

XOMA Corp
Form 10-Q
November 07, 2013

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10-Q

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

For the quarterly period ended September 30, 2013

or

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

For the transition period from _____ to _____

Commission File No. 0-14710

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

Delaware 52-2154066
(State or other jurisdiction (I.R.S. Employer Identification No.)
of incorporation or organization)

2910 Seventh Street, Berkeley, (510) 204-7200
California 94710
(Address of principal executive offices, (Telephone Number)
including zip code)

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

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

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

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

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

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

<u>Class</u>	<u>Outstanding at November 5, 2013</u>
Common Stock, \$0.0075 par value	93,077,887

XOMA CORPORATION
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PART I - FINANCIAL INFORMATION

ITEM 1. CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (unaudited)

XOMA CORPORATION

CONDENSED CONSOLIDATED BALANCE SHEETS

(in thousands, except share and per share amounts)

	September 30, 2013 (unaudited)	December 31, 2012 (Note 1)
ASSETS		
Current assets:		
Cash and cash equivalents	\$73,988	\$45,345
Short-term investments	-	39,987
Trade and other receivables, net	5,630	8,249
Prepaid expenses and other current assets	3,150	2,256
Total current assets	82,768	95,837
Property and equipment, net	6,917	8,143
Other assets	1,321	1,696
Total assets	\$91,006	\$105,676
LIABILITIES AND STOCKHOLDERS' (DEFICIT) EQUITY		
Current liabilities:		
Accounts payable	\$6,505	\$3,867
Accrued and other liabilities	8,016	13,045
Deferred revenue	3,414	3,409
Interest bearing obligation – current	4,085	3,391
Accrued Interest on interest bearing obligations – current	1,969	121
Total current liabilities	23,989	23,833
Deferred revenue – long-term	4,457	6,315
Interest bearing obligations – long-term	36,941	37,653
Contingent warrant liabilities	39,162	15,001
Other liabilities - long term	-	1,407
Total liabilities	104,549	84,209
Stockholders' (deficit) equity:		
Common stock, \$0.0075 par value, 138,666,666 shares authorized, 92,701,155 and 82,447,274 shares outstanding at September 30, 2013 and December 31, 2012, respectively	692	615
Additional paid-in capital	1,014,642	977,962
Accumulated other comprehensive income	-	8
Accumulated deficit	(1,028,877)	(957,118)
Total stockholders' (deficit) equity	(13,543)	21,467
Total liabilities and stockholders' (deficit) equity	\$91,006	\$105,676

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

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

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XOMA CORPORATION

CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE LOSS

(unaudited)

(in thousands, except per share amounts)

	Three months ended September 30,		Nine months ended September 30,	
	2013	2012	2013	2012
Revenues:				
License and collaborative fees	\$1,574	\$1,127	\$2,578	\$4,665
Contract and other	4,738	6,124	20,339	21,725
Total revenues	6,312	7,251	22,917	26,390
Operating expenses:				
Research and development	18,198	18,409	51,905	52,702
Selling, general and administrative	5,225	4,672	13,429	12,918
Restructuring	112	323	209	4,776
Total operating expenses	23,535	23,404	65,543	70,396
Loss from operations	(17,223)	(16,153)	(42,626)	(44,006)
Other expense:				
Interest expense	(1,159)	(1,144)	(3,495)	(3,211)
Other expense	(132)	(420)	92	(542)
Revaluation of contingent warrant liabilities	(11,125)	(9,208)	(25,745)	(25,746)
Net loss before taxes	(29,639)	(26,925)	(71,774)	(73,505)
Provision for income tax benefit	15	74	15	74
Net loss	\$(29,624)	\$(26,851)	\$(71,759)	\$(73,431)
Basic and diluted net loss per share of common stock	\$(0.34)	\$(0.39)	\$(0.85)	\$(1.22)
Shares used in computing basic and diluted net loss per share of common stock	87,033	68,189	84,205	60,239
Other comprehensive loss:				
Net loss	\$(29,624)	\$(26,851)	\$(71,759)	\$(73,431)
Net unrealized loss on available-for-sale securities	-	7	-	12
Comprehensive loss	\$(29,624)	\$(26,844)	\$(71,759)	\$(73,419)

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

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XOMA CORPORATION

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

(unaudited)

(in thousands)

	Nine Months Ended September 30,	
	2013	2012
Cash flows from operating activities:		
Net loss	\$(71,759)	\$(73,431)
Adjustments to reconcile net loss to net cash used in operating activities:		
Depreciation	2,014	3,308
Common stock contribution to 401(k)	828	1,134
Stock-based compensation expense	3,946	3,368
Accrued interest on interest bearing obligations	2,031	878
Revaluation of contingent warrant liabilities	25,745	25,746
Restructuring charge related to long-lived assets	-	2,241
Amortization of debt discount, final payment fee on debt, and debt issuance costs	1,841	1,388
Loss on sale and retirement of property & equipment	281	-
Unrealized gain on foreign currency exchange	(55)	(88)
Unrealized loss on foreign exchange options	184	721
Other non-cash adjustments	(21)	17
Changes in assets and liabilities:		
Trade and other receivables, net	2,637	5,251
Prepaid expenses and other assets	(1,042)	(421)
Accounts payable and accrued liabilities	(2,130)	3,451
Deferred revenue	(1,436)	(2,948)
Other liabilities	(1,666)	(47)
Net cash used in operating activities	(38,602)	(29,432)
Cash flows from investing activities:		
Purchase of investments	-	(16,988)
Proceeds from maturities of investments	40,000	-
Net purchase of property and equipment	(1,069)	(2,097)
Proceeds from sale of property and equipment	-	452
Net cash provided by (used in) investing activities	38,931	(18,633)
Cash flows from financing activities:		
Proceeds from issuance of common stock, net of issuance costs	29,959	39,624
Proceeds from exercise of warrants	438	-
Proceeds from issuance of long-term debt, net of issuance costs	-	4,439
Principal payments of debt	(2,083)	(2,143)
Net cash provided by financing activities	28,314	41,920
Net increase in cash and cash equivalents	28,643	(6,145)
Cash and cash equivalents at the beginning of the period	45,345	48,344
Cash and cash equivalents at the end of the period	\$73,988	\$42,199

Supplemental Cash Flow Information:

Cash paid for:

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Interest	\$988	\$723
Non-cash investing and financing activities:		
Issuance of warrants	\$-	\$6,390
Reclassification of contingent warrant liability to equity upon exercise of warrants	\$(1,585)	\$(337)
Interest added to principal balances on long-term debt	\$745	\$941
Investment in noncontrolling interest	\$171	\$-
Discount on long-term debt	\$-	\$(55)

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

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XOMA CORPORATION

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(unaudited)

1. Description of Business

XOMA Corporation (“XOMA” or the “Company”), a Delaware corporation combines a portfolio of late-stage clinical programs and research activities to develop innovative therapeutic antibodies for which it intends to commercialize. XOMA focuses its scientific research on allosteric modulation, which offers opportunities for new classes of therapeutic antibodies to treat a wide range of human diseases. XOMA is developing its lead product candidate gevokizumab (IL-1 beta modulating antibody) with Les Laboratoires Servier (“Servier”) through a global Phase 3 clinical development program and ongoing proof-of-concept studies in other IL-1-mediated diseases. XOMA’s scientific research also has produced the XMet platform, which consists of three classes of preclinical antibodies, including selective insulin receptor modulators that could offer new approaches in the treatment of diabetes. XOMA initiated commercial operations in January 2012 through the licensing of U.S. commercial rights to Servier’s ACEON® (perindopril erbumine) and certain U.S. rights to a patent-protected portfolio of fixed dose combination (“FDC”) product candidates where perindopril is combined with other active ingredients to treat cardiovascular disease. In July 2013, the Company transferred these rights to Symplmed Pharmaceuticals, LLC (“Symplmed”) in exchange for a minority equity position in Symplmed and up to double-digit royalties on sales of the first FDC product, if it is approved by the U.S. Food and Drug Administration (the “FDA”).

2. Basis of Presentation and Significant Accounting Policies

Basis of Presentation

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

In management’s opinion, the unaudited condensed consolidated financial statements include all adjustments, consisting only of normal recurring adjustments, which are necessary to present fairly the Company’s consolidated financial position as of September 30, 2013, the consolidated results of the Company’s operations for the three and nine months ended September 30, 2013 and 2012 and the Company’s cash flows for the nine months ended September 30, 2013 and 2012. The interim results of operations are not necessarily indicative of the results that may occur for the full fiscal year or future periods.

Use of Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States requires management to make estimates and assumptions that affect the reported amounts of assets, liabilities, revenue and expenses, and related disclosures. On an on-going basis, management evaluates its estimates including, but not limited to, those related to contingent warrant liabilities, revenue recognition, research and development expense, long-lived assets, derivative instruments, stock-based compensation, and restructuring liabilities. The Company bases its estimates on historical experience and on various other market-specific and other relevant

assumptions that are believed to be reasonable under the circumstances, the results of which form the basis for making judgments about the carrying values of assets and liabilities that are not readily apparent from other sources. Actual results may differ significantly from these estimates, such as the Company's billing under government contracts. Under the Company's contracts with the National Institute of Allergy and Infectious Diseases ("NIAID"), a part of the National Institutes of Health ("NIH"), the Company bills using NIH provisional rates and thus are subject to future audits at the discretion of NIAID's contracting office. These audits can result in adjustments to revenues previously reported.

Reclassifications

Certain reclassifications of prior period amounts have been made to the financial statements and accompanying notes to conform to the current period presentation. Prior period presentation of net product sales has been reclassified into contract and other revenue because the net product sales were not material for all periods presented. These reclassifications had no impact on the Company's previously reported net loss or cash flows.

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Long-lived Assets

The Company reviews the carrying values and depreciation lives of its long-lived assets whenever events or changes in circumstances indicate that the asset may not be recoverable. An impairment loss is recognized when the estimated future net cash flows expected to result from the use of an asset is less than its carrying amount. Long-lived assets include property and equipment and building and leasehold improvements. In connection with the Company's 2012 streamlining plan, the Company recorded an impairment loss of \$0.8 million during the nine months ended September 30, 2012. During the three and nine months ended September 30, 2012, the Company recorded accelerated depreciation of \$0.1 million and \$1.4 million, respectively, on long-lived assets. See Note 6: Streamlining and Restructuring Charges for additional disclosure on the 2012 streamlining plan.

Concentration of Risk

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

The Company has not experienced any significant credit losses and does not generally require collateral on receivables. For the nine months ended September 30, 2013, two customers represented 57% and 30% of total revenue and 27% and 50% of the accounts receivable balance.

For the nine months ended September 30, 2012, these two customers represented 45% and 35% of total revenues. As of December 31, 2012, there were receivables outstanding from these two customers representing 58% and 35% of the accounts receivable balance.

Newly Adopted Accounting Pronouncements

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

3. Condensed Consolidated Financial Statement Detail

Net Loss Per Share of Common Stock

Basic net loss per share of common stock is based on the weighted average number of shares of common stock outstanding during the period. Diluted net loss per share of common stock is based on the weighted average number of shares outstanding during the period, adjusted to include the assumed conversion of certain stock options, restricted stock units ("RSUs"), and warrants for common stock.

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

Three Months Ended September 30,	Nine Months Ended September 30,
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	2013	2012	2013	2012
Common stock options and restricted stock units	6,825	5,730	6,017	5,788
Warrants for common stock	15,970	16,626	16,106	12,942
Total	22,795	22,356	22,123	18,730

For the three and nine months ended September 30, 2013 and 2012, all outstanding securities were considered anti-dilutive, and therefore the calculation of basic and diluted net loss per share was the same.

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Cash and Cash Equivalents

At September 30, 2013, cash and cash equivalents consisted of demand deposits of \$16.2 million and money market funds of \$57.8 million with maturities of less than 90 days at the date of purchase. At December 31, 2012, cash and cash equivalents consisted of demand deposits of \$7.8 million and money market funds of \$37.5 million with maturities of less than 90 days at the date of purchase.

Short-term Investments

At September 30, 2013, the Company did not have short-term investments. At December 31, 2012, short-term investments consisted of U.S. treasury securities of \$40.0 million with maturities of greater than 90 days and less than one year from the date of purchase.

Foreign Exchange Options

The Company holds debt and may incur revenue and expenses denominated in foreign currencies, which exposes it to market risk associated with foreign currency exchange rate fluctuations between the U.S. dollar and the Euro. The Company is required in the future to make principal and accrued interest payments in Euros on its €15.0 million loan from Servier (See Note 7: Long-Term Debt and Other Financings). In order to manage its foreign currency exposure related to these payments, in May 2011, the Company entered into two foreign exchange option contracts to buy €1.5 million and €15.0 million in January 2014 and January 2016, respectively. By having these option contracts in place, the Company's foreign exchange rate risk is reduced if the U.S. dollar weakens against the Euro. However, if the U.S. dollar strengthens against the Euro, the Company is not required to exercise these options, but will not receive any refund on premiums paid.

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

The foreign exchange options were revalued at September 30, 2013 and had an aggregate fair value of \$0.3 million. The Company recognized a \$0.2 million loss on revaluation for the nine months ended September 30, 2013. The Company recognized losses for the three and nine months ended September 30, 2012 of \$0.1 million and \$0.7 million, respectively, as a result of the revaluation.

Accrued Liabilities

Accrued liabilities consisted of the following at September 30, 2013 and December 31, 2012 (in thousands):

	September 30, 2013	December 31, 2012
Accrued management incentive compensation	\$ 3,112	\$ 3,978
Accrued payroll and other benefits	2,708	2,461
Accrued clinical trial costs	500	4,702
Other	1,696	1,904
Total	\$ 8,016	\$ 13,045

Contingent Warrant Liabilities

In March 2012, in connection with an underwritten offering, the Company issued five-year warrants to purchase 14,834,577 shares of XOMA's common stock at an exercise price of \$1.76 per share. These warrants contain provisions that are contingent on the occurrence of a change in control, which would conditionally obligate the Company to repurchase the warrants for cash in an amount equal to their fair value using the Black-Scholes Option Pricing Model (the "Black-Scholes Model") on the date of such change in control. Due to these provisions, the Company is required to account for the warrants issued in March 2012 as a liability at fair value. In addition, the estimated liability related to the warrants is required to be revalued at each reporting period until the earlier of the exercise of the warrants, at which time the liability will be reclassified to stockholders' equity, or expiration of the warrants. At December 31, 2012, the fair value of the warrant liability was estimated to be \$15.0 million using the Black-Scholes Model. The Company revalued the warrant liability at September 30, 2013 using the Black-Scholes Model and recorded the \$25.7 million increase in the fair value as a loss in the revaluation of contingent warrant liabilities line of its condensed consolidated statements of comprehensive loss. The Company also reclassified \$1.6 million from contingent warrant liabilities to equity on its condensed consolidated balance sheets due to the exercise of warrants. As of September 30, 2013, 13,673,183 of these warrants were outstanding and had a fair value of \$39.1 million. This increase in liability is due primarily to the increase in the market price of the Company's common stock at September 30, 2013 compared to December 31, 2012.

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In February 2010, in connection with an underwritten offering, the Company issued five-year warrants to purchase 1,260,000 shares of XOMA's common stock at an exercise price of \$10.50 per share. In June 2009, the Company issued warrants to certain institutional investors as part of a registered direct offering. These warrants represent the right to acquire an aggregate of up to 347,826 shares of XOMA's common stock over a five year period beginning December 11, 2009 at an exercise price of \$19.50 per share. These warrants contain provisions that are contingent on the occurrence of a change in control, which would conditionally obligate the Company to repurchase the warrants for cash in an amount equal to their fair value using the Black-Scholes Model on the date of such change in control. Due to these provisions, the Company is required to account for the warrants issued in February 2010 and June 2009 as liabilities at fair value. As of September 30, 2013, all of these warrants were outstanding and had an aggregate fair value of approximately \$0.1 million.

4. Fair Value Measurements

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

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

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

Level 3 – Unobservable inputs.

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The following tables set forth the Company's fair value hierarchy for its financial assets and liabilities measured at fair value on a recurring basis as of September 30, 2013 and December 31, 2012.

Financial assets and liabilities carried at fair value as of September 30, 2013 and December 31, 2012 were classified as follows (in thousands):

	Fair Value Measurements at September 30, 2013 Using Quoted Prices in Active Markets for Identical Assets (Level 1)			Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Total
Assets:						
Money market funds ⁽¹⁾	\$57,756	\$ -	\$ -			\$57,756
Foreign exchange options ⁽³⁾	-	304	-			304
Total	\$57,756	\$ 304	\$ -			\$58,060

Liabilities:

Contingent warrant liabilities	\$-	\$ -	\$ 39,162			\$39,162
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	Fair Value Measurements at December 31, 2012 Using Quoted Prices in Active Markets for Identical Assets (Level 1)			Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Total
Assets:						
Money market funds ⁽¹⁾	\$37,461	\$ -	\$ -			\$37,461
U.S. treasury securities ⁽²⁾	39,987	-	-			39,987
Foreign exchange options ⁽³⁾	-	488	-			488
Total	\$77,448	\$ 488	\$ -			\$77,936

Liabilities:

Contingent warrant liabilities	\$-	\$ -	\$ 15,001			\$15,001
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(1) Included in cash and cash equivalents

(2) Included in short-term investments

(3) Included in other assets

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The fair value of the foreign exchange options at September 30, 2013 and December 31, 2012 was determined using readily observable market inputs from actively quoted markets obtained from various third-party data providers. These inputs, such as spot rate, forward rate and volatility have been derived from readily observable market data, meeting the criteria for Level 2 in the fair value hierarchy.

The fair value of the contingent warrant liabilities was determined at September 30, 2013 and December 31, 2012 using the Black-Scholes Model, which requires inputs such as the expected term of the warrants, volatility and risk-free interest rate. These inputs are subjective and generally require significant analysis and judgment to develop.

The fair value of the contingent warrant liabilities was estimated using the following range of assumptions at September 30, 2013 and December 31, 2012:

	September 30, 2013	December 31, 2012
Expected volatility	40 %	40 %
Risk-free interest rate	0.1% - 0.7 %	0.3% - 0.7 %
Expected term	1.2 - 3.4 years	1.9 - 4.2 years

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The following table provides a summary of changes in the fair value of the Company's Level 3 financial liabilities for the nine months ended September 30, 2013 (in thousands):

	September 30, 2013
Contingent warrant liabilities	15,001
Balance at December 31, 2012	(1,585)
Reclassification of contingent warrant liability to equity upon exercise of warrants	25,746
Net increase in fair value of contingent warrant liabilities upon revaluation	39,162
Balance at September 30, 2013	

For the three and nine months ended September 30, 2013, the Company recognized net increases of \$11.1 million and \$25.7 million, respectively, in the estimated fair value of the contingent warrant liabilities resulting in recognized losses in the revaluation of contingent warrant liabilities line of the condensed consolidated statements of comprehensive loss.

For the three and nine months ended September 30, 2012, the Company recognized net increases of \$9.2 million and \$25.7 million, respectively, in the estimated fair value of the contingent warrant liabilities resulting in recognized losses in the revaluation of contingent warrant liabilities line of the condensed consolidated statements of comprehensive loss.

5. Licensing, Collaborative and Other Arrangements

In July 2013, the Company transferred U.S. development and commercialization rights to the perindopril franchise to Symplmed. Under the terms of the arrangement, XOMA received a minority equity position in Symplmed and up to double-digit royalties on sales of the first fixed-dose combination containing perindopril arginine and amlodipine besylate, if it is approved by the FDA. The Company recorded the minority equity position in the other assets line of its condensed consolidated balance sheets. Symplmed, under a sublicense agreement, assumes U.S. marketing responsibilities for ACEON (perindopril erbumine), and XOMA continues to manage and be reimbursed for sales and distribution within its established commercial infrastructure until the ACEON New Drug Application ("NDA") is transferred to Symplmed. XOMA also continues to record gross ACEON sales in the contracts and other revenue line of its condensed consolidated statements of comprehensive loss until the ACEON NDA is transferred. Following the ACEON NDA transfer, Symplmed will pay XOMA single-digit royalties on sales of ACEON.

6. Streamlining and Restructuring Charges

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

In connection with the streamlining of operations, the Company incurred restructuring charges in the first nine months of 2012 of \$2.0 million related to severance, other termination benefits and outplacement services, \$2.2 million related to the impairment and accelerated depreciation of various assets and leasehold improvements, and \$0.7 million related to moving and other facility costs. In the first nine months of 2013, the Company has incurred \$0.2 million in restructuring charges related to facility costs and does not expect to incur additional significant restructuring charges during the remainder of 2013 related to these streamlining activities.

7. Long-Term Debt and Other Financings

Long-Term Debt

Novartis Note

In May 2005, the Company executed a secured note agreement with Novartis (then Chiron Corporation), which is due and payable in full in June 2015. Under the note agreement, the Company borrowed semi-annually to fund up to 75% of the Company's research and development and commercialization costs under its collaboration arrangement with Novartis, not to exceed \$50 million in aggregate principal amount. Interest on the principal amount of the loan accrues at six-month LIBOR plus 2%, which was equal to 2.41% at September 30, 2013, and is payable semi-annually in June and December of each year. Additionally, the interest rate resets in June and December of each year. At the Company's election, the semi-annual interest payments can be added to the outstanding principal amount, in lieu of a cash payment, as long as the aggregate principal amount does not exceed \$50 million. The Company has made this election for all interest payments thus far. Loans under the note agreement are secured by the Company's interest in its collaboration with Novartis, including any payments owed to it thereunder.

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At September 30, 2013 and December 31, 2012, the outstanding principal balance under this note agreement was \$14.6 million and \$14.4 million, respectively. Pursuant to the terms of the arrangement as restructured in November 2008, the Company will not make any additional borrowings under the Novartis note. Due to the structure of the secured note agreement with Novartis and since there is no liquid market for this obligation, there is no practical method to estimate fair value of this long-term debt.

Servier Loan

In December 2010, in connection with the license and collaboration agreement entered into with Servier, the Company executed a loan agreement with Servier (the "Servier Loan Agreement"), which provided for an advance of up to €15.0 million. The loan was fully funded in January 2011, with the proceeds converting to approximately \$19.5 million. The loan is secured by an interest in XOMA's intellectual property rights to all gevokizumab indications worldwide, excluding certain rights in the U.S. and Japan. Interest is calculated at a floating rate based on a Euro Inter-Bank Offered Rate ("EURIBOR") and subject to a cap. The interest rate is reset semi-annually in January and July of each year. The interest rate for the initial interest period was 3.22%. The interest rate has been reset to 3.83% for the six-month period from July 2011 through January 2012, 3.54% for the six-month period from January 2012 through July 2012, 2.80% for the six-month period from July 2012 through January 2013, 2.33% for the six-month period from January 2013 through July 2013, and 2.33% for the six-month period from July 2013 through January 2014. Interest is payable semi-annually; however, the Servier Loan Agreement provides for a deferral of interest payments over a period specified in the agreement. During the deferral period, accrued interest will be added to the outstanding principal amount for the purpose of interest calculation for the next six-month interest period. On the repayment commencement date, all unpaid and accrued interest shall be paid to Servier and thereafter, all accrued and unpaid interest shall be due and payable at the end of each six-month period. The loan matures in 2016; however, after a specified period prior to final maturity, the loan is to be repaid (i) at Servier's option, by applying up to a significant percentage of any milestone or royalty payments owed by Servier under the Company's collaboration agreement and (ii) using a significant percentage of any upfront, milestone or royalty payments the Company receives from any third-party collaboration or development partner for rights to gevokizumab in the U.S. and/or Japan. In addition, the loan becomes immediately due and payable upon certain customary events of default. At September 30, 2013 and December 31, 2012, the outstanding principal balance under this loan was \$20.3 million and \$19.8 million, respectively, using the Euro to US Dollar exchange rates of 1.3520 and 1.3215, respectively. For the three and nine months ended September 30, 2013, the Company recorded unrealized foreign exchange losses of \$0.8 million and \$0.5 million, respectively, related to the re-measurement of the loan, compared to an unrealized foreign exchange loss of \$0.4 million and an unrealized foreign exchange gain of \$0.1 million, for the same periods in 2012.

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

The loan discount is amortized under the effective interest method over the expected five-year life of the loan. The Company recorded non-cash interest expense of \$0.4 million and \$1.2 million in the three and nine months ended September 30, 2013, respectively, and \$0.4 million and \$1.1 million in the three and nine months ended September 30, 2012, respectively, resulting from the amortization of the loan discount. At September 30, 2013 and December 31, 2012, the net carrying value of the loan was \$15.8 million and \$14.2 million, respectively. For the three and nine months ended September 30, 2013, the Company recorded unrealized foreign exchange gains of \$0.2 million and \$0.1 million, respectively, related to the re-measurement of the loan discount, compared to an unrealized foreign exchange gain of \$0.1 million and an unrealized foreign exchange loss of \$0.1 million, respectively, for the same periods in 2012.

The Company believes realization of the benefit and the associated deferred revenue is contingent on the loan remaining outstanding over the five-year contractual term of the loan. If the Company were to stop providing service under the collaboration arrangement and the arrangement is terminated, the maturity date of the loan would be accelerated and a portion of measured benefit would not be realized. As the realization of the benefit is contingent, in part, on the provision of future services, the Company is recognizing the deferred revenue over the expected five-year life of the loan. The deferred revenue is amortized under the effective interest method, and the Company recorded \$0.4 million and \$1.2 million of related non-cash revenue during the three and nine months ended September 30, 2013, respectively, and \$0.4 million and \$1.1 million during the three and nine months ended September 30, 2012, respectively.

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General Electric Capital Corporation Term Loan

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

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

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

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

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

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

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At September 30, 2013 and December 31, 2012, the outstanding principal balance under the Amended Term Loan was \$10.4 million and \$12.5 million, respectively.

Interest Expense

Interest expense and amortization of debt issuance costs and discounts, recorded as other expense in the condensed consolidated statements of comprehensive loss for the three and nine months ended September 30, 2013 and 2012 are shown below (in thousands):

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2013	2012	2013	2012
Interest expense				
Servier loan	\$547	\$558	\$1,600	\$1,583
GECC term loan	508	475	1,584	1,298
Novartis note	90	99	272	298
Other	14	12	39	32
Total interest expense	\$1,159	\$1,144	\$3,495	\$3,211

Other Financings

Underwritten Offering

On August 23, 2013, the Company completed an underwritten public offering of 8,736,187 shares of its common stock, including 1,139,502 shares of its common stock that were issued upon the exercise of the underwriters' 30-day over-allotment option to purchase additional shares, at a public offering price of \$3.62 per share. Total gross proceeds from the offering were approximately \$31.6 million, before deducting underwriting discounts and commissions and estimated offering expenses totaling approximately \$2.2 million.

8. Income Taxes

The Company recognized \$15,000 of income tax benefit relating to refundable credits for the three and nine months ended September 30, 2013, compared to \$0.1 million during the same period of 2012. The Company's effective tax rate will fluctuate from period to period due to several factors inherent in the nature of the Company's operations and business transactions. The factors that most significantly impact this rate include the variability of licensing transactions in foreign jurisdictions.

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

9. Stock-based Compensation

In the first nine months of 2013, the Board of Directors of the Company approved grants under the Company's Long Term Incentive Plan for an aggregate of 1,144,403 stock options and an aggregate of 958,385 RSUs to certain employees and the directors of the Company. The stock options vest monthly over four years for employees and one year for directors of the Company, and the RSUs vest annually over three years, in equal increments.

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

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The fair value of the stock options granted was estimated based on the following weighted average assumptions for three and nine months ended September 30, 2013 and 2012:

	Three Months Ended September 30, 2013		Nine Months Ended September 30, 2012	
Dividend yield	0 %	0 %	0 %	0 %
Expected volatility	92 %	92 %	92 %	92 %
Risk-free interest rate	1.43 %	0.72 %	0.87 %	1.05 %
Expected term	5.6 years	5.6 years	5.6 years	5.6 years

Stock option activity for the nine months ended September 30, 2013 was as follows:

	Options	Weighted Average Exercise Price Per Share	Weighted Average Remaining Contractual Life (in years)	Aggregate Intrinsic Value (in thousands)
Options outstanding at December 31, 2012	6,788,383	\$ 8.99	7.36	\$ 1,531
Granted	1,144,403	\$ 3.10		
Exercised	(297,149)	\$ 1.75		
Forfeited, expired or cancelled	(129,296)	\$ 17.88		
Options outstanding at September 30, 2013	7,506,341	\$ 8.23	7.01	\$ 8,262
Options exercisable at September 30, 2013	4,817,306	\$ 11.13	6.03	\$ 4,050

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

Unvested RSU activity for the nine months ended September 30, 2013 is summarized below:

	Number of Shares	Weighted- Average Grant-Date Fair Value
Unvested balance at December 31, 2012	1,459,853	\$ 2.75
Granted	958,385	\$ 2.96
Vested	(419,760)	\$ 2.99
Forfeited	(45,434)	\$ 2.29
Unvested balance at September 30, 2013	1,953,044	\$ 2.63

The following table shows total stock-based compensation expense included in the condensed consolidated statements of comprehensive loss for the three and nine months ended September 30, 2013 and 2012 (in thousands):

Three Months Ended September 30, 2013		Nine Months Ended September 30, 2012	

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Research and development	\$474	\$1,304	\$1,904	\$1,984
Selling, general and administrative	753	818	2,042	1,384
Total stock-based compensation expense	\$1,227	\$2,122	\$3,946	\$3,368

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

Forward Looking Statements

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

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

Overview

XOMA discovers and develops innovative antibody-based therapeutics. Our lead drug candidate, gevokizumab, is a potent, fully humanized monoclonal antibody with unique allosteric modulating properties that binds to the inflammatory cytokine interleukin-1 beta ("IL-1 beta"). We believe, by targeting IL-1 beta, gevokizumab has the potential to address the underlying inflammatory causes of a wide range of diseases that have been identified as unmet medical needs.

Together with our development partner, Les Laboratoires Servier ("Servier"), we initiated three Phase 3 clinical trials evaluating gevokizumab for the treatment of non-infectious uveitis ("NIU") involving the intermediate and/or posterior segment of the eye and Behçet's uveitis, a severe subset of NIU. XOMA is responsible for all of the clinical study sites in the United States, and Servier is responsible for all of the clinical study sites outside of the United States. These studies are known as the EYEGUARD™ program, which includes EYEGUARD-A (patients with acute NIU), EYEGUARD-B (patients with Behçet's uveitis), and EYEGUARD-C (patients with NIU controlled with corticosteroids, with or without immunosuppressive medications). As of September 30, 2013, we have over 60 of the targeted 70 clinical sites up and running in the U.S. where we are working to accelerate enrollment, and we are working closely with SERVIER to identify ways to expedite the site activation process outside the United States. We anticipate disclosing the top-line results of the EYEGUARD studies in 2014.

In October 2013, we announced three-month results from our gevokizumab Phase 2 clinical study in patients with erosive osteoarthritis of the hand (“EOA”) who also have C-reactive protein (“CRP”) levels greater than or equal to 2.5 mg/L. The three-month results demonstrated that gevokizumab has a clinical effect on the target patient population. The study will continue on a blinded basis until all patients receive the full six months of treatment. We will review the six-month results along with the three-month results from our gevokizumab Phase 2 clinical EOA study in patients who do not have elevated CRP levels, at which time we will make final decisions regarding a potential Phase 3 program in EOA.

In June 2013, we launched a pilot study in inflammatory pyoderma gangrenosum (“PG”), and in tandem, treated two patients with generalized pustular psoriasis (“GPP”) under compassionate use protocols. PG and GPP are two rare diseases classified as neutrophilic dermatoses. In October 2013, we selected PG as the next indication for Pivotal clinical development based on compelling results from the pilot study. We will request a meeting with the FDA to review the data and discuss the requirements to move gevokizumab into a pivotal Phase 3 program in this indication.

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Two additional studies are being conducted in collaboration with the United States National Institutes of Health (“NIH”). In March 2013, we announced that a gevokizumab study in patients with non-infectious anterior scleritis had opened for enrollment at the National Eye Institute (“NEI”), and in August 2013, we announced a gevokizumab clinical study in patients with inflammatory autoimmune inner ear disease (“AIED”) will be run by the North Shore-Long Island Jewish Health System in collaboration with the National Institute on Deafness and Other Communication Disorders.

Separately, Servier instituted its own active development program for gevokizumab beyond the NIU and Behçet’s uveitis Phase 3 program. In 2012, Servier initiated a gevokizumab Phase 2 study in patients with acute coronary syndrome, a cardiovascular disease. Servier also began testing gevokizumab in a variety of small clinical studies, including polymyositis/dermatomyositis and Schnitzler syndrome. Servier indicated these are the first studies in an extensive multi-indication exploratory program it expects to be conducting.

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

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

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

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

Significant Developments in the First Nine Months of 2013

Gevokizumab

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

In April 2013, the NEI opened a non-infectious, active, anterior scleritis trial for patient enrollment. The open-label single-arm Phase 1/2 study is designed to assess the safety and potential efficacy of gevokizumab in patients experiencing non-infectious, active, anterior scleritis, which is the inflammation of the sclera.

In May 2013, we announced we had initiated a second clinical study in inflammatory osteoarthritis of the hand based upon our findings that patients who met all of the eligibility criteria for our original study were not able to participate due to the requirement C-reactive protein (CRP) levels must be greater than or equal to 2.5 mg/L. This second study has the same design and eligibility requirements with the exception that participants with a CRP level of less than 2.5 mg/L may enroll. The study is capturing the same pain and functional endpoints as the primary study, yet the design does not include radiographic/MRI images of the affected joints.

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In June 2013, we opened enrollment in an open-label pilot study to determine gevokizumab's potential to treat acute inflammatory PG. In October 2013, we announced that we will be requesting a meeting with the FDA to review the data and discuss the requirements to move gevokizumab into a pivotal Phase 3 program in this indication. Our decision is the result of data generated from our open-label pilot study in PG.

In June 2013, Servier launched its own independent proof-of-concept clinical program to evaluate the safety and efficacy of gevokizumab in indications different from ours. The first such studies are in polymyositis/dermatomyositis and Schnitzler syndrome.

In July 2013, we announced the completion of patient enrollment in our Phase 2 proof-of-concept study in EOA.

In August 2013, we announced that a gevokizumab clinical study in patients with AIED will be run by the North Shore-Long Island Jewish Health System in collaboration with the National Institute on Deafness and Other Communication Disorders.

Perindopril Franchise

In July 2013, we transferred U.S. development and commercialization rights to the perindopril franchise to Symplmed. Under the terms of the arrangement, we received a minority equity position in Symplmed and up to double-digit royalties on sales of the first fixed-dose combination containing perindopril arginine and amlodipine besylate, if it is approved by the FDA. We recorded the minority equity position in the other assets line of our condensed consolidated balance sheets. Symplmed, under a sublicense agreement, assumes U.S. marketing responsibilities for ACEON (perindopril erbumine), and we continue to manage and be reimbursed for sales and distribution within its established commercial infrastructure until the ACEON New Drug Application (“NDA”) is transferred to Symplmed. We also continue to record gross ACEON sales in the contracts and other revenue line of our condensed consolidated statements of comprehensive loss until the ACEON NDA is transferred. Following the ACEON NDA transfer, Symplmed will pay us single-digit royalties on sales of ACEON.

Management Addition

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

Financing

In August 2013, we completed an underwritten public offering of 8,736,187 share of our common stock for gross proceeds of \$31.6 million, before deducting underwriting discounts and commissions and estimated offering expenses totaling approximately \$2.2 million.

Results of Operations

Revenues

Total revenues for the three and nine months ended September 30, 2013 and 2012, were as follows (in thousands):

	Three Months Ended September 30,			Nine Months Ended September 30,		
			Increase (Decrease)			Increase (Decrease)
	2013	2012		2013	2012	
License and collaborative fees	\$ 1,574	\$ 1,127	\$ 447	\$ 2,578	\$ 4,665	\$ (2,087)

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Contract and other	4,738	6,124	(1,386)	20,339	21,725	(1,386)
Total revenues	\$6,312	\$7,251	\$ (939)	\$22,917	\$26,390	\$ (3,473)

License and Collaborative Fees

License and collaborative fee revenue includes fees and milestone payments related to the out-licensing of our products and technologies. The increase in license and collaborative fee revenue for the three months ended September 30, 2013, as compared to the same period of 2012, was due primarily to a \$0.6 million increase in milestone payments. The decrease in license and collaborative fee revenue for the nine months ended September 30, 2013, as compared to the same period of 2012, was due primarily to a \$2.2 million decrease in licensing fees from two licensing contracts, partially offset by a \$0.2 million increase in milestone payments. The generation of future revenue related to license fees and other collaborative arrangements is dependent on our ability to attract new licensees to our antibody technologies and new collaboration partners. We expect license and collaboration fee revenue in the remainder of 2013 to be comparable to 2012 levels.

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Contract and Other Revenue

Contract and other revenues include agreements where we provide contracted research and development services to our contract and collaboration partners, including Servier and NIAID. The following table shows the activity in contract and other revenue for the three and nine months ended September 30, 2013 and 2012 (in thousands):

	Three Months Ended September 30,			Nine Months Ended September 30,		
	2013	2012	Increase (Decrease)	2013	2012	Increase (Decrease)
Servier	\$1,399	\$3,461	\$ (2,062)	\$11,882	\$10,715	\$ 1,167
NIAID	2,614	2,074	540	6,770	9,106	(2,336)
Other	725	589	136	1,687	1,904	(217)
Total contract and other	\$4,738	\$6,124	\$ (1,386)	\$20,339	\$21,725	\$ (1,386)

The decrease in revenue from Servier for the three months ended September 30, 2013, as compared to the same period of 2012, is due primarily to our collaboration with Servier meeting the initial \$50 million cap of fully reimbursable NIU costs during the third quarter of 2013. Servier and XOMA will each pay 50% of remaining NIU clinical development and CMC costs. The increase in revenue from Servier for the nine months ended September 30, 2013, as compared to the same period of 2012, is due primarily to an increase in reimbursable clinical development activity with Servier. This increase is partially offset by a decrease in NIAID revenue due primarily to decreased activity under NIAID Contract No. HHSN272200800028C (“NIAID 3”) and the recognition of \$2.0 million in revenue during the first quarter of 2012 related to an adjustment to previously-reported revenue from NIAID resulting from an audit by NIAID’s contracting office. This revenue, which was previously deferred, was recognized upon the completion of negotiations with and approval by the NIH in March 2012.

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

Research and Development Expenses

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

Research and development expenses were \$18.2 million and \$51.9 million for the three and nine months ended September 30, 2013, respectively, compared with \$18.4 million and \$52.7 million, respectively, for the same periods of 2012. The decrease of \$0.2 million for the three months ended September 30, 2013, as compared to the same period in 2012, was due primarily to the absence of fixed dose combination (“FDC”) clinical trial costs in Q3 2013, a decrease in internal facility costs as a result of the 2012 streamlining of operations, and a decrease in employee compensation costs, partially offset by higher internal proprietary project costs and professional service fees. The decrease of \$0.8 million for the nine months ended September 30, 2013, as compared to the same period in 2012, was due primarily to decreases in FDC clinical trial costs, and internal facility costs as a result of the 2012 streamlining of operations, partially offset by increases in employee compensation costs and higher external manufacturing activity and internal proprietary project costs.

Salaries and related personnel costs are a significant component of research and development expenses. We recorded \$6.4 million and \$20.6 million in research and development salaries and employee-related expenses for the three and nine months ended September 30, 2013, respectively, as compared with \$6.8 million and \$19.8 million for the same periods of 2012. The decrease of \$0.4 million for the three months ended September 30, 2013, as compared to the same period of 2012, was due primarily to a \$0.8 million decrease in stock-based compensation, partially offset by a \$0.4 million increase in salaries and benefits as a result of an increase in headcount. The increase of \$0.8 million for the nine months ended September 30, 2013, as compared to the same period of 2012, is due primarily to a \$0.9 million increase in salaries and benefits, the result of an increase in headcount.

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

	Three Months Ended September 30, 2013		Nine Months Ended September 30, 2013	
	2013	2012	2013	2012
Earlier stage programs	\$10,310	\$8,954	\$28,429	\$27,066
Later stage programs	7,888	9,455	23,476	25,636
Total	\$18,198	\$18,409	\$51,905	\$52,702

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

	Three Months Ended September 30, 2013		Nine Months Ended September 30, 2013	
	2013	2012	2013	2012
Internal projects	\$10,915	\$8,426	\$30,892	\$23,860
Collaborative and contract arrangements	7,283	9,983	21,013	28,842
Total	\$18,198	\$18,409	\$51,905	\$52,702

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

We expect our research and development spending in the remainder of 2013 to increase compared to 2012 levels due primarily to our ongoing global Phase 3 clinical program for gevokizumab for the NIU indications, under our license and collaboration agreement with Servier, and our ongoing Phase 2 proof-of-concept program.

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

Selling, General and Administrative Expenses

Selling, general and administrative expenses include salaries and related personnel costs, facilities costs and professional fees. Selling, general and administrative expenses were \$5.2 million and \$13.4 million for the three and nine months ended September 30, 2013, respectively, compared with \$4.7 million and \$12.9 million for the same periods of 2012. The \$0.5 million increase for the three months ended September 30, 2013, as compared to the same period of 2012, was due primarily to a \$1.1 million increase in professional service fees, partially offset by a \$0.4 million decrease in severance expense. The \$0.5 million increase for the nine months ended September 30, 2013, as compared to the same period of 2012, was due primarily to a \$0.7 million increase in stock-based compensation, partially offset by a \$0.4 million decrease in severance expense.

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Streamlining and Restructuring Charges

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

In connection with the streamlining of operations, we incurred restructuring charges in the first nine months of 2012 of \$2.0 million related to severance, other termination benefits and outplacement services, \$2.2 million related to the impairment and accelerated depreciation of various assets and leasehold improvements, and \$0.7 million related to moving and other facility charges. In the first nine months of 2013, we have incurred \$0.2 million in restructuring charges related to facility costs and do not expect to incur additional significant restructuring charges during the remainder of 2013 related to these streamlining activities.

Other Income (Expense)

Interest Expense

Interest expense and amortization of debt issuance costs and discounts are shown below for the three and nine months ended September 30, 2013 and 2012 (in thousands):

	Three Months Ended September 30,			Nine Months Ended September 30,		
	2013	2012	Increase (Decrease)	2013	2012	Increase (Decrease)
Interest expense						
Servier loan	\$547	\$558	\$ (11)	\$1,600	\$1,583	\$ 17
GECC term loan	508	475	33	1,584	1,298	286
Novartis note	90	99	(9)	272	298	(26)
Other	14	12	2	39	32	7
Total interest expense	\$1,159	\$1,144	\$ 15	\$3,495	\$3,211	\$ 284

The increase in interest expense of \$0.3 million for the nine months ended September 30, 2013, as compared to the same period of 2012 was due primarily to an increase in the principal of the GECC term loan, which was amended in September 2012.

Other Expense

Other expense primarily consisted of unrealized (losses) gains. The following table shows the activity in other expense for the three and nine months ended September 30, 2013 and 2012 (in thousands):

	Three Months Ended September 30,			Nine Months Ended September 30,		
	2013	2012	Increase (Decrease)	2013	2012	Increase (Decrease)
Other expense:						
Unrealized foreign exchange (loss) gain ⁽¹⁾	\$(322)	\$(318)	\$ (4)	\$(57)	\$96	\$ (153)

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Unrealized gain (loss) on foreign exchange options	7	(110)	117	(184)	(721)	537
Other	183	8	175	333	83	250
Total other expense	\$(132)	\$(420)	\$ 288	\$92	\$(542)	\$ 634

(1) Unrealized foreign exchange gain (loss) for the three and nine months ended September 30, 2013 and 2012 primarily relates to the re-measurement of the €15 million Servier loan.

Revaluation of Contingent Warrant Liabilities

In March 2012, in connection with an underwritten offering, we issued five-year warrants to purchase 14,834,577 shares of XOMA's common stock at an exercise price of \$1.76 per share. These warrants contain provisions that are contingent on the occurrence of a change in control, which would conditionally obligate us to repurchase the warrants for cash in an amount equal to their fair value using the Black-Scholes Option Pricing Model (the "Black-Scholes Model") on the date of such change in control. Due to these provisions, we are required to account for the warrants issued in March 2012 as a liability at fair value. In addition, the estimated liability related to the warrants is required to be revalued at each reporting period until the earlier of the exercise of the warrants, at which time the liability will be reclassified to stockholders' equity, or expiration of the warrants. At December 31, 2012, the fair value of the warrant liability was estimated to be \$15.0 million using the Black-Scholes Model. We revalued the warrant liability at September 30, 2013 using the Black-Scholes Model and recorded the \$25.7 million increase in the fair value as a loss in the revaluation of contingent warrant liabilities line of our condensed consolidated statements of comprehensive loss. We also reclassified \$1.6 million from contingent warrant liabilities to equity on our condensed consolidated balance sheets due to the exercise of warrants. As of September 30, 2013, 13,673,183 of these warrants were outstanding and had a fair value of \$39.1 million. This increase in liability is due primarily to the increase in the market value of our common stock at September 30, 2013 compared to December 31, 2012.

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In February 2010, in connection with an underwritten offering, we issued five-year warrants to purchase 1,260,000 shares of XOMA's common stock at an exercise price of \$10.50 per share. In June 2009, we issued warrants to certain institutional investors as part of a registered direct offering. These warrants represent the right to acquire an aggregate of up to 347,826 shares of XOMA's common stock over a five year period beginning December 11, 2009, at an exercise price of \$19.50 per share. These warrants contain provisions that are contingent on the occurrence of a change in control, which would conditionally obligate us to repurchase the warrants for cash in an amount equal to their fair value using the Black-Scholes Model on the date of such change in control. Due to these provisions, we are required to account for the warrants issued in February 2010 and June 2009 as liabilities at fair value. As of September 30, 2013, all of these warrants were outstanding and had an aggregate fair value of approximately \$0.1 million.

The following table provides a summary of the changes in fair value of contingent warrant liabilities for the nine months ended September 30, 2013 (in thousands):

	September 30, 2013
Contingent warrant liabilities	
Balance at December 31, 2012	15,001
Reclassification of contingent warrant liability to equity upon exercise of warrants	(1,585)
Net increase in fair value of contingent warrant liabilities upon revaluation	25,746
Balance at September 30, 2013	39,162

Income Taxes

We recognized \$15,000 of income tax benefit relating to refundable credits for the three and nine months ended September 30, 2013, compared to \$0.1 million during the same period of 2012.

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

We do not expect the unrecognized tax benefits to change significantly over the next twelve months. We will recognize interest and penalties accrued on any unrecognized tax benefits as a component of income tax expense. As of September 30, 2013, we have not accrued interest or penalties related to uncertain tax positions.

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Liquidity and Capital Resources

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

	September 30, 2013	December 31, 2012	Change
Cash and cash equivalents	\$ 73,988	\$ 45,345	\$28,643
Short-term investments	\$ -	\$ 39,987	\$(39,987)
Working Capital	\$ 58,779	\$ 72,004	\$(13,225)

	Nine Months Ended September 30,		
	2013	2012	Change
Net cash used in operating activities	\$(38,602)	\$(29,432)	\$(9,170)
Net cash provided by (used in) investing activities	38,931	(18,633)	57,564
Net cash provided by financing activities	28,314	41,920	(13,606)
Net increase in cash, cash equivalents and short-term investments	\$28,643	\$(6,145)	\$34,788

Working Capital

The decrease in working capital was due primarily to an \$11.3 million decrease in cash, cash equivalents, and short-term investments and a \$2.5 million reclassification of principal and accrued interest on our interest bearing obligations from long-term to short-term.

Cash Used in Operating Activities

Net cash used in operating activities was \$38.6 million for the nine months ended September 30, 2013, compared with \$29.4 million for the same period in 2012. Net cash used in operating activities was \$9.2 million higher in the first nine months of 2013 due primarily to an increase in external manufacturing costs and spending on internal proprietary projects.

Cash Provided by (Used in) Investing Activities

Net cash provided by investing activities was \$38.9 million for the nine months ended September 30, 2013, compared with net cash used in investing activities of \$18.6 million for the same period of 2012. The \$57.6 million change in cash provided by investing activities was due primarily to the maturity of \$40.0 million in short-term investments during the first nine months of 2013 and the purchase of \$17.0 million in short-term investments during the first nine months of 2012.

Cash Provided by Financing Activities

Net cash provided by financing activities was \$28.3 million for the nine months ended September 30, 2013, compared with \$41.9 million for the same period of 2012. Cash provided by financing activities in the first nine months of 2013 related to net proceeds received from the issuance of common stock of \$29.4 million in the August 2013 public offering, \$0.6 million of net proceeds received from employee stock purchases, and \$0.4 million of net proceeds from the exercise of warrants. These net proceeds were partially offset by \$2.1 million of principal payments on our loan with GECC. Cash provided by financing activities in the first nine months of 2012 related to net proceeds received from the issuance of common stock and warrants of \$36.2 million in the March 2012 public offering, net proceeds of

\$3.2 million received from the issuance of common stock under the 2011 ATM Agreement, and net loan proceeds of \$4.4 million received from GECC, partially offset by \$2.1 million of principal payments on our loan with GECC.

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

* * *

We have incurred significant operating losses and negative cash flows from operations since our inception. At September 30, 2013, we had cash and cash equivalents of \$74.0 million. During the remainder of 2013, we expect to continue using our cash, cash equivalents and short-term investments to fund ongoing operations. Additional licensing, antibody discovery and development collaboration agreements, government funding and financing arrangements may positively impact our cash balances. Based on our cash reserves and anticipated spending levels, revenue from collaborations including the gevokizumab license and collaboration agreement with Servier, funding from the loan agreement with GECC, our March 2012, October 2012, and August 2013 public offerings, biodefense contracts and licensing transactions and other sources of funding that we believe to be available, we estimate we have sufficient cash resources to meet our anticipated net cash needs into 2015. Any significant revenue shortfalls, increases in planned spending on development programs or more rapid progress of development programs than anticipated, as well as the unavailability of anticipated sources of funding, could shorten this period. If adequate funds are not available, we will be required to delay, reduce the scope of, or eliminate one or more of our product development programs and further reduce personnel-related costs. Progress or setbacks by potentially competing products may also affect our ability to raise new funding on acceptable terms.

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Critical Accounting Estimates

Critical accounting estimates are those that require significant judgment and/or estimates by management at the time that the financial statements are prepared such that materially different results might have been reported if other assumptions had been made. We consider certain accounting policies including, but not limited to, revenue recognition, research and development expense, long-lived assets, contingent warrant liabilities, derivative instruments and stock-based compensation to be critical policies. There have been no significant changes in our critical accounting estimates during the nine months ended September 30, 2013, as compared with those previously disclosed in our Annual Report on Form 10-K for the fiscal year ended December 31, 2012, filed with the SEC on March 12, 2013.

ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

Interest Rate Risk

We are exposed to market risks in the ordinary course of our business. These risks primarily include risk related to interest rate sensitivities. Our market risks related to interest rate sensitivities at September 30, 2013, have not changed materially from those discussed in Item 7A of our Form 10-K for the year ended December 31, 2012 filed with the SEC.

Foreign Currency Risk

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

Our loan from Servier was fully funded in January 2011, with the proceeds converting to approximately \$19.5 million using the January 13, 2011 Euro to U.S. dollar exchange rate of 1.3020. At September 30, 2013, the €15.0 million outstanding principal balance under the Servier Loan Agreement would have equaled approximately \$20.3 million using the September 30, 2013 Euro to USD exchange rate of 1.3520. In May 2011, in order to manage our foreign currency exposure relating to our principal and interest payments on our loan from Servier, we entered into two foreign exchange option contracts to buy €1.5 million and €15.0 million in January 2014 and January 2016, respectively. Upfront premiums paid on these foreign exchange option contracts totaled \$1.5 million and they had an aggregate fair value of \$0.3 million at September 30, 2013. Our use of derivative financial instruments represents risk management; we do not enter into derivative financial contracts for trading purposes.

ITEM 4. CONTROLS AND PROCEDURES

Evaluation of Controls and Procedures

Under the supervision and with the participation of our management, including our Chief Executive Officer (our principal executive officer) and our Vice President, Finance, Chief Financial Officer and Secretary (our principal financial and principal accounting officer), we conducted an evaluation of our disclosure controls and procedures, as such term is defined under Rule 13a-15(e) promulgated under the Securities Exchange Act of 1934, as amended, as of the end of the period covered by this report. Based on this evaluation, our Chief Executive Officer and our Vice

President, Finance, Chief Financial Officer and Secretary concluded that our disclosure controls and procedures are effective as of the end of the period covered by this report in timely alerting them to material information relating to us and our consolidated subsidiaries required to be included in our periodic SEC filings.

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Changes in Internal Control

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

PART II – OTHER INFORMATION

ITEM 1. LEGAL PROCEEDINGS

None.

ITEM 1A. RISK FACTORS

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

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

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

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

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

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

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

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Based on our cash and cash equivalents of \$74.0 million at September 30, 2013, anticipated spending levels, anticipated cash inflows from collaborations, biodefense contracts and licensing transactions, funding availability including under our loan agreements, the proceeds from our recent public offering and other sources of funding that will we believe to be available, we believe we have sufficient cash resources to meet our anticipated net cash needs into 2015. Any significant revenue shortfalls, increases in planned spending on development programs, more rapid progress of development programs than anticipated, or the initiation of new clinical trials, as well as the unavailability of anticipated sources of funding, could shorten this period or otherwise have a material adverse impact on our ability to finance our continued operations. If adequate funds are not available, we will be required to delay, reduce the scope of, or eliminate one or more of our product development programs and further reduce personnel-related costs. Progress or setbacks by potentially competing products also may affect our ability to raise new funding on acceptable terms. As a result, we do not know when or whether:

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

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

We have experienced significant losses, and as of September 30, 2013, we had an accumulated deficit of \$1,029 million.

For the three and nine months ended September 30, 2013, we had net losses of approximately \$29.6 million, or \$0.34 per share of common stock (basic and diluted) and \$71.8 million, or \$0.85 per share of common stock (basic and diluted), respectively. For the three and nine months ended September 30, 2012, we had net losses of approximately \$26.9 million, or \$0.39 per share of common stock (basic and diluted) and \$73.4 million, or \$1.22 per share of common stock (basic and diluted), respectively.

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

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

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

- In December 2010, we entered into a license and collaboration agreement with Servier, to jointly develop and commercialize gevokizumab in multiple indications. Under the terms of the agreement, Servier has worldwide rights to cardiovascular disease and diabetes indications and rights outside the United States and Japan to all other indications, including Behçet's uveitis and other inflammatory and oncology indications. In late 2011, we announced Servier agreed to include the NIU Phase 3 trials under the terms of the collaboration agreement for Behçet's uveitis. We retain development and commercialization rights for NIU and other inflammatory disease and oncology indications in the United States and Japan and have an option to reacquire rights to cardiovascular disease and diabetes indications from Servier in these territories. Should we exercise this option, we will be required to pay an option fee to Servier and partially reimburse a specified portion of Servier's incurred development expenses. The

agreement contains mutual customary termination rights relating to matters such as material breach by either party. Servier may terminate for safety issues, and we may terminate the agreement, with respect to a particular country or the European Patent Organization (“EPO”) member states, for any challenge to our patent rights in that country or any EPO member state, respectively, by Servier. Servier also has a unilateral right to terminate the agreement for the European Union (“EU”) or for non-EU countries, on a country-by-country basis, or in its entirety, in each case with six months’ notice.

In December 2010, we entered into a loan agreement with Servier (the “Servier Loan Agreement”), which provides for an advance of up to €15.0 million and was funded fully in January 2011 with the proceeds converting to approximately \$19.5 million at the January 13, 2011, Euro-to-U.S.-dollar exchange rate of 1.3020. This loan is secured by an interest in our intellectual property rights to all gevokizumab indications worldwide, excluding the United States and Japan. The loan has a final maturity date in 2016; however, after a specified period prior to final maturity, the loan is required to be repaid (1) at Servier’s option, by applying up to a significant percentage of any milestone or royalty payments owed by Servier under our collaboration agreement and (2) using a significant percentage of any upfront, milestone or royalty payments we receive from any third-party collaboration or development partner for rights to gevokizumab in the United States and/or Japan. In addition, the loan becomes immediately due and payable upon certain customary events of default. At September 30, 2013, the €15.0 million outstanding principal balance under this Servier Loan Agreement would have equaled approximately \$20.3 million using the September 30, 2013 Euro-to-U.S.-dollar exchange rate of 1.352.

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

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

Drug development has inherent risk, and we are required to demonstrate through adequate and well-controlled clinical trials that our product candidates are effective, with a favorable benefit-risk profile for use in their target profiles before we can seek regulatory approvals for their commercial use. It is possible we may never receive regulatory approval for any of our product candidates. Even if a product candidate receives regulatory approval, the resulting product may not gain market acceptance among physicians, patients, healthcare payors and the medical community.

In March 2011, we announced our 421-patient Phase 2b trial of gevokizumab in Type 2 diabetes did not achieve the primary endpoint of reduction in hemoglobin A1c (“HbA1c”) after six monthly treatments with gevokizumab compared to placebo. In June 2011, we announced top-line trial results from our six-month 74-patient Phase 2a trial of gevokizumab in Type 2 diabetes, and there were no differences in glycemic control between the drug and placebo groups as measured by HbA1c levels.

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

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

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

insofar as we might desire to use U.S. Dollars to make contract payments denominated in the foreign currency where the trial is being conducted.

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

Administering any of our products or potential products may produce undesirable side effects, also known as adverse effects. Toxicities and adverse effects that we have observed in preclinical studies for some compounds in a particular research and development program may occur in preclinical studies or clinical trials of other compounds from the same program. Such toxicities or adverse effects could delay or prevent the filing of an IND (or a foreign equivalent) with respect to such products or potential products or cause us to cease clinical trials with respect to any drug candidate. In clinical trials, administering any of our products or product candidates to humans may produce adverse effects. These adverse effects could interrupt, delay or halt clinical trials of our products and product candidates and could result in the FDA or other regulatory authorities denying approval of our products or product candidates for any or all targeted indications. The FDA, other regulatory authorities, our collaboration or development partners or we may suspend or terminate clinical trials at any time. Even if one or more of our product candidates were approved for sale, the occurrence of even a limited number of toxicities or adverse effects when used in large populations may cause the FDA to impose restrictions on, or stop, the further marketing of such drugs. Indications of potential adverse effects or toxicities that may occur in clinical trials and that we believe are not significant during the course of such clinical trials may actually turn out later to constitute serious adverse effects or toxicities when a drug has been used in large populations or for extended periods of time. Any failure or significant delay in completing preclinical studies or clinical trials for our product candidates, or in receiving and maintaining regulatory approval for the sale of any drugs resulting from our product candidates, may severely harm our reputation and business.

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

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

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

In the United States, the FDA regulates pharmaceutical products under the Federal Food, Drug, and Cosmetic Act and other laws, including, in the case of biologics, the Public Health Service Act. At the present time, we believe many of our product candidates (including gevokizumab, XMetA, XMetD, XMetS and XOMA 3AB) will be regulated by the FDA as biologics and some of our product candidates will be regulated by the FDA as drugs. Initiation of clinical

trials requires approval by health authorities. Clinical trials involve the administration of the investigational new drug to healthy volunteers or to patients under the supervision of a qualified principal investigator. Clinical trials must be conducted in accordance with FDA and International Conference on Harmonisation of Technical Requirements for Registration of Pharmaceuticals for Human Use Good Clinical Practices and the European Clinical Trials Directive under protocols that detail the objectives of the study, the parameters to be used to monitor safety and the efficacy criteria to be evaluated. Other national, foreign and local regulations also may apply. The developer of the drug must provide information relating to the characterization and controls of the product before administration to the patients participating in the clinical trials. This requires developing approved assays of the product to test before administration to the patient and during the conduct of the trial. In addition, developers of pharmaceutical products must provide periodic data regarding clinical trials to the FDA and other health authorities, and these health authorities may issue a clinical hold upon a trial if they do not believe, or cannot confirm, that the trial can be conducted without unreasonable risk to the trial participants. We cannot assure you that U.S. and foreign health authorities will not issue a clinical hold with respect to any of our clinical trials in the future.

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

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

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

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

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

Several third parties provide services in connection with our preclinical and clinical development programs, including in vitro and in vivo studies, assay and reagent development, immunohistochemistry, toxicology, pharmacokinetics, clinical trial support, manufacturing and other outsourced activities. If these service providers do not adequately perform the services for which we have contracted or cease to continue operations and we are not able to find a replacement provider quickly or we lose information or items associated with our product candidates, our development programs may be delayed.

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

The FDA has awarded orphan drug status to gevokizumab for the treatment of non-infectious, intermediate, posterior or pan uveitis, and chronic non-infectious anterior uveitis and Behçet's uveitis. Under the Orphan Drug Act, the first company to receive FDA approval for gevokizumab for the designated orphan drug indication will obtain seven years of marketing exclusivity, during which time the FDA may not approve another company's application for gevokizumab for the same orphan indication. Even though we have obtained orphan drug designation for certain indications for gevokizumab and even if we obtain orphan drug designation for our future product candidates or other indications, due to the uncertainties associated with developing pharmaceutical products, we may not be the first to obtain marketing approval for any particular orphan indication, or we may not obtain approval for an indication for which we have obtained orphan drug designation. Further, even if we obtain orphan drug exclusivity for a product, that exclusivity may not protect the product effectively from competition because different drugs can be approved for the same condition. Even after an orphan drug is approved, the FDA can subsequently approve the same drug for the same condition if the FDA concludes that the later drug is safer, more effective or makes a major contribution to patient care. Orphan drug designation neither shortens the development time or regulatory review time of a drug, nor gives the drug any advantage in the regulatory review or approval process.

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

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

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

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

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

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

We are authorized to issue, without stockholder approval, 1,000,000 shares of preferred stock, of which none were issued and outstanding as of November 5, 2013, which may give other stockholders dividend, conversion, voting, and

liquidation rights, among other rights, which may be superior to the rights of holders of our common stock. In April 2011, the 2,959 Series B convertible preference shares previously issued to Genentech were converted by Genentech into 254,560 shares of common stock. In addition, we are authorized to issue, generally without stockholder approval, up to 138,666,666 shares of common stock, of which 93,077,887 were issued and outstanding as of November 5, 2013. If we issue additional equity securities, the price of our common stock may be materially and adversely affected.

On February 4, 2011, we entered into an At Market Issuance Sales Agreement (the “2011 ATM Agreement”) with McNicoll, Lewis & Vlak LLC (now known as MLV & Co. LLC, “MLV”), under which we may sell shares of our common stock from time to time through MLV, as our agent for the offer and sale of the shares, in an aggregate amount not to exceed the amount that can be sold under our Registration Statement on Form S-3 (File No. 333-172197) filed with the SEC on February 11, 2011, and amended on March 10, 2011, June 3, 2011, and January 3, 2012, which was most recently declared effective by the SEC on January 17, 2012. MLV may sell the shares by any method permitted by law deemed to be an “at the market” offering as defined in Rule 415 of the Securities Act, including without limitation sales made directly on The NASDAQ Global Market, on any other existing trading market for our common stock or to or through a market maker. MLV also may sell the shares in privately negotiated transactions, subject to our prior approval. From the inception of the 2011 ATM Agreement through November 5, 2013, we sold a total of 7,572,327 shares of common stock under this agreement for aggregate gross proceeds of \$14.6 million.

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On March 9, 2012, we completed an underwritten public offering of 29,669,154 shares of our common stock, and accompanying warrants to purchase one half of a share of common stock for each share purchased, at a public offering price of \$1.32 per share. Total gross proceeds from the offering were approximately \$39.2 million, before deducting underwriting discounts and commissions and estimated offering expenses totaling approximately \$3.0 million. The warrants, which represent the right to acquire an aggregate of up to 14,834,577 shares of common stock, are exercisable immediately and have a five-year term and an exercise price of \$1.76 per share. As of November 5, 2013, 13,313,335 of these warrants were outstanding.

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

On August 23, 2013, we completed an underwritten public offering of 8,736,187 shares of our common stock, including 1,139,502 shares of our common stock that were issued upon the exercise of the underwriters' 30-day over-allotment option to purchase additional shares, at a public offering price of \$3.62 per share. Total gross proceeds from the offering were approximately \$31.6 million, before deducting underwriting discounts and commissions and estimated offering expenses totaling approximately \$2.2 million.

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

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

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

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

There can be no assurance the market price of our common stock will not decline below its present market price or there will be an active trading market for our common stock. The market prices of biotechnology companies have been and are likely to continue to be highly volatile. Fluctuations in our operating results and general market conditions for biotechnology stocks could have a significant impact on the volatility of our common stock price. We have experienced significant volatility in the price of our common stock. From January 1, 2013, through November 5, 2013, the share price of our common stock has ranged from a high of \$5.54 to a low of \$2.43. Factors contributing to such volatility include, but are not limited to:

- results of preclinical studies and clinical trials;
- the pace of enrollment in our clinical trials
- information relating to the safety or efficacy of products or product candidates;
 - developments regarding regulatory filings;
- announcements of new collaborations;
- failure to enter into collaborations;

·developments in existing collaborations;

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- our funding requirements and the terms of our financing arrangements;
- technological innovations or new indications for our therapeutic products and product candidates;
- introduction of new products or technologies by us or our competitors;
- sales and estimated or forecasted sales of products for which we receive royalties, if any;
- government regulations;
 - developments in patent or other proprietary rights;
- the number of shares issued and outstanding;
- the number of shares trading on an average trading day;
- announcements regarding other participants in the biotechnology and pharmaceutical industries; and
 - market speculation regarding any of the foregoing.

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

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

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

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

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

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

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

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

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

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

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

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

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

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

Even approved and marketed products are subject to risks relating to changes in the market for such products. Introduction or increased availability of generic versions of products can alter the market acceptance of branded products, such as ACEON. In addition, unforeseen safety issues may arise at any time, regardless of the length of time a product has been on the market.

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

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

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

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

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

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

In December 2011, we entered into a loan agreement with GECC (the "GECC Loan Agreement"), under which GECC agreed to make a term loan in an aggregate principal amount of \$10 million to XOMA (US) LLC, our wholly owned subsidiary, and upon execution of the GECC Loan Agreement, GECC funded the term loan. The term loan is guaranteed by us and our two other principal subsidiaries, XOMA Ireland Limited and XOMA Technology Ltd. As security for our obligations under the GECC Loan Agreement, we, XOMA (US) LLC, XOMA Ireland Limited and XOMA Technology Ltd. each granted a security interest pursuant to a guaranty, pledge and security agreement in substantially all of our existing and after-acquired assets, excluding our intellectual property assets (such as those relating to our gevokizumab and anti-botulism products). We were required to repay the principal amount of the Term Loan over a period of 42 installments of principal and accrued interest, but we amended the GECC Loan Agreement on September 27, 2012, as described below. The GECC Loan Agreement contains customary representations and warranties and customary affirmative and negative covenants, including restrictions on the ability to incur indebtedness, grant liens, make investments, dispose of assets, enter into transactions with affiliates and amend existing

material agreements, in each case subject to various exceptions. In addition, the GECC Loan Agreement contains customary events of default that entitle GECC to cause any or all of the indebtedness under the GECC Loan Agreement to become immediately due and payable. The events of default include any event of default under a material agreement or certain other indebtedness. We may prepay the term loan in full voluntarily, but not in part, and any voluntary and certain mandatory prepayments are subject to a prepayment premium of 3% in the first year of the loan, 2% in the second year and 1% thereafter, with certain exceptions. We also will be required to pay the final payment fee in connection with any voluntary or mandatory prepayment. Pursuant to the GECC Loan Agreement, we issued to GECC unregistered stock purchase warrants, which entitle GECC to purchase up to an aggregate of 263,158 unregistered shares of XOMA common stock at an exercise price equal to \$1.14 per share, are exercisable immediately and expire on December 30, 2016.

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

We have licensed our bacterial cell expression technology, an enabling technology used to discover and screen, as well as develop and manufacture, recombinant antibodies and other proteins for commercial purposes, to over 60 companies. As of November 5, 2013, we were aware of two antibody products manufactured using this technology that have received FDA approval, Genentech's LUCENTIS® (ranibizumab injection) for treatment of neovascular wet age-related macular degeneration and UCB's CIMZIA® (certolizumab pegol) for treatment of Crohn's disease and rheumatoid arthritis. In the third quarter of 2009, we sold our LUCENTIS royalty interest to Genentech. In the third quarter of 2010, we sold our CIMZIA royalty interest.

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

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

We do not know whether we, our collaborators or licensees will successfully develop and market any of the products that are or may become the subject of any of our collaboration or licensing arrangements. In some cases these arrangements provide for funding solely by our collaborators or licensees, and in other cases, all of the funding for certain projects and a significant portion of the funding for other projects is to be provided by our collaborator or licensee, and we provide the balance of the funding. Even when we have a collaborative relationship, other circumstances may prevent it from resulting in successful development of marketable products. In addition, third-party arrangements such as ours also increase uncertainties in the related decision-making processes and resulting progress under the arrangements, as we and our collaborators or licensees may reach different conclusions, or support different paths forward, based on the same information, particularly when large amounts of technical data are involved. Furthermore, our contracts with NIAID contain numerous standard terms and conditions provided for in

the applicable Federal acquisition regulations and customary in many government contracts, some of which could allow the U.S. government to exercise certain rights under the technology developed under these contracts. Uncertainty exists as to whether we will be able to comply with these terms and conditions in a timely manner, if at all. In addition, we are uncertain as to the extent of NIAID's demands and the flexibility that will be granted to us in meeting those demands.

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

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

Developments by others may render our products, product candidates, or technologies obsolete or uncompetitive.

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

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

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

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

Gevokizumab

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

- Novartis markets and is developing ILARIS® (canakinumab, ACZ885), a fully human monoclonal antibody that selectively binds to and neutralizes IL-1 beta. Since 2009, canakinumab has been approved in over 50 countries for the treatment of children and adults suffering from Cryopyrin-Associated Periodic Syndrome ("CAPS"). Novartis has filed for regulatory approval of canakinumab in the United States and Europe for the treatment of acute attacks in gouty arthritis. On March 1, 2013, Novartis announced that they received EU approval for Ilaris in patients suffering acute gouty arthritis attacks which cannot gain relief from current treatments. It is administered as a single 150 mg subcutaneous injection. In May 2013, Novartis received FDA approval, and in September 2013 Novartis received EU approval, to treat active systemic juvenile idiopathic arthritis. Novartis also is pursuing other diseases in which IL-1

beta may play a prominent role, such as systemic secondary prevention of cardiovascular events.

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

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In 2008, Swedish Orphan Biovitrum obtained from Amgen the global exclusive rights to Kineret® (anakinra) for rheumatoid arthritis as currently indicated in its label. In November 2009, the agreement regarding Swedish Orphan Biovitrum's Kineret license was expanded to include certain orphan indications. Kineret is an IL-1 receptor antagonist (IL-1ra) that has been evaluated in multiple IL-1-mediated diseases, including indications we are considering for gevokizumab. In addition to other on-going studies, a proof-of-concept clinical trial in the United Kingdom investigating Kineret in patients with a certain type of myocardial infarction, or heart attack, has been completed. In August 2010, Biovitrum announced the FDA had granted orphan drug designation to Kineret for the treatment of CAPS, and in January 2013 they obtained FDA approval for NOMID, a severe form of CAPS. Shanghai CP Guojian Pharmaceutical is developing an injectable formulation of recombinant human IL-1Ra, presumed to be a follow-on biologic version of anakinra, for the potential treatment of rheumatoid arthritis. In February 2010, an NDA was filed with the SFDA; in January 2012, supplemental materials were required by the SFDA to conclude the review.

In February 2008, Regeneron Pharmaceuticals, Inc. ("Regeneron"), announced it had received marketing approval from the FDA for ARCALYST® (rilonacept) injection for subcutaneous use, an interleukin-1 blocker or IL-1 Trap, for the treatment of CAPS, including Familial Cold Auto-inflammatory Syndrome and Muckle-Wells Syndrome in adults and children 12 and older. In September 2009, Regeneron announced rilonacept was approved in the EU for CAPS, but by February 2013, the company had withdrawn the approved application for CAPS in the EU. In June 2010 and February 2011, Regeneron announced positive results of two Phase 3 clinical trials of rilonacept in gout. In November 2011, Regeneron announced the FDA had accepted for review Regeneron's supplemental BLA for ARCALYST for the prevention and treatment of gout. However, following the FDA's issuance of a Complete Response Letter, in October 2012 Regeneron announced it had discontinued development of the drug for gout.

AbbVie is developing ABT-981, a dual variable domain immunoglobulin (DVD-Ig) that incorporates anti-IL-1 alpha and anti-IL-1 beta antibodies, for the potential treatment of osteoarthritis. By January 2012, the drug had entered phase I development.

AbbVie is developing ABT-981, a dual variable domain immunoglobulin (DVD-Ig) that incorporates anti-IL-1 alpha and anti-IL-1 beta antibodies, for the potential treatment of osteoarthritis. By January 2012, the drug had entered phase I development.

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

In June 2009, Cytos Biotechnology AG announced the initiation of an ascending dose Phase 1/2a study of CYT013-IL1bQb, a therapeutic vaccine targeting IL-1 beta, in Type 2 diabetes. In 2010, this study was extended to include two additional groups of patients. However, in August 2011, the company put development on hold in order to reduce costs.

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

XOMA 3AB

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

Cangene Corporation has a contract with the U.S. Department of Health & Human Services, expected to be worth \$423.0 million, to manufacture and supply an equine heptavalent botulism anti-toxin. In March 2013, the product was approved by the FDA.

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

Patricia K. Vincent

2006

450,000

1,639,333

8,836

311,669

195,422

46,322

2,651,582

President and Chief
Executive Officer of Public Service Company of Colorado (PSCo)

Gary R. Johnson

2006

410,000

1,470,741

272,657

216,418

152,026

2,521,842

Vice President and
General Counsel(7)

(1) Amounts in this column reflect that portion of the awards under the Executive Annual Incentive Award Plan that are attributable to the leadership-rating factor, a discretionary adjustment applied by the Governance, Compensation and Nominating Committee.

(2) Amounts in this column reflect the dollar amount recognized for financial statement reporting purposes for 2006 in accordance with Statement of Financial Accounting Standards 123R, *Share Based Payment* (SFAS 123R), for (i) the performance shares that were granted in 2004 (with a 1/1/04 to 12/31/06 performance period), 2005 (with a 1/1/05 to 12/31/07 performance period) and 2006 (with a 1/1/06 to 12/31/08 performance period), (ii) performance-based restricted stock units granted in 2004, 2005 and 2006 and (iii) the incremental value attributable to the premium (5% for unrestricted stock and 20% for restricted stock) received for electing to receive stock in lieu of a portion of the cash payment otherwise payable under the Executive Annual Incentive Award Plan. The assumptions used in the valuation are discussed in Note 8 to our Consolidated Financial Statements included in our Form 10-K for the year ended December 31, 2006.

(3) Amounts in this column reflect the dollar amount recognized for financial statement reporting purposes for 2006 in accordance with SFAS 123R for stock options awarded prior to 2002. The assumptions used in this valuation are discussed in Note 8 to our Consolidated Financial Statements included in our Form 10-K for the year ended December 31, 2006.

(4) The amounts in this column represent awards earned under the Xcel Energy Inc. Executive Annual Incentive Award Plan that was approved by shareholders in 2005, including amounts that the executive officer elected to receive in shares of unrestricted and restricted common stock in lieu of a portion of the cash payment for which they were otherwise entitled under the Xcel Energy Inc. Executive Annual Incentive Award Plan. This

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amount does not, however, reflect the premium (5% for unrestricted stock and 20% for restricted stock) attributable to the election to receive shares of stock in lieu of a cash payment. The value of the premium is reflected in the Stock Awards column. The number of shares of stock issued is set forth below (shares were actually issued in February 2007 following determination of bonus amounts by the Governance, Compensation and Nominating Committee):

Name	Shares of Unrestricted Common Stock	Shares of Restricted Common Stock
Richard C. Kelly		21,394
Benjamin G.S. Fowke III		9,486
Paul J. Bonavia	18,327	
Patricia K. Vincent		
Gary R. Johnson		

(5) Amounts in this column reflect the actuarial increase in the present value of the executive officer's benefits under all pension plans established by the Company determined using interest rate and mortality rate assumptions consistent with those used in the Company's financial statements and includes amounts which the executive officers may not currently be entitled to receive because such amounts are not vested. The increase from the prior year is generally due to (1) the additional years of service earned by the executive officer under the plans, (2) the increase in the final average salary from the prior year used to determine plan benefits, and (3) the interest earned on accumulated benefits during the year (that is, the decrease in the deferral period until benefits commence as the executive officer approaches retirement). For Mr. Johnson, this amount also includes preferential earnings of approximately \$17,993 under a nonqualified compensation plan from a grandfathered deferred compensation benefit.

(6) The amounts represented in the All Other Compensation column for the Named Executive Officers include the following:

Name	Company Matching 401(k) Contributions (\$)	Contributions to the Non-Qualified Savings Plan (\$)	Value of the remainder of insurance premiums paid by the Company under the Officer Survivor Benefit Plan (\$)	Imputed Income as a result of the Life Insurance paid by the Company (\$)	Accrued Vacation Pay (\$)	Reimbursement for Taxes on Personal Benefits	Perquisites and Other Personal Benefits(1)	Total (\$)
Richard C. Kelly	8,800	30,850		10,705	20,192	11,858	39,105	121,510
Benjamin G.S. Fowke III	8,800	10,800		1,262	9,615	4,616	39,082	74,175
Paul J. Bonavia	8,800			5,484	9,904	7,890	39,071	71,149
Patricia K. Vincent	8,800	9,200		1,125			27,197	46,322
Gary R. Johnson	1,400		5,598	7,353	7,885	34,199	95,591	152,026

	Home Security	Financial Planning	Cash Allowance	Parking	Executive Medical & Physical	Airplane Travel 1/
Richard C. Kelly	15,384	2,400	18,000	3,321		
Benjamin G.S. Fowke III		9,500	18,000	3,205	8,377	
Paul J. Bonavia	9,033	2,215	18,000	2,986	6,837	
Patricia K. Vincent			18,000	2,360	6,837	
Gary R. Johnson	669	66,323	18,000	3,321	7,278	

1/ Executive officers and their families may use the corporate aircraft for personal travel only in the event the aircraft already is scheduled to fly to the destination and an open seat is available. The aggregate cost of personal use of the corporate aircraft is determined on a per flight basis and includes the cost of actual fuel used, the cost of on-board catering, the hourly cost of aircraft maintenance for the applicable number of flight hours, landing fees, trip related hangar and parking costs, universal weather monitoring costs, if applicable, crew expenses and other variable costs specifically incurred. Because the plane may only be used for personal travel if the aircraft already is scheduled to fly to the destination and an open seat is available, there is no incremental cost to the Company for such

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personal use. The Company has significant corporate operations in Minneapolis, Minnesota and Denver, Colorado and some executive officers, including several of the Named Executive Officers, split time between those offices and utilize the corporate aircraft to get back and forth between Minneapolis and Denver. These trips are not considered personal travel.

(7) Mr. Johnson retired on March 31, 2007.

Grants of Plan-Based Awards

Name (a)	Grant Date (b)	Date of Committee Action(1) (c)	Estimated Future Payouts Under Non-Equity Incentive Plan Awards(2)			Estimated Future Payouts Under Equity Incentive Plan Awards(3)			All Other Stock Awards: Number of Shares of Stock or Units (#)(4) (j)	All Other Option Awards: Number of Securities Underlying Options (#) (k)	Exercise Price of Awards (\$/Sh) (l)	Grant Date and Fair Value of Stock Awards (m)
			Threshold (\$) (d)	Target (\$) (e)	Maximum (\$) (f)	Threshold (\$) (g)	Target (\$) (h)	Maximum (\$) (i)				
Richard C. Kelly	1/1/06	12/13/05				25,018	100,073	200,146				1,364,996
	1/1/06	12/13/05					67,663.50					1,023,749
	1/1/06	12/13/05					22,554.50					341,250
	1/1/06	12/13/05	525,000	1,050,000	1,575,000							
	2/21/07								21,394			
Benjamin G.S. Fowke III	1/1/06	12/13/05				6,186	24,743	49,486				337,495
	1/1/06	12/13/05					16,730.25					253,129
	1/1/06	12/13/05					5,576.75					84,376
	1/1/06	12/13/05	162,500	325,000	482,138							
	2/21/07								9,486			
Paul J. Bonavia	1/1/06	12/13/05				6,372	25,486	50,972				347,629
	1/1/06	12/13/05					17,232					260,720
	1/1/06	12/13/05					5,744					86,907
	1/1/06	12/13/05	167,375	334,750	507,648							
	2/21/07								18,327			
Patricia K. Vincent	1/1/06	12/13/05				4,536	18,145	36,290				247,498
	1/1/06	12/13/05					12,268.50					185,622
	1/1/06	12/13/05					4,089.50					61,874
	1/1/06	12/13/05	123,750	247,500	375,334							
Gary R. Johnson	1/1/06	12/13/05				4,133	16,532	33,064				225,496
	1/1/06	12/13/05					11,178					169,123
	1/1/06	12/13/05					3,726					56,374
	1/1/06	12/13/05	112,750	225,500	338,250							

(1) The Committee approved the awards December 13, 2005, effective as of January 1, 2006.

(2) Amounts reflect annual incentive awards pursuant to the Executive Annual Incentive Award Plan, exclusive of the leadership-rating factor discussed below. The actual payments of these awards are included in the Non-Equity Incentive Plan Compensation column in the Summary Compensation Table.

(3) Amounts reflect performance shares (top number) and performance-based restricted stock units based on EPS growth measurement (second number) and performance-based restricted stock units based on environmental index measurement (third number) issued under the 2005 Omnibus Incentive Plan. Performance share payout values, while based on percentile performance, are also determined by the price of Xcel Energy common stock at payout.

(4) Amounts reflect the shares of restricted and unrestricted stock received by the executive officers as a result of their election to receive such stock in lieu of a portion of the cash payment for which they were otherwise entitled under the Executive Annual Incentive Award Plan for 2006. The Committee approved the awards February 21, 2007. The value of these shares is included in the Stock Awards column of the Summary Compensation Table.

Annual incentive awards, expressed as a percentage of salary, were set by the Committee under the Xcel Energy Executive Annual Incentive Award Plan. Payouts of annual incentive awards are dependent on the level of achievement of corporate financial and operational goals and business unit operational goals approved by the Committee, with each individual having the opportunity to earn from 0% to approximately 150% of his or her target annual incentive award based on the level of achievement in 2006 of the goals applicable to such individual.

Corporate goals for 2006 include targeted earnings per share of \$1.35, a customer service measurement, an environmental measurement related to air emissions and operations measurements related to generation availability, system reliability and safety. Business unit goals included customer service, reliability, safety, environmental responsibility, and management relative to budgeted financial results, measured at a business unit level.

Target annual incentive awards, as a percentage of base salary, were set for all Xcel Energy officers, ranging from 100% of salary for Mr. Kelly to 55% to 65% of salary for the other Named Executive Officers. With the approval of the Committee, an award may be multiplied by a leadership-rating factor from zero to two.

Payout of the annual incentive award for Mr. Kelly was dependent entirely on attaining corporate goals. For the other executive officers, including Named Executive Officers, the formula was weighted 67% to attaining corporate goals and 33% to attaining business unit operational goals.

In order to encourage increased share ownership by executive officers, the Xcel Energy Annual Incentive Plan provides an option for executives to receive their payments in shares of common stock or shares of restricted common stock (which vests in equal annual installments over a three-year period) in lieu of cash. A 5% premium is added to amounts paid in shares of common stock, and a 20% premium is added to amounts paid in shares of restricted common stock.

The target awards and payouts under the Annual Incentive Plan for 2006 are discussed in more detail above under the heading Compensation Discussion and Analysis.

The Committee also approved target long-term incentive grants under the Xcel Energy 2005 Omnibus Incentive Plan. As explained below, payout of long-term incentive grants is dependent on achievement of performance goals set by the Committee. Long-term incentive grants were made 50% in the form of performance-based restricted stock units and 50% in the form of performance shares. The amounts of the awards for each individual were established by the Committee and expressed as a percentage of such individual's base salary. The actual number of performance-based restricted stock units and performance shares awarded to an individual were determined by dividing the dollar value of such percentage of base salary by the expected value of each award type as determined on Jan. 3, 2006. For Mr. Kelly, his target long-term award for 2006 was set at 260% of his salary. For the other Named Executive Officers, the percentage ranged from 110% to 135%.

Performance-based restricted stock units (Units) represent an equal number of shares of Xcel Energy common stock. Prior to the expiration of the restricted period, the Units may not be sold or otherwise transferred by the recipients. Units are credited during the restricted period at the same rate as dividends paid on all other shares of outstanding common stock. The dividend equivalents are subject to all terms of the original grant.

Payout of the Units and the lapsing of restrictions on the transfer of Units are based on two separate performance criteria. Of the awarded Units, 75% of them plus associated earned dividend equivalents will be settled, and the restricted period will lapse, after Xcel Energy achieves 15% earnings per share on continuing operations (EPS) growth (adjusted for corporate-owned life insurance) measured against Dec. 31, 2005 EPS (adjusted for corporate-owned life insurance).

Additionally, Xcel Energy's annual dividend paid on its common stock must remain at \$0.86 per share or greater. EPS growth will be measured annually at the end of each fiscal year. However, in no event will the restrictions lapse prior to Dec. 31, 2007. If the performance criteria have not been met within four years of the date of grant, all associated Units shall be forfeited.

The remaining 25% of awarded Units plus associated earned dividend equivalents will be settled, and the restricted period will lapse, after the average of actual performance results for nitrogen oxide (NOx), sulfur dioxide (SO₂) and carbon dioxide (CO₂) emissions reductions (measured as a percentage of target performance) meets or exceeds 100%. For these purposes, the targets were 2.7 pounds per megawatt hour (lbs/MWh) for NOx, 3.4 lbs/MWh for SO₂ and 1,476 lbs/MWh for CO₂. Performance against these environmental targets will be measured annually at the end of each fiscal year. However, in no event will the restrictions lapse prior to Dec. 31, 2007. If the performance criteria have not been met within four years of the date of grant, all associated Units shall be forfeited.

The awards of performance shares also represent an equal number of shares of Xcel Energy common stock. Performance shares may not be sold or otherwise transferred. Payout of the performance share award will be dependent entirely on a single measure, total shareholder return (TSR) relative to peers over a three-year period. At the end of the three-year period, the performance share component provides for payout at the target level if Xcel Energy's TSR is at the 50th percentile of the peer group and payout at 200% of the target level for performance at or above the 90th percentile of the peer group. The performance share component provides smaller payouts for performance below the 50th percentile. No payout will be made for performance below the 35th percentile.

The target long-term incentive awards for 2006 as well as the payout of certain long-term incentive awards granted in 2004 and 2005, are discussed in more detail above under the heading Compensation Discussion and Analysis.

Other perquisites and benefits provided to executives generally are not tied to the Company's financial performance, but are primarily designed to attract and retain executives. Among the perquisites and benefits provided by the Company in 2006 to its executives were a cash perquisite allowance of \$18,000, reimbursement for financial planning services up to 2% of the executive officer's base salary (unused amounts may be carried over from prior years), home security systems (including installation and monitoring), executive medical insurance and physicals. In addition, Company-paid life insurance in an amount equal to four times base pay, reduced to two times base salary post retirement (which, in general, the executives would purchase upon termination by repaying to the Company the greater of the cash surrender value or the aggregate premiums paid by the Company), and benefits provided under the Xcel Energy Inc. Nonqualified Deferred Compensation Plan and the Xcel Energy Supplemental Executive Retirement Plan that make up for retirement benefits that cannot be paid under the Company's qualified retirement plans due to Internal Revenue Code limitations and the exclusion of certain elements of pay from pension-covered earnings. The aggregate incremental cost to the Company for providing these perquisites to each of the Named Executive Officers is included in the Summary Compensation Table.

Certain executive officers, including four of the Named Executive Officers, may receive severance benefits in accordance with the Xcel Energy Senior Executive Severance and Change in Control Policy that is discussed below. Mr. Bonavia may receive severance benefits under his employment agreement, which is discussed below.

Based on the fair value of equity awards granted to the Named Executive Officers in 2006 and the base salary of the Named Executive Officers, Salary accounted for approximately 22-38% of total compensation, while incentive compensation accounted for approximately 62-78% of the total compensation. Because the value of certain equity awards included in the Summary Compensation table is based on the SFAS 123R value rather than fair value, these percentages may not be able to be derived using the amounts reflected in the Summary Compensation table.

Outstanding Equity Awards at Fiscal Year-End

Name (a)	Option Awards					Stock Awards		Equity Incentive Plan Awards:	Equity Incentive Plan Awards:
	Number of Securities Underlying Unexercised Options (#) Exercisable (b)	Number of Securities Underlying Unexercised Options (#) (c)	Number of Securities Underlying Unexercised Options (#) (d)	Exercise Price (\$) (e)	Option Expiration Date (f)	Number of Shares or Units of Stock That Have Not Vested (g)	Market Value of Shares or Units of Stock That Have Not Vested (\$)(1) (h)	Number of Unearned Shares, Units or Other Rights That Have Not Vested (i)	Market or Payout Value of Unearned Shares, Units or Other Rights That Have Not Vested \$(1) (j)
Richard C. Kelly	155,000			26.8548	8/3/07	2,380,760 (2)	54,900	46,842.049 (5)	1,080,178 (5)
	69,750			20.0403	12/12/09	3,293,886 (3)	75,957	70,730.673 (6)	1,631,049 (6)
	228,000			26.3125	8/20/10			23,590.832 (7)	544,005 (7)
Benjamin G.S. Fowke III								57,044 (8)	1,315,435 (8)
								100,073 (9)	2,307,683 (9)
	6,975			31.0081	12/13/08	1,668,191 (4)	38,468	15,969.851 (5)	368,265 (5)
	11,625			20.0403	12/12/09	861,925 (2)	19,876	17,488.629 (6)	403,288 (6)
Paul J. Bonavia								5,832.990 (7)	134,509 (7)
								19,448 (8)	448,471 (8)
								24,743 (9)	570,574 (9)
	136,400			30.1613	12/14/07	2,608,152 (2)	60,144	16,513.456 (5)	380,800 (5)
Patricia K. Vincent								20,110 (8)	463,737 (8)
								25,486 (9)	587,707 (9)
	12,400			20.0403	12/12/09	2,901,957 (2)	66,919	16,332.802 (5)	376,634 (5)
	60,000			26.3125	8/20/10	2,153,536 (3)	49,661	12,824.629 (6)	295,736 (6)
Gary R. Johnson								4,277.404 (7)	98,637 (7)
								19,890 (8)	458,663 (8)
								18,145 (9)	418,424 (9)
	24,800			29.2742	1/24/09			14,518.046 (5)	334,786 (5)
	47,000			30.4300	4/1/11			11,684.696 (6)(10)	269,449 (6)(10)
Gary R. Johnson								3,897.202 (7)(10)	89,869 (7)(10)
								17,680 (8)	407,701 (8)
	10,138			23.7188	1/22/07			16,532 (9)(10)	381,228 (9)(10)
	9,376			26.8750	1/28/08				
	24,703			26.3125	1/27/09				
Gary R. Johnson									
	38,188			19.3125	1/26/10				
Gary R. Johnson									
	147,000			26.3125	8/20/10				

(1) Values were calculated based on a \$23.06 closing price of Xcel Energy common stock, as reported on the New York Stock Exchange at December 29, 2006.

(2) Representing restricted stock that the executive officers elected to receive in lieu of cash compensation for which they were otherwise entitled under the Executive Annual Incentive Award Plan. One-half of the restrictions lapsed on March 1, 2007 with the remaining half of the restrictions lapsing on March 1, 2008 or next available trading day if March 1 is not a trading day.

(3) Representing restricted stock that the executive officers elected to receive in lieu of cash compensation for which they were otherwise entitled under the Executive Annual Incentive Award Plan. The restrictions lapse in equal annual installments on March 1, 2007, March 1, 2008 and March 1, 2009, or the next available trading day if March 1 is not a trading day.

(4) Representing restricted stock that the executive officers elected to receive in lieu of cash compensation for which they were otherwise entitled under the Executive Annual Incentive Award Plan. The restrictions lapsed on March 1, 2007.

(5) Representing performance-based restricted stock units granted January 1, 2005, and earned dividend equivalents, measured against 12% earnings per share on continuing operations (EPS) growth (adjusted for corporate-owned life insurance) measured against December 31, 2004 EPS (adjusted for corporate-owned life insurance). However, in no event will the restrictions lapse prior to December 31, 2006.

(6) Representing performance-based restricted stock units granted January 1, 2006, and earned dividend equivalents, measured against 15% earnings per share (EPS) on continuing operations growth (adjusted for

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corporate-owned life insurance) measured against December 31, 2005 EPS (adjusted for corporate-owned life insurance). However, in no event will the restrictions lapse prior to December 31, 2007.

(7) Representing performance-based restricted stock units granted January 1, 2006, and earned dividend equivalents, measured against an environmental goal as described on page 48. However, in no event will the restrictions lapse prior to December 31, 2007.

(8) Representing performance shares granted January 1, 2005 for the performance period January 1, 2005 to December 31, 2007. Actual performance share payout values, while based on percentile performance, are also determined by the price of Xcel Energy common stock at payout. Values in table assume target level performance.

(9) Representing performance shares granted January 1, 2006 for the performance period January 1, 2006 to December 31, 2008. Actual performance share payout values, while based on percentile performance, are also determined by the price of Xcel Energy common stock at payout. Values in table assume target level performance.

(10) As a result of Mr. Johnson's retirement, these awards were forfeited on March 31, 2007.

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Option Exercises and Stock Vested

Name (a)	Option Awards		Stock Awards	
	Number of Shares Acquired on Exercise (#) (b)	Value Realized on Exercise (\$) (c)	Number of Shares Acquired on Vesting (#) (d)	Value Realized on Vesting (\$) (e)
Richard C. Kelly			1,151.218	(1) 21,321 (2)
			64,362.050	(3) 1,316,204 (4)
			70,346	(5) 1,712,925 (6)
			15,614.016	(7) 360,059 (8)
Benjamin G.S. Fowke III			2,030.336	(1) 37,602 (2)
			19,185.749	(3) 392,349 (4)
			20,970	(5) 510,620 (6)
			5,323.284	(7) 122,755 (8)
Paul J. Bonavia			1,261.174	(1) 23,357 (2)
			22,383.942	(3) 457,752 (4)
			24,465	(5) 595,723 (6)
			5,504.485	(7) 126,933 (8)
Patricia K. Vincent			1,403.243	(1) 25,988 (2)
			23,183.771	(3) 474,108 (4)
			25,339	(5) 617,005 (6)
			5,444.267	(7) 125,545 (8)
Gary R. Johnson			20,785.409	(3) 425,062 (4)
			22,718	(5) 553,183 (6)
			4,839.349	(7) 111,595 (8)

(1) Reflects vesting of restricted stock received in lieu of cash compensation they were otherwise entitled to receive under the Executive Annual Incentive Award Plan.

(2) Value is based on the average of the high and low market price of Xcel Energy common stock on March 1, 2006, or \$18.52, the date the restrictions lapsed.

(3) Reflects settlement of performance-based restricted stock units granted in 2004.

(4) Value is based on closing market price of Xcel Energy common stock on August 2, 2006, or \$20.45, the date the restrictions lapsed.

(5) Reflects vesting of performance shares for the performance period January 1, 2004 to December 31, 2006. Performance Shares were actually settled on February 21, 2007 following certification of satisfaction of performance measured by the Governance, Compensation and Nominating Committee.

(6) Value is based on closing market price of Xcel Energy common stock on February 20, 2007, or \$24.35, the date prior to the Governance, Compensation and Nominating Committee meeting.

(7) Reflects settlement of performance-based restricted stock units based on environmental index metric granted in 2005.

(8) Value is based on closing market price of Xcel Energy common stock on December 29, 2006, or \$23.06, the date the restrictions lapsed.

Pension Benefits

Name (a)	Plan Name (b)	Number of Years Credited Service # (c)	Present Value of Accumulated Benefit (\$) (d)	Payments During Last Fiscal Year (\$) (e)
Richard C. Kelly	Xcel Energy Pension Plan	39	730,028	0
	Nonqualified Pension Plan	39	271,935	0
	SERP	39	9,130,189	0
Benjamin G.S. Fowke III	Xcel Energy Pension Plan	10	205,060	0
	Nonqualified Pension Plan	10	294,617	0
	SERP	10	546,918	0
Paul J. Bonavia	Xcel Energy Pension Plan	9	110,493	0
	Nonqualified Pension Plan	9	66,989	0
	SERP	16	1,258,338	0
Patricia K. Vincent	Xcel Energy Pension Plan	8	173,752	0
	Nonqualified Pension Plan	8	268,461	0
	SERP	13	463,708	0
Gary R. Johnson	Xcel Energy Pension Plan	28	772,752	0
	Nonqualified Pension Plan	28	866,082	0
	SERP	28	782,887	0
	Deferred Compensation(1)	28	1,005,115	0

(1) Representing amounts from a grandfathered deferred compensation benefit that will provide a supplemental benefit to Mr. Johnson on his retirement. The value considers incentive compensation as part of the definition of final average pay that would otherwise be excluded from the definition of final average pay in calculating Mr. Johnson's pension benefit under the traditional benefit pension benefit formula.

The Company maintains several defined benefit plans in which the Named Executive Officers participate. One is the Xcel Energy Pension Plan, which provides funded, tax-qualified benefits. The benefits under the Xcel Energy Pension plan are subject to compensation and benefit limits under the Internal Revenue Code. The second is the Xcel Energy Inc. Nonqualified Pension Plan (referred to as the Nonqualified Pension Plan), which provides unfunded, non-qualified benefits for compensation that is in excess of the limits applicable to the Xcel Energy Pension Plan. The third is the Xcel Energy Supplemental Executive Retirement Plan (referred to as the SERP), which provides unfunded, non-qualified benefits that are offset by benefits under the Xcel Energy Pension Plan and the Nonqualified Pension Plan.

The Pension Benefits Table shows the Named Executive Officer's number of years of credited service, the Present Value of Accumulated Benefits, and the payments made during the last fiscal year under each of the plans noted above. For these purposes, the Present Value of Accumulated Benefits is the present value as of December 31, 2006 of the annual pension benefit that was earned as of December 31, 2006 that would be payable under each plan for the executive officer's life beginning at the executive officer's normal retirement age. Certain assumptions regarding interest rates and mortality were used to determine the present value of the benefit that is payable beginning at normal retirement age. Those assumptions are consistent with those used in the Company's financial statements. Normal retirement age for this purpose is defined by the various plans in which the executives participate. The Present Value of Accumulated Benefits is determined for each plan assuming benefits commence at the age described below:

- **Xcel Energy Pension Plan** the basic benefit payable under the Xcel Energy Pension Plan to each executive is determined under one of three formulas: the final average pay formula (the Traditional Benefit formula), the Pension Equity Benefit formula or the Account Balance Benefit formula. The Present Value of Accumulated Benefits for the Traditional Benefit formula is determined assuming that the benefit commences at the normal retirement age defined by the Plan, which is age 65. Mr. Johnson is the only named executive officer that participates in the Traditional Benefit formula. As discussed previously, Mr. Johnson retired on March 31, 2007. For a discussion of Mr. Johnson's retirement benefits, see Potential Payments Upon Termination or Change in Control Gary R. Johnson Retirement Agreement, below. For participants in the Pension Equity Benefit formula (including Mr. Fowke and Ms. Vincent) and the Account Balance Benefit formula (including Mr. Kelly and Mr. Bonavia), the Present Value of Accumulated Benefits does not assume benefits commence at a particular age. Instead, for those two formulas, the Present Value of Accumulated Benefits is stated as the current accumulated value of the pension equity benefit or the account balance, whichever is applicable.
- **Nonqualified Pension Plan** the Present Value of Accumulated Benefits for the Traditional Benefit formula is determined assuming that the benefit commences at the earliest age at which benefits are unreduced for early commencement, which is the earliest of (1) the age at which the participant has completed 40 years of credited service, (2) the later of age 62 and the completion of at least 20 years of vesting service, or (3) the later of age 55 and the age at which the sum of the participant's age and years of credited service equals 90 or more (Rule-of-90). The Present Value of Accumulated Benefits for participants in the Pension Equity Benefit formula and the Account Balance Benefit formula is stated as the current accumulated value of the pension equity benefit or the account balance, whichever is applicable.
- **SERP** the Present Value of Accumulated Benefits is determined assuming that the benefit payable under this plan commences at the normal retirement age defined by the Plan, which is age 62 (or, for Mr. Bonavia, age 60).

Xcel Energy Pension Plan

There are three general benefit components payable under the Xcel Energy Pension Plan, the basic benefit, the retirement spending account and the social security supplement.

Basic Benefit

As mentioned above, the basic benefit is determined under one of three formulas: the Traditional Benefit formula, the Pension Equity Benefit formula or the Account Balance Benefit formula.

Traditional Benefit Formula

The Basic Benefit is determined as follows:

- Monthly benefit, payable as a single life annuity at the participant's normal retirement age, equal to the sum of 1.1333% of the participant's highest average monthly base pay plus .5% of highest average monthly base pay in excess of one-third of the monthly Social Security Wage Base for the current year, times years of credited service (up to 30 years).
- Highest average monthly base pay is equal to the highest average monthly rate of base pay during any 48 consecutive months of covered employment. Base pay is regular, straight-time earnings, including employee contributions to the 401(k) Savings Plan, the Flexible Benefits Plan and, effective January 1, 2002, the Deferred Compensation Plan.

If a participant retires after earning 40 years of credited service, or reaching age 62 with 20 years of vesting service, or reaching Rule-of-90, the full accrued benefit described above is payable. Mr. Johnson would have attained Rule-of-90 benefit eligibility by December 31, 2007. If retirement occurs between ages 57 and 62 with at least 20 years of vesting service, the Basic Benefit is reduced 0.333% for each month that benefits commence prior to age 62.

If a participant terminates employment prior to reaching the eligibility provisions described above, but after reaching age 57 and with at least five years of vesting service, the Basic Benefit is reduced 0.333% for each month that early commencement precedes age 65. If the participant's age at commencement is less than 57, the benefit payable is the amount that is actuarially equivalent to the benefit payable at age 65.

Pension Equity Benefit Formula

Basic Benefit:

- Monthly benefit, payable as a single life annuity at the participant's normal retirement age, which is the actuarial equivalent of the participant's Pension Equity Plan (PEP) Balance. The PEP Balance is equal to 10% of the participant's highest average pay times years of credited service times twelve (12).
- Highest average pay is equal to the highest average monthly rate of base pay plus incentive pay during any 48 consecutive months of covered employment. Base pay is regular, straight-time earnings, including employee contributions to the 401(k) Savings Plan, the Flexible Benefits Plan and, effective January 1, 2002, the Deferred Compensation Plan.

If a participant terminates employment after completing five years of vesting service, the benefit is calculated as described above but based on service and final average salary at termination.

Account Balance Benefit Formula

Basic Benefit:

- Monthly benefit, payable as a single life annuity at the participant's normal retirement age, which is the actuarial equivalent of the participant's Account Balance. The Account Balance is determined as follows:

(a) *Retirement Program Credits*

A retirement program credit is added to the account balance depending on age plus years of credited service and base pay for the year as follows:

Age + Years of Credited Service	Retirement Program Credits	
55-59	5.25	%
60-64	6.00	%
65-69	7.00	%
70-74	8.00	%
75-79	9.00	%
80 and more	10.00	%

Base pay is regular, straight-time earnings, including employee contributions to the 401(k) Savings Plan, the Flexible Benefits Plan and, effective January 1, 2002, the Deferred Compensation Plan.

(b) *Transition Credits*

Employees who were active participants in a predecessor plan may be eligible for transition credits. These credits are granted annually for up to five years from the effective date of the plan.

Age + Years of Credited Service	Transition Credits	
56-58	7.00	%
59-61	8.00	%
62-64	9.00	%
65 or more	10.00	%

Interest is added to the account balance at the end of each plan year. Interest is based on the account balance at the beginning of the year. The rate of interest applied is equal to the average of the annual rate of interest on 30-year Treasury securities for the months of August and September of the preceding calendar year, but not less than 5% (5% for 2006).

If a participant terminates employment after completing five years of vesting service, the benefit is calculated as described above but based on service and pay through the date of termination. The Account Balance continues to accrue interest until the benefit is commenced.

If the participant elects an annuity and commences payment after age 55, the amount payable is determined by converting the Account Balance at commencement into an annuity based on a table of factors.

Retirement Spending Account

The Retirement Spending Account is the same whether a participant is in the Traditional Benefit formula, the Pension Equity Benefit formula or the Account Balance Benefit formula. In each case, the

Retirement Spending Account is a monthly benefit, payable as a single life annuity, that is the actuarial equivalent of the Retirement Spending Account balance. The Retirement Spending Account balance is the accumulated value at retirement of the initial account balance, annual credits, and annual interest credits.

- Initial account balance equal to \$1,400 times all years of service as of December 31, 2002 (1998 for Mr. Johnson)
- Annual credits equal to \$1,400
- Interest credits based on one-year treasury constant maturities plus 1%

Social Security Supplement

The Social Security Supplement is the same whether a participant is in the Traditional Benefit formula, the Pension Equity Benefit formula or the Account Balance Benefit formula. In each case, the Social Security Supplement is a supplement that is paid from the participant's retirement date to his or her retirement age for purposes of Social Security. The monthly supplement is equal to \$50 times the number of years of service (limited to 20 years). Participants are eligible for the Social Security Supplement if they are (1) age 57 with 20 years of service, (2) age 55 and the sum of age and credited service is greater than or equal to 90 or (3) age 65 with 1 year of service.

Credited Service; Distributions

Generally, a participant's years of credited service are based on the years of employment with the Company and its predecessors. However, in certain cases, credit for service prior to participation in the plan may be granted. The years of credited service listed in the above table for the Xcel Energy Pension Plan for all of the Company's Named Executive Officers are based only on their period of service while employed by the Company and its predecessors.

Benefits provided under the Xcel Energy Pension Plan are based on compensation up to the compensation limit under Section 401(a)(17) of the Internal Revenue Code (\$220,000 in 2006). In addition, benefits provided under the Xcel Energy Pension Plan may not exceed a benefit limit under Section 415(b) of the Internal Revenue Code (\$175,000 payable as a single life annuity beginning at normal retirement age in 2006).

Benefits are payable under one of the optional forms of payment elected by the participant, including a lump sum. Benefits under the Xcel Energy Pension Plan are funded by an irrevocable tax-exempt trust. A participant's benefit under the Xcel Energy Pension Plan is payable from the assets held by the tax-exempt trust.

Nonqualified Pension Plan

The Nonqualified Pension Plan replaces the benefit that would have been payable through the Xcel Energy Pension Plan if not limited as noted above by Internal Revenue Code sections 401(a)(17) and 415(b). All active participants must receive their Nonqualified Pension Plan benefit as a lump sum.

Generally, a participant's years of credited service are based on their years of employment with the Company and its predecessors. However, in certain cases, credit for service prior to participation in the plan may be granted. The years of credited service listed above for the Nonqualified Pension Plan for all of the Company's Named Executive Officers are based only on their period of service while employed by the Company and its predecessors.

The Nonqualified Pension Plan is unfunded and maintained as a book reserve account. No funds are set aside in a trust or otherwise; participants in the Nonqualified Pension Plan are general

creditors of the Company with respect to the payment of their Nonqualified Pension Plan benefits. The executive officer's account under the Nonqualified Pension Plan cannot be sold, transferred or otherwise anticipated before it becomes payable under the terms of the plan.

SERP

The SERP provides a target percentage of final average compensation based on years of service, offset by the benefits received from the Xcel Energy Pension Plan and the Nonqualified Pension Plan. Final average compensation for the SERP is defined as the average of the highest three calendar years of compensation during the five calendar year period immediately preceding the calendar year in which the participant retires or terminates employment. Compensation is defined as the participant's base pay plus any bonus earned for that year regardless of whether such bonus is paid in that year or in the next year under the Company's regular annual incentive plan.

The SERP benefit, defined as a 20-year certain annuity, accrues ratably over 20 years and, when fully accrued, is equal to (a) 55% of final average compensation minus (b) any other qualified or nonqualified benefits. The Retirement Spending Account and Social Security Supplement are not included in the offset. The SERP benefit is payable as a single lump-sum amount equal to the actuarial equivalent present value of the 20-year certain annuity or in an actuarial equivalent life-only or joint and 50% survivor annuity. Benefits generally are payable at age 62, or as early as age 55, but would be reduced 5% for each year that the benefit commencement date precedes age 62.

Generally, a participant's years of credited service are based on their years of employment with the Company and its predecessors. However, in certain cases, credit for service prior to participation in the plan may be granted. Except for Mr. Bonavia and Ms. Vincent, the years of credited service listed above for the SERP for the Named Executive Officers are based only on their period of service while employed by the Company and its predecessors. The Company has granted Ms. Vincent five additional credited years of service for purposes of SERP accrual, which are included in the above table. Additionally, the Company has agreed to accrue SERP benefits for Mr. Bonavia ratably over 11 years rather than 20 years, with the years of credited service in the table above imputed to reflect that rate, and to permit distribution of his full unreduced benefit as early as age 60.

The SERP is unfunded and maintained as a book reserve account. No funds are set aside in a trust or otherwise; participants in the SERP are general creditors of the Company with respect to the payment of their SERP benefits. The executive's account under the SERP cannot be sold, transferred or otherwise anticipated before it becomes payable under the terms of the plan.

Nonqualified Deferred Compensation

Name (a)	Executive Contributions in Last FY (\$)(1) (b)		Registrant Contributions in Last FY (\$) (c)		Aggregate Earnings in Last FY (\$) (d)		Aggregate Withdrawals/Distributions (\$) (e)		Aggregate Balance at Last FYE (\$) (f)	
Richard C. Kelly		36,798		22,100		89,240		0		595,773
Benjamin G.S. Fowke III		13,200		8,850		39,241		0		235,647
Paul J. Bonavia		0		0		119,805		0		707,222
Patricia K. Vincent		13,500		9,600		31,662		0		157,832
Gary R. Johnson		0		0		70,358		0		997,886

(1) Reflects the following amounts for each of the following executive officers which is reported as compensation to such executive officer in the Summary Compensation Table on page 44: Mr. Kelly: \$36,798; Mr. Fowke: \$13,200; and Ms. Vincent: \$13,500.

The Company has a nonqualified deferred compensation plan (the Deferred Compensation Plan) that generally allows key employees, including all executive officers, to defer compensation above government limitations on 401(k) contributions that apply to the Company's qualified 401(K) savings plan (the Savings Plan) and to defer taxation on all earnings on compensation deferred into the plan. For 2006, the maximum limitation on elective salary deferrals and the limitation on the amount of compensation that may be taken into account for deferrals under the Savings Plan was \$15,000 and \$220,000, respectively.

Each executive officer may elect each year to separately defer all or any portion of his or her base pay and annual incentive pay otherwise payable in the next following calendar year. In addition, if the executive participates under the Account Balance benefit formula or Pension Equity benefit formula of the Company's qualified pension plan, the Company will contribute a matching contribution.

Prior to January 1, 2007, the Company matched (i) 100% of deferrals into the Deferred Compensation Plan and the Savings Plan up to 3% of base salary and (ii) 50% of deferrals into the Deferred Compensation Plan and the Savings Plan that exceed 3% of base salary but not in excess of 5% of base salary. Effective January 1, 2007, the Company changed the matching contributions formula to 50% of deferrals into the Deferred Compensation Plan and the Savings Plan up to 8% of base salary. Matching credits under the Deferred Compensation Plan are immediately vested. The Company also has the option to make discretionary credits but did not do so in 2006.

Deferrals, plus any Company match, are credited to a special recordkeeping account in the participant's name. Earnings on the deferrals are indexed to the assumed investment funds selected by the participant. For 2006, those investment fund options (and the associated returns) included an Xcel Energy common stock fund, Vanguard® Prime Money Market Fund (4.88%), Vanguard® Inflation-Protected Securities Fund (0.43%), PIMCO Total Return Fund (3.74%), Vanguard® Total Bond Market Index Fund (4.27%), Vanguard® Wellington™ Fund (14.97%), Vanguard® 500 Index Fund (15.64%), Longleaf Partners Fund (21.63%), Vanguard® PRIMECAP Fund (23.32%), Vanguard® Mid-Cap Index Fund (13.60%), Wasatch Core Growth Fund (6.68%), Vanguard® Small-Cap Index Fund (15.64%), and Vanguard® Developed Markets Index Fund (26.18%), Company matches are credited to an Xcel Energy common stock fund. Participants may change their assumed investment fund on a daily basis.

The executive's account is payable on the earlier of the executive's termination of employment or death, and will be paid in a lump sum or in ten equal annual installments as elected by the executive or, if no election is made, in a lump sum. The distribution will be made (or will begin) as of the next January 31 or July 31 that first follows the sixth-month anniversary of the executive's termination of

employment. Payment to the executive's beneficiary in the event of the participant's death will be made in a lump sum unless the executive was already receiving installment payments. In that case, the installment payments will continue to be paid to the executive's beneficiary. In addition, the executive can receive a distribution in the event of an extreme financial hardship that cannot be satisfied by any other means.

The Deferred Compensation Plan is unfunded. No property is set aside in a trust or otherwise to pay the Deferred Compensation Plan benefits and the Company is not obligated to invest in the Xcel Energy Stock Fund or any of the mutual funds selected by the executive. In other words, each executive officer participating in the Deferred Compensation Plan is an unsecured general creditor of the Company with respect to the executive officer's Deferred Compensation Plan account. The executive's account under the Deferred Compensation Plan cannot be sold, transferred or otherwise anticipated before it becomes payable under the terms of the Deferred Compensation Plan.

COMPENSATION COMMITTEE REPORT

The Governance, Compensation and Nominating Committee oversees (i) the compensation of the Company's directors and principal officers, (ii) the Company's executive compensation policy and (iii) the Company's benefit programs.

The Governance, Compensation and Nominating Committee has five members, none of whom has any relationship to the Company that interferes with the exercise of his or her independence from management and the Company, and each of whom qualifies as independent under the standards used by the New York Stock Exchange, where the Company's shares are listed.

The Governance, Compensation and Nominating Committee has reviewed and discussed with management the Compensation Discussion and Analysis appearing elsewhere in this proxy statement. Based on the review and discussions referred to above, the Governance, Compensation and Nominating Committee recommended to the Company's Board of Directors that the Compensation Discussion and Analysis be included in the Company's Proxy Statement on Schedule 14A.

Compensation Committee

Douglas W. Leatherdale, Chairman

C. Coney Burgess, Member

Fredric W. Corrigan, Member

A. Barry Hirschfeld, Member

Richard H. Truly, Member

David A. Westerlund, Member

LEGAL PROCEEDINGS

Beginning in July 2002, several lawsuits purporting to be class actions on behalf of certain purchasers of the Company's common stock were filed in the U.S. District Court for the District of Minnesota. The lawsuits, which were consolidated, alleged violations of Section 10(b) of the 1934 Act and Rule 10b-5 thereunder relating to allegedly false and misleading disclosures concerning, among other things, round trip energy trades and the nature, extent and seriousness of liquidity and credit difficulties at NRG. The complaints named Xcel Energy; Wayne H. Brunetti, former chairman and chief executive officer; Edward J. McIntyre, former vice president and chief financial officer; former chairman James J. Howard; Gary R. Johnson, general counsel, and Richard C. Kelly, then president of Xcel Energy Enterprises, as defendants.

In August 2002, a shareholder derivative action was filed in the U.S. District Court for the District of Minnesota, purportedly on behalf of Xcel Energy, against the directors and certain present and former officers, citing allegedly false and misleading disclosures and asserting breach of fiduciary duty.

In September and October 2002, two essentially identical actions were filed in the U.S. District Court for the District of Colorado, purportedly on behalf of classes of employee participants in the Company's and its predecessors' 401(k) or employee stock ownership plans. The complaints alleged violations of the Employee Retirement Income Security Act of 1974 (ERISA) in the form of breach of fiduciary duty in allowing or encouraging the purchase, contribution and/or retention of the Company's common stock in the plans. The complaints named as defendants Xcel Energy, its directors, certain former directors and certain former officers.

On April 1, 2005, the U.S. District Court for the District of Minnesota approved a settlement agreement relating to all of these lawsuits. Under the terms of the settlement of the securities and ERISA claims, the Company's insurance carriers agreed to pay \$70.5 million and the Company paid \$17.5 million. Settlement of the derivative lawsuit involved the Company's adoption of certain corporate governance measures and payment of plaintiff's attorney's fees and expenses, of which the Company paid \$125,000. The settlements included no admission of liability by the Company or any individual defendant.

The Company is obligated to indemnify its officers and directors under certain circumstances to the fullest extent permitted by Minnesota law. As part of that obligation, the Company has advanced and will continue to advance certain attorneys' fees and expenses incurred by officers and directors in various litigation, including the litigation described above. In connection with the derivative proceedings described above, for the period July 31, 2002 through March 31, 2003, the period April 1, 2003 through March 31, 2004, the period April 1, 2004 through March 31, 2005, and the period April 1, 2005 through March 1, 2006, the Company has advanced expenses of approximately \$22,000, \$56,000, \$107,000 and less than \$5,000, respectively, to the law firm of Jones Day on behalf of the Company's directors and Mr. Edward J. McIntyre, former vice president and chief financial officer, approximately \$15,000, \$7,000, \$3,000 and less than \$1,000, respectively, to the law firm of Briggs and Morgan on behalf of the Company's directors and Mr. Edward J. McIntyre, former vice president and chief financial officer and approximately \$8,000, \$7,000, \$4,000 and less than \$1,000, respectively, to the law firm of Rider Bennett on behalf of Mr. James J. Howard, former chairman.

RELATED PARTY TRANSACTIONS

One of our directors, Mr. Richard K. Davis, is the President and Chief Executive Officer of U.S. Bancorp. During 2006, U.S. Bancorp or its affiliates served as trustee for some of our debt securities and performed investment and other banking services for the Company. For these services, the Company paid U.S. Bancorp and its affiliates approximately \$600,000. The Company's bylaws provide that transactions between the Company and an organization in which one of the Company's directors

is a director or officer may be authorized, approved or ratified by a majority of the Board of Directors of the Company, with the interested director not voting. In accordance with the terms of the Company's bylaws, the Board of Directors of the Company approved these services to be provided by U.S. Bancorp.

POTENTIAL PAYMENTS UPON TERMINATION OR CHANGE IN CONTROL

Paul J. Bonavia Employment Agreement

In connection with and effective upon completion of the merger between Northern States Power Company and NCE that formed Xcel Energy in 2000, we and Paul J. Bonavia entered into an amendment to an employment agreement between Mr. Bonavia and NCE. Except as discussed below, the original agreement expired December 14, 2000. Mr. Bonavia also previously had entered into a change in control agreement with NCE that provided for severance benefits similar to those provided under the 1999 Policy discussed below. In connection with the merger, Mr. Bonavia's position changed from Senior Vice President, General Counsel and President of NCE's International business unit to President of our Energy Markets business unit. In the amendment, Mr. Bonavia agreed not to assert before January 6, 2003 that his duties and responsibilities had been diminished, and thus he waived the right to claim certain benefits under the 1999 Xcel Energy senior executive severance policy (the "1999 Policy") relating to this change in his status prior to that date. If certain conditions were met on January 6, 2003 or within seven business days thereafter, which conditions included the termination of Mr. Bonavia's employment, Mr. Bonavia would have been entitled to severance benefits comparable to those provided to the other senior executives under the 1999 Policy, which terminated on August 18, 2003 on its scheduled termination date. In further amendments, Mr. Bonavia agreed to continue his employment through August 31, 2003. Mr. Bonavia also agreed not to assert at any time that his duties and responsibilities have been diminished. In return, we agreed that if we terminate Mr. Bonavia's employment at any time for any reason other than cause, as defined in the 1999 Policy, or if Mr. Bonavia terminates his employment for any reason after August 31, 2003, then he will be entitled to severance benefits comparable to those provided to the other senior executives under the 1999 Policy as if he had terminated on January 6, 2003, and as adjusted for inflation. The severance benefits payable under the 1999 Policy included generally 2.5 times salary, bonus and long-term compensation, as well as payments for an additional 2.5 years of service under the pension and retirement savings plans. Assuming that Mr. Bonavia's employment was terminated December 31, 2006 other than following a change in control, the severance benefits payable to Mr. Bonavia under his employment agreement would have been approximately \$4,100,000. Assuming that Mr. Bonavia's employment was terminated December 31, 2006 following a change in control, any severance benefits that Mr. Bonavia might be entitled to under the change in control agreement would have been approximately \$6,000,000 plus a tax gross up.

Gary R. Johnson Retirement Agreement

On March 31, 2007, Mr. Gary R. Johnson, Vice President and General Counsel of Xcel Energy Inc. (the "Company"), retired. In connection with his retirement, Mr. Johnson and the Company entered into an agreement providing for the compensation and benefits he is to receive from the Company following his retirement. This agreement recognizes that Mr. Johnson will be entitled following his retirement to receive all benefits for which he qualifies under the terms of Company plans, programs, policies and practices under which he is covered. The benefits that Mr. Johnson is entitled to receive upon termination include:

- the ability to exercise outstanding stock options through the end of their respective terms
- participation in outstanding performance share and restricted stock units awarded in 2005 in accordance with their terms, with an estimated value, assuming payout at target and a

March 20, 2007 stock price, of approximately \$805,970 (performance share and restricted stock units awarded in 2006 and 2007 will be forfeited upon retirement unless the Governance, Compensation and Nominating Committee of the Board of Directors acts to provide a benefit to participants who retire during the term of an award and permits Mr. Johnson to be included in this group)

- vested benefits under the Company's pension plan, non-qualified pension plan and Supplemental Executive Retirement Plan (SERP) (i.e., taking into account any reductions for early retirement) (estimated to have a present value of approximately \$4,535,257)
- accrued vacation/paid time off (\$30,356)
- vested benefits under the Company's 401(k) plan and deferred compensation plan
- post-employment/ retirement coverage under the Company's group health and life plans (with an estimated value of premiums for group term life insurance of approximately \$3,200; premiums for group health being fully retiree-paid)

In addition, the agreement provides that Mr. Johnson will be entitled to the following additional benefits:

- a cash payment equal to \$56,375, representing one-fourth of his 2007 annual incentive target award (such payment to be made at the time the 2007 annual incentive is paid to other participants in February 2008)
- a cash payment of \$1,070,000, payable in a lump sum on October 15, 2007
- a cash payment, payable in a lump sum on October 15, 2007, equal to the actuarial equivalent present value of credits under the pension plan and nonqualified pension plan, deferred compensation plan and SERP that would be needed to allow him to reach the age and years of service criteria, the so-called Rule of 90 , when benefits would be unreduced for early retirement by continuing employment through and retiring at November 1, 2007 (estimated to be approximately \$180,583)
- a cash payment, payable in a lump sum on October 15, 2007, equal to the actuarial equivalent present value of the estimated difference in the amount of retiree medical premiums that he would be required to pay from April 1, 2007 through March 31, 2009 and those medical premiums he would have paid as an active employee for such period (estimated to be approximately \$27,693)
- executive life insurance coverage until December 31, 2011 equal to his coverage currently in force (200% of final base salary) (estimated premiums of approximately \$83,000)

As a condition to and in consideration of receiving these benefits, Mr. Johnson signed a release of claims agreement. These additional benefits are less than Mr. Johnson would have received if his employment was terminated without cause under the Company's 2003 Severance and Change in Control Policy (discussed below).

2003 Severance and Change in Control Policy

In October of 2003, we adopted the Xcel Energy Senior Executive Severance and Change in Control Policy (as amended, the 2003 Policy). The 2003 policy was intended to replace the 1999 Policy and, in many ways, operates similarly to the 1999 policy. Each of our Named Executive Officers, other than Mr. Bonavia, are participants in the 2003 Policy. Additional participants may be named by the Board or the Governance, Compensation and Nominating Committee from time to time.

Under the 2003 Policy, a participant whose employment is terminated will receive severance benefits unless:

- the employer terminated the participant for cause (as defined in the 2003 Policy);
- termination was because of the participant's death, disability or retirement;
- the participant's division, subsidiary or business unit was sold and the buyer agreed to continue the participant's employment with specified protections for the participant; or
- the participant terminated voluntarily.

The severance benefits for executive officers under the 2003 Policy include the following:

- a cash payment equal to two times the participant's annual base salary and target annual incentive award;
- prorated target annual incentive compensation for the year of termination;
- a cash payment ranging from approximately \$45,000 to \$75,000 (depending on salary range) for financial planning and outplacement services;
- a cash payment equal to the value of the additional amounts that would have been credited to or paid on behalf of the participant under pension and retirement savings plans if the participant had remained employed for another two years;
- continued medical, dental and life insurance benefits for two years; and
- continued perquisite allowance for two years.

If the participant is terminated, including a voluntary termination following a diminution in salary, benefits or responsibilities, within two years following a change in control the participant will receive benefits under the 2003 Policy similar to the severance benefits above, except that the cash payment will be equal to two or three times the participant's annual base salary and target annual incentive award, the cash payment for the value of additional retirement savings and pension credits will be for two or three years and medical, dental and life insurance, financial planning and perquisite allowance benefits will be continued for two or three years. In addition, each of the participants entitled to enhanced benefits upon a change-in-control will be entitled to receive an additional cash payment to make the participant whole for any excise tax on excess parachute payments that he or she may incur, with certain limitations specified in the 2003 Policy.

For these purposes, a change of control generally means (i) any acquisition of 20% or more of either our common stock or combined voting power (subject to limited exceptions for acquisitions directly from us, acquisitions by us or one of our employee benefit plans, or acquisitions pursuant to specified business combinations in which (a) our shareholders will own more than 60% of the shares of the resulting corporation, (b) no one person will own 20% or more of the shares of the resulting corporation, and (c) a majority of the board of the resulting corporation will be our incumbent directors), (ii) directors of the Company as of the date of the 2003 Policy and those directors who have been elected subsequently and whose nomination was approved by such directors fail to constitute a majority of the Board, (iii) a merger, share exchange or sale of all or substantially all of the assets of the Company (each, a "business combination") (except those business combinations that satisfy clauses (a), (b) and (c) above), or (iv) shareholder approval of a complete liquidation or dissolution of the Company.

In October 2006, the Governance, Compensation and Nominating Committee amended the 2003 Policy to reduce the separation benefits payable to an executive officer other than in the event of a change in control to the following: (i) a lump sum severance benefit equal to one times annual salary

and target annual incentive; (ii) a lump sum payment equal to the actuarial equivalent of the additional benefits accrued under the Company's retirement plans as if the executive officer had continued in employment for one additional year; (iii) a lump sum payment equal to the additional employer contributions that the executive officer would have received under the Company's savings plans if the executive officer's employment had continued for one additional year; and (iv) for a period of one year following termination, continued medical, dental and life insurance benefits, and perquisite cash allowance. This change will be effective October 2009.

In addition, pursuant to the terms of the Company's incentive compensation plans, upon a change in control, all stock-based awards, such as stock options and restricted stock, will vest immediately and all cash-based awards, such as performance shares and restricted stock units, will vest and be paid out immediately in cash as if the applicable performance goals had been obtained at target levels. All outstanding stock options are already exercisable, therefore, a change in control would have no impact on stock options. The amounts payable in cash for each of the named executive officers relating to the performance shares and restricted stock units are included in the Incentive Compensation row of the Termination upon Change in Control column in the table of Aggregate Termination Payments below. Additionally, restrictions would lapse on the following shares of restricted stock: Richard C. Kelly, 5,674.646 shares with an aggregate value of \$130,857; Benjamin G.S. Fowke III, 4,377.629 shares with an aggregate value of \$100,948; Paul J. Bonavia, 2,608.152 shares with an aggregate value of \$60,144; Patricia K. Vincent, 5,055.493 shares with an aggregate value of \$116,580; and Gary R. Johnson, 0 shares with an aggregate value of \$0.

To receive the benefits under the 2003 Policy, the participant must also sign an agreement releasing all claims against the employer and its affiliates and agreeing not to compete with the employer and its affiliates and not to solicit their employees and customers for one year.

Disability Benefits

Each of the Named Executive Officers would also be eligible for a disability benefit through the Xcel Energy Pension Plan in the event of a total and permanent disability. This disability benefit is generally available to all employees of the Company.

For participants in the Account Balance Benefit formula (Mr. Kelly and Mr. Bonavia), the monthly disability benefit payable from the Xcel Energy Pension Plan is equal to 60% of the participant's basic monthly earnings, reduced by any Social Security disability payments. This monthly annuity would be payable until normal retirement age, at which time the normal retirement benefit under the Xcel Energy Pension Plan would commence. The Nonqualified Pension Plan benefit would also be payable upon reaching normal retirement age. Mr. Kelly and Mr. Bonavia would also be eligible for the immediate commencement of a life annuity that is actuarially equivalent to their accrued SERP benefits at the time of disability.

For participants in the Traditional Benefit formula the monthly disability benefit payable from the Xcel Energy Pension Plan is equal to 1.4% of the participant's projected earnings multiplied by the participant's projected credited service (not more than 30 years). The projected earnings for this purpose are the final average earnings determined by projecting current pay to the participant's normal retirement age. Projected credited service is determined by projecting current service to the participant's normal retirement age. This monthly annuity would be payable until normal retirement age, at which time the normal retirement benefit under the Xcel Energy Pension Plan would commence. The Nonqualified Pension Plan benefit would also be payable upon reaching normal retirement age.

For participants in the Pension Equity Benefit formula (Mr. Fowke and Ms. Vincent), the monthly disability benefit payable from the Xcel Energy Pension Plan is equal to 1.2% of the participant's final average earnings at the time of disability multiplied by the participant's projected credited service.

Projected credited service is determined by projecting current service to the participant's normal retirement age. This monthly annuity would be payable until normal retirement age, at which time the normal retirement benefit under the Xcel Energy Pension Plan would commence. The Nonqualified Pension Plan benefit would also be payable upon reaching normal retirement age. Mr. Fowke and Ms. Vincent would also be eligible for the immediate commencement of a life annuity that is actuarially equivalent to their accrued SERP benefits at the time of disability.

Retirement Benefits

Upon retirement, the executive officers also will be entitled to receive the retirement benefits described above under the caption "Pension Benefits" on pages 52 to 57 and the nonqualified deferred compensation described under the caption "Nonqualified Deferred Compensation" on pages 58 to 59.

Outstanding Incentive Compensation Awards

As discussed above, pursuant to the terms of the Company's incentive compensation plans, upon a change in control, all stock-based awards, such as stock options and restricted stock, will vest immediately and all cash-based awards, such as performance shares and restricted stock units, will vest and be paid out immediately in cash as if the applicable performance goals had been obtained at target levels. Upon voluntary termination or involuntary termination with cause, all stock options (other than those issued to Mr. Johnson and those issued to the other NEOs on or after August 2000), restricted stock, restricted stock units and performance shares will be forfeited. Stock options issued to Mr. Johnson and those issued to the other NEOs on or after August 2000 will be exercisable for 3 months or their stated term, whichever is earlier, following a voluntary termination. Upon involuntary termination without cause, stock options issued prior to August 2000 to the NEOs other than Mr. Johnson will be forfeited, stock options issued to Mr. Johnson and those issued to the other NEOs on or after August 2000 will be exercisable for 36 months or their stated term, whichever is earlier, restrictions on the restricted stock held by Mr. Kelly and Mr. Bonavia will lapse, restricted stock held by Mr. Fowke and Ms. Vincent will be forfeited, restricted stock units and performance shares awarded in 2005 will continue to remain outstanding on their original terms and conditions, and restricted stock units and performance shares awarded in 2006 and 2007 will be forfeited. Upon retirement, all stock options will continue to be exercisable for their stated terms, restrictions on the restricted stock held by Mr. Kelly and Mr. Bonavia will lapse, restricted stock held by Mr. Fowke and Ms. Vincent will be forfeited, restricted stock units and performance shares awarded in 2005 will continue to remain outstanding on their original terms and conditions, and restricted stock units and performance shares awarded in 2006 and 2007 will be forfeited. Upon termination due to death or disability, stock options issued prior to August 2000 to the NEOs other than Mr. Johnson will be exercisable for 12 months or their stated term, whichever is earlier, stock options issued to Mr. Johnson and those issued to the other NEOs on or after August 2000, will be exercisable for 36 months or their stated term, whichever is earlier, restrictions will lapse on restricted stock, and restricted stock units and performance shares will continue to remain outstanding on their original terms and conditions, except that 2005 awards of performance shares will be paid on a prorated basis for the period of the performance cycle prior to termination.

Aggregate Termination Payments

Assuming that (i) the Named Executive Officers were terminated on December 31, 2006 and (ii) that the price of our common stock was \$23.06 (the closing price on December 29, 2006), then the Named Executive Officers would be entitled to the following payments upon a termination of employment or change in control:

	Termination upon Change in Control	Voluntary termination/ Retirement	Involuntary Termination with Cause	Involuntary Termination without Cause	Death	
Richard C. Kelly						
Severance Payments	\$ 6,300,000	\$ 0	\$ 0	\$ 5,437,300	\$ 0	
Retirement/Pension(1)	5,188,922	1,143,628	1,143,628	5,230,031	1,143,628	
Benefits(2)	496,557	0	0	199,147	0	
Incentive Compensation(3)	7,009,207	(4) 0	(5) 0	0	(5) 1,442,376	(6)
Tax gross-up	5,802,138	0	0	0	0	
Paid-time-off (PTO) cash out	185,769	185,769	185,769	185,769	185,769	
Total	\$ 24,982,593	\$ 1,329,397	\$ 1,329,397	\$ 11,052,247	\$ 2,771,773	
Benjamin G.S. Fowke						
Severance Payments	\$ 2,475,000	\$ 0	\$ 0	\$ 2,100,200	\$ 0	
Retirement/Pension(1)	1,030,993	106,595	106,595	780,292	106,595	
Benefits(2)	185,688	0	0	47,131	0	
Incentive Compensation(3)	2,026,053	(4) 0	(7) 0	0	(7) 438,546	(6)
Tax gross-up	1,752,378	0	0	0	0	
PTO cash out	71,315	71,315	71,315	71,315	71,315	
Total	\$ 7,541,427	\$ 177,910	\$ 177,910	\$ 2,998,938	\$ 616,456	
Paul J. Bonavia						
Severance Payments	\$ 3,813,053	\$ 4,100,000	\$ 0	\$ 4,100,000	\$ 4,100,000	
Retirement/Pension(1)	2,169,061	106,922	106,922	0	106,922	
Benefits(2)	156,620	0	0	119,696	0	
Incentive Compensation(3)	2,046,232	(4) 0	(5) 0	0	(5) 421,540	(6)
Tax gross-up	3,663,542	0	0	0	0	
PTO cash out	97,058	97,058	97,058	97,058	97,058	
Total	\$ 11,945,566	\$ 4,303,980	\$ 203,980	\$ 4,316,754	\$ 4,725,520	
Patricia K. Vincent						
Severance Payments	\$ 2,092,500	\$ 0	\$ 0	\$ 1,762,500	\$ 0	
Retirement/Pension(1)	865,301	143,099	143,099	642,222	143,099	
Benefits(2)	160,197	0	0	35,299	0	
Incentive Compensation(3)	1,764,674	(4) 0	(7) 0	0	(7) 311,669	(6)
Tax gross-up	1,317,775	0	0	0	0	
PTO cash out	74,423	74,423	74,423	74,423	74,423	
Total	\$ 6,274,870	\$ 217,522	\$ 217,522	\$ 2,514,444	\$ 529,191	
Gary R. Johnson(8)						
Severance Payments	\$ 1,906,500	\$ 0	\$ 0	\$ 1,581,700	\$ 0	
Retirement/Pension(1)	1,081,861	1,071,664	1,071,664	1,071,664	1,071,664	
Benefits(2)	205,393	0	0	72,893	0	
Incentive Compensation(3)	1,483,034	(4) 0	(7) 0	0	(7) 272,657	(6)
Tax gross-up	1,375,201	0	0	0	0	
PTO cash out	25,231	25,231	25,231	25,231	25,231	
Total	\$ 6,077,220	\$ 1,096,895	\$ 1,096,895	\$ 2,751,488	\$ 1,369,552	

(1) Represents the actuarial present value of pension benefits that would be received upon a specified termination event over and above those included in the Pension Benefits table on page 52, which the executive officers also would be entitled to receive. The amounts shown in the Pension Benefits table are based on prescribed assumptions for age at payment, interest rate and mortality. In the event of immediate termination of employment, benefits would be calculated using actual assumptions set forth in the pension plan documents, which differ from the prescribed assumptions used for purposes of calculating the actuarial present value of accumulated benefits for the Pension Benefits table. In addition, the retirement benefits payable subsequent to specific events (for example, a change in control) will be modified as described above. The retirement amounts shown in this section represent the increase, if any, in the present value of pension benefits due

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to the difference in assumptions for age at payment, interest rates and mortality. These amounts also reflect the increase due to changes in benefit level required for the specific termination event identified in the table.

- (2) For these purposes we have assumed that health care costs will increase at the rate of 5% per year.
- (3) In addition, executive officers will have the ability, under the circumstances outlined in Outstanding Incentive Compensation Awards, to exercise the stock options set forth in the Outstanding Equity Awards at Fiscal Year-End table on page 49 .
- (4) Represents the dollar value of all performance shares and restricted stock units that will vest and be paid out immediately in cash as if the applicable performance goals had been obtained at target levels. Does not include the value of restricted stock for which restrictions would lapse, which values are set forth under 2003 Severance and Change in Control Policy above.
- (5) Does not include the value of restricted stock for which restrictions would lapse upon retirement or involuntary termination without cause, which values are set forth under 2003 Severance and Change in Control Policy above, or the value of restricted stock units and performance shares awarded in 2005, which will remain outstanding on their original terms and conditions upon retirement or involuntary termination without cause.
- (6) Represents payout of earned annual incentive awards. This amount also is included in the Non-Equity Incentive Plan Compensation column of the Summary Compensation Table. Does not include the value of restricted stock for which restrictions would lapse upon, which values are set forth under 2003 Severance and Change in Control Policy above, or the value of restricted stock units and performance shares, which will remain outstanding on their original terms and conditions, except that 2005 awards of performance shares will be paid on a prorated basis for the period of the performance cycle prior to termination.
- (7) Does not include the value of restricted stock units and performance shares awarded in 2005, which will remain outstanding on their original terms and conditions upon retirement.
- (8) As explained above, Mr. Johnson retired on March 31, 2007. The benefits he actually will receive are discussed above under the caption Gary R. Johnson Retirement Agreement .

SECURITIES AUTHORIZED FOR ISSUANCE UNDER EQUITY COMPENSATION PLANS

Plan Category	Number of securities to be issued upon exercise of outstanding options, warrants and rights	Weighted-average exercise price of outstanding options, warrants and rights	Number of securities remaining available for future issuance under equity compensation plans (excluding securities reflected in the first column)
Equity compensation plans approved by security holders ⁽¹⁾	14,932,908	\$ 27.36	8,579,103
Equity compensation plans not approved by security holders	n/a	n/a	(2)

(1) Plan Category	Number of securities to be issued upon exercise of outstanding options, warrants and rights	Weighted-average exercise price of outstanding options, warrants and rights	Number of securities remaining available for future issuance under equity compensation plans (excluding securities reflected in the first column)
PSCo Omnibus Incentive Plan	55,645	\$ 25.16	
Xcel Energy Inc. 2005 Omnibus Incentive Plan	926,952 (3)	\$ N/A	7,396,848 (4)
Xcel Energy Inc. Omnibus Incentive Plan	7,770,303 (3)	\$ 26.54	(5)
NRG Long-Term Incentive Compensation Plan	1,579,222	\$ 35.45	
NCE Omnibus Incentive Plan	2,907,389	\$ 26.43	
NSP Executive Long-Term Incentive Award Stock Plan	1,414,958	\$ 24.10	
Xcel Energy Inc. Executive Annual Incentive Award Plan (Effective May 25, 2005)	17,746	\$ N/A	1,182,254
Xcel Energy Inc. Executive Annual Incentive Award Plan	260,693		(6)
Stock Equivalent Plan for Non-Employee Directors	200,306		549,694

(2) Xcel Energy had a Stock Equivalent Plan for Non-Employee Directors to more closely align directors' interests with those of our shareholders. Under this Stock Equivalent Plan, directors could receive an annual award of stock equivalent units with each unit having a value equal to one share of our common stock. Stock equivalent units do not entitle a director to vote and are only payable as a distribution of whole shares of the Company's common stock upon a director's termination of service. The stock equivalent units fluctuate in value as the value of our common stock fluctuates. Additional stock equivalent units are accumulated upon the payment of, and at the same value as, dividends declared on Xcel Energy common stock. The shareholders approved an amended and restated plan at the 2004 annual meeting. For awards made prior to this shareholder approval, the number of shares of the Company's common stock to be used for distribution under this Stock Equivalent Plan are purchased on the open market.

(3) Includes stock options, performance shares, performance-based restricted stock units and reinvested dividend equivalents with respect to performance-based restricted stock units. For performance shares, the actual number of securities to be paid out will be dependent upon Xcel

Energy's TSR compared to a peer group. Performance-based restricted stock units are subject to forfeiture as described under Long-Term Incentives in Compensation Discussion and Analysis above.

(4) Awards can take the form of stock options, stock appreciation rights, restricted stock, restricted stock units, performance shares or performance units.

(5) The Xcel Energy Inc. 2005 Omnibus Incentive Plan was approved by shareholders at the 2005 annual meeting and replaces the Xcel Energy Inc. Omnibus Incentive Plan approved by shareholders in 2000. No additional awards will be made under the Xcel Energy Inc. Omnibus Incentive Plan.

(6) The Xcel Energy Inc. Executive Annual Incentive Plan (Effective May 25, 2005) was approved by shareholders at the 2005 annual meeting and replaces the Xcel Energy Inc. Executive Annual Incentive Plan approved by shareholders in 2000. No additional awards will be made under the Xcel Energy Inc. Executive Annual Incentive Plan.

REPORT OF THE AUDIT COMMITTEE OF THE BOARD OF DIRECTORS

The role of the Audit Committee is to assist the Board of Directors in its oversight of the Company's financial reporting process. The Audit Committee is composed of Roger R. Hemminghaus, Chair, Fredric W. Corrigan, Douglas W. Leatherdale, Albert F. Moreno, Margaret R. Preska and Timothy V. Wolf.

The Board of Directors, in its business judgment, has determined that all members of the Audit Committee are independent, as required by the listing standards of the New York Stock Exchange. The Audit Committee operates pursuant to a charter that was last amended and restated by the Audit Committee on March 1, 2005 and approved by the Board on March 2, 2005. The Audit Committee reviewed and reaffirmed the charter without change on January 31, 2006. As set forth in the charter, management of the Company is responsible for the preparation, presentation, and integrity of the Company's financial statements, the Company's accounting and financial reporting principles and internal controls and procedures designed to assure compliance with accounting standards and applicable laws and regulations. Our independent auditors, Deloitte & Touche LLP, are responsible for auditing the Company's consolidated financial statements and expressing an opinion as to whether they are presented fairly, in all material respects, in conformity with accounting principles generally accepted in the United States of America.

In the performance of its oversight function, the Audit Committee has:

- Considered and discussed the audited financial statements with management and our independent auditors. The Audit Committee's review included a discussion of the quality, not just the acceptability, of the accounting principles, the reasonableness of significant judgments and the clarity of disclosures in the financial statements;
- Discussed with our independent auditors the matters required to be discussed by Statements on Auditing Standards No. 61, *Communication with Audit Committees* as amended, as adopted by the Public Company Accounting Oversight Board in Rule 3200T;
- Received the written disclosures and the letter from our independent auditors required by Independence Standards Board Standard No. 1, *Independence Discussions with Audit Committees*, as adopted by the Public Company Accounting Oversight Board, and discussed the independence of Deloitte & Touche LLP with them;

- Reviewed and pre-approved the services provided by our independent auditors other than their audit services and considered whether the provision of such other services by our independent auditors is compatible with maintaining their independence; and
- Discussed with the Company's internal and independent auditors the overall scope and plans for their respective audits for the year 2007. The Audit Committee meets with the internal and independent auditors, with and without management present, to discuss the results of their examinations, their evaluations of the Company's internal controls and the overall quality of the Company's financial reporting.

Based upon the reports and discussions described in this report, and subject to the limitations on the role and responsibilities of the Audit Committee referred to in the charter, the Audit Committee recommended to the Board of Directors, and the Board has approved, that the audited financial statements be included in our Annual Report on Form 10-K for the year ended December 31, 2006, to be filed with the Securities and Exchange Commission. The Audit Committee has appointed Deloitte & Touche LLP as the Company's independent auditors for 2007. Shareholder ratification of this appointment is included as Proposal No. 2 in these proxy materials.

Submitted by the Audit Committee of the Xcel Energy Board of Directors

Roger R. Hemminghaus, Chair
Fredric W. Corrigan
Douglas W. Leatherdale

Albert F. Moreno
Margaret R. Preska
Timothy V. Wolf*

* Mr. Wolf became a member of the Audit Committee, effective January 30, 2007. He joins in the report of the Audit Committee to the extent it covers the period for which he served on the Committee during 2007.

INDEPENDENT PUBLIC ACCOUNTANTS

Deloitte & Touche LLP has audited the Company's consolidated financial statements since 2002. Audit services provided by Deloitte & Touche LLP in 2006 included the audits of consolidated financial statements and management's assessment of internal control over financial reporting of the Company; reviews of interim consolidated financial information; and consultation on matters related to accounting and financial reporting. Representatives of Deloitte & Touche LLP will be present at the Annual Meeting and will have the opportunity to make a statement if they so desire. Such representatives will be available to respond to appropriate questions from shareholders at the Annual Meeting.

Independent Public Accountants Fees

For the years ended December 31, 2006 and December 31, 2005, professional services were performed by Deloitte & Touche LLP, the member firms of Deloitte Touche Tohmatsu and their respective affiliates (collectively, Deloitte & Touche). Total fees paid to Deloitte & Touche in 2006 and 2005 were \$6,197,000 and \$5,421,000, respectively.

Audit Fees

The aggregate audit fees include fees billed for the audit of the Company's and subsidiaries annual financial statements, management's assessment of the Company's internal control over financial reporting and for the reviews of the financial statements included in the Company's Quarterly Reports on Form 10-Q. These amounts include estimated billings for the completion of the audits,

which billings were rendered after the year-end being audited. Total audit fees for 2006 and 2005 were \$5,188,000 and \$4,207,000, respectively.

Audit-Related Fees

The aggregate fees billed for audit-related services for the fiscal year ended December 31, 2006 were \$630,000. These fees included \$413,000 for agreed upon procedures related to the Southwestern Public Service Company rate case, \$179,000 for employee benefit plan audits and \$38,000 for other audits and accounting consultation.

The aggregate fees billed for audit-related services for the fiscal year ended December 31, 2005 were \$335,000. These fees included \$164,000 for employee benefit plan audits and \$171,000 for other audits and accounting consultation.

Tax Fees

The aggregate fees billed for tax services for the fiscal year ended December 31, 2006 were \$379,000. These fees included \$237,000 for other tax compliance services, and \$142,000 for other tax planning services.

The aggregate fees billed for tax services for the fiscal year ended December 31, 2005 were \$879,000. These fees included \$179,000 for tax planning and compliance services related to the Company's investment in NRG, which was divested in 2003, \$340,000 for other tax compliance services, and \$360,000 for other tax planning services.

All Other Fees

There were no other fees billed for the fiscal years ended December 31, 2006 and December 31, 2005.

Audit Committee Pre-Approval Policies

Rules adopted by the Securities and Exchange Commission in order to implement requirements of the Sarbanes-Oxley Act require public company audit committees to pre-approve audit and non-audit services. Our Audit Committee has adopted detailed pre-approval policies and procedures pursuant to which audit, audit-related and tax services, and all permissible non-audit services, are pre-approved by category of service. The fees are budgeted, and actual fees versus the budget are monitored throughout the year. During the year, circumstances may arise when it may become necessary to engage the independent auditor for additional services not contemplated in the original pre-approval. In those instances, we will obtain the specific pre-approval of the Audit Committee before engaging the independent auditor. The policies require the Audit Committee to be informed of each service, and the policies do not include any delegation of the Audit Committee's responsibilities to management. The Audit Committee may delegate pre-approval authority to one or more of its members. The member to whom such authority is delegated will report any pre-approval decisions to the Audit Committee at its next scheduled meeting.

All audit-related fees, tax fees and all other fees for 2006 were pre-approved by the Audit Committee.

Leased Employees

In connection with their audit of our 2006 annual financial statements, Deloitte & Touche's work was performed 100% by full-time, permanent employees of Deloitte & Touche.

OTHER BUSINESS

Management does not know of any business, other than that described in this proxy statement, that may be presented for action at the Annual Meeting of Shareholders. If any other matters are properly presented at the Annual Meeting for action, the persons named in the accompanying proxy will vote upon them in accordance with their best judgment.

By Order of the Board of Directors,

CATHY J. HART
Corporate Secretary

Minneapolis, Minnesota

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Annual Meeting Guidelines

In the interest of an orderly and constructive meeting, the following guidelines will apply to Xcel Energy's 2007 Annual Meeting of Shareholders:

1. The Annual Meeting of Shareholders is open only to Xcel Energy shareholders and Xcel Energy's invited guests. Shareholders attending the Annual Meeting should present an admittance ticket or evidence of Xcel Energy Inc. stock ownership to gain entrance. All attendees will be asked to provide photo identification, such as a driver's license, in order to gain admittance to the Annual Meeting. You will not be admitted without photo identification.
 2. The business of the meeting will follow as set forth in the agenda, which you will receive at the meeting entrance. If you wish to change your vote or have not voted, ballots will be distributed to you to cast your votes.
 3. Shareholder questions and comments related to the business of the Company will be addressed only during the question and answer portion of the agenda at the end of the Annual Meeting.
 4. If you wish to speak at the designated time in the question and answer portion of the Annual Meeting, please go to the nearest microphone and state your name before asking a question. You must ask a question and direct it to the Chairman. Questions from the floor are limited to three minutes to provide an opportunity for as many shareholders as possible.
 5. Although personal grievances, claims and political statements are not appropriate subjects for the Annual Meeting, you may submit any of these to an usher or Company representative and the Company will respond in writing.
 6. The use of cameras or sound recording equipment is prohibited, except by those employed by the Company to provide a record of the proceedings. The use of cell phones and other personal communication devices also is prohibited during the Annual Meeting.
 7. No firearms or weapons will be allowed in the meeting room.
 8. No banners, packages or signs will be allowed in the meeting room.
 9. Individuals wishing to gain admittance to the Annual Meeting will pass through a metal detector.
 10. Xcel Energy reserves the right to inspect all items entering the meeting room. Handbags and briefcases will be inspected.
-

ADMISSION TICKET

2007 Annual Meeting of Shareholders

Wednesday, May 23, 2007, 10:00 A.M. CDT

Doors will open at 9:00 A.M. MDT

The Minneapolis Convention Center
1301 Second Avenue South
Minneapolis, Minnesota

Shareholders who do not present an admission ticket or verification of ownership will not be admitted to the meeting.

Photo identification is required for admission.

Attached below is your proxy card for the 2007 Annual Meeting of Shareholders of Xcel Energy Inc.

You may vote by telephone, by Internet or by mail.

To vote by telephone or Internet, see instructions on reverse side.

To vote by mail, please return your proxy in the enclosed business reply envelope.

Proxy for Annual Meeting of Shareholders May 23, 2007

The undersigned, a holder of common and/or preferred stock of Xcel Energy Inc.(the Company) hereby appoints Benjamin G.S.Fowke III and Cathy J.Hart, or any one or more of them, as proxies with full power of substitution, to represent the undersigned at the Annual Meeting of Shareholders of the Company to be held on May23, 2007 and any adjournment or adjournments thereof, and to vote as designated hereon and in their discretion with respect to any other business properly brought before the Annual Meeting all shares of the common and/or preferred stock of the Company which the undersigned would be entitled to vote if personally present at such meeting, except for the shares of common stock held of record in the undersigned s account with the Plans (defined below), the voting instructions for which are explained below.

THIS CARD ALSO CONSTITUTES YOUR VOTING INSTRUCTIONS FOR SHARES HELD OF RECORD IN THE NEW CENTURY ENERGIES,INC. EMPLOYEES SAVINGS AND STOCK OWNERSHIP PLAN FOR BARGAINING UNIT EMPLOYEES AND FORMER NON-BARGAINING UNIT EMPLOYEES,THE XCEL ENERGY 401(K) SAVINGS PLAN AND THE NEW CENTURY ENERGIES,INC. EMPLOYEE INVESTMENT PLAN FOR BARGAINING UNIT EMPLOYEES AND FORMER NON-BARGAINING UNIT EMPLOYEES (PLANS) AND THE UNDERSIGNED HEREBY AUTHORIZES THE TRUSTEES OF THESE PLANS TO VOTE THE UNDERSIGNED S SHARES HELD IN ITS ACCOUNTS.

ADDRESS CHANGE/COMMENTS

XCEL ENERGY INC.

This proxy when properly executed will be voted in the manner designated hereon and in the discretion of the proxies with respect to any other matters properly

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brought before the meeting. If no direction is made, this proxy will be voted FOR items 1 and 2 and AGAINST items 3 and 4.

(CONTINUED AND IS TO BE SIGNED ON REVERSE SIDE)

**YOUR VOTE IS IMPORTANT
VOTE BY INTERNET / TELEPHONE
24 HOURS A DAY, 7 DAYS A WEEK**

VOTE BY INTERNET

<https://www.proxypush.com/xel>

- Go to the website address listed above.
- **Have your proxy card ready.**
- Follow the simple instructions that appear on your computer screen.

VOTE BY TELEPHONE

1-866-697-7120

- Use any touch-tone telephone.
- **Have your proxy card ready.**
- Follow the simple recorded instructions.

VOTE BY MAIL

- Mark, sign and date your proxy card.
- Detach your proxy card.
- Return your proxy card in the postage-paid envelope provided.

OR

OR

If you have submitted your proxy by telephone or the Internet there is no need for you to mail back your proxy.

ELECTRONIC DELIVERY OF SHAREHOLDER MATERIALS

Reduce paper mailed to your home and help lower Xcel's printing and mailing costs. We are pleased to offer our shareholders the benefits and convenience of viewing proxy statements, proxy cards and annual reports on-line. To sign up for electronic delivery, please follow the instructions above to vote using the Internet and, when prompted, indicate that you agree to receive or access shareholder materials electronically in future years. You may also enroll at anytime by visiting <https://www.proxyconsent.com/xel> and follow the instructions provided.

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CALL TOLL-FREE TO VOTE

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X

Votes MUST be indicated (X) in Black or Blue ink

The Board of Directors recommends a vote FOR items 1 and 2 and AGAINST items 3 and 4.

1. To elect a board of directors

2. To ratify the appointment of Deloitte & Touche LLP as Xcel Energy Inc.'s principal independent

FOR AGAINST ABSTAIN

O O O

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accountants for 2007

FOR	WITHHOLD	EXCEPTIONS*			
ALL	FOR ALL		O	O	O
Nominees: 01 - C. Coney Burgess, 02 - Fredric W. Corrigan, 03 - Richard K. Davis, 04 - Roger R. Hemminghaus, 05 - A. Barry Hirschfeld, 06 - Richard C. Kelly, 07 - Douglas W. Leatherdale, 08 - Albert F. Moreno, 09 - Dr. Margaret R. Preska, 10 - A. Patricia Sampson, 11 - Richard H. Truly, 12 - David A. Westerlund and 13 - Timothy V. Wolf			O	O	O
			O	O	O

3. Shareholder proposal relating to the separation of the role of chairman of the board and chief executive officer

4. Shareholder proposal relating to financial performance criteria for the Company's executive compensation plans

(Instructions: To withhold authority to vote for any individual nominee, mark the

Exceptions box and write that nominee's name on the following blank line.)

To change your address, please mark this box.

*Exceptions

To include any comments, please mark this box.

				SCAN LINE		
				The signer(s) hereby acknowledge(s) receipt of the Notice of Annual Meeting of Shareholders and accompanying Proxy Statement. The signer(s) hereby revoke(s) all proxies heretofore given by the signer(s) to vote at said Annual Meeting and any adjournments or postponements thereof. NOTE: Please sign exactly as name appears herein. Joint owners should each sign. When signing as attorney, executor, administrator, trustee or guardian, please give full title as such.		
				Date	Share Owner sign here	Co-owner sign here