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

FORM 10-Q

(Mark One)

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

For the quarterly period ended March 31, 2016

OR

☐ **TRANSITION REPORT UNDER SECTION 13 OF 15(d) OF THE EXCHANGE ACT OF 1934**

From the transition period from to .

Commission File Number 001-35798

KALOBIOS PHARMACEUTICALS, INC.

(Exact name of registrant as specified in its charter)

Delaware	**77-0557236**
(State or other jurisdiction of incorporation)	(IRS Employer Identification No.)

1000 Marina Blvd., Suite 250, Brisbane, CA 94005
(Address of principal executive offices)
(Zip Code)

Registrant's telephone number, including area code: **(650) 243-3100**

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 ☒

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

As of September 22, 2016, there were 14,903,022 shares of common stock of the issuer outstanding.

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PART I. FINANCIAL INFORMATION

Item 1. Financial Statements

KaloBios Pharmaceuticals, Inc. (Debtor-In-Possession)
Condensed Consolidated Balance Sheets
(in thousands, except share and per share data)
(Unaudited)

	March 31, 2016	December 31, 2015
Assets		
Current assets:		
Cash and cash equivalents	$ 6,577	$ 8,431
Prepaid expenses and other current assets	1,696	1,963
Total current assets	8,273	10,394
Property and equipment, net	170	288
Restricted cash	50	193
Other assets	-	271
Total assets	$ 8,493	$ 11,146
Liabilities and stockholders' equity		
Current liabilities:		
Accounts payable	$ 3,211	$ -
Accrued compensation	32	-
Other accrued liabilities	75	-
Total current liabilities	3,318	-
Liabilities subject to compromise	4,867	5,414
Total liabilities	8,185	5,414
Stockholders' equity:		
Common stock, $0.001 par value: 85,000,000 shares authorized at March 31, 2016 and December 31, 2015; 4,450,994 shares issued and outstanding at March 31, 2016 and December 31, 2015	4	4
Additional paid-in capital	219,321	219,319
Accumulated deficit	(219,017)	(213,591)
Total stockholders' equity	308	5,732
Total liabilities and stockholders' equity	$ 8,493	$ 11,146

See accompanying notes.

KaloBios Pharmaceuticals, Inc. (Debtor-In-Possession)
Condensed Consolidated Statements of Operations and Comprehensive Loss
(in thousands, except share and per share data)
(Unaudited)

	Three Months Ended March 31,	
	2016	**2015**
Operating expenses:		
Research and development	$ 1,704	$ 5,905
General and administrative	1,205	3,437
Total operating expenses	2,909	9,342
Loss from operations	(2,909)	(9,342)
Other (expense) income:		
Interest expense	-	(280)
Interest income	-	16
Other expense, net	-	(16)
Reorganization items, net	(2,517)	-
Net loss	(5,426)	(9,622)
Other comprehensive income:		
Net unrealized gains on marketable securities	-	6
Comprehensive loss	$ (5,426)	$ (9,616)
Basic and diluted net loss per common share	$ (1.22)	$ (2.33)
Weighted average common shares outstanding used to calculate basic and diluted net loss per common share	4,450,994	4,124,022

See accompanying notes.

KaloBios Pharmaceuticals, Inc. (Debtor-In-Possession)
Condensed Consolidated Statements of Cash Flows
(in thousands, except share and per share data)
(Unaudited)

	Three Months Ended March 31,	
	2016	2015
Operating activities:		
Net loss	$ (5,426)	$ (9,622)
Adjustments to reconcile net loss to net cash used in operating activities:		
Depreciation and amortization	33	48
Gain on lease termination	(227)	-
Noncash interest expense	-	56
Financing derivative	-	3
Amortization of premium on marketable securities	-	80
Stock based compensation expense	2	305
Modification of stock options related to executive retirement	-	389
Modification of stock options related to restructuring activities	-	414
Changes in operating assets and liabilities:		
Prepaid expenses and other assets	538	583
Accounts payable	3,211	(965)
Accrued compensation	32	(133)
Accrued research and clinical liabilities	-	(159)
Other liabilities	75	(13)
Deferred rent	-	(1)
Liabilities subject to compromise	(235)	-
Net cash used in operating activities	(1,997)	(9,015)
Investing activities:		
Purchase of marketable securities	-	(3,703)
Proceeds from maturities of marketable securities	-	15,822
Purchases of property and equipment	-	(108)
Changes in restricted cash	143	-
Net cash provided by investing activities	143	12,011
Financing activities:		
Principal payments under notes payable	-	(1,295)
Net cash used infinancing activities	-	(1,295)
Net (decrease) increase in cash and cash equivalents	(1,854)	1,701
Cash and cash equivalents, beginning of period	8,431	10,923
Cash and cash equivalents, end of period	$ 6,577	$ 12,624
Supplemental cash flow disclosure:		
Cash paid for interest	$ -	$ 233

See accompanying notes.

KaloBios Pharmaceuticals, Inc. (Debtor-In-Posession)
Notes to Condensed Consolidated Financial Statements
(Unaudited)

1. Organization and Description of Business

Description of the Business

KaloBios Pharmaceuticals, Inc. (the "Company") is a biopharmaceutical company focused on developing medicines for patients with neglected and rare diseases, with an ancillary focus on pediatric conditions, and on executing its Responsible Pricing Model in the commercialization of the Company's product candidates that may be approved. The Company's lead product candidate is benznidazole for the treatment of Chagas disease, a parasitic illness that can lead to long-term heart, intestinal and neurological problems. As more fully described in Note 11, the Company acquired certain worldwide rights to benznidazole on June 30, 2016. The Company is developing one of its proprietary monoclonal antibodies, lenzilumab (formerly known as KB003), for the treatment of chronic myelomonocytic leukemia and potentially for the treatment of juvenile myelomonocytic leukemia, both of which are rare hematologic cancers with high unmet medical need. The Company is exploring partnering another of its proprietary monoclonal antibodies, ifabotuzumab (formerly known as KB004), for the treatment of certain rare solid and hematologic cancers. With a focus on neglected, rare and orphan diseases, the Company believes that it has the opportunity to benefit from various regulatory incentives, such as orphan drug exclusivity, breakthrough therapy designation, fast track designation, accelerated approval, priority review and priority review vouchers ("PRV"), where available, that provide for certain periods of exclusivity, expedited review and/or other benefits.

The Company has undergone a significant transformation in the last year. As a result of challenges facing it at the time, on December 29, 2015, the Company filed a voluntary petition for bankruptcy protection under Chapter 11 of Title 11 of the U.S. Bankruptcy Code. On June 30, 2016, the Company's Second Amended Plan of Reorganization, dated May 9, 2016, as amended (the "Plan"), became effective and the Company emerged from its Chapter 11 bankruptcy proceedings. Refer to Note 2 for additional details regarding the Company's bankruptcy proceedings.

The Company was incorporated on March 15, 2000 in California and reincorporated as a Delaware corporation in September 2001. All of the Company's assets are located in California.

Liquidity and Going Concern

The Company has incurred significant losses and had an accumulated deficit of $219.0 million as of March 31, 2016. The Company has financed its operations primarily through the sale of equity securities, debt financings, interest income earned on cash and cash equivalents, grants and the payments received under its agreements with Novartis Pharma AG ("Novartis") and Sanofi Pasteur S.A. ("Sanofi"). The Company completed its initial public offering in February 2013. To date, none of the Company's product candidates have been approved for sale and therefore the Company has not generated any revenue from product sales. Management expects operating losses to continue for the foreseeable future. As a result, the Company will continue to require additional capital through equity offerings, debt financing and/or payments under new or existing licensing or collaboration agreements. If sufficient funds are not available on acceptable terms when needed, the Company could be required to significantly reduce its operating expenses and delay, reduce the scope of, or eliminate one or more of its development programs. The Company's ability to access capital when needed is not assured and, if not achieved on a timely basis when needed, could materially harm its business, financial condition and results of operations. These conditions raise substantial doubt about the Company's ability to continue as a going concern.

The Condensed Consolidated Financial Statements for the quarterly period ended March 31, 2016 were prepared on the basis of a going concern, which contemplates that the Company will be able to realize assets and discharge liabilities in the normal course of business. The ability of the Company to meet its total liabilities of $8.2 million at March 31, 2016 and to continue as a going concern is dependent upon the availability of future funding. The financial statements do not include any adjustments that might be necessary if the Company is unable to continue as a going concern.

Delisting of Common Stock

On January 13, 2016, the Company's common stock was suspended from the Nasdaq Global Market and began trading on the over-the-counter market under the ticker symbol KBIOQ. On January 26, 2016, NASDAQ filed a Form 25 with the Securities and Exchange Commission to complete the delisting of the common stock, and the delisting was effective on February 5, 2016.

Basis of Presentation

The accompanying interim unaudited Condensed Consolidated Financial Statements have been prepared in accordance with U.S. generally accepted accounting principles ("U.S. GAAP") for interim financial information and on a basis consistent with the annual consolidated financial statements and include all adjustments necessary for the presentation of the Company's condensed consolidated financial position, results of operations and cash flows for the periods presented. The Condensed Consolidated Financial Statements include the accounts of the Company and its wholly owned subsidiaries. These financial statements have been prepared on a basis that assumes that the Company will continue as a going concern, which contemplates the realization of assets and the satisfaction of liabilities and commitments in the normal course of business. The December 31, 2015 Condensed Consolidated Balance Sheet was derived from the audited financial statements but does not include all disclosures required by U.S. GAAP. These interim financial results are not necessarily indicative of the results to be expected for the year ending December 31, 2016, or for any other future annual or interim period. The accompanying unaudited Condensed Consolidated Financial Statements should be read in conjunction with the audited consolidated financial statements and the related notes thereto included in the 2015 Annual Report.

The preparation of financial statements in conformity with U.S. GAAP requires management to make estimates and assumptions that affect the amounts and disclosures reported in the Condensed Consolidated Financial Statements and accompanying notes. Actual results could differ materially from those estimates. The Company believes judgment is involved in determining the valuation of the financing derivative, the fair value-based measurement of stock-based compensation, accruals and warrant valuations. The Company evaluates its estimates and assumptions as facts and circumstances dictate. As future events and their effects cannot be determined with precision, actual results could differ from these estimates and assumptions, and those differences could be material to the Condensed Consolidated Financial Statements.

2. Chapter 11 Filing

On December 29, 2015, the Company filed a voluntary petition for bankruptcy protection under Chapter 11 of the U.S. Bankruptcy Code. The filing was made in the United States Bankruptcy Court for the District of Delaware (the "Bankruptcy Court") (Case No. 15-12628 (LSS)).

In connection with financing efforts as part of the Company's bankruptcy proceedings, on April 1, 2016, the Company entered into a Debtor-in-Possession Credit and Security Agreement (the "Credit Agreement") with a group of lenders (the "DIP Lenders"), pursuant to which the Company received $3 million in funds for working capital, bankruptcy-related costs, costs related to its plan of reorganization, payment of certain fees to the DIP Lenders and other costs associated with the ordinary course of business. Funds received under the Credit Agreement bore interest at a rate of 12% and were due and payable upon the Effective Date of the Plan, as defined below. Payment due under the Credit Agreement was convertible into shares of the Company's common stock, with share amounts subject to calculation as provided in the Credit Agreement.

On April 1, 2016, the Company also entered into a Securities Purchase Agreement (the "SPA") with the DIP Lenders. The SPA provided for the sale of the Company's common stock, with share amounts subject to calculation as provided in the SPA, in respect of exit financing in the amount of $11,000,000 to be received upon the Effective Date of the Plan, as defined below.

Refer to Note 13 for additional information on the Credit Agreement and the SPA.

Plan of Reorganization

On May 9, 2016, the Company filed with the Bankruptcy Court the Plan and related amended disclosure statement pursuant to Chapter 11 of the Bankruptcy Code. On June 16, 2016, the Bankruptcy Court entered an order confirming the Plan.

The Plan became effective on June 30, 2016 (the "Effective Date") and the Company emerged from its Chapter 11 bankruptcy proceedings. In connection with such emergence, as further described in Note 13, the Company consummated the transactions and other items described below.

- Pursuant to the SPA and in repayment of its obligations under the Credit Agreement, the Company issued an aggregate of 9,497,515 shares of its common stock to the DIP Lenders.
- The Company became obligated to issue 327,608 shares of common stock to the plaintiffs in litigation related to the Company's 2015 private financing transaction in accordance with the settlement stipulation discussed in Note 13 below. The Company recorded an obligation in stockholders' equity to issue the related shares and recorded the related expense of approximately $1.5 million as of December 31, 2015.
- The Company reserved 300,000 shares of common stock for issuance to the plaintiffs in class action litigation related to the events surrounding the Company's former Chairman and Chief Executive Officer. The Company recorded an obligation in stockholders' equity to issue the related shares and recorded the related expense of approximately $1.3 million as of December 31, 2015.
- The Company became obligated to issue 3,750 shares of common stock to a former director in satisfaction of claims against the Company. The Company recorded an obligation in stockholders' equity to issue the related shares and recorded the related expense of approximately $16,000 as of December 31, 2015.
- The Company reserved for issuance shares of common stock in an amount as yet to be determined in connection with the settlement of certain other claims and interests as set forth in the Plan. As of March 31, 2016, management does not believe the issuance of additional common stock for any such claims is probable. As such, no accrual has been made in the Condensed Consolidated Financial Statements.
- The Company issued promissory notes in an aggregate principal amount of approximately $1.2 million to certain vendors in accordance with the Plan. The notes are unsecured, bear interest at 10% per annum and will be due and payable in full, including principal and accrued interest, on June 30, 2019.

Pre-Petition Claims

On February 29, 2016, the Company filed its schedules of assets and liabilities and statement of financial affairs (the "Schedules") with the Bankruptcy Court. The Bankruptcy Court entered an order setting April 1, 2016 as the deadline for filing proofs of claim (the "Bar Date"). The Bar Date is the date by which non-government claims against the Company relating to the period prior to the commencement of the Company's Chapter 11 case must be filed if such claims are not listed in liquidated, non-contingent and undisputed amounts in the Schedules, or if the claimant disagrees with the amount, characterization or classification of its claim as reflected in the Schedules. Claims that are subject to the Bar Date and that were not filed on or prior to the Bar Date may be barred from participating in any distribution that may be made under a plan of reorganization in the Company's Chapter 11 case.

As of the Effective Date, approximately 195 proofs of claim were outstanding (including claims that were previously identified on the Schedules) totaling approximately $32 million. Prior to the Bar Date, certain investors filed a class action claim in the amount of $20 million in connection with events surrounding the Company's former Chairman and Chief Executive Officer. On June 16, 2016, a settlement stipulation related to the class action suit was approved under order of the Bankruptcy Court. The settlement stipulation required the Company to issue 300,000 shares of common stock and submit a payment of $250,000 to the claimants. See Note 12 for additional information on this matter and settlement. Separately, a claim was filed by certain investors in the Company's 2015 private financing transaction totaling approximately $6.9 million. On May 9, 2016, a settlement stipulation related to this suit was approved under order of the Bankruptcy Court. The settlement stipulation required the Company to issue 327,608 shares of common stock and submit a payment of $250,000 to the claimants. See Note 12 for additional information on this matter and settlement. As of December 31, 2015, the Company recorded an obligation in stockholders' equity to issue the related shares totaling approximately $2.8 million and recorded the cash liability of $500,000 in Liabilities subject to compromise in the accompanying Condensed Consolidated Balance Sheets. Excluding these stipulated claims, all other proofs of claim amount to approximately $5.1 million. As of December 31, 2015, the Company recorded a liability of approximately $4.5 million, which represents its estimate of the amount expected to be allowed by the Bankruptcy Court, in Liabilities subject to compromise in the accompanying Condensed Consolidated Balance Sheets. In addition, the Company also had liabilities related to accrued compensation and deferred rent, totaling approximately $0.4 million, included in Liabilities subject to compromise in the accompanying Condensed Consolidated Balance Sheets, as of December 31, 2015. As of March 31, 2016, the Company has a remaining balance of $4.9 million in Liabilities subject to compromise which has been reduced from December 31, 2015 as a result of the termination of its former lease and the related remaining deferred rent as well as the payment of certain claims totaling approximately $211,000.

In March 2016, the Company entered into a termination agreement (the "Lease Termination Agreement") related to the lease of its prior facility in South San Francisco, California. The Lease Termination Agreement, approved by order of the Bankruptcy Court issued March 15, 2016, waived all damages related to early termination of the lease, relieved the Company of March rental expenses and set an effective termination date of March 31, 2016. In accordance with the termination of the lease, the Company wrote off remaining deferred rent liabilities of approximately $312,000 and disposed of certain leasehold improvements and furniture and fixtures with a net book value of approximately $85,000. The resulting gain of $227,000 is included in Reorganization items, net in the accompanying Condensed Consolidated Statement of Operations and Consolidated loss for the three months ended March 31, 2016. Concurrent with the termination of its prior lease, the Company entered into a lease agreement for a new facility in Brisbane, California. The new lease commenced in April 2016 and will expire in March 2017.

The reconciliation of certain proofs of claim filed against the Company in the Bankruptcy Case, including certain General Unsecured Claims and Other Subordinated Claims, is ongoing. As a result of its examination of the claims, the Company may ask the Bankruptcy Court to disallow, reduce, reclassify or otherwise adjudicate certain claims the Company believes are subject to objection or otherwise improper. Under the terms of the Plan, the Company has until December 27, 2016 to file additional objections to disputed claims, subject to this deadline's extension by the Bankruptcy Court. The Company may compromise certain claims with or without specific prior approval of the Bankruptcy Court and may identify additional liabilities that will need to be recorded or reclassified to liabilities subject to compromise. The resolution of such claims could result in material adjustments to the Company's financial statements. Other than with respect to certain matters relating to the implementation of the Plan or over which the Bankruptcy Court may have retained jurisdiction, the Company is no longer operating under the direct supervision of the Bankruptcy Court. Nevertheless, the Bankruptcy Case remains open. The Company anticipates that the Bankruptcy Case will be closed following the completion of the claims reconciliation process.

Financial Reporting in Reorganization

The Company applied Financial Accounting Standards Board ("FASB") Accounting Standards Codification ("ASC") 852, *Reorganizations*, which is applicable to companies under bankruptcy protection, and requires amendments to the presentation of key financial statement line items. It requires that the financial statements for periods subsequent to the Chapter 11 filing distinguish transactions and events that are directly associated with the reorganization from the ongoing operations of the business. Revenues, expenses, realized gains and losses, and provisions for losses that can be directly associated with the reorganization and restructuring of the business must be reported separately as reorganization items in the Condensed Consolidated Statements of Operations and Comprehensive Loss. The balance sheet must distinguish pre-petition liabilities subject to compromise from both those pre-petition liabilities that are not subject to compromise and from post-petition liabilities. Liabilities that may be subject to a plan of reorganization must be reported at the amounts expected to be allowed in the Company's Chapter 11 case, even if they may be settled for lesser amounts as a result of the plan of reorganization or negotiations with creditors.

As of March 31, 2016 and December 31, 2015, Liabilities subject to compromise consisted of the following:

(in thousands)	March 31, 2016	December 31, 2015
Litigation accrual expense	$ 500	$ 500
Accounts payable and accrued liabilities	4,367	4,570
Accrued compensation	-	32
Deferred rent	-	312
Total liabilities subject to compromise	**$ 4,867**	**$ 5,414**

For the three months ended March 31, 2016, Reorganization items, net consisted of the following charges:

(in thousands)	Three months ended March 31,2016
Legal fees	$ 2,516
Professional fees	228
Gain on lease termination	(227)
Total reorganization items, net	**$ 2,517**

3. Summary of Significant Accounting Policies

There have been no material changes in the Company's significant accounting policies to those previously disclosed in the 2015 Annual Report.

4. Potentially Dilutive Securities

The Company's potential dilutive securities, which include stock options, restricted stock units and warrants, have been excluded from the computation of diluted net loss per common share as the effect of including those securities would be to reduce the net loss per common share and be antidilutive. Therefore, the denominator used to calculate both basic and diluted net loss per common share is the same in each period presented.

The following outstanding potentially dilutive securities have been excluded from the computations of diluted net loss per common share:

	As of March 31,	
	2016	2015
Options to purchase common stock	397,988	502,602
Restricted stock units	3,750	—
Warrants to purchase common stock	131,193	11,067
	532,931	513,669

5. Investments

At March 31, 2016, the amortized cost and fair value of investments, with gross unrealized gains and losses, were as follows:

(in thousands)	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
Money market funds	$ 245	$ —	$ —	$ 245
Total investments	$ 245	$ —	$ —	$ 245
Reported as:				
Cash and cash equivalents				$ 195
Restricted cash, long-term				50
Total investments				$ 245

At December 31, 2015, the amortized cost and fair value of investments, with gross unrealized gains and losses, were as follows:

(in thousands)	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
Money market funds	$ 196	$ —	$ —	$ 196
Total investments	$ 196	$ —	$ —	$ 196
Reported as:				
Cash and cash equivalents				$ 3
Restricted cash, long-term				193
Total investments				$ 196

6. Fair Value of Financial Instruments

Cash, accounts payable and accrued liabilities are carried at cost, which approximates fair value given their short-term nature. Marketable securities and cash equivalents are carried at fair value.

The fair value of financial instruments reflects the amounts that would be received upon the sale of an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date (exit price). The fair value hierarchy is based on three levels of inputs that may be used to measure fair value, of which the first two are considered observable, and the third is considered unobservable, as follows:

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

Level 2 — Inputs other than those included in Level 1 that are directly or indirectly observable, such as quoted prices for similar assets or liabilities in active markets; quoted prices for identical or similar assets or liabilities in markets that are not active; or other inputs that are observable or can be corroborated by observable market data for substantially the full term of the assets or liabilities.

Level 3 — Unobservable inputs that are supported by little or no market activity and that are significant to the fair value of the assets or liabilities.

The Company measures the fair value of financial assets and liabilities using the highest level of inputs that are reasonably available as of the measurement date. The following tables summarize the fair value of financial assets that are measured at fair value and the classification by level of input within the fair value hierarchy:

	Fair Value Measurements as of March 31, 2016			
(in thousands)	**Level 1**	**Level 2**	**Level 3**	**Total**
Investments:				
Money market funds	$ 245	$ —	$ —	$ 245
Total assets measured at fair value	$ 245	$	$ —	$ 245

	Fair Value Measurements as of December 31, 2015			
(in thousands)	**Level 1**	**Level 2**	**Level 3**	**Total**
Investments:				
Money market funds	$ 196	$ —	$ —	$ 196
Total assets measured at fair value	$ 196	$ —	$ —	$ 196

In 2014, the Company recorded a financing derivative liability resulting from an embedded derivative related to the prepayment feature of its loan and security agreement with MidCap Financial SBIC LP, which was entered into by the Company in September 2012 and subsequently amended (the "Loan and Security Agreement"). At March 31, 2015, the Company re-measured the financing derivative liability as $92,000, resulting in a loss of $3,000 for the three month period ended March 31, 2015. The loss is included in Other income (expense), net in the accompanying Condensed Consolidated Statements of Operations and Comprehensive Loss. The fair value of this derivative was determined using Level 3 inputs, or significant unobservable inputs. The value of the financing derivative was determined by comparing the difference between the fair value of the notes payable with and without the financing derivative by calculating the respective present values from future cash flows using a 14% discount rate, adjusted for the probability of the occurrence of an event of default under the Loan and Security Agreement. The 14% discount rate assumption was based on an effective borrowing rate under the current circumstances considering the quoted borrowing rate for the Company and the imputed fair value of any additional financial instruments that may be required to be extended to the lender in order to obtain such debt financing. The probability of the occurrence of an event of default under the Loan and Security Agreement was based on management's judgment. Refer to Note 7 for additional details regarding the Loan and Security Agreement.

The following table presents changes in financial instruments measured at fair value using Level 3 inputs:

	Fair Value Measurements of Level 3 Liabilities (in thousands)
Balance as of December 31, 2014	$ 89
Loss on re-measurement of the financing derivative liability	3
Balance as of March 31, 2015	92
Loss on re-measurement of the financing derivative liability	135
Balance as of June 30, 2015	227
Loss on re-measurement of the financing derivative liability	114
Balance as of September 30, 2015	341
Loan payoff	(341)
Balance as of December 31, 2015 and March 31, 2016	$ —

There were no notes payable outstanding as of March 31, 2016 or December 31, 2015.

7. Notes Payable

Loan and Security Agreement

In August 2015, the Company entered into Amendment No. 2 to the Loan and Security Agreement, whereby the Company agreed to maintain, in a separate account with a financial institution (held in the Company's name), an amount equal to the aggregate of the remaining future principal, interest and exit fee due under the Loan and Security Agreement, equating to $8.3 million as of the date of Amendment No. 2. Under the terms of the Loan and Security Agreement, as amended, MidCap Financial was permitted to draw payments from this account as they become due, and upon such draws, there would be a corresponding reduction in the amount owed to MidCap Financial by the Company. MidCap Financial had exclusive control to withdraw funds from that account at any time. The account was to be maintained either until the debt has been repaid in full, or until MidCap Financial determined that the Company has satisfied certain capital requirements related to the Company's future operating plans.

In November 2015, the Company elected to exercise its prepayment right to repay the loan in full and paid MidCap Financial $6.6 million in full settlement of the remaining outstanding principal balance, accrued interest, the exit fee and a reduced prepayment fee of 1%. The prepayment resulted in a gain on extinguishment of debt of $61,000 in the fourth quarter of 2015.

8. Commitments and Contingencies

Contractual Obligations and Commitments

As of March 31, 2016, there were no material changes to the Company's contractual obligations from those set forth in the 2015 Annual Report.

Guarantees and Indemnifications

The Company has certain agreements with service providers with which it does business that contain indemnification provisions pursuant to which the Company typically agrees to indemnify the party against certain types of third-party claims. The Company accrues for known indemnification issues when a loss is probable and can be reasonably estimated. The Company would also accrue for estimated incurred but unidentified indemnification issues based on historical activity. As the Company has not incurred any indemnification losses to date, there were no accruals for or expenses related to indemnification issues for any period presented.

9. Share Based Compensation

2012 Equity Incentive Plan

Under the Company's 2012 Equity Incentive Plan, the Company may grant shares, stock units, stock appreciation rights, performance cash awards and/or options to employees, directors, consultants, and other service providers. For options, the per share exercise price may not be less than the fair market value of a Company common share on the date of grant. Awards generally vest and become exercisable over three to four years and expire 10 years from the date of grant.

A summary of stock option activity for the three months ended March 31, 2016 under all of the Company's options plans is as follows:

	Options	Weighted Average Exercise Price
Outstanding at December 31, 2015	465,401	$ 19.29
Granted	—	—
Exercised	—	—
Cancelled (forfeited)	(3,416)	5.86
Cancelled (expired)	(63,997)	33.51
Outstanding at March 31, 2016	397,988	$ 17.12

There were no options granted or exercised during the three months ended March 31, 2016. In addition, 3,750 restricted stock units were outstanding as of March 31, 2016.

2012 Employee Stock Purchase Plan

The Employee Stock Purchase Plan (the "ESPP") provided eligible employees with the opportunity to acquire an ownership interest in the Company through periodic payroll deductions, based on a six-month look-back period, at a price equal to the lesser of 85% of the fair market value of the ordinary shares at either the beginning of the offering period, or the fair market value on the purchase date. The ESPP was structured as a qualified employee stock purchase plan under Section 423 and a qualified pension, profit sharing or stock bonus plan under Section 401(a) of the Internal Revenue Code of 1986 and was not subject to the provisions of the Employee Retirement Income Security Act of 1974. There were 21,058 shares initially authorized for issuance under the plan, and the first offering period commenced on June 1, 2014 and ended on October 31, 2014. The second offering period commenced on November 1, 2014 and ended on April 30, 2015. There were 583 and 375 shares issued under the plan on October 31, 2014 and April 30, 2015, respectively. Under the terms of the ESPP, offerings subsequent to the second offering were to commence on May 1 and November 1 and end on April 30 and October 31 each year. On March 3, 2016, the ESPP was terminated.

Stock-Based Compensation

The Company recorded stock-based compensation expense in the Condensed Consolidated Statements of Operations and Comprehensive Loss as follows:

	Three Months Ended March 31,	
(in thousands)	**2016**	**2015**
General and administrative	$ 1	$ 142
Research and development	1	163
	$ 2	$ 305

During the three months ended March 31, 2015, in addition to the amounts shown above, the Company recorded charges of $389,000 and $414,000 related to the fair value of stock options that were modified due to executive retirement and restructuring activities, and classified $420,000 and $383,000 as General and administrative expenses and Research and development expenses, respectively. During the three months ended March 31, 2016 the Company did not record any such charges.

At March 31, 2016, the Company had $23,000 of total unrecognized stock-based compensation expense, net of estimated forfeitures, related to outstanding stock options that will be recognized over a weighted-average period of 3.3 years.

10. Restructuring Charges

Restructuring charges incurred during the nine months ended September 30, 2015 primarily consist of severance and other post-termination benefit costs resulting from the cost reduction program implemented by the Company in January 2015. These activities primarily consisted of 20% reduction of the Company's workforce. Restructuring charges incurred during the three months ended December 31, 2015 primarily relate to a board-approved restructuring plan announced in November 2015 to reduce costs and extend the cash runway in order to allow the Company to evaluate strategic alternatives. As part of the restructuring plan, the Company elected to exercise its right to prepay the Loan and Security Agreement and paid MidCap Financial $6.6 million in full settlement of the remaining outstanding principal balance, accrued interest, the exit fee and a reduced prepayment fee of 1%. In addition, the Company undertook a reduction in force that eliminated the positions of 17 employees or more than 60% of the Company's workforce.

Per ASC 420-10-05-1, Exit or Disposal Cost Obligations, include, but are not limited to, involuntary termination benefits provided to employees under the terms of a one-time benefit arrangement that, in substance, is not an ongoing benefit arrangement or a deferred compensation contract, and certain contract termination costs. Restructuring costs are expensed during the period in which the Company determines it will incur those costs and all requirements of accrual are met.

A summary of the activity is presented below:

(in thousands)	Contract termination costs - R&D	Salaries and benefits - R&D	Salaries and benefits - G&A	Total
Balance as of December 31, 2014	$ 1,185	$ —	$ —	$ 1,185
Accrued	—	522	82	604
Paid	(479)	(257)	—	(736)
Balance as of March 31, 2015	706	265	82	1,053
Accrued	—	57	122	179
Paid	(135)	(142)	—	(277)
Balance as of June 30, 2015	571	180	204	955
Accrued	—	—	—	—
Adjustments	(78)	—	—	(78)
Paid	(493)	(148)	(136)	(777)
Balance as of September 30, 2015	—	32	68	100
Accrued	—	588	807	1,395
Paid	—	(620)	(864)	(1,484)
Balance as of December 31,2015	—	—	11	11
Accrued	—	—	—	—
Paid	—	—	—	—
Balance as of March 31, 2016	$ —	$ —	$ 11	$ 11

As disclosed in Note 9, during the three months ended March 31, 2015, in addition to the restructuring charges in the table above, the Company recorded charges of $389,000 and $414,000 related to the fair value of stock options that were modified due to executive retirement and restructuring activities, and classified $420,000 and $383,000 as General and administrative expenses and Research and development expenses, respectively. During the three months ended March 31, 2016 the Company did not record any such charges.

11. Savant Arrangements

On February 29, 2016, the Company entered into a binding letter of intent (the "LOI") with Savant Neglected Diseases, LLC ("Savant"). The LOI provided that the Company would acquire certain worldwide rights relating to benznidazole (the "Compound") from Savant. Under the LOI, the Company made a non-refundable deposit to Savant of $500,000, which was credited towards the Initial Payment (as defined below), and agreed to make monthly payments to Savant equal to $87,500 for development services performed by Savant relating to the Compound.

The LOI provided that in consideration for the assets to be acquired, the Company would provide consideration to Savant, including:

- $3,000,000 (the "Initial Payment") payable as soon as practicable but in no event later than the Company emerging from its Chapter 11 bankruptcy pursuant to a plan of reorganization (the "Bankruptcy Exit");

- a five-year warrant from the date of the Bankruptcy Exit to purchase up to 200,000 shares of common stock at a per share price of $2.25, exercisable for 25% of the shares immediately and exercisable for the remaining shares upon reaching certain milestones related to regulatory approval of the Compound; and
- certain additional payments to be further specified in the definitive agreements.

On the Effective Date, as authorized by the Plan and the Confirmation Order, the Company and Savant entered into an Agreement for the Manufacture, Development and Commercialization of Benznidazole for Human Use (the "MDC Agreement"), pursuant to which the Company acquired certain worldwide rights relating to the Compound. The MDC Agreement consummates the transactions contemplated by the LOI.

Under the terms of the MDC Agreement, the Company acquired certain regulatory and non-intellectual property assets relating to the Compound and any product containing the Compound and an exclusive license of certain intellectual property assets related to the Compound. Savant will retain the right to use the licensed intellectual property for veterinary uses. The MDC Agreement provides that the Company and Savant will jointly conduct research and development activities with respect to the Compound, while the Company will be solely responsible for commercializing the Compound. The Company will fund the development program for the Compound and will reimburse Savant for its development program costs.

As required by the MDC Agreement, on the Effective Date, the Company made payments to Savant totaling $2,687,500, consisting of the remaining portion of the Initial Payment less the deposit in the amount of $2,500,000, an initial monthly Joint Development Program Cost payment of $87,500, and reimbursement of Savant's legal fees capped at $100,000. The MDC Agreement provides for milestone payments, including payments related to U.S. and foreign regulatory submissions, of up to $21 million and certain other contingent payments. Additionally, the Company will pay Savant royalties on any net sales of the Compound, which royalty would increase if a PRV is granted subsequent to regulatory approval of the Compound. The MDC Agreement also provides that Savant is entitled to a portion of the amount the Company receives upon the sale, if any, of a PRV relating to the Compound.

In addition, on the Effective Date the Company and Savant also entered into a Security Agreement (the "Security Agreement"), pursuant to which the Company granted Savant a continuing senior security interest in the assets and rights acquired by the Company pursuant to the MDC Agreement and certain future assets developed from those acquired assets.

On the Effective Date, the Company issued to Savant a five year warrant (the "Warrant") to purchase 200,000 shares of the Company's Common Stock, at an exercise price of $2.25 per share, subject to adjustment. The Warrant is exercisable for 25% of the shares immediately and exercisable for the remaining shares upon reaching certain regulatory related milestones. In addition, pursuant to the MDC Agreement, the Company has granted Savant certain "piggyback" registration rights for the shares issuable under the Warrant.

The Company has determined that the acquisition of the Compound should be treated as a purchase of in-process research and development. Accordingly, during the three months ended March 31, 2016, the Company recorded $750,000, which includes an additional $250,000 payment made in 2015 to Savant, as Research and development expense in the accompanying Condensed Consolidated Statement of Operations and Comprehensive Loss. In addition, during the three months ended June 30, 2016, the Company recorded $87,500 in connection with the Joint Development Program as research and development expense in the accompanying Condensed Consolidated Statement of Operations and Comprehensive Loss. Subsequent to March 31, 2016, the Company made additional payments to Savant of $2,500,000 related to the purchase of the Compound, reimbursement of legal expenses of $100,000 (as noted above) and additional payments related to the Joint Development Program, each of which will be included as Research and development expense in future periods.

12. Litigation

Bankruptcy Proceeding

The Company filed for protection under Chapter 11 of Title 11 of the United States Bankruptcy Code on December 29, 2015. See Note 2 and Note 13 for additional information related to the bankruptcy.

Securities Class Action Litigation

On December 18, 2015, a putative class action lawsuit (captioned *Li v. KaloBios Pharmaceuticals, Inc. et al.*, 5:15-cv-05841-EJD) was filed against the Company in the United States District Court for the Northern District of California (the "Class Action Court"), alleging violations of the federal securities laws by Martin Shkreli, the Company's former Chairman and Chief Executive Officer. On December 23, 2015, a putative class action lawsuit was filed against the Company in the Class Action Court (captioned *Sciabacucchi v. KaloBios Pharmaceuticals, Inc. et al.*, 3:15-cv-05992-CRB), similarly alleging violations of the federal securities laws by Mr. Shkreli. On December 31, 2015, a putative class action lawsuit was filed against the Company in the Class Action Court (captioned *Isensee v. KaloBios Pharmaceuticals, Inc. et al*., Case No. 15-cv-06331-EJD) also alleging violation of the federal securities laws by Mr. Shkreli. On April 28, 2016, the Class Action Court consolidated these cases (the "Securities Class Action Litigation") and appointed certain plaintiffs as the lead plaintiffs. The lead plaintiffs in the Securities Class Action Litigation were seeking damages of $20.0 million on behalf of all the affected members of the class represented in the Securities Class Action Litigation, (the "Securities Class Action Members").

On June 15, 2016, a settlement stipulation (the "Securities Class Action Settlement"), was approved by the Bankruptcy Court. Subject to the approval of the Class Action Court, the Securities Class Action Settlement required us to issue 300,000 shares of common stock and submit a payment of $250,000 the Securities Class Action Members and advance insurance proceeds of $1.25 million to the Securities Class Action Members (collectively, the consideration is the "Securities Class Action Settlement Consideration"). Subject to the final approval of the Securities Class Action Settlement, any Securities Class Action Member is entitled to share in the Securities Class Action Settlement Consideration. The Securities Class Action Settlement provides for releases and related injunctions to be granted for the benefit of, among others, the Company, Ronald Martell, Herb Cross and all of the Company's past, present and future directors, officers and employees, excluding Mr. Shkreli. Alternatively, Securities Class Action Members may exclude themselves from the Securities Class Action Settlement and are thereby not bound by the terms of the Securities Class Action Settlement nor entitled to receive any amount of the Securities Class Action Settlement Consideration. Such individuals remain free to assert claims against the Company and such claims were subordinated to the level of the Company's common stock and otherwise remain subject to the Company's objection. The Company's agreement to the Securities Class Action Settlement was not in any way an admission of the Company's wrongdoing or liability.

PIPE Litigation

On January 7, 2016, certain investors (the "PIPE Claimants"), commenced an adversary proceeding (captioned *Gregory Rea, et al. v. KaloBios Pharmaceuticals, Inc.*, Adv. Pro. No. 16-50001 (LSS)) in the Bankruptcy Court against the Company alleging implied trust theories, breach of contract, fraud and violations of the federal securities laws in connection with the PIPE Claimants' purchase of the Company's common stock in the Private Placement (the "PIPE Litigation"). The PIPE Claimants also raised certain other objections to the Company's bankruptcy proceeding. The PIPE Claimants sought an aggregate total of approximately $6.9 million in damages.

On May 9, 2016, the Bankruptcy Court entered an order approving a settlement stipulation between the Company and the PIPE Claimants (the "Settlement Stipulation"). Under the Settlement Stipulation, in connection with the effectiveness of the Plan, and per the terms of the Settlement Stipulation, the Company became obligated to issue 327,608 shares to the PIPE Claimants and make a payment of $250,000 to the PIPE Claimants for the purpose of satisfying expenses related to the PIPE Settlement.

Claim by Marek Biestek

Marek Biestek was a director of the Company who, while not a plaintiff in the above described PIPE Litigation, filed a proof of claim alleging damages from the PIPE transaction and filed an objection to the confirmation of our Plan. To resolve his objection to the Plan, we settled with him individually by issuing him 3,750 additional shares of common stock. Mr. Biestek, as a former director of the company, was excluded from the Securities Class Action Members and therefore received nothing from the Securities Class Action Litigation.

As of December 31, 2015, the Company recorded an obligation in stockholders' equity to issue the shares related to all of the above claims that totals approximately $2.8 million and recorded the cash Liability of $500,000 in Liabilities subject to compromise in the accompanying Condensed Consolidated Balance Sheet.

13. Subsequent Events

Bankruptcy Related Financing Arrangements

On April 1, 2016, as described in Note 2, the Company entered into the Credit Agreement with Black Horse Capital Master Fund Ltd., as administrative agent and lender ("BHCMF" or the "Agent"), Black Horse Capital LP, as a lender ("BHC"), Cheval Holdings, Ltd., as a lender ("Cheval") and Nomis Bay LTD, as a lender ("Nomis" and, together with BHCMF, BHC and Cheval, the "Lenders"). The Credit Agreement provided for a debtor-in-possession credit facility in the original principal amount of $3,000,000 (the "Term Loan"). The Credit Agreement provided that the Term Loan will be made by the Lenders at an original discount equal to $191,000 (the "Upfront Fee") and required the payment by the Company to the Lenders of a commitment fee equal to $150,000 (the "Commitment Fee"). In accordance with the terms of the Credit Agreement, the Company used the proceeds of the Term Loan for working capital, bankruptcy-related costs, costs related to the Company's plan of reorganization, the payment of certain fees and expenses owed to the Agent and the Lenders in connection with the Credit Agreement and other costs incurred in the ordinary course of business.

Pursuant to the terms of the Credit Agreement, the Term Loan bore interest at a rate per annum equal to 12.00%.

In accordance with the bidding procedures order entered by the Bankruptcy Court, the Term Loan and the SPA were together subject to competing, higher and better offers.

The Company's obligations under the Credit Agreement were secured pursuant to an Intellectual Property Security Agreement.

In connection with the Credit Agreement, the Company executed in favor of the Agent an Intellectual Property Security Agreement, dated as of April 1, 2016 (the "IP Security Agreement"). Under the terms of the IP Security Agreement, the Company pledged all of its intellectual property to the Agent for the ratable benefit of the Lenders, as collateral for its obligations under the Credit Agreement.

The Credit Agreement provided that the outstanding principal balance of the Term Loan, plus accrued and unpaid interest, plus the Upfront Fee, plus the Commitment Fee and all other non-contingent obligations would mature on the earlier of an event of default under the Credit Agreement or the effective date of the Company's plan of reorganization. The Maturity Date was deemed to occur simultaneously with the Effective Date and, accordingly, on June 30, 2016, 2,350,480 shares of common stock were issued to the Lenders in repayment of the Company's debt obligations under the Credit Agreement, including 201,436 shares to BHC, 470,096 shares to BHCMF, 503,708 shares to Cheval, 940,192 shares to Nomis and 235,048 shares to Cortleigh Limited ("Cortleigh"). Pursuant to the terms of the Credit Agreement, the Company also paid $406,285 to BHC in payment of its fees and expenses and $285,000 to Nomis in payment of its fees and expenses.

On April 1, 2016, as described in Note 2, the Company also entered into the SPA with the Lenders. The SPA provides for the sale to the Lenders on the closing date of an aggregate of 5,885,000 shares of common stock, subject to adjustment as provided in the SPA, in respect of exit financing in the amount of $11,000,000 (the "Exit Financing") plus an exit financing commitment fee of $770,000 payable by the Company to the Lenders, plus payment to the Lenders of their fees and expenses incurred in connection with the Exit Financing and the SPA. Nomis subsequently assigned twenty percent (20%) of its interest in the shares of common stock to be purchased by Nomis under the SPA and the Credit Agreement to Cortleigh (collectively with the Lenders, the "Purchasers").

The consummation of the transactions contemplated by the SPA were contingent on, among other things, the funding of the Term Loan, the approval of the Bankruptcy Court of the Company's plan of reorganization, and the simultaneous closing of the Company's transaction with Savant. In addition, the closing of the transactions under the SPA were contingent upon the board of directors of the Company, upon the effectiveness of the confirmed plan of reorganization, consisting of (i) one director to be designated by Nomis; (ii) one director to be jointly designated by BHC, BHCF, and Cheval; (iii) the Chief Executive Officer of the Company to be designated jointly and unanimously by the Lenders; and (iv) two independent directors to be designated jointly and unanimously by the Lenders.

The issuance of the shares contemplated by the SPA was consummated on the Effective Date, and the Company issued to the Purchasers an aggregate of 7,147,035 shares of common stock for an aggregate purchase price of $11,000,000, including 612,501 shares to BHC, 1,429,407 shares to BHCMF, 1,531,610 shares to Cheval, 2,858,814 shares to Nomis and 714,703 shares to Cortleigh. Pursuant to the terms of the SPA, the Company paid $427,383 to BHC in payment of its fees and expenses and $303,886 to Nomis in payment of its fees and expenses.

Emergence from Bankruptcy

On May 9, 2016, the Company filed with the Bankruptcy Court the Plan and related amended disclosure statement pursuant to Chapter 11 of the Bankruptcy Code. On June 16, 2016, the Bankruptcy Court entered an order confirming the Plan (the "Confirmation Order"). On May 9, 2016, the Bankruptcy Court entered an order (the "Order") approving the Settlement Stipulation entered into between (i) Gregory Rea, RTAT LLC, Nancy Retzlaff, Armistice Capital Master Fund, Ltd. Andrew Pizzo and Sabine Gritti and (ii) the Company. The Settlement Stipulation provides for the resolution among the parties of the PIPE Litigation in connection with the purchase and sale of the Company's common stock in the Private Placement, certain objections related to the Company's bankruptcy proceedings and all related matters. Pursuant to the terms of the Settlement Stipulation, the plaintiffs in the PIPE Litigation received 327,608 shares of the common stock of the Company as reorganized pursuant to the Plan, in addition to certain other consideration.

On the Effective Date, the Plan became effective and the Company emerged from its Chapter 11 bankruptcy proceedings.

On the Effective Date, in accordance with the terms of the Plan, in addition to shares issued to the Lenders and the Purchasers under the Credit Agreement and SPA, respectively, and shares issued in connection with the Settlement Stipulation, the Company reserved for issuance 300,000 shares to the plaintiffs in a class action lawsuit related to the events surrounding the Company's former Chairman and Chief Executive Officer, and the Company became obligated to issue 3,750 shares to Marek Biestek, a former director, in satisfaction of claims by Mr. Biestek against the Company. In addition, on the Effective Date, the Company reserved for issuance shares of common stock in connection with certain other claims and interests as set forth in the Plan in an amount as yet to be determined.

In accordance with the Plan, on the Effective Date, the Company became obligated to issue promissory notes (the "Notes") in the estimated aggregate principal amount of approximately $1.2 million to certain holders of allowed general unsecured claims in the Company's bankruptcy proceedings. The Notes are unsecured, bear interest at a rate of 10% per annum and mature on June 30, 2019.

Governance Arrangements

On the Effective Date, the Company and Martin Shkreli, the Company's former Chief Executive Officer, former Chairman and former controlling stockholder, entered into a Corporate Governance Agreement (the "Governance Agreement"), which provides for certain terms and conditions regarding the acquisition, disposition, holding and voting of securities of the Company by Mr. Shkreli. The Governance Agreement applies to all common stock owned by Mr. Shkreli or affiliates he controls.

Under the terms of the Governance Agreement, for 180 days following the Effective Date, Mr. Shkreli could not sell his shares of common stock at a price per share that was less than the greater of (x) $2.50 and (y) a 10% discount to the prior two week volume-weighted average price (the "Market Discount Price"). In addition, for 180 days following the 61st day after the Effective Date, the Company had a right to purchase any or all of Mr. Shkreli's shares at a purchase price per share equal to the Market Discount Price. For a limited time, the Company also had a right of first refusal to purchase shares that Mr. Shkreli proposed to sell. Mr. Shkreli was also prohibited from transferring any shares to his affiliates or associates unless such transferee agreed to be subject to the terms of the Governance Agreement. Transfers of shares by Mr. Shkreli not made in compliance with the Governance Agreement would be null and void.

Under the terms of the Governance Agreement, Mr. Shkreli will not have any right to nominate directors to the board of directors of the Company and agreed in connection with any stockholder vote to vote his shares in proportion to the votes of the Company's public stockholders. The Governance Agreement also prohibits Mr. Shkreli or his affiliates for a period of 24 months after the date of the Governance Agreement, from, among other things:

- purchasing any stock or assets of the Company;
- participating in any proposal for any merger, tender offer or other business combination, or similar extraordinary transaction involving the Company or any of its subsidiaries;
- seeking to control or influence the management, the Company's Board or the policies of the Company; or
- submitting any proposal to be considered by the stockholders of the Company.

In addition, any material transaction between Mr. Shkreli or his associates and the Company, or relating to the Governance Agreement, cannot be taken without the prior approval of the Company's Board.

The Governance Agreement provides for a mutual release between the Company and Mr. Shkreli of all claims and liabilities existing as of the date of execution.

On August 25 and August 26, 2016, Mr. Shkreli sold all of his shares of the Company to third party investors in private transactions.

Stock Issuance

On May 24, 2016, the board of directors approved a one-time equity award (the "Equity Award") to each of Cameron Durrant, Ronald Barliant and David Moradi. On the Effective Date, in accordance with the Plan, the Company became obligated to issue an aggregate 323,155 shares of common stock under the Equity Award.

Board Changes

On the Effective Date, in accordance with the Plan, Cameron Durrant, current Chief Executive Officer of the Company, as joint designee of BHCMF, BHC and Cheval (the "Black Horse Entities") and Nomis, continued as a director, Ronald Barliant, current member of the Board, continued as a director as the designee of the Black Horse Entities, Dale Chappell became a director as a designee of Nomis, and Timothy Morris and Ezra Friedberg became directors as joint designees of the Black Horse Entities and Nomis.

Stock Option Grant

On September 13, 2016, the Company issued stock options to its Chief Executive Officer to purchase 1,043,022 shares of the Company's common stock at an exercise price of $3.38, the closing price on the date of issuance. The options will vest and become exercisable in 12 equal quarterly installments beginning on December 13, 2016.

Amendment to 2012 Equity Incentive Plan

On September 13, 2016, the Board of Directors of the Company approved an amendment to the Company's 2012 Equity Incentive Plan to increase the number of shares of the Company's common stock available for issuance under the Plan by 3,000,000 shares and to increase the annual maximum aggregate number of shares subject to stock option awards that may be granted to any one person under the Plan from 125,000 to 1,100,000.

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

You should read the following discussion and analysis together with our financial statements and the notes to those statements included elsewhere in this Quarterly Report on Form 10-Q and our Annual Report on Form 10-K for the fiscal year ended December 31, 2015. This Quarterly Report on Form 10-Q contains statements that discuss that discuss future events or expectations, projections of results of operations or financial condition, trends in our business, business prospects and strategies and other "forward-looking" information. In some cases, you can identify "forward-looking statements" by words like "may," "will," "should," "expects," "plans," "anticipates," "believes," "estimates," "predicts," "intends," "potential" or "continue" or the negative of those words and other comparable words. These statements may relate to, among other things, our expectations regarding the scope, progress, expansion, and costs of researching, developing and commercializing our product candidates; our intent to in-license or acquire additional product candidates; our opportunity to benefit from various regulatory incentives and the application of our Responsible Pricing Model; expectations for our financial results, revenue, operating expenses and other financial measures in future periods; and the adequacy of our sources of liquidity to satisfy our working capital needs, capital expenditures, and other liquidity requirements. Actual events or results may differ materially due to known and unknown risks, uncertainties and other factors such as:

- *the uncertainties inherent in the development and launch of any new pharmaceutical product;*
- *our ability to successfully and timely complete clinical trials for our drug candidates in clinical development;*
- *our ability to obtain the necessary U.S. and international regulatory approvals for our drug candidates and to qualify for or benefit from various regulatory incentives;*
- *the scope and validity of intellectual property and other competitive protection for our drug candidates;*
- *our ability to identify, in-license and acquire additional product candidates or to form partnerships for the sale, licensing, collaborative development or marketing of our existing product candidates;*
- *our ability to maintain or engage third-party manufacturers to manufacture, supply, store and distribute supplies of our drug candidates for our clinical trials;*
- *our lack of profitability and the need for additional capital to operate our business; and*
- *the success of any product.*

These are only some of the factors that may affect the forward-looking statements contained in this annual report. For a discussion identifying additional important factors that could cause actual results to vary materially from those anticipated in the forward-looking statements, see "Risk Factors" in Item 1A of Part I of our Annual Report on Form 10-K for the fiscal year ended December 31, 2015. You should review these risk factors for a more complete understanding of the risks associated with an investment in our securities. However, we operate in a competitive and rapidly changing environment and new risks and uncertainties emerge, are identified or become apparent from time to time. It is not possible for us to predict all risks and uncertainties that could have an impact on the forward-looking statements contained in this annual report. You should be aware that the forward-looking statements contained in this annual report are based on our current views and assumptions. We undertake no obligation to revise or update any forward-looking statements made in this annual report to reflect events or circumstances after the date hereof or to reflect new information or the occurrence of unanticipated events, except as required by law. The forward-looking statements in this annual report are intended to be subject to protection afforded by the safe harbor for forward-looking statements contained in the Private Securities Litigation Reform Act of 1995.

Overview

We are a biopharmaceutical company focused on developing medicines for patients with neglected and rare diseases, with an ancillary focus on pediatric conditions, and on executing our Responsible Pricing Model in the commercialization of our products that may be approved. Our lead product candidate is benznidazole for the treatment of Chagas disease, a parasitic illness that can lead to long-term heart, intestinal and neurological problems. We are developing one of our proprietary monoclonal antibodies, lenzilumab (formerly known as KB003), for the treatment of chronic myelomonocytic leukemia, or CMML, and potentially for the treatment of juvenile myelomonocytic leukemia, or JMML, both of which are rare hematologic cancers with high unmet medical need. We are exploring development of another of our proprietary monoclonal antibodies, ifabotuzumab (formerly known as KB004), for the treatment of certain rare solid and hematologic cancers. With a focus on neglected, rare and orphan diseases, we believe we have the opportunity to benefit from various regulatory incentives, such as orphan drug exclusivity, breakthrough therapy designation, fast track designation, accelerated approval, priority review and priority review vouchers, or PRVs, where available, that provide for certain periods of exclusivity, expedited review and/or other benefits.

Upon approval of any of our products, we intend to apply our Responsible Pricing Model, which focuses on affordability for patients and payers, transparency for all stakeholders, and delivery of a reasonable return in recognition of the risks we are taking in our development efforts.

Benznidazole is an oral small molecule antiprotozoal for the treatment of Chagas disease, which is also known as American trypanosomiasis. Benznidazole has undergone numerous clinical trials and studies that show efficacy against Chagas disease and we believe is the current preferred treatment for Chagas disease in the countries where it is approved. No treatments for Chagas disease are approved by the United States Food and Drug Administration, or FDA, for use in the United States. We recently acquired certain worldwide rights relating to benznidazole for human use from Savant Neglected Diseases, LLC, or Savant, and we are focused on the development necessary to seek and obtain FDA approval of benznidazole. We believe benznidazole as a treatment for Chagas disease could qualify for priority review and potentially other FDA regulatory incentives, and to receive a PRV if FDA approves the drug for marketing.

Lenzilumab is a recombinant monoclonal antibody, or mAb, that neutralizes soluble granulocyte-macrophage colony-stimulating factor, or GM-CSF, a critical cytokine for the growth of certain hematologic malignancies and solid tumors. Consistent with our strategic focus on neglected and rare diseases, in July 2016, we initiated dosing in a Phase 1 clinical trial in patients with CMML to identify the maximum tolerated dose, or MTD, or recommended Phase 2 dose of lenzilumab and to assess lenzilumab's safety, pharmacokinetics, and clinical activity.

Ifabotuzumab is an anti-EphA3 mAb that has the potential to offer a novel approach to treating both solid tumors and hematologic malignancies. EphA3 is aberrantly expressed on the tumor cell surface of certain cancers. We have completed the Phase 1 dose escalation portion of a Phase 1/2 clinical trial in ifabotuzumab in multiple hematologic malignancies and are evaluating whether to conduct further studies of ifabotuzumab in rare solid tumors such as glioblastoma, other brain cancers in children and rare hematologic cancer indications. We also have an additional drug candidate, KB001-A, a recombinant, PEGylated, anti-Pseudomonas PcrV high-affinity Fab antibody that we are no longer developing, but which is being considered for partnering or out-licensing.

Lenzilumab, ifabotuzumab and KB001-A were each developed with our proprietary, patent-protected Humaneered® technology, which consists of methods for converting antibodies (typically murine) into engineered, high-affinity antibodies designed for human therapeutic use, typically for chronic conditions.

Our strategy also involves identifying, acquiring, developing and supporting the commercialization of additional treatments for neglected and rare diseases. We believe the treatment of neglected and rare diseases represents an opportunity to enter underserved patient populations and serve specialty markets. We also believe our focus on neglected and rare diseases provides us the opportunity to benefit from various regulatory incentives referenced above. The potential opportunities afforded by these regulatory programs provide an important incentive to support our efforts to develop medicines for patients with neglected and rare diseases and to apply our Responsible Pricing Model for any of our approved products.

We have incurred significant losses and had an accumulated deficit of $219.0 million as of March 31, 2016. We expect to continue to incur net losses as we develop our drug candidates, expand clinical trials for our drug candidates currently in clinical development, expand our development activities and seek regulatory approvals. Significant capital is required to continue to develop and to launch a product and many expenses are incurred before revenue is received, if any. We are unable to predict the extent of any future losses or when we will receive revenue or become profitable, if at all.

We will require substantial additional capital to support our business efforts, including obtaining regulatory approvals for benznidazole or other product candidates, clinical trials and other studies, and, if approved, the commercialization of our product candidates. We anticipate that in the future we will seek additional financing from a number of sources, including, but not limited to, the sale of equity or debt securities, strategic collaborations, and licensing of our product candidates. Additional funding may not be available to us on a timely basis or at acceptable terms, if at all. Our ability to access capital when needed is not assured and, if not achieved on a timely basis, would materially harm our business, financial condition and results of operations. If adequate funds are not available, we may be required to delay, reduce the scope of, or eliminate one or more of our development programs. We may also be required to sell or license to others our technologies, product candidates, or development programs that we would have preferred to develop and commercialize ourselves and on less than favorable terms, if at all.

On January 13, 2016, our common stock was suspended from the Nasdaq Global Market and began trading on the over-the-counter market under the ticker symbol KBIOQ. On January 26, 2016, NASDAQ filed a Form 25 with the Securities and Exchange Commission to complete the delisting of our common stock, and the delisting was effective on February 5, 2016.

If management is unsuccessful in efforts to raise additional capital, based on our current levels of operating expenses, our current capital is not expected to be sufficient to fund our operations for the next twelve months. These conditions raise substantial doubt about our ability to continue as a going concern. The Condensed Consolidated Financial Statements for the quarter ended March 31, 2016 were prepared on the basis of a going concern, which contemplates that we will be able to realize our assets and discharge liabilities in the normal course of business. Our ability to meet our liabilities and to continue as a going concern is dependent upon the availability of future funding. The financial statements do not include any adjustments that might be necessary if we are unable to continue as a going concern.

As a result of challenges facing us at the time, on December 29, 2015, we filed a voluntary petition for bankruptcy protection under Chapter 11 of Title 11 of the U.S. Bankruptcy Code. On June 30, 2016, our Second Amended Plan of Reorganization, dated May 9, 2016, as amended, or the Plan, became effective and we emerged from our Chapter 11 bankruptcy proceedings. For further information on our bankruptcy and emergence from bankruptcy, see Note 2 to the Condensed Consolidated Financial Statements included in Item 1 of this Quarterly Report on Form 10-Q.

Critical Accounting Policies and Use of Estimates

Our management's discussion and analysis of our financial condition and results of operations is based on our consolidated financial statements, which have been prepared in accordance with accounting principles generally accepted in the United States, or GAAP. The preparation of our financial statements in conformity with GAAP requires our management to make estimates and assumptions that affect the amounts and disclosures reported in the financial statements and accompanying notes. Actual results could differ materially from those estimates. Our management believes judgment is involved in determining revenue recognition, valuation of financing derivative, the fair value-based measurement of stock-based compensation, accruals and warrant valuations. Our management evaluates estimates and assumptions as facts and circumstances dictate. As future events and their effects cannot be determined with precision, actual results could differ from these estimates and assumptions, and those differences could be material to the consolidated financial statements. If our assumptions change, we may need to revise our estimates, or take other corrective actions, either of which may also have a material adverse effect on our statements of operations, liquidity and financial condition.

We are an emerging growth company under the JOBS Act. Emerging growth companies can delay adopting new or revised accounting standards until such time as those standards apply to private companies. We have elected to avail ourselves of this exemption from new or revised accounting standards and, therefore, we may not be subject to the same new or revised accounting standards as other public companies that are not emerging growth companies.

There were no material changes in our critical accounting policies and use of estimates during the three months ended March 31, 2016, as compared to those disclosed in "Management's Discussion and Analysis of Financial Condition and Results of Operations—Critical Accounting Policies and Use of Estimates" in our 2015 Annual Report on Form 10-K (File No. 001-35798), filed with the SEC on September 1, 2016.

Results of Operations

General

We have not generated net income from operations, except for the year ended December 31, 2007 during which we recognized a one-time license payment from Novartis. At March 31, 2016, we had an accumulated deficit of $219.0 million, primarily as a result of research and development and general and administrative expenses. While we may in the future generate revenue from a variety of sources, including license fees, milestone payments, and research and development payments in connection with strategic partnerships, our product candidates may never be successfully developed or commercialized and we may therefore never realize revenue from any product sales, particularly because most of our product candidates are at an early stage of development. Accordingly, we expect to continue to incur substantial losses from operations for the foreseeable future, and there can be no assurance that we will ever generate significant revenue or profits.

Our operations during the quarter ended March 31, 2016 primarily related to our status as a debtor in possession and other matters in connection with our Chapter 11 bankruptcy proceedings, in addition to our efforts to obtain certain rights related to our lead product candidate benznidazole. Accordingly, comparisons of our operations and results for the quarter ended March 31, 2016 to our prior year operations and results may only provide a limited benefit, and similarly should not be relied on as an indicator of our future operations or results.

Research and Development Expenses

Conducting research and development is central to our business model. We expense both internal and external research and development costs as incurred. We track external research and development costs incurred by project for each of our clinical programs. We began tracking our external costs by project beginning January 1, 2008, and we have continued to refine our systems and our methodology in tracking external research and development costs. Our external research and development costs consist primarily of:

- expenses incurred under agreements with contract research organizations, investigative sites, and consultants that conduct our clinical trials and a substantial portion of our preclinical activities;
- the cost of acquiring and manufacturing clinical trial and other materials; and
- other costs associated with development activities, including additional studies.

Other research and development costs consist primarily of internal research and development costs, such as salaries and related fringe benefit costs for our employees (such as workers compensation and health insurance premiums), stock-based compensation charges, travel costs, lab supplies, overhead expenses such as rent and utilities, and external costs not allocated to one of our clinical programs. Internal research and development costs generally benefit multiple projects and are not separately tracked per project.

The following table shows our total research and development expenses for the three months ended March 31, 2016 and 2015 and for the period from January 1, 2008 to March 31, 2016:

	Three Months Ended March 31,		For the Period from January 1, 2008 to
(In thousands)	**2016**	**2015**	**March 31, 2016**
External costs:			
KB001	$ 5	$ 1,014	$ 33,761
Lenzilumab	77	313	40,580
Ifabotuzumab	115	2,011	36,954
Benznidazole	847	-	847
Internal costs	660	2,567	74,742
Total research and development	$ 1,704	$ 5,905	$ 186,884

General and Administrative Expenses

General and administrative expenses consist principally of personnel-related costs, professional fees for legal, consulting, audit and tax services, rent and other general operating expenses not otherwise included in research and development.

Comparison of Three Months Ended March 31, 2016 and 2015

(in thousands)	Three Months Ended March 31, 2016	2015	Increase/ (Decrease) in thousands	%
Operating expenses:				
Research and development	$ 1,704	$ 5,905	$ (4,201)	-71%
General and administrative	1,205	3,437	(2,232)	-65%
Loss from operations	(2,909)	(9,342)	(6,433)	-69%
Interest expense	-	(280)	(280)	-100%
Interest income	-	16	(16)	-100%
Other expense, net	-	(16)	(16)	-100%
Reorganization items, net	(2,517)	-	2,517	100%
Net loss	$ (5,426)	$ (9,622)	$ (4,228)	-44%

Research and development expenses decreased $4.2 million, from $5.9 million for the three months ended March 31, 2015 to $1.7 million for the three months ended March 31, 2016. The decrease is due to the suspension of essentially all development projects until after our emergence from bankruptcy on June 30, 2016, offset by expenses of $847,000 related to the acquisition of certain rights related to benznidazole and certain other payments made pursuant to the Agreement for the Manufacture, Development and Commercialization of Benznidazole for Human Use, or the MDC Agreement, with Savant.

General and administrative expenses decreased $2.2 million, from $3.4 million for the three months ended March 31, 2015 to $1.2 million for the three months ended March 31, 2016, due to the restructuring activities that took place primarily in the last quarter of 2015 resulting in, among other things, a decrease of approximately 70% of our workforce.

Reorganization items, net for the three months ended March 31, 2016 were $2.5 million, compared to none for the three months ended March 31, 2016. The reorganization items relate to amounts incurred during the quarter related to our reorganization activities and the bankruptcy plan, including legal fees of $2.5 million and professional fees of $0.2 million, offset by a net gain on the termination of the lease of our former South San Francisco office of $0.2 million.

Interest expense of $0.3 million recognized for the three months ended March 31, 2015 was related to the Loan and Security Agreement with MidCap Financial SBIC LP that was entered into by the Company in September 2012. The loan was paid off in the fourth quarter of 2015.

Interest income and Other expense, net, for the three months ended March 31, 2015 primarily consist of interest earned on our cash and cash equivalents, foreign currency gains and losses and realized gains and losses on the sale of investments. There was no Interest income and Other expense, net, for the three months ended March 31, 2016.

Liquidity and Capital Resources

Since our inception, we have financed our operations primarily through proceeds from the public offerings of our common stock, private placements of our preferred stock, debt financings, interest income earned on cash and cash equivalents and marketable securities, borrowings against lines of credit, and receipts from agreements with Sanofi and Novartis. At March 31, 2016, we had cash and cash equivalents of $6.6 million.

The following table sets forth the primary sources and uses of cash and cash equivalents for each of the periods presented below:

(in thousands)	Three Months Ended March 31, 2016	2015
Net cash used in operating activities	$ (1,997)	$ (9,015)
Net cash provided by investing activities	143	12,011
Net cash used in financing activities	—	(1,295)
Net (decrease) increase in cash and cash equivalents	$ (1,854)	$ 1,701

Net cash used in operating activities was $2.0 million and $9.0 million for the three months ended March 31, 2016 and 2015, respectively. The primary use of cash in 2015 was to fund our operations related to the development of our product candidates in 2015, whereas the primary use of cash in 2016 was to fund our operations related to our reorganization activities and the bankruptcy plan. Cash used in operating activities of $2.0 million for the three months ended March 31, 2016 primarily related to our net loss of $5.4 million, adjusted for non-cash items, such as a gain on lease termination of $0.2 million and net cash outflows of $3.6 million related to changes in operating assets and liabilities, primarily accounts payable and accrued expenses.

Net cash used in operating activities of $9.0 million for the three months ended March 31, 2015 primarily related to our net loss of $9.6 million, adjusted for non-cash items, such as $0.3 million of stock-based compensation expense, $0.8 million related to the fair value of stock options that were modified due to executive retirement and restructuring activities, other non-cash items of $0.2 million and net cash outflows of $0.7 million related to changes in operating assets and liabilities.

Net cash provided by investing activities was $0.1 million for the three months ended March 31, 2016, primarily related to the reduction in restricted cash related to the termination of our former office lease in South San Francisco. Net cash provided by investing activities was $12.0 million for the three months ended March 31, 2015, primarily related to proceeds from maturities of marketable securities of $15.8 million, partially offset by purchases of investments of $3.7 million.

Net cash used in financing activities was $0 for the three months ended March 31, 2016. Net cash used in financing activities was $1.3 million for the three months ended March 31, 2015, and consisted primarily of payments on our borrowings.

In connection with our emergence from bankruptcy, on June 30, 2016 we closed an $11 million financing that provided the funds required to enable our exit from Chapter 11, as well as to fund our current working capital needs. However, we will require substantial additional capital to support our business efforts, including obtaining regulatory approvals for benznidazole or other product candidates, clinical trials and other studies, and, if approved, the commercialization of our product candidates. The amount of capital we will require and the timing of our need for additional capital will depend on many factors, including:

- the type, number, timing, progress, costs, and results of the product candidate development programs that we are pursuing or may choose to pursue in the future;
- the scope, progress, expansion, costs, and results of our pre-clinical and clinical trials;
- the timing of and costs involved in obtaining regulatory approvals;
- our ability to establish and maintain development partnering arrangements and any associated funding;
- the emergence of competing products or technologies and other adverse market developments;
- the costs of maintaining, expanding, and protecting our intellectual property portfolio, including potential litigation costs and liabilities;
- the resources we devote to marketing, and, if approved, commercializing our product candidates;
- the scope, progress, expansion and costs of manufacturing our product candidates; and
- the costs associated with being a public company.

We anticipate that in the future we will seek additional financing from a number of sources, including, but not limited to, the sale of equity or debt securities, strategic collaborations, and licensing of our product candidates. Additional funding may not be available to us on a timely basis or at acceptable terms, if at all. Our ability to access capital when needed is not assured and, if not achieved on a timely basis, would materially harm our business, financial condition and results of operations. If adequate funds are not available, we may be required to delay, reduce the scope of, or eliminate one or more of our development programs. We may also be required to sell or license to others our technologies, product candidates, or development programs that we would have preferred to develop and commercialize ourselves and on less than favorable terms, if at all.

If management is unsuccessful in efforts to raise additional capital, based on our current levels of operating expenses, our current capital is not expected to be sufficient to fund our operations for the next twelve months. These conditions raise substantial doubt about our ability to continue as a going concern.

On January 13, 2016, our common stock was suspended from the Nasdaq Global Market and began trading on the over-the-counter market under the ticker symbol KBIOQ. On January 26, 2016, NASDAQ filed a Form 25 with the Securities and Exchange Commission to complete the delisting of our common stock, and the delisting was effective on February 5, 2016. Although our common stock is listed for quotation on the OTC Pink marketplace operated by OTC Markets Group, Inc., trading is limited and an active market for our common stock may never develop in the future, which could harm our ability to raise capital to continue to fund operations.

Off-Balance Sheet Arrangements

We currently have no off-balance sheet arrangements, such as structured finance, special purpose entities or variable interest entities.

Item 4. Controls and Procedures.

Management's Evaluation of our Disclosure Controls and Procedures

"Disclosure controls and procedures," as defined in Rules 13a-15(e) and 15d-15(e) promulgated under the Securities Exchange Act of 1934, as amended, or the Exchange Act, means controls and other procedures that are designed to ensure that information required to be disclosed by us in the reports that we file or submit under the Exchange Act is recorded, processed, summarized and reported within the time periods specified in the SEC's rules and forms.

Disclosure controls and procedures include, without limitation, those designed to ensure that this information is accumulated and communicated to our management to allow timely decisions regarding required disclosure. Management, including our Chief Executive Officer and Interim Chief Financial Officer, has evaluated the effectiveness of our disclosure controls and procedures as of the end of the period covered by this report. Based upon the evaluation and in light of our inability to timely file this Quarterly Report on Form 10-Q, our Chief Executive Officer and Interim Chief Financial Officer concluded that the disclosure controls and procedures were not effective as of March 31,2016 to ensure that information required to be disclosed in the reports we file and submit under the Exchange Act is (i) recorded, processed, summarized and reported as and when required and (ii) accumulated and communicated to our management, including our Chief Executive Officer and Interim Chief Financial Officer, as appropriate to allow timely discussion regarding required disclosure.

Changes in Internal Control Over Financial Reporting

Our management is responsible for establishing and maintaining adequate internal control over financial reporting (as defined in Rule 13a-15(f) and 15d-15(f) under the Exchange Act). Our Chief Executive Officer and Interim Chief Financial Officer assessed the effectiveness of our internal control over financial reporting as of March 31, 2016. In making this assessment, our Chief Executive Officer and Interim Chief Financial Officer used the criteria set forth by the Committee of Sponsoring Organizations of the Treadway Commission, or COSO", in *Internal Control—Integrated Framework*. Based on that assessment and using the COSO criteria, our Chief Executive Officer and Interim Chief Financial Officer have concluded that, as of March 31, 2016, our internal control over financial reporting was not effective because of the material weaknesses described below.

A material weakness is defined as "a deficiency, or a combination of deficiencies in internal control over financial reporting, such that there is a reasonable possibility that a material misstatement of the company's annual or interim financial statements will not be prevented or detected on a timely basis."

The ineffectiveness of our internal control over financial reporting was due to the following material weaknesses which each reflect our limited number of accounting and financial reporting personnel and high levels of turnover in our personnel responsible for performing activities related to our internal control over financial reporting: (i) an inability to complete our financial statement close process in a timely and accurate manner; (ii) an insufficient degree of segregation of duties amongst our accounting and financial reporting personnel; and (iii) a lack of technical competency in review and approval of financial reporting processes.

During 2016, our management intends to work to remediate the material weaknesses identified above, which could include the addition of accounting and financial reporting personnel and/or the engagement of accounting and personnel consultants on a limited-time basis until we add a sufficient number of personnel.

Despite the existence of the material weaknesses above, we believe that our Condensed Consolidated Financial Statements contained in this Form 10-Q fairly present our financial position, results of operations and cash flows as of and for the periods presented in all material respects.

Other than as described above, there has been no change in our internal control over financial reporting during the quarter ended March 31, 2016, that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

Inherent Limitations of Controls

Management does not expect that our disclosure controls and procedures or our internal control over financial reporting will prevent or detect all error and all fraud. Controls and procedures, no matter how well designed and operated, can provide only reasonable assurance of achieving their objectives and management necessarily applies its judgment in evaluating the cost-benefit relationship of possible controls and procedures. Because of the inherent limitations in all control systems, no evaluation of controls can provide absolute assurance that all control issues and instances of fraud, if any, within the Company have been detected. These inherent limitations include the realities that judgments in decision-making can be faulty, and that breakdowns can occur because of a simple error or mistake. Additionally, controls can be circumvented by the individual acts of some persons, by collusion of two or more people, or by management override of the controls. The design of any system of controls also is based in part upon certain assumptions about the likelihood of future events, and there can be no assurance that any design will succeed in achieving its stated goals under all potential future conditions. Over time, controls may become inadequate because of changes in conditions, or deterioration in the degree of compliance with the policies or procedures. Because of the inherent limitations in a cost-effective control system, misstatements due to error or fraud may occur and not be detected.

PART II. OTHER INFORMATION

Item 6. Exhibits.

A list of exhibits is set forth on the Exhibit Index immediately following the signature page of this Quarterly Report on Form 10-Q, and is incorporated herein by reference.

SIGNATURES

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

KALOBIOS PHARMACEUTICALS, INC.

Date: September 23, 2016

By: /s/ Cameron Durrant
Cameron Durrant
Chief Executive Officer
(Principal Executive Officer)

Date: September 23, 2016

By: /s/ Dean Witter, III
Dean Witter, III
Interim Chief Financial Officer
(Principal Financial and Accounting Officer)

EXHIBIT INDEX

Exhibit No.	Description
10.1†	Binding Letter of Intent, dated February 29, 2016, between the Registrant and Savant Neglected Diseases, LLC.
10.2*	Letter Agreement, dated March 1, 2016, between the Registrant and Cameron Durrant, M.D.
31.1	Certification of Chief Executive Officer of the Registrant, as required by Rule 13a-14(a) or Rule 15d-14(a) of the Securities Exchange Act of 1934, as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
31.2	Certification of Interim Chief Financial Officer of the Registrant, as required by Rule 13a-14(a) or Rule 15d-14(a) of the Securities Exchange Act of 1934, as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
32.1**	Certification by the Chief Executive Officer, as required by Rule 13a-14(b) or Rule 15d-14(b) and Section 1350 of Chapter 36 of Title 18 of the United States Code (18 U.S.C. §1350).
32.2**	Certification by the Interim Chief Financial Officer, as required by Rule 13a-14(b) or Rule 15d-14(b) and Section 1350 of Chapter 36 of Title 18 of the United States Code (18 U.S.C. §1350).
101.INS	XBRL Instance Document
101.SCH	XBRL Taxonomy Extension Schema Document
101.CAL	XBRL Taxonomy Extension Calculation Linkbase Document
101.DEF	XBRL Taxonomy Extension Definition Linkbase Document
101.LAB	XBRL Taxonomy Extension Label Linkbase Document
101.PRE	XBRL Taxonomy Extension Presentation Linkbase Document

† Confidential Treatment has been requested with respect to certain portions of this exhibit. Omitted portions have been filed separately with the Securities and Exchange Commission.

* Indicates management contract or compensatory plan.

** The Certifications attached as Exhibits 32.1 and 32.2 that accompanies this Quarterly Report on Form 10-Q are not deemed filed with the Securities and Exchange Commission and are not to be incorporated by reference into any filing of KaloBios Pharmaceuticals, Inc. under the Securities Act of 1933, as amended, or the Securities Exchange Act of 1934, as amended, whether made before or after the date of this Form 10-Q, irrespective of any general incorporation language contained in such filing.

Exhibit 10.1

[***] INDICATES MATERIAL THAT WAS OMITTED AND FOR WHICH CONFIDENTIAL TREATMENT WAS REQUESTED. ALL SUCH OMITTED MATERIAL WAS FILED SEPARATELY WITH THE SECURITIES AND EXCHANGE COMMISSION PURSUANT TO RULE 24b-2 PROMULGATED UNDER THE SECURITIES EXCHANGE ACT OF 1934, AS AMENDED.

February 22, 2016

Via E-Mail

Savant Neglected Diseases, LLC
Attn: Stephen L. Hurst, JD
[***]

Mailing Address:
P.O. Box 620732
Woodside, CA 94062

Street Address:
740 Bair Island Road #106
Redwood City, CA 94063

Ladies and Gentlemen:

This binding letter of intent (this "**Letter**") outlines the basic terms and conditions of the proposed acquisition of certain regulatory and non-intellectual property assets (the "**Regulatory and Other Assets**") and the proposed exclusive license of intellectual property assets not constituting Regulatory and Other Assets (the "**IP Assets**") (together, the "**Transaction**") by KaloBios Pharmaceuticals, Inc., a Delaware corporation (the "**Purchaser**"), in each case of the worldwide rights in and relating to benznidazole for human use (the "**Product**") owned by Savant Neglected Diseases, LLC, a Delaware limited liability company (the "**Company**"). Without limiting the foregoing, the Regulatory and Other Assets shall include (i) all relevant existing inventories, (ii) all INDs and foreign equivalents and all other regulatory filings and documentation related thereto, and (iii) all asset-related agreements and arrangements, including manufacturing and other agreements and arrangements; and the IP Assets shall include (i) inventions, patents, copyrights, domains and trademarks, and all applications and registrations with respect thereto, (ii) all trade secrets, know-how and confidential information related thereto. The Definitive Agreement (as defined below) shall include schedules of the Regulatory and Other Assets, which shall include documentation, records, data, information and materials pertaining to the Product, as well as schedules of IP Assets. Except for obligations of the Purchaser hereunder, the Company shall remain liable for, and the Purchaser shall not assume or become obligated for, any debts, liabilities or obligations whatsoever of the Company, including, without limitation, taxes, the indebtedness of the Company and any liabilities or obligations accrued but not yet satisfied or paid prior to the closing of the transactions contemplated by this Letter. Further, the parties will cooperate to structure the transaction in a tax-efficient, mutually acceptable manner.

1. Basic Terms.

A. Structure.

The parties intend to jointly develop the Product and for the Purchaser to fund such development. Further, the Purchaser will be identified as the sponsor for, and will own, all FDA filings relating to the Product. The Purchaser will acquire the Regulatory and Other Assets at closing of the Transaction (the "**Closing**"). Without limiting the foregoing, the Closing shall occur upon the satisfaction of the "conditions to closing," set forth in the Definitive Agreement, which conditions shall include obtaining a judicial order approving the Transaction and the effective date of the Purchaser's plan of reorganization (the "**Bankruptcy Exit**"). The Company will exclusively license the IP Assets to the Purchaser and the Purchaser will non-exclusively license its development data and results (as further defined in the Definitive Agreement) to the Company exclusively for use in the Company Field. Also at the Closing, the Purchaser will grant the Company a non-exclusive, perpetual, irrevocable, royalty-free license to the IP Assets to develop and commercialize veterinary products (the "**Retained Field**") and the right of reference to the information included in the submissions to the FDA for the Product solely for use in the Retained Field.

B. Development Matters.

a. The parties acknowledge that time is of the essence with respect to the matters set forth in this Letter and the development of the Product. Upon execution of this Letter (including prior to Bankruptcy Exit), the Purchaser shall pay the Company eighty-seven thousand, five hundred dollars ($87,500) per month in advance for services performed by [***] full time employees towards development of the Assets in accordance with a mutually agreed development plan (the "**Development Services**").

b. Immediately upon execution of this Letter by both parties, the parties shall establish a joint steering committee with equal representation and voting rights (the "**JSC**") to oversee the collaboration and the activities of the parties under the Development Program and the Commercialization Program (each, as defined below). All other joint committees under the Definitive Agreement, including the JDC and JCC (each, as defined below), shall be subordinate to the JSC. The JSC shall meet at least once annually, and during the term of the Development Program, the JDC shall meet at least once quarterly. From time to time, the JSC, JDC or JCC may establish subcommittees and project teams, with equal representation, to oversee activities, day-to-day operations, and particular projects under the collaboration.

c. Each party shall make all decisions and conduct all of its obligations under the collaboration in a manner in its good faith determination to be consistent with and in accordance with agreed upon guiding principles, including the following: (i) maximize the overall value of the Product to stakeholders, including patients, (without consideration to any particular product or the payments between the parties hereunder); (ii) conduct the development and manufacture of the Product in a coordinated manner, with each party actively participating with defined roles and responsibilities; and (iii) use Diligent Efforts to pursue the best combination of quality, safety, effectiveness and speed in the development and manufacture of the Product.

d. Concurrent with the execution of this Letter, the parties shall establish a joint development committee with equal representation and voting rights (the "**JDC**"). Subject to the JDC's oversight, the parties shall prepare, and use Diligent Efforts to conduct, a development program for the Product (including the conduct of clinical and regulatory activities) on a collaborative basis (the "**Development Program**") in accordance with a plan and budget established and approved by the JDC (the "**Development Plan**"). Until the Closing or the JDC approves a new work plan and cost estimate ("**WPCE**") the WPCE attached hereto shall govern the Development Program.

e. Each party shall have the right to propose to the JDC specific development activities for the Product for inclusion in the Development Plan. The JDC shall assign responsibilities to each party under such Development Plan, including with respect to clinical development, based upon each party's expertise, capabilities and infrastructure and overall project budget.

f. Each party shall take the lead and be responsible for those activities assigned to it under such Development Plan, and shall report to the JDC, at least on a quarterly basis, the progress and results of activities for which it is responsible under the applicable Development Plan.

g. Without limiting the foregoing, the parties shall use "**Diligent Efforts**" (to be defined in the Definitive Agreement) to develop and obtain regulatory approval for the Product as soon as reasonably practicable in the United States.

h. The Purchaser shall fund the development costs incurred by the parties in accordance with the Development Plan. The Development Services will be paid by the Purchaser [***] and otherwise on the terms and conditions set forth in the Definitive Agreement.

i. Prior to filing the US NDA, the parties shall establish a joint commercialization committee with equal representation (the "**JCC**") to oversee the Commercialization Program.

j. Subject to the JCC's oversight, the Purchaser shall assess an optimal commercialization program to commercialize the Product (the "**Commercialization Program**") in accordance with a plan established by Purchaser, which plan may include out-licensing or partnering commercial rights to the Product (the "**Commercialization Plan**").

k. The Purchaser shall take the lead and be responsible for all activities under the Commercialization Plan and shall report to the JCC, at least on an annual basis, the progress and results of such activities. Without limiting the foregoing, Purchaser shall use Diligent Efforts to support launch of the Product in the United States as soon as reasonably practicable following regulatory approval for the benefit of stakeholders, including patients.

l. If the JDC or JCC is unable to reach consensus on a matter, it shall refer such matter to the JSC for decision. If the JSC is unable to reach consensus on a particular matter, then it shall escalate such matter to the parties' respective CEOs. If the CEOs are not able to resolve a particular dispute, such dispute will be decided by whichever party has final decision making responsibility with respect to such matter in the Definitive Agreement, or if no party has final say, then the matter will be submitted for binding arbitration in the manner as specified in this Letter or as otherwise set forth in the Definitive Agreement.

C. Drug Pricing Matters.

The parties will pledge in the Definitive Agreement that no patient in need of the Product living within a country within the jurisdiction of any regulatory approvals will be denied access to the Product because of an inability to pay for the drug meaning that reasonable efforts will be made to ensure industry standard access programs will be in place to support the launch. An example of an industry standard access program is a patient assistance program.

D. Consideration for the Regulatory and Other Assets.

The Purchaser will make the following payments as consideration for the Regulatory and Other Assets:

a. Three million dollars ($3,000,000) payable as soon as is practicable but in no event later than the Bankruptcy Exit (the "**Initial Payment**"); and

b. A five-year warrant from the date of Bankruptcy Exit exercisable at a per share price of $2.25, for 200,000 shares of Common Stock of the Purchaser with 25% of the shares immediately exercisable and an additional [***] of the shares being exercisable upon each of the following events: [***]. The parties agree the face value of this warrant is $100. To the extent permitted under applicable law, including securities and bankruptcy laws, the warrants and shares underlying the warrants will be freely tradable.

c. Additional payments totaling twenty-one million dollars ($21,000,000) shall be paid by the Purchaser to the Company upon consummation of the following development goals (each, a "**Milestone Payment**"): [***]. The occurrence of a change of control of the Purchaser will cause [***] of all unpaid binding and ongoing Milestone Payments to become due and payable immediately by the Purchaser to the Company, irrespective of whether the payment event has occurred. Upon payment of the amount pursuant to the preceding sentence, all unpaid Milestone Payments shall be reduced, ratably, by the amount paid.

d. Prior to the payment in full of all obligations by the Purchaser, the Company shall be granted a senior security interest ("**Senior Security Interest**") over the Regulatory and Other Assets and any resulting developments therefrom. The Senior Security Interest secures all payments due and owing the Company by Purchaser under the Transaction. The terms of the Senior Security Interest shall be set forth in a Security Agreement to be executed by the parties at Closing.

e. Following (A) the Purchaser's receipt of a Priority Review Voucher (the " **Voucher**") and (B) the Purchaser's sale of the Voucher, the Purchaser shall pay to the Company an amount equal to [***] from the Purchaser's sale of the Voucher. In the event that the Purchaser or its affiliate(s) does not engage in a sale of the voucher and instead uses the voucher for its own benefit, the Definitive Agreement will set forth a mechanism to value the Voucher and for the Company to receive an amount equal to [***] of that value.

E. The IP Assets.

a. Under the Definitive Agreements, the Purchaser shall be granted an exclusive world-wide royalty-bearing, sub-licensable license to the IP Assets. Such license will provide for the following payments:

b. The Purchaser will pay to the Company [***] payments, on a [***] basis, equal to [***] of the global Net Sales (as defined below) of the Product, while the Assets have regulatory exclusivity in the applicable jurisdiction, made by the Purchaser or any party deriving Product marketing rights from the Purchaser or any of its affiliates.

c. Net Sales means the full invoiced price for all Products ("**Gross Sales**") sold to customers less the following deductions:

i. transportation and insurance charges related to the delivery of the Products to customers;

ii. normal trade, volume and cash discounts, including retroactive price reductions, pertaining to the sale of the Products;

iii. any service fees actually paid to customers as a requirement for the stocking and subsequent re-distribution of the Products;

iv. credits, allowances or refunds given or made to customers for rejection, damage, defect, recall or return of the Products to the Purchaser by customers;

v. sales and excise taxes, value added taxes, other taxes (excluding income taxes) or other governmental charges otherwise imposed upon the amounts billed for the Products, as adjusted for rebates and refunds or duties that fall due or are absorbed or otherwise imposed on or paid by the Purchaser on sales of Products and other governmental charges imposed upon the importation or sale of the Products;

vi. chargebacks and rebates to third parties in the applicable reporting quarter, including, without limitation, to managed care health organizations, federal and state government agencies, and/or other purchasers of the Products, and group purchasing organization administration fees;

vii. the amount of the rebate that is provided or credited with respect to couponing, a patient assistance program, a patient insurance co-pay program or any program designed to provide a discount to the patient for the cost of a prescription for the Products;

viii. delayed shipping credits, discounts or payments related to the impact of Product price increases between purchase dates and shipping dates; and fees for service payments to customers for non-separable services (including compensation for maintaining agreed Product inventory levels and providing Product-related information); and

ix. all such deductions being supported by reasonable written documentation provided by the Purchaser in the quarterly payment reports.

d. The Company and their financial representatives shall be entitled to audit the [***] payment reports, but not more than [***] per calendar year.

e. The license shall be terminable by the Company upon the occurrence of certain events set forth in the Definitive Agreement, which events are customary for licensors to be able to terminate licenses, such as a material breach of the provisions of the license or the Purchaser's material breach of its obligations in the Definitive Agreement(s). Additionally, the license shall be terminable by the Company if Martin Shkreli is appointed as an agent, employee, consultant, officer or director of the Purchaser.

2. Deposit.

Concurrent with the mutual execution of this Letter, the Purchaser will make a non-refundable deposit in respect of the Transaction of five hundred thousand dollars ($500,000) (the "**Deposit**") to be credited towards the Initial Payment.

3. Definitive Agreement.

The parties will enter into one or more definitive agreements (together, the "**Definitive Agreement(s)**") in respect of the Transaction. As a condition to the Closing, the Company will receive a legal opinion from the Purchaser's counsel concerning the validity and enforceability of the transactions contemplated hereby. The Definitive Agreement will contain a Closing condition for a Bankruptcy Exit with an unencumbered cash balance of $10,000,000 (inclusive of the Initial Payment). The Definitive Agreement will provide for a covenant that, if determined by the Board of Directors of the Purchaser to be in the best interests of the Purchaser, the Purchaser shall use diligent efforts to regain a listing for its Common Stock on a national securities exchange

4. Conditions.

The Purchaser will use best efforts to seek bankruptcy court approval for any pre-Bankruptcy Exit payments and for the transactions contemplated hereby to the extent required.

5. Due Diligence.

Each party will provide to the other, including their directors, officers, employees, agents, lenders, investors, funding sources, counsel, accountants, consultants or advisors ("**Representatives**"), complete access to all of their books, records, premises, personnel, customers and suppliers for purposes of further the transactions contemplated hereby, subject to a party's obligations to a third party to maintain the confidentiality of that third party's information. The Purchaser agrees that all information so provided will be treated by the parties, including their Representatives, as Confidential Information in accordance with the Confidential Disclosure Agreement dated December 1, 2015, between the Company and the Purchaser (the "**CDA**").

6. Closing and Termination.

The date of Closing shall be as agreed upon by the parties in the Definitive Agreement. This Letter and the obligations of the parties other than those in the CDA will terminate upon the earliest of (i) June 30, 2016, if the Purchaser has not consummated a Bankruptcy Exit with an unencumbered cash balance of $10,000,000 (inclusive of the Initial Payment), (ii) the date upon which the bankruptcy court orders the conversion of Purchaser's present Chapter 11 bankruptcy proceedings into a Chapter 7 dissolution proceeding, (iii) any criminal indictment of any officer or director of the Purchaser if that indictment is reasonable expected to have a material adverse effect on the Transaction, or (iv) any material breach of any representation or warranty of the Purchaser, or (v) any material breach by the Purchaser of any obligations herein, which following written notice thereof, is not cured within 15 days thereafter. The period commencing on the date that this Letter is signed by both parties and continuing until the earliest to occur of the events set forth in subsections (i) through (v), above, shall be referred to as the "**Exclusivity Period**").

During the Exclusivity Period, the Company shall not, nor shall it affirmatively permit any of its affiliates, shareholders, directors, managers, officers or employees to, nor shall it authorize any of its or its affiliates, shareholders, representatives, advisors, bankers or agents to, directly or indirectly (together, the "**Company Parties**"), (i) solicit, initiate, or encourage the submission of any proposal or indication of interest relating to an Alternative Transaction, (ii) participate in any discussions or negotiations regarding, or furnish to any person or entity any non-public information with respect to, or knowingly take any other action to facilitate any inquiries or the making of any proposal that constitutes, or may reasonably be expected to lead to, an Alternative Transaction or (iii) authorize, consummate or engage in, or enter into any agreement or understanding with respect to, an Alternative Transaction. Immediately upon the commencement of the Exclusivity Period, the Company will cease and cause to be terminated any and all discussions and negotiations with all persons and entities (other than the Purchaser and its affiliates) regarding any Alternative Transaction or any other transaction that could reasonably be expected to lead to an Alternative Transaction. The Company will promptly inform the Purchaser of any offer, proposal or expression of interest for the Product (whether written or oral) or any portion thereof that it or any of its affiliates, representatives or advisors may receive during the Exclusivity Period.

For purposes hereof, "**Alternative Transaction**" means any (i) merger, consolidation, investment, share exchange or sale, or other similar transaction involving all or any portion of the equity securities of the Company or any of its subsidiaries that could, in the reasonable determination of the Purchaser, result in the interruption of the Development Services being provided by the Company, (ii) any sale, license or other disposition of all or any material portion of the assets related to the Product, or (iii) any other transaction involving the Company, any of its subsidiaries or shareholders or any of their respective representatives or affiliates that would intentionally prevent, impede or materially delay the Transactions.

Notwithstanding the Exclusivity Period, the Company Parties are free to solicit and sell securities at any time, so long as the Development Services continue on an uninterrupted basis, and the Company Parties are free to solicit and conduct any collaboration or partnering transactions for other assets not to be purchased by or licensed to the Purchaser in connection with the Transaction, in either case, on the condition that any transaction permitted pursuant to this paragraph that results in a change in control of the Company will provide that the acquiring party in the change in control transaction commit in writing to pursue the Transaction.

7. Public Announcement.

All press releases and public announcements relating to the Transaction will be jointly prepared; provided, that either party may make a public announcement relating to the Transaction required by applicable law or an applicable listing rule or regulation.

8. Expenses.

Each party will pay all of its own expenses, including legal fees, incurred in connection with the Transaction; provided that upon Bankruptcy Exit, the Purchaser shall reimburse the Company for all of its documented additional legal expenses and other expenses resulting from the Purchaser's bankruptcy proceedings incurred between December 17, 2015 and the Bankruptcy Exit, not to exceed one hundred thousand dollars ($100,000).

9. Representations and Warranties of the Purchaser; Covenants of the Purchaser.

The Purchaser hereby makes the representations and warranties on Exhibit A hereto to the Company. The Purchaser hereby covenants to the obligations on Exhibit A hereto.

10. Binding Agreement.

The parties intend to negotiate and document the Transaction subsequent to the date of this Letter. The failure of the parties to reach a mutually acceptable Definitive Agreement prior to June 30, 2016 shall be subject to arbitration pursuant to the procedures below.

11. Arbitration.

To the greatest extent permitted by applicable law, any dispute, claim or controversy arising out of or relating to this Letter or the breach, termination, enforcement, interpretation or validity thereof, including the determination of the scope or applicability of this Letter to arbitrate, shall be determined by binding arbitration in San Francisco, California. Prior to initiating arbitration proceedings, a party notify the other party in writing of such dispute, claim or controversy and request a good faith negotiation between executives who have authority to settle the controversy. In the event the parties fail to reach agreement to either resolve their dispute, claim or controversy or to continue their negotiations within [***] of the delivery of such written request, either party may initiate binding arbitration proceedings. The arbitration shall be administered by JAMS pursuant to JAMS' Streamlined Arbitration Rules and Procedures. Judgment on the Award may be entered in any court having jurisdiction. This clause shall not preclude parties from seeking provisional remedies in aid of arbitration from a court of appropriate jurisdiction. For any dispute, claim or controversy arising prior to the execution of a Definitive Agreement, the arbitration shall be before [***] unless otherwise specified herein. The arbitrator must be [***]. If no individual satisfies the foregoing requirement, the arbitration shall be administered by [***], [***] of whom must be [***], another [***] of whom must be [***], and those [***] individuals shall appoint [***].

Each party will be responsible for its costs and attorneys' fees incurred in connection with the arbitration; provided that the arbitrator(s) shall have the discretion to award an appropriate percentage of the costs and attorneys' fees reasonably incurred if such party demonstrates to the arbitrator(s) satisfaction that the other party acted in bad faith in the negotiation of the Definitive Agreement or any agreement related thereto or in bad faith in the arbitration.

12. Governing Law.

This Letter shall be governed by and construed in accordance with the laws of the State of Delaware, which shall be the proper law hereof notwithstanding any rule or principle of conflict of laws under which any other body of law would be made applicable. The parties acknowledge that this Letter evidences a transaction involving interstate commerce. Notwithstanding the provision in the preceding paragraph with respect to applicable substantive law, any arbitration conducted pursuant to the terms of this Letter shall be governed by the Federal Arbitration Act (9 U.S.C., Secs. 1-16).

[Signature Page to Follow]

[***] INDICATES MATERIAL THAT WAS OMITTED AND FOR WHICH CONFIDENTIAL TREATMENT WAS REQUESTED. ALL SUCH OMITTED MATERIAL WAS FILED SEPARATELY WITH THE SECURITIES AND EXCHANGE COMMISSION PURSUANT TO RULE 24b-2 PROMULGATED UNDER THE SECURITIES EXCHANGE ACT OF 1934, AS AMENDED.

If the foregoing accurately reflects the basic terms and conditions upon which the Company would be willing to consummate the Transaction contemplated by this Letter, please sign one copy of this Letter and return it to the undersigned, in which case both parties are acknowledging their intent to comply with the terms and conditions hereof, some of which, as set forth above, are binding commitments.

Very truly yours,

KALOBIOS PHARMACEUTICALS, INC.

By: /s/ Cameron Durrant
Dr. Cameron Durrant, MD, MBA
Chairman of the Board

Agreed to this 29 day of February, 2016

SAVANT NEGLECTED DISEASES, LLC

By: /s/ Stephen L. Hurst
Stephen L. Hurst
Managing Member

[***] INDICATES MATERIAL THAT WAS OMITTED AND FOR WHICH CONFIDENTIAL TREATMENT WAS REQUESTED. ALL SUCH OMITTED MATERIAL WAS FILED SEPARATELY WITH THE SECURITIES AND EXCHANGE COMMISSION PURSUANT TO RULE 24b-2 PROMULGATED UNDER THE SECURITIES EXCHANGE ACT OF 1934, AS AMENDED.

Exhibit A

Representations and Warranties of the Purchaser

As of the date first set forth above, the Purchaser represents and warrants to the Company as follows:

a. It is a corporation duly organized, validly existing, and in good standing under the laws of the jurisdiction in which it was incorporated or formed;

b. Subject only to the bankruptcy court's discretionary authority with respect to the granting of a decree ordering specific performance or other equitable remedies, (i) it has the full power and authority and the legal right to enter into this Letter; (ii) it has taken all necessary governance action on its part required to authorize the execution and delivery of this Letter and the performance of its obligations hereunder; and (iii) the Letter has been duly executed and delivered on behalf of the Purchaser, and constitute legal, valid, and binding obligations of the Purchaser that are enforceable against it in accordance with their terms;

c. The Purchaser has adequate cash on hand to fund all cash payments to the Company from the Purchaser required to be made under this Letter prior to the Bankruptcy Exit (but not including those payments required to be made under the Definitive Agreement).

d. Other than bankruptcy court approval, the execution and delivery of the Letter, the performance of the Purchaser's obligations hereunder (i) do not and will not conflict with or violate any requirement of applicable law; (ii) do not and will not conflict with or violate the certificate of incorporation, bylaws or other organizational documents of the Purchaser; and (iii) do not and will not conflict with, violate, breach or constitute a default under any contractual obligations of the Purchaser or any of its affiliate(s);

e. There are no actions, suits, claims, investigations or other legal proceedings pending or, to the Purchaser's knowledge, threatened against or by the Purchaser or any affiliate(s) of the Purchaser that challenge or seek to prevent, enjoin or otherwise delay the transactions contemplated by the Letter other than the Purchaser's present bankruptcy proceedings; and

f. Except for Batuta Capital Advisors LLC, retained by the Purchaser and the fees of which will be paid by the Purchaser, no broker, investment banker, agent, finder or other intermediary acting on behalf of any member of the Purchaser or its affiliate(s) or under the authority of the Purchaser or any affiliate is or will be entitled to any broker's or finder's fee or any other commission or similar fee directly or indirectly in connection with the Transaction.[1]

[1] KBIO broker to be included, but fees will be paid exclusively by KBIO.

[***] INDICATES MATERIAL THAT WAS OMITTED AND FOR WHICH CONFIDENTIAL TREATMENT WAS REQUESTED. ALL SUCH OMITTED MATERIAL WAS FILED SEPARATELY WITH THE SECURITIES AND EXCHANGE COMMISSION PURSUANT TO RULE 24b-2 PROMULGATED UNDER THE SECURITIES EXCHANGE ACT OF 1934, AS AMENDED.

g. None of the Purchaser, any of its predecessors, any affiliated issuer, any director, executive officer, other officer of the Purchaser, any beneficial owner (as that term is defined in Rule 13d-3 under the Securities Exchange Act of 1934, as amended) of 20% or more of the Purchaser's outstanding voting equity securities (with the sole exception of Martin Shkreli who is known by the parties to be under federal indictment on securities fraud charges and is not an employee, director, consultant, or agent of the Purchaser and has not have any influence upon the management or direction of the Purchaser in any form at any time), calculated on the basis of voting power, in any capacity at the date hereof (each, a "**Purchaser Covered Person**" and, collectively, "**Purchaser Covered Persons**") is subject to any of the "Bad Actor" disqualifications described in Rule 506(d)(1)(i) to (viii) under the Securities Act of 1933, as amended (a "**Disqualification Event**"), except for a Disqualification Event covered by Rule 506(d)(2) or (d)(3) under the Securities Act of 1933. The Purchaser has exercised reasonable care to determine (i) the identity of each person that is a Purchaser Covered Person; and (ii) whether any Purchaser Covered Person is subject to a Disqualification Event.

h. No Purchaser Covered Person is, or has been, debarred under Section 306(a) or 306(b) of the Food, Drug & Cosmetic Act or by the analogous laws of any regulatory authority;

i. No Purchaser Covered Person has, to the Purchaser's Knowledge, been charged with, or convicted of, any felony or misdemeanor within the ambit of 42 U.S.C. §§ 1320a-7(a), 1320a-7(b)(l)-(3), or pursuant to the analogous Laws of any Regulatory Authority, or is proposed for exclusion, or the subject of exclusion or debarment proceedings by a Regulatory Authority, during the employee's or consultant's employment or contract term with the Company; and

j. No Purchaser Covered Person is, or has been, excluded, suspended or debarred from participation, or otherwise ineligible to participate, in any U.S. or non-U.S. health care programs (or has been convicted of a criminal offense that falls within the scope of 42 U.S.C. §1320a-7 but not yet excluded, debarred, suspended, or otherwise declared ineligible), or excluded, suspended or debarred by a regulatory authority from participation, or otherwise ineligible to participate, in any procurement or non-procurement programs.

Covenants of the Purchaser

Until the Closing and full payment of all binding and ongoing option payments, the Purchaser covenants and agrees to take the following actions if the failure to take such action will have a material adverse effect on the Product:

a. It will, with immediate effect, terminate the employment of any Purchaser Covered Person who is an employee of the Purchaser if such Purchaser Covered Person is subject to any Disqualification Event;

b. It will, with immediate effect, terminate the employment of any Purchaser Covered Person who is an employee of the Purchaser if such Purchaser Covered Person is charged with any felony or misdemeanor within the ambit of 42 U.S.C. §§ 1320a-7(a), 1320a-7(b)(l)-(3), or pursuant to the analogous laws of any regulatory authority, or is proposed for exclusion, or the subject of exclusion or debarment proceedings by a regulatory authority, during the employee's employment term with the Purchaser; and

c. It will, with immediate effect, terminate the employment of any Purchaser Covered Person who becomes excluded, suspended or debarred from participation, or otherwise is ineligible to participate, in any U.S. or non-U.S. health care programs (or has been convicted of a criminal offense that falls within the scope of 42 U.S.C. §1320a-7 but not yet excluded, debarred, suspended, or otherwise declared ineligible), or excluded, suspended or debarred by a regulatory authority from participation, or otherwise ineligible to participate, in any procurement or non-procurement programs.

[***] INDICATES MATERIAL THAT WAS OMITTED AND FOR WHICH CONFIDENTIAL TREATMENT WAS REQUESTED. ALL SUCH OMITTED MATERIAL WAS FILED SEPARATELY WITH THE SECURITIES AND EXCHANGE COMMISSION PURSUANT TO RULE 24b-2 PROMULGATED UNDER THE SECURITIES EXCHANGE ACT OF 1934, AS AMENDED.

Exhibit 10.2

March 1, 2016

Dr. Cameron Durrant
3059 CR 204
Oxford, FL 34484-2821

Dear Dr. Durrant,

KaloBios Pharmaceuticals, Inc. (the "Company") is pleased to offer you employment as the Chief Executive Officer of the Company (the "CEO"), effective as of March 1, 2016, on the terms set forth in this letter (this "Letter"). In such role, you will have all of the duties, responsibilities and authority commensurate with such position, and you will report to the Board of Directors of the Company (the "Board"). Your employment as the CEO will continue until terminated by either you or the Company. Your employment with the Company may only be terminated by you or the Company as of the last business day of a calendar month, provided that in order for such a termination to be effective, either you or the Board, as applicable, must provide written notice of termination to the other party by the 20th day of the month of termination. Upon your termination of employment for any reason, you will not be eligible to receive any severance payments or benefits.

During your employment as the CEO, you will receive a base salary of $50,000 per month. Your monthly base salary will be paid to you in a single lump sum, less applicable tax withholding, on the first business day of each month, provided that your base salary payment for the month of March 2016 will be paid to you as soon as practicable following the date of your execution of this Letter. During your employment as the CEO, you will be eligible to participate in the employee benefit plans that are generally made available to other executives of the Company. During your employment as the CEO, you will not be eligible to receive compensation for your service as a director of the Company, other than the compensation set forth in this Letter.

During your employment as the CEO, you will be reimbursed for your reasonable business related expenses. Any such reimbursement will be reimbursed to you as promptly as practical and in any event not later than the last day of the calendar month after the calendar month in which the expenses are incurred, any right to reimbursement or in kind benefits will not be subject to liquidation or exchange for another benefit, and the amount of the expenses eligible for reimbursement during any taxable year will not affect the amount of expenses eligible for reimbursement in any other taxable year.

You hereby agree that you will execute the Company's customary form of Proprietary Information and Inventions Agreement as soon as practicable following the date of your execution of this Letter.

The Company will indemnify you to the maximum extent that its officers, directors and employees are entitled to indemnification pursuant to the Company's certificate of incorporation and bylaws, subject to applicable law.

The nature of your employment relationship is at-will. Accordingly, either you or the Company may terminate your employment at any time, subject to the provisions of the first paragraph above, and for any or no reason, subject to the terms and conditions of this Letter.

This Letter is the entire agreement between you and the Company with regard to the subject matter hereof. This Letter may not be amended or modified, except by an express written agreement signed by both you and a duly authorized officer of the Company. This Letter will be governed by and construed in accordance with the laws of the State of California without regard to conflict of laws principles. This Letter and all matters arising out of it will be enforced and/or interpreted before a trier of fact in the County of San Mateo, State of California only, all parties agreeing to submit to such jurisdiction. This Letter may be executed simultaneously in two or more counterparts, each of which will be deemed an original, but all of which together will constitute one and the same instrument

We hope that you will accept our offer to join the Company. You may indicate your agreement with these terms and accept this offer by signing and dating the enclosed duplicate original of this Letter and returning it to me.

Sincerely,

KaloBios Pharmaceuticals, Inc.

/s/ Dean Witter, III
Name: Dean Witter, III
Title: Interim CFO

Acknowledged and Agreed:

/s/ Cameron Durrant
Dr. Cameron Durrant
Date: March 1, 2016

Exhibit 31.1

CERTIFICATION PURSUANT TO
SECTION 302 OF THE SARBANES-OXLEY ACT OF 2002
CERTIFICATIONS

I, Cameron Durrant., certify that:

1. I have reviewed this Quarterly Report on Form 10-Q of KaloBios Pharmaceuticals, Inc.;

2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;

3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;

4. The registrant's other certifying officer(s) and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:

a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;

b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;

c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and

d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and

5. The registrant's other certifying officer(s) and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):

a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and

b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: September 23, 2016

/s/ Cameron Durrant
Cameron Durrant,
Chief Executive Officer
(Principal Executive Officer)

Exhibit 31.2

CERTIFICATION PURSUANT TO
SECTION 302 OF THE SARBANES-OXLEY ACT OF 2002
CERTIFICATIONS

I, Dean Witter, III, certify that:

1. I have reviewed this Quarterly Report on Form 10-Q of KaloBios Pharmaceuticals, Inc.;

2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;

3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;

4. The registrant's other certifying officer(s) and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:

a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;

b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;

c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and

d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and

5. The registrant's other certifying officer(s) and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):

a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and

b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: September 23, 2016

/s/ Dean Witter, III
Dean Witter, III
Interim Chief Financial Officer
(Principal Financial and Accounting Officer)

Exhibit 32.1

CERTIFICATIONS OF
PRINCIPAL EXECUTIVE OFFICER AND PRINCIPAL FINANCIAL OFFICER
PURSUANT TO 18 U.S.C. SECTION 1350,
AS ADOPTED PURSUANT TO
SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002

I, Cameron Durrant, certify, pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that the Quarterly Report on Form 10-Q of KaloBios Pharmaceuticals, Inc. for the quarter ended March 31, 2016 fully complies with the requirements of Section 13(a) or 15(d) of the Exchange Act and that information contained in such Quarterly Report on Form 10-Q fairly presents in all material respects the financial condition and results of operations of KaloBios Pharmaceuticals, Inc.

By:	/s/ Cameron Durrant
Name:	Cameron Durrant
Title:	Chief Executive Officer (Principal Executive Officer)
Date:	September 23, 2016

Exhibit 32.2

CERTIFICATION OF
PRINCIPAL EXECUTIVE OFFICER AND PRINCIPAL FINANCIAL OFFICER
PURSUANT TO 18 U.S.C. SECTION 1350,
AS ADOPTED PURSUANT TO
SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002

I, Dean Witter, III, certify pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that the Quarterly Report on Form 10-Q of KaloBios Pharmaceuticals, Inc. for the quarter ended March 31, 2016 fully complies with the requirements of Section 13(a) or 15(d) of the Exchange Act and that information contained in such Quarterly Report on Form 10-Q fairly presents in all material respects the financial condition and results of operations of KaloBios Pharmaceuticals, Inc.

By: /s/ Dean Witter, III
Name: Dean Witter, III
Title: Chief Financial Officer
(Principal Financial and Accounting Officer)
Date: September 23, 2016