

Founder hopes Peloton Therapeutics is a catalyst for UTSW's BioCenter

By GARY JACOBSON

Staff Writer

gjacobson@dallasnews.com

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The timing could not have been worse for BioCenter, UT Southwestern Medical Center's biotech park on Inwood Road.

Announced in fall 2008 amid the global economic meltdown, the BioCenter was touted as a place where companies could germinate in close proximity to the medical center's world-class investigators. BioCenter would help commercialize UTSW-developed technologies and attract existing biotech firms to North Texas.

Four buildings, with a total of about a half-million square feet of space, were planned. The first of these, costing about \$33 million so far, opened in 2009.

Two years later, that first building — the only one constructed to date — remains largely vacant, home to four small companies and some UTSW staffers.

But there are signs that BioCenter finally is starting to fulfill some of its promise.

Peloton Therapeutics Inc., a cancer drug company based on discoveries by UTSW researchers, has taken at least 12,000 square feet of space, said Ray Wheatley, UTSW's director for technology transfer.

And three other startups could be on the verge of taking space, Wheatley said during a recent tour. "We'd already be full if it weren't for the economy," he said.

Translating research into something to sell is a long, extremely high-risk process, especially in biotech, where it can take a decade or more to develop a product.

And even the greatest of ideas can have little or no commercial value.

The patent connected to UTSW faculty member Bruce Beutler's recent Nobel Prize in medicine, for example, probably will never earn licensing income, Wheatley said.

All-star cast

Peloton could be different. It has an all-star cast of researchers, advisers and investors with successful pedigrees and powerful connections.

Founder and UTSW faculty member Steve McKnight said the fact that UTSW discoveries have not yet spilled over into the creation of a thriving North Texas biotech industry "has been a real disappointment."

He hopes Peloton can be a catalyst.

"Twenty years from now, there's going to be a new Amgen somewhere, or a new Genentech," McKnight said during an interview in his office at UTSW. "If we don't try, it won't be here."

Peloton, which hopes to have its BioCenter labs running by spring, has received an \$11 million grant from the Cancer Prevention and Research Institute of Texas and a total of \$18 million in early financing from two investment firms and Dallas philanthropist Peter O'Donnell Jr.

Last year, the *Austin American-Statesman* called O'Donnell the UT System's "best-known anonymous donor" and said he had contributed more than \$135 million to the university over the years.

With Peloton, O'Donnell is an investor, not a donor.

McKnight, professor and chairman of the biochemistry department, and David Goeddel, managing partner at the Column Group, a California venture firm that led the Peloton investment, have a strong track record.

In 1991, they helped found a California biotech company called Tularik Inc., which Amgen acquired in a 2004 deal that valued Tularik at nearly \$2 billion. Earlier in his career, Goeddel was the first scientist hired by Genentech.

Peloton's board of directors includes UTSW professor and Nobel Prize winner Michael Brown, who is also on the board of the drug giant Pfizer Inc., as well as Brett Ringle and John Creecy, formerly affiliated with Hunt Petroleum Corp., which was acquired by XTO Energy in 2008.

Hunt Petroleum had been owned by trusts established by oil legend H.L. Hunt. Ringle and Creecy are now with Remeditex Ventures, which is backed by Hunt heir Lyda Hill and invests in early-stage biomedical companies.

Also, Brown and his Nobel Prize-winning research partner at UTSW, Joseph Goldstein, are scientific partners in the Column Group. And Dennis Stone, Wheatley's former boss at UTSW, is chief scientific officer at Remeditex.

McKnight acknowledges that the odds are stacked against Peloton, as they are against any biotech startup, but says the company is three years closer to clinical trials on humans than Tularik was when it was founded.

"I think we have a real good shot on goal," he said of Peloton.

Lofty goal

UTSW earned a record \$15.5 million in technology transfer income — derived from commercializing the medical center's inventions and discoveries — in fiscal 2011, which ended Aug. 31. That included nearly \$6.5 million from the sale of equity and stock transactions, a clue to a growing strategy.

"We want to get more involved in startups," Wheatley said.

Since the mid-1980s, Wheatley said, UTSW has helped start about 25 companies. Slightly more than half are still in business.

UTSW has earned a total of \$147.6 million in technology transfer income since 1984, the vast majority of it from about 600 licensing agreements, according to statistics provided by the school.

Ten years from now, Wheatley predicted, UTSW-related inventions — from disease-fighting drugs to devices that seal off brain aneurysms — will generate significantly more from royalties and related income than they do now, perhaps even "hundreds of millions of dollars a year."

Unrealistic?

UTSW certainly has some work to do to get there.

Only two U.S. hospitals and research facilities exceeded \$100 million in licensing income in 2010, according to a survey by the Association of University Technology Managers. City of Hope near Los Angeles received \$202 million and Sloan-Kettering Institute in New York received \$139 million.

Four universities or university systems also exceeded that level, led by Northwestern with \$180 million. The UT system reported \$38.3 million in license-related income.

Another UTSW-related company with strong potential is Reata Pharmaceuticals, founded in 2002. The company's initial focus was cancer, but attention has shifted to chronic kidney disease.

Last year, Reata, based in Irving, signed a deal with Abbott Laboratories potentially valued at more than \$800 million. Last quarter, Reata received \$300 million from venture capital firms, the most nationally during that span.

"The FDA loves Reata," Wheatley said, referring to the federal agency that approves new drugs.

High risk, rewards

While commercializing biotech discoveries is high-risk, one big success can dwarf everything else.

Steve VanNurden, chairman of Mayo Clinic Ventures in Minnesota, estimates that the clinic would have earned "hundreds of millions of dollars" over the years if it had exploited the rights to cortisone instead of giving them away (to Merck), a common practice at the time. Two Mayo Clinic scientists isolated cortisone and identified its therapeutic power in the 1930s and 1940s and shared a Nobel Prize for their work in 1950.

"Sooner or later, we'll get another one," VanNurden said.

Since 1998, he said, Mayo Clinic has started about 45 companies. The institution generally earns between \$22 million and \$25 million a year in licensing-related income from Mayo inventions.

Universities and research institutes started to ramp up their patent and licensing activity after the passage of the Bayh-Dole Act in 1980, which gave them control of intellectual property developed from government-funded research and required them to promote and attempt to commercialize their inventions.

At UTSW, half of licensing income, after recovery of patent-related expenses, goes to the inventor or inventors, a quarter to the inventor's lab and a quarter to UTSW.

In UTSW startup companies, Wheatley said, ownership equity stakes vary widely. "We have to handcraft every deal," he said.

He declined to give details for specific companies but said UTSW usually takes an equity share of 5 percent to 30 percent, depending upon the amount of UTSW technology involved.

UTSW investigators can't be officers or board members of companies that use their inventions, but they can be on scientific advisory boards and be founders. Their ownership stake cannot exceed UTSW's.

Investors, company managers and employees receive the balance of ownership.

"If you want three Nobel Prize winners on your board, you're going to have to set aside a big chunk of equity to get them," Wheatley said.

Investors own the majority of Peloton, McKnight said. A good piece of equity is reserved for employees, who, along with the founder, will own about 20 percent of the enterprise, he said.

As a company takes on more outside investment, original stakeholders can see considerable dilution. But if the company gets big enough, even a small share can be valuable.

McKnight, for example, left Tularik to join the UTSW faculty in 1996, though he remained on Tularik's board. At the time of the deal with Amgen, McKnight's remaining Tularik stock — less than 1 percent of the shares outstanding — converted into about \$12 million worth of Amgen stock, according to his SEC filings.

That's for a company that never had a product that generated revenue and had an accumulated deficit of more than \$400 million.

While money is an important incentive, McKnight said, the goal of everyone involved in Peloton is to build a great company, not make a quick buck.

"The best legacy you could leave behind is a company like Amgen or Genentech," he said. "If you have an exit strategy at the start, you've already decided you're not going to be great."

POTENTIAL CONFLICTS AT ISSUE: Peloton founder says situation requires care

Steve McKnight, chairman of the biochemistry department at UT Southwestern Medical Center, admits there is a lot of potential for conflict of interest with his new cancer drug company, Peloton Therapeutics.

"Starting with me," he said.

In his 15 years at the school, he said, he has hired many people and currently supervises many UTSW researchers whose discoveries could be commercialized.

"I have to be really, really careful that they don't put their technology into this company just because I'm their boss," McKnight said. Individual researchers must decide what's best for them.

Another concern is that one of the early Peloton investors is Dallas philanthropist Peter O'Donnell Jr., a major donor to the UT System and UTSW.

"We're walking on thin ice because there is potential to foul up what has been a wonderful relationship, which is something we do not want to do," McKnight said.

"We have to be ultra-, ultra-careful."

O'Donnell has invested about \$3 million in Peloton, McKnight said.

A three-person oversight committee has been appointed to help manage potential conflicts, McKnight said. And UTSW investigators involved with the company who reported to him now report to the dean.

Asked about donors becoming investors, UTSW said in a statement: "We have an obligation as an institution to optimize the commercialization of our scientific discoveries to the ultimate benefit of patients, but we also have a responsibility to ensure that we minimize and manage any potential conflicts of interest whether at the individual or institutional level."