
**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 June 30, 2017

or

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

For the transition period from _____ to _____.

Commission File Number 001-36510

ZAFGEN, INC.

(Exact name of registrant as specified in its charter)

Delaware
(State or other jurisdiction of
incorporation or organization)

20-3857670
(IRS Employer
Identification No.)

Zafgen, Inc.
175 Portland Street, 4th Floor
Boston, Massachusetts 02114
(Address of principal executive offices, including zip code)

Registrant's Telephone Number, Including Area Code:
(617) 622-4003

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, a smaller reporting company, or an emerging growth company. See the definitions of "large accelerated filer," "accelerated filer," "smaller reporting company" and "emerging growth company" in Rule 12b-2 of the Exchange Act.

Large accelerated filer	<input type="checkbox"/>	Accelerated filer	<input checked="" type="checkbox"/>
Non-accelerated filer	<input type="checkbox"/> (Do not check if a smaller reporting company)	Emerging growth company	<input checked="" type="checkbox"/>
Smaller reporting company	<input type="checkbox"/>		

If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the Exchange Act.

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 July 31, 2017, there were 27,483,925 shares of the registrant's Common Stock, \$0.001 par value per share, outstanding.

FORWARD-LOOKING STATEMENTS

This Quarterly Report on Form 10-Q Report, or Quarterly Report, contains forward-looking statements that involve risks and uncertainties. We make such forward-looking statements pursuant to the safe harbor provisions of the Private Securities Litigation Reform Act of 1995 and other federal securities laws. All statements other than statements of historical facts contained in this Quarterly Report are forward-looking statements. In some cases, you can identify forward-looking statements by terminology such as “may,” “will,” “should,” “expects,” “intends,” “plans,” “anticipates,” “believes,” “estimates,” “predicts,” “potential,” “continue” or the negative of these terms or other comparable terminology. These forward-looking statements include, but are not limited to, statements about:

- the accuracy of our estimates regarding expenses, future revenues, cash forecasts and capital requirements;
- our plans to commercialize ZGN-1061 as a treatment for metabolic diseases including type 2 diabetes and obesity;
- our ability to successfully advance ZGN-1061 into later-stage clinical trials;
- our ability to dissociate effects of methionine aminopeptidase 2, or MetAP2, inhibitors from prothrombotic effects or other adverse events observed in clinical development of beloranib;
- our ability to provide a compelling argument for improved safety of ZGN-1061 and other novel MetAP2 inhibitors relative to first generation compounds, including beloranib;
- regulatory and political developments in the United States and foreign countries;
- the performance of our third-party contract manufacturers and clinical research organizations;
- our ability to obtain and maintain intellectual property protection for our proprietary assets;
- the size of the potential markets for our product candidates and our ability to serve those markets;
- the rate and degree of market acceptance of our product candidates for any indication once approved;
- our ability to obtain additional financing when needed;
- the success of competing products that are or become available for the indications that we are pursuing;
- the loss of key scientific or management personnel; and
- other risks and uncertainties, including those listed under Part II, Item 1A. Risk Factors.

Any forward-looking statements in this Quarterly Report reflect our current views with respect to future events or to our future financial performance and involve known and unknown risks, uncertainties and other factors that may cause our actual results, performance or achievements to be materially different from any future results, performance or achievements expressed or implied by these forward-looking statements. Factors that may cause actual results to differ materially from current expectations include, among other things, those listed under Part II, Item 1A. Risk Factors and elsewhere in this Quarterly Report. Given these uncertainties, you should not place undue reliance on these forward-looking statements. Except as required by law, we assume no obligation to update or revise these forward-looking statements for any reason, even if new information becomes available in the future.

This Quarterly Report also contains estimates, projections and other information concerning our industry, our business, and the markets for certain diseases, including data regarding the estimated size of those markets, and the incidence and prevalence of certain medical conditions. Information that is based on estimates, forecasts, projections, market research or similar methodologies is inherently subject to uncertainties and actual events or circumstances may differ materially from events and circumstances reflected in this information. Unless otherwise expressly stated, we obtained this industry, business, market and other data from reports, research surveys, studies and similar data prepared by market research firms and other third parties, industry, medical and general publications, government data and similar sources.

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Zafgen, Inc.

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PART I – FINANCIAL INFORMATION**Item 1. Financial Statements****ZAFGEN, INC.****CONDENSED CONSOLIDATED BALANCE SHEETS****(In thousands, except share and per share data)****(Unaudited)**

	<u>June 30,</u> <u>2017</u>	<u>December 31,</u> <u>2016</u>
Assets		
Current assets:		
Cash and cash equivalents	\$ 31,726	\$ 32,352
Marketable securities	74,266	96,842
Tax incentive receivable	368	347
Prepaid expenses and other current assets	1,605	1,358
Total current assets	<u>107,965</u>	<u>130,899</u>
Tax incentive receivable	234	—
Property and equipment, net	588	661
Other assets	58	61
Total assets	<u>\$ 108,845</u>	<u>\$ 131,621</u>
Liabilities and Stockholders' Equity		
Current liabilities:		
Accounts payable	\$ 4,447	\$ 2,572
Accrued expenses	2,709	3,733
Notes payable, current	2,063	3,589
Total current liabilities	<u>9,219</u>	<u>9,894</u>
Total liabilities	<u>9,219</u>	<u>9,894</u>
Commitments and contingencies (Note 7)		
Stockholders' equity:		
Preferred stock; \$0.001 par value per share; 5,000,000 shares authorized as of June 30, 2017 and December 31, 2016; no shares issued and outstanding as of June 30, 2017 and December 31, 2016	—	—
Common stock, \$0.001 par value per share; 115,000,000 shares authorized as of June 30, 2017 and December 31, 2016; 27,449,465 and 27,332,551 shares issued and outstanding as of June 30, 2017 and December 31, 2016, respectively	27	27
Additional paid-in capital	363,547	359,329
Accumulated deficit	(263,907)	(237,549)
Accumulated other comprehensive loss	(41)	(80)
Total stockholders' equity	<u>99,626</u>	<u>121,727</u>
Total liabilities and stockholders' equity	<u>\$ 108,845</u>	<u>\$ 131,621</u>

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

ZAFGEN, INC.

CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS AND COMPREHENSIVE LOSS
(In thousands, except share and per share data)
(Unaudited)

	Three Months Ended June 30,		Six Months Ended June 30,	
	2017	2016	2017	2016
Revenue	\$ —	\$ —	\$ —	\$ —
Operating expenses:				
Research and development	10,528	10,163	20,205	22,660
General and administrative	3,008	4,899	6,596	10,259
Total operating expenses	13,536	15,062	26,801	32,919
Loss from operations	(13,536)	(15,062)	(26,801)	(32,919)
Other income (expense):				
Interest income	247	225	474	434
Interest expense	(53)	(140)	(126)	(300)
Foreign currency transaction gains (losses), net	(5)	(51)	95	21
Total other income (expense), net	189	34	443	155
Net loss	\$ (13,347)	\$ (15,028)	\$ (26,358)	\$ (32,764)
Net loss per share, basic and diluted	\$ (0.49)	\$ (0.55)	\$ (0.96)	\$ (1.20)
Weighted average common shares outstanding, basic and diluted	27,407,408	27,272,225	27,379,122	27,267,830
Comprehensive loss:				
Net loss	\$ (13,347)	\$ (15,028)	\$ (26,358)	\$ (32,764)
Other comprehensive loss:				
Unrealized gain (loss) on marketable securities	22	(15)	39	193
Total other comprehensive income (loss)	22	(15)	39	193
Total comprehensive loss	\$ (13,325)	\$ (15,043)	\$ (26,319)	\$ (32,571)

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

ZAFGEN, INC.

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

(In thousands)

(Unaudited)

	<u>Six Months Ended June 30,</u>	
	<u>2017</u>	<u>2016</u>
Cash flows from operating activities:		
Net loss	\$ (26,358)	\$ (32,764)
Adjustments to reconcile net loss to net cash used in operating activities		
Stock-based compensation expense	4,103	5,610
Non-cash interest expense	10	24
Depreciation expense	89	102
Unrealized foreign currency transaction gains	(21)	(108)
Premium on marketable securities, net	(224)	(233)
Amortization of premium on marketable securities	145	715
Changes in operating assets and liabilities:		
Prepaid expenses and other current assets	(247)	374
Tax incentive receivable	(234)	(250)
Accounts payable	1,875	(4,710)
Accrued expenses	(998)	(1,039)
Net cash used in operating activities	<u>(21,860)</u>	<u>(32,279)</u>
Cash flows from investing activities:		
Proceeds from sales and maturities of marketable securities	79,994	88,660
Purchases of marketable securities	(57,300)	(69,907)
Purchases of property and equipment	(16)	(660)
Net cash provided by investing activities	<u>22,678</u>	<u>18,093</u>
Cash flows from financing activities:		
Repayments of notes payable	(1,559)	(1,438)
Proceeds from exercise of common stock options and employee stock purchase plan	115	55
Net cash used in financing activities	<u>(1,444)</u>	<u>(1,383)</u>
Net decrease in cash and cash equivalents	(626)	(15,569)
Cash and cash equivalents at beginning of period	32,352	35,595
Cash and cash equivalents at end of period	<u>\$ 31,726</u>	<u>\$ 20,026</u>
Supplemental disclosure of non-cash investing and financing activities:		
Property and equipment included in accounts payable	<u>\$ —</u>	<u>\$ 204</u>
Supplemental disclosure of cash flow information:		
Cash paid for interest	<u>\$ 103</u>	<u>\$ 224</u>

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

ZAFGEN, INC.

**NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited)**

1. Nature of the Business and Basis of Presentation

Zafgen, Inc., or the Company, was incorporated on November 22, 2005 under the laws of the State of Delaware. The Company is a biopharmaceutical company dedicated to significantly improving the health and well-being of patients affected by metabolic diseases including type 2 diabetes and obesity. The Company is focused on developing novel therapeutics that treat the underlying biological mechanisms through the methionine aminopeptidase 2 (“MetAP2”) pathway. The Company has pioneered the study of MetAP2 inhibitors in both common and rare forms of obesity. The Company’s lead product candidate is ZGN-1061, a novel fumagillin-class MetAP2 inhibitor administered by subcutaneous injection, which is currently being profiled for its utility in the treatment of metabolic diseases including type 2 diabetes and obesity. Since its inception, the Company has devoted substantially all of its efforts to research and development, recruiting management, acquiring operating assets and raising capital. Currently, the Company is focusing its personnel and financial resources on ZGN-1061 and the discovery of novel and highly differentiated MetAP2 inhibitors.

The Company is subject to risks common to companies in the biotechnology industry including, but not limited to, new technological innovations, protection of proprietary technology, dependence on key personnel, compliance with government regulations and the need to obtain additional financing. Product candidates currently under development will require significant additional research and development efforts, including extensive pre-clinical and clinical testing and regulatory approval, prior to commercialization. These efforts require significant amounts of additional capital, adequate personnel infrastructure, and extensive compliance-reporting capabilities.

The Company’s product candidates are all in the research and development stage. There can be no assurance that the Company’s research and development will be successfully completed, that adequate protection for the Company’s intellectual property will be obtained, that any product candidates developed will obtain necessary government regulatory approval or that any approved products will be commercially viable. Even if the Company’s product development efforts are successful, it is uncertain when, if ever, the Company will generate significant revenue from product sales. The Company operates in an environment of rapid change in technology and substantial competition from pharmaceutical and biotechnology companies. In addition, the Company is dependent upon the services of its employees and consultants.

The Company has incurred losses and negative cash flows from operations since its inception. As of June 30, 2017, the Company had an accumulated deficit of \$263.9 million. From its inception through June 30, 2017, the Company received net proceeds of \$333.3 million from the sales of redeemable convertible preferred stock, the issuance of convertible promissory notes, the proceeds from its initial public offering (“IPO”) in June 2014 and its follow-on offering in January 2015. Until such time, if ever, as the Company can generate substantial product revenue, the Company expects to finance its cash needs through a combination of equity offerings, debt financings, collaborations, strategic alliances, licensing arrangements and other sources of funding. If the Company is unable to raise additional funds through equity, debt financings or licensing arrangements when needed, the Company may be required to delay, limit, reduce or terminate product development or future commercialization efforts or grant rights to develop and market products or product candidates that the Company would otherwise prefer to develop and market itself. Based on its current operating plans, the Company believes its cash, cash equivalents and marketable securities of \$106.0 million as of June 30, 2017 will be sufficient to fund its anticipated level of operations and capital expenditures for a period of at least one year from the issuance date of this Quarterly Report.

The condensed consolidated financial statements include the accounts of the Company and its wholly owned subsidiaries Zafgen Securities Corporation, Zafgen Australia Pty Limited, and Zafgen Animal Health, LLC. All intercompany balances and transactions have been eliminated.

Unaudited Interim Financial Information

The condensed consolidated balance sheet as of December 31, 2016 was derived from the Company’s audited financial statements, but does not include all disclosures required by accounting principles generally accepted in the United States of America, or GAAP. The accompanying unaudited condensed consolidated financial statements as of June 30, 2017 and for the three and six months ended June 30, 2017 and 2016, have been prepared by the Company, pursuant to the rules and regulations of the Securities and Exchange Commission, or SEC, for interim financial statements. Certain information and footnote disclosures normally included in financial statements prepared in accordance with GAAP have been condensed or omitted pursuant to such rules and regulations. However, the Company believes that the disclosures are adequate to make the information presented not misleading. These condensed consolidated financial statements should be read in conjunction with the Company’s audited consolidated financial statements and the notes thereto for the year ended December 31, 2016, included in the Company’s Annual Report on Form 10-K, for the year ended

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December 31, 2016, on file with the SEC. In the opinion of management, all adjustments, consisting only of normal recurring adjustments necessary for a fair statement of the Company's condensed consolidated financial position as of June 30, 2017 and condensed consolidated results of operations and cash flows for the three and six months ended June 30, 2017 and 2016 have been made. The results of operations for the three and six months ended June 30, 2017 are not necessarily indicative of the results of operations that may be expected for the year ending December 31, 2017.

2. Summary of Significant Accounting Policies

Use of Estimates

The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, the disclosure of contingent assets and liabilities as of the date of the condensed consolidated financial statements, and the reported amounts of expenses during the reporting periods. Significant estimates and assumptions reflected in these condensed consolidated financial statements include, but are not limited to, the accrual of research and development expenses and the valuation of stock-based awards. Estimates are periodically reviewed in light of changes in circumstances, facts and experience. Actual results could differ from the Company's estimates.

Marketable securities

Marketable securities consist of investments with original maturities greater than ninety days. The Company has classified its investments with maturities beyond one year as short term, based on their highly liquid nature and because such marketable securities represent the investment of cash that is available for current operations. The Company considers its investment portfolio of investments as available-for-sale. Accordingly, these investments are recorded at fair value, which is based on quoted market prices. Unrealized gains and losses are reported as a component of accumulated other comprehensive income (loss) in stockholders' equity. Realized gains and losses and declines in value judged to be other than temporary are included as a component of other income (expense), net based on the specific identification method. When determining whether a decline in value is other than temporary, the Company considers various factors, including whether the Company has the intent to sell the security, and whether it is more likely than not that the Company will be required to sell the security prior to recovery of its amortized cost basis. Fair value is determined based on quoted market prices.

Net Income (Loss) Per Share

Basic net income (loss) per share is computed by dividing the net income (loss) attributable to common stockholders by the weighted average number of common shares outstanding for the period. Diluted net income (loss) per share attributable to common stockholders is computed by dividing the diluted net income (loss) attributable to common stockholders by the weighted average number of common shares, including potential dilutive common shares assuming the dilutive effect of outstanding stock options and unvested restricted common shares, as determined using the treasury stock method. For periods in which the Company has reported net losses, diluted net loss per common share attributable to common stockholders is the same as basic net loss per common share attributable to common stockholders, since dilutive common shares are not assumed to have been issued if their effect is antidilutive.

The Company excluded the following common stock equivalents, outstanding as of June 30, 2017 and 2016, from the computation of diluted net loss per share for the three months ended June 30, 2017 and 2016 because they had an anti-dilutive impact due to the net loss incurred for the periods:

	As of June 30,	
	2017	2016
Options to purchase common stock	4,185,866	3,976,995
Unvested restricted common stock	11,065	9,955
	<u>4,196,931</u>	<u>3,986,950</u>

Recently Issued and Adopted Accounting Pronouncements

In May 2014, the Financial Accounting Standards Board (the “FASB”) issued ASU No. 2014-09, *Revenue from Contracts with Customers* (Topic 606), which supersedes all existing revenue recognition requirements, including most industry-specific guidance. The new standard requires a company to recognize revenue when it transfers goods or services to customers in an amount that reflects the consideration that the company expects to receive for those goods or services. The FASB has continued to issue accounting standards updates to clarify and provide implementation guidance related to Revenue from Contracts with Customers, including ASU 2016-08, *Revenue from Contract with Customers: Principal versus Agent Considerations*, ASU 2016-10, *Revenue from Contracts with Customers: Identifying Performance Obligations and Licensing*, and ASU 2016-12, *Revenue from Contracts with Customers: Narrow-Scope Improvements and Practical Expedients*. These amendments address a number of areas, including the entity’s identification of its performance obligations in a contract, collectability, non-cash consideration, presentation of sales tax and an entity’s evaluation of the nature of its promise to grant a license of intellectual property and whether or not that revenue is recognized over time or at a point in time. These new standards will be effective for the Company beginning January 1, 2018. The Company early adopted the standard as of January 1, 2017, however there is no impact of this new guidance on its condensed consolidated financial statements as it does not currently have any revenue generating arrangements.

In February 2016, the FASB issued ASU No. 2016-02, *Leases*. This guidance will require that lease arrangements longer than 12 months result in an entity recognizing an asset and liability equal to the present value of the lease payments in the statement of financial position. This guidance is effective for annual periods beginning after December 15, 2018, and interim periods therein. This standard requires a modified retrospective transition approach for all leases existing at, or entered into after, the date of initial application, with an option to use certain transition relief. Early adoption is permitted. The Company is evaluating the effect that this guidance will have on its condensed consolidated financial statements.

In March 2016, the FASB issued ASU No. 2016-09, *Improvements to Employee Share-Based Payment Accounting*. This standard was adopted on January 1, 2017 on a modified retrospective basis. As a result the Company has made an accounting policy election to account for forfeitures as they occur. The adoption of this guidance also requires excess tax benefits and tax deficiencies be recorded in the income statement as opposed to additional paid-in capital when the awards vest or are settled. The adoption of this guidance had an immaterial impact on the Company’s condensed consolidated financial statements as of and for the three and six months ended June 30, 2017.

In August 2016, the FASB issued ASU No. 2016-15, *Statement of Cash Flows: Classification of Certain Cash Receipts and Cash Payments*. This guidance addresses the presentation and classification of certain cash receipts and cash payments in the statement of cash flows. The standard will be effective for annual periods beginning after December 15, 2017, and interim periods therein. Early adoption is permitted. The Company is evaluating the effect that this guidance will have on its condensed consolidated financial statements.

In May 2017, the FASB issued ASU No. 2017-09, *Compensation – Stock Compensation: Scope of Modification Accounting*. This guidance addresses which changes to the terms or conditions of a share-based payment award require an entity to apply modification accounting. The standard will be effective for annual periods beginning after December 15, 2017, and interim periods therein. Early adoption is permitted. The Company is evaluating the effect that this guidance will have on its condensed consolidated financial statements.

3. Fair Value Measurements and Marketable Securities

Fair Value Measurements

The following tables present information about the Company's financial assets that have been measured at fair value as of June 30, 2017 and December 31, 2016, and indicate the fair value of the hierarchy of the valuation inputs utilized to determine such fair value. In general, fair values determined by Level 1 inputs utilize quoted prices (unadjusted) in active markets for identical assets or liabilities. Fair value determined by Level 2 inputs utilize observable inputs other than Level 1 prices, such as quoted prices, for similar assets or liabilities, quoted market prices 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 related assets or liabilities. Fair values determined by Level 3 inputs are unobservable data points for the asset or liability, and include situations where there is little, if any, market activity for the asset or liability.

The following tables summarize the Company's cash equivalents and marketable securities as of June 30, 2017 and December 31, 2016:

	June 30, 2017			
	Total	Quoted Prices in Active Markets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
(in thousands)				
Cash equivalents:				
Money market funds	\$ 25,771	\$25,771	\$ —	\$ —
Commercial paper	1,997	—	1,997	—
Total cash equivalents	<u>27,768</u>	<u>25,771</u>	<u>1,997</u>	<u>—</u>
Marketable securities:				
Corporate bonds	55,077	—	55,077	—
Commercial paper	19,189	—	19,189	—
Total marketable securities	<u>74,266</u>	<u>—</u>	<u>74,266</u>	<u>—</u>
Total cash equivalents and marketable securities	<u>\$102,034</u>	<u>\$25,771</u>	<u>\$ 76,263</u>	<u>\$ —</u>

	December 31, 2016			
	Total	Quoted Prices in Active Markets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
(in thousands)				
Cash equivalents:				
Money market funds	\$ 22,091	\$22,091	\$ —	\$ —
Commercial paper	2,997	—	2,997	—
Corporate bonds	1,500	—	1,500	—
Total cash equivalents	<u>26,588</u>	<u>22,091</u>	<u>4,497</u>	<u>—</u>
Marketable securities:				
Corporate bonds	69,622	—	69,622	—
Commercial paper	27,220	—	27,220	—
Total marketable securities	<u>96,842</u>	<u>—</u>	<u>96,842</u>	<u>—</u>
Total cash equivalents and marketable securities	<u>\$123,430</u>	<u>\$22,091</u>	<u>\$ 101,339</u>	<u>\$ —</u>

The carrying amounts reflected in the condensed consolidated balance sheets for tax incentive receivable, accounts payable, and accrued expenses approximate fair value due to their short-term maturities. The carrying value of the Company's outstanding notes payable approximates fair value (a Level 2 fair value measurement), reflecting interest rates currently available to the Company.

Marketable Securities

The following tables summarize the Company's marketable securities as of June 30, 2017 and December 31, 2016:

	June 30, 2017			Fair Value
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	
	(in thousands)			
Assets:				
Corporate bonds (due within 1 year)	\$ 55,112	\$ —	\$ (35)	\$ 55,077
Commercial paper (due within 1 year)	19,193	—	(4)	19,189
	<u>\$ 74,305</u>	<u>\$ —</u>	<u>\$ (39)</u>	<u>\$ 74,266</u>
	December 31, 2016			Fair Value
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	
	(in thousands)			
Assets:				
Corporate bonds (due within 1 year)	\$ 68,777	\$ —	\$ (54)	\$ 68,723
Corporate bonds (due after 1 year through 2 years)	901	—	(2)	899
Commercial paper (due within 1 year)	27,244	—	(24)	27,220
	<u>\$ 96,922</u>	<u>\$ —</u>	<u>\$ (80)</u>	<u>\$ 96,842</u>

4. Accrued Expenses

Accrued expenses consisted of the following as of June 30, 2017 and December 31, 2016:

	June 30, 2017	December 31, 2016
	(in thousands)	
Accrued payroll and related expenses	\$ 1,241	\$ 2,008
Accrued research and development expenses	1,073	892
Accrued professional fees	293	347
Accrued restructuring	—	376
Accrued other	102	110
	<u>\$ 2,709</u>	<u>\$ 3,733</u>

5. Notes Payable

The Company has outstanding amounts due under a loan and security agreement with Oxford Finance LLC and Midcap Financial, or the 2014 Credit Facility, entered into in March 2014. All promissory notes issued under the 2014 Credit Facility are collateralized by substantially all of the Company's personal property, other than its intellectual property. There are no financial covenants associated with the 2014 Credit Facility; however, there are negative covenants restricting the Company's activities, including limitations on dispositions, mergers or acquisitions; encumbering or granting a security interest in its intellectual property; incurring indebtedness or liens; paying dividends; making certain investments; and certain other business transactions.

During the three months ended June 30, 2017 and 2016, the Company recognized less than \$0.1 million and \$0.1 million, respectively, of interest expense related to the 2014 Credit Facility. During the six months ended June 30, 2017 and 2016, the Company recognized \$0.1 million and \$0.3 million, respectively, of interest expense related to the 2014 Credit Facility. The effective annual interest rate of the outstanding debt under the 2014 Credit Facility is approximately 10.8%.

6. Stock-Based Awards

The Company grants equity awards under its 2014 Stock Option and Incentive Plan, or the 2014 Stock Option Plan, and is authorized to issue common stock under its 2014 Employee Stock Purchase Plan. The Company also has outstanding stock-based awards under its Amended and Restated 2006 Stock Option Plan but is no longer granting awards under this plan. As of June 30, 2017, 2,014,395 shares are available for grant under the 2014 Stock Option Plan, including 1,093,302 shares automatically added to the 2014 Stock Option Plan on January 1, 2017 as a result of a provision in the 2014 Stock Option Plan.

The Company recorded stock-based compensation expense related to stock options and restricted common stock in the following expense categories within its condensed consolidated statements of operations:

	<u>Three Months Ended June 30,</u>		<u>Six Months Ended June 30,</u>	
	<u>2017</u>	<u>2016</u>	<u>2017</u>	<u>2016</u>
	(in thousands)			
Research and development	\$ 877	\$ 1,002	\$ 1,733	\$ 1,830
General and administrative	\$ 1,225	1,852	2,370	3,780
	<u>\$ 2,102</u>	<u>\$ 2,854</u>	<u>\$ 4,103</u>	<u>\$ 5,610</u>

7. Commitments and Contingencies

Leases

The Company has a lease for office space in Boston, Massachusetts, effective as of July 28, 2014, with a term expiring July 31, 2017 and an option to extend the lease for three additional years. In March 2015, the Company entered into an operating lease for additional office space in Boston, Massachusetts, effective as of April 15, 2015, with a term expiring on July 31, 2017, and two options to extend this lease for three additional years each. In October 2015, the Company entered into an operating lease for office space in San Diego, California, effective as of October 1, 2015, with a term expiring on September 30, 2019, and an option to extend this lease for five additional years. In January 2017, the Company extended the leases for both office spaces in Boston, Massachusetts with new terms expiring on July 31, 2020. As of July 31, 2017, the Company negotiated the financial terms of these extensions with additional minimum lease payments of \$0.2 million for the remainder of 2017, \$0.4 million for the years 2018 and 2019 and \$0.2 million for 2020 not reflected in the table below. The Company also has the option to extend both of these leases in Boston, Massachusetts for an additional three years. With the landlord's consent, the Company has subleased 2,976 square feet of office space in Boston, Massachusetts to an unrelated third party which began on January 1, 2017 and expires on June 30, 2018. The Company expects to receive approximately \$0.2 million in sublease rental income during the sublease period.

Future minimum lease payments for its operating leases as of June 30, 2017 were as follows:

<u>Year Ending December 31,</u>	
<u>(in thousands)</u>	
2017 (July to December)	\$ 80
2018	106
2019	82
	<u>\$268</u>

During the three months ended June 30, 2017 and 2016, the Company recognized \$0.1 million of rental expense related to office space. During the six months ended June 30, 2017 and 2016, the Company recognized \$0.2 million of rental expense related to office space.

Intellectual Property Licenses

The Company has acquired exclusive rights to develop patented compounds and related know-how for beloranib under two licensing agreements with two third parties in the course of its research and development activities. The licensing rights obligate the Company to make payments to the licensors for license fees, milestones, license maintenance fees and royalties. The Company is also responsible for patent prosecution costs.

As of June 30, 2017, the Company is obligated to make additional milestone payments of up to \$12.3 million upon reaching certain pre-commercialization milestones, such as clinical trials and government approvals (including the U.S. Food and Drug Administration, or FDA, approval of a New Drug Application, or NDA), and up to \$12.5 million upon reaching certain product

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commercialization milestones related to the development of beloranib. Under one of the license agreements, the Company is also obligated to pay up to \$1.3 million with respect to each subsequent licensed product, if any, that is a new chemical entity. In addition, the Company will owe single-digit royalties on sales of commercial products developed using these licensed technologies, if any.

There were no milestones achieved during the three or six months ended June 30, 2017 or 2016. The Company is also obligated to pay to the licensors a percentage of fees received if and when the Company sublicenses the technology. As of June 30, 2017, the Company has not yet developed a commercial product using the licensed technologies and it has not entered into any sublicense agreements for the technologies.

Indemnification Agreements

In the ordinary course of business, the Company may provide indemnification of varying scope and terms to vendors, lessors, business partners, and other parties with respect to certain matters including, but not limited to, losses arising out of breach of such agreements or from intellectual property infringement claims made by third parties. In addition, the Company has entered into indemnification agreements with members of management team and the board of directors of the Company that will require the Company, among other things, to indemnify them against certain liabilities that may arise by reason of their status or service as directors or officers. The maximum potential amount of future payments the Company could be required to make under these indemnification agreements is, in many cases, unlimited. To date, the Company has not incurred any material costs as a result of such indemnifications. The Company does not believe that the outcome of any claims under indemnification arrangements will have a material effect on its financial position, results of operations or cash flows, and it has not accrued any liabilities related to such obligations in its condensed consolidated financial statements as of June 30, 2017.

Legal Proceedings

The Company accrues a liability for legal contingencies when it believes that it is both probable that a liability has been incurred and that the Company can reasonably estimate the amount of the loss. The Company reviews these accruals and adjusts them to reflect ongoing negotiations, settlements, rulings, advice of legal counsel and other relevant information. To the extent new information is obtained and the views on the probable outcomes of claims, suits, assessments, investigations or legal proceedings change, changes in the Company's accrued liabilities would be recorded in the period in which such determination is made. In addition, in accordance with the relevant authoritative guidance, for any matters in which the likelihood of material loss is at least reasonably possible, the Company will provide disclosure of the possible loss or range of loss. If a reasonable estimate cannot be made, however, the Company will provide disclosure to that effect. The Company expenses legal costs as they are incurred.

On October 21, 2015, a purported stockholder of the Company filed a putative class action lawsuit in the U.S. District Court for the District of Massachusetts, against the Company and Thomas E. Hughes, captioned *Aviad Bessler v. Zafgen, Inc. and Thomas E. Hughes*, No. 1:15-cv-13618. An amended complaint was filed on February 22, 2016. The amended complaint alleges violations of Sections 10(b) and 20(a) of the Securities Exchange Act of 1934 and SEC Rule 10b-5 based on allegedly false and misleading statements and omissions regarding the Company's clinical trials for its drug beloranib. On August 9, 2016, the District Court granted the motion to dismiss and dismissed the amended complaint with prejudice. On August 12, 2016, plaintiffs filed a notice of appeal to the First Circuit Court of Appeals and on April 7, 2017, the dismissal with prejudice was affirmed.

The Company may periodically become subject to other legal proceedings and claims arising in connection with ongoing business activities, including claims or disputes related to patents that have been issued or that are pending in the field of research on which the Company is focused. The Company is not aware of any material claims as of June 30, 2017.

8. Retirement Plan

The Company has a Savings Incentive Match Plan, or SIMPLE IRA, for employees. Under the terms of the plan, the Company contributes 2% of an employee's annual base salary, up to a maximum of the annual Internal Revenue Service compensation limits, for all full-time employees.

During the three months ended June 30, 2017 and 2016, the Company recognized less than \$0.1 million of expense related to its contributions to the plan. During the six months ended June 30, 2017 and 2016, the Company recognized \$0.1 million of expense related to its contributions to the plan.

9. Australia Research and Development Tax Incentive

The Company's wholly owned subsidiary, Zafgen Australia Pty Limited, which conducts core research and development activities on behalf of the Company, is eligible to receive a 45% refundable tax incentive for qualified research and development activities through December 31, 2016 and 43.5% beginning January 1, 2017. For the three months ended June 30, 2017 and 2016, \$0.2 million was recorded as a reduction to research and development expenses in the condensed consolidated statements of operations. For the six months ended June 30, 2017 and 2016, \$0.2 million and \$0.3 million, respectively, were recorded as a reduction to research and development expenses in the condensed consolidated statements of operations. The refund is denominated in Australian dollars and, therefore, the related receivable is re-measured into U.S. dollars as of each reporting date. For the three months ended June 30, 2017 and 2016, the Company recorded in its condensed consolidated statements of operations unrealized foreign currency exchange gains of nil and losses of less than \$0.1 million, respectively, related to this tax incentive receivable. For the six months ended June 30, 2017 and 2016, the Company recorded in its condensed consolidated statements of operations unrealized foreign currency exchange gains of less than \$0.1 million related to this tax incentive receivable. As of June 30, 2017 and December 31, 2016, the Company's tax incentive receivable from the Australian government was \$0.6 million and \$0.3 million, respectively.

10. Restructuring

On July 19, 2016, the Company announced that following a comprehensive review of its assets and clinical programs, as well as feedback from regulatory authorities, the Company refocused its resources on development of a differentiated MetAP2 inhibitor, ZGN-1061. As part of the strategic restructuring, the Company reorganized its operations to align with its new priorities focused on ZGN-1061 development. The Company's workforce was reduced by approximately 31% as of December 2016. The following table summarizes the restructuring reserve for the periods indicated:

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	<u>Six Months Ended</u> <u>June 30, 2017</u>	<u>Year Ended</u> <u>December 31, 2016</u>
	(in thousands)	
Restructuring reserve beginning balance	\$ 376	\$ —
Restructuring expenses incurred during the period	24	1,223
Amounts paid during the period	(400)	(847)
Restructuring reserve ending balance	<u>\$ —</u>	<u>\$ 376</u>

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

The following discussion and analysis of our financial condition and results of operations should be read in conjunction with our condensed consolidated financial statements and related notes appearing elsewhere in this Quarterly Report on Form 10-Q, or Quarterly Report, and the audited consolidated financial statements and notes thereto and management's discussion and analysis of financial condition and results of operations for the year ended December 31, 2016 included in our Annual Report on Form 10-K for the year ended December 31, 2016. Some of the information contained in this discussion and analysis or set forth elsewhere in this Quarterly Report, including information with respect to our plans and strategy for our business, includes forward-looking statements that involve risks and uncertainties. As a result of many factors, including those factors set forth in the "Risk Factors" section of this Quarterly Report, our actual results could differ materially from the results described, in or implied, by these forward-looking statements.

Our actual results and timing of certain events may differ materially from the results discussed, projected, anticipated, or indicated in any forward-looking statements. We caution you that forward-looking statements are not guarantees of future performance and that our actual results of operations, financial condition and liquidity, and the development of the industry in which we operate may differ materially from the forward-looking statements contained in this Quarterly Report. In addition, even if our results of operations, financial condition and liquidity, and the development of the industry in which we operate are consistent with the forward-looking statements contained in this Quarterly Report, they may not be predictive of results or developments in future periods.

The following information and any forward-looking statements should be considered in light of factors discussed elsewhere in this Quarterly Report, including those risks identified under the Risk Factors section.

We caution readers not to place undue reliance on any forward-looking statements made by us, which speak only as of the date they are made. We disclaim any obligation, except as specifically required by law and the rules of the SEC, to publicly update or revise any such statements to reflect any change in our expectations or in events, conditions or circumstances on which any such statements may be based, or that may affect the likelihood that actual results will differ from those set forth in the forward-looking statements.

Overview

We are a biopharmaceutical company dedicated to significantly improving the health and well-being of patients affected by metabolic diseases including type 2 diabetes and obesity. We are focused on developing novel therapeutics that treat the underlying biological mechanisms through the methionine aminopeptidase 2, or MetAP2, pathway. We have pioneered the study of MetAP2 inhibitors in both common and rare forms of obesity. Our lead product candidate is ZGN-1061, a novel fumagillin-class MetAP2 inhibitor administered by subcutaneous injection, which is currently being profiled for its utility in the treatment of metabolic diseases including type 2 diabetes and obesity. We have completed a Phase 1 clinical trial of ZGN-1061 in the Netherlands, which was comprised of a single ascending dose, or SAD, portion and a multiple ascending dose, or MAD, portion. This clinical trial evaluated ZGN-1061 for safety, tolerability and pharmacokinetics while also gaining an early indication of efficacy over four weeks of treatment. We reported positive top line results from this clinical trial in May 2017 and presented the full data package at the American Diabetes Association's 77th Annual Scientific Sessions in June 2017. ZGN-1061 demonstrated rapid drug absorption and clearance in line with criteria established in advance for the molecule, and has a favorable safety profile, with no evidence of prothrombotic effects. The data show that ZGN-1061 treatment causes improvements across multiple metabolic measures consistent with MetAP2 inhibition, and patients in the clinical trial experienced mean weight loss of up to approximately one pound per week. We plan to advance ZGN-1061 into a Phase 2 clinical trial in patients with type 2 diabetes who are overweight or obese, in Australia and New Zealand in the third quarter of 2017.

ZGN-1061 acts through potent inhibition of MetAP2, an enzyme that modulates the activity of key cellular processes that control metabolism. MetAP2 inhibitors work, at least in part, by directing MetAP2 binding to cellular stress and growth factor mediators, thereby reducing the tone of signals that drive lipid synthesis by the liver and fat storage throughout the body. In this manner, MetAP2 inhibition serves the purpose of re-establishing balance to the ways the body stores and metabolizes fat and glucose. MetAP2 inhibitors reduce the production of new fatty acid molecules by the liver and help convert stored fats into useful energy, while reducing hunger. In animal models that mimic aspects of type 2 diabetes, these processes lead to improvement of glycemic control independent of weight loss.

ZGN-1061 was discovered by our researchers as part of a multi-year campaign to identify novel compounds for development in the treatment of type 2 diabetes, and that avoided limiting pre-clinical safety concerns observed with beloranib, including teratogenicity and effects on testicular function. To date, the compound has similar efficacy, potency, and range of activity in animal models as beloranib, but displays highly differentiated properties and improved safety margins in pre-clinical studies, supporting the value of the compound as a more highly optimized MetAP2 inhibitor. Further, the compound displays improved safety margins in non-clinical safety studies relative to beloranib for effects on coagulation in dogs, an effect that correlates with reduced impact on endothelial cell proliferation *in vitro*.

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Since our inception in November 2005, we have devoted substantially all of our resources to developing ZGN-1061, beloranib, and ZGN-839, building our intellectual property portfolio, developing our supply chain, business planning, raising capital, and providing general and administrative support for such operations. From our inception through our initial public offering, or IPO, in June 2014, we received gross proceeds of \$104.0 million from sales of redeemable convertible preferred stock and, to a lesser extent, through the issuances of convertible promissory notes. During June 2014, we completed our IPO with net proceeds of \$102.7 million after deducting underwriting discounts and commissions paid by us. On January 28, 2015, we completed a follow-on offering of our common stock, with net proceeds of \$130.0 million after deducting underwriting discounts and commissions paid by us.

We have never generated any revenue and have incurred net losses in each year since our inception. We have an accumulated deficit of \$263.9 million as of June 30, 2017. Our net loss was \$26.4 million for the six months ended June 30, 2017 and \$57.9 million for the year ended December 31, 2016. These losses have resulted principally from costs incurred in connection with in-licensing of beloranib, research and development activities and general and administrative costs associated with our operations. We expect to incur significant expenses and operating losses for the foreseeable future.

We expect to continue to incur expenses in connection with our ongoing activities, if and as we:

- advance the development of ZGN-1061 through Phase 2 and later-stage clinical trials;
- seek to identify additional product candidates and indications for our product candidates;
- seek to obtain regulatory approvals for our product candidates;
- add operational, financial and management information systems;
- add personnel, including personnel to support our product development and future commercialization; and
- maintain, leverage and expand our intellectual property portfolio.

As a result, we will need additional financing to support our continuing operations. Until such time that we can generate significant revenue from product sales, if ever, we expect to finance our operations through a combination of public, private equity, debt financings, or other sources, which may include collaborations with third parties. Arrangements with collaborators or others may require us to relinquish rights to certain of our technologies or product candidates. In addition, we may never successfully complete development of any of our product candidates, obtain adequate patent protection for our technology, obtain necessary regulatory approval for our product candidates or achieve commercial viability for any approved product candidates. Adequate additional financing may not be available to us on acceptable terms, or at all. Our failure to raise capital as and when needed would have a negative impact on our financial condition and our ability to pursue our business strategy. We will need to generate significant revenue to achieve profitability, and we may never do so.

We expect that our existing cash, cash equivalents and marketable securities as of June 30, 2017, will enable us to fund our operating expenses and capital expenditure requirements for a period of at least one year from the issuance date of this Quarterly Report. See “– Liquidity and Capital Resources.”

Financial Operations Overview

Revenue

We have not generated any revenue from product sales since our inception, and do not expect to generate any revenue from the sale of products in the near future. If our development efforts result in clinical success and regulatory approval or collaboration agreements with third parties for our product candidates, we may generate revenue from those product candidates or collaborations.

Operating Expenses

The majority of our operating expenses since inception have consisted primarily of research and development activities, and general and administrative costs.

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Research and Development Expenses

Research and development expenses, which consist primarily of costs associated with our product research and development efforts, are expensed as incurred. Research and development expenses consist primarily of:

- personnel costs, including salaries, related benefits and stock-based compensation for employees engaged in scientific research and development functions;
- third-party contract costs relating to research, formulation, manufacturing, pre-clinical studies and clinical trial activities;
- external costs of outside consultants;
- payments made under our third-party licensing agreements;
- sponsored research agreements;
- laboratory consumables; and
- allocated facility-related costs.

We are currently primarily focused on developing ZGN-1061 and other early research activities and typically use our employee, consultant and infrastructure resources across our research and development programs. We track outsourced development costs by product candidate or development program, but we do not allocate personnel costs, external consultant costs, payments made under our licensing agreements or other internal costs to specific development programs or product candidates unless the payments are specifically identifiable to a development program or product candidate. We record our research and development expenses net of any research and development tax incentives we are entitled to receive from government authorities.

Research and development activities are central to our business. Product candidates in later stages of clinical development generally have higher development costs than those in earlier stages of clinical development, primarily due to the increased size and duration of later-stage clinical trials. We expect that our research and development expenses will increase in the foreseeable future as we pursue later stages of clinical development of our product candidates.

We cannot determine with certainty the duration and completion costs of the current or future clinical trials of our product candidates or if, when, or to what extent we will generate revenue from the commercialization and sale of any of our product candidates that obtain regulatory approval. We may never succeed in achieving regulatory approval for any of our product candidates. The duration, costs, and timing of clinical trials and development of our product candidates will depend on a variety of factors, including:

- the scope, rate of progress, and expense of clinical trials and other research and development activities;
- clinical trial results;
- uncertainties in clinical trial enrollment rate or design;
- significant and changing government regulation;
- the timing and receipt of any regulatory approvals; and
- the U.S. Food and Drug Administration, or FDA's or other regulatory authority's influence on clinical trial design.

A change in the outcome of any of these variables with respect to the development of a product candidate could mean a significant change in the costs and timing associated with the development of that product candidate. For example, if the FDA, or another regulatory authority were to require us to conduct clinical trials beyond those that we currently anticipate will be required for the completion of clinical development of a product candidate, or if we experience significant delays in enrollment in any of our clinical trials, we could be required to expend significant additional financial resources and time on the completion of clinical development.

General and Administrative Expenses

General and administrative expenses consist primarily of personnel costs, consisting of salaries, related benefits and stock-based compensation, of our executive, finance, business and corporate development and other administrative functions. General and administrative expenses also include travel expenses, allocated facility-related costs not otherwise included in research and development expenses, insurance expenses, and professional fees for auditing, tax and legal services, including legal expenses to pursue patent protection of our intellectual property. We expect that general and administrative expenses will decrease during 2017 as compared to 2016 primarily due to reduced headcount and related costs.

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Other Income (Expense)

Interest income. Interest income consists of interest earned on our cash equivalents and marketable securities. Our interest income has not been significant due to low interest earned on invested balances. We anticipate that our interest income will decrease as we incur operating losses.

Interest expense. Interest expense relates to outstanding borrowings under the 2014 Credit Facility, consisting of the stated interest of 8.1% per year due on outstanding borrowings, a final payment of 6% of amounts drawn down that is being recorded as interest expense over the term through the maturity date using the effective-interest method, the amortization of deferred financing costs, the accretion of debt discounts relating to the 2014 Credit Facility, and a fee which was paid to the lender upon the completion of our IPO.

Foreign currency transaction gains (losses), net. Foreign currency transaction gains (losses), net consists of the realized and unrealized gains and losses from foreign currency-denominated cash balances, vendor payables and tax-related receivables from the Australian government. We currently do not engage in hedging activities related to our foreign currency-denominated receivables and payables; as such, we cannot predict the impact of future foreign currency transaction gains and losses on our operating results. See “– Quantitative and Qualitative Disclosures about Market Risk.”

Income Taxes

Since our inception in 2005, we have not recorded any U.S. federal or state income tax benefits for the net losses we have incurred in each year or our earned tax credits, due to our uncertainty of realizing a benefit from those items. As of December 31, 2016, we had net operating loss carryforwards for federal and state income tax purposes of \$49.1 million and \$35.9 million, respectively, which begin to expire in 2026 and 2030, respectively. As of December 31, 2016, we did not record deferred tax assets of \$12.8 million (gross) that were attributable to stock option exercises which will be recorded as an increase in additional paid in capital once they are realized in accordance with accounting for stock-based compensation awards. These deductions are not reflected in the federal and state net operating loss carryforwards and the capitalized research and development expense deferred tax assets in the amounts of \$9.4 million, \$7.2 million, and \$3.4 million, respectively. As of December 31, 2016, we also had available tax credit carryforwards for federal and state income tax purposes of \$13.1 million and \$1.9 million, respectively, which begin to expire in 2026 and 2021, respectively.

Results of Operations

Comparison of the Three Months Ended June 30, 2017 and 2016

The following table summarizes our results of operations for the three months ended June 30, 2017 and 2016:

	Three Months Ended June 30,		
	2017	2016	Increase (Decrease)
	(in thousands)		
Statement of Operations Data:			
Revenue	\$ —	\$ —	\$ —
Operating expenses:			
Research and development	10,528	10,163	365
General and administrative	3,008	4,899	(1,891)
Total operating expenses	13,536	15,062	(1,526)
Loss from operations	(13,536)	(15,062)	1,526
Other income (expense):			
Interest income	247	225	22
Interest expense	(53)	(140)	87
Foreign currency transaction gains (losses), net	(5)	(51)	46
Total other income (expense), net	189	34	155
Net loss	<u>\$ (13,347)</u>	<u>\$ (15,028)</u>	<u>\$ 1,681</u>

Research and development expenses

	Three Months Ended June 30,		
	2017	2016	Increase (Decrease)
	(in thousands)		
Direct research and development expenses by program:			
ZGN-1061:			
Pre-clinical and manufacturing	\$ 3,969	\$ 1,244	\$ 2,725
Clinical trials	934	202	732
Subtotal	4,903	1,446	3,457
Discovery and screening	1,551	—	1,551
Beloranib:			
Pre-clinical and manufacturing	386	1,304	(918)
Clinical trials	27	1,965	(1,938)
Subtotal	413	3,269	(2,856)
ZGN-839	—	377	(377)
Subtotal	6,867	5,092	1,775
Unallocated expenses:			
Personnel related	1,821	2,238	(417)
Non-cash stock-based compensation	877	1,002	(125)
Consultants	567	1,291	(724)
Other	396	540	(144)
Subtotal	3,661	5,071	(1,410)
Total research and development expenses	<u>\$10,528</u>	<u>\$10,163</u>	<u>\$ 365</u>

Research and development expenses for the three months ended June 30, 2017 increased \$0.4 million compared to the three months ended June 30, 2016. The increase was primarily due to increased costs of \$3.5 million related to our ZGN-1061 program and an increase of \$1.6 million related to work on discovery and screening, partially offset by a \$2.9 million decrease in our beloranib program and a decrease of \$1.4 million associated with our unallocated expenses.

Costs associated with our ZGN-1061 program increased period over period by \$3.5 million. In the third quarter of 2016 we initiated a Phase 1 clinical trial for ZGN-1061 which completed recruiting and dosing patients in the first quarter of 2017. The overall increase is primarily due to additional pre-clinical studies as well as drug product and drug substance activities as we prepare for the initiation of a Phase 2 clinical trial for which we plan to enroll approximately 120 patients for 12 weeks of dosing which we expect to commence in the third quarter of 2017. The expenses during the 2016 period were for startup costs for the Phase 1 clinical trial of ZGN-1061 in the Netherlands, which was comprised of 39 patients in a single ascending dose, or SAD, portion and 29 patients in a multiple ascending dose, or MAD, portion.

Clinical trials costs and related expenses for beloranib decreased by \$1.9 million period over period and pre-clinical and manufacturing costs decreased \$0.9 million period over period, both as a result of the suspension of our beloranib program in July 2016. During the three months ended June 30, 2016, we reported topline clinical data from our Phase 2b clinical trial in patients with severe obesity complicated by type 2 diabetes and our U.S. Phase 3 clinical trial in patients with Prader-Willi Syndrome, or PWS, in the first quarter of 2016 and recorded additional clinical trial and other costs related to the clinical program in the three months ended June 30, 2016.

Unallocated expenses decreased period over period primarily due to a decrease of \$0.7 million in consultants, as well as a decrease in personnel related costs of \$0.4 million. Consultant costs decreased primarily related to our beloranib program which we suspended further development in July 2016. Personnel related expenses decreased primarily from a reduction in the number of employees for the second quarter of the 2017 as compared to 2016, as we had a reduction in workforce which took place in July 2016. Other unallocated expenses decreased due to lower travel expenses and facilities expenses.

General and administrative expenses

	Three Months Ended June 30,		
	2017	2016	Increase (Decrease)
	(in thousands)		
Personnel related	\$ 586	\$1,039	\$ (453)
Non-cash stock-based compensation	1,225	1,852	(627)
Professional fees	742	1,497	(755)
Other	455	511	(56)
Total general and administrative expenses	<u>\$3,008</u>	<u>\$4,899</u>	<u>\$ (1,891)</u>

General and administrative expenses for the three months ended June 30, 2017 decreased \$1.9 million compared to the three months ended June 30, 2016. The decrease was due to a decrease in professional fees of \$0.8 million, non-cash stock-based compensation expense of \$0.6 million, and personnel related costs of \$0.5 million. Professional fees decreased primarily due to lower legal fees as the class action lawsuit plaintiffs had filed a notice of appeal to the First Circuit Court of Appeals and on April 7, 2017, the dismissal with prejudice was affirmed. The decrease was also due to lower commercial readiness costs and investor relations and public relations costs compared to the same period in 2016, primarily as a result of suspending development of beloranib in July 2016. Non-cash stock compensation decreased due mainly to our earliest stock option grants becoming fully expensed, as well as a lower stock option grant price for the 2017 annual grant. Personnel related expenses decreased primarily due to a reduction in the number of employees for the second quarter of 2017 as compared to 2016, as we had a reduction in workforce which took place in July 2016.

Other income (expense), net

Interest expense. Interest expense for the three months ended June 30, 2017 and 2016 of less than \$0.1 million and \$0.1 million, respectively, was related to interest expense on our outstanding borrowings under the 2014 Credit Facility. Interest expense consists primarily of the stated interest of 8.1% per year due on outstanding borrowings. It also includes expense related to the final payment of 6% of amounts drawn down that is being recorded over the term through the maturity date using the effective-interest method and the amortization of deferred financing costs and debt discounts relating to the 2014 Credit Facility.

Interest income. Interest income of \$0.2 million for the three months ended June 30, 2017 and 2016 was related to interest earned on our marketable securities balances.

Foreign currency transaction gains (losses), net. We had foreign currency transaction losses of less than \$0.1 million for the three months ended June 30, 2017 and 2016. Foreign currency transaction gains and losses consisted of the realized and unrealized gains and losses from foreign currency-denominated cash balances, vendor payables and tax-related receivables from the Australian government, generally reflecting the fluctuation of the Australian dollar relative to the U.S. dollar.

Results of Operations**Comparison of the Six Months Ended June 30, 2017 and 2016**

The following table summarizes our results of operations for the six months ended June 30, 2017 and 2016:

	Six Months Ended June 30,		
	2017	2016	Increase (Decrease)
	(in thousands)		
Statement of Operations Data:			
Revenue	\$ —	\$ —	\$ —
Operating expenses:			
Research and development	20,205	22,660	(2,455)
General and administrative	6,596	10,259	(3,663)
Total operating expenses	26,801	32,919	(6,118)
Loss from operations	(26,801)	(32,919)	6,118
Other income (expense):			
Interest income	474	434	40
Interest expense	(126)	(300)	174
Foreign currency transaction gains (losses), net	95	21	74
Total other income (expense), net	443	155	288
Net loss	<u>\$ (26,358)</u>	<u>\$ (32,764)</u>	<u>\$ 6,406</u>

Research and development expenses

	Six Months Ended June 30,		
	2017	2016	Increase (Decrease)
	(in thousands)		
Direct research and development expenses by program:			
ZGN-1061:			
Pre-clinical and manufacturing	\$ 7,868	\$ 2,213	\$ 5,655
Clinical trials	2,429	277	2,152
Subtotal	<u>10,297</u>	<u>2,490</u>	<u>7,807</u>
Discovery and screening	<u>2,069</u>	<u>265</u>	<u>1,804</u>
Beloranib:			
Pre-clinical and manufacturing	590	3,665	(3,075)
Clinical trials	40	5,704	(5,664)
Subtotal	<u>630</u>	<u>9,369</u>	<u>(8,739)</u>
ZGN-839	—	726	(726)
Subtotal	<u>12,996</u>	<u>12,850</u>	<u>146</u>
Unallocated expenses:			
Personnel related	3,703	4,446	(743)
Non-cash stock-based compensation	1,733	1,830	(97)
Consultants	1,037	2,478	(1,441)
Other	736	1,056	(320)
Subtotal	<u>7,209</u>	<u>9,810</u>	<u>(2,601)</u>
Total research and development expenses	<u>\$20,205</u>	<u>\$22,660</u>	<u>\$ (2,455)</u>

Research and development expenses for the six months ended June 30, 2017 decreased \$2.5 million compared to the six months ended June 30, 2016. The decrease was primarily due to an \$8.7 million decrease in our beloranib program and a decrease of \$2.6 million associated with our unallocated expenses partially offset by increased costs of \$7.8 million related to our ZGN-1061 program, as well as an increase in discovery and screening expenses of \$1.8 million.

Costs associated with our ZGN-1061 program increased period over period by \$7.8 million. In the third quarter of 2016 we initiated the Phase 1 clinical trial for ZGN-1061 which completed recruiting and dosing patients in the first quarter of 2017. The overall increase is primarily due to additional pre-clinical studies as well as drug product and drug substance activities as we start to prepare for the Phase 2 clinical trial which plans to enroll 120 patients for a 12 week trial with dosing commencing in the third quarter of 2017. The expenses during the 2016 period were for startup costs for the Phase 1 clinical trial of ZGN-1061 in the Netherlands, which was comprised of 39 patients in a single ascending dose, or SAD, portion and 29 patients in a multiple ascending dose, or MAD, portion.

Of the decrease in our beloranib program, clinical trials and related expenses for beloranib decreased by \$5.7 million period over period and pre-clinical and manufacturing costs decreased \$3.1 million period over period, both as a result of the suspension of our beloranib program in July 2016. During the six months ended June 30, 2016, we reported topline clinical data from our Phase 2b clinical trial in patients with severe obesity complicated by type 2 diabetes and our U.S. Phase 3 clinical trial in patients with PWS.

Unallocated expenses decreased period over period primarily due to a decrease of \$1.4 million in consultants, as well as a decrease in personnel related costs of \$0.7 million. Consultant costs decreased primarily related to our beloranib program which we suspended in July 2016. Personnel related expenses decreased primarily from a reduction in the number of employees for the first and second quarters of the 2017 as compared to 2016, as we had a reduction in workforce which took place in July 2016. Other unallocated expenses decreased due to lower travel expenses and facilities expenses.

General and administrative expenses

	Six Months Ended June 30,		
	2017	2016	Increase (Decrease)
	(in thousands)		
Personnel related	\$1,213	\$ 2,061	\$ (848)
Non-cash stock-based compensation	2,370	3,780	(1,410)
Professional fees	2,119	3,284	(1,165)
Other	894	1,134	(240)
Total general and administrative expenses	<u>\$6,596</u>	<u>\$10,259</u>	<u>\$ (3,663)</u>

General and administrative expenses for the six months ended June 30, 2017 decreased \$3.7 million compared to the six months ended June 30, 2016. The decrease was due to a decrease in non-cash stock-based compensation expense of \$1.4 million, professional fees of \$1.2 million and personnel related costs of \$0.8 million. Non-cash stock compensation decreased due mainly to our earliest stock option grants becoming fully expensed, as well as a lower stock option grant price for the 2017 annual grant. Professional fees decreased primarily due to lower legal fees as the class action lawsuit plaintiffs had filed a notice of appeal to the First Circuit Court of Appeals and on April 7, 2017, the dismissal with prejudice was affirmed. The decrease was also due to lower commercial readiness costs and investor relations and public relations costs compared to the same period in 2016, primarily as a result of suspending development of beloranib in July 2016. Personnel related expenses decreased primarily from a reduction in the number of employees for the first and second quarters of 2017 as compared to 2016, as we had a reduction in workforce which took place in July 2016.

Other income (expense), net

Interest expense. Interest expense for the six months ended June 30, 2017 and 2016 of \$0.1 million and \$0.3 million, respectively, was related to interest expense on our outstanding borrowings under the 2014 Credit Facility. Interest expense consists primarily of the stated interest of 8.1% per year due on outstanding borrowings. It also includes expense related to the final payment of 6% of amounts drawn down that is being recorded over the term through the maturity date using the effective-interest method and the amortization of deferred financing costs and debt discounts relating to the 2014 Credit Facility.

Interest income. Interest income of \$0.5 million and \$0.4 million, respectively, for the six months ended June 30, 2017 and 2016 was related to interest earned on our marketable securities balances.

Foreign currency transaction gains (losses), net. We had foreign currency transaction gains of \$0.1 million and less than \$0.1 million, respectively, for the six months ended June 30, 2017 and 2016. Foreign currency transaction gains and losses consisted of the realized and unrealized gains and losses from foreign currency-denominated cash balances, vendor payables and tax-related receivables from the Australian government, generally reflecting the fluctuation of the Australian dollar relative to the U.S. dollar.

Liquidity and Capital Resources

As of June 30, 2017, we had cash, cash equivalents and marketable securities totaling \$106.0 million. We invest our cash in money market funds, commercial paper and corporate bonds, with the primary objectives to preserve principal, provide liquidity and maximize income without significantly increasing risk.

Since our inception in November 2005, we have not generated any revenue and have incurred recurring net losses. As of June 30, 2017, we had an accumulated deficit of \$263.9 million. From our inception through our IPO in June 2014, we received gross proceeds of \$104.0 million from sales of redeemable convertible preferred stock and, to a lesser extent, through the issuances of convertible promissory notes and a loan security agreement. During June 2014, we completed our IPO with net proceeds of \$102.7 million after deducting underwriting discounts and commissions paid by us. On January 28, 2015, we completed a follow-on offering of our common stock, with net proceeds of \$130.0 million after deducting underwriting discounts and commissions paid by us.

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We have outstanding amounts under the 2014 Credit Facility, which we entered into in March 2014. All promissory notes issued under the 2014 Credit Facility are collateralized by substantially all of our personal property, other than our intellectual property. There are no financial covenants associated with the 2014 Credit Facility; however, there are negative covenants restricting our activities, including limitations on dispositions, mergers or acquisitions; encumbering or granting a security interest in our intellectual property; incurring indebtedness or liens; paying dividends; making certain investments; and certain other business transactions.

Upon entering into this 2014 Credit Facility, we were obligated to make monthly, interest-only payments on any term loans funded under the 2014 Credit Facility until December 1, 2014 and, thereafter, to pay 36 consecutive, equal monthly installments of principal and interest from January 1, 2015 through December 1, 2017. As per the terms of the agreement, in June 2014, upon the completion of our IPO, the term of monthly, interest-only payments was extended until June 1, 2015. Outstanding term loans under the 2014 Credit Facility bear interest at an annual rate of 8.1%. In addition, a final payment equal to 6.0% of any amounts drawn under the facility is due upon the earlier of the maturity date, acceleration of the term loans or prepayment of all or part of the term loans. We were also obligated to pay a separate fee upon any initial public offering; a sale of substantially all of our assets; or a merger, reorganization or sale of our voting equity securities where existing voting stockholders hold less than 50% of voting equity securities after such a transaction.

The following table summarizes our sources and uses of cash for each of the periods presented below:

	Six Months Ended	
	June 30,	
	2017	2016
	(in thousands)	
Cash used in operating activities	\$ (21,860)	\$ (32,279)
Cash provided by investing activities	22,678	18,093
Cash used in financing activities	(1,444)	(1,383)
Net decrease in cash and cash equivalents	\$ (626)	\$ (15,569)

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Net cash used in operating activities

During the six months ended June 30, 2017, operating activities used \$21.9 million of cash, resulting from our net loss of \$26.4 million, partially offset by changes in our operating assets and liabilities of \$0.4 million and non-cash charges of \$4.1 million. Our net loss was primarily attributed to research and development activities related to our ZGN-1061 program and our general and administrative expenses. Our net non-cash charges during the six months ended June 30, 2017, consisted primarily of stock-based compensation expense of \$4.1 million. Net cash used in changes in our operating assets and liabilities during the six months ended June 30, 2017, consisted primarily of a \$0.9 million increase in accounts payable and accrued expenses partially offset by an increase in prepaid expenses and other current assets of \$0.2 million as well as an increase in the tax receivable of \$0.2 million.

During the six months ended June 30, 2016, operating activities used \$32.3 million of cash, resulting from our net loss of \$32.8 million and changes in our operating assets and liabilities of \$5.6 million, partially offset by non-cash charges of \$6.1 million. Our net loss was primarily attributed to research and development activities related to our beloranib program, our ZGN-1061 program, and our general and administrative expenses. Our net non-cash charges during the six months ended June 30, 2016, consisted primarily of stock-based compensation expense of \$5.6 million. Net cash used in changes in our operating assets and liabilities during the six months ended June 30, 2016, consisted primarily of a \$5.7 million decrease in accounts payable and accrued expenses and a \$0.3 million increase in our tax incentive receivable, partially offset by a \$0.4 million decrease in prepaid expenses and other current assets.

Net cash provided by investing activities

During the six months ended June 30, 2017, investing activities provided \$22.7 million of cash resulting from proceeds from sales and maturities of marketable securities of \$80.0 million, offset primarily by the use of cash for purchases of marketable securities of \$57.3 million.

During the six months ended June 30, 2016, investing activities provided \$18.1 million of cash resulting from proceeds from sales and maturities of marketable securities of \$88.7 million, offset by the use of cash for purchases of marketable securities of \$69.9 million and purchases of property and equipment of \$0.7 million.

Net cash used in financing activities

During the six months ended June 30, 2017, financing activities used \$1.6 million for payments related to our notes payable, partially offset by \$0.1 million received from proceeds relating to the exercise of common stock options and common stock purchased under our 2014 Employee Stock Purchase Plan.

During the six months ended June 30, 2016, financing activities used \$1.4 million for payments related to our notes payable, partially offset by \$0.1 million received from proceeds relating to the exercise of common stock options and common stock purchased under our 2014 Employee Stock Purchase Plan.

Operating Capital Requirements

ZGN-1061 recently completed Phase 1 clinical development, therefore we expect to continue to incur significant expenses and operating losses for the foreseeable future. We anticipate that we will continue to incur expenses, if and as we:

- advance the development of ZGN-1061 through Phase 2 clinical development and if successful, later-stage clinical trials;
- seek to identify additional product candidates and indications for our product candidates;
- seek to obtain regulatory approvals for our product candidates;
- add operational, financial and management information systems;
- add personnel, including personnel to support our product development and future commercialization; and
- maintain, leverage and expand our intellectual property portfolio.

We expect that our existing cash, cash equivalents and marketable securities as of June 30, 2017, will enable us to fund our operating expenses and capital expenditure requirements for a period of at least one year from the issuance date of this Quarterly Report. We have based this estimate on assumptions that may prove to be wrong, and we may use our available capital resources sooner than we currently expect. Because of the numerous risks and uncertainties associated with the development of ZGN-1061 and our other research and development activities and because the extent to which we may enter into collaborations with third parties for the development of our product candidates is unknown, we are unable to estimate the amounts of increased capital outlays and operating expenses associated with completing the research and development of our product candidates. Our future capital requirements for ZGN-1061 will depend on many factors, including:

- the costs, timing and outcome of regulatory review;
- the costs of future research and development activities, including clinical trials;
- the costs of preparing, filing and prosecuting patent applications, maintaining and enforcing our intellectual property rights and defending intellectual property-related claims;
- the extent to which we acquire or in-license other products, product candidates, or technologies; and
- our ability to establish any future collaboration arrangements on favorable terms, if at all.

Until such time, if ever, as we can generate substantial product revenue, we expect to finance our cash needs through a combination of equity offerings, debt financings, collaborations, strategic alliances and licensing arrangements. To the extent that we raise additional capital through the sale of equity or convertible debt securities, the ownership interest of our stockholders will be diluted, and the terms of these securities may include liquidation or other preferences that adversely affect the rights of our common stockholders. Debt financing, if available, may involve agreements that include covenants limiting or restricting our ability to take specific actions, such as incurring additional debt, making capital expenditures or declaring dividends and may require the issuance of warrants, which could potentially dilute their ownership interest. If we raise additional funds through collaborations, strategic alliances or licensing arrangements with third parties, we may have to relinquish valuable rights to our technologies, future revenue streams, research programs or grant licenses on terms that may not be favorable to us. If we are unable to raise additional funds through equity, or debt financings when needed, we may be required to delay, limit, reduce or terminate our product development or future commercialization efforts or grant rights to develop and market ZGN-1061 that we would otherwise prefer to develop and market ourselves.

Since our inception in 2005, we have not recorded any U.S. federal or state income tax benefits for the net losses we have incurred in each year or our earned tax credits, due to our uncertainty of realizing a benefit from those items. As of December 31, 2016, we had net operating loss carryforwards for federal and state income tax purposes of \$49.1 million and \$35.9 million, respectively, which begin to expire in 2026 and 2030, respectively. As of December 31, 2016, we did not record deferred tax assets of \$12.8 million (gross) that were attributable to stock option exercises which will be recorded as an increase in additional paid in capital once they are realized in accordance with accounting for stock-based compensation awards. These deductions are not reflected in the federal and state net operating loss carryforwards and the capitalized research and development expense deferred tax assets in the amounts of \$9.4 million, \$7.2 million, and \$3.4 million, respectively. As of December 31, 2016, we also had available tax credit carryforwards for federal and state income tax purposes of \$13.1 million and \$1.9 million, respectively, which begin to expire in 2026 and 2021, respectively. We have not completed a study to assess whether an ownership change, generally defined as a greater than 50% change (by value) in the equity ownership of our corporate entity over a three-year period, has occurred or whether there have been multiple ownership changes since our inception, due to the significant costs and complexities associated with such studies. Accordingly, our ability to utilize our tax carryforwards may be limited. Additionally, U.S. tax laws limit the time during which these carryforwards may be utilized against future taxes. As a result, we may not be able to take full advantage of these carryforwards for federal and state tax purposes.

Contractual Obligations and Commitments

During the six months ended June 30, 2017, there have been no material changes to our contractual obligations and commitments outside the ordinary course of business from those described under the heading “Management’s Discussion and Analysis of Financial Condition and Results of Operations – Contractual Obligations and Commitments” in our Annual Report on Form 10-K for the year ended December 31, 2016, and in our Quarterly Report on Form 10-Q for the period ended March 31, 2017, as filed with the SEC on May 9, 2017. As of July 31, 2017, we negotiated the financial terms of the lease extensions for both of our office spaces in Boston, Massachusetts with additional minimum lease payments of \$0.2 million for the remainder of 2017, \$0.4 million for the years 2018 and 2019 and \$0.2 million for 2020.

Off-Balance Sheet Arrangements

During the periods presented we did not have and we do not currently have, any off-balance sheet arrangements, as defined under Securities and Exchange Commission rules, such as relationships with unconsolidated entities or financial partnerships, which are often referred to as structured finance or special purpose entities, established for the purpose of facilitating financing transactions that are not required to be reflected on our balance sheets.

Application of Critical Accounting Policies

Our condensed consolidated financial statements are prepared in accordance with GAAP. The preparation of our financial statements and related disclosures requires us to make estimates, assumptions and judgments that affect the reported amount of assets, liabilities, revenue, costs and expenses, and related disclosures. We believe that of our critical accounting policies which are described under the heading “Management’s Discussion and Analysis of Financial Condition and Results of Operations – Critical Accounting Policies and Significant Judgments and Estimates” in our Annual Report on Form 10-K for the year ended December 31, 2016, the following accounting policies involve the most judgment and complexity:

- accrued research and development costs; and
- stock-based compensation.

Accordingly, we believe the policies set forth above are critical to fully understanding and evaluating our financial condition and results of operations. If actual results or events differ materially from the estimates, judgments and assumptions used by us in applying these policies, our reported financial condition and results of operations could be materially affected. There have been no material changes to our critical accounting policies since December 31, 2016.

Recently Issued Accounting Pronouncements

Please read Note 2 to our condensed consolidated financial statements included in Part I Item 1, “Financial Statements and Supplementary Data,” of this Quarterly Report for a description of recent accounting pronouncements applicable to our business.

Item 3. Quantitative and Qualitative Disclosure about Market Risk

Interest Rate Fluctuation Risk

Our cash, cash equivalents, and marketable securities as of June 30, 2017 consisted of cash, corporate bonds, commercial paper, and money market accounts. The primary objectives of our investment activities are to preserve principal, provide liquidity and maximize income without significantly increasing risk. Our primary exposure to market risk is interest income sensitivity, which is affected by changes in the general level of U.S. interest rates. If market interest rates were to increase immediately and uniformly by 50 basis points, or one-half of a percentage point, from levels as of June 30, 2017, the net fair value of our interest-sensitive financial instruments would have resulted in a hypothetical decline of \$0.1 million.

Foreign Currency Exchange Risk

Foreign currency transaction exposure results primarily from transactions with our contract research organizations, or CROs, and other providers related to our clinical trials that are denominated in currencies other than the functional currency of the legal entity in which the transaction is recorded by us, primarily the Australian dollar. Any transaction gains or losses resulting from currency fluctuations is recorded on a separate line in our condensed consolidated statement of operations. Net foreign currency transaction gains of \$0.1 million and less than \$0.1 million were recorded for the six months ended June 30, 2017 and 2016, respectively.

Currently, our largest foreign currency exposures are those with respect to the Australian dollar. Relative to foreign currency exposures existing as of June 30, 2017, a 10% unfavorable movement in foreign currency exchange rates would expose us to an increased net loss. For the six months ended June 30, 2017, we estimated that a 10% unfavorable movement in foreign currency exchange rates would have increased our net loss by \$0.1 million. This amount is based on a sensitivity analysis performed on our financial position as of June 30, 2017. We have experienced and will continue to experience fluctuations in our net income (loss) as a result of revaluing our assets and liabilities that are not denominated in the functional currency of the entity that recorded the asset or liability. At this time, we do not hedge our foreign currency risk.

Item 4. Management's Evaluation of our Disclosure Controls and Procedures

We maintain disclosure controls and procedures (as defined in Rules 13a-15(e) or 15d-15(e) under the Securities Exchange Act of 1934, as amended, or the Exchange Act) that are designed to ensure that information required to be disclosed in the reports that we file or submit under the Exchange Act is (1) recorded, processed, summarized, and reported within the time periods specified in the SEC's rules and forms and (2) accumulated and communicated to our management, including our principal executive officer and principal financial officer, as appropriate, to allow timely decisions regarding required disclosure.

Based on this evaluation, our management, with the participation of our principal executive officer and principal financial officer, evaluated the effectiveness of our disclosure controls and procedures as of the end of the period covered by this report. In designing and evaluating our disclosure controls and procedures, our management recognizes that any 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. Our principal executive officer and principal financial officer have concluded based upon the evaluation described above that, as of June 30, 2017, our disclosure controls and procedures were effective at the reasonable assurance level.

We continue to review and document our disclosure controls and procedures, including our internal controls and procedures for financial reporting, and may from time to time make changes aimed at enhancing their effectiveness and to ensure that our systems evolve with our business.

Changes in Internal Control Over Financial Reporting

During the three months ended June 30, 2017, there have been no changes in our internal control over financial reporting (as defined in Rules 13a-15(f) or 15d-15(d) under the Exchange Act) that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

PART II – OTHER INFORMATION

Item 1. Legal Proceedings

On October 21, 2015, a purported stockholder of the Company filed a putative class action lawsuit in the U.S. District Court for the District of Massachusetts, against the Company and Thomas E. Hughes, captioned *Aviad Bessler v. Zafgen, Inc. and Thomas E. Hughes*, No. 1:15-cv-13618. An amended complaint was filed on February 22, 2016. The amended complaint alleges violations of

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Sections 10(b) and 20(a) of the Securities Exchange Act of 1934 and SEC Rule 10b-5 based on allegedly false and misleading statements and omissions regarding our clinical trials for beloranib. On August 9, 2016, the District Court granted the motion to dismiss and dismissed the amended complaint with prejudice. On August 12, 2016, plaintiffs filed a notice of appeal to the First Circuit Court of Appeals and, on April 7, 2017, the dismissal with prejudice was affirmed.

In the future, we may become party to legal matters and claims arising in the ordinary course of business, the resolution of which we do not anticipate would have a material adverse impact on our financial position, results of operations or cash flows.

Item 1A. Risk Factors

Investing in our common stock involves a high degree of risk. You should carefully consider the risks described below, as well as the other information in this Quarterly Report on Form 10-Q, or Quarterly Report, and in our other public filings before making an investment decision. Our business, prospects, financial condition, or operating results could be harmed by any of these risks, as well as other risks not currently known to us or that we currently consider immaterial. If any such risks or uncertainties actually occur, our business, financial condition or operating results could differ materially from the plans, projections and other forward-looking statements included in the section titled "Management's Discussion and Analysis of Financial Condition and Results of Operations" and elsewhere in this Quarterly Report and in our other public filings. The trading price of our common stock could decline due to any of these risks, and as a result, you may lose all or part of your investment.

Risks Related to Product Development, Regulatory Approval and Commercialization

We currently depend almost entirely on the success of one product candidate, ZGN-1061, which recently completed Phase 1 clinical development. We cannot be certain that we will be able to obtain regulatory approval for ZGN-1061, or successfully commercialize ZGN-1061 if approved.

We currently have only one product candidate, ZGN-1061, which recently completed Phase 1 clinical development in the Netherlands, and our business currently depends almost entirely on its successful clinical development, regulatory approval and commercialization. We currently have no drug products for sale and may never be able to develop marketable drug products. In order to conduct clinical trials in the United States we need to file an Investigational New Drug Application, or IND with the U.S. Food and Drug Administration, or FDA. Because our business is almost entirely dependent upon this one product candidate, any setback in our pursuit of regulatory approval for ZGN-1061 would have a material adverse effect on our business and prospects. The clinical trials of our product candidates are, and the manufacturing and marketing of our product candidates will be, subject to extensive and rigorous review and regulation by numerous government authorities in the United States and in other countries where we intend to test and, if approved, market any product candidate. Before obtaining regulatory approvals for the commercial sale of any product candidate, we must demonstrate through pre-clinical testing and clinical trials that the product candidate is safe and effective for use in each target indication. This process can take many years and will likely include post-marketing studies, or PMS, post-marketing requirements, or PMRs, and surveillance such as Risk Evaluation and Mitigation Strategies, or REMS, which will require the expenditure of substantial resources beyond the proceeds we currently have on hand.

Furthermore, we are not permitted to market ZGN-1061 in the United States until we receive approval of a New Drug Application, or NDA, from the FDA, or in any foreign countries until we receive the requisite marketing approval from such countries. Development of diabetes drugs requires approximately 2,500 subjects randomized to active doses of the product with 1,300 to 1,500 subjects exposed for a year and 300 to 500 subjects exposed for 18 months in order to estimate the safety of the drug in an NDA. In addition, it is anticipated that the FDA may require that their guidance for assessment of cardiovascular risk with diabetes products be followed which may require testing of 5,000 to 10,000 subjects. Pursuant to the FDA's draft guidance documents to industry related to the development of weight management drugs, in order to reasonably estimate the safety of a weight-management drug in an NDA, Phase 3 clinical trials must randomize approximately 3,000 subjects to active doses of the product and 1,500 subjects to placebo in clinical trials of one-year duration. Meeting the requirements of the FDA or certain European regulatory authorities may require that we conduct additional pivotal clinical trials. Accordingly, obtaining approval of an NDA or Marketing Authorization Application, or MAA, is a complex, lengthy, expensive and uncertain process.

The FDA and certain European regulatory authorities may delay, limit or deny approval of ZGN-1061 for many reasons, including, among others:

- the FDA may not accept our IND for ZGN-1061 or may put it on clinical hold;
- we may not be able to demonstrate that ZGN-1061 is safe and effective to the satisfaction of the FDA and the European Medicines Agency, or EMA;
- the results of our clinical trials may not meet the level of statistical or clinical significance required by the FDA and EMA for marketing approval;
- the FDA and EMA may disagree with the number, design, size, duration, conduct or implementation of our clinical trials;

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- the FDA and EMA may require that we conduct additional clinical trials or pre-clinical studies;
- the FDA and EMA may not approve the formulation, labeling or specifications of ZGN-1061;
- the contract research organizations, or CROs, that we retain to conduct our clinical trials may take actions outside of our control that materially adversely impact our clinical trials;
- the FDA and EMA may find the data from pre-clinical studies and clinical trials insufficient to demonstrate that ZGN-1061's clinical and other benefits outweigh its safety risks;
- the FDA and EMA may disagree with our interpretation of data from our pre-clinical studies and clinical trials;
- the FDA and EMA may not accept data generated at our clinical trial sites;
- if and when our NDA is submitted and reviewed by an FDA advisory committee, the FDA may have difficulties scheduling an advisory committee meeting in a timely manner or the advisory committee may recommend against approval of our application or may recommend that the FDA require, as a condition of approval, additional pre-clinical studies or clinical trials, limitations on approved labeling or distribution and use restrictions;
- the FDA could require development of a REMS as a condition of approval or post-approval, or may not agree with our proposed REMS, or may impose additional requirements that limit the promotion, advertising, distribution, or sales of ZGN-1061;
- the FDA and EMA may find deficiencies with or not approve the manufacturing processes or facilities of third-party manufacturers with which we contract; or
- the FDA and EMA may change their approval policies or adopt new regulations.

Any of these factors, many of which are beyond our control, could jeopardize our ability to obtain and/or maintain regulatory approval for and successfully market ZGN-1061. Of the large number of drugs in development in the United States, only a small percentage will successfully complete the FDA regulatory approval process and be commercialized. Accordingly, even if we are able to obtain the requisite financing to continue to fund our development and clinical trials, we cannot assure you that ZGN-1061 or any other of our product candidates will be successfully developed or commercialized.

Favorable results from pre-clinical studies and Phase 1 clinical trial of ZGN-1061 to date are not necessarily predictive of the results of longer-term pre-clinical studies or clinical trials of ZGN-1061. Given the thrombosis findings in humans treated with beloranib, development costs for ZGN-1061 may be higher and we may be unable to successfully develop, obtain regulatory approval for and commercialize ZGN-1061.

Favorable results from our pre-clinical studies of ZGN-1061 may not necessarily be predictive of the results from clinical trials. To date we have shown that ZGN-1061 has similar potency against the MetAP2 target and similar activity in mouse and rat models of obesity compared to beloranib. Toxicology studies in rats and dogs have shown that ZGN-1061 is not exhibiting any testicular safety signals or activation of thrombosis-related biochemical markers, and displays an appreciable margin for embryofetal toxicity, compared to beloranib, which showed testicular toxicity and pro-thrombotic effects with a small therapeutic margin and no margin for embryofetal toxicity. However, we can provide no assurance that the results of this pre-clinical development program will be replicated in future clinical trials of ZGN-1061. Many companies in the pharmaceutical and biotechnology industries have suffered significant setbacks in clinical trials after achieving positive results in pre-clinical and early-stage development. In particular, we have suffered significant setbacks in later-stage clinical trials of our former lead product candidate, beloranib, after achieving positive results in pre-clinical and clinical development, and we cannot be certain that we will not face similar setbacks in our development of ZGN-1061. The setbacks in later-stage clinical development have been caused by, among other things, pre-clinical findings made while clinical trials were underway or safety or efficacy observations made in clinical trials, including previously unreported or ununderstood adverse events. Moreover, pre-clinical and clinical data are often susceptible to varying interpretations and analyses, and many companies that believed their product candidates performed satisfactorily in pre-clinical studies and clinical trials nonetheless failed to obtain FDA and/or EMA approval. If we fail to produce positive results in our clinical trials of ZGN-1061, the development timeline and regulatory approval and commercialization prospects for our lead product candidate, and, correspondingly, our business and financial prospects, would be materially adversely affected.

Our product candidates may cause undesirable side effects that could delay or prevent their regulatory approval, limit the commercial profile of an approved label, or result in significant negative consequences following marketing approval, if any.

Undesirable side effects caused by our product candidates could cause us or regulatory authorities such as the FDA to interrupt, delay or halt clinical trials and could result in a more restrictive label or the delay or denial of regulatory approval by the FDA or other regulatory authorities. For example, common adverse events observed in patients treated with beloranib versus placebo included diarrhea, injection site bruising, dizziness, decreased appetite, anxiety and sleep disturbances (insomnia principally manifested as delayed onset of sleep and abnormal dreams), among others. In addition, an imbalance in the number of thrombotic events observed in

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patients treated with beloranib as compared to patients on placebo in our clinical trials was observed. We may see similar adverse events with ZGN-1061 as we saw with beloranib, and therefore, we will study many of these parameters in pre-clinical and clinical development of ZGN-1061. In the first small Phase 1 clinical trial assessment of ZGN-1061's safety, the most common side effects were mild gastrointestinal issues, (comparable between ZGN-1061 and placebo groups), headache and procedural-related irritation.

Further, if ZGN-1061 receives marketing approval and we or others identify undesirable side effects caused by the product (or any other similar product) after the approval, a number of potentially significant negative consequences could result, including:

- regulatory authorities may request that we withdraw the product from the market or may limit their approval of the product through labeling or other means;
- regulatory authorities may require the addition of labeling statements, such as a “black box” warning or a contraindication or a precaution;
- we may be required to change the way the product is distributed or administered, conduct additional clinical trials or change the labeling of the product;
- we may decide to remove the products from the marketplace;
- we could be sued and held liable for injury caused to individuals exposed to or taking our product candidates; and
- our reputation may suffer.

Any of these events could prevent us from achieving or maintaining market acceptance of the affected product candidate and could substantially increase the costs of commercializing our product candidates and significantly impact our ability to successfully commercialize our product candidates and generate revenues.

Failures or delays in the commencement or completion of our planned clinical trials of ZGN-1061 could result in increased costs to us and could delay, prevent or limit our ability to generate revenue and continue our business.

ZGN-1061 recently completed Phase 1 clinical development in the Netherlands and will require substantial further clinical development before we can submit an NDA to the FDA or an MAA to the EMA for its marketing approval.

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Despite the guidance we may receive from the FDA, the EMA, or other applicable regulatory authorities including Australia and New Zealand, any of these regulatory authorities can change their positions on the acceptability of our clinical trial designs or the clinical endpoints selected, which may require us to complete additional clinical trials or impose stricter approval conditions than we currently expect. Successful completion of such clinical trials is a prerequisite to submitting an NDA to the FDA and an MAA to the EMA and, consequently, the ultimate approval and commercial marketing of ZGN-1061. We do not know whether any clinical trials will begin or be completed on schedule, if at all, as the commencement and completion of clinical trials can be delayed or prevented for a number of reasons, including, among others:

- the FDA, EMA or other governing bodies in Europe or Australia and New Zealand may deny permission to pursue clinical trials and/or indications we want to initiate;
- delays in regulatory filings or receiving regulatory approvals of INDs, or clinical trial authorization applications, or CTAs, that may be required;
- unfavorable results from our pre-clinical and /or non-clinical studies, the FDA, the EMA or the applicable regulatory authorities in Australia or New Zealand, may require additional pre-clinical and /or non-clinical studies;
- delays in reaching or failing to reach agreement on acceptable terms with prospective CROs and clinical trial sites, the terms of which can be subject to extensive negotiation and may vary significantly among different CROs and trial sites;
- inadequate quantity or quality of a product candidate or other materials necessary to conduct clinical trials, for example delays in the manufacturing of sufficient supply of finished drug product;
- difficulties obtaining Institutional Review Board, or IRB, and/or ethics committee approval to conduct a clinical trial at a prospective site or sites in the United States, the European Union, Australia or New Zealand;
- challenges in recruiting and enrolling patients to participate in clinical trials, including the size and nature of the patient population, the proximity of patients to clinical trial sites, eligibility criteria for the clinical trial, the nature of the clinical trial protocol, the availability of approved effective treatments for the relevant disease and competition from other clinical trial programs for similar indications;
- severe or unexpected drug-related side effects experienced by patients in a clinical trial, including side effects previously identified in our previous clinical trials for belorانب;
- the FDA, the EMA, or the applicable regulatory authorities in Australia and New Zealand may disagree with our clinical trial design and our interpretation of data from clinical trials, or may change the requirements for approval even after it has reviewed and commented on the design for our clinical trials;
- difficulties in retaining or recruiting clinical investigators and/or patients in our ongoing or future clinical trials;
- reports from pre-clinical, non-clinical or clinical testing of other weight loss therapies that raise safety or efficacy concerns; and
- difficulties retaining patients who have enrolled in a clinical trial but may be prone to withdraw due to rigors of the clinical trial, lack of efficacy, side effects, screening and monitoring measures, personal issues or loss of interest.

Clinical trials may also be delayed or terminated as a result of ambiguous or negative interim results. In addition, a clinical trial may be suspended or terminated by us, the FDA, other regulatory authorities, the IRBs, or ethics committees, at the sites where the IRBs or ethics committees are overseeing a clinical trial, a data monitoring committee, or DMC, overseeing the clinical trial at issue or other regulatory authorities due to a number of factors, including, among others:

- failure to conduct the clinical trial in accordance with regulatory requirements or our clinical protocols;
- inspection of the clinical trial operations or trial sites by the FDA, the EMA, or the applicable regulatory authorities in Australia and New Zealand that reveals deficiencies or violations that require us to undertake corrective action, including the imposition of a partial clinical hold or a full clinical hold;
- unforeseen safety issues, including any that could be identified in our non-clinical or pre-clinical studies, adverse side effects or lack of effectiveness;
- changes in government regulations or administrative actions;
- problems with clinical supply materials; and
- lack of adequate funding to continue the clinical trial.

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Changes in regulatory requirements, FDA guidance or guidance from EMA, Australia or New Zealand or unanticipated events during our clinical trials of ZGN-1061 may occur, which may result in changes to clinical trial protocols or additional clinical trial requirements, which could result in increased costs to us and could delay our development timeline.

Changes in regulatory requirements, FDA guidance or guidance from EMA or unanticipated events during our clinical trials may force us to adjust our clinical program or the FDA, the EMA, or the applicable regulatory authorities in Australia and New Zealand may impose additional clinical trial and/or pre-clinical study requirements. For instance, the FDA issued draft guidance on developing products for weight management in February 2007, and issued draft guidance on developing products for the treatment of diabetes in February 2008 but these guidance documents may be revised at any time. In December 2008, FDA established guidance on evaluating cardiovascular risk of new therapies for the treatment of type 2 diabetes. In March 2012, the FDA's Endocrinologic and Metabolic Drugs Advisory Committee met to discuss possible changes to how the FDA evaluates the cardiovascular safety of weight-management drugs and although new guidance has not been issued yet it may occur at any time. Amendments to our clinical trial protocols would require resubmission to the FDA, the EMA, or the applicable regulatory authorities in Australia and New Zealand as well as IRBs and ethics committees for review and approval, which may adversely impact the cost, timing or successful completion of a clinical trial. If we experience delays completing, or if we terminate, any of our clinical trials, or if we are required to conduct additional clinical trials and/or pre-clinical studies, the commercial prospects for ZGN-1061 may be harmed and our ability to generate product revenue will be delayed.

We rely, and expect that we will continue to rely, on third parties to conduct any future clinical trials for ZGN-1061. If these third parties do not successfully carry out their contractual duties or meet expected deadlines, we may not be able to develop and obtain regulatory approval for or commercialize ZGN-1061 and our business could be substantially harmed.

We enter into agreements with third-party CROs to provide monitors for and to manage data for our ongoing clinical trials. We rely heavily on these parties for execution of clinical trials for ZGN-1061 and control only certain aspects of their activities. As a result, we have less direct control over the conduct, timing and completion of these clinical trials and the management of data developed through the clinical trials than would be the case if we were relying entirely upon our own staff. Communicating with outside parties can also be challenging, potentially leading to mistakes as well as difficulties in coordinating activities. Outside parties may:

- have staffing difficulties;
- fail to comply with contractual obligations;
- experience regulatory compliance issues;
- undergo changes in priorities or become financially distressed; or
- form relationships with other entities, some of which may be our competitors.

These factors may materially adversely affect the willingness or ability of third parties to conduct our clinical trials and may subject us to unexpected cost increases that are beyond our control. Nevertheless, we are responsible for ensuring that each of our clinical trials is conducted in accordance with the applicable protocol, legal and regulatory requirements and scientific standards, and our reliance on CROs does not relieve us of our regulatory responsibilities. We and our CROs are required to comply with requirements for Good Clinical Practice, or GCPs, which are legal requirements enforced by the FDA, the Competent Authorities of the Member States of the European Economic Area and comparable foreign regulatory authorities for any products in clinical development. The FDA enforces these GCP regulations through periodic inspections of clinical trial sponsors, principal investigators and clinical trial sites, IRBs, and other vendors that may be involved in the clinical development of new products. If we or our investigators or CROs fail to comply with applicable GCPs, the clinical data generated in our clinical trials may be deemed unreliable and the FDA or comparable foreign regulatory authorities may require us to perform additional clinical trials before approving our marketing applications. We cannot assure you that, upon inspection, the FDA will determine that any of our clinical trials comply with GCPs. In addition, our clinical trials must be conducted with products produced under current Good Manufacturing Practices, or cGMPs' regulations, to assure the identity, strength, quality, and purity of our drug product candidates being used in the clinical trials, as well as the to-be-marketed formulation and product. Our failure or the failure of our CROs and/or contract manufacturing organizations, or CMOs, to comply with these regulations may require us to repeat clinical trials, which would delay the regulatory approval process and could also subject us to enforcement action, up to and including, civil and criminal penalties.

Although we do design our clinical trials for ZGN-1061, investigators and CROs conduct all of the clinical trials. As a result, many important aspects of our drug development programs are outside of our direct control. In addition, the investigators or CROs may not perform all of their obligations under arrangements with us or in compliance with regulatory requirements, but we remain responsible and are subject to enforcement action that may include civil penalties up to and including criminal prosecution for any violations of FDA laws and regulations during the conduct of our clinical trials. If the investigators or CROs do not perform clinical trials in a satisfactory manner, breach their obligations to us, or fail to comply with regulatory requirements, the development and commercialization of ZGN-1061 may be delayed or our development program materially and irreversibly harmed. We cannot control the amount and timing of resources these investigators or CROs devote to our program or ZGN-1061. If we are unable to rely on clinical data collected by our investigators or CROs, we could be required to repeat, extend the duration of, or increase the size of our clinical trials and this could significantly delay commercialization and require significantly greater expenditures.

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If any of our relationships with these third-party investigators or CROs terminate, we may not be able to enter into arrangements with alternative investigators or CROs in a timely manner, or at all. If investigators or CROs do not successfully carry out their contractual duties or obligations or meet expected deadlines, if they need to be replaced or if the quality or accuracy of the clinical data they obtain is compromised due to the failure to adhere to our clinical protocols, regulatory requirements or for other reasons, any such clinical trials may be extended, delayed or terminated, and we may not be able to obtain regulatory approval for or successfully commercialize ZGN-1061. As a result, our financial results and the commercial prospects for ZGN-1061 in the subject indication would be harmed, our costs could increase and our ability to generate revenue could be delayed.

We rely completely on third-party suppliers to manufacture our clinical drug supplies for ZGN-1061, and we intend to rely on third parties to produce commercial supplies of ZGN-1061 and pre-clinical, clinical and commercial supplies of any future product candidate.

We do not currently have, nor do we currently plan to acquire, the infrastructure or capability to internally manufacture our clinical drug supply of ZGN-1061, or any future product candidates, for use in the conduct of our pre-clinical studies and clinical trials, and we lack the internal resources and the capability to manufacture any product candidates on a clinical or commercial scale. The facilities used by our CMOs to manufacture the active drug substance and final drug product must be approved by our quality assurance unit and inspected by the FDA and other comparable foreign regulatory agencies.

We rely on our CMOs to comply with cGMPs for manufacture of raw materials, active drug substance and finished drug products. If our CMOs cannot successfully manufacture material that conforms to our specifications and the regulatory requirements of the FDA or applicable foreign regulatory agencies, the CMOs will not be able to secure and/or maintain regulatory approval for their manufacturing facilities. While we manage our quality expectations through an audit program for our vendors and suppliers, we have no direct control over our CMOs' ability to maintain adequate quality control, quality assurance and qualified personnel. Furthermore, our CMOs are engaged with third party vendors to supply and/or manufacture starting materials or components for them, which exposes our CMOs to regulatory risks for the production of such materials and components. As a result, failure to satisfy the regulatory requirements for the production of those materials and components may affect the regulatory clearance of our CMOs' facilities generally. If the FDA or an applicable foreign regulatory agency does not approve these facilities for the manufacture of our product candidates or if it withdraws its approval in the future, we may need to find alternative manufacturing facilities, which would adversely impact our ability to develop, obtain regulatory approval for or market our product candidates.

We rely completely on third-party suppliers to manufacture our pre-clinical and clinical drug supplies for ZGN-1061. Currently each batch of ZGN-1061 is individually contracted under a work order, which is governed by a quality and service agreement. The current drug substance manufacturing process will support pre-clinical studies and early clinical trials and will be further optimized to support advanced clinical development and commercialization. Current drug substance, including key starting material, in inventory, is expected to support Phase 2 clinical trials. A new formulation with longer shelf life has been developed and manufactured to support Phase 2 clinical development.

Even if we receive marketing approval for ZGN-1061 in the United States, we may never receive regulatory approval to market ZGN-1061 outside of the United States.

We intend to pursue marketing approval of ZGN-1061 in the United States, the European Union and in other countries worldwide. In order to market any product outside of the United States, we must establish and comply with the numerous and varying safety, efficacy and other regulatory requirements of other countries, including potential additional clinical trials and/or pre-clinical studies. Approval procedures vary among countries and can involve additional product candidate testing and additional administrative review periods. The time required to obtain approvals in other countries might differ from that required to obtain FDA approval. The marketing approval processes in other countries may implicate all of the risks detailed above regarding FDA approval in the United States as well as other risks. In particular, in many countries outside of the United States, products must receive pricing and reimbursement approval before the product can be commercialized. Obtaining this approval can result in substantial delays in bringing products to market in such countries. In addition, on March 20, 2017, the United Kingdom government started the process to leave the European Union by April 2019, or Brexit. The effects of Brexit will depend on any agreements the United Kingdom makes to retain access to European Union markets either during a transitional period or more permanently. Brexit could lead to legal uncertainty and potentially divergent national laws and regulation as the United Kingdom determines which European Union laws to replace or replicate. Marketing approval in one country does not necessarily ensure marketing approval in another, but a failure or delay in obtaining marketing approval in one country may have a negative effect on the regulatory process or commercial activities in others. Failure to obtain marketing approval in other countries or any delay or other setback in obtaining such approval would impair our ability to market ZGN-1061 in such foreign markets. Any such impairment would reduce the size of our potential market, which could have a material adverse impact on our business, results of operations and prospects.

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Even if we receive marketing approval for ZGN-1061, it may not achieve broad market acceptance, which would limit the revenue that we generate from its sales.

The commercial success of ZGN-1061, if developed and approved for marketing by the FDA or EMA or other applicable regulatory authorities, will depend upon the awareness and acceptance of ZGN-1061 among the medical community, including physicians, patients, advocacy groups and healthcare payors. Market acceptance of ZGN-1061, if approved, will depend on a number of factors, including, among others:

- the relative convenience and ease of subcutaneous injections as the necessary method of administration of ZGN-1061;
- the prevalence and severity of any adverse side effects associated with ZGN-1061;
- limitations or warnings contained in the labeling approved for ZGN-1061 by the FDA, EMA, or other regulatory authorities, such as a “black box” warning;
- availability of alternative treatments, including a number of competitive type 2 diabetes or obesity therapies already approved or expected to be commercially launched in the near future;
- the willingness of the target patient population to try new therapies and of physicians to prescribe these therapies;
- the strength of marketing and distribution support and timing of market introduction of competitive products;
- publicity concerning our products or competing products and treatments;
- pricing;
- the effectiveness of our sales and marketing strategies;
- our ability to increase awareness of ZGN-1061 through marketing efforts;
- our ability to obtain sufficient third-party coverage or reimbursement;
- the willingness of patients to pay out-of-pocket in the absence of third-party coverage; and
- the likelihood that the FDA may require development of a REMS, as a condition of approval or post-approval or may not agree with our proposed REMS or may impose additional requirements that limit the promotion, advertising, distribution or sales of ZGN-1061.

If ZGN-1061 is approved but does not achieve an adequate level of acceptance by patients, advocacy groups, physicians and payors, we may not generate sufficient revenue from ZGN-1061 to become or remain profitable. Before granting reimbursement approval, healthcare payors may require us to demonstrate that, in addition to treating type 2 diabetes or obesity in patients, ZGN-1061 also provides incremental health benefits to patients. Our efforts to educate the medical community and third-party payors about the benefits of ZGN-1061 may require significant resources and may never be successful.

If we are unable to establish sales and marketing capabilities or enter into agreements with third parties to market and sell ZGN-1061, we may not be able to generate any revenue.

We do not currently have an established infrastructure for the sales, marketing and distribution of pharmaceutical products. In order to market ZGN-1061, if approved by the FDA or any other regulatory body, we must build our sales, marketing, managerial and other non-technical capabilities or make arrangements with third parties to perform these services. If we are unable to establish adequate sales, marketing and distribution capabilities, whether independently or with third parties, or if we are unable to do so on commercially reasonable terms, our business, results of operations, financial condition and prospects will be materially adversely affected.

Even if we receive marketing approval for ZGN-1061, we may still face future development and regulatory difficulties.

Even if we receive marketing approval for ZGN-1061, regulatory authorities may still impose significant restrictions on ZGN-1061’s indicated uses or marketing or impose ongoing requirements for potentially costly post-approval studies. ZGN-1061 will also be subject to ongoing FDA and EMA requirements governing the labeling, packaging, storage and promotion of the product and recordkeeping and submission of safety and other post-market information. The FDA has significant post-market authority, including, for example, the authority to require labeling changes based on new safety information and to require post-market studies or clinical trials to evaluate serious safety risks related to the use of a drug. The FDA also has the authority to require, as part of an NDA or post-approval, the submission of a REMS. Any REMS required by the FDA may lead to increased costs to assure compliance with new post-approval regulatory requirements and potential requirements or restrictions on the sale of approved products, all of which could lead to lower sales volume and revenue. Additionally, the FDA may require a PMS and/or PMRs, that could represent and result in additional restrictions and/or limitations for the product.

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Manufacturers of drug products and their facilities are subject to continual review and periodic inspections by the FDA and other regulatory authorities for compliance with cGMPs and other regulations. If we or a regulatory agency discover problems with ZGN-1061, such as adverse events of unanticipated severity or frequency, or problems with the facility where ZGN-1061 is manufactured, a regulatory agency may impose restrictions on ZGN-1061, the manufacturer or us, including requiring withdrawal of ZGN-1061 from the market or suspension of manufacturing. If we or the manufacturing facilities for ZGN-1061 fail to comply with applicable regulatory requirements, a regulatory agency may, among other things:

- issue warning letters or untitled letters;
- seek an injunction or impose civil or criminal penalties or monetary fines;
- suspend or withdraw marketing approval;
- suspend any ongoing clinical trials;
- refuse to approve pending applications or supplements to applications submitted by us;
- suspend or impose restrictions on operations, including costly new manufacturing requirements; or
- seize or detain products, refuse to permit the import or export of products, or request that we initiate a product recall.

Competing technologies could emerge, including devices and surgical procedures, adversely affecting our opportunity to generate revenue from the sale of ZGN-1061.

The biotechnology and pharmaceutical industries are intensely competitive and subject to rapid and significant technological change. We have competitors in a number of jurisdictions, many of which have substantially greater name recognition, commercial infrastructures and financial, technical and personnel resources than we have. Established competitors may invest heavily to quickly discover and develop novel compounds that could make ZGN-1061 obsolete or uneconomical. Any new product that competes with an approved product may need to demonstrate compelling advantages in efficacy, convenience, tolerability and safety to be commercially successful. Other competitive factors, including generic competition, could force us to lower prices or could result in reduced sales. In addition, new products developed by others could emerge as competitors to ZGN-1061. If we are not able to compete effectively against our current and future competitors, our business will not grow and our financial condition and operations will suffer.

Our future growth depends, in part, on our ability to penetrate foreign markets, where we would be subject to additional regulatory burdens and other risks and uncertainties.

Our future profitability will depend, in part, on our ability to commercialize ZGN-1061 in foreign markets for which we may rely on collaborations with third parties. If we commercialize ZGN-1061 in foreign markets, we would be subject to additional risks and uncertainties, including:

- our customers' ability to obtain reimbursement for ZGN-1061 in foreign markets;
- our inability to directly control commercial activities because we are relying on third parties;
- the burden of complying with complex and changing foreign regulatory, tax, accounting and legal requirements;
- different medical practices and customs in foreign countries affecting acceptance in the marketplace;
- import or export licensing requirements;
- longer accounts receivable collection times;
- longer lead times for shipping;
- language barriers for technical training;
- reduced protection of intellectual property rights in some foreign countries;
- foreign currency exchange rate fluctuations; and
- the interpretation of contractual provisions governed by foreign laws in the event of a contract dispute.

Foreign sales of ZGN-1061 could also be adversely affected by the imposition of governmental controls, political and economic instability, trade restrictions and changes in tariffs.

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We are subject to healthcare laws and regulations, which could expose us to criminal sanctions, civil penalties, contractual damages, reputational harm and diminished profits and future earnings.

Healthcare providers, physicians and others will play a primary role in the recommendation and prescription of ZGN-1061, if approved. Our future arrangements with third-party payors will expose us to broadly applicable fraud and abuse and other healthcare laws and regulations that may constrain the business or financial arrangements and relationships through which we market, sell and distribute ZGN-1061, if we obtain marketing approval. Restrictions under applicable federal and state healthcare laws and regulations include the following:

- The federal Anti-Kickback Statute prohibits, among other things, persons from knowingly and willfully soliciting, offering, receiving or paying remuneration, directly or indirectly, in cash or in kind, to induce or reward either the referral of an individual for, or the purchase, order or recommendation of, any good or service, for which payment may be made under federal healthcare programs such as Medicare and Medicaid.
- The federal false claims laws impose criminal and civil penalties, including those from civil whistleblower or qui tam actions pursuant to the federal False Claims Act, against individuals or entities for knowingly presenting, or causing to be presented, to the federal government, claims for payment that are false or fraudulent or making a false statement to avoid, decrease, or conceal an obligation to pay money to the federal government.
- The federal Health Insurance Portability and Accountability Act of 1996, as amended by the Health Information Technology for Economic and Clinical Health Act, imposes criminal and civil liability for executing a scheme to defraud any healthcare benefit program and also imposes obligations, including mandatory contractual terms, with respect to safeguarding the privacy, security and transmission of individually identifiable health information.
- The federal false statements statute prohibits knowingly and willfully falsifying, concealing or covering up a material fact or making any materially false statement in connection with the delivery of or payment for healthcare benefits, items or services.
- The federal transparency requirements, sometimes referred to as the “Sunshine Act,” under the Patient Protection and Affordable Care Act, require manufacturers of drugs, devices, biologics, and medical supplies to report to the Department of Health and Human Services information related to physician payments and other transfers of value and physician ownership and investment interests.
- Analogous state laws and regulations, such as state anti-kickback and false claims laws and transparency laws, may apply to sales or marketing arrangements and claims involving healthcare items or services reimbursed by non-governmental third-party payors, including private insurers, and some state laws require pharmaceutical companies to comply with the pharmaceutical industry’s voluntary compliance guidelines and the relevant compliance guidance promulgated by the federal government in addition to requiring drug manufacturers to report information related to payments to physicians and other healthcare providers or marketing expenditures and drug pricing.

Ensuring that our future business arrangements with third parties comply with applicable healthcare laws and regulations could be costly. It is possible that governmental authorities will conclude that our business practices do not comply with current or future statutes, regulations or case law involving applicable fraud and abuse or other healthcare laws and regulations. If our operations, including anticipated activities to be conducted by our sales team, were found to be in violation of any of these laws or any other governmental regulations that may apply to us, we may be subject to significant civil, criminal and administrative penalties, damages, fines and exclusion from government funded healthcare programs, such as Medicare and Medicaid, any of which could substantially disrupt our operations. If any of the physicians or other providers or entities with whom we expect to do business is found not to be in compliance with applicable laws, they may be subject to criminal, civil or administrative sanctions, including exclusions from government funded healthcare programs.

The FDA and other regulatory agencies actively enforce the laws and regulations prohibiting the promotion of off-label uses. If we are found to have improperly promoted off-label uses, we may become subject to significant liability.

The FDA and other regulatory agencies strictly regulate the promotional claims that may be made about prescription products, such as ZGN-1061, if approved. In particular, a product may not be promoted for uses that are not approved by the FDA or such other regulatory agencies as reflected in the product’s approved labeling. If we receive marketing approval for ZGN-1061, physicians may nevertheless prescribe ZGN-1061 to their patients in a manner that is inconsistent with the approved label. If we are found to have promoted such off-label uses, we may become subject to significant liability. The federal government has levied large civil and criminal fines against companies for alleged improper promotion and has enjoined several companies from engaging in off-label promotion and required that they enter into corporate integrity agreements with the Office of Inspector General of the Department of Health and Human Services, or OIG. The FDA has also requested that companies enter into consent decrees or permanent injunctions under which specified promotional conduct is changed or curtailed. If we cannot successfully manage the promotion of ZGN-1061, if approved, we could become subject to significant liability, which would materially adversely affect our business and financial condition.

Even if approved, reimbursement policies could limit our ability to sell ZGN-1061.

If approved by regulatory authorities, market acceptance and sales of ZGN-1061 will depend on reimbursement policies and may be affected by healthcare reform measures. Government authorities and third-party payors, such as private health insurers and health maintenance organizations, decide which medications they will pay for and establish reimbursement levels for those medications. Cost containment is a primary concern in the U.S. healthcare industry and elsewhere. Government authorities and these third-party payors have attempted to control costs by limiting coverage and the amount of reimbursement for particular medications. We cannot be sure that reimbursement will be available for ZGN-1061 and, if reimbursement is available, the level of such reimbursement. Reimbursement may impact the demand for, or the price of, ZGN-1061. If reimbursement is not available or is available only at limited levels, we may not be able to successfully commercialize ZGN-1061.

In some foreign countries, particularly in Canada and European countries, the pricing of prescription pharmaceuticals is subject to strict governmental control. In these countries, pricing negotiations with governmental authorities can take six to 12 months or longer after the receipt of regulatory approval and product launch. To obtain favorable reimbursement for the indications sought or pricing approval in some countries, we may be required to conduct a clinical trial that compares the cost-effectiveness of ZGN-1061 with other available therapies. If reimbursement for ZGN-1061 is unavailable in any country in which we seek reimbursement, if it is limited in scope or amount, if it is conditioned upon our completion of additional clinical trials, or if pricing is set at unsatisfactory levels, our operating results could be materially adversely affected.

Our development programs for our product candidates, which are primarily related to ZGN-1061, may require substantial financial resources and may ultimately be unsuccessful.

Our lead product candidate ZGN-1061 recently completed Phase 1 clinical development, and there are a number of FDA and certain European regulatory requirements that we must satisfy before we can commence late-stage clinical trials of ZGN-1061. Satisfaction of these requirements will entail substantial time, effort and financial resources. We may never satisfy these requirements. We believe that our cash, cash equivalents and marketable securities will be sufficient to fund operations for a period of at least one year from the issuance date of this Quarterly Report, but we may need to raise more funds to continue development and commercialization of ZGN-1061 and our other product candidates, which may not be easily available. Furthermore, any time, effort and financial resources we expend on our other early-stage development programs may adversely affect our ability to continue development and commercialization of ZGN-1061, and we may never commence clinical trials of such development programs despite expending significant resources in pursuit of their development. If we do commence clinical trials of our other potential product candidates, such product candidates may never be approved by the FDA or other regulatory authorities.

Risks Relating to Our Intellectual Property Rights

If we are unable to adequately protect our proprietary technology or maintain issued patents which are sufficient to protect ZGN-1061 or future product candidates, others could compete against us more directly, which would have a material adverse impact on our business, results of operations, financial condition and prospects.

Our commercial success will depend in part on our success in obtaining and maintaining issued patents and other intellectual property rights in the United States and elsewhere and protecting our proprietary technology. If we do not adequately protect our intellectual property and proprietary technology, competitors may be able to use our technologies and erode or negate any competitive advantage we may have, which could harm our business and ability to achieve profitability. Our owned patent application relates to compositions of matter and methods of use of ZGN-1061.

As of July 31, 2017, we own one issued U.S. patent, one pending U.S. patent application, one pending Patent Cooperation Treaty, or PCT, patent application, and two pending U.S. provisional patent applications that relate to ZGN-1061.

As of July 31, 2017, we own 15 issued U.S. patents, and 9 pending U.S. patent applications with pending foreign counterpart applications, all of which relate to our internal efforts to discover novel MetAP2 inhibitors.

We cannot provide any assurances that any of our pending patent applications that mature into issued patents will include claims with a scope sufficient to protect ZGN-1061 and our other product candidates. Other parties have developed technologies that may be related or competitive to our approach, and may have filed or may file patent applications and may have received or may receive patents that may overlap or conflict with our patent applications, either by claiming the same methods or formulations or by claiming subject matter that could dominate our patent position. The patent positions of biotechnology and pharmaceutical companies, including our patent position, involve complex legal and factual questions, and, therefore, the issuance, scope, validity and enforceability of any patent claims that we may obtain cannot be predicted with certainty. Patents, if issued, may be challenged, deemed unenforceable, invalidated, or circumvented. U.S. patents and patent applications may also be subject to interference proceedings, *ex parte* reexamination, or *inter partes* review proceedings, supplemental examination and challenges in district court. Patents may be subjected to opposition, post-grant review, or comparable proceedings lodged in various foreign, both national and

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regional, patent offices. These proceedings could result in either loss of the patent or denial of the patent application or loss or reduction in the scope of one or more of the claims of the patent or patent application. In addition, such proceedings may be costly. Thus, any patents that we may own or exclusively license may not provide any protection against competitors. Furthermore, an adverse decision in an interference proceeding can result in a third party receiving the patent right sought by us, which in turn could affect our ability to develop, market or otherwise commercialize ZGN-1061 and our other product candidates.

Furthermore, though an issued patent is presumed valid and enforceable, its issuance is not conclusive as to its validity or its enforceability and it may not provide us with adequate proprietary protection or competitive advantages against competitors with similar products. Competitors may also be able to design around our patents. Other parties may develop and obtain patent protection for more effective technologies, designs or methods. The laws of some foreign countries do not protect our proprietary rights to the same extent as the laws of the United States, and we may encounter significant problems in protecting our proprietary rights in these countries. If these developments were to occur, they could have a material adverse effect on our potential future sales.

Our ability to enforce our patent rights depends on our ability to detect infringement. It is difficult to detect infringers who do not advertise the components that are used in their products. Moreover, it may be difficult or impossible to obtain evidence of infringement in a competitor's or potential competitor's product. Any litigation to enforce or defend our patent rights, even if we were to prevail, could be costly and time-consuming and would divert the attention of our management and key personnel from our business operations. We may not prevail in any lawsuits that we initiate and the damages or other remedies awarded if we were to prevail may not be commercially meaningful.

In addition, proceedings to enforce or defend our patents could put our patents at risk of being invalidated, held unenforceable, or interpreted narrowly. Such proceedings could also provoke third parties to assert claims against us, including that some or all of the claims in one or more of our patents are invalid or otherwise unenforceable. If any of our patents covering ZGN-1061 are invalidated or found unenforceable, our financial position and results of operations would be materially and adversely impacted. In addition, if a court found that valid, enforceable patents held by third parties covered ZGN-1061, our financial position and results of operations would also be materially and adversely impacted.

The degree of future protection for our proprietary rights is uncertain, and we cannot ensure that:

- any of our patents, or any of our pending patent applications, if issued, will include claims having a scope sufficient to protect ZGN-1061 or any other products or product candidates;
- any of our pending patent applications will issue as patents;
- we will be able to successfully develop and commercialize ZGN-1061, if approved, before our relevant patents expire;
- we were the first to make the inventions covered by each of our patents and pending patent applications;
- we were the first to file patent applications for these inventions;
- others will not develop similar or alternative technologies that do not infringe our patents;
- any of our patents will be found to ultimately be valid and enforceable;
- any patents issued to us will provide a basis for an exclusive market for our commercially viable products, will provide us with any competitive advantages or will not be challenged by third parties;
- we will develop additional proprietary technologies or product candidates that are separately patentable; or
- that our commercial activities or products will not infringe upon the patents of others.

We rely upon unpatented trade secrets, unpatented know-how and continuing technological innovation to develop and maintain our competitive position, which we seek to protect, in part, by confidentiality agreements with our employees and our collaborators and consultants. We also have agreements with our employees and selected consultants that obligate them to assign their inventions to us and have non-compete agreements with some, but not all, of our consultants. It is possible that technology relevant to our business will be independently developed by a person that is not a party to such an agreement. Furthermore, if the employees and consultants who are parties to these agreements breach or violate the terms of these agreements, we may not have adequate remedies for any such breach or violation, and we could lose our trade secrets through such breaches or violations. Further, our trade secrets could otherwise become known or be independently discovered by our competitors.

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We may infringe the intellectual property rights of others, which may prevent or delay our product development efforts and stop us from commercializing or increase the costs of commercializing ZGN-1061, if approved.

Our success will depend in part on our ability to operate without infringing the intellectual property and proprietary rights of third parties. We cannot assure you that our business, products and methods do not or will not infringe the patents or other intellectual property rights of third parties.

The pharmaceutical industry is characterized by extensive litigation regarding patents and other intellectual property rights. Other parties may allege that ZGN-1061 or the use of our technologies infringes patent claims or other intellectual property rights held by them or that we are employing their proprietary technology without authorization. Patent and other types of intellectual property litigation can involve complex factual and legal questions, and their outcome is uncertain. Any claim relating to intellectual property infringement that is successfully asserted against us may require us to pay substantial damages, including treble damages and attorneys' fees if we are found to be willfully infringing another party's patents, for past use of the asserted intellectual property and royalties and other consideration going forward if we are forced to take a license. In addition, if any such claim were successfully asserted against us and we could not obtain such a license, we may be forced to stop or delay developing, manufacturing, selling or otherwise commercializing ZGN-1061.

Even if we are successful in these proceedings, we may incur substantial costs and divert management time and attention in pursuing these proceedings, which could have a material adverse effect on us. If we are unable to avoid infringing the patent rights of others, we may be required to seek a license, defend an infringement action or challenge the validity of the patents in court, or redesign our products. Patent litigation is costly and time consuming. We may not have sufficient resources to bring these actions to a successful conclusion. In addition, intellectual property litigation or claims could force us to do one or more of the following:

- cease developing, selling or otherwise commercializing ZGN-1061;
- pay substantial damages for past use of the asserted intellectual property;
- obtain a license from the holder of the asserted intellectual property, which license may not be available on reasonable terms, if at all; and
- in the case of trademark claims, redesign or rename the trademarks or trade names of our product candidates to avoid infringing the intellectual property rights of third parties, which may not be possible and, even if possible, could be costly and time-consuming.

Any of these risks coming to fruition could have a material adverse effect on our business, results of operations, financial condition and prospects.

We may be subject to claims challenging the inventorship or ownership of our patents and other intellectual property.

We may also be subject to claims that former employees, collaborators or other third parties have an ownership interest in our patents or other intellectual property. Litigation may be necessary to defend against these and other claims challenging inventorship or ownership. If we fail in defending any such claims, in addition to paying monetary damages, we may lose valuable intellectual property rights, such as exclusive ownership of, or right to use, valuable intellectual property. Such an outcome could have a material adverse effect on our business. Even if we are successful in defending against such claims, litigation could result in substantial costs and be a distraction to management and other employees.

Obtaining and maintaining our patent protection depends on compliance with various procedural, document submission, fee payment and other requirements imposed by governmental patent agencies, and our patent protection could be reduced or eliminated for non-compliance with these requirements.

The U.S. Patent and Trademark Office, or U.S. PTO, and various foreign governmental patent agencies require compliance with a number of procedural, documentary, fee payment and other provisions during the patent process. There are situations in which noncompliance can result in abandonment or lapse of a patent or patent application, resulting in partial or complete loss of patent rights in the relevant jurisdiction. In such an event, competitors might be able to enter the market earlier than would otherwise have been the case.

We may be involved in lawsuits to protect or enforce our patents or the patents of our licensors, which could be expensive, time-consuming and unsuccessful.

Competitors may infringe our patents or the patents of our licensors. To counter infringement or unauthorized use, we may be required to file infringement claims, which can be expensive and time-consuming. In addition, in an infringement proceeding, a court may decide that a patent of ours or our licensors is not valid, is unenforceable and/or is not infringed, or may refuse to stop the other party from using the technology at issue on the grounds that our patents do not cover the technology in question. An adverse result in any litigation or defense proceedings could put one or more of our patents at risk of being invalidated or interpreted narrowly and could put our patent applications at risk of not issuing.

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Interference proceedings provoked by third parties or brought by us may be necessary to determine the priority of inventions with respect to our patents or patent applications or those of our licensors. An unfavorable outcome could require us to cease using the related technology or to attempt to license rights to it from the prevailing party. Our business could be harmed if the prevailing party does not offer us a license on commercially reasonable terms. Our defense of litigation or interference proceedings may fail and, even if successful, may result in substantial costs and distract our management and other employees. We may not be able to prevent, alone or with our licensors, misappropriation of our intellectual property rights, particularly in countries where the laws may not protect those rights as fully as in the United States.

Furthermore, because of the substantial amount of discovery required in connection with intellectual property litigation, there is a risk that some of our confidential information could be compromised by disclosure during this type of litigation. There could also be public announcements of the results of hearings, motions or other interim proceedings or developments. If securities analysts or investors perceive these results to be negative, it could have a material adverse effect on the price of our common stock.

Issued patents covering our product candidates could be found invalid or unenforceable if challenged in court.

If we or one of our licensing partners initiated legal proceedings against a third party to enforce a patent covering our product candidate, the defendant could counterclaim that the patent covering our product candidate is invalid and/or unenforceable. In patent litigation in the United States, defendant counterclaims alleging invalidity and/or unenforceability are commonplace. Grounds for a validity challenge include alleged failures to meet any of several statutory requirements, including lack of novelty, obviousness or non-enablement. Grounds for unenforceability assertions include allegations that someone connected with prosecution of the patent withheld relevant information from the U.S. PTO, or made a misleading statement, during prosecution. Third parties may also raise similar claims before administrative bodies in the United States or abroad, even outside the context of litigation. Such mechanisms include re-examination, post grant review and equivalent proceedings in foreign jurisdictions, e.g., opposition proceedings. Such proceedings could result in revocation or amendment of our patents in such a way that they no longer cover our product candidates or competitive products. The outcome following legal assertions of invalidity and unenforceability is unpredictable. With respect to validity, for example, we cannot be certain that there is no invalidating prior art, of which we and the patent examiner were unaware during prosecution. If a defendant were to prevail on a legal assertion of invalidity and/or unenforceability, we would lose at least part, and perhaps all, of the patent protection on our product candidates. Such a loss of patent protection would have a material adverse impact on our business.

We do not seek to protect our intellectual property rights in all jurisdictions throughout the world and we may not be able to adequately enforce our intellectual property rights even in the jurisdictions where we seek protection.

Filing, prosecuting and defending patents on product candidates in all countries and jurisdictions throughout the world would be prohibitively expensive, and our intellectual property rights in some countries outside the United States could be less extensive than those in the United States. In addition, the laws of some foreign countries do not protect intellectual property rights to the same extent as federal and state laws in the United States. Consequently, we may not be able to prevent third parties from practicing our inventions in all countries outside the United States, or from selling or importing products made using our inventions in and into the United States or other jurisdictions. Competitors may use our technologies in jurisdictions where we have not obtained patent protection to develop their own products and further, may export otherwise infringing products to territories where we have patent protection, but enforcement is not as strong as that in the United States. These products may compete with our products and our patents or other intellectual property rights may not be effective or sufficient to prevent them from competing.

Many companies have encountered significant problems in protecting and defending intellectual property rights in foreign jurisdictions. The legal systems of certain countries, particularly certain developing countries, do not favor the enforcement of patents and other intellectual property protection, particularly those relating to biopharmaceuticals, which could make it difficult for us to stop the infringement of our patents or marketing of competing products in violation of our proprietary rights generally. For example, an April 2014 report from the Office of the United States Trade Representative identified a number of countries, including India and China, where challenges to the procurement and enforcement of patent rights have been reported. Several countries, including India and China, have been listed in the report every year since 1989. Proceedings to enforce our patent rights in foreign jurisdictions could result in substantial costs and divert our efforts and attention from other aspects of our business, could put our patents at risk of being invalidated or interpreted narrowly, could put our patent applications at risk of not issuing and could provoke third parties to assert claims against us. We may not prevail in any lawsuits that we initiate and the damages or other remedies awarded, if any, may not be commercially meaningful. Accordingly, our efforts to enforce our intellectual property rights around the world may be inadequate to obtain a significant commercial advantage from the intellectual property that we develop or license.

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We are dependent on licensed intellectual property for certain early-stage product candidates. If we were to lose our rights to licensed intellectual property, we may not be able to continue developing or commercializing such product candidates, if approved.

We have an exclusive license with Children's Medical Center Corporation, pursuant to which we exclusively licensed certain patent rights relating to decreasing the growth of fat tissue on a worldwide basis. We may enter into additional licenses to third-party intellectual property that are necessary or useful to our business. Current or future licensors may also allege that we have breached our license agreement and may accordingly seek to terminate our license with them. In addition, current or future licensors may decide to terminate our license at will. If successful, this could result in our loss of the right to use the licensed intellectual property, which could materially adversely affect our ability to develop and commercialize a product candidate or product, if approved, as well as harm our competitive business position and our business prospects.

We have not yet registered trademarks for a commercial trade name for ZGN-1061 and failure to secure such registrations could adversely affect our business.

We have not yet registered trademarks for a commercial trade name for ZGN-1061. Any future trademark applications may be rejected during trademark registration proceedings. Although we would be given an opportunity to respond to those rejections, we may be unable to overcome such rejections. In addition, in the U.S. PTO and in comparable agencies in many foreign jurisdictions, third parties are given an opportunity to oppose pending trademark applications and to seek to cancel registered trademarks. Opposition or cancellation proceedings may be filed against our trademarks, and our trademarks may not survive such proceedings. Moreover, any name we propose to use with our product candidates in the United States must be approved by the FDA, regardless of whether we have registered it, or applied to register it, as a trademark. The FDA typically conducts a review of proposed product names, including an evaluation of potential for confusion with other product names. If the FDA objects to any of our proposed proprietary product names, we may be required to expend significant additional resources in an effort to identify a suitable substitute name that would qualify under applicable trademark laws, not infringe the existing rights of third parties and be acceptable to the FDA.

If we do not obtain additional protection under the Hatch-Waxman Amendments and similar foreign legislation by extending the patent terms and obtaining data exclusivity for ZGN-1061, our business may be materially harmed.

Depending upon the timing, duration and specifics of development and FDA marketing approval of ZGN-1061, one or more of our U.S. patents may be eligible for limited patent term restoration under the Drug Price Competition and Patent Term Restoration Act of 1984, referred to as the Hatch-Waxman Amendments. The Hatch-Waxman Amendments permit a patent restoration term of up to five years as compensation for patent term lost during product development and the FDA regulatory review process. However, we may not be granted an extension because of, for example, failing to apply within applicable deadlines, failing to apply prior to expiration of relevant patents or otherwise failing to satisfy applicable requirements. Moreover, the applicable time period or the scope of patent protection afforded could be less than we request. If we are unable to obtain patent term extension or restoration or the term of any such extension is less than we request, our competitors may obtain approval of competing products following our patent expiration, and our ability to generate revenues could be materially adversely affected.

Changes in U.S. patent law could diminish the value of patents in general, thereby impairing our ability to protect our products.

The United States has recently enacted and is currently implementing the America Invents Act of 2011, which is wide-ranging patent reform legislation. Further, the U.S. Supreme Court has ruled on several patent cases in recent years, either narrowing the scope of patent protection available in certain circumstances or weakening the rights of patent owners in certain situations. In addition to increasing uncertainty with regard to our ability to obtain future patents, this combination of events has created uncertainty with respect to the value of patents, once obtained. Depending on decisions by the U.S. Congress, the federal courts and the U.S. PTO, the laws and regulations governing patents could change in unpredictable ways that would weaken our ability to obtain new patents or to enforce our existing patents or future patents.

We may be subject to damages resulting from claims that we or our employees have wrongfully used or disclosed alleged trade secrets of their former employers.

Our employees have been previously employed at other biotechnology or pharmaceutical companies, including our competitors or potential competitors. Although we are not aware of any claims currently pending against us, we may be subject to claims that these employees or we have inadvertently or otherwise used or disclosed trade secrets or other proprietary information of the former employers of our employees. Litigation may be necessary to defend against these claims. Even if we are successful in defending against these claims, litigation could result in substantial costs and be a distraction to management. If we fail in defending such claims, in addition to paying money claims, we may lose valuable intellectual property rights or personnel. A loss of key personnel or their work product could hamper or prevent our ability to develop and commercialize ZGN-1061 and other product candidates, which would materially adversely affect our business, financial condition and results of operations.

General Company-Related Risks

We have recently reduced the size of our organization, and we may encounter difficulties in managing this development and restructuring, which could disrupt our operations. In addition, we may not achieve anticipated benefits and savings from the reduction.

In July 2016, our board of directors approved the suspension of further development of beloraniib and a restructuring plan, pursuant to which our workforce was reduced by approximately 31% as of December 2016. The workforce reduction resulted in the loss of longer-term employees, the loss of institutional knowledge and expertise and the reallocation and combination of certain roles and responsibilities across the organization, all of which could adversely affect our operations. Given the complexity of our business, we must continue to implement and improve our managerial, operational and financial systems, manage our facilities and continue to recruit and retain qualified personnel. This will be made more challenging given the workforce reduction described above. As a result, our management may need to divert a disproportionate amount of its attention away from our day-to-day activities, and devote a substantial amount of time to managing these activities. Further, the restructuring and possible additional cost containment measures may yield unintended consequences, such as attrition beyond our intended workforce reduction and reduced employee morale. In addition, we may not achieve anticipated benefits from the workforce reduction. Due to our limited resources, we may not be able to effectively manage our operations or recruit and retain qualified personnel, which may result in weaknesses in our infrastructure and operations, risks that we may not be able to comply with legal and regulatory requirements, and loss of employees and reduced productivity among remaining employees. For example, the workforce reduction may negatively impact our clinical and regulatory functions, which would have a negative impact on our ability to successfully develop, and ultimately, commercialize ZGN-1061. If our management is unable to effectively manage this transition and workforce reduction and additional cost containment measures, our expenses may be more than expected and we may not be able to implement our business strategy. As a result, our future financial performance and our ability to commercialize ZGN-1061 successfully would be negatively affected.

Our future success depends on our ability to retain our executive officers, and particularly our current President and Chief Executive Officer, and to attract, retain and motivate qualified personnel.

We are highly dependent on Dr. Thomas E. Hughes, our President and Chief Executive Officer. We have entered into a severance and change in control agreement with Dr. Hughes, but he may terminate his employment with us at any time. Although we do not have any reason to believe that we will lose the services of Dr. Hughes in the foreseeable future, the loss of his services might impede the achievement of our research, development and commercialization objectives. We also do not have any key-man life insurance on Dr. Hughes.

Our success also depends upon the principal members of our executive, medical and development teams. We have entered into a severance and change in control agreement with our executive officers and department vice president level employees, but they may terminate their employment with us at any time. The loss of the services of any of these persons might impede the achievement of our development and commercialization objectives.

With any change in leadership, there is also a risk to retention of employees, as well as the potential for disruption to business operations, initiatives, plans and strategies.

We rely on consultants and advisors, including scientific and clinical advisors, to assist us in formulating our development and commercialization strategy. Our consultants and advisors may be employed by employers other than us and may have commitments under consulting or advisory contracts with other entities that may limit their availability to us and may not be subject to our standard non-compete agreements. Recruiting and retaining qualified scientific personnel and sales and marketing personnel will also be critical to our success. We may not be able to attract and retain these personnel on acceptable terms given the workforce reduction and competition among numerous pharmaceutical and biotechnology companies for similar personnel. We also experience competition for the hiring of scientific personnel from universities and research institutions. Failure to succeed in clinical trials may make it more challenging to recruit and retain qualified scientific personnel.

Our employees may engage in misconduct or other improper activities, including violating applicable regulatory standards and requirements or engaging in insider trading, which could significantly harm our business.

We are exposed to the risk of employee fraud or other misconduct. Misconduct by employees could include intentional failures to comply with the regulations of the FDA and applicable non-U.S. regulators, provide accurate information to the FDA and applicable non-U.S. regulators, comply with healthcare fraud and abuse laws and regulations in the United States and abroad, report financial information or data accurately or disclose unauthorized activities to us. In particular, sales, marketing and business arrangements in the healthcare industry are subject to extensive laws and regulations intended to prevent fraud, misconduct, kickbacks, self-dealing and other abusive practices. These laws and regulations restrict or prohibit a wide range of pricing, discounting, marketing and promotion, sales commission, customer incentive programs and other business arrangements. Employee misconduct could also involve the improper use of, including trading on, information obtained in the course of clinical trials, which

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could result in regulatory sanctions and serious harm to our reputation. We have adopted an insider trading policy and a code of conduct, but it is not always possible to identify and deter employee misconduct, and the precautions we take to detect and prevent this activity may be ineffective in controlling unknown or unmanaged risks or losses or in protecting us from governmental investigations or other actions or lawsuits stemming from a failure to comply with these laws or regulations. If any such actions are instituted against us, and we are not successful in defending ourselves or asserting our rights, those actions could have a significant impact on our business, including the imposition of significant fines or other sanctions.

We face potential product liability exposure, and, if claims are brought against us, we may incur substantial liability.

The use of belorانب and ZGN-1061 in clinical trials and the sale of ZGN-1061, if developed and approved, exposes us to the risk of product liability claims. Product liability claims might be brought against us by patients, healthcare providers or others selling or otherwise coming into contact with ZGN-1061. For example, we may be sued if any product we develop allegedly causes injury or death or is found to be otherwise unsuitable during product testing, manufacturing, marketing or sale. Any such product liability claims may include allegations of defects in manufacturing, defects in design, a failure to warn of dangers inherent in the product, including as a result of interactions with alcohol or other drugs, negligence, strict liability and a breach of warranties. Claims could also be asserted under state consumer protection acts. If we become subject to product liability claims and cannot successfully defend ourselves against them, we could incur substantial liabilities. In addition, regardless of merit or eventual outcome, product liability claims may result in, among other things:

- withdrawal of patients from our clinical trials;
- substantial monetary awards to patients or other claimants;
- decreased demand for ZGN-1061 or any future product candidates following marketing approval, if obtained;
- damage to our reputation and exposure to adverse publicity;
- increased FDA warnings on product labels;
- litigation costs;
- distraction of management's attention from our primary business;
- loss of revenue; and
- the inability to successfully commercialize ZGN-1061 or any future product candidates, if approved.

We maintain product liability insurance coverage for our clinical trials with a \$10.0 million annual aggregate coverage limit. Nevertheless, our insurance coverage may be insufficient to reimburse us for any expenses or losses we may suffer. Moreover, in the future, we may not be able to maintain insurance coverage at a reasonable cost or in sufficient amounts to protect us against losses, including if insurance coverage becomes increasingly expensive. If and when we obtain marketing approval for ZGN-1061, we intend to expand our insurance coverage to include the sale of commercial products; however, we may not be able to obtain this product liability insurance on commercially reasonable terms. Large judgments have been awarded in class action lawsuits based on drugs that had unanticipated side effects. The cost of any product liability litigation or other proceedings, even if resolved in our favor, could be substantial, particularly in light of the size of our business and financial resources. A product liability claim or series of claims brought against us could cause our stock price to decline and, if we are unsuccessful in defending such a claim or claims and the resulting judgments exceed our insurance coverage, our financial condition, business and prospects could be materially adversely affected.

We must maintain effective internal control over financial reporting, and if we are unable to do so, the accuracy and timeliness of our financial reporting may be adversely affected, which could have a material adverse effect on our business and stock price.

We currently are an "emerging growth company," as defined in the Jumpstart our Business Startups Act of 2012, or the JOBS Act, and we have taken advantage of certain exemptions from various reporting requirements that are applicable to other public companies that are not "emerging growth companies" including not being required to comply with the auditor attestation requirements of Section 404(b) of the Sarbanes-Oxley Act.

We must maintain effective internal control over financial reporting in order to accurately and timely report our results of operations and financial condition. In addition, as a public company, the Sarbanes-Oxley Act of 2002, or the Sarbanes-Oxley Act, requires, among other things, that we assess the effectiveness of our disclosure controls and procedures quarterly and the effectiveness of our internal control over financial reporting at the end of each fiscal year.

The rules governing the standards that must be met for our management to assess our internal control over financial reporting pursuant to Section 404 of the Sarbanes-Oxley Act are complex and require significant documentation, testing and possible remediation. These stringent standards require that our audit committee be advised and regularly updated on management's review of internal control over financial reporting. Our management may not be able to effectively and timely implement controls and

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procedures that adequately respond to the increased regulatory compliance and reporting requirements that are applicable to us as a public company. If we fail to staff our accounting and finance function adequately or maintain internal control over financial reporting adequate to meet the demands that will be placed upon us as a public company, including the requirements of the Sarbanes-Oxley Act, our business and reputation may be harmed and our stock price may decline. Furthermore, investor perceptions of us may be adversely affected, which could cause a decline in the market price of our common stock.

Our ability to use our net operating loss carryforwards and certain tax credit carryforwards may be subject to limitation.

Since our inception in 2005, we have not recorded any U.S. federal or state income tax benefits for the net losses we have incurred in each year or our earned tax credits, due to our uncertainty of realizing a benefit from those items. As of December 31, 2016, we had net operating loss carryforwards for federal and state income tax purposes of \$49.1 million and \$35.9 million, respectively, which begin to expire in 2026 and 2030, respectively. As of December 31, 2016, we did not record deferred tax assets of \$12.8 million (gross) that were attributable to stock option exercises which will be recorded as an increase in additional paid in capital once they are realized in accordance with accounting for stock-based compensation awards. These deductions are not reflected in the federal and state net operating loss carryforwards and the capitalized research and development expense deferred tax assets in the amounts of \$9.4 million, \$7.2 million, and \$3.4 million, respectively. As of December 31, 2016, we also had available tax credit carryforwards for federal and state income tax purposes of \$13.1 million and \$1.9 million, respectively, which begin to expire in 2026 and 2021, respectively. Under Section 382 of the Internal Revenue Code of 1986, as amended, or the Code, changes in our ownership may limit the amount of our net operating loss carryforwards and tax credit carryforwards that could be utilized annually to offset our future taxable income, if any. This limitation would generally apply in the event of a cumulative change in ownership of our company of more than 50% within a three-year period. Any such limitation may significantly reduce our ability to utilize our net operating loss carryforwards and tax credit carryforwards before they expire. Our follow-on public offering, initial public offering, or IPO, private placements and other transactions that have occurred since our inception, may trigger such an ownership change pursuant to Section 382. Any such limitation, whether as the result of our recent follow-on public offering, IPO, prior private placements, sales of our common stock by our existing stockholders or additional sales of our common stock by us, could have a material adverse effect on our results of operations in future years. We have not completed a study to assess whether an ownership change for purposes of Section 382 has occurred, or whether there have been multiple ownership changes since our inception, due to the significant costs and complexities associated with such study.

Unfavorable global economic conditions could adversely affect our business, financial condition or results of operations.

Our results of operations could be adversely affected by general conditions in the global economy and in the global financial markets. A severe or prolonged economic downturn could result in a variety of risks to our business, including, weakened demand for our product candidates and our ability to raise additional capital when needed on acceptable terms, if at all. A weak or declining economy could also strain our suppliers, possibly resulting in supply disruption, or cause our customers to delay making payments for our services. Any of the foregoing could harm our business and we cannot anticipate all of the ways in which the current economic climate and financial market conditions could adversely impact our business.

Our internal computer systems, or those of our third-party CROs or other contractors or consultants, may fail or suffer security breaches, which could result in a material disruption of our ZGN-1061 or other product candidate development programs.

Despite the implementation of security measures, our internal computer systems and those of our third-party CROs and other contractors and consultants are vulnerable to damage from computer viruses, unauthorized access, natural disasters, terrorism, war and telecommunication and electrical failures. While we have not experienced any such system failure or accident, if such an event were to occur and cause interruptions in our operations, it could result in a material disruption of our programs. For example, the loss of clinical trial data for ZGN-1061 could result in delays in our regulatory approval efforts and significantly increase our costs to recover or reproduce the data. To the extent that any disruption or security breach results in a loss of or damage to our data or applications or other data or applications relating to our technology or product candidates, or inappropriate disclosure of confidential or proprietary information, we could incur liabilities and the further development of ZGN-1061 could be delayed.

We may not be successful in our efforts to identify or discover additional product candidates.

The success of our business depends primarily upon our ability to identify, develop and commercialize products based on our MetAP2 platform. Although ZGN-1061 is currently in clinical development, our research programs may fail to identify other potential product candidates for clinical development for a number of reasons. Our research methodology may be unsuccessful in identifying potential product candidates or our potential product candidates may be shown to have harmful side effects or may have other characteristics that may make the products unmarketable or unlikely to receive marketing approval.

If any of these events occur, we may be forced to abandon our development efforts for a program or programs, which would have a material adverse effect on our business and could potentially cause us to cease operations. Research programs to identify new product candidates require substantial technical, financial and human resources. We may focus our efforts and resources on potential programs or product candidates that ultimately prove to be unsuccessful.

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We may seek to establish collaborations and, if we are not able to establish them on commercially reasonable terms, we may have to alter our development and commercialization plans or expand our internal efforts and growth.

Our drug development programs and the potential commercialization of our product candidates will require substantial additional cash to fund expenses. For some of our product candidates, we may decide to collaborate with pharmaceutical and biotechnology companies for the development and potential commercialization of those product candidates in some or all markets.

We face significant competition in seeking appropriate collaborators. Whether we reach a definitive agreement for a collaboration will depend, among other things, upon our assessment of the collaborator's resources and expertise, the terms and conditions of the proposed collaboration and the proposed collaborator's evaluation of a number of factors. Those factors may include the design or results of clinical trials, the likelihood of approval by the FDA or similar regulatory authorities outside the United States, the potential market for the applicable product candidate, the costs and complexities of manufacturing and delivering such product candidate to patients, the potential of competing products, the existence of uncertainty with respect to our ownership of technology, which can exist if there is a challenge to such ownership without regard to the merits of the challenge and industry and market conditions generally. The collaborator may also consider alternative product candidates or technologies for similar indications that may be available to collaborate on and whether such collaboration could be more attractive than the one with us for our product candidate. The terms of any collaboration or other arrangements that we may establish may not be favorable to us.

We may also be restricted under existing license agreements from entering into future agreements on certain terms with potential collaborators. Collaborations are complex and time-consuming to negotiate and document. In addition, there have been a significant number of recent business combinations among large pharmaceutical companies that have resulted in a reduced number of potential future collaborators.

We may not be able to negotiate collaborations on a timely basis, on acceptable terms, or at all. If we are unable or unwilling to do so, we may have to curtail the development of the product candidate for which we are seeking to collaborate, reduce or delay its development program or one or more of our other development programs, delay its potential commercialization in some or all markets or reduce the scope of any sales or marketing activities, or increase our expenditures and undertake development or commercialization activities at our own expense, including potentially increasing our infrastructure and investment outside the United States. If we elect to increase our expenditures to fund development or commercialization activities on our own, we may need to obtain additional capital, which may not be available to us on acceptable terms or at all. If we do not have sufficient funds, we may not be able to further develop our product candidates or bring them to market and generate product revenue. In addition such efforts may require diversion of a disproportionate amount of our attention away from other day-to-day activities, and require devotion of a substantial amount of our time to managing these expansion activities.

In addition, any future collaborations that we enter into may not be successful. The success of our collaboration arrangements will depend heavily on the efforts and activities of our collaborators. Collaborators generally have significant discretion in determining the efforts and resources that they will apply to these collaborations. Disagreements between parties to a collaboration arrangement regarding clinical development and commercialization matters can lead to delays in the development process or commercializing the applicable product candidate and, in some cases, termination of the collaboration arrangement. These disagreements can be difficult to resolve if neither of the parties has final decision-making authority. Collaborations with pharmaceutical or biotechnology companies and other third parties often are terminated or allowed to expire by the other party. Any such termination or expiration would adversely affect us financially and could harm our business reputation.

We may acquire businesses or products, or form strategic alliances, in the future, and we may not realize the benefits of such acquisitions or alliances.

We may acquire additional businesses or products, form strategic alliances or create joint ventures with third parties that we believe will complement or augment our existing business. If we acquire businesses with promising markets or technologies, we may not be able to realize the benefit of such transactions if we are unable to successfully integrate such businesses with our existing operations and company culture. We may encounter numerous difficulties in developing, manufacturing and marketing any new products resulting from a strategic alliance or acquisition that delay or prevent us from realizing their expected benefits or enhancing our business. We cannot assure you that, following any such transaction, we will achieve the expected synergies to justify the transaction.

Risks Related to Our Financial Position and Need for Capital

We have not generated any revenue from product sales. We have incurred significant operating losses since our inception, and anticipate that we will incur continued losses for the foreseeable future.

Biopharmaceutical product development is a highly speculative undertaking and involves a substantial degree of risk. Our operations to date have been limited primarily to organizing and staffing our company and conducting research and development activities for beloranib, ZGN-1061 and ZGN-839 and early research activities. We have never generated any revenue from product sales. We have not obtained regulatory approvals for any of our product candidates.

Since our inception and until recently, we focused substantially all of our efforts and financial resources on developing beloranib, which was in Phase 3 clinical development for our lead indication of the treatment of hyperphagia and obesity in patients with Prader-Willi Syndrome, or PWS, and Phase 2 clinical development for the treatment of obesity in patients with hypothalamic injury-associated obesity, or HIAO. In December 2015, the FDA put the beloranib IND on full clinical hold. Due to the uncertainties, costs and risks associated with the development of beloranib, in July 2016, we suspended further development of beloranib and directed our efforts and financial resources to developing ZGN-1061. In October 2016, we suspended our development of ZGN-839 in order to focus all of our resources to developing ZGN-1061 and the discovery of novel and highly differentiated MetAP2 inhibitors.

We have funded our operations to date through proceeds from sales of redeemable convertible preferred stock, convertible debt and proceeds from our IPO and follow-on public offering, and have incurred losses in each year since our inception. Our net losses were \$26.4 million for the six months ended June 30, 2017 and \$57.9 million for the year ended December 31, 2016. As of June 30, 2017, we had an accumulated deficit of \$263.9 million. Substantially all of our operating losses resulted from costs incurred in connection with our development programs for beloranib, ZGN-1061 and ZGN-839, early research activities, licensing milestone fees and from general and administrative costs associated with our operations. We expect to incur increasing levels of operating losses over the next several years and for the foreseeable future. Our prior losses, combined with expected future losses, have had and will continue to have an adverse effect on our stockholders' equity and working capital. We expect our research and development expenses will increase over time in connection with our clinical trials of ZGN-1061, and of any other product candidates we may choose to pursue. In addition, if and when we obtain marketing approval for ZGN-1061, we will incur significant sales, marketing and outsourced manufacturing expenses. We will continue to incur additional costs associated with operating as a public company. As a result, we expect to continue to incur significant operating losses that would increase over time for the foreseeable future. Because of the numerous risks and uncertainties associated with developing pharmaceutical products, we are unable to predict the extent of any future losses or when we will become profitable, if at all. Even if we do become profitable, we may not be able to sustain or increase our profitability on a quarterly or annual basis.

Our ability to become profitable depends upon our ability to generate revenue. To date, we have not generated any revenue from any of our product candidates, and we do not know when, or if, we will generate any revenue. We do not expect to generate significant revenue unless and until we obtain marketing approval of, and begin to sell, ZGN-1061. Our ability to generate revenue depends on a number of factors, including, but not limited to, our ability to:

- initiate and successfully complete clinical trials that meet their clinical endpoints;
- initiate and successfully complete all safety studies required to obtain U.S. and foreign marketing approval for ZGN-1061 in the indications we are pursuing;
- commercialize ZGN-1061, if developed and approved, by developing a sales force or entering into collaborations with third parties; and
- achieve market acceptance of ZGN-1061 in the medical community and with third-party payors.

Absent our entering into a collaboration or partnership agreement, we expect to incur significant sales and marketing costs when we prepare to commercialize ZGN-1061. Even if we initiate and successfully complete our clinical trials of ZGN-1061, and ZGN-1061 is approved for commercial sale, and despite expending these costs, ZGN-1061 may not be a commercially successful drug. We may not achieve profitability soon after generating product sales, if ever. If we are unable to generate sufficient product revenue, we will not become profitable and may be unable to continue operations without continued funding.

We will need to raise additional funding, which may not be available on acceptable terms, or at all. Failure to obtain this necessary capital when needed may force us to delay, limit or terminate our product development efforts or other operations.

Developing small molecule products is expensive, and we expect our research and development expenses to increase substantially in connection with our ongoing activities, particularly as we advance ZGN-1061 into later stage clinical trials. Depending on the status of regulatory approval or, if approved, commercialization of ZGN-1061 or any of our other product candidates, as well as the progress we make in selling ZGN-1061 or any of our other product candidates, we may require additional capital to fund operating needs thereafter. We may also need to raise additional funds sooner if we choose to pursue additional indications and/or geographies for ZGN-1061 or our other product candidates or otherwise expand more rapidly than we presently anticipate.

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As of June 30, 2017, our cash, cash equivalents and marketable securities were \$106.0 million. We expect that our cash, cash equivalents and marketable securities will be sufficient to fund our current operations for a period of at least one year from the issuance date of this Quarterly Report. However, our operating plan may change as a result of many factors currently unknown to us, and we may need to seek additional funds sooner than planned, through public or private equity or debt financings, government or other third-party funding, marketing and distribution arrangements and other collaborations, strategic alliances and licensing arrangements or a combination of these approaches. In any event, we will require additional capital to obtain regulatory approval for, and to commercialize, our product candidates. Raising funds in the current economic environment may present additional challenges. Even if we believe we have sufficient funds for our current or future operating plans, we may seek additional capital if market conditions are favorable or if we have specific strategic considerations.

Any additional fundraising efforts may divert our management from their day-to-day activities, which may adversely affect our ability to develop and commercialize our product candidates. In addition, we cannot guarantee that future financing will be available in sufficient amounts or on terms acceptable to us, if at all. Moreover, the terms of any financing may adversely affect the holdings or the rights of our stockholders and the issuance of additional securities, whether equity or debt, by us, or the possibility of such issuance, may cause the market price of our shares to decline. The sale of additional equity or convertible securities would dilute all of our stockholders. The incurrence of indebtedness would result in increased fixed payment obligations and we may be required to agree to certain restrictive covenants, such as limitations on our ability to incur additional debt, limitations on our ability to acquire, sell or license intellectual property rights and other operating restrictions that could adversely impact our ability to conduct our business. We could also be required to seek funds through arrangements with collaborative partners or otherwise at an earlier stage than otherwise would be desirable and we may be required to relinquish rights to some of our technologies or product candidate or otherwise agree to terms unfavorable to us, any of which may have a material adverse effect on our business, operating results and prospects.

If we are unable to obtain funding on a timely basis, we may be required to significantly curtail, delay or discontinue one or more of our research or development programs or the commercialization of any product candidate or be unable to expand our operations or otherwise capitalize on our business opportunities, as desired, which could materially affect our business, financial condition and results of operations.

Raising additional capital may cause dilution to our existing stockholders, restrict our operations or require us to relinquish rights.

We may seek additional capital through a combination of private and public equity offerings, debt financings, collaborations and strategic and licensing arrangements. To the extent that we raise additional capital through the sale of common stock or securities convertible or exchangeable into common stock, a stockholder's ownership interest in our company will be diluted. In addition, the terms of any such securities may include liquidation or other preferences that materially adversely affect the rights of our stockholders. Debt financing, if available, would increase our fixed payment obligations and may involve agreements that include covenants limiting or restricting our ability to take specific actions, such as incurring additional debt, making capital expenditures or declaring dividends. If we raise additional funds through collaboration, strategic partnerships and licensing arrangements with third parties, we may have to relinquish valuable rights to ZGN-1061 or other product candidates, our intellectual property, future revenue streams or grant licenses on terms that are not favorable to us.

Risks Related to Our Common Stock

We expect that our stock price may fluctuate significantly.

The market price of shares of our common stock, similar to the market price of shares of common stock of other biopharmaceutical companies, is subject to wide fluctuations. From January 1, 2017 to June 30, 2017 the daily closing price of our common stock on the NASDAQ Global Market ranged from a high of \$5.08 to a low of \$3.24 and will continue to be subject to wide fluctuations in response to many risk factors listed in this section, and others beyond our control, including:

- plans for, progress of, or results from pre-clinical studies and clinical trials of ZGN-1061 and/or other product candidates;
- the failure of the FDA to accept our IND for ZGN-1061;
- the failure of the FDA or the EMA to approve ZGN-1061;
- our ability to establish an adequate safety margin and profile for ZGN-1061, including risk of serious thromboembolic events;
- announcements of new products, technologies, commercial relationships, acquisitions or other events by us or our competitors;
- the success or failure of other type 2 diabetes or weight loss therapies;

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- regulatory or legal developments in the United States and other countries;
- failure of ZGN-1061, if successfully developed and approved, to achieve commercial success;
- fluctuations in stock market prices and trading volumes of similar companies;
- general market conditions and overall fluctuations in U.S. equity markets;
- variations in our quarterly operating results;
- changes in our financial guidance or securities analysts' estimates of our financial performance;
- changes in accounting principles;
- our ability to raise additional capital and the terms on which we can raise it;
- sales of large blocks of our common stock, including sales by our executive officers, directors and significant stockholders;
- additions or departures of key personnel;
- discussion of us or our stock price by the press and by online investor communities; and
- other risks and uncertainties described in these risk factors.

These and other market and industry factors may cause the market price and demand for our common stock to fluctuate substantially, regardless of our actual operating performance, which may limit or prevent investors from readily selling their shares of common stock and may otherwise negatively affect the liquidity of our common stock. In addition, the stock market in general, and NASDAQ listed and biopharmaceutical companies in particular, have experienced extreme price and volume fluctuations that have often been unrelated or disproportionate to the operating performance of these companies. In the past, when the market price of a stock has been volatile, holders of that stock have instituted securities class action litigation against the company that issued the stock.

On October 21, 2015, a purported stockholder of the Company filed a putative class action lawsuit in the U.S. District Court for the District of Massachusetts, against the Company and Thomas E. Hughes, captioned *Aviad Bessler v. Zafgen, Inc. and Thomas E. Hughes*, No. 1:15-cv-13618. An amended complaint was filed on February 22, 2016. The amended complaint alleges violations of Sections 10(b) and 20(a) of the Securities Exchange Act of 1934 and SEC Rule 10b-5 based on allegedly false and misleading statements and omissions regarding our clinical trials for beloranib. On August 9, 2016, the District Court granted the motion to dismiss and dismissed the amended complaint with prejudice. On August 12, 2016, plaintiffs filed a notice of appeal to the First Circuit Court of Appeals and, on April 7, 2017 the dismissal with prejudice was affirmed.

Our executive officers, directors, and principal stockholders exercise significant control over our company.

As of July 31, 2017, the existing holdings of our executive officers, directors, principal stockholders and their affiliates, including investment funds affiliated with Atlas Ventures, or Atlas, and entities affiliated with Fidelity Investment (FMR LLC), or Fidelity, represent beneficial ownership, in the aggregate, of approximately 36.8% of our common stock. As a result, these stockholders, if they act together, are able to influence our management and affairs and control the outcome of matters submitted to our stockholders for approval, including the election of directors and any sale, merger, consolidation, or sale of all or substantially all of our assets. The concentration of voting power among these stockholders may have an adverse effect on the price of our common stock. In addition, this concentration of ownership might adversely affect the market price of our common stock by:

- delaying, deferring or preventing a change of control of us;
- impeding a merger, consolidation, takeover or other business combination involving us; or
- discouraging a potential acquirer from making a tender offer or otherwise attempting to obtain control of us.

Future sales of our common stock may cause our stock price to decline.

Sales of a substantial number of shares of our common stock in the public market or the perception that these sales might occur could significantly reduce the market price of our common stock and impair our ability to raise adequate capital through the sale of additional equity securities.

We have broad discretion in how we use the proceeds of our follow-on public offering. We may not use these proceeds effectively, which could affect our results of operations and cause our stock price to decline.

We have considerable discretion in the application of the net proceeds of our follow-on public offering. We intend to use the net proceeds to advance the clinical development of ZGN-1061 and to fund new and ongoing research and development activities,

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working capital and other general corporate purposes, which may include funding for the hiring of personnel, capital expenditures, early commercialization activities, the costs of operating as a public company and potential business development activities. As a result, investors will be relying upon management's judgment with only limited information about our specific intentions for the use of the balance of the net proceeds. We may use the net proceeds for purposes that do not yield a significant return or any return at all for our stockholders. In addition, pending their use, we may invest the net proceeds in a manner that does not produce income or that loses value.

We may be at an increased risk of securities class action litigation.

Historically, securities class action litigation has often been brought against a company following a decline in the market price of its securities. This risk is especially relevant for us because biotechnology and pharmaceutical companies have experienced significant stock price volatility in recent years.

On October 21, 2015, a purported stockholder of the Company filed a putative class action lawsuit in the U.S. District Court for the District of Massachusetts, against the Company and Thomas E. Hughes, captioned *Aviad Bessler v. Zafgen, Inc. and Thomas E. Hughes*, No. 1:15-cv-13618. An amended complaint was filed on February 22, 2016. The amended complaint alleges violations of Sections 10(b) and 20(a) of the Securities Exchange Act of 1934 and SEC Rule 10b-5 based on allegedly false and misleading statements and omissions regarding our clinical trials for belorانب. On August 9, 2016, the District Court granted the motion to dismiss and dismissed the amended complaint with prejudice. On August 12, 2016, plaintiffs filed a notice of appeal to the First Circuit Court of Appeals and, on April 7, 2017 the dismissal with prejudice was affirmed.

We are an "emerging growth company" and have availed ourselves of reduced disclosure requirements applicable to emerging growth companies, which could make our common stock less attractive to investors.

We are an "emerging growth company," as defined in the JOBS Act, and we have taken advantage of certain exemptions from various reporting requirements that are applicable to other public companies that are not "emerging growth companies" including not being required to comply with the auditor attestation requirements of Section 404(b) of the Sarbanes-Oxley Act, reduced disclosure obligations regarding executive compensation in our periodic reports and proxy statements, and exemptions from the requirements of holding a nonbinding advisory vote on executive compensation and shareholder approval of any golden parachute payments not previously approved. In addition, Section 107 of the JOBS Act also provides that an emerging growth company can take advantage of the extended transition period provided in Section 7(a)(2)(B) of the Securities Act, for complying with new or revised accounting standards. In other words, an emerging growth company can delay the adoption of certain accounting standards until those standards would otherwise apply to private companies. However, we are electing not to take advantage of such extended transition period, and as a result we will comply with new or revised accounting standards on the relevant dates on which adoption of such standards is required for non-emerging growth companies. Section 107 of the JOBS Act provides that our decision to not take advantage of the extended transition period for complying with new or revised accounting standards is irrevocable. We cannot predict if investors will find our common stock less attractive because we may rely on any of the exemptions available under the JOBS Act. If some investors find our common stock less attractive as a result, there may be a less active trading market for our common stock and our stock price may be more volatile. We may take advantage of these reporting exemptions until we are no longer an emerging growth company. We will remain an emerging growth company until the earliest of (i) the last day of the fiscal year in which we have total annual gross revenue of \$1.0 billion or more; (ii) December 31, 2019; (iii) the date on which we have issued more than \$1.0 billion in nonconvertible debt during the previous three years; and (iv) the date on which we are deemed to be a large accelerated filer under the rules of the SEC.

We have never paid dividends on our common stock and we do not anticipate paying any dividends in the foreseeable future. Consequently, any gains from an investment in our common stock will likely depend on whether the price of our common stock increases.

We have not paid dividends on any of our common stock to date and we currently intend to retain all of our future earnings, if any, to fund the development and growth of our business. As a result, capital appreciation, if any, of our common stock will be the sole source of gains for our common stockholders for the foreseeable future. Consequently, in the foreseeable future, our common stockholders will likely only experience a gain from their investment in our common stock if the price of our common stock increases.

If equity research analysts do not continue to publish research or reports about our business or if they issue unfavorable commentary or downgrade our common stock, the price of our common stock could decline.

The trading market for our common stock relies in part on the research and reports that equity research analysts publish about us and our business. We do not control these analysts. The price of our common stock could decline if one or more equity analysts downgrade our common stock or if analysts issue other unfavorable commentary or cease publishing reports about us or our business.

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Anti-takeover provisions contained in our amended and restated certificate of incorporation and amended and restated bylaws, as well as provisions of Delaware law, could impair a takeover attempt.

Our amended and restated certificate of incorporation, amended and restated bylaws and Delaware law contain provisions which could have the effect of rendering more difficult, delaying or preventing an acquisition deemed undesirable by our board of directors. Our corporate governance documents include provisions:

- creating a classified board of directors whose members serve staggered three-year terms;
- authorizing “blank check” preferred stock, which could be issued by our board of directors without stockholder approval and may contain voting, liquidation, dividend, and other rights superior to our common stock;
- limiting the liability of, and providing indemnification to, our directors and officers;
- limiting the ability of our stockholders to call and bring business before special meetings;
- requiring advance notice of stockholder proposals for business to be conducted at meetings of our stockholders and for nominations of candidates for election to our board of directors;
- controlling the procedures for the conduct and scheduling of board of directors and stockholder meetings; and
- providing our board of directors with the express power to postpone previously scheduled annual meetings and to cancel previously scheduled special meetings.

These provisions, alone or together, could delay or prevent hostile takeovers and changes in control or changes in our management.

As a Delaware corporation, we are also subject to provisions of Delaware law, including Section 203 of the Delaware General Corporation law, which prevents some stockholders holding more than 15% of our outstanding common stock from engaging in certain business combinations without approval of the holders of substantially all of our outstanding common stock.

Any provision of our amended and restated certificate of incorporation, amended and restated bylaws or Delaware law that has the effect of delaying or deterring a change in control could limit the opportunity for our stockholders to receive a premium for their shares of our common stock, and could also affect the price that some investors are willing to pay for our common stock.

Item 6. Exhibits

The exhibits filed as part of this Quarterly Report are set forth on the Exhibit Index, which is incorporated herein by reference.

SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) 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.

ZAFGEN, INC.

Date: August 9, 2017

By: /s/ Thomas E. Hughes, Ph.D.
Thomas E. Hughes, Ph.D.
President and Chief Executive Officer
(Principal Executive Officer)

Date: August 9, 2017

By: /s/ Patricia L. Allen
Patricia L. Allen
Chief Financial Officer
(Principal Financial and Accounting Officer)

EXHIBIT INDEX

<u>Exhibit No.</u>	<u>Description</u>
31.1*	Certification of Principal Executive Officer pursuant to 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 Principal Financial Officer pursuant to 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 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
101.INS*	XBRL Instance Document.
101.SCH*	XBRL Taxonomy Extension Schema Document.
101.CAL*	XBRL Taxonomy Extension Calculation Document.
101.DEF*	XBRL Taxonomy Extension Definition Linkbase Document.
101.LAB*	XBRL Taxonomy Extension Labels Linkbase Document.
101.PRE*	XBRL Taxonomy Extension Presentation Link Document.

* Filed herewith.

** Furnished herewith.

Certification

I, Thomas E. Hughes, certify that:

1. I have reviewed this quarterly report on Form 10-Q for the period ended June 30, 2017 of Zafgen, 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: August 9, 2017

/s/ Thomas E. Hughes

Thomas E. Hughes
President and Chief Executive Officer
(Principal Executive Officer)

Certification

I, Patricia Allen, certify that:

1. I have reviewed this quarterly report on Form 10-Q for the period ended June 30, 2017 of Zafgen, 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: August 9, 2017

/s/ Patricia Allen

Patricia Allen
Chief Financial Officer
(Principal Financial and Accounting Officer)

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

In connection with the Quarterly Report on Form 10-Q of Zafgen, Inc. (the "Company") for the period ended June 30, 2017, as filed with the Securities and Exchange Commission on the date hereof (the "Report"), each of the undersigned officers hereby certify, pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, 18 U.S.C. Section 1350, that to his or her knowledge:

- 1) the Report which this statement accompanies fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934, as amended; and
- 2) the information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

Dated: August 9, 2017

/s/ Thomas E. Hughes

Thomas E. Hughes
President and Chief Executive Officer
(Principal Executive Officer)

Dated: August 9, 2017

/s/ Patricia Allen

Patricia Allen
Chief Financial Officer
(Principal Financial and Accounting Officer)