In these financially straitened times in which the IPO window is nailed shut there appears to be an increasing trend for reverse mergers, whereby a distressed public company, sometimes with a decent cash pile, is taken over by a private entity seeking a public listing, cash, or both.

One company which has recently completed one of these reverse mergers is Transcept Pharmaceuticals and speaking to *EP Vantage*, Transcept’s chief executive officer, Glenn Oclassen, was unequivocal that the primary motive for reversing into Novacea, which had a significant cash pile of $90m, was for the money, way ahead of any aspirations to become a public company.

**No longer a badge of shame**

A few years ago, before the credit crunch and the closing of the IPO window, a metaphorical ‘badge of shame’ would hang around the neck of companies conducting a reverse merger in order to gain a public listing, particularly as the cash levels involved were often fairly low.

However, this strategic move, particularly when a private company can access decent cash reserves instead of having to tap existing investors for additional funding, is becoming increasingly acceptable with the result that there has been an uptick in the trend for reverse mergers (Affitech continues reverse merger trend, March 4, 2009).

Pointing to the fact Transcept emerged victorious from a long and exhaustive selection process in which Novacea had around 90 applicants to conduct a reverse merger, no doubt attracted by the $90m on offer, Mr Oclassen says, “the big difference was the amount of money, at $30m or $40m it would not have been worth it; this allows us to get this product off the ground, with or without a partner.”

**Sleep maintenance**

The product Mr Oclassen refers to is Transcept’s lead pipeline candidate, Intermezzo, a low-dose but rapidly acting formulation of zolpidem to treat insomnia.

Having identified one of the main problems for insomnia patients taking zolpidem, developed by Sanofi-Aventis and sold as Ambien, is not in falling asleep initially but waking in the middle of the night, Intermezzo is designed to be taken only when the patient wakes up and with its rapid absorption technology a dose of the drug can send a patient to sleep within 15 minutes.

Intermezzo was filed with the FDA in September last year and has been given a PDUFA action date of July 30.

In such a notoriously competitive market, which traditionally requires significant promotion by both a large sales force and DTC advertising, the company clearly faces significant challenges in persuading both the FDA and physicians that the differentiation of Intermezzo from Ambien is a significant advance in treatment options for insomnia patients.

**Active discussions**

With 70% of the insomnia market in the US within the primary care setting, Transcept is actively seeking a partner for this portion of the market and Mr Oclassen believes, “we need somebody with 800 – 2000 reps in the US and a gap in their product portfolio and an interest in the insomnia market”.

With the timing, size and scope of a deal hard to predict, and it seems likely a partner will wait for FDA approval before signing on the dotted line. Mr Oclassen is hopeful that the company can hire their own sales force of around 120 reps and target the remaining 30% of the market of around 17,000 doctors and psychiatrists.
Although getting a partner on board would be the ideal scenario, the cash acquired through the Novacea merger has clearly put Transcept in a much stronger position and can at least get the ball rolling with commercialisation of Intermezzo. Outside the US, Transcept is also looking for a partner to cover all regulatory and commercial development of the drug.

Regarding the market opportunity, Transcept has conducted research which suggests Intermezzo could be a $600m per year drug, a significant product for most pharmaceutical companies let alone a relatively small company such as Transcept.

Advice for reverse mergers

Returning to the reverse merger theme, Mr Oclassen has some fairly forthright views and advice for any other company considering such a move.

Pointing to the fact the Novacea merger was a relatively clean transaction, with no products or employees to try and integrate or eliminate, Mr Oclassen believes this is one of the most important features in making these deals as smooth as possible. “The fear on the part of surviving company is being wound up with a lot of stuff to deal with, which diverts attention away from the reason you’re seeking the cash in the first place”, says Mr Oclassen.

In many respects the fundamental negotiations over price and gaining shareholder approval is the most straightforward part of these deals.

Mr Oclassen also admits that the instant transition from private to public company can be, “wrenching…as it eats up money and gigantic amounts of management time, even more precious than cash”. Mr Oclassen goes on to say: “you devote so much of your day to something that has nothing to do with products, technology, customers or the FDA, but just to do with the SEC and auditors and other aspects”.

The warning to other companies seeking a similar strategic move is apparent, although when presented with an opportunity to access $90m which could prove transformational for a company like Transcept, the challenges are clearly worth overcoming.