UNITED THERAPEUTICS CORP
Form 10-Q
October 29, 2009

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UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

FORM 10-Q

(Mark One)

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

For the quarterly period ended September 30, 2009

OR

o 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 0-26301

United Therapeutics Corporation

(Exact Name of Registrant as Specified in Its Charter)

Delaware (State or Other Jurisdiction of Incorporation or Organization)	**52-1984749** (I.R.S. Employer Identification No.)
1110 Spring Street, Silver Spring, MD (Address of Principal Executive Offices)	**20910** (Zip Code)

(301) 608-9292

(Registrant s Telephone Number, Including Area Code)

(Former Name, Former Address and Former Fiscal Year, If Changed Since Last Report)

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 x No o

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 o No o

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

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

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

The number of shares outstanding of the issuer s common stock, par value $.01 per share, as of October 25, 2009 was 53,839,788.

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PART I. FINANCIAL INFORMATION

Item 1. Consolidated Financial Statements

UNITED THERAPEUTICS CORPORATION

CONSOLIDATED BALANCE SHEETS

(In thousands, except per share data)

	September 30, 2009 (Unaudited)	December 31, 2008 (As Adjusted)(1)
Assets		
Current assets:		
Cash and cash equivalents	$ 134,502	$ 129,452
Marketable investments	100,994	106,596
Accounts receivable, net of allowance of $60 and none at September 30, 2009 and December 31, 2008	45,645	28,311
Other receivable	3,323	2,289
Prepaid expenses	8,137	11,600
Inventories, net	24,814	14,372
Deferred tax assets	4,736	4,827
Total current assets	322,151	297,447
Marketable investments	129,493	100,270
Marketable investments and cash restricted	39,807	45,755
Goodwill and other intangibles, net	19,416	7,838
Property, plant, and equipment, net	299,260	222,717
Deferred tax assets	178,007	178,842
Other assets ($7,184 and $7,685 at September 30, 2009 and December 31, 2008, respectively, measured under the fair value option)	16,593	21,665
Total assets	$ 1,004,727	$ 874,534
Liabilities and Stockholders Equity		
Current liabilities:		
Accounts payable	$ 17,688	$ 20,334
Accrued expenses	27,000	20,853
Other current liabilities	39,814	16,506
Convertible senior notes	216,525	
Total current liabilities	301,027	57,693
Convertible senior notes		205,691
Lease obligation	30,057	29,261
Other liabilities	23,204	15,673
Total liabilities	354,288	308,318
Commitments and contingencies:		
Common stock subject to repurchase	10,882	10,882
Stockholders equity:		
Preferred stock, par value $.01, 10,000,000 shares authorized, no shares issued		
Series A junior participating preferred stock, par value $.01, 100,000 authorized, no shares issued		
Common stock, par value $.01, 100,000,000 shares authorized, 56,262,808 and 55,324,302 shares issued at September 30, 2009, and December 31, 2008, respectively, and 53,801,218 and 52,862,712 outstanding at September 30, 2009, and December 31, 2008, respectively	282	276
Additional paid-in capital	781,435	722,293
Accumulated other comprehensive loss	(3,630)	(5,913)
Treasury stock at cost, 2,461,590 shares at September 30, 2009 and December 31, 2008	(67,395)	(67,395)
Accumulated deficit	(71,135)	(93,927)
Total stockholders equity	639,557	555,334
Total liabilities and stockholders equity	$ 1,004,727	$ 874,534

See accompanying notes to consolidated financial statements.

(1) Adjusted retrospectively for the adoption of guidance pertaining to convertible debt instruments that may be settled in cash upon conversion included in Financial Accounting Standards Board (FASB) Accounting Standards Codification (ASC) 470-20, ***Debt with Conversion Options and Other Options*** **(FASB ASC 470-20). Prior to the introduction of FASB ASC 470-20, this guidance was formerly provided under FASB Staff Position No. APB 14-1,** ***Accounting for Convertible Debt Instruments That May Be Settled in Cash Upon Conversion (Including Partial Cash Settlement)*** **(FSP APB 14-1). See Note 9** ***Debt Adoption of FASB ASC 470-20 (Formerly FSP APB 14-1).***

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UNITED THERAPEUTICS CORPORATION

CONSOLIDATED STATEMENTS OF OPERATIONS

(In thousands, except per share data)

	Three Months Ended September 30, 2009	Three Months Ended September 30, 2008 As Adjusted (1)	Nine Months Ended September 30, 2009	Nine Months Ended September 30, 2008 As Adjusted (1)
	(Unaudited)		(Unaudited)	
Revenues:				
Net product sales	$ 94,058	$ 72,149	$ 251,925	$ 196,799
Service sales	2,876	2,324	8,054	6,944
License fees	281	559	946	1,892
Total revenues	97,215	75,032	260,925	205,635
Operating expenses:				
Research and development	31,551	19,213	81,156	59,430
Selling, general and administrative	41,172	30,018	119,761	72,442
Cost of product sales	11,576	6,950	28,657	19,689
Cost of service sales	1,179	791	3,168	2,270
Total operating expenses	85,478	56,972	232,742	153,831
Income from operations	11,737	18,060	28,183	51,804
Other (expense) income:				
Interest income	1,085	2,311	4,141	8,723
Interest expense	(3,331)	(2,624)	(9,216)	(8,909)
Equity (loss) income in affiliate	(42)	1	(99)	(155)
Other, net	(403)	(493)	491	32
Total other (expense) income, net	(2,691)	(805)	(4,683)	(309)
Income before income tax	9,046	17,255	23,500	51,495
Income tax benefit (expense)	2,891	(6,285)	(708)	(18,752)
Net income	$ 11,937	$ 10,970	$ 22,792	$ 32,743
Net income per common share:				
Basic	$ 0.22	$ 0.24	$ 0.43	$ 0.72
Diluted	$ 0.21	$ 0.22	$ 0.41	$ 0.66
Weighted average number of common shares outstanding:				
Basic	53,455	45,868	53,108	45,248
Diluted	57,653	50,964	55,297	49,414

See accompanying notes to consolidated financial statements.

(1) Adjusted for the retrospective adoption of guidance set forth under FASB ASC 470-20, formerly FSP APB 14-1. See Note 9 *Debt Adoption of FASB ASC 470-20 (Formerly FSP APB 14-1).*

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UNITED THERAPEUTICS CORPORATION

CONSOLIDATED STATEMENTS OF CASH FLOWS

(In thousands)

	Nine Months Ended September 30, 2009	Nine Months Ended September 30, 2008 (as adjusted)(1)
	(Unaudited)	
Cash flows from operating activities:		
Net income	$ 22,792	$ 32,743
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	6,673	3,146
Provision for bad debt and inventory obsolescence	985	499
Deferred tax expense	708	18,752
Share-based compensation	73,712	27,158
Amortization of debt discount and debt issue costs	11,685	10,907
Amortization of discount or premium on investments	1,132	(993)
Equity loss in affiliate and other	(3,248)	(1,724)
Excess tax benefits from share-based compensation	(2,710)	(19,105)
Changes in operating assets and liabilities:		
Accounts receivable	(17,345)	(7,541)
Inventories	(8,965)	(1,007)
Prepaid expenses	3,478	(1,052)
Other assets	(5,889)	(8,540)
Accounts payable	(2,723)	14,113
Accrued expenses	6,182	3,691
Other liabilities	(12,826)	6,695
Net cash provided by operating activities	73,641	77,742
Cash flows from investing activities:		
Purchases of property, plant and equipment	(73,893)	(87,855)
Acquisition of Tyvaso Inhalation System business	(3,378)	
Purchases of held-to-maturity investments	(212,230)	(288,878)
Purchases of available-for-sale investments		(24,600)
Sales of available-for-sale investments		36,850
Redemptions of trading investments	225	
Maturities of held-to-maturity investments	183,099	197,356
Restrictions on cash	11,591	1,780
Net cash used by investing activities	(94,586)	(165,347)
Cash flows from financing activities:		
Proceeds from the exercise of stock options	23,036	37,456
Excess tax benefits from share-based compensation	2,710	19,105
Principal payments on debt	(240)	(32)
Net cash provided by financing activities	25,506	56,529
Effect of exchange rate changes on cash and cash equivalents	489	(274)
Net increase (decrease) in cash and cash equivalents	5,050	(31,350)
Cash and cash equivalents, beginning of period	129,452	139,323
Cash and cash equivalents, end of period	$ 134,502	$ 107,973
Supplemental schedule of cash flow information:		
Cash paid for interest	$ 1,250	$ 1,250
Cash paid for income taxes	$ 11,304	$ 1,628
Non-cash investing and financing activities:		
Lease obligation incurred	$	$ 29,000
Acquisition of Tyvaso Inhalation System business	$ 5,063	$
Non-cash additions to property, plant and equipment	$ 3,935	$

See accompanying notes to consolidated financial statements.

(1) Adjusted for the retrospective adoption of FASB ASC 470-20, formerly FSP APB 14-1. See Note 9 *Debt Adoption of FASB ASC 470-20 (Formerly FSP APB 14-1).*

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UNITED THERAPEUTICS CORPORATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

September 30, 2009
(UNAUDITED)

1. Business Description

United Therapeutics Corporation is a biotechnology company focused on the development and commercialization of unique products to address the unmet medical needs of patients with chronic and life-threatening cardiovascular and infectious diseases and cancer. We were incorporated in 1996 under the laws of the State of Delaware and our wholly-owned subsidiaries include Lung Rx, LLC, Unither Pharmaceuticals, LLC, Unither Telmed, Ltd., Unither.com, Inc., United Therapeutics Europe, Ltd., Unither Therapeutik GmbH, Unither Pharma, LLC, Medicomp, Inc., Unither Neurosciences, Inc., LungRx Limited, Unither Biotech Inc., and Unither Virology, LLC. As used in these notes to the consolidated financial statements, unless the context requires otherwise, the terms we, us, our, and similar terms refer to United Therapeutics Corporation and its consolidated subsidiaries.

Our lead product is Remodulin® (treprostinil sodium) Injection (Remodulin), which was initially approved in 2002 by the United States Food and Drug Administration (FDA).

We have generated pharmaceutical revenues and license fees in the United States, Canada, the European Union (EU), South America and Asia. In addition, we have generated non-pharmaceutical revenues from telemedicine products and services in the United States.

2. Basis of Presentation

The accompanying unaudited consolidated financial statements have been prepared in accordance with the rules and regulations of the United States Securities and Exchange Commission (SEC) for interim financial information. Accordingly, they do not include all of the information and footnotes required by United States generally accepted accounting principles (GAAP) for complete financial statements. These consolidated financial statements should be read in conjunction with the audited consolidated financial statements and the accompanying notes contained in our Annual Report on Form 10-K for the year ended December 31, 2008. The financial statements as of December 31, 2008, and for the three- and nine-month periods ended September 30, 2008, presented in this Quarterly Report on Form 10-Q have been adjusted for the retrospective adoption of FASB ASC 470-20 (formerly FSP APB 14-1) on January 1, 2009. See Note 9 to these consolidated financial statements for further discussion.

In our management s opinion, the accompanying consolidated financial statements contain all adjustments, including normal recurring adjustments, necessary to present fairly our financial position as of September 30, 2009, results of operations for the three- and nine-month periods ended September 30, 2009 and 2008, and cash flows for the nine months ended September 30, 2009 and 2008. Interim results are not necessarily indicative of annual results. We have evaluated subsequent events through October 29, 2009, which is the date our financial statements were issued. No material events have occurred during the period from September 30, 2009, to October 29, 2009, that would require recognition in these financial statements.

3. Inventories

Inventories are stated at the lower of cost (first-in, first-out method) or market (current replacement cost) and consist of the following, net of reserves (in thousands):

	September 30, 2009	December 31, 2008
Raw materials	$ 4,040	$ 3,387
Work-in-progress	11,457	6,558
Finished goods	8,541	4,085
Delivery pumps, cardiac monitoring equipment and medical supplies	776	342
Total inventories	$ 24,814	$ 14,372

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4. Fair Value Measurements

FASB ASC Topic 820, *Fair Value Measurement and Disclosures* (FASB ASC Topic 820) (formerly Statement of Financial Accounting Standards (SFAS) No. 157, *Fair Value Measurements*), defines fair value and establishes a fair value hierarchy based on the quality and reliability of the inputs or assumptions used in fair value measurements. Assets and liabilities that are measured, or permitted to be measured at fair value, are required to be classified and disclosed in one of the following categories based on the lowest level input that is significant to a fair value measurement:

Level 1 Fair value is determined by using unadjusted quoted prices that are available in active markets for identical assets and liabilities.

Level 2 Fair value is determined by using inputs other than Level 1 quoted prices that are directly or indirectly observable.

Level 3 Fair value is determined by inputs that are unobservable and not corroborated by market data.

Financial assets and liabilities subject to fair value measurements are as follows (in thousands):

	As of September 30, 2009			
	Level 1	Level 2	Level 3	Balance
Assets				
Auction-rate securities(1)	$	$	$ 29,079	$ 29,079
Auction-rate securities put option(2)			7,184	7,184
Available-for-sale equity investment	148			148
Money market funds(3)	80,969			80,969
Federally-sponsored and corporate debt securities(4)		236,897		236,897
Total Assets	$ 81,117	$ 236,897	$ 36,263	$ 354,277
Liabilities				
Convertible senior notes	$ 342,470	$	$	$ 342,470
Contingent consideration Tyvaso Inhalation System acquisition(5)			3,907	3,907
Total liabilities	$ 342,470	$	$ 3,907	$ 346,377

	As of December 31, 2008			
	Level 1	Level 2	Level 3	Balance
Assets				
Auction-rate securities(1)	$	$	$ 27,976	$ 27,976
Auction-rate securities put option(2)			7,685	7,685
Available-for-sale equity investment	97			97
Money market funds(3)	96,179			96,179
Federally-sponsored and corporate debt securities(4)		209,313		209,313

Total Assets	$	96,276	$	209,313	$	35,661	$	341,250
Liabilities								
Convertible senior notes	$	239,429	$		$		$	239,429

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(1) Included in non-current marketable investments on the accompanying consolidated balance sheets refer to the section below entitled *Auction-Rate Securities* for a discussion of the valuation techniques used to estimate the fair value of these securities.

(2) Included within non-current other assets on the accompanying consolidated balance sheets see the section below entitled *Auction-Rate Securities* for further information regarding the approach used to estimate the fair value of this option.

(3) Included in cash and cash equivalents and marketable investments and cash restricted on the accompanying consolidated balance sheets.

(4) Included in current and non-current marketable investments on the accompanying consolidated balance sheets. The fair value of these securities is derived from pricing models using observable market data including interest rates, yield curves, recently reported trades of comparable securities, credit spreads and benchmark securities. See also Note 5 *Held-to-Maturity Investments*.

(5) Included in non-current liabilities on the accompanying consolidated balance sheet. See also Note 16 *Acquisition.*

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A reconciliation of the beginning and ending balances of assets measured at fair value using significant unobservable inputs (Level 3) for the three- and nine-month periods ended September 30, 2009, respectively, is presented below (in thousands):

	Auction-rate Securities	Auction-Rate Securities Put Option	Contingent Consideration Tyvaso Inhalation System Acquisition	Total
Balance July 1, 2009	$ 28,000	$ 8,344	$	$ 36,344
Transfers to (from) Level 3				
Total gains/(losses) realized/unrealized included in earnings(1)	1,254	(1,160)		94
Total gains/(losses) included in other comprehensive income				
Purchases/issuances/settlements, net	(175)		3,907	3,732
Balance September 30, 2009	$ 29,079	$ 7,184	$ 3,907	$ 40,170

	Auction-rate Securities	Auction-Rate Securities Put Option	Contingent Consideration Tyvaso Inhalation System Acquisition	Total
Balance January 1, 2009	$ 27,976	$ 7,685	$	$ 35,661
Transfers to (from) Level 3				
Total gains/(losses) realized/unrealized included in earnings(1)	1,328	(501)		827
Total gains/(losses) included in other comprehensive income				
Purchases/issuances/settlements, net	(225)		3,907	3,682
Balance September 30, 2009	$ 29,079	$ 7,184	$ 3,907	$ 40,170

(1) Gains of $94,000 and $827,000 for the three- and nine-month periods ended September 30, 2009, respectively, were included in earnings and are attributable to the change in unrealized gains from securities still held at September 30, 2009 (recognized within other income on the consolidated statements of operations).

Auction-Rate Securities

Our marketable investments include AAA-rated, auction-rate securities (ARS) collateralized by student loans that are approximately 91% guaranteed by the federal government. Since February 2008, our ARS have been rendered illiquid as a result of the collapse of the credit markets. Consequently, the fair value of our ARS has been estimated using both a discounted cash flow (DCF) approach and a market comparables method. For the market comparables method, we consider market data pricing to estimate the discount being applied to similar securities upon sale in the secondary market. Although the volume of secondary market activity has been increasing, we do not believe it occurs with sufficient frequency to rely solely on such data to determine the fair value of our ARS. As such, we also utilize a DCF model to estimate their fair value. The key assumptions of the DCF model are subjective and include the following: a reference, or benchmark rate of interest based on the London Interbank Offered Rate (LIBOR), the amounts and timing of cash flows, and the weighted average expected life of a security and its underlying collateral. In addition, the model considers the risks associated with: (i) the creditworthiness of the issuer; (ii) the quality of the collateral underlying the investment; and (iii) illiquidity. The benchmark interest rate is then adjusted upward depending on the degree of risk associated with each security within our auction-rate portfolio. We estimate illiquidity premiums based on an analysis of the average discounts applied to recent sales of comparable ARS within the secondary market.

To mitigate the risks associated with our ARS, we entered into an Auction-Rate Securities Rights Offer (Rights Offer) in November 2008 with the investment firm that maintains our ARS account. Pursuant to the Rights Offer, we can sell our ARS to the investment firm for a price equal to their par value (approximately $36.5 million) at any time between June 30, 2010, and July 2, 2012 (Put Option). To help meet any immediate liquidity needs, the Rights Offer permits us to borrow up to the par value of our ARS; however, we do not expect to exercise this right. The Put Option represents a freestanding, non-transferable financial instrument that is being accounted for under the fair value option set forth under FASB ASC Topic 825, *Financial Instruments* (formerly SFAS No.159, *The Fair Value Option for Financial Assets and Financial Liabilities Including an amendment of FASB Statement No. 115*). Accordingly, all changes in fair value of the Put Option will be recognized within earnings. For the three- and nine-month periods ended September 30, 2009, we recognized losses of $1.2 million and $501,000, respectively, related to the Put Option, which has been

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included in other income on the consolidated statements of operations. Since there is not an observable market for the Put Option, its fair value has been estimated using significant unobservable inputs; therefore, it has been categorized as a Level 3 asset within the fair value hierarchy.

We employed a DCF model to estimate the fair value of the Put Option. We believe that the estimated fair value of the Put Option represents the incremental value associated with the ability to recover the full cost of our ARS at a significantly earlier date than would be otherwise possible, if at all, and the ability to obtain an immediate loan under the Rights Offer, as this right possesses value regardless of whether we expect to borrow under the Rights Offer. Key assumptions used in the DCF model are subjective and include the following: (i) a discount factor equal to the rate of interest consistent with the expected term of the Put Option and risk profile of the investment firm subject to the Put Option; (ii) the amount and timing of expected cash flows; (iii) the expected life of the Put Option prior to its exercise; and (iv) assumed loan amounts. This DCF methodology considered two scenarios. The first scenario assumed that we would borrow up to 50% of the par value of our ARS and the second scenario assumed that we would borrow up to 75% of the par value of our ARS. Under the DCF model, increases in the assumed loan balance would result in an increase in the fair value of the Put Option because the risk of counterparty non-performance diminishes. The estimated fair values generated under both scenarios were given equal weight in estimating the fair value of the Put Option.

Fair Value of Financial Instruments

The carrying amounts of cash and cash equivalents, accounts receivables, accounts payable, and accrued expenses approximate fair value because of their short maturities. The fair value of marketable investments is presented in Note 5 and the fair value of the 0.50% Convertible Senior Notes due October 2011 (Convertible Senior Notes) is reported above.

5. Investments

Held-to-Maturity Investments

Marketable investments classified as held-to-maturity consist of the following (in thousands):

	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
Government-sponsored enterprises at September 30, 2009	$ 168,241	$ 985	$ (9)	$ 169,217
Corporate notes and bonds at September 30, 2009	67,492	202	(14)	67,680
Total	$ 235,733	$ 1,187	$ (23)	$ 236,897
As reported on the consolidated balance sheets at September 30, 2009:				
Current marketable securities	$ 100,994			
Noncurrent marketable securities	134,739			
	$ 235,733			

	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
Government-sponsored enterprises at December 31, 2008	$ 154,115	$ 1,718	$ (18)	$ 155,815
Corporate notes and bonds at December 31, 2008	53,509	140	(151)	53,498
Total	$ 207,624	$ 1,858	$ (169)	$ 209,313
As reported on the consolidated balance sheets at December 31, 2008:				
Current marketable securities	$ 106,596			
Noncurrent marketable securities	101,028			
	$ 207,624			

Certain held-to-maturity investments have been pledged as collateral to Wachovia Development Corporation under the laboratory lease described in Note 10 to these consolidated financial statements, and are classified as restricted marketable investments and cash on our consolidated balance sheets as of September 30, 2009, and December 31, 2008.

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The following table summarizes gross unrealized losses and the length of time marketable investments have been in a continuous unrealized loss position (in thousands):

	As of September 30, 2009		As of December 31, 2008	
	Fair Value	Gross Unrealized Loss	Fair Value	Gross Unrealized Loss
Government sponsored:				
Less than one year	$ 12,001	$ (9)	$ 9,886	$ (18)
Greater than one year				
	12,001	(9)	9,886	(18)
Corporate notes:				
Less than one year	$ 26,743	$ (14)	$ 21,278	$ (151)
Greater than one year				
	26,743	(14)	21,278	(151)
Total	$ 38,744	$ (23)	$ 31,164	$ (169