercise our option to co-promote any of the products for which we have elected co-fund development under our strategic alliance with GSK;

we advance potential drug candidates through preclinical studies and into clinical trials;

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we expand our research programs and further develop our proprietary drug discovery technologies; or

we elect to fund development or commercialization of any drug candidate.

We intend to pursue selective strategic alliances to enable us to maintain financial and operational flexibility.

Cardiovascular

We have focused our cardiovascular research and development activities on heart failure, a disease most often characterized by compromised contractile function of the heart that impacts its ability to effectively pump blood throughout the body. We have discovered and optimized small molecules that have the potential to improve cardiac systolic performance by specifically binding to and activating cardiac myosin, a cytoskeletal protein essential for cardiac muscle contraction. This work gave rise to our drug candidate CK-1827452, a novel small molecule cardiac myosin activator. CK-1827452 entered clinical trials in 2006. Based on data from our first-time-in-humans Phase I clinical trial with this drug candidate, in April 2007, we initiated a clinical trials program for CK-1827452, comprised of Phase I and Phase IIa clinical trials designed to evaluate the safety, tolerability, pharmacodynamics and pharmacokinetic profile of both intravenous and oral formulations of this drug candidate in a diversity of patients, including patients with stable heart failure and patients with ischemic cardiomyopathy. Our goal is to develop CK-1827452 as a potential treatment across the continuum of care in heart failure, both in the hospital setting as an intravenous formulation for the treatment of acutely decompensated heart failure and in the outpatient setting as an oral formulation for the treatment of chronic heart failure.

In the first-time-in-humans Phase I clinical trial of CK-1827452, evaluating a six-hour intravenous infusion of this drug candidate in healthy volunteers, CK-1827452 was well-tolerated and statistically significant and concentration-dependent increases in indices of left ventricular function were demonstrated. In addition, CK-1827452 exhibited generally linear, dose-proportional pharmacokinetics across the dose range studied. The adverse effects at intolerable doses in humans appeared similar to the adverse findings which occurred at similar plasma concentrations in the preclinical safety studies. These effects are believed to be related to an excess of the intended pharmacologic effect, resulting in excessive prolongation of the systolic ejection time, and resolved promptly with discontinuation of the infusions of CK-1827452. The activity of CK-1827452 in this trial was consistent with results from preclinical evaluations of CK-1827452 in normal dogs. Further clinical trials are necessary to determine whether similar results will also be seen in patients with heart failure.

In December 2006, we entered into a collaboration and option agreement with Amgen to discover, develop and commercialize novel small-molecule therapeutics that activate cardiac muscle contractility for potential applications in the treatment of heart failure, including CK-1827452. The agreement provides Amgen with a non-exclusive license and access to certain technology, as well as an option to receive an exclusive license to develop and commercialize CK-1827452 and other drug candidates arising from the collaboration, subject to Cytokinetics development and commercial participation rights. The option is for worldwide license rights, excluding Japan. Amgen s option is exercisable during a defined period, the ending of which is dependent upon the satisfaction of certain conditions, primarily the delivery of Phase I and Phase IIa clinical trials data for CK-1827452 in accordance with an agreed development plan, the results of which may reasonably support its progression into Phase IIb clinical development.

Currently ongoing and recently completed clinical trials of CK-1827452 are as follows:

CK-1827452 (intravenous)

Phase IIa stable heart failure (safety and tolerability): In June 2008, as part of the Late Breaking Trials Session at the 2008 Heart Failure Congress of the European Society of Cardiology in Milan, Italy, we announced results from an interim analysis of an ongoing Phase IIa, multi-center, double-blind, randomized, placebo-controlled, dose-escalation clinical trial of CK-1827452 administered intravenously to patients with stable heart failure. The trial s primary objective is to evaluate the safety and tolerability of CK-1827452. Its secondary objectives are to establish a relationship between the plasma concentration and the pharmacodynamic effects of CK-1827452 and to determine its pharmacokinetics in stable heart failure patients. In addition to routine assessments of vital signs, blood samples and electrocardiographic monitoring, echocardiograms are being performed to evaluate cardiac function at various pre-defined

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time points. The clinical trial is planned to consist of at least five cohorts of eight patients with stable heart failure. In the first four cohorts, patients undergo four treatment periods, receiving three escalating active doses of CK-1827452 and one placebo treatment randomized into the dose escalation sequence to maintain blinding. Patients receive a loading infusion to rapidly achieve a target plasma concentration of CK-1827452 during the first hour, followed by a slower infusion intended to maintain that plasma concentration during the remainder of the infusion. The first two of these cohorts were designed to study a range of target CK-1827452 plasma concentrations, from 90 ng/ml in the lowest dose regimen in Cohort 1 to 650 ng/ml in the highest dose regimen in Cohort 2; Cohorts 3 and 4 were designed to gain experience across the same range plasma of concentrations, but with infusions of a longer duration. In Cohorts 1 and 2, the second, slower, maintenance infusion was continued for one hour; in Cohort 3, the maintenance infusion was continued for 23 hours. At the time of the interim analysis, 22 patients had been evaluated in this clinical trial (8 patients from each of the completed Cohorts 1 and 2, and 6 patients from the then-ongoing Cohort 3.) The safety data from this analysis suggest that CK-1827452 was well-tolerated with no serious adverse events reported in patients exposed to the intended range of doses and plasma concentrations. A pharmacodynamic-pharmacokinetic analysis of data from these 22 patients showed that when compared to placebo, CK-1827452 produced statistically significant and clinically relevant increases in Doppler-derived stroke volume and fractional shortening as a consequence of statistically significant prolongations of systolic ejection time. At the highest CK-1827452 concentrations studied, stroke volume, the volume of blood pumped during each heartbeat, increased versus placebo from its mean baseline value of 71 mL by 19 ± 4 mL ($p < 0.0001$). In addition, fractional shortening increased versus placebo by 4.0 ± 2% ($p = 0.01$), and systolic ejection time by 95 ± 9 msec ($p < 0.0001$). These promising data reflect what we believe is the clinically relevant activity of this novel drug candidate. Following review of safety data from this interim analysis, we opened enrollment in a fourth cohort in this trial. This cohort will also evaluate a one-hour loading infusion followed by 23 hours of maintenance infusion over the same range of target CK-1827452 plasma concentrations evaluated in Cohort 3. We anticipate that final data will be available from this trial during the second half of 2008.

Phase IIa stable heart failure (cardiac catheterization): In the second quarter of 2008, we opened enrollment in an open-label, non-randomized Phase IIa clinical trial designed to evaluate an intravenous formulation of CK-1827452 administered to patients with stable heart failure undergoing clinically indicated coronary angiography in a cardiac catheterization laboratory. The primary objective of this trial is to evaluate the potential effects of CK-1827452 on myocardial efficiency, defined as the ratio of ventricular performance to myocardial oxygen consumption. The secondary objective of this trial is to measure the potential effects of CK-1827452 on ventricular performance, myocardial oxygen consumption, hemodynamics, pressure-volume relationships and systolic ejection time. We continue to screen patients for the potential initiation of this trial.

CK-1827452 (oral)

Phase I drug-drug interaction: In April 2007, we announced the initiation of a single-center, open-label, sequential, parallel group, Phase I clinical trial of CK-1827452 designed to evaluate the potential for drug-drug interactions occurring via each of two drug-metabolizing enzymes, cytochrome P450 3A4 (CYP3A4) and cytochrome P450 2D6 (CYP2D6). In June 2008, we announced interim results which showed that, in CYP2D6 extensive metabolizers, the potent CYP3A4 inhibitor ketoconazole caused a modest reduction in the clearance of CK-1827452 and consequently, a modest but statistically significant increase in the elimination half-life of CK-1827452, from 22 to 27 hours ($p < 0.01$). This increase in the half-life of CK-1827452 with ketoconazole resulted in an approximate 50% increase in the area under the CK-1827452 plasma concentration versus time curve (AUC), which reflects the overall exposure to the study drug, and which was also statistically significant ($p < 0.01$). The maximum CK-1827452 plasma concentration (Cmax) was unaffected by ketoconazole (65 versus 67 ng/mL). Diltiazem, a moderate inhibitor of CYP3A4, had no effect on either the Cmax or AUC of CK-1827452 when the two were co-administered to CYP2D6 extensive metabolizer subjects, although the half-life increased slightly, from 18 to 20 hours ($p < 0.01$). We continue to screen and enroll subjects with the poor metabolizer genotype for CYP2D6, who comprise approximately 5% or less of the population. We anticipate that final data from this trial will be available in 2008.

Phase I oral multi-dose: In June 2008, we announced final results from a Phase I clinical trial designed to evaluate the safety, tolerability, pharmacokinetics and dose-proportionality of an oral formulation of CK-1827452 administered both as a single oral dose and as multiple oral doses of 10 mg and 30 mg strength capsules. The primary objective of

this study was to evaluate the safety and

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tolerability of CK-1827452 after a single oral dose and after multiple oral doses to steady-state in healthy men and women. The secondary objective of this study was to evaluate the pharmacokinetics of CK-1827452 after a single oral dose and after multiple oral doses to steady-state and to compare the pharmacokinetic parameters between healthy men and women. CK-1827452 was well-tolerated in the trial, with no drug-related serious adverse events. Dose-proportionality between the 10 mg and 30 mg dose levels was observed in both men and women, both after a single dose and after multiple doses to steady-state, with similar pharmacokinetics observed between men and women.

Phase I modified release: In December 2007, we initiated a single-center, two-part, open-label, Phase I clinical trial of up to twelve healthy male volunteers. Since an immediate release formulation of CK-1827452 was found to be rapidly absorbed in a previous study in healthy subjects, the purpose of developing these modified release forms was to reduce the rate of drug absorption without significantly affecting the overall bioavailability. The primary objective of this study was to assess the pharmacokinetics and relative bioavailability of three different oral modified release prototypes of CK 1827452 as compared to the immediate release formulation in up to twelve healthy male subjects. The secondary objective of the trial was to determine whether there is an effect of food on the pharmacokinetics of one of these oral modified release prototypes of CK-1827452. The single-dose pharmacokinetics of one formulation, in both the fasted and fed states, demonstrated that it reduced Cmax and elevated the trough plasma concentration as compared to the immediate release formulation without a substantial effect on overall bioavailability, resulting in a smaller range of fluctuation in plasma concentrations as compared to oral dosing with the immediate release formulation. This prototype modified release oral formulation of CK-1827452 has been selected to proceed forward into further clinical testing.

CK-1827452 (intravenous to oral)

In April 2008, we initiated a double-blind, randomized, placebo-controlled Phase IIa clinical trial designed to evaluate both an intravenous and an oral formulation of CK-1827452 in patients with ischemic cardiomyopathy and angina. The primary objective of this trial is to assess the effect of intravenous CK-1827452 on symptom-limited treadmill exercise tolerance. The secondary objectives of this trial are to assess the tolerability of CK-1827452 administered as an oral formulation, and to evaluate the resulting plasma concentrations. The target Cmax in Cohort 1 is 295 ng/mL; the target Cmax in Cohort 2 is 550 ng/mL. We recently completed enrollment of the first cohort of patients in this trial. We are conducting an interim safety analysis of clinical data arising from the first cohort in order to enable the initiation of the second and final cohort.

CK-1827452 is at too early a stage of development for us to predict if or when we will be in a position to generate any revenues or material net cash flows from its commercialization. We currently fund all research and development costs associated with this program. We recorded research and development expenses for activities relating to our cardiovascular program of approximately $10.5 million for the six months ended June 30, 2008, and $11.5 million for the six months ended June 30, 2007. We anticipate that our expenditures relating to the research and development of compounds in our cardiovascular program will increase significantly as we advance CK-1827452 through clinical development. Our expenditures will also increase if Amgen does not exercise its option and we elect to develop CK-1827452 or related compounds independently, or if we elect to co-fund later-stage development of CK-1827452 or other compounds in our cardiovascular program under our collaboration and option agreement with Amgen following Amgen s exercise of its option. If Amgen elects to exercise its option, it would be responsible for development and commercialization of CK-1827452 and related compounds, subject to our development and commercial participation rights. In addition, we may be eligible to receive precommercialization and commercialization milestone payments of up to $600 million on CK-1827452 and other products arising from the research under the collaboration, as well as escalating royalties based on increasing levels of annual net sales of products commercialized under the agreement. The agreement also provides for us to receive increased royalties by co-funding Phase III development costs of drug candidates under the collaboration. If we elect to co-fund such costs, we would be entitled to co-promote products in North America and participate in agreed commercial activities in institutional care settings, at Amgen s expense.

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If Amgen elects not to exercise its option on CK-1827452, we may then independently proceed to develop CK-1827452 and the collaboration with Amgen would terminate.

Oncology

In the six months ended June 30, 2008, we continued to advance our oncology development programs for our drug candidates ispinesib and SB-743921 as they progressed in Phase I of their respective Phase I/II clinical trials and GSK continued conducting the first-time-in-humans Phase I clinical trial of our drug candidate GSK-923295. These three drug candidates are being developed in connection with our collaboration and license agreement with GSK. This strategic alliance is focused on novel small molecule therapeutics targeting a family of cytoskeletal proteins known as mitotic kinesins for the treatment of cancer. Pursuant to a November 2006 amendment to the GSK collaboration and license agreement, we assumed responsibility, at our expense, for the continued research, development and commercialization of ispinesib and SB-743921, subject to GSK s option to resume development and commercialization of either or both of ispinesib and SB-743921. This option is exercisable until the end of 2008. For those drug candidates that GSK develops under the strategic alliance, we can elect to co-fund certain later-stage development activities which would increase our potential royalty rates on sales of resulting drugs and provide us with the option to secure co-promotion rights in North America. If we elect to co-fund later-stage development of GSK-923295, the royalty rates to be paid to us for future sales of any resulting drugs would increase, and could result in increased payments to us based on increasing product sales and co-funding by us. If we elect to co-fund later-stage development of ispinesib or SB-743921, we believe that the royalty rates to be paid to us for future sales of any resulting drugs would increase to an even higher percentage rate, and could result in increased payments to us, based on increasing product sales and co-funding by us. If we exercise our co-promotion option, then we are entitled to receive reimbursement from GSK for certain sales force costs we incur in support of our commercial activities. We are also researching other compounds for the potential treatment of cancer.

Ispinesib

The clinical trials program sponsored by GSK and the NCI for ispinesib, an inhibitor of kinesin spindle protein, consisted of nine Phase II clinical trials and eight Phase I or Ib clinical trials evaluating the use of this drug candidate in a variety of both solid and hematologic cancers. We believe that the breadth of this clinical trials program took into consideration the potential and the complexity of developing a drug candidate such as ispinesib, and should help us to identify those tumor types and dosing regimens that are the most promising for the continued development of ispinesib. We have reported Phase II clinical trial data for ispinesib in metastatic breast, non-small cell lung, ovarian, colorectal, head and neck, hepatocellular, renal and prostate cancers and in melanoma. To date, we believe some clinical activity for ispinesib has been observed in non-small cell lung, ovarian and breast cancers, with the most clinical activity observed in a Phase II clinical trial evaluating ispinesib in the treatment of patients with locally advanced or metastatic breast cancer that had failed treatment with taxanes and anthracyclines. Under our strategic alliance with GSK, we have initiated a focused development program for ispinesib in the treatment of patients with locally advanced or metastatic breast cancer. This program is intended to build upon the previous data from the clinical trials conducted by GSK and the NCI, and is designed to further define the clinical activity profile of ispinesib in chemotherapy-naïve locally advanced or metastatic breast cancer patients in preparation for potentially initiating a later stage clinical trials program of ispinesib for the second-line treatment of advanced breast cancer.

Currently ongoing and recently completed clinical trials of ispinesib are as follows:

Breast Cancer: In December 2007, we initiated, at our expense, an open-label, non-randomized Phase I/II clinical trial designed to evaluate ispinesib as monotherapy administered as a first-line treatment in chemotherapy-naïve patients with locally advanced or metastatic breast cancer. This trial is designed to be a proof-of-concept study to potentially amplify the signals of clinical activity seen in GSK s Phase II monotherapy trial of ispinesib in breast cancer that had failed to respond or progressed after treatment with an anthracycline and a taxane, and is intended to provide the data necessary to inform ispinesib s further development, as well as to inform GSK s potential exercise of its option to develop and commercialize ispinesib. The primary objectives of the Phase I portion of this clinical trial are to determine the dose limiting toxicities and maximum tolerated dose, and to assess the safety and tolerability of ispinesib administered as a 1-hour intravenous infusion on days 1 and 15 of a 28-day cycle. The secondary objectives are to characterize the pharmacokinetics of ispinesib on this schedule and to evaluate the effect of ispinesib on

biomarkers of cell proliferation in patients with accessible tumors.

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In June 2008, a poster containing interim data from Phase I of this trial was presented at the 2008 Annual Meeting of the American Society of Clinical Oncology (ASCO) in Chicago, IL. At the interim analysis point, the authors concluded that preliminary data suggests that ispinesib is well-tolerated when dosed on days 1 and 15 every 28 days at doses up to 12 mg/m^2. The most common toxicity in this clinical trial observed to date has been neutropenia. No neuropathy, alopecia or Grade 2 or higher gastrointestinal toxicity has been observed in this trial. We continue to enroll patients and dose-escalate in the Phase I portion of this Phase I/II clinical trial. We anticipate that data from the ongoing Phase I portion of this trial will be available in the third quarter of 2008.

Ispinesib with capecitabine: In June 2008, we announced the results of a Phase Ib clinical trial sponsored by GSK designed to evaluate ispinesib in combination with capecitabine, an oral chemotherapy agent commonly used in the treatment of breast cancer. This trial was an open-label, dose-escalation study of ispinesib in combination with capecitabine on an every 21-day schedule in subjects with advanced solid tumors. Its primary objectives were to assess the safety and tolerability and to determine the optimally tolerated regimen of ispinesib when administered as a 1-hour infusion on day 1 in combination with daily administration of capecitabine given on days 1 through 14 of the 21-day cycle. The secondary objective was to assess the clinical activity of this combination in patients with advanced solid tumors. Although a single dose regimen was not formally confirmed as the optimally tolerated regimen, ispinesib administered at 18 mg/m^2, its maximum tolerated dose as monotherapy, was well-tolerated in combination with therapeutic doses of capecitabine at daily doses of 2000 mg/m^2 and 2500 mg/m^2. The investigators in this clinical trial concluded that the combination of ispinesib with capecitabine had an acceptable tolerability profile on the 21-day schedule investigated in the trial. The dose limiting toxicities in this combination regimen were consistent with the monotherapy toxicities of ispinesib (prolonged neutropenia) and capecitabine (rash). In this trial, the best response observed among the 24 patients treated was a partial response by Response Evaluation Criteria In Solid Tumors in a patient with advanced breast cancer. In addition, 11 patients had a response of stable disease by this criteria.

Pediatric Solid Tumors: In June 2008, at the ASCO annual meeting, the NCI presented final data from a Phase I clinical trial designed to evaluate the safety, tolerability, pharmacodynamics and pharmacokinetic profile of ispinesib as monotherapy administered as a one-hour infusion on days 1, 8 and 15 of a 28-day schedule to pediatric patients with relapsed or refractory solid tumors. Of the 24 patients enrolled in this clinical trial, 18 were evaluable for toxicity and 23 were evaluable for a response. The authors concluded that the maximum tolerated dose on this schedule for this patient population was 9 mg/m^2. In this clinical trial, the dose limiting toxicities observed were neutropenia (n=3), hyperbilirubinemia (n=1) and elevated ALT (n=1). The best response observed was stable disease at 7 courses in one patient. Three patients experienced stable disease for longer than 3 courses of therapy. The authors concluded that ispinesib was well-tolerated in pediatric patients, with neutropenia and hepatotoxicity representing the most commonly observed dose limiting toxicities.

Acute Leukemias, Chronic Myelogenous Leukemia or Advanced Myelodysplastic Syndromes: The NCI has completed enrollment in a Phase I clinical trial designed to evaluate the safety, tolerability and pharmacokinetic profile of ispinesib as monotherapy administered as a one-hour infusion on days 1, 2 and 3 of a 21-day cycle in adult patients with relapsed or refractory acute leukemias, chronic myelogenous leukemia in blast crisis or advanced myelodysplastic syndromes.

We expect that it will take several years before ispinesib can be commercialized, if at all. Ispinesib is at too early a stage of development for us to predict if and when we will be in a position to generate any revenues or material net cash flows from any resulting drugs. Accordingly, we cannot reasonably estimate when and to what extent ispinesib will generate revenues or material net cash flows, which may vary widely depending on numerous factors, including, but not limited to, the safety and efficacy profile of the drug, receipt of regulatory approvals, market acceptance, then-prevailing reimbursement policies, competition and other market conditions. We have assumed responsibility for funding the research and development costs associated with ispinesib pursuant to the November 2006 amendment to our collaboration and license agreement with GSK. We have initiated a focused development program for ispinesib in the treatment of patients with locally advanced or metastatic breast cancer designed to further define the clinical activity profile of ispinesib in advanced breast cancer patients. If GSK does not exercise its option to resume responsibility for some or all of the development and commercialization activities associated with this drug candidate, and we continue to advance the drug candidate on our own, our expenditures relating to research and development of

this drug candidate will increase significantly.

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SB-743921

SB-743921, our second anti-cancer drug candidate, also inhibits kinesin spindle protein but is structurally distinct from ispinesib. SB-743921 is also being developed in connection with our strategic alliance with GSK. Though we are aware of no clinical shortcomings of ispinesib that are addressed by SB-743921, we believe that having two kinesin spindle protein inhibitors in concurrent clinical development increases the likelihood that a commercial product will result from this research and development program.

SB-743921 was studied by GSK in a dose-escalating Phase I clinical trial evaluating its safety, tolerability and pharmacokinetics in advanced cancer patients. The primary objectives of this clinical trial were to determine the dose limiting toxicities and to establish the maximum tolerated dose of SB-743921 administered intravenously on a once every 21-day schedule. Secondary objectives included assessment of the safety and tolerability of SB-743921, characterization of the pharmacokinetics of SB-743921 on this schedule and a preliminary assessment of its anti-tumor activity. The observed toxicities at the recommended Phase II dose were manageable. Dose limiting toxicities in this clinical trial consisted predominantly of neutropenia and elevations in hepatic enzymes and bilirubin. Disease stabilization, ranging from 9 to 45 weeks, was observed in seven patients. One patient with cholangiocarcinoma had a confirmed partial response at the maximum tolerated dose.

Phase I/II Hodgkin and non-Hodgkin Lymphoma: In 2006, we initiated, at our expense, an additional clinical trial of SB-743921 in hematologic cancers. We continue to enroll and dose-escalate patients in Phase I of an open-label, non-randomized Phase I/II clinical trial to investigate the safety, tolerability, pharmacodynamics and pharmacokinetic profile of SB-743921 administered as a one-hour infusion on days 1 and 15 of a 28-day schedule in patients with Hodgkin or non-Hodgkin lymphoma, first without, and then with, the addition of granulocyte colony-stimulating factor (G-CSF). In June 2008, in association with proceedings at both the ASCO annual meeting and the 10th International Conference on Malignant Lymphoma in Lugano, Switzerland, interim data from the Phase I portion of this trial were presented. At the interim analysis point, 46 patients had been enrolled and 43 patients were treated. Of the treated patients, 43 were evaluable for safety and 28 were evaluable for efficacy. The authors concluded that the pattern of neutropenia onset and recovery support a dosing schedule for SB-743921 of days 1 and 15 of a 28-day cycle. The maximum tolerated dose of SB-743921 was 6 mg/m^2 when given days 1 and 15 every 28 days without G-CSF support. This represents a greater dose density (0.43 mg/m^2/day) than on the previously studied schedule; i.e., 4 mg/m^2 once every 21 days (0.19 mg/m^2/day). The only dose limiting toxicity observed without G-CSF was neutropenia; therefore further dose escalation with empiric, prophylactic G-CSF is ongoing. The trial is currently enrolling at 8 mg/m^2. The declines from baseline seen in neutrophil counts on day 8 and 22 without G-CSF were not observed with 6 mg/m^2 plus G-CSF, suggesting further dose escalation with G-CSF may be possible. Grade 3 and 4 toxicities other than neutropenia were uncommon; in particular, no evidence of neuropathy or alopecia was observed. To date, one objective partial response has been observed at the maximum tolerated dose without G-CSF in a patient with Hodgkin lymphoma. We anticipate that final data will be available from the Phase I portion of this trial in 2008.

The clinical trials program for SB-743921 may proceed for several years, and we will not be in a position to generate any revenues or material net cash flows from this drug candidate until and unless the program is successfully completed, regulatory approval is achieved and a drug is commercialized. SB-743921 is at too early a stage of development for us to predict when or if this may occur. The November 2006 amendment to our collaboration and license agreement with GSK provides for us to fund the future development of SB-743921 in all cancer indications subject to GSK s option to resume responsibility for some or all development and commercialization activities. As a result of our conduct of our current Phase I/II clinical trial of SB-743921 in hematologic cancers, and any further development activities for SB-743921 we may conduct under this amendment, our expenditures relating to research and development of this drug candidate will increase significantly.

If GSK exercises its option for either or both of ispinesib and SB-743921, it will pay us an option fee equal to the costs we independently incurred for the development of that drug candidate, plus a premium intended to compensate us for the cost of capital associated with such costs, subject to an agreed limit for such costs and premium. Upon GSK exercising its option for a drug candidate, we may receive additional precommercialization milestone payments with respect to such drug candidate and increased royalties on net sales of any resulting product, in each case, beyond those contemplated under the original agreement.

GSK-923295

GSK-923295 is the third drug candidate to arise from our strategic alliance with GSK. GSK-923295 is an inhibitor of a second mitotic kinesin, centromere-associated protein E. Centromere-associated protein E is directly involved in coordinating the decision a cell makes to divide with the actual trigger of the mechanics of cell division. These processes are essential for cancer cells to grow. GSK-923295

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causes partial and complete shrinkages of human tumors in animal models and has exhibited properties in these studies that distinguish it from ispinesib and SB-743921.

Phase I First-Time-in-Humans: During the quarter, GSK continued to enroll patients and dose-escalate in a first-time-in-humans Phase I clinical trial of GSK-923295. This trial is an open-label, non-randomized, dose-finding trial designed to investigate the safety, tolerability, pharmacodynamics and pharmacokinetic profile of GSK-923295 in patients with advanced solid tumors. The initiation of this clinical trial in August 2007 triggered a milestone payment of $1.0 million from GSK to Cytokinetics under our collaboration and license agreement with GSK. An oral presentation at the April 2008 American Association of Cancer Research Annual Meeting highlighted interim clinical data from this trial. The authors concluded that the pharmacokinetics of GSK-923295 were generally dose-proportional over the dose range of 10 to 80 mg/m2 and that intrapatient pharmacokinetics on days 1 and 15 were similar. We anticipate that data from this trial will be available in the third quarter of 2008.

In June 2008, we amended our collaboration and license agreement with GSK to extend the research term for an additional year through June 19, 2009 to facilitate continued research activities under an updated research plan focused on centromere-associated protein E. Under the June 2008 amendment, GSK will have no obligation to reimburse us for full-time employee equivalents (FTEs) or other research-related expenses during the extension of the research term.

The development program for GSK-923295 may proceed for several years, and we will not be in a position to generate any revenues or material net cash flows from this potential drug candidate unless the program is successfully completed, regulatory approval is achieved and a drug is commercialized. GSK-923295 is at too early a stage of development for us to predict when or if this may occur. If GSK abandons development of GSK-923295 prior to regulatory approval, we may undertake and fund the clinical development of this drug candidate, or its commercialization, or we may seek a new partner for such clinical development or commercialization, or curtail or abandon such clinical development.

We recorded research and development expenses for activities relating to our mitotic kinesin programs of approximately $4.0 million for the six months ended June 30, 2008, and $2.9 million for the six months ended June 30, 2007. We anticipate that our expenditures relating to the development of ispinesib and SB-743921 will increase significantly as we advance through clinical development. Our expenditures will also increase if GSK does not exercise its option to resume responsibility for some or all of the development and commercialization activities associated with ispinesib and SB-743921, or if we elect to co-fund later-stage development for one or more of ispinesib, SB-743921 and GSK-923295. For those drug candidates and potential drug candidates that GSK develops under the strategic alliance, which currently includes GSK-923295 and which may include either or both of ispinesib and SB-743921 if so elected by GSK pursuant to its option, we may elect to co-fund certain later-stage development activities which would increase our potential royalty rates on sales of resulting drugs and provide us with the option to secure co-promotion rights in North America. We expect that the royalties to be paid on potential future sales, if any, by GSK of each of ispinesib, SB-743921 and GSK-923295 will be based on increasing product sales and our anticipated level of co-funding, if any. If we exercise our co-promotion option, then we will receive reimbursement from GSK for certain sales force costs we incur in support of our commercial activities.

Research

In April 2008, we announced the selection of a development compound directed towards the skeletal sarcomere. Preclinical data indicates that this compound is a highly specific small molecule activator of the troponin complex, increasing its sensitivity to calcium, and subsequently leading to an increase in skeletal muscle contractility. This compound has demonstrated encouraging pharmacological activity in non-clinical models that may relate to the potential treatment of skeletal muscle weakness associated with neuromuscular diseases or other conditions. This potential drug candidate is the fifth development compound to emerge from our research activities focused on discovering novel therapeutics directed towards cytoskeletal biology.

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In the second quarter, we advanced novel smooth muscle myosin inhibitors in lead optimization activities towards the potential selection of one or more development compounds. Company scientists have characterized compounds arising from this research in pharmacology studies and have demonstrated encouraging evidence of efficacy for an inhaled formulation of certain of these compounds in preclinical bronchoconstriction models related to asthma and other reactive airways disorders.

Development Risks

The successful development of all of our drug candidates is highly uncertain. We cannot estimate with certainty or know the exact nature, timing and estimated costs of the activities necessary to complete the development of any of our drug candidates or the date of completion of these development activities. We cannot estimate with certainty any of the foregoing due to the numerous risks and uncertainties associated with developing our drug candidates, including, but not limited to:

- the uncertainty of the timing of the initiation and completion of patient enrollment in our clinical trials;
- the possibility of delays in the collection of clinical trial data and the uncertainty of the timing of the analyses of our clinical trial data after such trials have been initiated and completed;
- our potential inability to obtain or retain partners to assist in the design, management and funding of later stage clinical trials;
- the possibility of delays in characterization, synthesis or optimization of potential drug candidates;
- delays or additional costs in developing appropriate formulations of our drug candidates for clinical trial use;
- the uncertainty of clinical trial results;
- the uncertainty of obtaining FDA or other foreign regulatory agency approval required for the clinical investigation of new therapies; and
- the uncertainty related to the development of commercial scale manufacturing processes and qualification of a commercial scale manufacturing facility.

If we fail to complete the development of any of our drug candidates in a timely manner, it could have a material adverse effect on our operations, financial position and liquidity. In addition, any failure by us or our partners to obtain, or any delay in obtaining, regulatory approvals for our drug candidates could have a material adverse effect on our results of operations. A further discussion of the risks and uncertainties associated with completing our programs on schedule, or at all, and certain consequences of failing to do so are discussed further in the risk factors entitled We have never generated, and may never generate, revenues from commercial sales of our drugs and we may not have drugs to market for at least several years, if ever, Clinical trials may fail to demonstrate the desired safety and efficacy of our drug candidates, which could prevent or significantly delay completion of clinical development and regulatory approval and Clinical trials are expensive, time consuming and subject to delay, as well as other risk factors.

Revenues

Our current revenue sources are limited, and we do not expect to generate any direct revenue from product sales for several years. We have recognized revenues from our strategic alliances with Amgen, GSK and AstraZeneca for license fees and contract research activities.

Under our collaboration and option agreement with Amgen, we received an upfront, non-refundable license and technology access fee of $42.0 million. In connection with entering into the agreement, we also entered into a common stock purchase agreement with Amgen. In January 2007, we issued 3,484,806 shares of our common stock to Amgen for net proceeds of $32.9 million, of which the $6.9 million purchase premium was recorded as deferred revenue. We are amortizing the upfront fee and stock premium to license revenue ratably over the maximum term of the non-exclusive license, which is four years. We may receive additional payments from Amgen upon achieving

certain precommercialization and commercialization milestones. Milestone payments are non-refundable and are recognized as revenue when earned, as evidenced by achievement of the specified milestones and the absence of ongoing performance obligations.

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We may also be eligible to receive reimbursement for contract development activities subsequent to Amgen s option exercise, which we will record as revenue if and when the related expenses are incurred. We record amounts received in advance of performance as deferred revenue.

Charges to GSK in 2006 were based on negotiated rates intended to approximate the costs for our FTEs performing research under the strategic alliance and our out-of-pocket expenses, which we recorded as the related expenses were incurred. GSK paid us an upfront licensing fee, which we recognized ratably over the strategic alliance s initial five-year research term, which ended in June 2006. In 2007, we received a $1.0 million milestone payment from GSK relating to its initiation of a phase I clinical trial of GSK-295. We may receive additional payments from GSK upon achieving certain precommercialization milestones. Milestone payments are non-refundable and are recognized as revenue when earned, as evidenced by achievement of the specified milestones and the absence of ongoing performance obligations. We record amounts received in advance of performance as deferred revenue. The revenues recognized to date are nonrefundable, even if the relevant research effort is not successful.

Charges to AstraZeneca in 2005 were based on negotiated rates intended to approximate the costs for our FTEs performing research under the strategic alliance. The revenues recognized since inception to date are not refundable. The research term of our collaboration and license agreement with AstraZeneca expired in December 2005, and we formally terminated that agreement in August 2006.

Because a substantial portion of our revenues for the foreseeable future will depend on achieving development and other precommercialization milestones under our strategic alliances with GSK and Amgen, our results of operations may vary substantially from year to year.

We expect that our future revenues will most likely be derived from royalties on sales from drugs licensed to GSK or Amgen under our strategic alliances and from those licensed to future partners, as well as from direct sales of our drugs. If Amgen exercises its option, we will retain a product-by-product option to co-fund certain later-stage development activities under our strategic alliance with Amgen, thereby potentially increasing our royalties and affording us co-promotion rights in North America. For those products being developed by GSK under our strategic alliance, we also retain a product-by-product option to co-fund certain later-stage development activities, thereby potentially increasing our royalties and affording us co-promotion rights in North America. If we exercise our co-promotion rights under either strategic alliance, we are entitled to receive reimbursement for certain sales force costs we incur in support of our commercial activities.

Research and Development Expenses

We incur research and development expenses associated with both partnered and unpartnered research activities, as well as the development and expansion of our drug discovery technologies. Research and development expenses related to our strategic alliance with GSK consisted primarily of costs related to research and screening, lead optimization and other activities relating to the identification of compounds for development as mitotic kinesin inhibitors for the treatment of cancer. Prior to June 2006, certain of these costs were reimbursed by GSK on an FTE basis. From 2001 through November 2006, GSK funded the majority of the costs related to the clinical development of ispinesib and SB-743921. Under our November 2006 amendment to our collaboration and license agreement with GSK, we assumed responsibility for the continued research, development and commercialization of inhibitors of kinesin spindle protein, including ispinesib and SB-743921, and other mitotic kinesins other than centromere-associated protein E, at our sole expense subject to GSK s option to resume responsibility for the development and commercialization of either or both of ispinesib and SB-743921, exercisable during a defined period. We also have the option to co-fund certain later-stage development activities for GSK-923295. Our conduct of the research and development of ispinesib and SB-743921 and the potential exercise of our co-funding option will result in a significant increase in research and development expenses. We expect to incur research and development expenses in the continued conduct of preclinical studies and clinical trials for CK-1827452 and other of our cardiac myosin activator compounds for the treatment of heart failure and in