

ENDO PHARMACEUTICALS HOLDINGS INC  
Form 10-Q  
October 31, 2011  
Table of Contents

**UNITED STATES**  
**SECURITIES AND EXCHANGE COMMISSION**

Washington, DC 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 SEPTEMBER 30, 2011.**

**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: 001-15989**

**ENDO PHARMACEUTICALS HOLDINGS INC.**

(Exact Name of Registrant as Specified in Its Charter)

Edgar Filing: ENDO PHARMACEUTICALS HOLDINGS INC - Form 10-Q

**Delaware**  
(State or other jurisdiction of  
incorporation or organization)

**13-4022871**  
(I.R.S. Employer

Identification Number)

**100 Endo Boulevard Chadds Ford, Pennsylvania**  
(Address of Principal Executive Offices)

**19317**  
(Zip Code)

**(610) 558-9800**

(Registrant's Telephone Number, Including Area Code)

**Not applicable**

(Former name, former address and former fiscal year, if changed since last report)

Indicate by check whether the registrant: (1) has filed all reports required to be filed by Sections 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 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, or a smaller reporting company. See definitions of large accelerated filer, accelerated filer and smaller reporting company in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer

Accelerated filer

Non-accelerated filer  (Do not check if a smaller reporting company)

Smaller reporting company

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Act). YES  NO

Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practical date.

Common Stock, \$0.01 par value

Shares outstanding as of October 17, 2011: 116,836,364

**Table of Contents**

**ENDO PHARMACEUTICALS HOLDINGS INC.**

**INDEX**

	<b>Page</b>
<u>Forward-Looking Statements</u>	i
 <b><u>PART I. FINANCIAL INFORMATION</u></b> 	
Item 1. <u>Financial Statements</u>	1
<u>Condensed Consolidated Balance Sheets (Unaudited) September 30, 2011 and December 31, 2010</u>	1
<u>Condensed Consolidated Statements of Operations (Unaudited) Three and Nine months ended September 30, 2011 and 2010</u>	2
<u>Condensed Consolidated Statements of Cash Flows (Unaudited) Nine months ended September 30, 2011 and 2010</u>	3
<u>Notes to Condensed Consolidated Financial Statements (Unaudited)</u>	4
Item 2. <u>Management's Discussion and Analysis of Financial Condition and Results of Operations</u>	68
Item 3. <u>Quantitative and Qualitative Disclosures About Market Risk</u>	98
Item 4. <u>Controls and Procedures</u>	98
 <b><u>PART II. OTHER INFORMATION</u></b> 	
Item 1. <u>Legal Proceedings</u>	98
Item 1A. <u>Risk Factors</u>	98
Item 2. <u>Unregistered Sales of Equity Securities and Use of Proceeds</u>	98
Item 3. <u>Defaults Upon Senior Securities</u>	98
Item 4. <u>Removed and Reserved</u>	98
Item 5. <u>Other Information</u>	98
Item 6. <u>Exhibits</u>	98
<b><u>SIGNATURES</u></b>	99

**Table of Contents**

**FORWARD-LOOKING STATEMENTS**

Statements contained or incorporated by reference in this Quarterly Report on Form 10-Q contain information that includes or is based on forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, as amended, or the Securities Act, and Section 21E of the Securities Exchange Act of 1934, as amended, or the Exchange Act. These statements, including estimates of future revenues, future expenses, future net income and future net income per share, contained in the section titled Management's Discussion and Analysis of Financial Condition and Results of Operations, in our Annual Report on Form 10-K for the year ended December 31, 2010, filed with the Securities and Exchange Commission on February 28, 2011, are subject to risks and uncertainties. Forward-looking statements include the information concerning our possible or assumed results of operations. Also, statements including words such as believes, expects, anticipates, intends, estimates, plan, will, may or similar expressions are forward-looking. We have based these forward-looking statements on our current expectations and projections about the growth of our business, our financial performance and the development of our industry. Because these statements reflect our current views concerning future events, these forward-looking statements involve risks and uncertainties. Investors should note that many factors, as more fully described under the caption Risk Factors in Item 1A of our Annual Report on Form 10-K for the year ended December 31, 2010 and as otherwise enumerated herein or therein, could affect our future financial results and could cause our actual results to differ materially from those expressed in forward-looking statements contained in our Annual Report on Form 10-K. Important factors that could cause our actual results to differ materially from the expectations reflected in the forward-looking statements in our Annual Report on Form 10-K include those factors described herein under the caption Risk Factors and in documents incorporated by reference, including, among others:

our ability to successfully develop, commercialize and market new products;

timing and results of pre-clinical or clinical trials on new products;

our ability to obtain regulatory approval of any of our pipeline products;

government regulation of the pharmaceutical industry and the effect of healthcare reform on our business;

competition for the business of our branded and generic pharmaceuticals, our devices and services, and our acquisition of rights to intellectual property assets;

our ability to sustain our sales and profit on generic pharmaceutical products over time;

our ability to maintain our manufacturing facilities in compliance with regulatory requirements;

market acceptance of our future products;

our dependence on a small number of branded pharmaceuticals products with time-limited exclusivity rights;

our dependence on outside manufacturers for the manufacture of most of our branded pharmaceuticals products;

our dependence on third parties to supply raw materials and to provide services for certain core aspects of our business;

new regulatory action or lawsuits relating to our use of narcotics in most of our core products;

our exposure to product liability claims and product recalls and the possibility that we may not be able to adequately insure ourselves;

our ability to protect our proprietary technology;

the successful efforts of manufacturers of branded pharmaceuticals to use litigation and legislative and regulatory efforts to limit the use of generics and certain other products;

our ability to successfully implement our acquisition and in-licensing strategy;

regulatory or other limits on the availability of controlled substances that constitute the active ingredients of some of our products and products in development;

the availability of third-party reimbursement for our products;

the outcome of any pending or future litigation or claims by third parties or the government, and the performance of indemnitors with respect to claims for which we have the right to be indemnified;

our dependence on sales to a limited number of large pharmacy chains and wholesale drug distributors for a large portion of our total revenues;

significant litigation expenses, including to defend or assert patent infringement claims;

any interruption or failure by our suppliers, distributors and collaboration partners to meet their obligations pursuant to various agreements with us;

**Table of Contents**

a determination by a regulatory agency that we are engaging or have engaged in inappropriate sales or marketing activities, including promoting the off-label use of our products;

existing suppliers become unavailable or lose their regulatory status as an approved source, causing an inability to obtain required components, raw materials or products on a timely basis or at commercially reasonable prices;

the loss of branded product exclusivity periods and related intellectual property;

our ability to successfully execute our strategy;

disruption of our operations if our information systems fail or if we are unsuccessful in implementing necessary upgrades or new software;

our ability to maintain or expand our business if we are unable to retain or attract key personnel and continue to attract additional professional staff;

our ability to successfully integrate Generics International (US Parent), Inc., or Qualitest, and American Medical Systems Holdings, Inc., or AMS, and realize all anticipated benefits of our acquisitions, including the projected synergies of these acquisitions;

HealthTronics, Inc.'s, or HealthTronics', and AMS's ability to establish or maintain relationships with physicians and hospitals;

HealthTronics' and AMS's ability to comply with special risks and requirements related to their respective medical products manufacturing business;

the risks associated with our reliance on single- or sole-source suppliers for certain raw materials and certain components used in our products; and

the risks associated with our international operations.

We do not undertake any obligation to update our forward-looking statements after the date of this Report for any reason, even if new information becomes available or other events occur in the future. You are advised, however, to consult any further disclosures we make on related subjects in our 10-Q, 10-K, and 8-K reports filed with the Securities and Exchange Commission (SEC). Also note that we provide the preceding cautionary discussion of the risks, uncertainties and possibly inaccurate assumptions relevant to our business. These are factors that, individually or in the aggregate, we think could cause our actual results to differ materially from expected and historical results. We note these factors for investors as permitted by Section 27A of the Securities Act and Section 21E of the Exchange Act. You should understand that it is not possible to predict or identify all such factors. Consequently, you should not consider the preceding to be a complete discussion of all potential risks or uncertainties.

**Table of Contents****PART I. FINANCIAL INFORMATION****Item 1. Financial Statements****ENDO PHARMACEUTICALS HOLDINGS INC.****CONDENSED CONSOLIDATED BALANCE SHEETS (UNAUDITED)****(In thousands, except share and per share data)**

	<b>September 30, 2011</b>	<b>December 31, 2010</b>
<b>ASSETS</b>		
<b>CURRENT ASSETS:</b>		
Cash and cash equivalents	\$ 419,671	\$ 466,214
Marketable securities	41,010	
Accounts receivable, net	721,984	547,807
Inventories, net	282,540	178,805
Prepaid expenses and other current assets	29,424	22,841
Income taxes receivable		3,143
Deferred income taxes	182,475	140,724
Total current assets	1,677,104	1,359,534
MARKETABLE SECURITIES	20,396	23,509
PROPERTY, PLANT AND EQUIPMENT, NET	273,488	215,295
GOODWILL	2,496,859	715,005
OTHER INTANGIBLES, NET	2,766,049	1,531,760
OTHER ASSETS	126,947	67,286
TOTAL ASSETS	\$ 7,360,843	\$ 3,912,389
<b>LIABILITIES AND STOCKHOLDERS EQUITY</b>		
<b>CURRENT LIABILITIES:</b>		
Accounts payable	\$ 243,647	\$ 241,114
Accrued expenses	654,608	469,721
Current portion of long-term debt	74,334	24,993
Acquisition-related contingent consideration	6,228	
Income taxes payable	14,819	
Total current liabilities	993,636	735,828
DEFERRED INCOME TAXES	727,393	217,334
ACQUISITION-RELATED CONTINGENT CONSIDERATION	2,529	16,050
LONG-TERM DEBT, LESS CURRENT PORTION, NET	3,565,184	1,045,801
OTHER LIABILITIES	84,536	94,047
<b>COMMITMENTS AND CONTINGENCIES (NOTE 12)</b>		
<b>STOCKHOLDERS EQUITY:</b>		
Preferred Stock, \$0.01 par value; 40,000,000 shares authorized; none issued		
Common Stock, \$0.01 par value; 350,000,000 shares authorized; 138,020,933 and 136,309,917 shares issued; 116,842,811 and 116,057,895 shares outstanding at September 30, 2011 and December 31, 2010, respectively	1,378	1,363
Additional paid-in capital	933,584	860,882
Retained earnings	1,515,316	1,364,297

Edgar Filing: ENDO PHARMACEUTICALS HOLDINGS INC - Form 10-Q

Accumulated other comprehensive loss	(7,298)	(1,161)
Treasury stock, 21,178,122 and 20,252,022 shares at September 30, 2011 and December 31, 2010, respectively	(518,492)	(483,790)
Total Endo Pharmaceuticals Holdings Inc. stockholders' equity	1,924,488	1,741,591
Noncontrolling interests	63,077	61,738
Total stockholders' equity	1,987,565	1,803,329
TOTAL LIABILITIES AND STOCKHOLDERS' EQUITY	\$ 7,360,843	\$ 3,912,389

See Notes to Condensed Consolidated Financial Statements.



**Table of Contents****ENDO PHARMACEUTICALS HOLDINGS INC.****CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS (UNAUDITED)****(In thousands, except per share data)**

	<b>Three Months Ended</b>		<b>Nine Months Ended</b>	
	<b>September 30,</b>		<b>September 30,</b>	
	<b>2011</b>	<b>2010</b>	<b>2011</b>	<b>2010</b>
<b>REVENUES:</b>				
Net pharmaceutical product sales	\$ 569,657	\$ 389,264	\$ 1,603,004	\$ 1,143,734
Device, service and other revenues	189,421	54,839	323,711	61,305
<b>TOTAL REVENUES</b>	<b>759,078</b>	<b>444,103</b>	<b>1,926,715</b>	<b>1,205,039</b>
<b>COSTS AND EXPENSES:</b>				
Cost of revenues	302,172	133,920	770,427	335,209
Selling, general and administrative	244,359	137,816	581,878	404,402
Research and development	43,884	31,445	126,854	105,269
Impairment of long-lived assets	22,691		22,691	13,000
Acquisition-related items	5,818	24,990	29,517	31,315
<b>OPERATING INCOME</b>	<b>140,154</b>	<b>115,932</b>	<b>395,348</b>	<b>315,844</b>
INTEREST EXPENSE, NET	52,792	12,979	97,142	32,767
LOSS ON EXTINGUISHMENT OF DEBT, NET			8,548	
OTHER (INCOME), NET	(3,000)	(59)	(2,777)	(479)
<b>INCOME BEFORE INCOME TAX</b>	<b>90,362</b>	<b>103,012</b>	<b>292,435</b>	<b>283,556</b>
INCOME TAX	34,057	33,540	100,283	102,269
<b>CONSOLIDATED NET INCOME</b>	<b>56,305</b>	<b>69,472</b>	<b>192,152</b>	<b>181,287</b>
Less: Net income attributable to noncontrolling interests	15,656	15,266	41,133	15,266
<b>NET INCOME ATTRIBUTABLE TO ENDO PHARMACEUTICALS HOLDINGS INC.</b>	<b>\$ 40,649</b>	<b>\$ 54,206</b>	<b>\$ 151,019</b>	<b>\$ 166,021</b>
<b>NET INCOME PER SHARE:</b>				
Basic	\$ 0.35	\$ 0.47	\$ 1.30	\$ 1.43
Diluted	\$ 0.34	\$ 0.46	\$ 1.24	\$ 1.42
<b>WEIGHTED AVERAGE SHARES:</b>				
Basic	116,816	115,469	116,611	116,292
Diluted	120,847	116,597	121,432	117,096

See Notes to Condensed Consolidated Financial Statements.

**Table of Contents****ENDO PHARMACEUTICALS HOLDINGS INC.****CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS (UNAUDITED)****(In thousands)**

	<b>Nine Months Ended September 30,</b>	
	<b>2011</b>	<b>2010</b>
<b>OPERATING ACTIVITIES:</b>		
Consolidated net income	\$ 192,152	\$ 181,287
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	169,187	69,859
Stock-based compensation	34,224	16,753
Amortization of debt issuance costs and premium / discount	24,283	17,484
Selling, general and administrative expenses paid in shares of common stock	180	166
Deferred income taxes	(13,847)	(13,543)
Loss on disposal of property, plant and equipment	319	59
Change in the fair value of acquisition-related contingent consideration	(7,458)	2,150
Loss on extinguishment of debt	8,548	
Loss on auction-rate securities rights		15,659
Gain on trading securities		(15,420)
Impairment of long-lived assets	22,691	13,000
Changes in assets and liabilities which provided (used) cash:		
Accounts receivable	(96,409)	(51,623)
Inventories	(28,879)	2,895
Prepaid and other assets	(9,055)	7,314
Accounts payable	(21,656)	(21,058)
Accrued expenses	134,834	54,442
Other liabilities	(15,693)	(23)
Income taxes receivable/payable	25,110	3,583
<b>Net cash provided by operating activities</b>	<b>418,531</b>	<b>282,984</b>
<b>INVESTING ACTIVITIES:</b>		
Purchases of property, plant and equipment	(39,609)	(11,318)
Proceeds from sales property, plant and equipment	1,147	
Proceeds from sales of trading securities		230,867
Acquisitions, net of cash acquired	(2,368,357)	(333,349)
Proceeds from investments	36,000	
Purchases of investments	(6,009)	
Other investments	(388)	(1,648)
Payment on contingent consideration	(662)	
License fees	(2,300)	
Proceeds from sale of business	12,990	
<b>Net cash used in investing activities</b>	<b>(2,367,188)</b>	<b>(115,448)</b>
<b>FINANCING ACTIVITIES:</b>		
Capital lease obligations repayments		(285)
Tax benefits of stock awards	5,519	2,074
Exercise of Endo Pharmaceuticals Holdings Inc. stock options	21,780	8,728
Proceeds from issuance of 2019 and 2022 Notes	900,000	
Purchase of common stock	(34,702)	(58,974)

Edgar Filing: ENDO PHARMACEUTICALS HOLDINGS INC - Form 10-Q

Proceeds from issuance of Term Loans	2,200,000	
Principal payments on Term Loans	(550,813)	
Payment on AMS Convertible Notes	(519,040)	
Deferred financing fees	(81,535)	
Principal payment on HealthTronics senior credit facility		(40,000)
Distributions to noncontrolling interests	(39,392)	(13,971)
Buy-out of noncontrolling interests, net of contributions	(402)	(725)
Proceeds from other debt, net	302	1,230
Net cash provided by (used in) financing activities	1,901,717	(101,923)
Effect of foreign exchange rate	397	
NET (DECREASE) INCREASE IN CASH AND CASH EQUIVALENTS	(46,543)	65,613
CASH AND CASH EQUIVALENTS, BEGINNING OF PERIOD	466,214	708,462
CASH AND CASH EQUIVALENTS, END OF PERIOD	\$ 419,671	\$ 774,075
SUPPLEMENTAL INFORMATION:		
Interest paid	\$ 32,299	\$ 14,313
Income taxes paid	\$ 95,551	\$ 109,675
SCHEDULE OF NON-CASH INVESTING AND FINANCING ACTIVITIES		
Purchases of property, plant and equipment financed by capital leases	\$ 119	\$
Accrual for purchases of property, plant and equipment	\$ 2,849	\$ 2,085

See Notes to Condensed Consolidated Financial Statements.

**Table of Contents**

**ENDO PHARMACEUTICALS HOLDINGS INC.**

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

**FOR THE NINE MONTHS ENDED SEPTEMBER 30, 2011**

**NOTE 1. BASIS OF PRESENTATION**

The accompanying unaudited Condensed Consolidated Financial Statements have been prepared in accordance with generally accepted accounting principles for interim financial information and with the instructions to Form 10-Q and Article 10 of Regulation S-X of the Securities and Exchange Commission for interim financial information. Accordingly, they do not include all of the information and footnotes required by generally accepted accounting principles for complete financial statements. In the opinion of management, the accompanying Condensed Consolidated Financial Statements of Endo Pharmaceuticals Holdings Inc. (the Company or we, our, us, or Endo) and its subsidiaries, which are unaudited, include all normal and recurring adjustments considered necessary to present fairly the Company's financial position as of September 30, 2011 and the results of our operations and our cash flows for the periods presented. Operating results for the three-month and nine-month periods ended September 30, 2011 are not necessarily indicative of the results that may be expected for the year ending December 31, 2011.

In June 2011, the Company acquired AMS, a worldwide developer and provider of technology solutions to physicians treating men's and women's pelvic health conditions. In November 2010, the Company acquired Qualitest, a United States based privately-held generics company. In September 2010, the Company acquired its partner on Opana® ER, Penwest, a drug delivery company focused on applying its drug delivery technologies and drug formulation expertise to the formulation of its collaborators' product candidates under licensing collaborations. In July 2010, the Company acquired HealthTronics, a provider of healthcare services and manufacturer of medical devices, primarily for the urology community. The condensed consolidated results of operations presented herein reflect the operating results of AMS from and including June 18, 2011 and of Qualitest, Penwest, and HealthTronics from January 1, 2011. Additionally, all of the assets acquired and liabilities assumed in connection with the AMS, Qualitest, Penwest, and HealthTronics acquisitions are recorded at their respective fair values and are included in the accompanying Condensed Consolidated Financial Statements as of September 30, 2011.

**NOTE 2. RECENT ACCOUNTING PRONOUNCEMENTS**

In December 2010, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update (ASU) 2010-29 on interim and annual disclosure of pro forma financial information related to business combinations. The new guidance clarifies the acquisition date that should be used for reporting the pro forma financial information in which comparative financial statements are presented. It is effective prospectively for business combinations for which the acquisition date is on or after the beginning of the first annual reporting period beginning on or after December 15, 2010. The provisions of this ASU have been incorporated into this filing for our 2011 acquisitions.

In December 2010, the FASB issued ASU 2010-28 on accounting for goodwill. The guidance clarifies the impairment test for reporting units with zero or negative carrying amounts. The guidance is effective for fiscal years and interim periods within those years beginning after December 15, 2011. The adoption is not expected to have a material impact on the Company's Consolidated Financial Statements.

In December 2010, the FASB issued ASU 2010-27 on accounting for the annual fee imposed by the Patient Protection and Affordable Care Act, as amended by the Health Care and Education Reconciliation Act. The new guidance specifies that the liability for the fee should be estimated and recorded in full upon the first qualifying sale with a corresponding deferred cost that is amortized to expense. It is effective on a prospective basis for calendar years beginning after December 31, 2010. We expect this fee will be approximately \$18 million in 2011, which will be charged as an operating expense ratably throughout 2011.

In May 2011, the FASB issued ASU 2011-04 on fair value disclosures. This guidance amends certain accounting and disclosure requirements related to fair value measurements. It is effective on a prospective basis for interim and annual periods beginning after December 15, 2011. Early application is not permitted. The Company is currently evaluating ASU 2011-04 but we do not expect the impact of adoption to be material.

**Table of Contents**

In June 2011, the FASB issued ASU 2011-05 on the presentation of comprehensive income, which amends current comprehensive income guidance. This accounting update eliminates the option to present the components of other comprehensive income as part of the statement of shareholders' equity. Instead, the Company must report comprehensive income in either a single continuous statement of comprehensive income which contains two sections, net income and other comprehensive income, or in two separate but consecutive statements. ASU 2011-05 will be effective for public companies during the interim and annual periods beginning after December 15, 2011 with early adoption permitted. The adoption of ASU 2011-05 will not have an impact on the Company's consolidated financial position, results of operations or cash flows as it only requires a change in the format of the current presentation.

In September 2011, the FASB issued ASU 2011-08 on testing goodwill for impairment, which permits an entity to make a qualitative assessment of whether it is more likely than not that a reporting unit's fair value is less than its carrying value before applying the two-step goodwill impairment model that is currently in place. If it is determined through the qualitative assessment that a reporting unit's fair value is more likely than not greater than its carrying value, the remaining impairment steps would be unnecessary. The qualitative assessment is optional, allowing companies to go directly to the quantitative assessment. ASU 2011-08 will be effective for annual and interim goodwill impairment tests performed in fiscal years beginning after December 15, 2011, with early adoption permitted. The Company is currently evaluating ASU 2011-08.

**NOTE 3. FAIR VALUE MEASUREMENTS**

The financial instruments recorded in our Condensed Consolidated Balance Sheets include cash and cash equivalents, accounts receivable, marketable securities, auction-rate securities rights, equity and cost method investments, accounts payable, acquisition-related contingent consideration, our debt obligations, and derivative instruments. Included in cash and cash equivalents are money market funds representing a type of mutual fund required by law to invest in low-risk securities (for example, U.S. government bonds, U.S. Treasury Bills and commercial paper). Money market funds are structured to maintain the fund's net asset value at \$1 per unit, which assists in ensuring adequate liquidity upon demand by the holder. Money market funds pay dividends that generally reflect short-term interest rates. Thus, only the dividend yield fluctuates. Due to their short-term maturity, the carrying amounts of cash and cash equivalents, accounts receivable and accounts payable approximate their fair values.

The following table presents the carrying amounts and estimated fair values of our other financial instruments as of September 30, 2011 and December 31, 2010 (in thousands):

	September 30, 2011		December 31, 2010	
	Carrying Amount	Fair Value	Carrying Amount	Fair Value
<b>Current assets:</b>				
Commercial paper	\$ 41,010	\$ 41,010	\$	\$
Derivative instruments	930	930	\$	\$
<b>Long-term assets:</b>				
Auction-rate securities	17,416	17,416	17,332	17,332
Equity securities	2,980	2,980	6,177	6,177
Equity and cost method investments	20,616	n/a	34,677	n/a
	\$ 82,952		\$ 58,186	
<b>Current liabilities:</b>				
Acquisition-related contingent consideration - short-term	6,228	6,228		
Current portion of Term Loan Facility Due 2015			22,500	22,500
Current portion of Term Loan A Facility Due 2016	70,313	70,313		
3.25% AMS Convertible Notes due 2036	841	841		
4.00% AMS Convertible Notes due 2041	131	131		
Current portion of other long-term debt	3,049	3,049	2,493	2,493
Derivative instruments	31	31		

**Table of Contents**

	September 30, 2011		December 31, 2010	
	Carrying Amount	Fair Value	Carrying Amount	Fair Value
Long-term liabilities:				
Acquisition-related contingent consideration long-term	2,529	2,529	16,050	16,050
1.75% Convertible Senior Subordinated Notes Due 2015, less current portion, net	293,947	329,617	278,922	324,257
Term Loan Facility Due 2015, less current portion			377,500	380,038
Term Loan A Facility Due 2016, less current portion	1,415,625	1,406,362		
Term Loan B Facility Due 2018	563,250	561,926		
7.00% Senior Notes Due 2019	500,000	505,938		
7.00% Senior Notes Due 2020, net	389,954	404,250	386,716	403,308
7.25% Senior Notes Due 2022	400,000	404,750		
Other long-term debt, less current portion	2,408	2,408	2,663	2,663
Minimum Voltaren® Gel royalties due to Novartis	26,777	26,777	38,922	38,922
	\$ 3,675,083	\$ 3,725,150	\$ 1,125,766	\$ 1,190,231

Commercial paper has a maturity of eight months or less and is held with a highly rated financial institution. Commercial paper is carried at amortized cost, which is a reasonable approximation of fair value. Equity securities consist of publicly traded common stock, the value of which is based on a quoted market price. These securities are not held to support current operations and are therefore classified as non-current assets.

The acquisition-related contingent consideration, which is required to be measured at fair value on a recurring basis, consists primarily of contingent cash consideration related to the November 2010 acquisition of Qualitest. The fair value of our acquisition-related contingent consideration is determined using an income approach (present value technique), which is discussed in more detail below.

The fair value of our 1.75% Convertible Senior Subordinated Notes is based on an income approach known as the binomial lattice model which incorporated certain inputs and assumptions, including scheduled coupon and principal payments, the conversion feature inherent in the Convertible Notes, the put feature inherent in the Convertible Notes, and stock price volatility assumptions of 33% at September 30, 2011 and December 31, 2010 that were based on historic volatility of the Company's common stock and other factors. The fair values of our Term Loan Facilities and 2019, 2020, and 2022 Notes were estimated using a discounted cash flow model based on the contractual repayment terms of the respective instruments and discount rates that reflect current market conditions.

The total fair value of various foreign exchange forward contracts as of September 30, 2011 includes assets of \$0.9 million reported in Accounts receivable, net and liabilities of less than \$0.1 million, reported in Accrued expenses. We measure our derivative instruments at fair value on a recurring basis using significant observable inputs. Refer to Note 16 for more information regarding our derivative instruments.

The minimum Voltaren® Gel royalty due to Novartis AG was recorded at fair value at inception during 2008 using an income approach (present value technique) and is being accreted up to the maximum potential future payment of \$60.0 million. The Company is not aware of any events or circumstances that would have a significant effect on the fair value of this Novartis AG liability. We believe the carrying amount of this minimum royalty guarantee at September 30, 2011 and December 31, 2010 represents a reasonable approximation of the price that would be paid to transfer the liability in an orderly transaction between market participants at the measurement date. Accordingly, the carrying value approximates fair value as of September 30, 2011 and December 31, 2010.

The fair value of equity method and cost method investments is not readily available nor have we estimated the fair value of these investments and disclosure is not required. The Company is not aware of any identified events or changes in circumstances that would have a significant adverse effect on the carrying value of any of our equity or cost method investments included in our Condensed Consolidated Balance Sheet at September 30, 2011.

**Table of Contents**

As of September 30, 2011, the Company held certain assets and liabilities that are required to be measured at fair value on a recurring basis. Fair value guidance establishes a three-tier fair value hierarchy, which prioritizes the inputs used in measuring fair value. These tiers include:

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

Level 2 Inputs other than Level 1 that are observable, either directly or indirectly, such as quoted prices for similar assets or liabilities; quoted 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 assets or liabilities.

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

The Company's financial assets and liabilities measured at fair value on a recurring basis at September 30, 2011 and December 31, 2010, were as follows (in thousands):

	Fair Value Measurements at Reporting Date Using			Total
	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	
<b>As of September 30, 2011:</b>				
<b>Assets:</b>				
Money market funds	\$ 169,267	\$	\$	\$ 169,267
Equity securities	2,980			2,980
Commercial paper		41,010		41,010
Derivative instruments		930		930
Auction-rate securities			17,416	17,416
Total	\$ 172,247	\$ 41,940	\$ 17,416	\$ 231,603
<b>Liabilities:</b>				
Derivative instruments		31		31
Acquisition-related contingent consideration	short-term		6,228	6,228
Acquisition-related contingent consideration	long-term		2,529	2,529
Total	\$	\$ 31	\$ 8,757	\$ 8,788
<b>As of December 31, 2010</b>				
<b>Assets:</b>				
Money market funds	149,318			149,318
Equity securities	6,177			6,177
Auction-rate securities			17,332	17,332
Total	\$ 155,495	\$	\$ 17,332	\$ 172,827
<b>Liabilities:</b>				
Acquisition-related contingent consideration	long-term		16,050	16,050

## Edgar Filing: ENDO PHARMACEUTICALS HOLDINGS INC - Form 10-Q

Total	\$	\$	\$	16,050	\$	16,050
-------	----	----	----	--------	----	--------

Commercial paper is carried at amortized cost, which is a reasonable approximation of fair value, and has therefore been classified as Level 2. We measure our derivative instruments at fair value on a recurring basis using significant observable inputs, which is Level 2 as defined in the fair value hierarchy.

### *Overview of Auction-Rate Securities*

Auction-rate securities are long-term variable rate bonds tied to short-term interest rates. After the initial issuance of the securities, the interest rate on the securities is reset periodically, at intervals established at the time of



**Table of Contents**

issuance (e.g., every seven, twenty-eight, or thirty-five days; every six months; etc.). In an active market, auction-rate securities are bought and sold at each reset date through a competitive bidding process, often referred to as a Dutch auction. Auctions are successful when the supply and demand of securities are in balance. Financial institutions brokering the auctions would also participate in the auctions to balance the supply and demand. Beginning in the second half of 2007, auctions began to fail for specific securities and in mid-February 2008 auction failures became common, prompting market participants, including financial institutions, to cease or limit their exposure to the auction-rate market. Given the current negative liquidity conditions in the global credit markets, the auction-rate securities market became inactive. Consequently, our auction-rate securities are currently illiquid through the normal auction process. As a result of the inactivity in the market, quoted market prices and other observable data are not available or their utility is limited.

At September 30, 2011, the Company determined that the market for its auction-rate securities was still inactive. That determination was made considering that there are very few observable transactions for the auction-rate securities or similar securities, the prices for transactions that have occurred are not current, and the observable prices for those transactions to the extent they exist vary substantially either over time or among market makers, thus reducing the potential usefulness of those observations. In addition, the current lack of liquidity prevents the Company from comparing our securities directly to securities with quoted market prices.

Our auction-rate securities consist of municipal bonds with an auction reset feature, the underlying assets of which are student loans that are backed substantially by the federal government and have underlying credit ratings of AAA as of September 30, 2011 and December 31, 2010. The issuers have been making interest payments promptly.

***Overview of Auction-Rate Securities Rights***

In October 2008, UBS AG (UBS) made an offer (the UBS Offer) to the Company and other clients of UBS Securities LLC and UBS Financial Services Inc. (collectively, the UBS Entities), pursuant to which the Company received auction-rate securities rights (the Rights) to sell to UBS all auction-rate securities held by the Company as of February 13, 2008 in a UBS account (the Eligible Auction-Rate Securities). The Rights permitted the Company to require UBS to purchase the Eligible Auction-Rate Securities for a price equal to par value plus any accrued but unpaid dividends or interest beginning on June 30, 2010 and ending on July 2, 2012.

On November 10, 2008, the Company accepted the UBS Offer, awarding the UBS Entities the sole discretion and right to sell or otherwise dispose of, and/or enter orders in the auction process with respect to the Eligible Auction-Rate Securities on the Company's behalf until the Expiration Date, without prior notification, so long as the Company receives a payment of par value plus any accrued but unpaid dividends or interest upon any sale or disposition.

***Subsequent Accounting for Auction-Rate Securities and Auction-Rate Securities Rights***

Concurrent with the acceptance of the UBS offer, the Company made a one-time election to re-classify the Eligible Auction-Rate Securities from an available-for-sale security to a trading security. Subsequent changes to the fair value of these trading securities resulted in \$15.4 million of income during the nine months ended September 30, 2010 recorded in Other income, net in the Condensed Consolidated Statements of Operations.

As a result of our fair value election for the Rights, the fair value of the Rights was re-measured each reporting period with the corresponding changes in fair value reported in earnings. In June 2010, the Rights were exercised and all Eligible Auction-Rate Securities were sold at par. Accordingly, the Rights were written off in their entirety.

At September 30, 2011 and December 31, 2010, the fair value of the Rights was zero. Accordingly, the decrease in fair value for nine months ended September 30, 2010 of \$15.7 million was recognized as a charge to earnings and included in Other income, net in the Condensed Consolidated Statements of Operations.

***Valuation of the Auction-Rate Securities***

The Company determined that an income approach (present value technique) that maximizes the use of observable market inputs is the preferred approach to measuring the fair value of our securities. Specifically, the Company used the discount rate adjustment technique to determine an indication of fair value.

## Table of Contents

To calculate a price for our auction-rate securities, the Company calculates duration to maturity, coupon rates, market required rates of return (discount rate) and a discount for lack of liquidity in the following manner:

The Company identifies the duration to maturity of the auction-rate securities as the time at which principal is available to the investor. This can occur because the auction-rate security is paying a coupon that is above the required rate of return, and the Company treats the security as being called. It can also occur because the market has returned to normal and the Company treats the auctions as having recommenced. Lastly, and most frequently, the Company treats the principal as being returned as prepayment occurs and at the maturity of the security. The initial life used for each remaining security, representing time to maturity, was eight years as of September 30, 2011 and December 31, 2010.

The Company calculates coupon rates based on estimated relationships between the maximum coupon rate (the coupon rate in event of a failure) and market interest rates. The representative coupon rate was 3.80% on September 30, 2011 and 5.10% at December 31, 2010. The Company calculates appropriate discount rates for securities that include base interest rates, index spreads over the base rate, and security-specific spreads. These spreads include the possibility of changes in credit risk over time. The spread over the base rate applied to our securities was 217 basis points at September 30, 2011 and 218 basis points at December 31, 2010.

The Company believes that a market participant would require an adjustment to the required rate of return to adjust for the lack of liquidity. We do not believe it is unreasonable to assume a 150 basis points adjustment to the required rate of return and a term of either three, four or five years to adjust for this lack of liquidity. The increase in the required rate of return decreases the prices of the securities. However, the assumption of a three, four or five-year term shortens the times to maturity and increases the prices of the securities. The Company has evaluated the impact of applying each term and the reasonableness of the range indicated by the results. The Company chose to use a four-year term to adjust for the lack of liquidity as we believe it is the point within the range that is most representative of fair value. The Company's conclusion is based in part on the fact that the fair values indicated by the results are reasonable in relation to each other given the nature of the securities and current market conditions.

At September 30, 2011, the fair value of our auction-rate securities, as determined by applying the above described discount rate adjustment technique, was approximately \$17.4 million, representing an 8%, or \$1.4 million discount from their original purchase price or par value. This compares to approximately \$17.3 million, representing an 8%, or \$1.5 million discount from their original purchase price or par value at December 31, 2010. We believe we have appropriately reflected our best estimate of the assumptions that market participants would use in pricing the assets in a current transaction to sell the asset at the measurement date. Accordingly, the carrying value of our auction-rate securities at September 30, 2011 and December 31, 2010 were reduced by approximately \$1.4 million and \$1.5 million, respectively. These adjustments appropriately reflect the changes in fair value, which the Company attributes to liquidity issues rather than credit issues.

The portion of this decline in fair value related to the Eligible Auction-Rate Securities was recorded in earnings as of December 31, 2010 as an other-than-temporary impairment charge or as changes in the fair value of trading securities. The Company has assessed the portion of the decline in fair value not associated with the Eligible Auction-Rate Securities to be temporary due to the financial condition and near-term prospects of the underlying issuers, our intent and ability to retain our investment in the issuers for a period of time sufficient to allow for any anticipated recovery in market value and based on the extent to which fair value is less than par. Accordingly, we recorded a \$0.1 million gain and a \$0.4 million loss in Stockholders' equity in Accumulated other comprehensive loss as of September 30, 2011 and December 31, 2010, respectively. Securities not subject to the UBS Offer are analyzed each reporting period for other-than-temporary impairment factors. Any future fluctuation in fair value related to these instruments that the Company judges to be temporary, including any recoveries of previous write-downs, would be recorded to other comprehensive income. If the Company determines that any future valuation adjustment was other-than-temporary, it would record a charge to earnings as appropriate. However, there can be no assurance that our current belief that the securities not subject to the UBS Offer will recover their value will not change.

---

## **Table of Contents**

### ***Valuation of the Auction-Rate Securities Rights***

Until the Rights were exercised and all UBS securities were sold on June 30, 2010, the Company valued the Rights using an income approach (present value technique) that maximized the use of observable market inputs. Specifically, the Company used the discount rate adjustment technique to determine an indication of fair value.

### ***Overview of Acquisition-Related Contingent Consideration***

At September 30, 2011 and December 31, 2010, the fair value of the contingent consideration is \$8.8 million and \$16.1 million, respectively. The material components of this obligation are discussed below.

#### *Indevus*

On February 23, 2009 (the Indevus Acquisition Date), the Company completed its initial tender offer for all outstanding shares of common stock of Indevus and completed its acquisition of Indevus on March 23, 2009, at which time Indevus became a wholly-owned subsidiary of the Company. The Indevus Shares were purchased at a price of \$4.50 per Indevus Share, net to the seller in cash, plus contractual rights to receive up to an additional \$3.00 per Indevus Share in contingent cash consideration payments related to potential future regulatory and commercial milestones related to Aveed<sup>TM</sup> (the Aveed<sup>TM</sup> Contingent Cash Consideration Agreement) and the octreotide NDA for the treatment of acromegaly (the Octreotide Contingent Cash Consideration Agreement). Additionally, upon the acquisition of Indevus, the Company assumed a pre-existing contingent consideration obligation relating to Indevus' acquisition of Valera Pharmaceuticals, Inc. (the Valera Contingent Consideration Agreement), which could entitle former Valera shareholders to receive consideration from the Company upon U.S. Food and Drug Administration (FDA) approval of the octreotide implant for the treatment for acromegaly.

#### *Qualitest*

On November 30, 2010 (the Qualitest Acquisition Date), Endo acquired Qualitest, which was party to an asset purchase agreement with Teva Pharmaceutical Industries Ltd (Teva) (the Teva Agreement). Pursuant to this agreement, Qualitest purchased certain pipeline generic products from Teva and could be obligated to pay consideration to Teva upon the achievement of certain future regulatory milestones (the Teva Contingent Consideration).

### ***Valuation of the Acquisition-Related Contingent Consideration***

#### *Indevus*

The Indevus Contingent Consideration Agreements were measured and recognized at fair value upon the Indevus Acquisition Date and are required to be re-measured on a recurring basis, with changes to fair value recorded in Acquisition-related items in the accompanying Condensed Consolidated Statements of Operations. The fair values were determined using a probability-weighted discounted cash flow model, or income approach. This fair value measurement technique is based on significant inputs not observable in the market and thus represents a Level 3 measurement within the fair value hierarchy. The valuation of each Indevus Contingent Consideration Agreement is described in further detail below:

*Aveed<sup>TM</sup> Contingent Consideration* The range of the undiscounted amounts the Company could pay under the Aveed<sup>TM</sup> Contingent Cash Consideration Agreement is between zero and approximately \$175.0 million. Under this agreement, there are three scenarios that could potentially lead to amounts being paid to the former stockholders of Indevus. These scenarios are (1) obtaining an Aveed<sup>TM</sup> With Label approval, (2) obtaining an Aveed<sup>TM</sup> Without Label approval and (3) achieving the \$125.0 million sales milestone on or prior to the fifth anniversary of the date of the first commercial sale of Aveed<sup>TM</sup> should the Aveed<sup>TM</sup> Without Label approval be obtained. The fourth scenario is Aveed<sup>TM</sup> not receiving approval within three years of the closing of the Offer, which would result in no payment to the former stockholders of Indevus. Each scenario was assigned a probability based on the current regulatory status of Aveed<sup>TM</sup>. The resultant probability-weighted cash flows were then discounted using a discount rate of U.S. Prime plus 300 basis points, which the Company believes is appropriate and is representative of a market participant assumption. Using this valuation technique, the fair value of the contractual obligation to pay the Aveed<sup>TM</sup> Contingent Consideration was determined to be zero at September 30, 2011, \$7.1 million at December 31, 2010 and \$133.1 million on the Indevus Acquisition Date.



**Table of Contents**

*Octreotide Contingent Consideration* The range of the undiscounted amounts the Company could pay under the Octreotide Contingent Cash Consideration Agreement is between zero and approximately \$91.0 million. Under this agreement, the two scenarios that require consideration are (1) approval of octreotide on or before the fourth anniversary of the closing of the Offer or (2) no octreotide approval on or before the fourth anniversary of the closing of the Offer. Each scenario was assigned a probability based on the current development stage of octreotide. The resultant probability-weighted cash flows were then discounted using a discount rate of U.S. Prime plus 300 basis points, which the Company believes is appropriate and is representative of a market participant assumption. Using this valuation technique, the fair value of the contractual obligation to pay the Octreotide Contingent Consideration was determined to be zero at both September 30, 2011 and December 31, 2010 and \$39.8 million on the Indevus Acquisition Date.

*Valera Contingent Consideration* The range of the undiscounted amounts the Company could pay under the Valera Contingent Cash Consideration Agreement is between zero and approximately \$33.0 million. The fair value of the Valera Contingent Consideration is estimated using the same assumptions used for the Aveed™ Contingent Cash Consideration Agreement and Octreotide Contingent Cash Consideration Agreement, except that the probabilities associated with the Valera Contingent Consideration take into account the probability of obtaining the Octreotide Approval on or before the fourth anniversary of the closing of the Offer. This is due to the fact that the Valera Contingent Consideration will not be paid unless octreotide for the treatment of acromegaly is approved prior to April 18, 2012. Using this valuation technique, the fair value of the contractual obligation to pay the Valera Contingent Consideration was determined to be zero at both September 30, 2011 and December 31, 2010 and \$13.7 million on the Indevus Acquisition Date.

At September 30, 2011, the aggregate fair value of the three Indevus Contingent Consideration Agreements decreased from \$7.1 million at December 31, 2010 to zero at September 30, 2011. This decrease primarily reflects management's current assessment of the probability that it will not be obligated to make contingent consideration payments based on the anticipated timeline for the NDA filings and FDA approvals of Aveed™. The decrease in the liability was recorded as a gain and was included in Acquisition-related items in the accompanying Condensed Consolidated Statements of Operations.

*Qualitest*

On November 30, 2010 (the Qualitest Acquisition Date), Endo acquired Qualitest, who was party to an asset purchase agreement with Teva Pharmaceutical Industries Ltd (Teva) (the Teva Agreement). Pursuant to this agreement, Qualitest purchased certain pipeline generic products from Teva and could be obligated to pay consideration to Teva upon the achievement of certain future regulatory milestones (the Teva Contingent Consideration).

The range of the undiscounted amounts the Company could pay under the Teva Agreement is between zero and \$12.5 million. The Company is accounting for the Teva Contingent Consideration in the same manner as if it had entered into that arrangement with respect to its acquisition of Qualitest. Accordingly, the fair value was estimated based on a probability-weighted discounted cash flow model, or income approach. The resultant probability-weighted cash flows were then discounted using a discount rate of U.S. Prime plus 300 basis points. This fair value measurement is based on significant inputs not observable in the market and thus represents a Level 3 measurement within the fair value hierarchy. Using this valuation technique, the fair value of the contractual obligation to pay the Teva Contingent Consideration was determined to be \$8.6 million at September 30, 2011 and \$9.0 million at December 31, 2010 and the Qualitest Acquisition Date, respectively.

The decrease from December 31, 2010 to September 30, 2011 primarily reflects changes of our present value assumptions associated with our valuation model. The decrease in the liability was recorded as a gain and is included in Acquisition-related items in the accompanying Condensed Consolidated Statements of Operations.

***Fair Value Measurements Valued Using Significant Unobservable Inputs***

The following tables present changes to the Company's financial assets and liabilities measured at fair value on a recurring basis using significant unobservable inputs (Level 3) for the three months ended September 30, 2011 and 2010 (in thousands):

**Table of Contents**

	Fair Value Measurements Using Significant Unobservable Inputs (Level 3) Auction-rate Securities
<b>Assets:</b>	
Balance at July 1, 2011	\$ 17,505
Securities sold or redeemed	
Transfers in and/or (out) of Level 3	
Changes in fair value recorded in earnings	
Unrealized losses included in other comprehensive income	(89)
Balance at September 30, 2011	\$ 17,416

	Fair Value Measurements Using Significant Unobservable Inputs (Level 3) Acquisition-related Contingent Consideration
<b>Liabilities:</b>	
Balance at July 1, 2011	\$ (9,233)
Amounts (acquired) sold / (issued) settled, net	248
Transfers in and/or (out) of Level 3	
Changes in fair value recorded in earnings	228
Balance at September 30, 2011	\$ (8,757)

	Fair Value Measurements Using Significant Unobservable Inputs (Level 3)		
	Auction-rate Securities	Auction-rate Securities Rights	Total
<b>Assets:</b>			
Balance at July 1, 2010	\$ 17,695	\$	\$ 17,695
Securities sold or redeemed			
Securities purchased or acquired			
Transfers in and/or (out) of Level 3			
Changes in fair value recorded in earnings			
Unrealized gain included in other comprehensive loss	(190)		(190)
Balance at September 30, 2010	\$ 17,505	\$	\$ 17,505

	Fair Value Measurements Using Significant Unobservable Inputs (Level 3) Acquisition-related Contingent Consideration
<b>Liabilities:</b>	
Balance at July 1, 2010	\$ (59,590)
Amounts (acquired) sold / (issued) settled, net	
Transfers in and/or (out) of Level 3	
Changes in fair value recorded in earnings	(1,030)
Balance at September 30, 2010	\$ (60,620)

**Table of Contents**

The following tables present changes to the Company's financial assets and liabilities measured at fair value on a recurring basis using significant unobservable inputs (Level 3) for the nine months ended September 30, 2011 and 2010 (in thousands):

	Fair Value Measurements Using Significant Unobservable Inputs (Level 3) Auction-rate Securities
<b>Assets:</b>	
Balance at January 1, 2011	\$ 17,332
Securities sold or redeemed	
Transfers in and/or (out) of Level 3	
Changes in fair value recorded in earnings	
Unrealized gains included in other comprehensive income	84
Balance at September 30, 2011	\$ 17,416

	Fair Value Measurements Using Significant Unobservable Inputs (Level 3) Acquisition-related Contingent Consideration
<b>Liabilities:</b>	
Balance at January 1, 2011	\$ (16,050)
Amounts (acquired) sold / (issued) settled, net	(165)
Transfers in and/or (out) of Level 3	
Changes in fair value recorded in earnings	7,458
Balance at September 30, 2011	\$ (8,757)

	Fair Value Measurements Using Significant Unobservable Inputs (Level 3)		
	Auction-rate Securities	Auction-rate Securities Rights	Total
<b>Assets:</b>			
Balance at January 1, 2010	\$ 207,334	\$ 15,659	\$ 222,993
Securities sold or redeemed	(205,050)		(205,050)
Securities purchased or acquired			
Transfers in and/or (out) of Level 3			
Changes in fair value recorded in earnings	15,420	(15,659)	(239)
Unrealized gain included in other comprehensive loss	(199)		(199)



Edgar Filing: ENDO PHARMACEUTICALS HOLDINGS INC - Form 10-Q

Balance at September 30, 2010 \$ 17,505 \$ 17,505

	Fair Value Measurements Using Significant Unobservable Inputs (Level 3) Acquisition-related Contingent Consideration
<b>Liabilities:</b>	
Balance at January 1, 2010	\$ (58,470)
Amounts (acquired) sold / (issued) settled, net	

**Table of Contents**

	Fair Value Measurements Using Significant Unobservable Inputs (Level 3) Acquisition-related Contingent Consideration
Transfers in and/or (out) of Level 3	
Changes in fair value recorded in earnings	(2,150)
Balance at September 30, 2010	\$ (60,620)

At September 30, 2011 and December 31, 2010, the respective fair values of the Company's trading securities were zero. The following is a summary of available-for-sale securities held by the Company as of September 30, 2011 and December 31, 2010 (in thousands):

	Amortized Cost	Gross Unrealized Gains	Gross Unrealized (Losses)	Fair Value
<b>September 30, 2011:</b>				
Money market funds	\$ 169,267	\$	\$	\$ 169,267
<i>Total included in cash and cash equivalents</i>	\$ 169,267	\$	\$	\$ 169,267
Commercial paper	41,010			41,010
<i>Total other short-term available-for-sale securities</i>	\$ 210,277	\$	\$	\$ 210,277
Auction-rate securities	18,800		(1,384)	17,416
Equity securities	5,564		(2,584)	2,980
<i>Long-term available-for-sale securities</i>	\$ 24,364	\$	\$ (3,968)	\$ 20,396
<i>Total available-for-sale securities</i>	\$ 234,641	\$	\$ (3,968)	\$ 230,673
<b>December 31, 2010:</b>				
Money market funds	\$ 149,318	\$	\$	\$ 149,318
<i>Total included in cash and cash equivalents</i>	\$ 149,318	\$	\$	\$ 149,318
Auction-rate securities	18,800		(1,468)	17,332
Equity securities	5,564	613		6,177
<i>Long-term available-for-sale securities</i>	\$ 24,364	\$ 613	\$ (1,468)	\$ 23,509
<i>Total available-for-sale securities</i>	\$ 173,682	\$ 613	\$ (1,468)	\$ 172,827

**Table of Contents**

As previously discussed, the Company has determined that the gross unrealized losses associated with the auction-rate securities are not other-than-temporary. The Company also reviewed the gross unrealized losses associated with our equity securities as of September 30, 2011 and determined that these losses were not other-than-temporary, primarily because the Company has both the ability and intent to hold the investments for a period of time we believe will be sufficient to recover such losses.

We did not sell any of our remaining auction-rate securities during the three or nine months ended September 30, 2011. During the nine month period ended September 30, 2010, we sold \$230.3 million of auction-rate securities at par value. During the three month period ended September 30, 2010, there were no sales of auction-rate securities. There were no realized holding gains and losses resulting from the sales of our auction rate securities during the periods ended September 30, 2011 and 2010. The cost of securities sold is based on the specific identification method.

The underlying assets of our auction-rate securities are student loans. Student loans are insured by the Federal Family Education Loan Program, or FFELP.

As of September 30, 2011, the yields on our long-term auction-rate securities ranged from 0.32% to 0.34%. These yields represent the predetermined maximum reset rates that occur upon auction failures according to the specific terms within each security's prospectus. As of September 30, 2011, the weighted average yield for our long-term auction-rate securities was 0.33%. Total interest recognized on our auction-rate securities during the nine months ended September 30, 2011 and 2010 was less than \$0.1 million and \$0.6 million, respectively. The issuers have been making interest payments promptly.

The amortized cost and estimated fair value of available-for-sale debt and equity securities by contractual maturities are shown below (in thousands). Actual maturities may differ from contractual maturities because borrowers may have the right to call or prepay obligations with or without call or prepayment penalties.

	September 30, 2011		December 31, 2010	
	Amortized Cost	Fair Value	Amortized Cost	Fair Value
Available-for-sale debt securities:				
Due in less than 1 year	\$ 41,010	\$ 41,010	\$	\$
Due in 1 to 5 years				
Due in 5 to 10 years				
Due after 10 years	18,800	17,416	18,800	17,332
Equity securities	5,564	2,980	5,564	6,177
<b>Total</b>	<b>\$ 65,374</b>	<b>\$ 61,406</b>	<b>\$ 24,364</b>	<b>\$ 23,509</b>

**Table of Contents****NOTE 4. INVENTORIES**

Inventories are comprised of the following at September 30, 2011 and December 31, 2010, respectively (in thousands):

	September 30, 2011	December 31, 2010
Raw materials	\$ 87,967	\$ 45,957
Work-in-process	45,646	34,208
Finished goods	148,927	98,640
Total	\$ 282,540	\$ 178,805

Inventory amounts in the table above are shown net of obsolescence. Our reserve for obsolescence is not material to the Condensed Consolidated Balance Sheets for any of the periods presented and therefore has not been separately disclosed.

**NOTE 5. ACQUISITIONS****AMS**

On June 17, 2011 (the AMS Acquisition Date), the Company completed its acquisition of all outstanding shares of common stock of AMS for approximately \$2.4 billion in aggregate consideration, including \$70.8 million related to existing AMS stock-based compensation awards and certain other amounts, at which time AMS became a wholly-owned subsidiary of the Company. AMS's shares were purchased at a price of \$30.00 per share.

AMS is a worldwide developer and provider of technology solutions to physicians treating men's and women's pelvic health conditions. The AMS business and applicable services include:

*Men's Health.*

AMS supplies surgical solutions for the treatment of male urinary incontinence, the involuntary release of urine from the body. The fully implantable AMS 800® system includes an inflatable urethral cuff to restrict flow through the urethra and a control pump that allows the patient to discreetly open the cuff when he wishes to urinate. Since 2000, AMS has also been selling the InVance® sling system, a less-invasive procedure for men with moderate incontinence, and in 2007, AMS released the AdVance® sling system for the treatment of mild to moderate stress urinary incontinence. AMS also offers the UroLume® endoprosthesis stent as a less invasive procedure for patients who may not be good surgical candidates, as well as for men suffering from bulbar urethral strictures.

AMS also supplies penile implants to treat erectile dysfunction, the inability to achieve or maintain an erection sufficient for sexual intercourse, with a series of semi-rigid malleable prostheses and a complete range of more naturally functioning inflatable prostheses, including the AMS 700® MS. AMS has refined its implants over the years with improvements to the AMS 700® series of inflatable prostheses, including the AMS 700 LGX® and the MS Pump®. Another key factor that distinguishes AMS's products is the use of the InhibiZone® antibiotic coating, which received FDA approval in July 2009 for our product claim that InhibiZone® reduces the rate of revision surgery due to surgical infections.

*Women's Health.*

AMS offers a broad range of systems, led by Monarc® and MiniArc®, to treat female stress urinary incontinence, which generally results from a weakening of the tissue surrounding the bladder and urethra which can be a result of pregnancy, childbirth and aging. Monarc® incorporates unique helical needles to place a self-fixating, sub-fascial hammock through the obturator foramen. AMS's MiniArc® Single-Incision Sling for stress incontinence was released in 2007 and requires just one incision to surgically place a small sling under the urethra, which minimizes tissue disruption and potential for blood loss, thereby allowing the procedure to be done with less anesthesia on an outpatient basis. In 2010, AMS launched the MiniArc Precise™, which is designed to enhance the ease and accuracy of placement of the MiniArc® device.

AMS also offers solutions for pelvic floor prolapse and other pelvic floor disorders, which may be caused by pregnancy, labor, and childbirth. In 2008, AMS introduced the Elevate® transvaginal pelvic floor repair system, with no external incisions. Using an anatomically designed needle

and self-fixating tips, Elevate® allows for safe, simple

**Table of Contents**

and precise mesh placement through a single vaginal incision. The posterior system was launched in 2008 and the anterior system was launched in 2009.

*BPH Therapy.*

AMS's products can be used to relieve restrictions on the normal flow of urine from the bladder caused by bladder obstructions, generally the result of benign prostatic hyperplasia (BPH) or bulbar urethral strictures. AMS offers men experiencing a physical obstruction of the prostatic urethra an alternative to a transurethral resection of the prostate (TURP), with the GreenLight™ photovaporization of the prostate. This laser therapy is designed to reduce the comorbidities associated with TURP. AMS's GreenLight™ XPS and MoXy™ Liquid Cooled Fiber provide shorter treatment times with similar long-term results compared to other laser systems. The GreenLight™ laser system offers an optimal laser beam that balances vaporization of tissue with coagulation to prevent blood loss and providing enhanced surgical control compared to other laser systems. AMS also offers the StoneLight® laser and SureFlex™ fiber optics for the treatment of urinary stones. StoneLight® is a lightweight and portable 15-watt holmium laser that offers the right amount of power to effectively fragment most urinary stones. The SureFlex™ fiber optic line is engineered to deliver more energy safely and effectively, even under maximum scope deflection, for high performance holmium laser lithotripsy.

AMS's TherMatrx® product is designed for those men not yet to the point of urethral obstruction, but for whom symptomatic relief is desired. It is a less-invasive tissue ablation technique that can be performed in a physician's office using microwave energy delivered to the prostate.

The acquisition of AMS provides Endo scale in its Devices and Services business segment, and we believe the combination of AMS with Endo's existing platform will provide additional cost-effective solutions across the entire urology spectrum.

The operating results of AMS from and including June 18, 2011 are included in the accompanying Condensed Consolidated Statements of Operations. The Condensed Consolidated Balance Sheet as of September 30, 2011 reflects the acquisition of AMS.

The following table summarizes the fair values of the assets acquired and liabilities assumed at the AMS Acquisition Date (in thousands):

	June 17, 2011 (As initially reported)	Measurement period adjustments	June 17, 2011 (As adjusted)
Cash and cash equivalents	\$ 47,289	\$	\$ 47,289
Commercial paper	71,000		71,000
Accounts receivable	73,868		73,868
Other receivables	791		791
Inventories	75,525		75,525
Prepaid expenses and other current assets	7,133		7,133
Income taxes receivable	11,179	(4,022)	7,157
Deferred income taxes	15,360	(829)	14,531
Property and equipment	57,372	(960)	56,412
Other intangible assets	1,390,000		1,390,000
Other assets	4,581		4,581
<b>Total identifiable assets</b>	<b>\$ 1,754,098</b>	<b>\$ (5,811)</b>	<b>\$ 1,748,287</b>
Accounts payable	\$ 9,437	\$	\$ 9,437
Accrued expenses	45,648	150	45,798
Deferred income taxes	507,019	(10,885)	496,134
Long-term debt	520,012	363	520,375
Other liabilities	23,578		23,578
<b>Total liabilities assumed</b>	<b>\$ 1,105,694</b>	<b>\$ (10,372)</b>	<b>\$ 1,095,322</b>
<b>Net identifiable assets acquired</b>	<b>\$ 648,404</b>	<b>\$ 4,561</b>	<b>\$ 652,965</b>



**Table of Contents**

	June 17, 2011 (As initially reported)	Measurement period adjustments	June 17, 2011 (As adjusted)
Goodwill	\$ 1,752,427	\$ (5,434)	\$ 1,746,993
Net assets acquired	\$ 2,400,831	\$ (873)	\$ 2,399,958

The above estimated fair values of assets acquired and liabilities assumed are provisional and are based on the information that was available as of the AMS Acquisition Date to estimate the fair value of assets acquired and liabilities assumed. The Company believes that information provides a reasonable basis for estimating the fair values but the Company is waiting for additional information necessary to finalize those amounts, particularly with respect to the estimated fair value of intangible assets, property and equipment, contingent assets and liabilities, and deferred income taxes. Thus, the provisional measurements of fair value reflected are subject to change. Such changes could be significant. The Company expects to finalize the valuation and complete the purchase price allocation as soon as practicable but no later than one year from the AMS Acquisition Date.

The valuation of the intangible assets acquired and related amortization periods are as follows:

	Valuation (in millions)	Amortization Period (in years)
<b>Customer Relationships:</b>		
Men's Health	\$ 97.0	17
Women's Health	49.0	15
BPH	26.0	13
Total	\$ 172.0	16
<b>Developed Technology:</b>		
Men's Health	\$ 690.0	18
Women's Health	230.0	9
BPH	161.0	18
Total	\$ 1,081.0	16
<b>In Process Research &amp; Development:</b>		
Oracle	\$ 22.0	n/a
Genesis	14.0	n/a
TOPAS	8.0	n/a
Other	22.0	n/a
Total	\$ 66.0	n/a
<b>Tradename:</b>		
AMS	\$ 59.0	n/a
GreenLight	12.0	15
Total	\$ 71.0	n/a
Total other intangible assets	\$ 1,390.0	n/a

The fair value of the developed technology, in-process research and development and customer relationship assets were estimated using a discounted present value income approach. Under this method, an intangible asset's fair value is equal to the present value of the incremental after-tax cash flows (excess earnings) attributable solely to the intangible asset over its remaining useful life. To calculate fair value, the Company used cash flows discounted at rates considered appropriate given the inherent risks associated with each type of asset. The Company



## Edgar Filing: ENDO PHARMACEUTICALS HOLDINGS INC - Form 10-Q

believes that the level and timing of cash flows appropriately reflect market participant assumptions. The fair value of the AMS and GreenLight tradenames were estimated using an income approach, specifically known as the relief from royalty method. The relief from royalty method is based on a hypothetical royalty stream that would be received if the Company were to license the AMS or GreenLight tradename. Thus, we derived the hypothetical royalty income

**Table of Contents**

from the projected revenues of AMS and GreenLight products, respectively. Cash flows were assumed to extend through the remaining economic useful life of each class of intangible asset.

The \$1,747.0 million of goodwill was assigned to our Devices and Services segment. The goodwill recognized is attributable primarily to strategic and synergistic opportunities across the entire urology spectrum, expected corporate synergies, the assembled workforce of AMS and other factors. Approximately \$17.8 million of goodwill is expected to be deductible for income tax purposes.

Deferred tax assets of \$14.5 million are related primarily to federal net operating loss and credit carryforwards of AMS and its subsidiaries. Deferred tax liabilities of \$496.1 million are related primarily to the difference between the book basis and tax basis of identifiable intangible assets.

The Company recognized \$4.1 million and \$27.3 million of AMS acquisition-related costs that were expensed during the three and nine months ended September 30, 2011, respectively. These costs are included in Acquisition-related items in the accompanying Condensed Consolidated Statements of Operations and are comprised of the following items (in thousands):

	Acquisition-related Costs Three months ended September 30, 2011	Acquisition-related Costs Nine months ended September 30, 2011
Bank fees	\$	\$ 16,070
Legal, separation, integration, and other costs	4,069	11,263
<b>Total</b>	<b>\$ 4,069</b>	<b>\$ 27,333</b>

The amounts of revenue and net income of AMS included in the Company's Condensed Consolidated Statements of Operations from and including June 18, 2011 to September 30, 2011 are as follows (in thousands, except per share data):

	Revenue and Income included in the Condensed Consolidated Statements of Operations from and including June 18, 2011 to September 30, 2011
Revenue	\$ 158,331
Net loss attributable to Endo Pharmaceuticals Holdings Inc.	\$ (6,527)
Basic and diluted net loss per share	\$ (0.06)

The following supplemental pro forma information presents the financial results as if the acquisition of AMS had occurred on January 1, 2010 for the nine months ended September 30, 2011 and the three and nine months ended September 30, 2010. This supplemental pro forma information has been prepared for comparative purposes and does not purport to be indicative of what would have occurred had the acquisition been made on January 1, 2010, nor are they indicative of any future results.

	Nine months ended September 30, 2011
<b>Pro forma consolidated results (in thousands, except per share data):</b>	
Revenue	\$ 2,165,091
Net income attributable to Endo Pharmaceuticals Holdings Inc.	\$ 130,389
Basic net income per share	\$ 1.12

Diluted net income per share	\$	1.07
------------------------------	----	------

**Table of Contents**

	Three months ended September 30, 2010	Nine months ended September 30, 2010
<b>Pro forma consolidated results (in thousands, except per share data):</b>		
Revenue	\$ 568,285	\$ 1,600,870
Net income attributable to Endo Pharmaceuticals Holdings Inc.	\$ 33,843	\$ 92,610
Basic net income per share	\$ 0.29	\$ 0.80
Diluted net income per share	\$ 0.29	\$ 0.79

These amounts have been calculated after applying the Company's accounting policies and adjusting the results of AMS to reflect factually supportable adjustments that give effect to events that are directly attributable to the AMS Acquisition, including the borrowing under the 2011 Credit Facility, 2019 Notes, and 2022 Notes as well as the additional depreciation and amortization that would have been charged assuming the fair value adjustments primarily to property, plant and equipment, inventory, and intangible assets, had been applied on January 1, 2010, together with the consequential tax effects.

**Qualitest**

On November 30, 2010 (the Qualitest Acquisition Date), Endo completed its acquisition of all of the issued and outstanding capital stock of Generics International (US Parent), Inc. (Qualitest) from an affiliate of Apax Partners, L.P. for approximately \$770.0 million. In addition, Endo paid \$406.8 million to retire Qualitest's outstanding debt and related interest rate swap on November 30, 2010. In connection with the Qualitest acquisition, \$108 million of the purchase price was placed into two separate escrow accounts. One of the escrow accounts was \$8 million, some of which was used to fund working capital adjustments, as defined in the Qualitest Stock Purchase Agreement. This escrow was settled during the third quarter of 2011. There is also a \$100 million escrow account that will be used to fund all claims arising out of or related to the Qualitest acquisition.

In connection with the \$100 million escrow account, to the extent that we are able to realize tax benefits for costs that are funded by the escrow account, we will be required to share these tax benefits with Apax.

Qualitest is a manufacturer and distributor of generic drugs and over-the-counter pharmaceuticals throughout the United States. Qualitest's product portfolio is comprised of 175 product families in various forms including tablets, capsules, creams, ointments, suppositories, and liquids. This acquisition has enabled us to gain critical mass in our generics business while strengthening our pain portfolio through a larger breadth of product offerings.

The operating results of Qualitest from November 30, 2010 are included in the accompanying Condensed Consolidated Statements of Operations. The Consolidated Balance Sheet as of September 30, 2011 and December 31, 2010 reflect the acquisition of Qualitest, effective November 30, 2010, the date the Company obtained control of Qualitest.

The following table summarizes the fair values of the assets acquired and liabilities assumed at the Qualitest Acquisition Date (in thousands):

	November 30, 2010 (As initially reported)	Measurement period adjustments	November 30, 2010 (As adjusted)
Cash and cash equivalents	\$ 21,828	\$	\$ 21,828
Accounts receivable	93,228		93,228
Other receivables	1,483		1,483
Inventories	95,000		95,000
Prepaid expenses and other current assets	2,023	(121)	1,902
Deferred income taxes	63,509	5,457	68,966
Property, Plant and equipment	135,807		135,807
Other intangible assets	843,000	(7,000)	836,000
Total identifiable assets	\$ 1,255,878	\$ (1,664)	\$ 1,254,214

Edgar Filing: ENDO PHARMACEUTICALS HOLDINGS INC - Form 10-Q

Accounts payable	\$	27,422	\$	\$	27,422
------------------	----	--------	----	----	--------

**Table of Contents**

	November 30, 2010 (As initially reported)	Measurement period adjustments	November 30, 2010 (As adjusted)
Accrued expenses	55,210	3,852	59,062
Deferred income taxes	207,733	1,519	209,252
Long-term debt	406,758		406,758
Other liabilities	9,370	117	9,487
<b>Total liabilities assumed</b>	<b>\$ 706,493</b>	<b>\$ 5,488</b>	<b>\$ 711,981</b>
Net identifiable assets acquired	\$ 549,385	\$ (7,152)	\$ 542,233
Goodwill	\$ 219,986	\$ 7,828	\$ 227,814
<b>Net assets acquired</b>	<b>\$ 769,371</b>	<b>\$ 676</b>	<b>\$ 770,047</b>

The above estimated fair values of assets acquired and liabilities assumed are provisional and are based on the information that was available as of the Qualitest Acquisition Date. The Company believes that information provides a reasonable basis for estimating the fair values but the Company is waiting for additional information necessary to finalize those amounts, particularly with respect to intangible assets, certain liabilities and deferred income taxes. Thus, the provisional measurements of fair value reflected are subject to change. Such changes could be significant. The Company expects to finalize the valuation and complete the purchase price allocation as soon as practicable but no later than one year from the Qualitest Acquisition Date.

The valuation of the intangible assets acquired and related amortization periods are as follows:

	Valuation (in millions)	Amortization Period (in years)
<b>Developed Technology:</b>		
Hydrocodone and acetaminophen	\$ 119.0	17
Oxycodone and acetaminophen	30.0	17
Promethazine	46.0	16
Isosorbide Mononitrate ER	42.0	16
Multi Vitamins	38.0	16
Trazodone	17.0	16
Butalbital, acetaminophen, and caffeine	25.0	16
Triprevifem	16.0	13
Spiroonolactone	13.0	17
Hydrocortisone	34.0	16
Hydrochlorothiazide	16.0	16
Controlled Substances	52.0	16
Oral Contraceptives	8.0	13
Others	162.0	17
<b>Total</b>	<b>\$ 618.0</b>	<b>16</b>
<b>In Process Research &amp; Development:</b>		
Generics portfolio with anticipated 2011 launch	\$ 63.0	n/a
Generics portfolio with anticipated 2012 launch	30.0	n/a
Generics portfolio with anticipated 2013 launch	17.0	n/a
Generics portfolio with anticipated 2014 launch	88.0	n/a
<b>Total</b>	<b>\$ 198.0</b>	<b>n/a</b>
<b>Tradename:</b>		

Edgar Filing: ENDO PHARMACEUTICALS HOLDINGS INC - Form 10-Q

Qualitest tradename	\$	20.0	15
Total	\$	20.0	15
Total other intangible assets	\$	836.0	n/a

**Table of Contents**

The fair value of the developed technology assets and in-process research and development assets were estimated using an income approach. Under this method, an intangible asset's fair value is equal to the present value of the incremental after-tax cash flows (excess earnings) attributable solely to the intangible asset over its remaining useful life. To calculate fair value, the Company used probability-weighted cash flows discounted at rates considered appropriate given the inherent risks associated with each type of asset. The Company believes that the level and timing of cash flows appropriately reflect market participant assumptions. Cash flows were generally assumed to extend through the shorter of the patent or estimated useful life of the developed technology or in-process research and development asset. The fair value of the Qualitest tradename was estimated using an income approach, specifically known as the relief from royalty method. The relief from royalty method is based on a hypothetical royalty stream that would be received if the Company were to license the Qualitest tradename. Thus, we derived the hypothetical royalty income from the projected revenues of Qualitest.

The \$227.8 million of goodwill was assigned to our Generics segment. The goodwill recognized is attributable primarily to expected purchasing, manufacturing and distribution synergies as well as their assembled workforce. Approximately \$170.4 million of goodwill is expected to be deductible for income tax purposes.

Deferred tax assets of \$69.0 million are related primarily to federal and state net operating loss and credit carryforwards of Qualitest and its subsidiaries. Deferred tax liabilities of \$209.3 million are related primarily to the difference between the book basis and tax basis of identifiable intangible assets.

The Company recognized \$1.7 million and \$6.3 million of Qualitest acquisition-related costs that were expensed during the three and nine months ended September 30, 2011, respectively. These costs are included in Acquisition-related items in the accompanying Condensed Consolidated Statements of Operations and are comprised of the following items (in thousands):

	Acquisition-related Costs Three months ended September 30, 2011	Acquisition-related Costs Nine months ended September 30, 2011
Bank fees	\$	\$
Legal, separation, integration, and other costs	1,677	6,271
<b>Total</b>	<b>\$ 1,677</b>	<b>\$ 6,271</b>

The following supplemental pro forma information presents the financial results as if the acquisition of Qualitest had occurred on January 1, 2010 for the three and nine months ended September 30, 2010. This supplemental pro forma information has been prepared for comparative purposes and does not purport to be indicative of what would have occurred had the acquisition been made on January 1, 2010, nor are they indicative of any future results.

	Three months ended September 30, 2010	Nine months ended September 30, 2010
<b>Pro forma consolidated results (in thousands, except per share data):</b>		
Revenue	\$ 543,799	\$ 1,469,992
Net income attributable to Endo Pharmaceuticals Holdings Inc.	\$ 53,162	\$ 162,949
Basic net income per share	\$ 0.46	\$ 1.40
Diluted net income per share	\$ 0.46	\$ 1.39

These amounts have been calculated after applying the Company's accounting policies and adjusting the results of Qualitest to reflect the additional depreciation and amortization that would have been charged assuming the fair value adjustments primarily to property, plant and equipment and intangible assets, had been applied on January 1, 2010, together with the consequential tax effects.





**Table of Contents****Penwest Pharmaceuticals Co.**

On September 20, 2010 (the Penwest Acquisition Date), the Company completed its tender offer for the outstanding shares of common stock of Penwest and on November 4, 2010, we closed this acquisition for approximately \$171.8 million in aggregate cash consideration, at which time Penwest became our wholly-owned subsidiary. On August 22, 2011, Penwest was merged into Endo Pharmaceuticals Inc., at which time Penwest ceased its existence as a separate legal entity.

This transaction contributes to Endo's core pain management franchise and permits us to maximize the value of our oxycodone franchise.

The operating results of Penwest from September 20, 2010 are included in the accompanying Condensed Consolidated Statements of Operations. The Condensed Consolidated Balance Sheets as of September 30, 2011 and December 31, 2010 reflect the acquisition of Penwest, effective September 20, 2010, the date the Company obtained control of Penwest.

The following table summarizes the fair values of the assets acquired and liabilities assumed at the Penwest Acquisition Date (in thousands):

	September 20, 2010 (As initially reported)	Measurement period adjustments	September 20, 2010 (As adjusted)
Cash and cash equivalents	\$ 22,343	\$	\$ 22,343
Marketable securities	800		800
Accounts receivable	10,885	(19)	10,866
Other receivables	132	(1)	131
Inventories	396	11	407
Prepaid expenses and other current assets	716	(223)	493
Deferred income taxes	27,175	2,590	29,765
Property and equipment	1,115	(200)	915
Other intangible assets	111,200		111,200
Other assets	2,104		2,104
<b>Total identifiable assets</b>	<b>\$ 176,866</b>	<b>\$ 2,158</b>	<b>\$ 179,024</b>
Accounts payable	\$ 229	\$	\$ 229
Income taxes payable	347	(187)	160
Penwest shareholder liability	20,815	(20,815)	
Accrued expenses	1,455	87	1,542
Deferred income taxes	39,951	217	40,168
Other liabilities	4,403	117	4,520
<b>Total liabilities assumed</b>	<b>\$ 67,200</b>	<b>\$ (20,581)</b>	<b>\$ 46,619</b>
<b>Net identifiable assets acquired</b>	<b>\$ 109,666</b>	<b>\$ 22,739</b>	<b>\$ 132,405</b>
Goodwill	\$ 37,952	\$ 1,409	\$ 39,361
<b>Net assets acquired</b>	<b>\$ 147,618</b>	<b>\$ 24,148</b>	<b>\$ 171,766</b>

The above estimated fair values of assets acquired and liabilities assumed are based on the information that was available as of the Penwest Acquisition Date. As of September 30, 2011, our measurement period adjustments are complete.

The valuation of the intangible assets acquired and related amortization periods are as follows (in millions):

**Valuation**

		<b>Amortization Period (in years)</b>
<b>In Process Research &amp; Development:</b>		
Otsuka	\$ 5.5	n/a
A0001	1.6	n/a
Total	\$ 7.1	n/a

**Table of Contents**

	Valuation	Amortization Period (in years)
<b>Developed Technology:</b>		
Opana® ER	\$ 104.1	10
<b>Total</b>	<b>\$ 104.1</b>	<b>10</b>
Total other intangible assets	\$ 111.2	n/a

The fair values of the in-process research and development assets and developed technology asset were estimated using an income approach. To calculate fair value, the Company used probability-weighted cash flows discounted at rates considered appropriate given the inherent risks associated with the asset. The Company believes that the level and timing of cash flows appropriately reflect market participant assumptions. Cash flows were generally assumed to extend through the shorter of the patent or estimated useful life of our developed technology or in-process research and development asset.

The \$39.4 million of goodwill was assigned to our Branded Pharmaceuticals segment. The goodwill recognized is attributable primarily to the control premium associated with our oxymorphone franchise and other factors. None of the goodwill is expected to be deductible for income tax purposes.

Deferred tax assets of \$29.8 million are related primarily to federal net operating loss and credit carryforwards of Penwest. Deferred tax liabilities of \$40.2 million are related primarily to the difference between the book basis and tax basis of the identifiable intangible assets.

The Company recognized \$0.3 million and \$0.5 million of Penwest acquisition-related costs that were expensed during the three and nine months ended September 30, 2011, respectively. The Company also recognized \$6.9 million of Penwest acquisition-related costs that were expensed for both the three and nine month periods ended September 30, 2010. These costs are included in Acquisition-related items in the accompanying Condensed Consolidated Statements of Operations and are comprised of the following items (in thousands):

	Acquisition-related Costs Three and nine months ended September 30, 2010	
Bank fees	\$	3,660
Legal, separation, integration, and other costs		3,255
<b>Total</b>	<b>\$</b>	<b>6,915</b>

Due to the pro forma impacts of eliminating the pre-existing intercompany royalties between Penwest and Endo, which were determined to be at fair value, we have not provided supplemental pro forma information as amounts are not material to the Condensed Consolidated Statements of Operations. We have also considered the impacts of Penwest, since the date we obtained a majority interest, on our Consolidated Statement of Operations and concluded amounts were not material.

***HealthTronics, Inc.***

On July 2, 2010 (the HealthTronics Acquisition Date), the Company completed its initial tender offer for all outstanding shares of common stock of HealthTronics and obtained effective control of HealthTronics. On July 12, 2010, Endo completed its acquisition of HealthTronics for approximately \$214.8 million in aggregate cash consideration for 100% of the outstanding shares, at which time HealthTronics became a wholly-owned subsidiary of the Company. HealthTronics shares were purchased at a price of \$4.85 per HealthTronics Share. In addition, Endo paid \$40 million to retire HealthTronics debt that had been outstanding under its Senior Credit Facility. As a result of the acquisition, the HealthTronics Senior Credit Facility was terminated.

## **Table of Contents**

HealthTronics is a provider of healthcare services and manufacturer of medical devices, primarily for the urology community. The HealthTronics business and applicable services include:

### *Lithotripsy services.*

HealthTronics provides lithotripsy services, which is a medical procedure where a device called a lithotripter transmits high energy shockwaves through the body to break up kidney stones. Lithotripsy services are provided principally through limited partnerships and other entities that HealthTronics manages, which use lithotripters. In 2010, physician partners used our lithotripters to perform approximately 50,000 procedures in the U.S. While the physicians render medical services, HealthTronics does not. As the general partner of limited partnerships or the manager of other types of entities, HealthTronics also provide services relating to operating its lithotripters, including scheduling, staffing, training, quality assurance, regulatory compliance, and contracting with payors, hospitals, and surgery centers.

### *Prostate treatment services.*

HealthTronics provides treatments for benign and cancerous conditions of the prostate. In treating benign prostate disease, HealthTronics deploys three technologies in a number of its partnerships above: (1) photo-selective vaporization of the prostate (PVP), (2) trans-urethral needle ablation (TUNA), and (3) trans-urethral microwave therapy (TUMT). All three technologies apply an energy source which reduces the size of the prostate gland. For treating prostate and other cancers, HealthTronics uses a procedure called cryosurgery, a process which uses lethal ice to destroy tissue such as tumors for therapeutic purposes. In April 2008, HealthTronics acquired Advanced Medical Partners, Inc., which significantly expanded its cryosurgery partnership base. In July 2009, HealthTronics acquired Endocare, Inc., which manufactures both the medical devices and related consumables utilized by its cryosurgery operations and also provides cryosurgery treatments. The prostate treatment services are provided principally by using equipment that HealthTronics leases from limited partnerships and other entities that HealthTronics manages. Benign prostate disease and cryosurgery cancer treatment services are billed in the same manner as its lithotripsy services under either retail or wholesale contracts. HealthTronics also provides services relating to operating the equipment, including scheduling, staffing, training, quality assurance, regulatory compliance, and contracting.

### *Radiation therapy services.*

HealthTronics provided image guided radiation therapy (IGRT) technical services for cancer treatment centers. Its IGRT technical services related to providing the technical (non-physician) personnel to operate a physician practice group's IGRT equipment, leasing IGRT equipment to a physician practice group, providing services related to helping a physician practice group establish an IGRT treatment center, and managing an IGRT treatment center. In September 2011, the IGRT business was sold for approximately \$13.0 million. The impact of this sale was not material to the Company's Condensed Consolidated Statements of Operations.

### *Anatomical pathology services.*

HealthTronics provides anatomical pathology services primarily to the urology community. HealthTronics has one pathology lab located in Georgia, which provides laboratory detection and diagnosis services to urologists throughout the United States. In addition, in July 2008, HealthTronics acquired Uropath LLC, now referred to as HealthTronics Laboratory Solutions, which managed pathology laboratories located at Uropath sites for physician practice groups located in Texas, Florida and Pennsylvania. Through HealthTronics Laboratory Solutions, HealthTronics continues to provide administrative services to in-office pathology labs for practice groups and pathology services to physicians and practice groups with its lab equipment and personnel at the HealthTronics Laboratory Solutions laboratory sites.

### *Medical products manufacturing, sales and maintenance.*

HealthTronics manufactures and sells medical devices focused on minimally invasive technologies for tissue and tumor ablation through cryoablation, which is the use of lethal ice to destroy tissue, such as tumors, for therapeutic purposes. HealthTronics develops and manufactures these devices for the treatment of prostate and renal cancers and our proprietary technologies also have applications across a number of additional markets, including the ablation of tumors in the lung, liver metastases and palliative intervention (treatment of pain associated with

**Table of Contents**

metastases). HealthTronics manufactures the related spare parts and consumables for these devices. HealthTronics also sells and maintains lithotripters and related spare parts and consumables.

The acquisition of HealthTronics reflects Endo's desire to continue expanding our business beyond pain management into complementary medical areas where HealthTronics can be innovative and competitive. We believe this expansion will enable us to be a provider of multiple healthcare solutions and services that fill critical gaps in patient care.

The operating results of HealthTronics from July 2, 2010 are included in the accompanying Condensed Consolidated Statements of Operations. The Condensed Consolidated Balance Sheets as of September 30, 2011 and December 31, 2010 reflect the acquisition of HealthTronics, effective July 2, 2010, the date the Company obtained control of HealthTronics.

The following table summarizes the fair values of the assets acquired and liabilities assumed at the HealthTronics Acquisition Date (in thousands):

	<b>July 2, 2010</b>
Cash and cash equivalents	\$ 6,769
Accounts receivable	33,388
Other receivables	1,006
Inventories	12,399
Prepaid expenses and other current assets	5,204
Deferred income taxes	46,489
Property and equipment	30,687
Other intangible assets	73,124
Other assets	5,210
 Total identifiable assets	 \$ 214,276
Accounts payable	\$ 3,084
Accrued expenses	20,510
Deferred income taxes	22,376
Long-term debt	43,460
Other liabilities	1,785
 Total liabilities assumed	 \$ 91,215
Net identifiable assets acquired	\$ 123,061
Noncontrolling interests	\$ (63,227)
Goodwill	\$ 155,009
 Net assets acquired	 \$ 214,843

The above estimated fair values of assets acquired and liabilities assumed are based on the information that was available as of the HealthTronics Acquisition Date. As of September 30, 2011, our measurement period adjustments are complete.

The valuation of the intangible assets acquired and related amortization periods are as follows:

	<b>Valuation</b>	<b>Amortization</b>
	<b>(in millions)</b>	<b>Period</b>
		<b>(in years)</b>
Endocare Developed Technology	\$ 46.3	10
HealthTronics Tradename	14.6	15

Edgar Filing: ENDO PHARMACEUTICALS HOLDINGS INC - Form 10-Q

Service Contract(1)	12.2	n/a
Total	\$ 73.1	n/a

**Table of Contents**

(1) This intangible asset relates to our IGRT business, which was sold in September 2011 for approximately \$13.0 million. Accordingly, the carrying amount of this asset was reduced to zero at the time of sale.

The fair value of the developed technology asset was estimated using a discounted present value income approach. Under this method, an intangible asset's fair value is equal to the present value of the incremental after-tax cash flows (excess earnings) attributable solely to the intangible asset over its remaining useful life. To calculate fair value, the Company used probability-weighted cash flows discounted at rates considered appropriate given the inherent risks associated with each type of asset. The Company believes that the level and timing of cash flows appropriately reflect market participant assumptions. Cash flows were assumed to extend through the patent life of the purchased technology. The fair value of the HealthTronics Tradename was estimated using an income approach, specifically known as the relief from royalty method. The relief from royalty method is based on a hypothetical royalty stream that would be received if the Company were to license the HealthTronics Tradename. Thus, we derived the hypothetical royalty income from the projected revenues of HealthTronics' services.

HealthTronics has investments in partnerships and limited liability companies (LLCs) where we, as the general partner or managing member, exercise effective control. Accordingly, we consolidate various entities where we do not own 100% of the entity in accordance with the accounting consolidation principles. As a result, we are required to fair value the noncontrolling interests as part of our purchase price allocation. To calculate fair value, the Company used historical transactions which represented Level 2 data points within the fair value hierarchy to calculate applicable multiples of each respective noncontrolling interest in the partnerships and LLCs.

The \$155.0 million of goodwill was assigned to our Devices and Services segment. The goodwill recognized is attributable primarily to strategic and synergistic opportunities across the HealthTronics network of urology partnerships, expected corporate synergies, the assembled workforce of HealthTronics and other factors. Approximately \$33.6 million of goodwill is expected to be deductible for income tax purposes.

Deferred tax assets of \$46.5 million are related primarily to federal net operating loss and credit carryforwards of HealthTronics and its subsidiaries. Deferred tax liabilities of \$22.4 million are related primarily to the difference between the book basis and tax basis of identifiable intangible assets.

The Company recognized \$2.9 million of HealthTronics acquisition-related costs that were expensed during the nine months ended September 30, 2011. There were no HealthTronics acquisition-related costs expensed during the three months ended September 30, 2011. These costs are included in Acquisition-related items in the accompanying Condensed Consolidated Statements of Operations and are comprised of the following items (in thousands):

	<b>Acquisition-related Costs Nine months ended September 30, 2011</b>	
Bank fees	\$	
Legal, separation, integration, and other costs		2,861
<b>Total</b>	<b>\$</b>	<b>2,861</b>



**Table of Contents**

The Company recognized \$15.3 million and \$20.0 million of HealthTronics acquisition-related costs that were expensed during the three and nine months ended September 30, 2010, respectively. These costs are included in Acquisition-related items in the accompanying Condensed Consolidated Statements of Operations and are comprised of the following items (in thousands):

	Acquisition-related Costs	
	Three months ended September 30, 2010	Nine months ended September 30, 2010
Bank fees	\$ 5,230	\$ 5,230
Acceleration of outstanding HealthTronics stock-based compensation	7,924	7,924
Legal, separation, integration, and other costs	2,113	6,866
Total	\$ 15,267	\$ 20,020

The following supplemental pro forma information presents the financial results as if the acquisition of HealthTronics had occurred on January 1, 2010 for the nine months ended September 30, 2010. This supplemental pro forma information has been prepared for comparative purposes and does not purport to be indicative of what would have occurred had the acquisition been made on January 1, 2010, nor are they indicative of any future results.

	Nine months ended September 30, 2010
<b>Pro forma consolidated results (in thousands, except per share data):</b>	
Revenue	\$ 1,303,728
Net income attributable to Endo Pharmaceuticals Holdings Inc.	\$ 171,180
Basic net income per share	\$ 1.47
Diluted net income per share	\$ 1.46

These amounts have been calculated after applying the Company's accounting policies and adjusting the results of HealthTronics to reflect the additional depreciation and amortization that would have been charged assuming the fair value adjustments primarily to property, plant and equipment, and intangible assets, had been applied on January 1, 2010, together with the consequential tax effects.

**NOTE 6. SEGMENT RESULTS**

As a result of our 2010 acquisitions, the Company realigned its internal management reporting in 2010 to reflect a total of three reportable segments. These segments reflect the level at which executive management regularly reviews financial information to assess performance and to make decisions about resources to be allocated.

The three reportable business segments in which the Company now operates include: (1) Branded Pharmaceuticals, (2) Generics and (3) Devices and Services. Each segment derives revenue from the sales or licensing of their respective products or services and is discussed below.

**Branded Pharmaceuticals**

This group of products includes a variety of branded prescription products related to treating and managing pain as well as our urology, endocrinology and oncology products. The marketed products that are included in this operating segment include Lidoderm®, Opana® ER and Opana®, Percocet®, Voltaren® Gel, Frova®, Supprelin® LA, Vantas®, Valstar®, and Fortesta™ Gel.

**Table of Contents****Generics**

This segment is comprised of our legacy Endo non-branded generic portfolio and the portfolio from our recently acquired Qualitest business. Our generics business has historically focused on selective generics related to pain that have one or more barriers to market entry, such as complex formulation, regulatory or legal challenges or difficulty in raw material sourcing. With the addition of Qualitest, the segment's product offerings now include products in the pain management, urology, central nervous system (CNS) disorder, immunosuppression, oncology, and hypertension markets, among others.

**Devices and Services**

The Devices and Services operating segment provides urological services, products and support systems to urologists, hospitals, surgery centers and clinics across the United States. These services and products are sold through the following eight business lines: men's health, women's health, BPH therapy, lithotripsy services, prostate treatment services, radiation therapy services, anatomical pathology services, and medical products manufacturing, sales and maintenance. These business lines are discussed in greater detail within Note 5.

In 2010, the Company began to evaluate segment performance based on each segment's adjusted income (loss) before income tax. We define adjusted income (loss) before income tax as income (loss) before income tax before certain upfront and milestone payments to partners, acquisition-related items, cost reduction initiatives, asset impairment charges, amortization of intangible assets related to marketed products and customer relationships, inventory step-up recorded as part of our acquisitions, non-cash interest expense, and certain other items that the Company believes do not reflect its core operating performance. Certain corporate general and administrative expenses are not allocated and are therefore included within Corporate unallocated. We calculate consolidated adjusted income (loss) before income tax by adding the adjusted income (loss) before income tax of each of our reportable segments to corporate unallocated adjusted income (loss) before income tax.

The following represents selected information for the Company's reportable segments for the three and nine months ended September 30, 2011 and 2010 (in thousands):

	Three months ended September 30,		Nine months ended September 30,	
	2011	2010	2011	2010
Net revenues to external customers				
Branded Pharmaceuticals	\$ 425,511	\$ 364,986	\$ 1,199,292	\$ 1,072,362
Generics	147,975	27,431	415,431	80,991
Devices and Services	185,592	51,686	311,992	51,686
<b>Total consolidated net revenues to external customers</b>	<b>\$ 759,078</b>	<b>\$ 444,103</b>	<b>\$ 1,926,715</b>	<b>\$ 1,205,039</b>
Adjusted income (loss) before income tax				
Branded Pharmaceuticals	\$ 231,887	\$ 187,630	\$ 634,762	\$ 540,741
Generics	26,932	2,605	74,445	8,916
Devices and Services	54,755	20,479	94,670	20,479
Corporate unallocated	(93,844)	(50,316)	(217,145)	(138,605)
<b>Total consolidated adjusted income before income tax</b>	<b>\$ 219,730</b>	<b>\$ 160,398</b>	<b>\$ 586,732</b>	<b>\$ 431,531</b>

The table below provides reconciliations of our consolidated adjusted income (loss) before income tax to our consolidated income before income tax, which is determined in accordance with U.S. generally accepted accounting principles (GAAP), for the three and nine months ended September 30, 2011 and 2010 (in thousands):

	Three months ended September 30,		Nine months ended September 30,	
	2011	2010	2011	2010
Total consolidated adjusted income before income tax	\$ 219,730	\$ 160,398	\$ 586,732	\$ 431,531
Upfront and milestone payments to partners	(2,355)	(309)	(27,346)	(19,200)

Edgar Filing: ENDO PHARMACEUTICALS HOLDINGS INC - Form 10-Q

Acquisition-related items	(5,818)	(24,990)	(29,517)	(31,315)
---------------------------	---------	----------	----------	----------

**Table of Contents**

	Three months ended September 30,		Nine months ended September 30,	
	2011	2010	2011	2010
Cost reduction initiatives and separation benefits	(13,603)	(7,050)	(17,598)	(16,570)
Impairment of long-lived assets	(22,691)		(22,691)	(13,000)
Amortization of intangible assets related to marketed products and customer relationships	(58,846)	(19,378)	(136,501)	(53,730)
Inventory step-up	(23,937)	(1,414)	(40,718)	(1,414)
Non-cash interest expense	(4,754)	(4,245)	(14,014)	(12,507)
Loss on extinguishment of debt, net			(8,548)	
Gain on hedging activities for foreign currencies	2,636		2,636	
Other (expense) income, net				(239)
<b>Total consolidated income before income tax</b>	<b>\$ 90,362</b>	<b>\$ 103,012</b>	<b>\$ 292,435</b>	<b>\$ 283,556</b>

The following represents additional selected financial information for our reportable segments three and nine months ended September 30, 2011 and 2010 (in thousands):

	Three months ended September 30,		Nine months ended September 30,	
	2011	2010	2011	2010
<b>Depreciation expense</b>				
Branded Pharmaceuticals	\$ 3,110	\$ 3,125	\$ 9,552	\$ 9,719
Generics	3,461	266	8,645	675
Devices and Services	5,000	3,063	11,389	3,063
Corporate unallocated	880	840	2,649	2,222
<b>Total depreciation expense</b>	<b>\$ 12,451</b>	<b>\$ 7,294</b>	<b>\$ 32,235</b>	<b>\$ 15,679</b>
<b>Amortization expense</b>				
Branded Pharmaceuticals	\$ 26,101	\$ 18,209	\$ 78,361	\$ 52,779
Generics	9,728		29,325	
Devices and Services	23,168	1,401	29,266	1,401
<b>Total amortization expense</b>	<b>\$ 58,997</b>	<b>\$ 19,610</b>	<b>\$ 136,952</b>	<b>\$ 54,180</b>

Asset information is not accounted for at the segment level and consequently is not reviewed or included within our internal management reporting. Therefore, the Company has not disclosed asset information for each reportable segment.

**NOTE 7. INCOME TAXES**

The effective income tax rate on earnings from continuing operations before income taxes was 37.7% and 34.3% for the three and nine months ended September 30, 2011, respectively, compared to 32.6% and 36.1% for the three and nine months ended September 30, 2010, respectively.

Income tax for the three month period ended September 30, 2011 increased 2% to \$34.1 million from the comparable 2010 period. This increase is due to an increase in the effective income tax rate to 37.7% from 32.6% in the comparable 2010 period, offset by a decrease in pre-tax income. The increase in the effective income tax rate is primarily due to the establishment of a valuation allowance in the current period against an anticipated capital loss on our cost method investment in a privately-held company and an increase in the non-deductible charge for the Branded Prescription Drug fee. The increase is partially offset by the release of FIN 48 reserves due to statute of limitation expirations, an increase in the Domestic Production Activities deduction, the inclusion of transaction costs on acquisitions in the comparable 2010 period, a benefit from the Research and Development credit that was expired during the comparable 2010 period, and an increase in the Orphan Drug credit.

Income tax for the nine months ended September 30, 2011, decreased 2% from the comparable 2010 period to \$100.3 million. This fluctuation is due to the decrease in our effective income tax rate to 34.3% from 36.1% in the comparable 2010 period. The decrease in the effective income tax rate is primarily due to non-taxable income attributable to noncontrolling interests assumed as part of the HealthTronics acquisition, the release of FIN 48 reserves due to statute of limitation expirations, an increase in the Domestic Production Activities deduction, a benefit from

## Edgar Filing: ENDO PHARMACEUTICALS HOLDINGS INC - Form 10-Q

non-taxable reductions in the fair value of contingent consideration as compared to non-deductible increases in the fair value in the comparable prior period, a benefit from the Research and Development credit that was expired during the comparable 2010 period, and an increase in the Orphan Drug credit, partially offset by the establishment of a valuation allowance in the current period against an anticipated capital loss on our cost method investment in a privately-held company, and an increase in the non-deductible charge for the Branded Prescription Drug fee.

---

**Table of Contents**

**NOTE 8. LICENSE AND COLLABORATION AGREEMENTS**

***Commercial Products***

*Novartis AG and Novartis Consumer Health, Inc.*

On March 4, 2008, we entered into a License and Supply Agreement (the Voltaren® Gel Agreement) with and among Novartis AG and Novartis Consumer Health, Inc (Novartis) to obtain the exclusive U.S. marketing rights for the prescription medicine Voltaren® Gel (Voltaren® Gel or Licensed Product). Voltaren® Gel received regulatory approval in October 2007 from the U.S. Food and Drug Administration (the FDA), becoming the first topical prescription treatment for use in treating pain associated with osteoarthritis and the first new product approved in the U.S. for osteoarthritis since 2001. Voltaren® Gel was granted marketing exclusivity in the U.S. as a prescription medicine until October 2010.

Under the terms of the five-year Voltaren® Gel Agreement, Endo made an upfront cash payment of \$85 million. Endo has agreed to pay royalties to Novartis on annual Net Sales of the Licensed Product, subject to certain thresholds as defined in the Voltaren® Gel Agreement. In addition, Endo has agreed to make certain guaranteed minimum annual royalty payments of \$30 million per year payable in the fourth and fifth year of the Voltaren® Gel Agreement, subject to certain limitations including the launch of a generic to the Licensed Product in the United States. These guaranteed minimum royalties will be creditable against royalty payments on an annual basis such that Endo's obligation with respect to each year is to pay the greater of (i) royalties payable based on annual net sales of the Licensed Product or (ii) the guaranteed minimum royalty for such Voltaren® Gel Agreement year. No royalty payments were made to Novartis during the three or nine months ended September 30, 2011 or 2010. Novartis is also eligible to receive a one-time milestone payment of \$25 million if annual net sales of Voltaren® Gel exceed \$300 million in the U.S. The \$85 million upfront payment and the present value of the guaranteed minimum royalties have been capitalized as an intangible asset in the amount of \$129 million, representing the fair value of the exclusive license to market Voltaren® Gel. We are amortizing this intangible asset into cost of revenues over its estimated five-year useful life.

Endo is solely responsible to commercialize the Licensed Product during the term of the Voltaren® Gel Agreement. With respect to each year during the term of the Voltaren® Gel Agreement, Endo is required to incur a minimum amount of annual advertising and promotional expenses on the commercialization of the Licensed Product, subject to certain limitations. In addition, Endo is required to perform a minimum number of face-to-face one-on-one discussions with physicians and other healthcare practitioners (Details) for the purpose of promoting the Licensed Product within its approved indication during each year of the Voltaren® Gel Agreement. Further, during the term of the Voltaren® Gel Agreement, Endo will share in the costs of certain clinical studies and development activities initiated at the request of the FDA or as considered appropriate by Novartis and Endo.

During the term of the Voltaren® Gel Agreement, Endo has agreed to purchase all of its requirements for the Licensed Product from Novartis. The price was fixed for the first year and subject to annual changes based upon changes in the producer price index and raw materials.

Novartis has the exclusive right, at its sole discretion, to effect a switch of the Licensed Product from a prescription product to an over-the-counter (OTC) product in the United States (an OTC Switch) by filing an amendment or supplement to the Licensed Product New Drug Application or taking any other action necessary or advisable in connection therewith to effect the OTC Switch, and thereafter to commercialize such OTC product. Notwithstanding the foregoing, Novartis shall not launch an OTC equivalent product prior to a time specified in the Voltaren® Gel Agreement, and Novartis shall not take any action that results in the loss of the prescription product status for the Licensed Product prior to such time. Novartis will notify Endo if it submits a filing to the FDA in respect of an OTC equivalent product. In the event that Novartis gains approval of an OTC equivalent product that results in the Licensed Product being declassified as a prescription product, then Novartis will make certain royalty payments to Endo on net sales of such OTC equivalent product in the United States by Novartis, its affiliates and their respective licensees or sublicensees as set forth in the Voltaren® Gel Agreement. As a condition to the payment of any and all such royalties, net sales of the Licensed Product in the United States must have exceeded a certain threshold prior to the launch of the OTC equivalent product by Novartis or its affiliates.

The initial term of the Voltaren® Gel Agreement will expire on June 30, 2013. Endo has the option to extend the Voltaren® Gel Agreement for two successive one year terms. The Voltaren® Gel Agreement will remain in place after the first two renewal terms unless either party provides written notice of non-renewal to the other party at least

**Table of Contents**

six months prior to the expiration of any renewal term after the first renewal term or the Voltaren® Gel Agreement is otherwise terminated in accordance with its terms. Among other standard and customary termination rights granted under the Voltaren® Gel Agreement, the Voltaren® Gel Agreement can be terminated by either party upon reasonable written notice, if either party has committed a material breach that has not been remedied within ninety (90) days from the giving of written notice. Endo may terminate the Voltaren® Gel Agreement by written notice upon the occurrence of several events, including the launch in the United States of a generic to the Licensed Product. Novartis may terminate the Voltaren® Gel Agreement upon reasonable written notice (1) if Endo fails to deliver a set percentage of the minimum Details in any given six-month period under the Voltaren® Gel Agreement; or (2) on or after the launch in the United States of an OTC equivalent product by Novartis, its affiliates or any third party that does not result in the declassification of the Licensed Product as a prescription product, following which net sales in any six-month period under the Voltaren® Gel Agreement are less than a certain defined dollar amount.

*Hind Healthcare Inc.*

In November 1998, Endo entered into a license agreement (the Hind License Agreement) with Hind Healthcare Inc. (Hind), for the sole and exclusive right to develop, use, market, promote and sell Lidoderm® in the United States. Under the terms of the Hind License Agreement, Endo paid Hind approximately \$10 million based upon the achievement of certain milestones and capitalized this amount as an intangible asset representing the fair value of these exclusive rights. In addition, Endo pays Hind nonrefundable royalties based on net sales of Lidoderm®. Royalties are recorded as a reduction to net sales due to the nature of the license agreement and the characteristics of the license involvement by Hind in Lidoderm®. The royalty rate is 10% of net sales through the shorter of (1) the expiration of the last licensed patent or (2) November 2011, including a minimum royalty of at least \$500,000 per year. During the nine month periods ended September 30, 2011 and 2010 we recorded \$64.5 million and \$63.7 million for these royalties to Hind, respectively, which we recorded as a reduction to net pharmaceutical product sales. At September 30, 2011 and December 31, 2010, \$22.9 million and \$23.0 million, respectively, is recorded as a royalty payable and included in accounts payable in the accompanying Condensed Consolidated Balance Sheets. In March 2002, we extended this license with Hind to cover Lidoderm® in Canada and Mexico.

*Vernalis Development Limited*

In July 2004, we entered into a License Agreement with Vernalis Development Limited (Vernalis) under which Vernalis agreed to license, exclusively to us, rights to market frovatriptan succinate (Frova®) in North America (the Vernalis License Agreement). Frova® was launched June 2002 in the U.S. and indicated for the acute treatment of migraine headaches in adults. Under the terms of the Vernalis License Agreement, we paid Vernalis an upfront fee of \$30 million and annual \$15 million payments each in 2005 and 2006. We capitalized the \$30 million up-front payment, the present value of the two \$15 million anniversary payments. We are amortizing this intangible asset into cost of revenues on a straight-line basis over its estimated life of twelve and one-half years.

In addition, Vernalis could receive one-time milestone payments for the achievement of defined annual net sales targets. These sales milestone payments increase based on increasing net sales targets ranging from a milestone of \$10 million on \$200 million in net sales to a milestone of \$75 million on \$1.2 billion in net sales. These sales milestones could total up to \$255 million if all of the defined net sales targets are achieved. Beginning on January 1, 2007, we began paying royalties to Vernalis based on the net sales of Frova®. The term of the license agreement is for the shorter of the time (i) that there are valid claims on the Vernalis patents covering Frova® or there is market exclusivity granted by a regulatory authority, whichever is longer, or (ii) until the date on which a generic version of Frova® is first offered, but in no event longer than 20 years. We can terminate the license agreement under certain circumstances, including upon one years' written notice. In July 2007, Vernalis and Endo entered into an Amendment (Amendment No. 3) to the License Agreement dated July 14, 2004. Under Amendment No. 3, Vernalis granted an exclusive license to Endo to make, have made, use, commercialize and have commercialized Frova® in Canada, under the Canadian Trademark.

In February 2008, we entered into Amendment No. 4 to the Vernalis License Agreement (Amendment No. 4). In addition to amending certain specific terms and conditions of the License Agreement, Amendment No. 4 sets forth an annual minimum net sales threshold such that no royalties will be due on annual U.S. net sales of Frova® less than \$85 million. Prior to this amendment, royalties were payable by us to Vernalis on all net sales of Frova® in

## **Table of Contents**

the United States. Now, once the annual minimum net sales amount is reached, royalty payments will be due only on the portion of annual net sales that exceed the \$85 million threshold.

On August 15, 2011, the parties amended the Vernalis License Agreement (Amendment No. 5). Pursuant to Amendment No. 5, Vernalis assigned to the Company certain patents which were previously exclusively licensed by the Company. Amendment No. 5 did not alter the financial arrangement between the parties.

### *The Population Council*

The Company markets certain of its products utilizing the hydrogel polymer technology pursuant to an agreement between Indevus (now, Endo Pharmaceuticals Solutions Inc.) and the Population Council. Unless earlier terminated by either party in the event of a material breach by the other party, the term of the agreement is the shorter of twenty-five years from October 1997 or until the date on which The Population Council receives approximately \$40 million in payments from the Company. The Company is required to pay to The Population Council 3% of its net sales of Vantas<sup>®</sup> and any polymer implant containing a luteinizing hormone-releasing hormone (LHRH) analog. We are also obligated to pay royalties to the Population Council ranging from 0.5% of net sales to 4% of net sales under certain conditions. We are also obligated to pay the Population Council 30% of certain profits and payments received in certain territories by the Company from the licensing of Vantas<sup>®</sup> or any other polymer implant containing an LHRH analog and 5% for other implants.

### *Strakan International Limited*

In August 2009, we entered into a License and Supply Agreement with Strakan International Limited, a subsidiary of ProStrakan Group plc. (ProStrakan), which was subsequently acquired by Kyowa Hakko Kirin Co. Ltd., for the exclusive right to commercialize Fortesta<sup>™</sup> Gel in the U.S. (the ProStrakan Agreement). Fortesta<sup>™</sup> Gel, a patented two percent (2%) testosterone transdermal gel for testosterone replacement therapy in male hypogonadism. A metered dose delivery system permits accurate dose adjustment to increase the ability to individualize patient treatment. Under the terms of the ProStrakan Agreement, Endo paid ProStrakan an up-front cash payment of \$10 million, which was recorded as research and development expense.

The Company received FDA approval in December 2010, which triggered a one-time approval milestone to ProStrakan for \$12.5 million. The approval milestone was recorded as an intangible asset and is being amortized into cost of revenues on a straight-line basis over its estimated useful life. An additional milestone payment of \$7.5 million was triggered during the second quarter of 2011 pursuant to the terms of the ProStrakan Agreement. The \$7.5 million milestone was recorded to cost of revenues for the three months ended June 30, 2011. ProStrakan could potentially receive up to approximately \$167.5 million in additional payments linked to the achievement of future commercial milestones related to Fortesta<sup>™</sup> Gel.

ProStrakan will exclusively supply Fortesta<sup>™</sup> Gel to Endo at a supply price based on a percentage of annual net sales subject to a minimum floor price as defined in the ProStrakan Agreement. Endo may terminate the ProStrakan Agreement upon six months' prior written notice at no cost to the Company.

### *Products in Development*

#### *Grünenthal GMBH*

In February 2009, we entered into a Development, License and Supply Agreement (the Grünenthal Axomadol Agreement) with Grünenthal GMBH (Grünenthal), granting us the exclusive right in North America to develop and market Grünenthal's investigational drug, axomadol. In June 2011, we announced topline results from a Phase II study comparing the novel investigational drug axomadol against placebo in the treatment of patients with moderate to severe chronic lower back pain. The results indicated that axomadol did not meet predetermined study endpoints. In August 2011, we terminated the Grünenthal Axomadol Agreement, effective August 17, 2011.

In December 2007, we entered into a License, Development and Supply Agreement (the Grünenthal Oxymorphone Agreement) with Grünenthal for the exclusive clinical development and commercialization rights in Canada and the United States for a new oral formulation of long-acting oxymorphone, which is designed to be crush resistant. Under the terms of this agreement Grünenthal is responsible for development efforts to conduct pharmaceutical formulation development and will manufacture any such product or products which obtain FDA approval. Endo is responsible for conducting clinical development activities and for all development costs incurred to obtain regulatory approval. Under the terms of the Grünenthal Oxymorphone Agreement, we paid approximately \$4.9 million for the successful completion of a clinical milestone in 2010, which was recorded as research and





---

## **Table of Contents**

development expense. Additional payments of approximately 59.2 million euros (approximately \$80.5 million at September 30, 2011) may become due upon achievement of predetermined regulatory and commercial milestones. Endo will also make payments to Grünenthal based on net sales of any such product or products commercialized under this agreement.

### *Impax Laboratories, Inc.*

In June 2010, the Company entered into a Development and Co-Promotion Agreement (the Impax Agreement) with Impax Laboratories, Inc. (Impax), whereby the Company was granted a royalty-free license for the co-exclusive rights to co-promote a next generation Parkinson's disease product. Under the terms of the Impax Agreement, Endo paid Impax an upfront payment of \$10 million in 2010, which was recorded as research and development expense. The Company could be obligated to pay up to approximately \$30 million in additional payments linked to the achievement of future clinical, regulatory, and commercial milestones related to the development product. Prior to the completion of Phase III trials, Endo may only terminate the Impax Agreement upon a material breach.

### *Bioniche Life Sciences Inc.*

In July 2009, the Company entered into a License, Development and Supply Agreement (the Bioniche Agreement) with Bioniche Life Sciences Inc. and Bioniche Urology Inc. (collectively, Bioniche), whereby the Company licensed from Bioniche the exclusive rights to develop and market Bioniche's proprietary formulation of Mycobacterial Cell Wall-DNA Complex (MCC), known as Urocidin<sup>TM</sup>, in the U.S. with an option for global rights. We exercised our option for global rights in the first quarter of 2010. Urocidin<sup>TM</sup> is a patented formulation of MCC developed by Bioniche for the treatment of non-muscle-invasive bladder cancer that is currently undergoing Phase III clinical testing. Under the terms of the Bioniche Agreement, Endo paid Bioniche an up-front cash payment of \$20.0 million in July 2009 and milestone payments of \$4.0 million in 2010 resulting from the achievement of contractual milestones, both of which were recorded as research and development expense. In addition, Bioniche could potentially receive up to approximately \$67.0 million and \$29.0 million in additional payments linked to the achievement of future clinical, regulatory, and commercial milestones related to two separate indications for Urocidin<sup>TM</sup>. Bioniche will manufacture Urocidin<sup>TM</sup> and receive a transfer price for supply based on a percentage of Endo's annual net sales of Urocidin<sup>TM</sup>. Endo may terminate the Bioniche Agreement upon 180 days' prior written notice.

### *BayerSchering*

In July 2005, Indevus (now, Endo Pharmaceuticals Solutions Inc.) licensed exclusive U.S. rights from Schering AG, Germany, now BayerSchering Pharma AG (BayerSchering) to market a long-acting injectable testosterone preparation for the treatment of male hypogonadism that we refer to as Aved<sup>TM</sup> (the BayerSchering Agreement). The Company is responsible for the development and commercialization of Aved<sup>TM</sup> in the United States. BayerSchering is responsible for manufacturing and supplying the Company with finished product. As part of the BayerSchering Agreement, Indevus agreed to pay to BayerSchering up to \$30.0 million in up-front, regulatory milestone, and commercialization milestone payments, including a \$5.0 million payment due upon approval by the FDA to market Aved<sup>TM</sup>. Indevus also agreed to pay to BayerSchering 25% of net sales of Aved<sup>TM</sup> to cover both the cost of finished product and royalties. The BayerSchering Agreement expires ten years from the first commercial sale of Aved<sup>TM</sup>. Either party may also terminate the BayerSchering Agreement in the event of a material breach by the other party.

In October 2006, Indevus entered into a supply agreement with BayerSchering pursuant to which BayerSchering agreed to manufacture and supply Indevus with all of its requirements for Aved<sup>TM</sup> for a supply price based on net sales of Aved<sup>TM</sup>. The supply price is applied against the 25% of net sales owed to BayerSchering pursuant to the BayerSchering Agreement. The BayerSchering Agreement expires ten years after the first commercial sale of Aved<sup>TM</sup>.

### *Sanofi-Aventis*

In February 1994, Indevus (now, Endo Pharmaceuticals Solutions Inc.) licensed from Rhone-Poulenc Rorer, S.A., now Aventis Pharma S.A. (Sanofi-Aventis), exclusive, worldwide rights for the manufacture, use and sale of pegoclone under patent rights and know-how related to the drug, except that Indevus granted Sanofi-Aventis an

**Table of Contents**

option to sublicense, under certain conditions, rights to market paxlovid in France. Indevus paid Sanofi-Aventis a license fee and agreed to make milestone payments based on clinical and regulatory developments, and to pay royalties based on net sales through the expiration of the composition of matter patent. If sublicensed, the Company would pay to Sanofi-Aventis a portion of receipts from the sublicensee in lieu of payments. Under the terms of the agreement with Sanofi-Aventis, the Company is responsible for all costs of developing, manufacturing, and marketing paxlovid. This agreement expires with respect to each country upon the last to expire applicable patent. Additionally either party may also terminate this agreement in the event of a material breach by the other party. The Company could owe an additional \$11.1 million if certain clinical and regulatory development milestones are achieved, as well as royalties on net sales or a percentage of royalties it receives if the product is sublicensed.

*Hydron Technologies, Inc.*

In November 1989, GP Strategies Corporation (GP Strategies), then known as National Patent Development Corporation, entered into an agreement (the Hydron Agreement) with Dento-Med Industries, Inc., now known as Hydron Technologies, Inc. In June 2000, Valera Pharmaceuticals, Inc. (Valera, now a wholly-owned subsidiary of the Company known as Endo Pharmaceuticals Valera Inc.) entered into a contribution agreement with GP Strategies, pursuant to which Valera acquired the assets of GP Strategies' drug delivery business, including all intellectual property, and all of GP Strategies' rights under the Hydron Agreement, and certain other agreements with The Population Council and Shire US, Inc.

Pursuant to the Hydron Agreement, the Company has the exclusive right to manufacture, sell and distribute any prescription drug or medical device and certain other products made with hydrogel polymer technology. Hydron Technologies retained an exclusive, worldwide license to manufacture, market, or use products composed of, or produced with the use of, hydrogel polymer technology in certain consumer and oral health fields. Neither party is prohibited from manufacturing, exploiting, using or transferring the rights to any new non-prescription drug product containing hydrogel polymer technology, subject to certain exceptions, for limited exclusivity periods. Subject to certain conditions and exceptions, the Company is obligated to supply certain types of polymer to Hydron Technologies and Hydron Technologies is obligated to purchase such products from the Company. Under the Hydron Agreement, the Company also has the title to the Hydron® trademark and must maintain such trademark throughout the world. The Company has decided to stop using the Hydron® trademark and will transfer the title to such trademark to Hydron Technologies pursuant to the Hydron Agreement. This agreement continues indefinitely, unless terminated earlier by the parties. Each party may owe royalties up to 5% to the other party on certain products under certain conditions.

*Orion Corporation*

In January 2011, the Company entered into a Discovery, Development and Commercialization Agreement (the 2011 Orion Agreement) with Orion Corporation (Orion) to exclusively co-develop products for the treatment of certain cancers and solid tumors. Under the terms of the 2011 Orion Agreement, Endo and Orion each contributed four research programs to the collaboration to be conducted pursuant to the agreement. The development of each research program shall initially be the sole responsibility of the contributing party. However, upon the achievement of certain milestones, the non-contribution party shall have the opportunity to, at its option, obtain a license to jointly develop and commercialize any research program contributed by the other party for amounts defined in the 2011 Orion Agreement. Subject to certain limitations, upon the first commercial sale of any successfully launched jointly developed product, Endo shall be obligated to pay royalties to Orion based on net sales of the corresponding product in North America (the Endo territory) and Orion shall be obligated to pay royalties to Endo on net sales of the corresponding product in certain European countries (the Orion territory). The 2011 Orion Agreement shall expire in January 2016, unless terminated early or extended pursuant to the terms of the agreement. In January 2011, Endo exercised its option to obtain a license to jointly develop and commercialize Orion's Anti-Androgen program focused on castration-resistant prostate cancer, one of Orion's four contributed research programs, and made a corresponding payment to Orion for \$10 million, which was expensed in the first quarter of 2011.

*Teva Pharmaceutical Industries Ltd*

On November 30, 2010 (the Qualitest Acquisition Date), Endo acquired Qualitest, which was party to an asset purchase agreement with Teva Pharmaceutical Industries Ltd (Teva) (the Teva Agreement). Pursuant to the Teva Agreement, Qualitest purchased certain pipeline generic products from Teva and could be obligated to pay

**Table of Contents**

consideration to Teva upon the achievement of certain future regulatory milestones. At September 30, 2011, the maximum amount we could be obligated to pay under the Teva Agreement is \$12.5 million.

*EpiCept Corp.*

In December 2003, we entered into a license granting us exclusive, worldwide rights to certain patents of EpiCept Corp. (EpiCept) as well as exclusive, worldwide commercialization rights to EpiCept's LidoPAIN<sup>®</sup> BP product (EpiCept Agreement). The EpiCept Agreement provides for Endo to pay EpiCept milestones as well as royalties on the net sales of EpiCept's LidoPAIN<sup>®</sup> BP product. Under this Agreement, we made an upfront payment to EpiCept of \$7.5 million which we capitalized as an intangible asset representing the fair value of the exclusive right and the patents. We are amortizing this intangible asset over its useful life of thirteen (13) years. EpiCept has also retained an option to co-promote the LidoPAIN<sup>®</sup> BP product. Milestone payments made by Endo under this agreement, including regulatory milestones and sales thresholds, could total up to \$82.5 million. In addition, the EpiCept Agreement also contains terms and conditions customary for this type of arrangement, including representations, warranties, indemnities and termination rights. The EpiCept Agreement generally lasts until the underlying patents expire. In January 2009, EpiCept announced that it was discontinuing all drug discovery activities including the development of LidoPAIN<sup>®</sup> BP. However, the Company intends to maintain its patent rights conveyed by the EpiCept Agreement.

*Other*

We have entered into certain other collaboration and discovery agreements with third parties for the development of pain management and other products. These agreements require us to share in the development costs of such products and grant marketing rights to us for such products.

We have also licensed from universities and other similar firms rights to certain technologies or intellectual property generally in the field of pain management. We are generally required to make upfront payments as well as other payments upon successful completion of regulatory or sales milestones. In addition, these agreements generally require us to pay royalties on sales of the products arising from these agreements. These agreements generally permit Endo to terminate the agreement with no significant continuing obligation.

**NOTE 9. GOODWILL AND OTHER INTANGIBLE**

Changes in the carrying amount of our goodwill for the nine months ended September 30, 2011, are as follows:

<b>(in thousands)</b>	<b>Gross carrying amount</b>
Balance at December 31, 2010	\$ 715,005
Goodwill acquired during the period	1,779,906
Measurement period adjustments	4,280

**Table of Contents**

(in thousands)	Gross carrying amount
Effect of currency translation	(2,332)
Balance at September 30, 2011	\$ 2,496,859

In June 2011, we acquired AMS. As a result of this acquisition, we recognized goodwill of approximately \$1.7 billion. This acquisition is discussed in greater detail in Note 5. In September 2011, we acquired a small electronic medical records software company. The remaining goodwill acquired during the period relates to immaterial acquisitions in 2011.

Our other intangible assets consist of the following at September 30, 2011 and December 31, 2010, respectively (in thousands):

	September 30, 2011	December 31, 2010
<b>Indefinite-lived intangibles:</b>		
In-process research and development	\$ 337,000	\$ 271,000
Tradenames	59,000	27,000
<i>Total indefinite-lived intangibles</i>	\$ 396,000	\$ 298,000
<b>Definite-lived intangibles:</b>		
Licenses (weighted average life of 10 years)	640,142	638,142
Less accumulated amortization	(239,099)	(185,706)
Licenses, net	\$ 401,043	\$ 452,436
Customer relationships (weighted average life of 16 years)	171,308	
Less accumulated amortization	(3,200)	
Tradenames, net	\$ 168,108	\$
Tradenames (weighted average life of 15 years)	46,600	14,600
Less accumulated amortization	(2,555)	(486)
Tradenames, net	\$ 44,045	\$ 14,114
Developed technology (weighted average life of 16 years)	1,849,700	768,400
Less accumulated amortization	(92,847)	(14,614)
Developed technology, net	\$ 1,756,853	\$ 753,786
Service contract		13,424
Less accumulated amortization		
Service contract, net	\$	\$ 13,424
<i>Total definite-lived intangibles, net (weighted average life of 14 years)</i>	\$ 2,370,049	\$ 1,233,760
Other intangibles, net	\$ 2,766,049	\$ 1,531,760

Amortization expense for the nine month periods ended September 30, 2011 and 2010 was \$137.0 million and \$54.2 million, respectively. As of September 30, 2011, the weighted average amortization period for our definite-lived intangible assets in total was approximately 14 years.

## Edgar Filing: ENDO PHARMACEUTICALS HOLDINGS INC - Form 10-Q

Changes in the gross carrying amount of our other intangible assets for the nine months ended September 30, 2011, are as follows:

<b>(in thousands)</b>	<b>Gross carrying amount</b>
Balance at December 31, 2010:	\$ 1,732,566
Acquisitions	1,390,000
Patents	2,000
Measurement period adjustments	(8,258)
Sale of IGRT	(12,166)
Effect of currency translation	(692)
Other	300

**Table of Contents**

(in thousands)	<b>Gross carrying amount</b>
Balance at September 30, 2011	\$ 3,103,750

In September 2011, the IGRT business was sold for approximately \$13.0 million, at which time the related intangible asset, which had a gross carrying amount of \$12.2 million, was reduced to zero.

Estimated amortization of intangibles for the five fiscal years subsequent to December 31, 2010 is as follows (in thousands):

2011	\$ 195,688
2012	\$ 234,921
2013	\$ 193,147
2014	\$ 179,779
2015	\$ 179,353

**NOTE 10. COMPREHENSIVE INCOME**

Comprehensive income includes the following components for the three and nine months ended September 30, 2011 and 2010 (in thousands):

	Three Months Ended		Nine months ended	
	September 30,		September 30,	
	2011	2010	2011	2010
Consolidated net income	\$ 56,305	\$ 69,472	\$ 192,152	\$ 181,287
Other comprehensive income:				
Unrealized (loss) gain on securities, net of tax	(540)	36	(1,922)	(62)
Foreign currency translation loss, net of tax	(5,326)		(4,326)	
Fair value adjustment on derivatives designated as cash flow hedges, net of tax	111		111	
Consolidated total comprehensive income	\$ 50,550	\$ 69,508	\$ 186,015	\$ 181,225
Less: Total comprehensive income attributable to noncontrolling interests	15,656	15,266	41,133	15,266
Comprehensive income attributable to Endo Pharmaceuticals Holdings Inc.	\$ 34,894	\$ 54,242	\$ 144,882	\$ 165,959

**NOTE 11. STOCKHOLDERS EQUITY*****Stock-Based Compensation***

*Endo Pharmaceuticals Holdings Inc. 2000, 2004, 2007, and 2010 Stock Incentive Plans and the American Medical Systems Holdings, Inc. 2005 Stock Incentive Plan*

On August 11, 2000, we established the Endo Pharmaceuticals Holdings Inc. 2000 Stock Incentive Plan. The 2000 Stock Incentive Plan reserved an aggregate of 4,000,000 shares of common stock of the Company for issuance to employees, officers, directors and consultants. The 2000 Stock Incentive Plan provided for the issuance of stock options, restricted stock, stock bonus awards, stock appreciation rights or performance awards. The 2000 Stock incentive Plan expired in 2010. In May 2004, our stockholders approved the Endo Pharmaceuticals Holdings Inc. 2004 Stock Incentive Plan. The maximum number of shares of Company stock reserved for issuance under the 2004 Stock Incentive Plan is 4,000,000 shares. The 2004 Plan provides for the grant of stock options, stock appreciation rights, shares of restricted stock, performance shares, performance units or other share-based awards that may be granted to executive officers and other employees of the Company, including officers and directors who are employees, to non-employee directors and to consultants to the Company. In May 2007, our stockholders approved the Endo Pharmaceuticals Holdings Inc. 2007 Stock Incentive Plan. The maximum number of shares of Company stock reserved for issuance under the 2007 Stock Incentive Plan is 7,000,000 shares (subject to adjustment for certain transactions), but in no event may the total number of shares of Company stock subject to awards awarded to any one participant during any tax year of the Company exceed 750,000 shares (subject to adjustment for certain





**Table of Contents**

transactions). During 2009, 43,500 restricted stock units and 66,503 non-qualified stock options were granted to an executive officer of the Company as an inducement to commence employment with the Company. The restricted stock units and non-qualified stock options were granted outside of the 2007 Stock Incentive Plan but are subject to the terms and conditions of the 2007 Stock Incentive Plan and the applicable award agreements. In May 2010, our stockholders approved the Endo Pharmaceuticals Holdings Inc. 2010 Stock Incentive Plan. The maximum number of shares of Company stock reserved for issuance under the Plan includes 8,000,000 shares plus the number of shares of Company stock reserved but unissued under the Company's 2004 and 2007 Stock Incentive Plans as of April 28, 2010 and may be increased to include the number of shares of Company stock that become available for reuse under these plans following April 28, 2010, subject to adjustment for certain transactions. Notwithstanding the foregoing, of the 8,000,000 shares originally reserved for issuance under this Plan, no more than 4,000,000 of such shares shall be issued as awards, other than options, that are settled in the Company's stock. In no event may the total number of shares of Company stock subject to awards awarded to any one participant during any tax year of the Company, exceed 1,000,000 shares (subject to adjustment for certain transactions). In June 2011, in connection with our acquisition of AMS, we assumed the AMS 2005 Stock Incentive Plan. As of the AMS Acquisition Date, the number of shares of Company stock reserved for issuance under the Plan was 5,269,152. Approximately 22.2 million shares were reserved for future issuance upon exercise of options granted or to be granted under the Endo 2000, 2004, 2007, and 2010 Stock Incentive Plans and the AMS 2005 Stock Incentive Plan. As of September 30, 2011, stock options, restricted stock awards, performance stock units and restricted stock units have been granted under the Stock Incentive Plans.

The Company accounts for its stock-based compensation plans in accordance with the applicable accounting guidance. Accordingly, all stock-based compensation cost is measured at the grant date, based on the estimated fair value of the award, and is recognized as an expense in the income statement over the requisite service period.

The Company recognized stock-based compensation expense of \$15.5 million and \$34.2 million during the three and nine months ended September 30, 2011 and \$6.4 million and \$16.8 million, during the three and nine months ended September 30, 2010, respectively. As of September 30, 2011, the total remaining unrecognized compensation cost related to all non-vested stock-based compensation awards amounted to \$117.3 million. This expected cost does not include the impact of any future stock-based compensation awards.

*Stock Options*

For all of the Company's stock-based compensation plans, the fair value of each option grant was estimated at the date of grant using the Black-Scholes option-pricing model. Black-Scholes utilizes assumptions related to volatility, the risk-free interest rate, the dividend yield (which is assumed to be zero, as the Company has not paid cash dividends to date and does not currently expect to pay cash dividends) and the expected term of the option. Expected volatilities utilized in the model are based mainly on the historical volatility of the Company's stock price over a period commensurate with the expected life of the share option as well as other factors. The risk-free interest rate is derived from the U.S. Treasury yield curve in effect at the time of grant. We estimate the expected term of options granted based on our historical experience with our employees' exercise of stock options and other factors.

A summary of the activity under the Endo 2000, 2004, 2007, and 2010 Stock Incentive Plans and the AMS 2005 Stock Incentive Plan for the nine months ended September 30, 2011 is presented below:

	Number of Shares	Weighted Average Exercise Price	Weighted Average Remaining Contractual Term	Aggregate Intrinsic Value
Outstanding, January 1, 2011	5,891,400	\$ 22.60		
Granted	3,803,724	\$ 29.58		
Exercised	(961,683)	\$ 22.60		
Forfeited	(267,796)	\$ 25.36		
Expired	(30,923)	\$ 26.41		
Outstanding, September 30, 2011	8,434,722	\$ 25.67	7.27	\$ 35,967,432
Vested and expected to vest, September 30, 2011	7,667,048	\$ 25.45	7.18	\$ 33,540,237
Exercisable, September 30, 2011	2,507,289	\$ 23.66	5.74	\$ 12,451,004

**Table of Contents**

The total intrinsic value of options exercised during the nine months ended September 30, 2011 and 2010 was \$14.3 million and \$2.3 million, respectively. The weighted-average grant date fair value of the stock options granted in the nine months ended September 30, 2011 and 2010 was \$14.69 per option and \$7.38 per option, respectively, determined using the following assumptions:

	2011	2010
Average expected term (years)	5.0	5.3
Risk-free interest rate	2.0%	2.5%
Dividend yield	0.0	0.0
Expected volatility	32%	34%

The weighted average remaining requisite service period of the non-vested stock options was 2.5 years. As of September 30, 2011, the total remaining unrecognized compensation cost related to non-vested stock options amounted to \$53.5 million. This unrecognized compensation cost does not include the impact of any future stock-based compensation awards.

*Restricted Stock Units*

A summary of our restricted stock units as of September 30, 2011 is presented below:

	Number of Shares	Aggregate Intrinsic Value
Outstanding, January 1, 2011	2,211,303	
Granted	1,133,295	
Forfeited	(148,632)	
Vested	(543,519)	
Outstanding, September 30, 2011	2,652,447	\$ 75,011,201
Vested and expected to vest, September 30, 2011	2,300,858	\$ 64,400,247

The weighted average remaining requisite service period of the non-vested restricted stock units was 2.3 years. The weighted-average grant date fair value of the restricted stock units granted during the nine months ended September 30, 2011 and 2010 was \$34.71 per unit and \$20.78 per unit, respectively. As of September 30, 2011, the total remaining unrecognized compensation cost related to non-vested restricted stock units amounted to \$55.1 million. This unrecognized compensation cost does not include the impact of any future stock-based compensation awards.

*Restricted Stock Awards*

A summary of our restricted stock awards as of September 30, 2011 is presented below:

	Number of Shares	Weighted Average Fair Value Per Share	Aggregate Intrinsic Value
Outstanding, January 1, 2011		\$	
Granted	199,413	\$ 38.32	
Forfeited	(4,233)	\$ 38.32	
Vested	(7,558)	\$ 38.32	\$ 118,482
Non-vested, September 30, 2011	187,622	\$ 38.20	

The weighted average remaining requisite service period of the non-vested restricted stock was approximately 2.7 years.



**Table of Contents***Performance Shares*

Beginning in the first quarter ended March 31, 2010, the Company began to award performance stock units (PSU) to certain key employees. These PSUs are tied to both Endo's overall financial performance and Endo's financial performance relative to the financial performance of a selected industry group. Awards are granted annually, with each award covering a three-year performance cycle. Each PSU is convertible to one share of Endo common stock. Performance measures used to determine the actual number of performance shares issuable upon vesting include an equal weighting of Endo's total shareholder return (TSR) performance compared to the performance group over the three-year performance cycle and Endo's three-year cumulative revenue performance as compared to a three-year revenue target. TSR relative to peers is considered a market condition while cumulative revenue performance is considered a performance condition under applicable authoritative guidance. PSUs granted for the nine months ended September 30, 2011 and 2010 totaled approximately 160,000 and 163,000, respectively. As of September 30, 2011, there was approximately \$8.8 million of total unrecognized compensation costs related to PSUs. That cost is expected to be recognized over a weighted-average period of 3.0 years.

*Share Repurchase Program*

In April 2008, our Board of Directors approved a share repurchase program, authorizing the Company to repurchase in the aggregate up to \$750 million of shares of its outstanding common stock. Purchases under this program may be made from time to time in open market purchases, privately-negotiated transactions, and accelerated stock repurchase transactions or otherwise, as determined by Endo.

This program does not obligate Endo to acquire any particular amount of common stock. Additional purchases, if any, will depend on factors such as levels of cash generation from operations, cash requirements for investment in the Company's business, repayment of future debt, if any, current stock price, market conditions and other factors. The share repurchase program may be suspended, modified or discontinued at any time. As a result of a two-year extension approved by the Board of Directors in February 2010, the share repurchase plan is set to expire in April 2012.

Pursuant to the existing share repurchase program, we purchased approximately 0.9 million shares of our common stock during the nine month period ended September 30, 2011 totaling \$34.7 million and approximately 2.5 million shares of our common stock during the nine month period ended September 30, 2010 totaling \$59.0 million.

*Changes in Stockholders' Equity*

The following table displays a reconciliation of our beginning and ending balances in stockholders' equity for the nine months ended September 30, 2011 (dollars in thousands):

	Attributable to:		
	Endo Pharmaceuticals Holdings Inc.	Noncontrolling interests	Total Stockholders Equity
Stockholders' equity at January 1, 2011	\$ 1,741,591	\$ 61,738	\$ 1,803,329
Net income	151,019	41,133	192,152
Other comprehensive income	(6,137)		(6,137)
Compensation related to stock-based awards	34,224		34,224
Exercise of options	21,935		21,935
Common stock purchased	(34,702)		(34,702)
Distributions to noncontrolling interests		(39,392)	(39,392)
Buy-out of noncontrolling interests, net of contributions		(402)	(402)
Replacement equity issued in connection with the AMS acquisition	12,220		12,220
Other	4,338		4,338
Stockholders' equity at September 30, 2011	\$ 1,924,488	\$ 63,077	\$ 1,987,565



**Table of Contents****NOTE 12. COMMITMENTS AND CONTINGENCIES****Manufacturing, Supply and Other Service Agreements**

We contract with various third party manufacturers, suppliers and service providers to provide us with raw materials used in our products and semi-finished and finished goods, as well as certain packaging and labeling and sales and marketing services. Our most significant agreements are with Novartis Consumer Health, Inc. and Novartis AG (collectively, Novartis), Teikoku Seiyaku Co., Ltd., Mallinckrodt Inc., Noramco, Inc., Sharp Corporation, and Ventiv Commercial Services, LLC. If for any reason we are unable to obtain sufficient quantities of any of the finished goods or raw materials or components required for our products or services needed to conduct our business, it could have a material adverse effect on our business, financial condition, results of operations and cash flows.

*Novartis Consumer Health, Inc.*

On May 3, 2001, we entered into a long-term manufacturing and development agreement with Novartis Consumer Health, Inc. whereby Novartis Consumer Health, Inc. has agreed to manufacture certain of our commercial products and products in development. We are required to purchase, on an annual basis, a minimum amount of product from Novartis Consumer Health, Inc. The purchase price per product is equal to a predetermined amount per unit, subject to periodic adjustments. This agreement had a five-year initial term, with automatic five-year renewals thereafter. In August 2005, we extended this agreement until 2011. On February 23, 2011, we gave notice to Novartis that we would terminate this agreement effective February 2014. At September 30, 2011, based on the currently manufactured products at Novartis Consumer Health, Inc. we are required to purchase a minimum of approximately \$14 million of product from Novartis Consumer Health Inc. per year, or pro rata portion thereof, until the effective date of the termination of this agreement.

Pursuant to the March 2008 Voltaren® Gel License and Supply Agreement (the Voltaren® Gel Agreement) with Novartis AG and Novartis Consumer Health, Inc. Endo has agreed to purchase from Novartis all of its requirements for Voltaren® Gel during the entire term of the Voltaren® Gel Agreement. The price of product purchased under the Voltaren® Gel Agreement is fixed for the first year and subject to annual changes based upon changes in the producer price index and raw materials.

As part of the Voltaren® Gel Agreement, we also agreed to undertake advertising and promotion of Voltaren® Gel (A&P Expenditures), subject to certain thresholds set forth in the Voltaren® Gel Agreement. We agreed to spend a minimum of \$15 million on A&P Expenditures during the first Voltaren® Gel Agreement Year which ended on June 30, 2009. During the second Voltaren® Gel Agreement Year beginning on July 1, 2009 and extended through June 30, 2010, we had agreed to spend a minimum of \$20 million on A&P Expenditures. During the third Voltaren® Gel Agreement Year beginning on July 1, 2010 and extending through June 30, 2011, we had agreed to spend 15% of prior year sales or approximately \$13 million on A&P Expenditures. During the fourth Voltaren® Gel Agreement Year beginning on July 1, 2011 and extending through June 30, 2012, we have agreed to spend 13% of prior year sales or approximately \$16 million on A&P Expenditures. In subsequent Agreement Years, the minimum A&P Expenditures set forth in the Voltaren® Gel Agreement are determined based on a percentage of net sales of Voltaren® Gel. Amounts incurred by Endo for such A&P Expenditures were \$15.1 million and \$15.7 million for the nine months ended September 30, 2011 and 2010, respectively.

*Teikoku Seiyaku Co., Ltd.*

Under the terms of our agreement (the Teikoku Agreement) with Teikoku Seiyaku Co. Ltd. (Teikoku), a Japanese manufacturer, Teikoku manufactures Lidoderm® at its two Japanese facilities, located on adjacent properties, for commercial sale by us in the United States. We also have an option to extend the supply area to other territories. On April 24, 2007, we amended the Teikoku agreement (the Amended Agreement). The material components of the Amended Agreement are as follows:

We agreed to purchase a minimum number of patches per year through 2012, representing the noncancelable portion of the Amended Agreement.

Teikoku agreed to fix the supply price of Lidoderm® for a period of time after which the price will be adjusted at future dates certain based on a price index defined in the Amended Agreement. Since future price changes are unknown, we have used prices currently existing under the Amended Agreement, and estimated our minimum purchase requirement to be approximately \$32 million per year through 2012.



---

**Table of Contents**

The minimum purchase requirement shall remain in effect subsequent to 2012, except that Endo has the right to terminate the Amended Agreement after 2012, if we fail to meet the annual minimum requirement.

Following cessation of our obligation to pay royalties to Hind Healthcare Inc. (Hind) under the Sole and Exclusive License Agreement dated as of November 23, 1998, as amended, between Hind and Endo, we will pay to Teikoku annual royalties based on our annual net sales of Lidoderm®.

The Amended Agreement will expire on December 31, 2021, unless terminated in accordance with its terms. Either party may terminate this Agreement, upon thirty (30) days written notice, in the event that Endo fails to purchase the annual minimum quantity for each year after 2012 (e.g., 2013 through 2021) upon thirty (30) days written notice. Notwithstanding the foregoing, after December 31, 2021, the Amended Agreement shall be automatically renewed on the first day of January each year unless (i) we and Teikoku agree to terminate the Amended Agreement upon mutual written agreement or (ii) either we or Teikoku terminates the Amended Agreement with 180-day written notice to the other party, which notice shall not in any event be effective prior to July 1, 2022.

On January 6, 2010, the parties amended the Teikoku Agreement, effective December 16, 2009. Pursuant to the amendment, Teikoku has agreed to supply Lidoderm® at a fixed price for a period of time after which the price will be adjusted at certain future dates based on a price index defined in the amendment.

Effective November 1, 2010, the parties amended the Teikoku Agreement. Pursuant to this amendment, Teikoku has agreed to supply additional Lidoderm® at no cost to Endo in each of 2011, 2012 and 2013 in the event Endo's firm orders of Product exceed certain thresholds in those years.

*Mallinckrodt Inc.*

Under the terms of our agreement (the Mallinckrodt Agreement) with Mallinckrodt Inc. (Mallinckrodt), Mallinckrodt manufactures and supplies to us certain narcotic active drug substances, in bulk form, and raw materials for inclusion in our controlled substance pharmaceutical products. There is no minimum annual purchase commitment under the Mallinckrodt Agreement. However, we are required to purchase a fixed percentage of our annual requirements of each narcotic active drug substance covered by the Mallinckrodt Agreement from Mallinckrodt. The purchase price for these substances is equal to a fixed amount, adjusted on an annual basis. The initial term of this agreement was July 1, 1998 until September 30, 2013, with an automatic renewal provision for unlimited successive one-year periods. On September 30, 2011, we provided written notice to Mallinckrodt that the Company intends to let the Mallinckrodt Agreement expire effective September 30, 2013. The Company chose to allow the Mallinckrodt Agreement to expire in connection with its ongoing initiatives relating to the sourcing of active pharmaceutical ingredients. Prior to the expiration of the Mallinckrodt Agreement, the Company expects a new agreement with respect to narcotic active drug substances and raw materials to be put in place with a third party. The Company will continue to purchase certain narcotic active drug substances, in bulk form, under the terms of the Mallinckrodt Agreement through the expiration date.

*Noramco, Inc.*

Under the terms of our agreement (the Noramco Agreement) with Noramco Inc. (Noramco), Noramco manufactures and supplies to us certain narcotic active drug substances, in bulk form, and raw materials for inclusion in our controlled substance pharmaceutical products. There are no minimum annual purchase commitments under the Noramco Agreement. However, we are required to purchase a fixed percentage of our annual requirements of each narcotic active drug substance covered by the Noramco Agreement from Noramco. The purchase price for these substances is equal to a fixed amount, adjusted on an annual basis. The Noramco Agreement will expire on December 31, 2011, with automatic renewal provisions for unlimited successive one-year periods. On September 30, 2011, our wholly-owned subsidiary Vintage Pharmaceuticals, LLC (Vintage) provided written notice to Noramco that Vintage intends to let the Noramco Agreement expire effective March 31, 2012. Vintage chose to allow the Noramco Agreement to expire in connection with its ongoing initiatives relating to the sourcing of active pharmaceutical ingredients. Prior to the expiration of the Noramco Agreement, Vintage expects a new agreement with respect to narcotic active drug substances and raw materials to be in place with a third party. Vintage will continue to purchase certain narcotic active drug substances, in bulk form, under the terms of the Noramco Agreement through the expiration date.

*Sharp Corporation*

Under the terms of our agreement (the Sharp Agreement) with Sharp Corporation (Sharp), a U.S. manufacturer, Sharp performs certain services for Endo including the packaging and labeling of Lidoderm® at its facility in Allentown, Pennsylvania, for commercial sale by us in the United States. On December 6, 2010, the parties amended the Sharp Packaging and Labeling agreement, effective December 1, 2010, extending the



## Edgar Filing: ENDO PHARMACEUTICALS HOLDINGS INC - Form 10-Q

agreement until March 15, 2015. The Sharp Agreement is subject to renewal for additional one-year periods upon mutual agreement by both parties. Endo has the right to terminate the Sharp Agreement at any time upon ninety (90) days written notice.

**Table of Contents**

*Ventiv Commercial Services, LLC*

On November 24, 2010, we entered into a services agreement (the Ventiv Agreement) with Ventiv Commercial Services, LLC (Ventiv).

Under the terms of the Ventiv Agreement, Ventiv provides to Endo certain sales and promotional services through a contracted field force of 228 sales representatives, 24 district managers, one project manager, and one national sales director, collectively referred to as the Ventiv Field Force. The Ventiv Field Force is required to perform a minimum number of face-to-face, one-on-one discussions with physicians and other health care practitioners for the purpose of promoting Voltaren® Gel, Lidoderm®, Frova®, Opana® ER, and other Endo products within their respective approved indications during each year of the Ventiv Agreement, subject to certain provisions.

Under the terms of the Ventiv Agreement, we incurred a one-time implementation fee that we recognized in Selling, general, and administrative expense in the second half of 2010. In addition, each month we are required to pay Ventiv a monthly fixed fee during the term of the Ventiv Agreement based on a pre-approved budget. Ventiv is also eligible to earn a performance-based bonus equal to the fixed management fee during each year of the Ventiv Agreement. This performance-based bonus is payable upon the satisfaction of certain conditions, including the sale of a minimum number of Voltaren® Gel tubes and a minimum number of Details achieved. The Ventiv Agreement was set to expire on October 1, 2011. On July 21, 2011, Endo notified Ventiv of its decision to extend the term of the Ventiv Agreement to December 30, 2011.

The expenses incurred with respect to Ventiv under both the 2008 and the Ventiv Agreements were \$9.7 million and \$27.7 million for the three and nine months ended September 30, 2011, respectively, and \$3.4 million and \$9.1 million for the three and nine months ended September 30, 2010, respectively. These amounts were included within Selling, general and administrative expense in the accompanying Condensed Consolidated Statements of Operations.

*UPS Supply Chain Solutions*

Under the terms of this agreement, we utilize UPS Supply Chain Solutions to provide customer service support, chargeback processing, accounts receivables management and warehouse, freight and distribution services for certain of our products in the United States. The initial term of the agreement will extend to March 31, 2015. The agreement may be terminated by either party (1) without cause upon prior written notice to the other party; (2) with cause in the event of an uncured material breach by the other party and (3) if the other party become insolvent or bankrupt. In the event of termination of services provided under the Warehouse Distribution Services Schedule to the agreement (i) by Endo without cause or (ii) by UPS due to Endo's breach, failure by Endo to make payments

## **Table of Contents**

when due, or Endo's insolvency, we would be required to pay UPS certain termination costs. Such termination costs would not exceed \$1.4 million.

### *General*

In addition to the manufacturing and supply agreements described above, we have agreements with various companies for clinical development services. Although we have no reason to believe that the parties to these agreements will not meet their obligations, failure by any of these third parties to honor their contractual obligations may have a materially adverse effect on our business, financial condition, results of operations and cash flows.

### **Milestones and Royalties**

See Note 8 for a complete description of future milestone and royalty commitments pursuant to our acquisitions, license and collaboration agreements.

### **Employment Agreements**

We have entered into employment agreements with certain members of management.

### **Research Contracts**

We routinely contract with universities, medical centers, contract research organizations and other institutions for the conduct of research and clinical studies on our behalf. These agreements are generally for the duration of the contracted study and contain provisions that allow us to terminate prior to completion.

### **Legal Proceedings**

We and certain of our subsidiaries are involved in various claims, legal proceedings and governmental investigations that arise from time to time in the ordinary course of our business, including relating to product liability, intellectual property, regulatory compliance and commercial matters. While we cannot predict the outcome of our ongoing legal proceedings and we intend to vigorously defend our position, an adverse outcome in any of these proceedings could have a material adverse effect on our current and future financial position, results of operations and cash flows.

In view of the inherent difficulty of predicting the outcome of our various claims, legal proceedings and governmental investigations, particularly where there are many claimants and the claimants seek indeterminate damages and particularly given the various stages of our proceedings, we are unable to predict the outcome of these matters or the ultimate legal and financial liability, and at this time cannot reasonably estimate the possible loss or range of loss. Accordingly, there are claims, legal proceedings and governmental investigations in which we are involved where a loss is reasonably possible in future periods and for which we have not accrued a related liability. Likewise, it is reasonably possible that a future loss could exceed the related accrued liability.

### *Department of Health and Human Services Subpoena*

As previously reported, in January 2007 and April 2011, the Company received subpoenas issued by the United States Department of Health and Human Services, Office of Inspector General (OIG) and the United States Department of Justice, respectively. The subpoenas request documents relating to Lidoderm® (lidocaine patch 5%), focused primarily on the sale, marketing and promotion of Lidoderm®. The Company is cooperating with the government in responding to the subpoenas. At this time, the Company cannot predict or determine the outcome of the government's investigation or reasonably estimate the amount or range of amounts of fines or penalties, if any, that might result from a settlement or an adverse outcome from this investigation.

### *Pricing Litigation*

A number of cases were brought by state government entities that allege generally that our wholly-owned subsidiary, Endo Pharmaceuticals Inc. (EPI) and numerous other pharmaceutical companies reported false pricing information in connection with certain drugs that are reimbursable under Medicaid. These cases generally seek damages, treble damages, disgorgement of profits, restitution and attorneys' fees.

## Edgar Filing: ENDO PHARMACEUTICALS HOLDINGS INC - Form 10-Q

As previously reported, one of these cases, *State of Iowa v. Abbott Laboratories, Inc., et al.*, had been consolidated in the United States District Court for the District of Massachusetts under the Multidistrict Litigation Rules as *In re: Pharmaceutical Industry Average Wholesale Price Litigation, MDL 1456*. Without admitting any liability or wrongdoing, EPI and the plaintiff reached an agreement to resolve this case on terms that are not material to the Company's business, results of operations, financial condition or cash flows. Pursuant to that agreement, this matter was dismissed as to EPI on September 28, 2011.

## Edgar Filing: ENDO PHARMACEUTICALS HOLDINGS INC - Form 10-Q

There is a previously reported case pending in the Circuit Court of Montgomery County, Alabama against EPI and numerous other pharmaceutical companies: *State of Alabama v. Abbott Laboratories, Inc., et al.* In addition, there is a previously reported case pending in the Third Judicial District Court of Salt Lake County, Utah against EPI and numerous other pharmaceutical companies: *State of Utah v. Actavis US, Inc., et al.* As previously reported, there is a case pending in the 19th Judicial District, Parish of East Baton Rouge, Louisiana against EPI and numerous other pharmaceutical companies: *State of Louisiana v. Abbott Laboratories, Inc., et al.* These cases contain allegations similar to the allegations described above.

The Company intends to contest the above unresolved cases vigorously and to explore other options as appropriate in the best interests of the Company. Litigation similar to that described above may also be brought by other plaintiffs in various jurisdictions. However, we cannot predict the timing or outcome of any such litigation, or whether any such litigation will be brought against the Company or its subsidiaries.

**Table of Contents**

*Paragraph IV Certifications on Lidoderm®*

As previously reported, on January 15, 2010, the Company and the holders of the Lidoderm® NDA and relevant patent, Teikoku Seiyaku Co., Ltd., and Teikoku Pharma USA, Inc. (Teikoku) received a Paragraph IV Certification Notice under 21 U.S.C. 355(j) from Watson Laboratories, Inc. (Watson) advising of the filing of an Abbreviated New Drug Application (ANDA) for a generic version of Lidoderm® (lidocaine topical patch 5%). The Paragraph IV Certification Notice refers to U.S. Patent No. 5,827,529, which covers the formulation of Lidoderm®, a topical patch to relieve the pain of post herpetic neuralgia launched in 1999. This patent is listed in the FDA's Orange Book and expires in October 2015. As a result of this Notice, on February 19, 2010, the Company, Teikoku Seiyaku Co., Ltd. and Teikoku Pharma USA, Inc. filed a lawsuit against Watson in the United States District Court of the District of Delaware. Because the suit was filed within the 45-day period under the Hatch-Waxman Act for filing a patent infringement action, we believe that it triggered an automatic 30-month stay of approval under the Act. On March 4, 2010, Watson filed an Answer and Counterclaims, claiming U.S. Patent No. 5,827,529 is invalid or not infringed. In October 2010, Teikoku Pharma USA listed U.S. Patent No. 5,741,510 in the FDA Orange Book, and this patent expires in March 2014. On June 30, 2011, the Company and Teikoku filed a second lawsuit against Watson in the United States District Court of the District of Delaware alleging infringement of U.S. Patent Nos. 5,741,510, 6,096,333, and 6,096,334 which cover lidocaine patch formulations and manufacturing processes.

As previously reported, in January 2011, the Company and Teikoku received a Paragraph IV Certification Notice under 21 U.S.C. 355(j) from Mylan Technologies Inc. (Mylan) advising of the filing of an ANDA for a generic version of Lidoderm® (lidocaine topical patch 5%). The Paragraph IV Certification Notice refers to U.S. Patent Nos. 5,827,529 and 5,741,510, which cover the formulation of Lidoderm®. These patents are listed in the FDA's Orange Book and expire in October 2015 and March 2014, respectively. On March 14, 2011, the Company filed a lawsuit against Mylan in the United States District Court for the District of Delaware, claiming that the Paragraph IV Certification Notice served by Mylan failed to comply with the requirements of 21 U.S.C. sec. 355(b)(3)(C)(1) and 21 C.F.R. 214.95(a). In that suit, the Company seeks a declaration that Mylan's Paragraph IV Certification Notice is null, void and without legal effect, and that as a result, Mylan has failed to properly trigger the ANDA litigation process. In the alternative, the Company alleges that Mylan's submission of its ANDA constitutes infringement of the 510 patent under 35 U.S.C. sec. 271(e)(2)(A).

---

**Table of Contents**

Endo intends, and has been advised by Teikoku that they too intend, to vigorously defend Lidoderm<sup>®</sup>'s intellectual property rights and to pursue all available legal and regulatory avenues in defense of Lidoderm<sup>®</sup>, including enforcement of the product's intellectual property rights and approved labeling. However, there can be no assurance that we will be successful. If we are unsuccessful and either Watson or Mylan is able to obtain FDA approval of its product, either Watson or Mylan may be able to launch its generic version of Lidoderm<sup>®</sup> prior to the applicable patents' expirations in 2014 and 2015. Additionally, we cannot predict or determine the timing or outcome of this litigation but will explore all options as appropriate in the best interests of the Company. In addition to the above litigation, it is possible that another generic manufacturer may also seek to launch a generic version of Lidoderm<sup>®</sup> and challenge the applicable patents.

In addition to the above litigation, it is possible that another generic manufacturer may also seek to launch a generic version of Lidoderm<sup>®</sup> and challenge the applicable patents.

*Paragraph IV Certifications on Opana<sup>®</sup> ER*

As previously reported, in December 2007 and June 2008, the Company received notices from Impax Laboratories, Inc. (Impax) advising of the filing by Impax of an ANDA for a generic version of Opana<sup>®</sup> ER (oxymorphone hydrochloride extended-release tablets CII). Impax's notices included notification that it had filed Paragraph IV certifications under 21 U.S.C. Section 355(j) with respect to the patents that cover the formulation of Opana<sup>®</sup> ER. These patents are listed in the FDA's Orange Book and expire in 2013 and 2023. The Company timely filed lawsuits against Impax in the United States District Court for the District of Delaware in connection with Impax's ANDA.

As previously reported, on June 8, 2010, the Company settled all of the Impax litigation relating to Opana<sup>®</sup> ER. Both sides dismissed their respective claims and counterclaim with prejudice. Under the terms of the settlement, Impax agreed not to challenge the validity or enforceability of patents relating to Opana<sup>®</sup> ER. The Company agreed to grant Impax a license permitting the production and sale of generic Opana<sup>®</sup> ER for 5, 10, 20, 30 and 40 mg tablets commencing on January 1, 2013 or earlier under certain circumstances. Such license is exclusive for 5, 10, 20, 30 and 40 mg tablets of generic Opana<sup>®</sup> ER for which Impax obtains first applicant status as described in 21 U.S.C. Section 355(j)(5)(B)(iv), for the period beginning on January 1, 2013 or earlier under certain circumstances, and such exclusivity ends upon expiration or forfeit of the 180-day period described in 21 U.S.C. Section 355(j)(5)(B)(iv) for such dosage strength. Such license is also subject to any agreements executed by us and any third party holding an ANDA referencing Opana<sup>®</sup> ER as of or prior to June 8, 2010.

As previously reported, in February and June 2008, the Company received notices from Actavis South Atlantic LLC (Actavis), advising of the filing by Actavis of an ANDA for a generic version of Opana<sup>®</sup> ER. Actavis's notices included notification that it had filed Paragraph IV certifications under 21 U.S.C. Section 355(j) with respect to the patents that cover the formulation of Opana<sup>®</sup> ER. The Company timely filed lawsuits against Actavis in the United States District Court for the District of New Jersey in connection with Actavis's ANDA.

As previously reported, on February 20, 2009, the Company settled all of the Actavis litigation relating to Opana<sup>®</sup> ER. Under the terms of the settlement, Actavis agreed not to challenge the validity or enforceability of patents relating to Opana<sup>®</sup> ER. The Company agreed to grant Actavis a license permitting the production and sale of generic Opana<sup>®</sup> ER 7.5 and 15 mg tablets on July 15, 2011, or earlier under certain circumstances. The Company also granted Actavis a license to produce and market other strengths of Opana<sup>®</sup> ER generic commencing on the earlier of July 15, 2011 and the date on which any third party commences commercial sales of a generic form of the drug.

As previously reported, in July and November 2008, the Company received notices from Sandoz, Inc. (Sandoz), advising of the filing by Sandoz of an ANDA for a generic version of Opana<sup>®</sup> ER. Sandoz's notices included notification that it had filed a Paragraph IV certification under 21 U.S.C. Section 355(j) with respect to the patents that cover the formulation of Opana<sup>®</sup> ER. The Company timely filed lawsuits against Sandoz in the United States District Court for the District of Delaware in connection with Sandoz's ANDA.

As previously reported, on June 8, 2010, the Company settled all of the Sandoz litigation relating to Opana<sup>®</sup> ER. Both sides dismissed their respective claims and counterclaim with prejudice. Under the terms of the settlement, Sandoz agreed not to challenge the validity or enforceability of patents relating to Opana<sup>®</sup> ER.

---

## **Table of Contents**

The Company agreed to grant Sandoz a license permitting the production and sale of all strengths of Opana<sup>®</sup> ER commencing on September 15, 2012, or earlier under certain circumstances.

As previously reported, in September 2008 and June 2009, the Company received notices from Barr Laboratories, Inc. (Barr), advising of the filing by Barr of an ANDA for a generic version of Opana<sup>®</sup> ER. Barr's notices included notification that it had filed a Paragraph IV certification under 21 U.S.C. Section 355(j) with respect to the patents that cover the formulation of Opana<sup>®</sup> ER. The Company timely filed lawsuits against Barr in the United States District Court for the District of Delaware in connection with Barr's ANDA.

As previously reported, on April 12, 2010, the Company settled all of the Barr litigation relating to Opana<sup>®</sup> ER. Under the terms of the settlement, Barr agreed not to challenge the validity or enforceability of patents relating to Opana<sup>®</sup> ER. The Company agreed to grant Barr a license permitting the production and sale of all strengths of Opana<sup>®</sup> ER commencing on September 15, 2012, or earlier under certain circumstances.

As previously reported, in January and March 2010, the Company received notices from Watson Laboratories, Inc. (Watson) advising of the filing by Watson of an ANDA for a generic version of Opana<sup>®</sup> ER. Watson's notices included notification that it had filed a Paragraph IV certification under 21 U.S.C. Section 355(j) with respect to the patents that cover the formulation of Opana<sup>®</sup> ER. The Company timely filed lawsuits against Watson in the U.S. District Court for the District of New Jersey in connection with Watson's ANDA.

As previously reported, on October 4, 2010, the Company settled all of the Watson litigation relating to Opana<sup>®</sup> ER. Under the terms of the settlement, Watson agreed not to challenge the validity or enforceability of patents relating to Opana<sup>®</sup> ER. The Company agreed to grant Watson a license permitting the production and sale of all strengths of Opana<sup>®</sup> ER commencing on September 15, 2012, or earlier under certain circumstances.

As previously reported, in December 2009 and January 2010, the Company received notices from Roxane Laboratories, Inc. (Roxane) advising of the filing by Roxane of an ANDA for a generic version of Opana<sup>®</sup> ER. Roxane's notices included notification that it had filed a Paragraph IV certification under 21 U.S.C. Section 355(j) with respect to the patents that cover the formulation of Opana<sup>®</sup> ER. The Company timely filed lawsuits against Roxane in the U.S. District Court for the District of New Jersey in connection with Roxane's ANDA.

On May 4, 2011, the Company settled all of the Roxane litigation relating to Opana<sup>®</sup> ER. Under the terms of the settlement, Roxane agreed not to challenge the validity or enforceability of patents relating to Opana<sup>®</sup> ER. The Company agreed to grant Roxane a license permitting the production and sale of all strengths of Opana<sup>®</sup> ER commencing on September 15, 2012, or earlier under certain circumstances.

In addition to the above litigation, it is possible that another generic manufacturer may also seek to launch a generic version of Opana<sup>®</sup> ER and challenge the applicable patents. We intend to contest vigorously and pursue all available legal and regulatory avenues in defense of Opana<sup>®</sup> ER, including enforcement of our intellectual property rights and approved labeling. However, there can be no assurance that we will be successful. Additionally, we cannot predict or determine the timing or outcome of any of these litigations but will explore all options as appropriate in the best interests of the Company.

### *Paragraph IV Certification on Frova<sup>®</sup>*

As previously reported, in July 2011, the Company and its licensor, Vernalis Development Limited received a notice from Mylan Technologies Inc. (Mylan) advising of the filing by Mylan of an ANDA for a generic version of Frova<sup>®</sup> (frovatriptan succinate) 2.5 mg tablets. Mylan's notice included notification that it had filed a Paragraph IV certification under 21 U.S.C. Section 355(j) with respect to US Patent Nos. 5,464,864, 5,561,603, 5,637,611, 5,827,871, and 5,962,501, which cover Frova<sup>®</sup>. These patents are listed in the U.S. Food and Drug Administration's (FDA) Orange Book and expire between 2013 and 2015. As a result of this Notice, on August 16, 2011, the Company filed a lawsuit against Mylan in the United States District Court for the District of Delaware alleging infringement of U.S. Patent Nos. 5,464,864, 5,637,611, and 5,827,871. Because the suit was filed within the 45-day period under the Hatch-Waxman Act for filing a patent infringement action, we believe that it triggered an automatic 30-month stay of approval under the Act. On September 22, 2011, Mylan filed an Answer and Counterclaims, claiming the asserted patents are invalid or not infringed.

Endo intends to vigorously defend Frova<sup>®</sup>'s intellectual property rights and to pursue all available legal and regulatory avenues in defense of Frova<sup>®</sup>, including enforcement of the product's intellectual property rights and approved labeling. However, there can be no assurance that we will be successful. If we are unsuccessful and Mylan is able to obtain FDA approval of its product, Mylan may be able to launch its generic version of Frova<sup>®</sup> prior to the applicable patents' expirations in 2014 and 2015. Additionally, we cannot predict or determine the timing or outcome of this litigation but will explore all options as appropriate in the best interests of the Company. In addition to the above litigation, it is possible that another generic manufacturer may also seek to launch a generic version of Frova<sup>®</sup> and challenge the applicable patents.





---

**Table of Contents***MCP Cases*

Qualitest, and in certain cases the Company or certain of its subsidiaries, along with several other pharmaceutical manufacturers, have been named as defendants in numerous lawsuits in various federal and state courts alleging personal injury resulting from the use of the prescription medicine metoclopramide. Plaintiffs in these suits allege various personal injuries including tardive dyskinesia, other movement disorders, and death. The Company intends to contest these cases vigorously and to explore other options as appropriate in the best interests of the Company. Litigation similar to that described above may also be brought by other plaintiffs in various jurisdictions. However, we cannot predict the timing or outcome of any such litigation, or whether any additional litigation will be brought against the Company or its subsidiaries. Subject to certain terms and conditions, we will be indemnified by the former owners of Qualitest with respect to metoclopramide litigation arising out of the sales of the product by Qualitest between January 1, 2006 and the date on which the acquisition was completed, subject to an overall liability cap of \$100 million for all claims arising out of or related to the acquisition, including the claims described above.

*Propoxyphene Cases*

Qualitest and, in certain cases, the Company or certain of its subsidiaries, along with several other pharmaceutical manufacturers, have been named as defendants in several lawsuits originally filed in various federal and state courts alleging personal injury resulting from the use of the prescription medicine propoxyphene. Plaintiffs in these suits allege various personal injuries including cardiac impairment and damage. In August 2011, a multidistrict litigation (MDL) was formed, and cases pending in federal court are now coordinated in the Eastern District of Kentucky as part of MDL No. 2226. The Company intends to contest these cases vigorously and to explore other options as appropriate in the best interests of the Company. Litigation similar to that described above may also be brought by other plaintiffs in various jurisdictions. However, we cannot predict the timing or outcome of any such litigation, or whether any additional litigation will be brought against the Company or its subsidiaries. Subject to certain terms and conditions, we will be indemnified by the former owners of Qualitest with respect to propoxyphene litigation arising out of the sales of the product by Qualitest between January 1, 2006 and the date on which the acquisition was completed, subject to an overall liability cap of \$100 million for all claims arising out of or related to the acquisition, including the claims described above.

*Vaginal Mesh Cases*

On October 20, 2008, the FDA issued a Public Health Notification (PHN) regarding potential complications associated with transvaginal placement of surgical mesh to treat pelvic organ prolapse (POP) and stress urinary incontinence (SUI). The notification provides recommendations and encourages physicians to seek specialized training in mesh procedures, to advise their patients about the risks associated with these procedures and to be diligent in diagnosing and reporting complications.

In July 2011, FDA issued an update to the October 2008 PHN to further advise the public and the medical community of the potential complications associated with transvaginal placement of surgical mesh to treat POP and SUI. In this July 2011 update, the FDA maintained that adverse events are not rare, as previously reported, and questioned the relative effectiveness of transvaginal mesh as a treatment for POP as compared to non-mesh surgical repair. The July 2011 notification continued to encourage physicians to seek specialized training in mesh procedures, to consider and to advise their patients about the risks associated with these procedures and to be diligent in diagnosing and reporting complications. FDA also convened an advisory panel which met on September 8-9, 2011 to further address the safety and effectiveness of transvaginal surgical mesh used for repair of POP and SUI. At the conclusion of the meetings, the advisory panel recommended reclassifying transvaginal mesh products used to treat POP to Class III devices (pre-market approval) and recommended that manufacturers of these products be required to conduct additional post-market surveillance studies. The advisory panel recommended that transvaginal surgical mesh products used to treat SUI remain as Class II devices. Regarding retropubic and transobturator (TOT) slings, the advisory panel recommended that no additional post-market surveillance studies are necessary. Regarding mini-slings, the advisory panel recommended pre-market study for new devices and additional post-market surveillance studies. The advisory panel's recommendations are now under consideration by FDA.

Since 2008, AMS, and more recently, in certain cases the Company or certain of its subsidiaries, have been named as defendants in multiple lawsuits in various federal and state courts alleging personal injury resulting from use of transvaginal surgical mesh products designed to treat POP and SUI. Plaintiffs in these suits allege various personal injuries including chronic pain, incontinence and inability to control bowel function, and permanent deformities. AMS and the Company intend to contest these cases vigorously and to explore other options as appropriate in the best interests of AMS and the Company. Litigation similar to that described above may also be brought by other plaintiffs in various jurisdictions. However, we cannot predict the timing or outcome of any such litigation, or whether any additional litigation will be brought against the Company or its subsidiaries.

**Table of Contents***Other Legal Proceedings*

In addition to the above proceedings, we are involved in, or have been involved in, arbitrations or various other legal proceedings that arise from the normal course of our business. We cannot predict the timing or outcome of these claims and other proceedings. Currently, we are not involved in any arbitration and/or other legal proceeding that we expect to have a material effect on our business, financial condition, results of operations and cash flows.

**NOTE 13. NET INCOME PER SHARE**

The following is a reconciliation of the numerator and denominator of basic and diluted net income per share (in thousands, except per share data):

	<b>Three Months Ended September 30,</b>		<b>Nine months ended September 30,</b>	
	<b>2011</b>	<b>2010</b>	<b>2011</b>	<b>2010</b>
<b>Numerator:</b>				
Net income attributable to Endo Pharmaceuticals Holdings Inc. common stockholders	\$ 40,649	\$ 54,206	\$ 151,019	\$ 166,021
<b>Denominator:</b>				
For basic per share data weighted average shares	116,816	115,469	116,611	116,292
Dilutive effect of common stock equivalents	2,281	1,128	2,328	804
Dilutive effect of 1.75% Convertible Senior Subordinated Notes and warrants	1,750		2,493	
For diluted per share data weighted average shares	120,847	116,597	121,432	117,096
Basic net income per share attributable to Endo Pharmaceuticals Holdings Inc	\$ 0.35	\$ 0.47	\$ 1.30	\$ 1.43
Diluted net income per share attributable to Endo Pharmaceuticals Holdings Inc	\$ 0.34	\$ 0.46	\$ 1.24	\$ 1.42

Basic net income per share is computed based on the weighted average number of common shares outstanding during the period. Diluted income per common share is computed based on the weighted average number of common shares outstanding and, if there is net income during the period, the dilutive impact of common stock equivalents outstanding during the period. Common stock equivalents are measured under the treasury stock method.

The 1.75% Convertible Senior Subordinated Notes due April 15, 2015 are only included in the dilutive net income per share calculation using the treasury stock method during periods in which the average market price of our common stock was above the applicable conversion price of the Convertible Notes, or \$29.20 per share. In these periods, under the treasury stock method, we calculated the number of shares issuable under the terms of these notes based on the average market price of the stock during the period, and included that number in the total diluted shares outstanding for the period.

We have entered into convertible note hedge and warrant agreements that, in combination, have the economic effect of reducing the dilutive impact of the Convertible Notes. However, we separately analyze the impact of the convertible note hedge and the warrant agreements on diluted weighted average shares outstanding. As a result, the purchases of the convertible note hedges are excluded because their impact would be anti-dilutive. The treasury stock method is applied when the warrants are in-the-money with the proceeds from the exercise of the warrant used to repurchase shares based on the average stock price in the calculation of diluted weighted average shares. Until the

**Table of Contents**

warrants are in-the-money, they have no impact to the diluted weighted average share calculation. The total number of shares that could potentially be included if the warrants were exercised is approximately 13 million.

The following reconciliation shows the maximum potential dilution of shares currently excluded from the calculation of diluted net income per share for the nine months ended September 30 (in thousands):

	2011	2010
<b>Weighted average shares excluded:</b>		
1.75% Convertible senior subordinated notes due 2015 and warrants(1)	23,500	25,993
Employee stock-based awards	2,007	5,220
	25,507	31,213

(1) Amounts represent the incremental potential total dilution that could occur if our Convertible Notes and warrants were converted to shares of our common stock.

**NOTE 14. COST OF REVENUES**

The components of cost of revenues for the three and nine months ended September 30 (in thousands) were as follows:

	<b>Three Months Ended</b>		<b>Nine months ended</b>	
	<b>September 30,</b>		<b>September 30,</b>	
	<b>2011</b>	<b>2010</b>	<b>2011</b>	<b>2010</b>
Cost of net pharmaceutical product sales	\$ 208,666	\$ 107,414	\$ 609,878	\$ 308,703
Cost of device, service and other revenues	93,506	26,506	160,549	26,506
<b>Total cost of revenues</b>	<b>\$ 302,172</b>	<b>\$ 133,920</b>	<b>\$ 770,427</b>	<b>\$ 335,209</b>

**NOTE 15. DEBT**

The components of our total indebtedness at September 30, 2011 and December 31, 2010 (in thousands), were as follows:

	<b>September 30,</b>	<b>December 31,</b>
	<b>2011</b>	<b>2010</b>
1.75% Convertible Senior Subordinated Notes due 2015	\$ 379,500	\$ 379,500
Unamortized discount on 1.75% Convertible Senior Subordinated Notes due 2015	(85,553)	(100,578)
<b>1.75% Convertible Senior Subordinated Notes due 2015, net</b>	<b>\$ 293,947</b>	<b>\$ 278,922</b>
7.00% Senior Notes due 2019	\$ 500,000	\$
7.00% Senior Notes due 2020	\$ 400,000	\$ 400,000
Unamortized initial purchaser s discount	(10,046)	(13,284)
<b>7.00% Senior Notes due 2020, net</b>	<b>\$ 389,954</b>	<b>\$ 386,716</b>

Edgar Filing: ENDO PHARMACEUTICALS HOLDINGS INC - Form 10-Q

<i>7.25% Senior Notes due 2022</i>	\$ 400,000	\$
<i>3.25% AMS Convertible Notes due 2036</i>	\$ 841	\$
<i>4.00% AMS Convertible Notes due 2041</i>	\$ 131	\$
<i>Term Loan Facility Due 2015</i>	\$	\$ 400,000
<i>Term Loan A Facility Due 2016</i>	\$ 1,485,938	\$
<i>Term Loan B Facility Due 2018</i>	\$ 563,250	\$
<i>Other long-term debt</i>	\$ 5,457	\$ 5,156
<i>Total long-term debt, net</i>	\$ 3,639,518	\$ 1,070,794
Less current portion	\$ 74,334	\$ 24,993
<i>Total long-term debt, less current portion, net</i>	\$ 3,565,184	\$ 1,045,801

---

## **Table of Contents**

### ***Credit Facility***

In October 2009, we established a \$300 million, three-year senior secured revolving credit facility (the 2009 Credit Facility) with JP Morgan Chase Bank, Barclays Capital and certain other lenders. The 2009 Credit Facility was available for letters of credit, working capital and general corporate purposes. The 2009 Credit Facility also permitted up to \$100 million of additional revolving or term loan commitments from one or more of the existing lenders or other lenders.

Financing costs of \$5.2 million paid to establish the 2009 Credit Facility were deferred and were being amortized to interest expense over the life of the 2009 Credit Facility.

On November 30, 2010, we terminated the 2009 Credit Facility. Concurrent with the termination of the 2009 Credit Facility, we established a \$400 million, five-year senior secured term loan facility (the Term Loan Facility), and a \$500 million, five-year senior secured revolving credit facility (the 2010 Revolving Credit Facility and, together with the Term Loan Facility, the 2010 Credit Facility) with JP Morgan Chase Bank, Royal Bank of Canada, and certain other lenders. The 2010 Credit Facility was established primarily to finance our acquisition of Qualitest and was available for working capital, general corporate purposes and letters of credit. The agreement governing the 2010 Credit Facility (the 2010 Credit Agreement) also permitted up to \$200 million of additional revolving or term loan commitments from one or more of the existing lenders or other lenders with the consent of the JP Morgan Chase Bank (the administrative agent) without the need for consent from any of the existing lenders under the 2010 Credit Facility.

The obligations of the Company under the 2010 Credit Facility were guaranteed by certain of the Company's domestic subsidiaries and were secured by substantially all of the assets of the Company and the subsidiary guarantors. The 2010 Credit Facility contained certain usual and customary covenants, including, but not limited to covenants to maintain maximum leverage and minimum interest coverage ratios. Borrowings under the 2010 Credit Facility bore interest at an amount equal to a rate calculated based on the type of borrowing and the Company's Leverage Ratio. For term loans and revolving loans (other than Swing Line Loans), the Company had been permitted to elect to pay interest based on an adjusted LIBOR rate plus between 2.00% and 2.75% or an Alternate Base Rate (as defined in the 2010 Credit Agreement) plus between 1.00% and 1.75%. The Company had also paid a commitment fee of between 35 to 50 basis points, payable quarterly, on the average daily unused amount of the Revolving Credit Facility.

Financing costs of \$16.5 million paid to establish the 2010 Credit Facility were deferred and were amortized to interest expense over the life of the 2010 Credit Facility. Financing costs associated with the 2009 Credit Facility not yet amortized as of November 30, 2010 totaled approximately \$3.2 million on November 30, 2010. In accordance with the applicable accounting guidance for debt modifications, upon the termination of the 2009 Credit Facility, approximately \$0.3 million of this amount was written off in proportion to decreased lending capacity provided by certain individual loan syndicates with a corresponding charge to earnings. The remaining \$2.9 million was deferred and will be amortized over the life of the 2010 Credit Facility.

On June 17, 2011, we terminated the 2010 Credit Facility. Concurrent with the termination of the 2010 Credit Facility, we established a \$1,500 million, five-year senior secured term loan facility (the Term Loan A Facility), a \$700 million, seven-year senior secured term loan facility (the Term Loan B Facility, and, together with the Term Loan A Facility, the Term Loan Facilities), and a \$500 million, five-year senior secured revolving credit facility (the 2011 Revolving Credit Facility and, together with the Term Loan Facilities, the 2011 Credit Facility) with Morgan Stanley Senior Funding, Inc., as administrative agent, Bank of America, N.A., as Syndication Agent, and certain other lenders. The 2011 Credit Facility was established primarily to finance our acquisition of AMS and is available for working capital, general corporate purposes and lines of credit. The agreement governing the 2011 Credit Facility (the 2011 Credit Agreement) also permits up to \$500 million of additional revolving or term loan commitments from one or more of the existing lenders or other lenders with the consent of Morgan Stanley Senior Funding, Inc. (the administrative agent) without the need for consent from any of the existing lenders under the 2011 Credit Facility.

The obligations of the Company under the 2011 Credit Facility are guaranteed by certain of the Company's domestic subsidiaries and are secured by substantially all of the assets of the Company and the subsidiary guarantors. The 2011 Credit Facility contains certain usual and customary covenants, including, but not limited to covenants to maintain maximum leverage and minimum interest coverage ratios. Borrowings under the 2011 Credit Facility bear interest at an amount equal to a rate calculated based on the type of borrowing and the Company's Leverage Ratio. For term A loans and revolving loans (other than Swing Line Loans), the Company is permitted to

**Table of Contents**

elect to pay interest based on an adjusted LIBOR rate plus between 1.75% and 2.50% or an Alternate Base Rate (as defined in the 2011 Credit Agreement) plus between 0.75% and 1.50%. For term B loans, the Company may elect to pay interest based on an adjusted LIBOR rate plus 3.00% or an Alternate Base Rate plus 2.00%. The Company will pay a commitment fee of between 37.5 to 50 basis points, payable quarterly, on the average daily unused amount of the Revolving Credit Facility.

Financing costs of \$56.0 million paid to establish the 2011 Credit Facility, including \$43.4 million paid to investment bankers that also helped structure the AMS acquisition, were deferred and are being amortized to interest expense over the life of the 2011 Credit Facility. Unamortized financing costs associated with the prior credit facilities as of November 30, 2010 totaled approximately \$14.7 million on June 17, 2011. In accordance with the applicable accounting guidance for debt modifications and extinguishments, approximately \$8.5 million of this amount was written off and is included in the Condensed Consolidated Statements of Operations as a Loss on extinguishment of debt, net. The remaining \$6.2 million was deferred to be amortized over the life of the 2011 Credit Facility.

In September 2011, we made a \$135.0 million prepayment on our Term Loan B Facility. Pursuant to our rights under the 2011 Credit Agreement, we elected to apply a portion of this prepayment against all remaining contractual payments such that we have no remaining principal payment obligations until the maturity of the Term Loan B Facility on June 17, 2018.

We recognized \$32.3 million and \$3.0 million of interest expense related to our Credit Facilities for the nine months ended September 30, 2011 and 2010, respectively.

**7.00% Senior Notes Due 2019**

On June 8, 2011, we issued \$500 million in aggregate principal amount of 7.00% Notes due 2019 (the 2019 Notes) at an issue price of par. The 2019 Notes were issued in a private offering for resale to qualified institutional buyers pursuant to Rule 144A under the Securities Act of 1933, as amended. The 2019 Notes are senior unsecured obligations of the Company and are guaranteed on a senior unsecured basis by certain of the Company's domestic subsidiaries. Interest on the 2019 Notes is payable semiannually in arrears on January 15 and July 15 of each year, beginning on January 15, 2012. The 2019 Notes will mature on July 15, 2019, subject to earlier repurchase or redemption in accordance with the terms of the Indenture incorporated by reference herein. We received proceeds of approximately \$485.9 million from the issuance, net of certain costs of the offering, including \$9.9 million of costs paid to investment bankers that also helped structure the AMS acquisition.

On or after July 15, 2015, the Company may on any one or more occasions redeem all or a part of the 2019 Notes, at the redemption prices (expressed as percentages of principal amount) set forth below, plus accrued and unpaid interest and additional interest, if any, if redeemed during the twelve-month period beginning on July 15 of the years indicated below:

<b>Payment Dates (between indicated dates)</b>	<b>Redemption Percentage</b>
From July 15, 2015 to and including July 14, 2016	103.500%
From July 15, 2016 to and including July 14, 2017	101.750%
From July 15, 2017 and thereafter	100.000%

In addition, at any time prior to July 15, 2015, Endo may on any one or more occasions redeem all or a part of the 2019 notes at a specified redemption price set forth in the Indenture, plus accrued and unpaid interest and additional interest, if any.

At any time prior to July 15, 2014, the Company may redeem up to 35% of the aggregate principal amount of the 2019 Notes at a specified redemption price set forth in the Indenture, plus accrued and unpaid interest and additional interest, if any, with the net cash proceeds of an equity offering subject to certain provisions. If the Company experiences certain change of control events, it must offer to repurchase the 2019 Notes at 101% of their principal amount, plus accrued and unpaid interest and additional interest, if any.

The Indenture contains covenants that, among other things, restrict the Company's ability and the ability of its restricted subsidiaries to incur certain additional indebtedness and issue preferred stock, make restricted payments, sell certain assets, agree to any restrictions on the ability of restricted subsidiaries to make payments to the Company, create certain liens, merge, consolidate, or sell substantially all of the Company's assets, or enter into certain transactions with affiliates. These covenants are subject to a number of important exceptions and qualifications, including the fall away or revision of certain of these covenants upon the 2019 Notes receiving investment grade credit ratings.





**Table of Contents**

We recognized \$11.3 million of interest expense related to our 2019 Notes for the nine months ended September 30, 2011.

**7.00% Senior Notes Due 2020**

In November 2010, we issued \$400 million in aggregate principal amount of 7.00% Senior Notes due 2020 (the 2020 Notes) at an issue price of 99.105%. The 2020 Notes were issued in a private offering for resale to qualified institutional buyers pursuant to Rule 144A under the Securities Act of 1933, as amended. The 2020 Notes are senior unsecured obligations of the Company and are guaranteed on a senior unsecured basis by certain of the Company's domestic subsidiaries. Interest on the 2020 Notes is payable semiannually in arrears on June 15 and December 15 of each year, beginning on June 15, 2011. The 2020 Notes will mature on December 15, 2020, subject to earlier repurchase or redemption in accordance with the terms of the Indenture incorporated by reference herein. We received proceeds of approximately \$386.6 million from the issuance, net of the initial purchaser's discount and certain other costs of the offering.

On or after December 15, 2015, the Company may on any one or more occasions redeem all or a part of the 2020 Notes, at the redemption prices (expressed as percentages of principal amount) set forth below, plus accrued and unpaid interest and additional interest, if any, if redeemed during the twelve-month period beginning on December 15 of the years indicated below:

<b>Payment Dates (between indicated dates)</b>	<b>Redemption Percentage</b>
From December 15, 2015 to and including December 14, 2016	103.500%
From December 15, 2016 to and including December 14, 2017	102.333%
From December 15, 2017 to and including December 14, 2018	101.167%
From December 15, 2018 and thereafter	100.000%

In addition, at any time prior to December 15, 2013, the Company may redeem up to 35% of the aggregate principal amount of the 2020 Notes at a specified redemption price set forth in the Indenture, plus accrued and unpaid interest and additional interest, if any, with the net cash proceeds of an equity offering subject to certain provisions. If the Company experiences certain change of control events, it must offer to repurchase the 2020 Notes at 101% of their principal amount, plus accrued and unpaid interest and additional interest, if any.

The Indenture contains covenants that, among other things, restrict the Company's ability and the ability of its restricted subsidiaries to incur certain additional indebtedness and issue preferred stock, make restricted payments, sell certain assets, agree to any restrictions on the ability of restricted subsidiaries to make payments to the Company, create certain liens, merge, consolidate, or sell substantially all of the Company's assets, or enter into certain transactions with affiliates. These covenants are subject to a number of important exceptions and qualifications, including the fall away or revision of certain of these covenants upon the 2020 Notes receiving investment grade credit ratings.

We recognized \$21.7 million of interest expense related to our 2020 Notes for the nine months ended September 30, 2011.

**7.25% Senior Notes Due 2022**

On June 8, 2011, we issued \$400 million in aggregate principal amount of 7.25% Senior Notes due 2022 (the 2022 Notes) at an issue price of par. The 2022 Notes were issued in a private offering for resale to qualified institutional buyers pursuant to Rule 144A under the Securities Act of 1933, as amended. The 2022 Notes are senior unsecured obligations of the Company and are guaranteed on a senior unsecured basis by certain of the Company's domestic subsidiaries. Interest on the 2022 Notes is payable semiannually in arrears on January 15 and July 15 of each year, beginning on January 15, 2012. The 2022 Notes will mature on January 15, 2022, subject to earlier repurchase or redemption in accordance with the terms of the Indenture incorporated by reference herein. We received proceeds of approximately \$388.7 million from the issuance, net of certain costs of the offering, including \$7.9 million of costs paid to investment bankers that also helped structure the AMS acquisition.

On or after July 15, 2016, the Company may on any one or more occasions redeem all or a part of the 2022 Notes, at the redemption prices (expressed as percentages of principal amount) set forth below, plus accrued and

**Table of Contents**

unpaid interest and additional interest, if any, if redeemed during the twelve-month period beginning on July 15 of the years indicated below:

<b>Payment Dates (between indicated dates)</b>	<b>Redemption Percentage</b>
From July 15, 2016 to and including July 14, 2017	103.625%
From July 15, 2017 to and including July 14, 2018	102.417%
From July 15, 2018 to and including July 14, 2019	101.208%
From July 15, 2019 and thereafter	100.000%

In addition, at any time prior to July 15, 2016, Endo may on any one or more occasions redeem all or a part of the 2022 notes at a specified redemption price set forth in the Indenture, plus accrued and unpaid interest and additional interest, if any.

At any time prior to July 15, 2014, the Company may redeem up to 35% of the aggregate principal amount of the 2022 Notes at a specified redemption price set forth in the Indenture, plus accrued and unpaid interest and additional interest, if any, with the net cash proceeds of an equity offering subject to certain provisions. If the Company experiences certain change of control events, it must offer to repurchase the 2022 Notes at 101% of their principal amount, plus accrued and unpaid interest and additional interest, if any.

The Indenture contains covenants that, among other things, restrict the Company's ability and the ability of its restricted subsidiaries to incur certain additional indebtedness and issue preferred stock, make restricted payments, sell certain assets, agree to any restrictions on the ability of restricted subsidiaries to make payments to the Company, create certain liens, merge, consolidate, or sell substantially all of the Company's assets, or enter into certain transactions with affiliates. These covenants are subject to a number of important exceptions and qualifications, including the fall away or revision of certain of these covenants upon the 2022 Notes receiving investment grade credit ratings.

We recognized \$9.4 million of interest expense related to our 2022 Notes for the nine months ended September 30, 2011.

***1.75% Convertible Senior Subordinated Notes Due 2015***

In April 2008, we issued \$379.5 million in aggregate principal amount of 1.75% Convertible Senior Subordinated Notes due April 15, 2015 (the Convertible Notes) in a private offering for resale to qualified institutional buyers pursuant to Rule 144A under the Securities Act of 1933, as amended.

We received proceeds of approximately \$370.7 million from the issuance, net of the initial purchaser's discount and certain other costs of the offering. Interest is payable semiannually in arrears on each April 15 and October 15 with the first interest payment being made on October 15, 2008. The Convertible Notes will mature on April 15, 2015, unless earlier converted or repurchased by us.

Holders of the Convertible Notes may convert their notes based on a conversion rate of 34.2466 shares of our common stock per \$1,000 principal amount of notes (the equivalent of \$29.20 per share), subject to adjustment upon certain events, only under the following circumstances as described in the Indenture for the Convertible Notes (the Indenture): (1) during specified periods, if the price of our common stock reaches specified thresholds; (2) if the trading price of the Convertible Notes is below a specified threshold; (3) at any time after October 15, 2014; or (4) upon the occurrence of certain corporate transactions. We will be permitted to deliver cash, shares of Endo common stock or a combination of cash and shares, at our election, to satisfy any future conversions of the Convertible Notes. It is our current intention to settle the principal amount of any conversion consideration in cash.

Concurrently with the issuance of the Convertible Notes, we entered into a privately negotiated convertible note hedge transaction with affiliates of the initial purchasers. Pursuant to the hedge transaction we purchased common stock call options intended to reduce the potential dilution to our common stock upon conversion of the Convertible Notes by effectively increasing the initial conversion price of the Convertible Notes to \$40.00 per share, representing a 61.1% conversion premium over the closing price of our common stock on April 9, 2008 of \$24.85 per share. The call options allow us to purchase up to approximately 13.0 million shares of our common stock at an initial strike price of \$29.20 per share. The call options expire on April 15, 2015 and must be net-share settled. The

**Table of Contents**

cost of the call option was approximately \$107.6 million. In addition, we sold warrants to affiliates of certain of the initial purchasers whereby they have the option to purchase up to approximately 13.0 million shares of our common stock at an initial strike price of \$40.00 per share. The warrants expire on various dates from July 14, 2015 through October 6, 2015 and must be net-share settled. We received approximately \$50.4 million in cash proceeds from the sale of these warrants. The warrant transaction could have a dilutive effect on our net income per share to the extent that the price of our common stock exceeds the strike price of the warrants at exercise.

As discussed in Note 13, in periods in which our common stock price exceeds the conversion price of the Convertible Notes or the strike price of the warrants, we include the effects of the additional shares that may be issued in our diluted net income per share calculation using the treasury stock method.

On January 1, 2009 the Company retrospectively adopted the provisions of the authoritative guidance relating to the accounting for convertible debt instruments. The guidance requires that issuers of convertible debt instruments that may be settled in cash or other assets on conversion to separately account for the liability and equity components of the instrument in a manner that will reflect the entity's nonconvertible debt borrowing rate on the instrument's issuance date when interest cost is recognized in subsequent periods.

As a result of our adoption, we separated the debt portion of our Convertible Notes from the equity portion at their fair value retrospective to the date of issuance and are amortizing the resulting discount into interest expense over the life of the Convertible Notes.

The carrying values of the debt and equity components of our Convertible Notes at September 30, 2011 and December 31, 2010 are as follows (in thousands):

	September 30, 2011	December 31, 2010
Principal amount of Convertible Notes	\$ 379,500	\$ 379,500
Unamortized discount related to the debt component(1)	(85,553)	(100,578)
<b>Net carrying amount of the debt component</b>	<b>\$ 293,947</b>	<b>\$ 278,922</b>
Carrying amount of the equity component	\$ 142,199	\$ 142,199

(1) Represents the unamortized portion of the original purchaser's discount and certain other costs of the offering as well as the unamortized portion of the discount created from the separation of the debt portion of our Convertible Notes from the equity portion. This discount will be amortized to interest expense over the term of the Convertible Notes.

We recognized \$20.0 million and \$21.5 million of interest expense for the nine months ended September 30, 2011 and 2010, respectively. For the amounts recognized in 2011, \$5.0 million related to the contractual interest payments and \$15.0 million related to the amortization of the debt discount and certain other costs of the offering. This compared to \$7.7 million of contractual interest payments and \$13.8 million related to the amortization of the debt discount and certain other costs of the offering for the nine months ended September 30, 2010.

**3.25% Convertible AMS Notes Due 2036 and 4.00% Convertible AMS Notes Due 2041**

As a result of our acquisition of AMS, the Company assumed AMS's 3.25% Convertible Notes due 2036 (the 2036 Notes) and 4.00% Convertible Notes due 2041 (the 2041 Notes and, together with the 2036 Notes, the AMS Notes). In accordance with the indentures governing the AMS Notes, the AMS Notes were immediately convertible upon the closing of Endo's acquisition of AMS. From the AMS Acquisition Date until the make whole premium on the 2036 Notes expired on August 9, 2011, we paid \$95.7 million to redeem \$61.4 million of the 2036 Notes at a stated premium of 1.5571. From the AMS Acquisition Date until the make whole premium on the 2041 Notes expired on August 1, 2011, we paid \$423.4 million to redeem \$249.9 million of the 2041 Notes at a stated premium of 1.6940. Our obligation remaining related to the AMS Notes is less than \$1.0 million at September 30, 2011, excluding accrued interest.

**Table of Contents**

We recognized less than \$0.1 million of interest expense related to the AMS Notes for the nine months ended September 30, 2011.

***Non-recourse Notes***

On August 26, 2008, Indevus closed a private placement to institutional investors of \$105.0 million in aggregate principal amount of 16% non-convertible, non-recourse, secured promissory notes due 2024 (Non-recourse Notes). The Non-recourse Notes were issued by Ledgemont Royalty Sub LLC (Royalty Sub), which was a wholly-owned subsidiary of Indevus at the time of the Non-recourse Note issuance and subsequently became a wholly-owned subsidiary of the Company upon our acquisition of Indevus. As of the Indevus Acquisition Date, the Company recorded these notes at their fair value of approximately \$115.2 million and began amortizing these notes to their face value of \$105.0 million at maturity in 2024.

In August 2009, the Company commenced a cash tender offer for any and all outstanding Non-recourse notes. The purpose of the tender offer was to acquire any and all Notes to reduce our consolidated interest expense. The aggregate principal amount of Non-recourse Notes purchased represented approximately 46% of the \$105 million aggregate principal amount of Non-recourse Notes that were outstanding prior to the Expiration Time. Accordingly, the Company recorded a \$4.0 million gain on the extinguishment of debt, net of transaction costs. The gain was calculated as the difference between the aggregate amount paid to purchase the Non-recourse Notes and their carrying amount.

During the third quarter of 2010, Endo notified the holders of its intent to exercise its option to redeem the remaining \$57 million of principal at 108% of the principal amount for approximately \$62 million (amount excludes accrued and unpaid interest) on November 5, 2010. The Non-recourse Notes were redeemed in November 2010.

**Table of Contents****NOTE 16. DERIVATIVE INSTRUMENTS AND HEDGING ACTIVITIES**

We are exposed to certain risks relating to our ongoing business operations. We use derivative instruments to mitigate a portion of our exposure to volatility in foreign currency exchange rates. Foreign currency exchange forward contracts are used to manage the currency risk associated with forecasted sales to and receivables from certain subsidiaries, denominated in their local currencies. We hedge only exposures in the ordinary course of business. We account for our derivative instruments at fair value, which is determined based on quoted prices for similar contracts.

We account for certain of our derivative instruments under hedge accounting provided we meet designation documentary and analytic requirements. Hedge accounting creates the potential for a Consolidated Statement of Operations match between the changes in fair value of derivatives and the changes in the cost of the associated underlying transactions, in this case translation gain or loss. The effective portion of the change in the fair value of foreign currency exchange contracts is reported in accumulated other comprehensive income, a component of stockholders' equity, and is recognized as an adjustment to other (expense) income, in the same period the related expenses are recognized in earnings. The ineffective portion of contracts designated for hedge accounting and the gain or loss from changes in the fair value of contracts not designated for hedge accounting and contracts where hedge accounting is discontinued when it is determined the underlying transaction is not going to occur, are recognized currently in the Consolidated Statements of Operations. Amounts due from counterparties (unrealized hedge gains) or due to counterparties (unrealized hedge losses) are included in accounts receivable, net or other accrued expenses, respectively. Cash receipts or payments related to our derivatives are classified in the Consolidated Statement of Cash Flows as cash flows from operating activities, consistent with the related items being hedged, unless the derivative is not designated or does not qualify for hedge accounting, in which case the receipts or payments are classified in cash flows from investing activities.

At September 30, 2011, we have foreign currency exchange forward contracts outstanding which are intended as hedges of currency fluctuations for a portion of our forecasted sales to certain subsidiaries, denominated in euros, British pounds, Canadian dollars, Australian dollars, and Swedish krona. These derivative instruments have remaining terms between one and twelve months. Under applicable accounting guidance, we ceased applying hedge accounting treatment for these types of contracts upon acquisition of AMS. Consequently, changes in the market value were recognized currently in earnings during the third quarter. These contracts have been re-designated for hedge accounting effective October 4, 2011. The notional amount of these foreign currency exchange forward contracts was \$27.3 million at September 30, 2011. For these type of contracts purchased after the acquisition, hedge accounting was used during the third quarter. The notional amount of these foreign currency exchange forward contracts was \$10.1 million at September 30, 2011.

We have also entered into foreign currency exchange forward contracts to manage a portion of our exposure to foreign exchange rate fluctuations on certain inter-company receivables denominated in euros, British pounds, Canadian dollars, and Australian dollars. The notional amount of these contracts was \$12.0 million at September 30, 2011. The associated underlying transactions are expected to occur within the next month. These contracts do not qualify for hedge accounting.

At September 30, 2011 the fair value of derivatives designated for hedge accounting of \$0.4 million and derivatives not designated for hedge accounting of \$0.5 million was included in accounts receivable, net in the Consolidated Balance Sheets. The gain of \$0.4 million from contracts designated for hedge accounting was included in other comprehensive income and is expected to be reclassified into earnings within the next twelve months. No amounts were reclassified from accumulated other comprehensive income during the quarter. The amount of gain recognized in other (expense) income from contracts not designated for hedge accounting during the quarter was \$3.2 million.

**NOTE 17. SUPPLEMENTAL GUARANTOR INFORMATION**

In connection with the 2019 Notes, 2020 Notes and 2022 Notes, we have included this supplemental guarantor disclosure in accordance with Rule 3-10(g) of Regulation S-X. The 2019 Notes, 2020 Notes, and 2022 Notes are fully and unconditionally guaranteed, jointly and severally, on a senior unsecured basis by the following nineteen subsidiaries (together, the Guarantor Subsidiaries):

Endo Pharmaceuticals Inc.

Endo Pharmaceuticals Valera Inc.

American Medical Systems Holdings, Inc.

AMS Research Corporation

AMS Sales Corporation

Endo Pharmaceuticals Solutions Inc.

Ledgemont Royalty Sub LLC

American Medical Systems, Inc.

Laserscope

Generics International (US Parent), Inc.

## Edgar Filing: ENDO PHARMACEUTICALS HOLDINGS INC - Form 10-Q

Generics International (US Midco), Inc.

Generics International (US), Inc.

Generics Bidco II, LLC

Wood Park Properties LLC

Quartz Specialty Pharmaceuticals, LLC

Generics International (US Holdco), Inc.

Generics Bidco I, LLC

Moore Mill Properties LLC

Vintage Pharmaceuticals, LLC

Each of the Guarantor Subsidiaries is 100 percent owned by us. The following supplemental condensed consolidating financial information presents the Condensed Consolidated Balance Sheets as of September 30, 2011 and December 31, 2010, the Condensed Consolidated Statements of Operations for the three and nine months ended September 30, 2011 and 2010 and the Condensed Consolidated Statements of Cash Flows for the nine months ended September 30, 2011 and 2010, for the Guarantor Subsidiaries as a group, and separately for our non-Guarantor Subsidiaries as a group.

The following condensed consolidating financial statements are presented using the equity method of accounting for its investments in 100% owned subsidiaries. Under the equity method, the investments in subsidiaries are recorded at cost and adjusted for our share of the subsidiaries cumulative results of operations, capital contributions, distributions and other equity changes. The elimination entries principally eliminate investments in subsidiaries and intercompany balances and transactions. The financial information in this note should be read in conjunction with the Condensed Consolidated Financial Statements presented and other notes related thereto contained in this Quarterly Report on Form 10-Q for the quarter ended September 30, 2011.

**Table of Contents****CONDENSED CONSOLIDATING BALANCE SHEET (UNAUDITED)**

(In thousands)

	As of September 30, 2011				
	Endo Pharmaceuticals Holdings Inc.	Guarantor Subsidiaries	Non-Guarantor Subsidiaries	Eliminations	Consolidated Total
<b>ASSETS</b>					
<b>CURRENT ASSETS:</b>					
Cash and cash equivalents	\$ 41,067	\$ 337,309	\$ 41,295	\$	\$ 419,671
Marketable securities		41,010			41,010
Accounts receivable, net		622,333	69,221	30,430	721,984
Inventories, net		268,279	19,977	(5,716)	282,540
Prepaid expenses and other current assets	144	22,131	7,613	(464)	29,424
Deferred income taxes		176,667	5,808		182,475
<b>Total current assets</b>	<b>41,211</b>	<b>1,467,729</b>	<b>143,914</b>	<b>24,250</b>	<b>1,677,104</b>
INTERCOMPANY RECEIVABLES	769,241	6,576,263	210,379	(7,555,883)	
MARKETABLE SECURITIES		20,396			20,396
PROPERTY, PLANT AND EQUIPMENT, NET		245,235	28,491	(238)	273,488
GOODWILL		2,283,972	236,908	(24,021)	2,496,859
OTHER INTANGIBLES, NET		2,682,420	83,629		2,766,049
INVESTMENT IN SUBSIDIARIES	5,869,407	316,952		(6,186,359)	
OTHER ASSETS	86,835	27,678	12,434		126,947
<b>TOTAL ASSETS</b>	<b>\$ 6,766,694</b>	<b>\$ 13,620,645</b>	<b>\$ 715,755</b>	<b>\$(13,742,251)</b>	<b>\$ 7,360,843</b>
<b>LIABILITIES AND STOCKHOLDERS EQUITY</b>					
<b>CURRENT LIABILITIES:</b>					
Accounts payable		238,114	5,542	(9)	243,647
Accrued expenses	31,588	592,990	30,030		654,608
Current portion of long-term debt	70,313	972	3,049		74,334
Acquisition-related contingent consideration		6,063	165		6,228
Income taxes payable	(14,681)	38,634	(9,134)		14,819
<b>Total current liabilities</b>	<b>87,220</b>	<b>876,773</b>	<b>29,652</b>	<b>(9)</b>	<b>993,636</b>
INTERCOMPANY PAYABLES	1,189,346	6,278,356	88,181	(7,555,883)	
DEFERRED INCOME TAXES	2,865	724,348	180		727,393
ACQUISITION-RELATED CONTINGENT CONSIDERATION		2,529			2,529
LONG-TERM DEBT, LESS CURRENT PORTION, NET	3,562,775		2,409		3,565,184
OTHER LIABILITIES		73,988	10,548		84,536
<b>STOCKHOLDERS EQUITY:</b>					
Preferred Stock					
Common Stock	1,378				1,378
Additional paid-in capital	933,584	4,234,518	536,536	(4,771,054)	933,584
Retained earnings (deficit)	1,515,316	1,431,801	(9,698)	(1,422,103)	1,515,316
Accumulated other comprehensive loss	(7,298)	(1,668)	(5,130)	6,798	(7,298)
Treasury stock	(518,492)				(518,492)
<b>Total Endo Pharmaceuticals Holdings Inc. stockholders equity</b>	<b>1,924,488</b>	<b>5,664,651</b>	<b>521,708</b>	<b>(6,186,359)</b>	<b>1,924,488</b>

Edgar Filing: ENDO PHARMACEUTICALS HOLDINGS INC - Form 10-Q

Noncontrolling interests			63,077		63,077
Total stockholders' equity	1,924,488	5,664,651	584,785	(6,186,359)	1,987,565
<b>TOTAL LIABILITIES AND STOCKHOLDERS EQUITY</b>	<b>\$ 6,766,694</b>	<b>\$ 13,620,645</b>	<b>\$ 715,755</b>	<b>\$ (13,742,251)</b>	<b>\$ 7,360,843</b>



**Table of Contents****CONDENSED CONSOLIDATING BALANCE SHEET (UNAUDITED)**

(In thousands)

	As of December 31, 2010				
	Endo Pharmaceuticals Holdings Inc.	Guarantor Subsidiaries	Non-Guarantor Subsidiaries	Eliminations	Consolidated Total
<b>ASSETS</b>					
<b>CURRENT ASSETS:</b>					
Cash and cash equivalents	\$ 45,400	\$ 404,169	\$ 16,645	\$	\$ 466,214
Accounts receivable, net		514,566	33,246	(5)	547,807
Inventories, net		168,003	10,802		178,805
Prepaid expenses and other current assets		18,091	4,750		22,841
Income taxes receivable	5,858	(8,814)	6,099		3,143
Deferred income taxes		130,933	9,791		140,724
Total current assets	51,258	1,226,948	81,333	(5)	1,359,534
INTERCOMPANY RECEIVABLES	(69,344)	3,013,958	6,866	(2,951,480)	
MARKETABLE SECURITIES		23,509			23,509
PROPERTY, PLANT AND EQUIPMENT, NET		186,109	29,186		215,295
GOODWILL		561,725	153,280		715,005
OTHER INTANGIBLES, NET		1,460,295	71,465		1,531,760
INVESTMENT IN SUBSIDIARIES	3,302,001	(32)		(3,301,969)	
OTHER ASSETS		62,964	4,322		67,286
<b>TOTAL ASSETS</b>	<b>\$ 3,283,915</b>	<b>\$ 6,535,476</b>	<b>\$ 346,452</b>	<b>\$ (6,253,454)</b>	<b>\$ 3,912,389</b>
<b>LIABILITIES AND STOCKHOLDERS EQUITY</b>					
<b>CURRENT LIABILITIES:</b>					
Accounts payable	\$	\$ 238,374	\$ 2,740	\$	\$ 241,114
Accrued expenses	1,388	456,063	12,275	(5)	469,721
Current portion of long-term debt	22,500		2,493		24,993
Total current liabilities	23,888	694,437	17,508	(5)	735,828
INTERCOMPANY PAYABLES	460,776	2,431,113	59,591	(2,951,480)	
DEFERRED INCOME TAXES	7,472	222,118	(12,256)		217,334
ACQUISITION-RELATED CONTINGENT CONSIDERATION	7,050	9,000			16,050
LONG-TERM DEBT, LESS CURRENT PORTION, NET	1,043,138		2,663		1,045,801
OTHER LIABILITIES		83,553	10,494		94,047
<b>STOCKHOLDERS EQUITY:</b>					
Preferred Stock					
Common Stock	1,363				1,363
Additional paid-in capital	860,882	1,833,515	214,844	(2,048,359)	860,882
Retained earnings (deficit)	1,364,297	1,262,901	(8,130)	(1,254,771)	1,364,297
Accumulated other comprehensive loss	(1,161)	(1,161)		1,161	(1,161)
Treasury stock	(483,790)				(483,790)
Total Endo Pharmaceuticals Holdings Inc. stockholders equity	1,741,591	3,095,255	206,714	(3,301,969)	1,741,591
Noncontrolling interests			61,738		61,738

Edgar Filing: ENDO PHARMACEUTICALS HOLDINGS INC - Form 10-Q

Total stockholders' equity	1,741,591	3,095,255	268,452	(3,301,969)	1,803,329
<b>TOTAL LIABILITIES AND STOCKHOLDERS EQUITY</b>	<b>\$ 3,283,915</b>	<b>\$ 6,535,476</b>	<b>\$ 346,452</b>	<b>\$ (6,253,454)</b>	<b>\$ 3,912,389</b>

**Table of Contents****CONDENSED CONSOLIDATING STATEMENT OF OPERATIONS (UNAUDITED)****(In thousands)**

	For the Three Months Ended September 30, 2011				
	Endo Pharmaceuticals Holdings Inc.	Guarantor Subsidiaries	Non- Guarantor Subsidiaries	Eliminations	Consolidated Total
TOTAL REVENUES	\$	\$ 706,337	\$ 86,045	\$ (33,304)	\$ 759,078
COSTS AND EXPENSES:					
Cost of revenues		287,446	49,830	(35,104)	302,172
Selling, general and administrative	24	221,033	23,302		244,359
Research and development		43,606	278		43,884
Impairment of long-lived assets		22,691			22,691
Acquisition-related items		6,060	(242)		5,818
OPERATING (LOSS) INCOME	(24)	125,501	12,877	1,800	140,154
INTEREST EXPENSE, NET	1,963	50,818	11		52,792
OTHER (INCOME) EXPENSE, NET		(3,525)	455	70	(3,000)
(LOSS) INCOME BEFORE INCOME TAX	(1,987)	78,208	12,411	1,730	90,362
INCOME TAX	(1,143)	35,099	(637)	738	34,057
EQUITY FROM EARNINGS (LOSS) IN SUBSIDIARIES	41,493	(98)		(41,395)	
CONSOLIDATED NET INCOME	40,649	43,011	13,048	(40,403)	56,305
Less: Net income attributable to noncontrolling interests			15,656		15,656
NET INCOME (LOSS) ATTRIBUTABLE TO ENDO PHARMACEUTICALS HOLDINGS INC.	\$ 40,649	\$ 43,011	\$ (2,608)	\$ (40,403)	\$ 40,649

**Table of Contents****CONDENSED CONSOLIDATING STATEMENT OF OPERATIONS (UNAUDITED)**

(In thousands)

	For the Nine Months Ended September 30, 2011				
	Endo Pharmaceuticals Holdings Inc.	Guarantor Subsidiaries	Non- Guarantor Subsidiaries	Eliminations	Consolidated Total
TOTAL REVENUES	\$	\$ 1,809,956	\$ 193,661	\$ (76,902)	\$ 1,926,715
COSTS AND EXPENSES:					
Cost of revenues		738,961	110,320	(78,854)	770,427
Selling, general and administrative	58	540,457	41,363		581,878
Research and development		126,576	278		126,854
Impairment of long-lived assets		22,691			22,691
Acquisition-related items	(7,050)	35,288	1,279		29,517
OPERATING INCOME	6,992	345,983	40,421	1,952	395,348
INTEREST EXPENSE, NET	28,226	68,905	11		97,142
LOSS ON EXTINGUISHMENT OF DEBT, NET	8,548				8,548
OTHER (INCOME) EXPENSE, NET		(3,024)	88	159	(2,777)
(LOSS) INCOME BEFORE INCOME TAX	(29,782)	280,102	40,322	1,793	292,435
INCOME TAX	(13,431)	112,156	757	801	100,283
EQUITY FROM EARNINGS IN SUBSIDIARIES	167,370	954		(168,324)	
CONSOLIDATED NET INCOME	151,019	168,900	39,565	(167,332)	192,152
Less: Net income attributable to noncontrolling interests			41,133		41,133
NET INCOME (LOSS) ATTRIBUTABLE TO ENDO PHARMACEUTICALS HOLDINGS INC.	151,019	168,900	(1,568)	(167,332)	151,019

**Table of Contents****CONDENSED CONSOLIDATING STATEMENT OF OPERATIONS (UNAUDITED)**

(In thousands)

For the Three Months Ended September 30, 2010

	Endo Pharmaceuticals Holdings Inc.	Guarantor Subsidiaries	Non-Guarantor Subsidiaries	Eliminations	Consolidated Total
TOTAL REVENUES	\$	\$ 392,417	\$ 51,686	\$	\$ 444,103
COSTS AND EXPENSES:					
Cost of revenues		107,414	26,506		133,920
Selling, general and administrative	9,924	114,457	13,435		137,816
Research and development		31,445			31,445
Impairment of long-lived assets					
Acquisition-related items	890	24,100			24,990
OPERATING (LOSS) INCOME	(10,814)	115,001	11,745		115,932
INTEREST EXPENSE, NET	9,021	3,958			12,979
OTHER EXPENSE (INCOME), NET		347	(406)		(59)
(LOSS) INCOME BEFORE INCOME TAX	(19,835)	110,696	12,151		103,012
INCOME TAX	(3,400)	39,595	(2,655)		33,540
EQUITY FROM EARNINGS IN SUBSIDIARIES	70,641			(70,641)	
CONSOLIDATED NET INCOME	54,206	71,101	14,806	(70,641)	69,472
Less: Net income attributable to noncontrolling interests			15,266		15,266
NET INCOME (LOSS) ATTRIBUTABLE TO ENDO PHARMACEUTICALS HOLDINGS INC.	\$ 54,206	\$ 71,101	\$ (460)	\$ (70,641)	\$ 54,206

**Table of Contents****CONDENSED CONSOLIDATING STATEMENT OF OPERATIONS (UNAUDITED)**

(In thousands)

	For the Nine Months Ended September 30, 2010				
	Endo Pharmaceuticals Holdings Inc.	Guarantor Subsidiaries	Non- Guarantor Subsidiaries	Eliminations	Consolidated Total
TOTAL REVENUES	\$	\$ 1,153,353	\$ 51,686	\$	\$ 1,205,039
COSTS AND EXPENSES:					
Cost of revenues		308,703	26,506		335,209
Selling, general and administrative	9,940	381,027	13,435		404,402
Research and development		105,269			105,269
Impairment of long-lived assets		13,000			13,000
Acquisition-related items	1,780	29,535			31,315
OPERATING (LOSS) INCOME	(11,720)	315,819	11,745		315,844
INTEREST EXPENSE, NET	21,466	11,301			32,767
OTHER INCOME, NET		(73)	(406)		(479)
(LOSS) INCOME BEFORE INCOME TAX	(33,186)	304,591	12,151		283,556
INCOME TAX	(7,776)	112,700	(2,655)		102,269
EQUITY FROM EARNINGS IN SUBSIDIARIES	191,431			(191,431)	
CONSOLIDATED NET INCOME	166,021	191,891	14,806	(191,431)	181,287
Less: Net income attributable to noncontrolling interests			15,266		15,266
NET INCOME (LOSS) ATTRIBUTABLE TO ENDO PHARMACEUTICALS HOLDINGS INC.	\$ 166,021	\$ 191,891	\$ (460)	\$ (191,431)	\$ 166,021

**Table of Contents****CONDENSED CONSOLIDATING STATEMENT OF CASH FLOWS (UNAUDITED)**

(In thousands)

	Nine Months Ended September 30, 2011				Consolidated Total
	Endo Pharmaceuticals Holdings Inc.	Guarantor Subsidiaries	Non-Guarantor Subsidiaries	Eliminations	
<b>OPERATING ACTIVITIES:</b>					
Net cash provided by (used in) operating activities	(51,709)	301,150	169,090		418,531
<b>INVESTING ACTIVITIES:</b>					
Purchases of property, plant and equipment, net		(34,176)	(5,433)		(39,609)
Proceeds from sale of property, plant and equipment, net		340	807		1,147
Acquisitions, net of cash acquired		(2,243,486)	(124,871)		(2,368,357)
Proceeds from investments		36,000			36,000
Purchases of investments		(6,009)			(6,009)
Other investments		436	(824)		(388)
Payment on contingent consideration			(662)		(662)
License fees		(2,300)			(2,300)
Proceeds from sale of business			12,990		12,990
Net cash (used in) investing activities		(2,249,195)	(117,993)		(2,367,188)
<b>FINANCING ACTIVITIES:</b>					
Capital lease obligations repayments					
Tax benefits of stock awards		5,519			5,519
Exercise of Endo Pharmaceuticals Holdings Inc. stock options	21,780				21,780
Proceeds from issuance of 2019 and 2022 Notes	900,000				900,000
Purchase of common stock	(34,702)				(34,702)
Proceeds from issuance of Term Loans	2,200,000				2,200,000
Principal payments on Term Loan	(550,813)				(550,813)
Payment on AMS Convertible Notes		(519,040)			(519,040)
Deferred financing fees	(81,535)				(81,535)
Distributions to noncontrolling interests			(39,392)		(39,392)
Buy-out of noncontrolling interests, net of contributions			(402)		(402)
Proceeds from other debt, net			302		302
Intercompany activity	(2,407,354)	2,394,706	12,648		
Net cash (used in) provided by financing activities	47,376	1,881,185	(26,844)		1,901,717
Effect of foreign exchange rate			397		397
NET (DECREASE) INCREASE IN CASH AND CASH EQUIVALENTS	(4,333)	(66,860)	24,650		(46,543)
CASH AND CASH EQUIVALENTS, BEGINNING OF PERIOD	45,400	404,169	16,645		466,214
CASH AND CASH EQUIVALENTS, END OF PERIOD	\$ 41,067	\$ 337,309	\$ 41,295	\$	\$ 419,671





**Table of Contents****CONDENSED CONSOLIDATING STATEMENT OF CASH FLOWS (UNAUDITED)****(In thousands)**

	<b>Nine Months Ended September 30, 2010</b>				
	<b>Endo Pharmaceuticals Holdings Inc.</b>	<b>Guarantor Subsidiaries</b>	<b>Non-Guarantor Subsidiaries</b>	<b>Eliminations</b>	<b>Consolidated Total</b>
<b>OPERATING ACTIVITIES:</b>					
Net cash provided by (used in) operating activities	177,843	(130,498)	235,639		282,984
<b>INVESTING ACTIVITIES:</b>					
Purchases of property, plant and equipment, net		(10,278)	(1,040)		(11,318)
Proceeds from sales of trading securities		230,867			230,867
Acquisitions, net of cash acquired		(125,274)	(208,075)		(333,349)
Other investments		(1,648)			(1,648)
Net cash provided by (used in) investing activities		93,667	(209,115)		(115,448)
<b>FINANCING ACTIVITIES:</b>					
Capital lease obligations repayments		(285)			(285)
Tax benefits of stock awards		2,074			2,074
Exercise of Endo Pharmaceuticals Holdings Inc. stock options	8,728				8,728
Purchase of common stock	(58,974)				(58,974)
Principal payment on HealthTronics senior credit facility		(40,000)			(40,000)
Distributions to noncontrolling interests			(13,971)		(13,971)
Buy-out of noncontrolling interests, net of contributions			(725)		(725)
Proceeds from other debt, net		1,230			1,230
Intercompany activity	(125,274)	125,274			
Net cash (used in) provided by financing activities	(175,520)	88,293	(14,696)		(101,923)
<b>NET INCREASE IN CASH AND CASH EQUIVALENTS</b>					
	2,323	51,462	11,828		65,613
<b>CASH AND CASH EQUIVALENTS, BEGINNING OF PERIOD</b>					
	42,586	665,720	156		708,462
<b>CASH AND CASH EQUIVALENTS, END OF PERIOD</b>					
	\$ 44,909	\$ 717,182	\$ 11,984	\$	\$ 774,075

**Table of Contents**

**NOTE 18. SUBSEQUENT EVENTS**

On October 28, 2011, our subsidiary Endo Pharmaceuticals Inc., (the Tenant), entered into a lease agreement with RT/TC Atwater LP, a Delaware limited partnership relating to new Company headquarters consisting of approximately 300,000 square feet of office space located at 1400 Atwater Boulevard, Malvern, Pennsylvania. This lease is guaranteed by the Company.

The term of this lease is one-hundred and forty-four months, which is expected to commence in late 2012, and includes three renewal options, each for an additional sixty (60) month period. The monthly lease rate for the initial year will be \$466,250, and will increase by 2.25% each subsequent year. Under the terms of this lease, the Tenant will have a continuous and recurring right throughout the initial four (4) years of the lease term to lease up to an additional approximately one hundred fifty thousand (150,000) square feet. Additionally, as this is a build-to-suit lease agreement, the Tenant is responsible for all tenant improvement costs, less a tenant improvement allowance of \$45 per square foot times the rentable square footage of the building.

This lease agreement is filed herewith as Exhibit 99.1 and is incorporated herein by reference.

## **Table of Contents**

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

The following Management's Discussion and Analysis of Financial Condition and Results of Operations describes the principal factors affecting the results of operations, liquidity and capital resources, and critical accounting estimates of Endo. This discussion should be read in conjunction with the accompanying quarterly unaudited Condensed Consolidated Financial Statements and our Annual Report on Form 10-K, for the year ended December 31, 2010 (Annual Report). Our Annual Report includes additional information about our significant accounting policies, practices and the transactions that underlie our financial results, as well as a detailed discussion of the most significant risks and uncertainties associated with our financial and operating results. Except for the historical information contained in this Report, this Report, including the following discussion, contains forward-looking statements that involve risks and uncertainties. See "Forward-Looking Statements" beginning on page i of this Report.

## **EXECUTIVE SUMMARY**

### *About the Company*

We are a United States-based, specialty healthcare solutions company with a diversified business model, operating in three key business segments—branded pharmaceuticals, generics, and devices and services. We deliver an innovative suite of complementary branded and generic drugs, devices, services and clinical data to meet the needs of patients in areas such as pain management, urology, endocrinology and oncology. We believe that recent healthcare reform in the United States places a premium on providing cost-effective healthcare solutions, like those we offer. Over the past two years, we have successfully invested in and reshaped our company through a combination of organic and strategic growth initiatives, creating a vertically integrated company that we believe is positioned to address the changing economics that are driving the transformation of the U.S. healthcare environment.

We have built a diversified business model with three key business segments—branded pharmaceuticals, generics, and devices and services—providing focused solutions primarily in the pain management and urology therapeutic areas with an emerging presence in the oncology and endocrinology space. We believe this business model enables us to strengthen our partnerships with providers, payers and patients by offering multiple products and platforms to deliver healthcare solutions. We have a portfolio of branded pharmaceuticals that includes established brand names such as Lidoderm®, Opana® ER and Opana®, Percocet®, Frova®, Voltaren® Gel, Vantas®, Valstar®, Supprelin® LA and Fortesta® Gel. Branded products comprised approximately 62% of our revenues in the nine months ended September 30, 2011, with 31% of our revenues coming from Lidoderm. Our non-branded generic portfolio, which accounted for 22% of revenues in the nine months ended September 30, 2011, currently consists of products primarily focused on pain management. We focus on selective generics that we believe have one or more barriers to market entry, such as complex formulation, regulatory or legal challenges or difficulty in raw material sourcing. Additionally, we have a growing devices and services portfolio, which accounted for the remainder of our revenues for the nine months ended September 30, 2011. We generated total revenues of \$1,926.7 million for the nine months ended September 30, 2011.

On June 17, 2011, the Company acquired AMS, a provider of devices and therapies for male and female pelvic health. AMS is a market leading provider of medical devices and therapies that help restore pelvic health, and is recognized as a technology leader for developing minimally invasive and more cost effective solutions, serving urologists, urogynecologists, and gynecologists.

In November 2010, we acquired Qualitest, a leading United States based privately-held generics company. As a combined company, we expect to deliver more comprehensive healthcare solutions across our diversified businesses in Branded Pharmaceuticals, Generics, and Devices and Services in key therapeutic areas including pain and urology. Qualitest, the fifth largest U.S. generics company, as measured by prescriptions filled in the year ended December 31, 2010, is focused on cost-competitive, high-quality manufactured products with cost advantages or with high barriers to entry. We believe Qualitest brings critical mass to our current generics business, further diversifies our business lines and product offerings and enhances our portfolio of pain management products.

In July 2010, we completed our acquisition of HealthTronics, a provider of healthcare services and manufacturer of medical devices, primarily for the urology community. In September 2010, we acquired Penwest, a drug development company.

Financial information presented herein reflects the operating results of AMS from and including June 18, 2011 and of Qualitest, HealthTronics, and Penwest from January 1, 2011.

We have a dedicated pharmaceutical products sales forces in the United States, consisting of 440 Endo pharmaceutical sales representatives and 228 sales contracted representatives focusing primarily on pain products, 71 Endo sales representatives focusing primarily on bladder and prostate cancer products, 31 Endo medical center representatives focusing on the treatment of central precocious puberty and 23 Endo account executives focusing on managed markets customers. We also have 372 sales representatives focusing primarily on devices and services. We market our products and services to primary care physicians and specialty physicians, including those specializing in pain management,

## Edgar Filing: ENDO PHARMACEUTICALS HOLDINGS INC - Form 10-Q

orthopedics, neurology, rheumatology, surgery, anesthesiology, urology and pediatric endocrinology. Our sales force also targets retail pharmacies and other healthcare professionals throughout the United States.

---

## **Table of Contents**

### ***Changes in Directors & Officers and Other Related Matters***

On March 3, 2011, the Registrant increased the size of its Board of Directors from eight to nine and appointed David B. Nash, M.D., M.B.A. to fill this new vacancy. Dr. Nash is the founding dean of the Jefferson School of Population Health, located on the campus of Thomas Jefferson University in Philadelphia, Pennsylvania, having taken that position in 2008. Previously, Dr. Nash was the Chairman of the Department of Health Policy of the Jefferson Medical College from 2003 to 2008. Dr. Nash is internationally recognized for his work in outcomes management, medical staff development and quality-of-care improvement; his publications have appeared in more than 100 articles in major journals. Dr. Nash serves on the Board of Directors of Humana Inc., one of the nation's largest publicly traded health and supplemental benefits companies. Dr. Nash also has served as a member of the Board of Trustees of Catholic Healthcare Partners in Cincinnati, Ohio. The Board believes that Dr. Nash brings a value-added set of attributes that enhance the Company's ability to help people achieve lifelong well-being. Dr. Nash is a widely recognized innovator in an emerging medical discipline that unites population health, health policy, and individual health.

### ***Healthcare Reform***

On March 23, 2010, President Obama signed into law H.R. 3590, the Patient Protection and Affordable Care Act (PPACA), which will make major changes to the U.S. healthcare system. On March 30, 2010, the President signed H.R. 4872, the Health Care and Education Reconciliation Act of 2010 (Reconciliation Act), which included a package of changes to the PPACA, as well as additional elements to reform health care in the United States.

While some provisions of the new healthcare reform law have already taken effect, most of the provisions to expand access to health care coverage will not be implemented until 2014 and beyond. Since implementation is incremental to the enactment date of the law, there are still many challenges and uncertainties ahead. Such a comprehensive reform measure will require expanded implementation efforts on the part of federal and state agencies embarking on rule-making to develop the specific components of their new authority. The Company will monitor closely the implementation and any attempts to repeal, replace, or remove funding of the new health care reform law. This effort will primarily take place on two fronts: 1) in Congress through attempts to pass legislation to overturn all or specific sections of the law and 2) in the Courts through attempts to have the law declared unconstitutional.

The passage of the PPACA and the Reconciliation Act will result in a transformation of the delivery and payment for health care services in the U.S. The combination of these measures will expand health insurance coverage to an estimated 32 million Americans. In addition, there are significant health insurance reforms that are expected to improve patients' ability to obtain and maintain health insurance. Such measures include: the elimination of lifetime caps; no rescission of policies; and no denial of coverage due to preexisting conditions. The expansion of healthcare insurance and these additional market reforms should result in greater access to the Company's products.

Our estimate of the overall impact of healthcare reform reflects a number of uncertainties. However, we believe that the 2011 impact to our business will be largely attributable to changes in the Medicare Part D Coverage Gap, the imposition of an annual fee on branded prescription pharmaceutical manufacturers, and increased rebates in the Medicaid Fee-For-Service Program and Medicaid Managed Care plans. There are a number of other provisions in the legislation that collectively are expected to have a small impact, including originator average manufacturers price (AMP) for new formulations, and the expansion of 340B pricing to new entities. These various elements of healthcare reform are expected to adversely impact total revenues by approximately \$40 million in 2011 compared to approximately \$20 million in 2010.

In the United States, the Medicare Prescription Drug Improvement and Modernization Act of 2003 continues to provide an effective prescription drug benefit to seniors and individuals with disabilities in the Medicare program (Medicare Part D). Currently, uncertainty exists due to several Congressional proposals, some of which were considered during the debate on increasing the federal debt ceiling, that have the potential to impose new costs and increase pricing pressures on the pharmaceutical industry.

In response to the U.S. debt-ceiling crisis, Congress passed the Budget Control Act of 2011 on August 2, 2011. Within the Act, Congress created the Joint Select Committee on Deficit Reduction (JSC), which is charged with issuing a formal recommendation on how to reduce the federal deficit by \$1.2 to \$1.5 trillion over the next ten years. The Committee must finalize its deficit reduction plan by November 23, 2011 and Congress must hold an up-or-down vote on the report by December 23, 2011. If the committee fails to agree on a package or the full Congress fails to pass it, a process of sequestration occurs which will result in across-the-board spending cuts to certain government programs, including Medicare, in order to meet the deficit reduction goal. The JSC is considering a number of policy options for inclusion in its formal recommendation, some of which would impact the pharmaceutical industry and Endo.

### ***FDA Advisory Committee Regarding Acetaminophen***

## Edgar Filing: ENDO PHARMACEUTICALS HOLDINGS INC - Form 10-Q

The FDA held a public advisory committee meeting in June 2009 to discuss acetaminophen use in both over-the-counter (OTC) and prescription (Rx) products, the potential for liver injury, and potential interventions to reduce the incidence of liver injury. The panel's recommendations followed the release in May 2009 of an FDA report that found severe liver damage, and even death, can result from a lack of consumer awareness that acetaminophen can cause such injury. These recommendations were advisory in nature and the FDA was not bound to follow these recommendations.

On January 14, 2011, the FDA announced in the Federal Register that it was taking steps to reduce the maximum amount of acetaminophen in prescription drug products, to help reduce or prevent the risk of liver injury from an unintentional overdose of acetaminophen. A variety of combination drug products include acetaminophen, such as those that contain the opioids oxycodone hydrochloride or hydrocodone bitartrate and acetaminophen, among others. Under additional authority granted to the FDA by the Food and Drug Administration Amendments Act of 2007, the FDA notified holders of approved NDAs and ANDAs that they would

## **Table of Contents**

be required to modify the labeling of prescription acetaminophen drug products to reflect new safety information about acetaminophen and liver toxicity. The FDA also announced that it was asking product sponsors to limit the maximum strength of acetaminophen per unit of the combination drug products to 325 mg over a three-year phase-out period. At the end of that period, the FDA could seek to withdraw those products that contain more than 325 mg of acetaminophen from the market. Among the products impacted by the FDA's action are three Endo combination drug pain relief products: Percocet®, Endocet® and Zydone. These regulatory changes, or others required by the FDA, could have an adverse effect on our business, financial condition, results of operations, and cash flows.

### ***Pipeline Developments***

In June 2011, we announced topline results from a Phase II study comparing the novel investigational drug axomadol against placebo in the treatment of patients with moderate to severe chronic lower back pain. The results indicate that axomadol did not meet predetermined study end points. In August 2011, we terminated the Grünenthal Axomadol Agreement, effective August 17, 2011.

In February 2011, the FDA requested that additional pre-clinical studies, including a carcinogenicity study, be completed prior to the submission of the NDA for the octreotide implant for the treatment of acromegaly. Although this development causes a delay of up to four years in the timing associated with regulatory approval, the Company intends to continue the development of this product and is encouraged by recent preliminary results from its Phase III study.

In addition, the Company recently assessed all of its in-process research and development assets and concluded, separately, to discontinue development of its octreotide implant for the treatment of carcinoid syndrome due to recent market research that indicates certain commercial challenges, including the expected rate of physician acceptance and the expected rate of existing patients willing to switch therapies.

In January 2011, the Company entered into a Discovery, Development and Commercialization Agreement (the 2011 Orion Agreement) with Orion Corporation (Orion) to exclusively co-develop products for the treatment of certain cancers and solid tumors. In January 2011, Endo exercised its option to obtain a license to jointly develop and commercialize Orion's Anti-Androgen program focused on castration-resistant prostate cancer, one of Orion's four contributed research programs, and made a corresponding payment to Orion for \$10 million, which was expensed in the first quarter of 2011.

In July 2010, we filed an NDA with the FDA for a new extended-release formulation of oxymorphone, which is a semi-synthetic opioid analgesic intended for the treatment of moderate to severe chronic pain in patients requiring continuous, around-the-clock opioid treatment for an extended period of time. The NDA submission is based on a non-clinical and clinical development program designed to demonstrate the crush-resistant properties of this formulation of oxymorphone. In January 2011, we received a complete response letter from the FDA. The FDA issues complete response letters to communicate that its initial review of an NDA or ANDA is complete and that the application cannot be approved in its present form. A complete response also informs applicants of changes that must be made before an application can be approved, with no implication regarding the ultimate approvability of the application. The letter did not require that additional clinical studies be conducted for approval of the NDA. On June 23, 2011, we received notification from the FDA that Endo's complete response to the FDA's January 2011 complete response letter has been accepted. The FDA has set a Prescription Drug User Fee Act (PDUFA) date of December 13, 2011.

### ***Business Activity***

In December 2010, the FDA approved Fortesta™ Gel for the treatment of Low T, also known as hypogonadism. Endo introduced Fortesta™ Gel in the United States during the first quarter of 2011.

In June 2011, we initiated a voluntary nationwide recall of two lots of Endocet®. The Company's decision was primarily based on a June FDA Field Alert notifying us that pills of Endocet® 10/650mg dosage strength were found in at least one bottle of Endocet® 10/325mg dosage strength. The recall is ongoing and we do not expect it to have a material adverse effect on our business, financial condition, results of operations or cash flows. We are working with the third party manufacturer to investigate the finding and determine the root cause. Should it be determined that the third party manufacturer was responsible, we would expect them to reimburse us for all costs associated with the recall, currently estimated at \$3.6 million.

In September 2011, we initiated a voluntary nationwide retail-level recall of multiple lots of oral contraceptives. The recall is being implemented because of a packaging error, where select blisters were rotated 180 degrees within the card, reversing the weekly tablet orientation and making the lot number and expiry date no longer visible. These packaging defects do not pose any immediate health risks. Our third party manufacturer has assumed responsibility and will reimburse us for up to \$6.0 million of the total costs associated with the recall, currently estimated at \$10.7 million.

**RESULTS OF OPERATIONS**

Our quarterly results have fluctuated in the past, and may continue to fluctuate. These fluctuations are primarily due to (1) the timing of mergers, acquisitions and other business development activity, (2) the timing of new product launches, (3) purchasing patterns of our customers, (4) market acceptance of our products, (5) the impact of competitive products and products we recently acquired and (6) pricing. These fluctuations are also attributable to charges incurred for compensation related to stock compensation, amortization of intangible assets, impairment of intangible assets, and certain upfront, milestone and certain other payments made or accrued pursuant to acquisition or licensing agreements.



**Table of Contents****Consolidated Results Review**

**Revenues.** Revenues for the three and nine months ended September 30, 2011 increased 71% to \$759.1 million and 60% to \$1,926.7 million, respectively, from the comparable 2010 periods. These increases in revenues are primarily driven by organic growth in our branded pharmaceuticals product portfolio, including Opana ER and Voltaren Gel, as well as incremental revenues from our AMS and 2010 acquisitions, including \$158.3 million in revenues from AMS, \$325.1 million in revenues from Qualitest, and \$153.7 million in revenues from HealthTronics, which we acquired in June 2011, November 2010, and July 2010, respectively. Sales growth of our branded pharmaceuticals was essentially volume driven, while price fluctuations had no material impact.

The following table displays our revenues by category and as a percentage of total revenues for the three and nine months ended September 30, 2011 and 2010 (dollars in thousands). Certain prior year amounts have been reclassified to conform to the current year presentation:

	Three Months Ended September 30,				Nine months ended September 30,			
	2011		2010		2011		2010	
	\$	%	\$	%	\$	%	\$	%
Lidoderm®	\$ 207,364	27	\$ 196,263	44	\$ 592,929	31	\$ 574,960	48
Opana® ER	97,753	13	58,809	13	275,221	14	165,130	14
Voltaren® Gel	36,260	5	26,947	6	104,213	5	73,632	6
Percocet®	28,130	4	29,950	7	82,765	4	90,428	8
Frova®	14,815	2	14,136	3	42,186	2	43,898	4
Supprelin® LA	12,695	2	11,018	2	36,432	2	33,814	3
Other brands	28,494	4	27,863	6	65,546	3	90,500	8
Total brands*	425,511	56	364,986	82	1,199,292	62	1,072,362	89
Total generics	147,975	19	27,431	6	415,431	22	80,991	7
Total devices and services revenue	185,592	24	51,686	12	311,992	16	51,686	4
Total revenues*	\$ 759,078	100	\$ 444,103	100	\$ 1,926,715	100	\$ 1,205,039	100

\* Percentages may not add due to rounding.

**Lidoderm®.** Net sales of Lidoderm® for the three and nine months ended September 30, 2011 increased 6% to \$207.4 million and 3% to \$592.9 million, respectively, from the comparable 2010 periods. The increase in Lidoderm® is primarily attributable to increased volumes compared to the same period in 2010.

**Opana® ER.** Net Sales of Opana® ER for the three and nine months ended September 30, 2011 increased 66% to \$97.8 million and 67% to \$275.2 million, respectively, from the comparable 2010 periods. The growth in net sales is primarily attributable to continued prescription and market share growth of the product, as we continue to drive our promotional efforts through physician targeting. In addition, our strategy to aggressively contract with managed care organizations has resulted in increases in volume as we have broadened our access for the brand.

**Voltaren® Gel.** Net sales of Voltaren® Gel for the three and nine months ended September 30, 2011 increased 35% to \$36.3 million and 42% to \$104.2 million, respectively, from the comparable 2010 periods. The Company launched Voltaren® Gel in March 2008 and we believe the growth of Voltaren® Gel since its launch is driven by the product's proven clinical efficacy combined with our continued promotional activities aimed at increasing product awareness in the target audience.

**Percocet®.** Net sales of Percocet® for the three and nine months ended September 30, 2011 decreased 6% to \$28.1 million and 8% to \$82.8 million, respectively, from the comparable 2010 periods. The decreases are primarily attributable to decreased volumes compared to 2010.

**Frova®.** Net sales of Frova® for the three and nine months ended September 30, 2011 increased 5% to \$14.8 million and decreased 4% to \$42.2 million, respectively, from the comparable 2010 periods. The increase for the three months ended September 30, 2011 is primarily attributable to improvements in price realization. The decrease for the nine months ended September 30, 2011 is primarily attributable to reduced volumes during the first nine months of 2011 as compared to 2010, partially offset by improvements in price realization.

## Edgar Filing: ENDO PHARMACEUTICALS HOLDINGS INC - Form 10-Q

*Supprelin® LA*. Net sales of Supprelin® LA for the three and nine months ended September 30, 2011 increased 15% to \$12.7 million and 8% to \$36.4 million, respectively, from the comparable 2010 periods. These increases were driven by volume growth during the first nine months of 2011, resulting primarily from an increase in new patient starts and a growing base of continued care

**Table of Contents**

patients. We believe this growth is largely due to a strong base of national opinion leader support and ongoing efforts to streamline the treatment initiation process.

*Other brands.* Net sales of our other branded products for the three and nine months ended September 30, 2011 increased 2% to \$28.5 million and decreased 28% to \$65.5 million, from the comparable 2010 periods. The increase for the three months ended September 30, 2011 is primarily attributable to sales of Fortesta™ Gel, which we introduced in the United States during the first quarter of 2011, partially offset by decreased sales of Opana® as demand shifted to Opana® ER. The decrease for the nine months ended September 30, 2011 was primarily driven by decreased sales of Opana®. Additionally, sales declines in Vantas® were offset by increased sales from Valstar® and certain other brands.

*Generics.* Net sales of our generic products for the three and nine months ended September 30, 2011 increased 439% to \$148.0 million and 413% to \$415.4 million, respectively, from the comparable 2010 periods. This increase was largely attributable to our acquisition of Qualitest on November 30, 2010, which contributed \$113.6 million and \$325.1 million of net sales of generic products during the three and nine months ended September 30, 2011, respectively.

*Devices and Services.* Revenue for the three and nine months ended September 30, 2011 increased 259% to \$185.6 million and 504% to \$312.0 million, respectively, from the comparable 2010 periods. These amounts consist entirely of revenues from the acquisition of HealthTronics in July 2010 and AMS in June 2011.

*Gross Margin, Costs and Expenses.* The following table sets forth costs and expenses for the three and months ended September 30, 2011 and 2010:

	Three Months Ended September 30,		2010		Nine months ended September 30,		2010	
	2011	% of Revenues	2010	% of Revenues	2011	% of Revenues	2010	% of Revenues
	\$		\$		\$		\$	
Cost of revenues	\$ 302,172	40	\$ 133,920	30	\$ 770,427	40	\$ 335,209	28
Selling, general and administrative	244,359	32	137,816	31	581,878	30	404,402	34
Research and development	43,884	6	31,445	7	126,854	7	105,269	9
Impairment of long-lived assets	22,691	3			22,691	1	13,000	1
Acquisition related costs	5,818	1	24,990	6	29,517	2	31,315	3
Total costs and expenses*	\$ 618,924	82	\$ 328,171	74	\$ 1,531,367	79	\$ 889,195	74

\* Percentages may not add due to rounding.

*Cost of Revenues and Gross Margin.* Cost of revenues for the three and nine months ended September 30, 2011 increased 126% to \$302.2 million and 130% to \$770.4 million, respectively, from the comparable 2010 periods. This increase was primarily driven by our second half 2010 acquisitions as well as our June 2011 acquisition of AMS, which, on a combined basis, contributed approximately \$184.9 million and \$443.7 million to our cost of revenues during the three and nine months ended September 30, 2011, respectively, compared to \$26.5 million during the three and nine months ended September 30, 2010. The remaining increase relates to increased sales of our legacy Endo products. Gross profit margins for the three months ended September 30, 2011 and 2010 were 60% and 70%, respectively. Gross profit margins for the nine months ended September 30, 2011 and 2010 were 60% and 72%, respectively. The reduction in gross profit margins is primarily due to our recent acquisitions, which contributed a lower gross profit margin percentage than Endo's legacy products. Gross profit margin has also been unfavorably impacted by the increased amortization expense during the three and nine months ended September 30, 2011 compared to the comparable 2010 periods as a result of our recent acquisitions.

*Selling, General and Administrative Expenses.* Selling, general and administrative expenses for the three and nine months ended September 30, 2011 increased 77% to \$244.4 million and 44% to \$581.9 million, respectively, from the comparable 2010 periods. This increase was primarily driven by our second half 2010 acquisitions and our June 2011 acquisition of AMS, which, on a combined basis, contributed approximately \$100.6 million and \$152.5 million of expense during the three and nine months ended September 30, 2011, respectively, compared to \$17.7 million during the three and nine months ended September 30, 2010. The increase was also partially driven by certain separation costs associated with our AMS acquisition totaling \$10.2 million for the three months ended September 30, 2011.

**Research and Development Expenses.** Research and development expenses for the three and nine months ended September 30, 2011 increased 40% to \$43.9 million and 21% to \$126.9 million, respectively, from the comparable 2010 periods. These increases were primarily driven by the addition of AMS's, Qualitest's, and Penwest's research and development portfolios to our existing programs, the progress of our branded pharmaceutical portfolio's development, and the expansion of our efforts in the pharmaceutical discovery and device research and development areas.

**Table of Contents**

**Impairment of Long-Lived Assets.** In July 2008, the Company made a \$20 million investment in a privately-held company focused on the development of an innovative treatment for certain types of cancer. In September 2011, we impaired our investment in this privately-held company due to the negative clinical trial results related to its lead asset. Accordingly, we wrote off our investment in its entirety and recorded an impairment charge of \$22.7 million.

**Acquisition Related Items.** Acquisition-related items for the three and nine months ended September 30, 2011 decreased 77% to \$5.8 million and 6% to \$29.5 million, respectively, from the comparable 2010 periods. Acquisition-related items for the three and nine months ended September 30, 2011 primarily consisted of transaction fees of \$6.0 million and \$37.0 million, respectively, including legal, separation, integration, and other expenses for our recent acquisitions, partially offset by favorable changes in the fair value of the acquisition-related contingent consideration of \$0.2 million and \$7.5 million, respectively, which were recorded as gains. The change in the fair value of the acquisition-related contingent consideration primarily reflects changes of our present value assumptions associated with our valuation models. This compares to \$25.0 million in expense and \$31.3 million in expense, respectively, in the comparable 2010 periods resulting from changes in the fair value of the acquisition-related contingent consideration and other miscellaneous transaction and integration costs associated with our July 2010 acquisition of HealthTronics and 2009 acquisition of Indevus.

**Interest Expense, net.** The components of interest expense (income), net at September 30, 2011 and 2010 are as follows (in thousands):

	Three Months Ended September 30,		Nine months ended September 30,	
	2011	2010	2011	2010
Interest expense	\$ 52,939	\$ 13,147	\$ 97,587	\$ 33,782
Interest income	(147)	(168)	(445)	(1,015)
Interest expense, net	\$ 52,792	\$ 12,979	\$ 97,142	\$ 32,767

Interest expense for the three and nine months ended September 30, 2011 increased 303% to \$52.9 million and 189% to \$97.6 million, respectively, from the comparable 2010 periods. This increase is primarily due to \$37.9 million and \$45.1 million, respectively, of interest expense during the three and nine months ended September 30, 2011 resulting from the \$3.1 billion of indebtedness the Company incurred in June of 2011 as well as \$7.3 million and \$29.5 million, respectively, of interest expense during the three and nine months ended September 30, 2011 resulting from the \$800.0 million of indebtedness the Company incurred in November of 2010, \$400.0 million of which remains at September 30, 2011. These increases were partially offset by decreases in interest related to our early retirement of the 2009 Credit Facility and the Non-recourse Notes in 2010 and \$395.0 million of Term Loan debt in June 2011. Changes in interest income for the three and nine months ended September 30, 2011 resulted from fluctuations in the amount of cash invested in interest-bearing accounts, including our money market funds and auction-rate securities and the yields on those investments.

**Other income, net.** The components of Other income, net at September 30, 2011 and 2010 are as follows (in thousands):

	Three Months Ended September 30,		Nine months ended September 30,	
	2011	2010	2011	2010
Gain on trading securities	\$	\$	\$	\$ (15,420)
Loss on auction-rate securities rights				15,659
Other income, net	(3,000)	(59)	(2,777)	(718)
Other income, net	\$ (3,000)	\$ (59)	\$ (2,777)	\$ (479)

## Table of Contents

During the nine months ended September 30, 2010, the value of our trading auction-rate securities increased by \$15.4 million. The increases in fair value were more than offset by losses recorded as a result of decreases in the fair value of our auction-rate securities rights totaling \$15.7 million for the nine months ended September 30, 2010. As all auction-rate securities rights were exercised and all trading auction-rate securities were sold on June 30, 2010, there were no subsequent changes to their respective fair values.

**Income Tax.** Income tax for the three month period ended September 30, 2011 increased 2% to \$34.1 million from the comparable 2010 period. This increase is due to an increase in the effective income tax rate to 37.7% from 32.6% in the comparable 2010 period, offset by a decrease in pre-tax income. The increase in the effective income tax rate is primarily due to the establishment of a valuation allowance in the current period against an anticipated capital loss on our cost method investment in a privately-held company and an increase in the non-deductible charge for the Branded Prescription Drug fee. The increase is partially offset by the release of FIN 48 reserves due to statute of limitation expirations, an increase in the Domestic Production Activities deduction, the inclusion of transaction costs on acquisitions in the comparable 2010 period, a benefit from the Research and Development credit that was expired during the comparable 2010 period, and an increase in the Orphan Drug credit.

Income tax for the nine months ended September 30, 2011, decreased 2% from the comparable 2010 period to \$100.3 million. This fluctuation is due to the decrease in our effective income tax rate to 34.3% from 36.1% in the comparable 2010 period. The decrease in the effective income tax rate is primarily due to non-taxable income attributable to noncontrolling interests assumed as part of the HealthTronics acquisition, the release of FIN 48 reserves due to statute of limitation expirations, an increase in the Domestic Production Activities deduction, a benefit from non-taxable reductions in the fair value of contingent consideration as compared to non-deductible increases in the fair value in the comparable prior period, a benefit from the Research and Development credit that was expired during the comparable 2010 period, and an increase in the Orphan Drug credit, partially offset by the establishment of a valuation allowance in the current period against an anticipated capital loss on our cost method investment in a privately-held company, and an increase in the non-deductible charge for the Branded Prescription Drug fee.

**2011 Outlook.** We estimate that our 2011 total revenue will be between \$2.72 billion and \$2.80 billion with total Branded Pharmaceuticals segment revenues between \$1.625 billion and \$1.69 billion, total Generics segment revenue between \$550.0 million and \$575.0 million and total Device and Services segment revenue between \$520.0 million and \$550.0 million. Our estimate is based on the continued growth of both our generic and branded product portfolios, driven by ongoing prescription demand for our key inline products, including Lidoderm<sup>®</sup>, Opana<sup>®</sup> ER, and Voltaren<sup>®</sup> Gel, and by new revenues from launching Fortesta<sup>™</sup> Gel, the full-year effect of our acquisitions of Qualitest and HealthTronics, and approximately six months of revenues from AMS, which was acquired in June 2011. Cost of revenues as a percent of total revenues is expected to increase when compared to 2010. This increase is expected due to a full year of amortization expense associated with the intangible assets acquired with Qualitest and HealthTronics, approximately six months of amortization expenses associated with the intangible assets acquired with AMS, and a change in the mix of revenues as a result of the AMS, Qualitest, Penwest, and HealthTronics acquisitions. Selling, general and administrative expenses as a percentage of revenues are expected to decline in 2011, relative to 2010, reflecting new approaches to customer segmentation and marketing, annualized effects of the prior year's cost reduction efforts and forecasted synergies associated with our 2010 acquisitions and our acquisition of AMS. Selling, general and administrative expenses, however, will increase, reflecting the full year effects of our 2010 acquisitions and approximately six months of expenses from AMS. We will continue to provide promotional support behind our key on-market products. Research and development expenses are expected to increase due to the addition of AMS's and Qualitest's research and development portfolios to our existing programs, the progress of our branded pharmaceutical portfolio's development, and the expansion of our efforts in the pharmaceutical discovery and device research and development areas. There can be no assurance that the Company will achieve these results.

## **Business Segment Results Review**

As a result of our 2010 acquisitions, the Company realigned its internal management reporting in 2010 to reflect a total of three reportable segments. These segments reflect the level at which executive management regularly reviews financial information to assess performance and to make decisions about resources to be allocated.

The three reportable business segments in which the Company now operates include: (1) Branded Pharmaceuticals, (2) Generics and (3) Devices and Services. Each segment derives revenue from the sales or licensing of their respective products or services and is discussed below.

**Branded Pharmaceuticals.** This group of products includes a variety of branded prescription products related to treating and managing pain as well as our urology, endocrinology and oncology products. The established products that are included in this operating segment includes Lidoderm<sup>®</sup>, Opana<sup>®</sup> ER and Opana<sup>®</sup>, Percocet<sup>®</sup>, Voltaren<sup>®</sup> Gel, Frova<sup>®</sup>, Supprelin<sup>®</sup> LA, Vantas<sup>®</sup>, and Valstar<sup>®</sup>.

**Generics.** This segment is comprised of our legacy Endo non-branded generic portfolio and the portfolio from our recently acquired Qualitest business. Our generics business has historically focused on selective generics related to pain that have one or more barriers to market entry, such as complex formulation, regulatory or legal challenges or difficulty in raw material sourcing. With the addition of Qualitest, the segment's

## Edgar Filing: ENDO PHARMACEUTICALS HOLDINGS INC - Form 10-Q

product offerings now include products in the pain management, urology, central nervous system (CNS) disorder, immunosuppression, oncology and hypertension markets, among others.

***Devices and Services.*** The Devices and Services operating segment provides urological services, products and support systems to urologists, hospitals, surgery centers and clinics across the United States. These services and products are sold through the following eight business lines: men's health, women's health, BPH therapy, lithotripsy services, prostate treatment services, radiation therapy services, anatomical pathology services, and medical products manufacturing, sales and maintenance.

**Table of Contents**

In 2010, the Company began to evaluate segment performance based on each segment's adjusted income (loss) before income tax. We define adjusted income (loss) before income tax as income (loss) before income tax before certain upfront and milestone payments to partners, acquisition-related items, cost reduction initiatives, asset impairment charges, amortization of intangible assets related to marketed products and customer relationships, inventory step-up recorded as part of our acquisitions, non-cash interest expense, and certain other items that the Company believes do not reflect its core operating performance.

Certain corporate general and administrative expenses are not allocated and are therefore included within Corporate unallocated. We calculate consolidated adjusted income (loss) before income tax by adding the adjusted income (loss) before income tax of each of our reportable segments to corporate unallocated adjusted income (loss) before income tax.

Endo refers to adjusted income (loss) before income tax in making operating decisions because it believes it provides meaningful supplemental information regarding the Company's operational performance. For instance, Endo believes that this measure facilitates its internal comparisons to its historical operating results and comparisons to competitors' results. The Company believes this measure is useful to investors in allowing for greater transparency related to supplemental information used by Endo in its financial and operational decision-making. In addition, Endo has historically reported similar financial measures to its investors and believes that the inclusion of comparative numbers provides consistency in its financial reporting at this time. Further, Endo believes that adjusted income (loss) before income tax may be useful to investors as it is aware that certain of its significant stockholders utilize adjusted income (loss) before income tax to evaluate its financial performance. Finally, adjusted income (loss) before income tax is utilized in the calculation of adjusted diluted net income per share, which is used by the Compensation Committee of Endo's Board of Directors in assessing the performance and compensation of substantially all of its employees, including its executive officers.

There are limitations to using financial measures such as adjusted income (loss) before income tax. Other companies in our industry may define adjusted income (loss) before income tax differently than we do. As a result, it may be difficult to use adjusted income (loss) before income tax or similarly named adjusted financial measures that other companies may use to compare the performance of those companies to our performance. Because of these limitations, adjusted income (loss) before income tax should not be considered as a measure of the income generated by our business or discretionary cash available to us to invest in the growth of our business. The Company compensates for these limitations by providing reconciliations of our consolidated adjusted income (loss) before income tax to our consolidated income before income tax, which is determined in accordance with U.S. GAAP and included in the accompanying Condensed Consolidated Statements of Operations.

**Revenues.** The following table displays our revenue by reportable segment for the three and nine months ended September 30 2011 and 2010 (dollars in thousands):

	Three months ended September 30,		Nine months ended September 30,	
	2011	2010	2011	2010
Net revenues to external customers				
Branded Pharmaceuticals	\$ 425,511	\$ 364,986	\$ 1,199,292	\$ 1,072,362
Generics	147,975	27,431	415,431	80,991
Devices and Services	185,592	51,686	311,992	51,686
<b>Total consolidated net revenues to external customers</b>	<b>\$ 759,078</b>	<b>\$ 444,103</b>	<b>\$ 1,926,715</b>	<b>\$ 1,205,039</b>

**Branded Pharmaceuticals.** Net pharmaceutical product sales for the three and nine months ended September 30, 2011 increased 17% to \$425.5 million and 12% to \$1,199.3 million, respectively, from the comparable 2010 periods. These increases were primarily driven by increased revenues of Lidoderm®, Opana® ER and Voltaren® Gel.

**Generics.** Net pharmaceutical product sales for the three and nine months ended September 30, 2011 increased 439% to \$148.0 million and 413% to \$415.4 million, respectively, from the comparable 2010 periods. This increase was largely attributable to our acquisition of Qualitest on November 30, 2010, which contributed \$113.6 million and \$325.1 million of net sales of generic products during the three and nine months ended September 30, 2011, respectively.

**Devices and Services.** Revenue for the three and nine months ended September 30, 2011 increased 259% to \$185.6 million and 504% to \$312.0 million, respectively, from the comparable 2010 periods. These amounts consist entirely of revenues from the acquisition of HealthTronics in July 2010 and AMS in June 2011.



## Edgar Filing: ENDO PHARMACEUTICALS HOLDINGS INC - Form 10-Q

**Adjusted income (loss) before income tax.** The following table displays our adjusted income (loss) before income tax by reportable segment for the three and nine months ended September 30, 2011 and 2010 (dollars in thousands):

	Three months ended September 30,		Nine months ended September 30,	
	2011	2010	2011	2010
Adjusted income (loss) before income tax				

**Table of Contents**

	Three months ended September 30,		Nine months ended September 30,	
	2011	2010	2011	2010
Branded Pharmaceuticals	\$ 231,887	\$ 187,630	\$ 634,762	\$ 540,741
Generics	26,932	2,605	74,445	8,916
Devices and Services	54,755	20,479	94,670	20,479
Corporate unallocated	(93,844)	(50,316)	(217,145)	(138,605)
<b>Total consolidated adjusted income before income tax</b>	<b>\$ 219,730</b>	<b>\$ 160,398</b>	<b>\$ 586,732</b>	<b>\$ 431,531</b>

*Branded Pharmaceuticals.* Adjusted income before income tax for the three and nine months ended September 30, 2011 increased 24% to \$231.9 million and 17% to \$634.8 million, respectively, from the comparable 2010 periods. This increase was primarily driven by increased revenues from our Branded Pharmaceuticals segment as well as the decrease in the royalty expense to Penwest from \$10.2 million and \$29.8 million during the three and nine months ended September 30, 2010, respectively, to zero during the three and nine months ended September 30, 2011. This royalty was eliminated upon our acquisition of Penwest in the third quarter of 2010.

*Generics.* Adjusted income before income tax for the three and nine months ended September 30, 2011 increased 934% to \$26.9 million and 735% to \$74.4 million, respectively, from the comparable 2010 periods. This increase was primarily driven by increased revenues from our Generics segment as well as decreased research and development expense as a percentage of sales.

*Devices and Services.* Adjusted income before income tax during the three and nine months ended September 30, 2011 increased 167% to \$54.8 million and 362% to \$94.7 million, respectively, from the comparable 2010 periods. These amounts consists entirely of the operating results of HealthTronics, which we acquired in July 2010, and AMS, which we acquired in June 2011.

*Corporate unallocated.* Corporate unallocated adjusted loss before income tax for the three and nine months ended September 30, 2011 increased 87% to \$93.8 million and 57% to \$217.1 million, respectively, from the comparable 2010 periods, which is primarily attributable to the overall growth of our business and the related increase in corporate costs, including increases in net interest expense of \$39.8 million and \$64.4 million respectively.

*Reconciliation to GAAP.* The table below provides reconciliations of our consolidated adjusted income (loss) before income tax to our consolidated income before income tax, which is determined in accordance with U.S. generally accepted accounting principles (GAAP), for the three and nine months ended September 30, 2011 and 2010 (in thousands):

	Three months ended September 30,		Nine months ended September 30,	
	2011	2010	2011	2010
Total consolidated adjusted income before income tax	\$ 219,730	\$ 160,398	\$ 586,732	\$ 431,531
Upfront and milestone payments to partners	(2,355)	(309)	(27,346)	(19,200)
Acquisition-related items	(5,818)	(24,990)	(29,517)	(31,315)
Cost reduction initiatives and separation benefits	(13,603)	(7,050)	(17,598)	(16,570)
Impairment of long-lived assets	(22,691)		(22,691)	(13,000)
Amortization of intangible assets related to marketed products and customer relationships	(58,846)	(19,378)	(136,501)	(53,730)
Inventory step-up	(23,937)	(1,414)	(40,718)	(1,414)
Non-cash interest expense	(4,754)	(4,245)	(14,014)	(12,507)
Loss on extinguishment of debt, net			(8,548)	
Gain on hedging activities for foreign currencies	2,636		2,636	
Other (expense) income, net				(239)
<b>Total consolidated income before income tax</b>	<b>\$ 90,362</b>	<b>\$ 103,012</b>	<b>\$ 292,435</b>	<b>\$ 283,556</b>

**LIQUIDITY AND CAPITAL RESOURCES**

Our principal source of liquidity is cash generated from operations. Our principal liquidity requirements are for working capital for operations, licenses, milestone payments, capital expenditures and debt service payments. The Company continues to maintain a sufficient level of working capital, which was approximately \$683.5 million at September 30, 2011 compared to \$623.7 million at December 31, 2010. Historically, we

## Edgar Filing: ENDO PHARMACEUTICALS HOLDINGS INC - Form 10-Q

have generated positive cash flow from operating activities and have had access to broad financial markets that provide liquidity. Cash, cash equivalents and current marketable securities were approximately \$460.7 million at September 30, 2011 compared to \$466.2 million at December 31, 2010. Cash and cash equivalents at September 30, 2011 and December 31, 2010 primarily consisted of bank deposits, time deposits and money market funds.

In 2011, we expect that sales of our currently marketed branded and generic products as well as our devices and services will allow us to continue to generate positive cash flow from operations. We expect cash generated from operations together with our cash,

---

**Table of Contents**

cash equivalents and current marketable securities to be sufficient to cover cash needs for working capital, general corporate expenses, the payment of contractual obligations, including scheduled principal and interest payments on our outstanding borrowings and any regulatory and/or sales milestones that may become due.

Beyond 2011, we expect cash generated from operations together with our cash, cash equivalents and marketable securities to continue to be sufficient to cover cash needs for working capital and general corporate purposes, certain acquisitions of other businesses, including the potential payments of up to approximately \$336.7 million in contingent cash consideration payments related to our acquisitions of Indevus and Qualitest, products, product rights, or technologies, the payment of contractual obligations, including principal and interest payments on our indebtedness and our Revolving Credit Facility (defined below), and certain minimum royalties due to Novartis and the regulatory or sales milestones that may become due. At this time, we cannot accurately predict the effect of certain developments on the rate of sales growth, such as the degree of market acceptance, patent protection and exclusivity of our products, the impact of competition, the effectiveness of our sales and marketing efforts and the outcome of our current efforts to develop, receive approval for and successfully launch our near-term product candidates. Any of the above could adversely affect our future cash flows. We may need to obtain additional funding for future transactions, to repay our outstanding indebtedness, or for our future operational needs, and we cannot be certain that funding will be available on terms acceptable to us, or at all.

We may also elect to incur additional debt or issue equity or convertible securities to finance ongoing operations, acquisitions or to meet our other liquidity needs. Any issuances of equity securities or convertible securities could have a dilutive effect on the ownership interest of our current shareholders and may adversely impact net income per share in future periods. An acquisition may be accretive or dilutive and by its nature, involves numerous risks and uncertainties.

**Credit Facility.** In October 2009, we established a \$300 million, three-year senior secured revolving credit facility (the 2009 Credit Facility) with JP Morgan Chase Bank, Barclays Capital and certain other lenders. The 2009 Credit Facility was available for letters of credit, working capital and general corporate purposes. The 2009 Credit Facility also permitted up to \$100 million of additional revolving or term loan commitments from one or more of the existing lenders or other lenders.

On November 30, 2010, we terminated the 2009 Credit Facility. Concurrent with the termination of the 2009 Credit Facility, we established a \$400 million, five-year senior secured term loan facility (the Term Loan Facility), and a \$500 million, five-year senior secured revolving credit facility (the 2010 Revolving Credit Facility and, together with the Term Loan Facility, the 2010 Credit Facility) with JP Morgan Chase Bank, Royal Bank of Canada, and certain other lenders. The 2010 Credit Facility was established primarily to finance our acquisition of Qualitest and was available for working capital, general corporate purposes and letters of credit. The agreement governing the 2010 Credit Facility (the 2010 Credit Agreement) also permitted up to \$200 million of additional revolving or term loan commitments from one or more of the existing lenders or other lenders with the consent of the JP Morgan Chase Bank (the administrative agent) without the need for consent from any of the existing lenders under the 2010 Credit Facility.

The obligations of the Company under the 2010 Credit Facility were guaranteed by certain of the Company's domestic subsidiaries and were secured by substantially all of the assets of the Company and the subsidiary guarantors. The 2010 Credit Facility contained certain usual and customary covenants, including, but not limited to covenants to maintain maximum leverage and minimum interest coverage ratios. Borrowings under the 2010 Credit Facility bore interest at an amount equal to a rate calculated based on the type of borrowing and the Company's Leverage Ratio. For term loans and revolving loans (other than Swing Line Loans), the Company had been permitted to elect to pay interest based on an adjusted LIBOR rate plus between 2.00% and 2.75% or an Alternate Base Rate (as defined in the 2010 Credit Agreement) plus between 1.00% and 1.75%. The Company had also paid a commitment fee of between 35 to 50 basis points, payable quarterly, on the average daily unused amount of the Revolving Credit Facility.

On June 17, 2011, we terminated the 2010 Credit Facility. Concurrent with the termination of the 2010 Credit Facility, we established a \$1,500 million, five-year senior secured term loan facility (the Term Loan A Facility), a \$700 million, seven-year senior secured term loan facility (the Term Loan B Facility, and, together with the Term Loan A Facility, the Term Loan Facilities), and a \$500 million, five-year senior secured revolving credit facility (the 2011 Revolving Credit Facility and, together with the Term Loan Facilities, the 2011 Credit Facility) with Morgan Stanley Senior Funding, Inc., as administrative agent, Bank of America, N.A., as Syndication Agent, and certain other lenders. The 2011 Credit Facility was established primarily to finance our acquisition of AMS and is available for working capital, general corporate purposes and lines of credit. The agreement governing the 2011 Credit Facility (the 2011 Credit Agreement) also permits up to \$500 million of additional revolving or term loan commitments from one or more of the existing lenders or other lenders with the consent of Morgan Stanley Senior Funding, Inc. (the administrative agent) without the need for consent from any of the existing lenders under the 2011 Credit Facility.

The obligations of the Company under the 2011 Credit Facility are guaranteed by certain of the Company's domestic subsidiaries and are secured by substantially all of the assets of the Company and the subsidiary guarantors. The 2011 Credit Facility contains certain usual and customary covenants, including, but not limited to covenants to maintain maximum leverage and minimum interest coverage ratios. Borrowings under the

## Edgar Filing: ENDO PHARMACEUTICALS HOLDINGS INC - Form 10-Q

2011 Credit Facility bear interest at an amount equal to a rate calculated based on the type of borrowing and the Company's Leverage Ratio. For term A loans and revolving loans (other than Swing Line Loans), the

---

**Table of Contents**

Company is permitted to elect to pay interest based on an adjusted LIBOR rate plus between 1.75% and 2.50% or an Alternate Base Rate (as defined in the 2011 Credit Agreement) plus between 0.75% and 1.50%. For term B loans, the Company may elect to pay interest based on an adjusted LIBOR rate plus 3.00% or an Alternate Base Rate plus 2.00%. The Company will pay a commitment fee of between 37.5 to 50 basis points, payable quarterly, on the average daily unused amount of the Revolving Credit Facility.

In September 2011, we made a \$135.0 million prepayment on our Term Loan B Facility. Pursuant to our rights under the 2011 Credit Agreement, we elected to apply a portion of this prepayment against all remaining contractual payments such that we have no remaining principal payment obligations until the maturity of the Term Loan B Facility on June 17, 2018.

**7.00% Senior Notes Senior Notes due 2019.** On June 8, 2011, we entered into an indenture among the Company, the guarantors named therein and Wells Fargo Bank, National Association, as trustee, which governs the terms of the Company's \$500.0 million aggregate principal amount of 7.00% Senior Notes due 2019 (the 2019 Notes). The 2019 Notes were issued in a private offering exempt from the registration requirements of the Securities Act of 1933, as amended (the Securities Act) to qualified institutional buyers in accordance with Rule 144A and to persons outside of the United States pursuant to Regulation S under the Securities Act. The 2019 Notes are senior unsecured obligations of the Company and are guaranteed on a senior unsecured basis by certain of the Company's domestic subsidiaries. The Company used the net proceeds of the 2019 Notes offering to partially finance the acquisition of AMS, and to pay related fees and expenses.

The 2019 Notes bear interest at a rate of 7.00% per year, accruing from June 8, 2011. Interest on the 2019 Notes is payable semiannually in arrears on January 15 and July 15 of each year, beginning on January 15, 2012. The 2019 Notes will mature on July 15, 2019, subject to earlier repurchase or redemption in accordance with the terms of the indenture governing the 2019 Notes. The indenture governing the 2019 Notes contains covenants that, among other things, restrict the Company's ability and the ability of certain of its restricted subsidiaries to incur certain additional indebtedness and issue preferred stock; make certain dividends, distributions, investments and other restricted payments; sell certain assets; agree to any restrictions on the ability of restricted subsidiaries to make payments to the Company; create certain liens; enter into transactions with affiliates; designate subsidiaries as unrestricted subsidiaries; and consolidate, merge or sell substantially all of the Company's assets. These covenants are subject to a number of important exceptions and qualifications, including the fall away or revision of certain of these covenants upon The 2019 Notes receiving investment grade credit ratings.

**7.00% Senior Notes Senior Notes due 2020.** On November 23, 2010, we entered into an indenture among the Company, the guarantors named therein and Wells Fargo Bank, National Association, as trustee, which governs the terms of the Company's \$400.0 million aggregate principal amount of 7.00% Senior Notes due 2020 (the 2020 Notes). The 2020 Notes were issued in a private offering exempt from the registration requirements of the Securities Act of 1933, as amended (the Securities Act) to qualified institutional buyers in accordance with Rule 144A and to persons outside of the United States pursuant to Regulation S under the Securities Act. The 2020 Notes are senior unsecured obligations of the Company and are guaranteed on a senior unsecured basis by certain of the Company's domestic subsidiaries. The Company used the net proceeds of the 2020 Notes offering to partially finance the acquisition of Qualitest, and to pay related fees and expenses.

The 2020 Notes bear interest at a rate of 7.00% per year, accruing from November 23, 2010. Interest on the 2020 Notes is payable semiannually in arrears on June 15 and December 15 of each year, beginning on June 15, 2011. The 2020 Notes will mature on December 15, 2020, subject to earlier repurchase or redemption in accordance with the terms of the indenture governing the 2020 Notes. The indenture governing the 2020 Notes contains covenants that, among other things, restrict the Company's ability and the ability of certain of its restricted subsidiaries to incur certain additional indebtedness and issue preferred stock; make certain dividends, distributions, investments and other restricted payments; sell certain assets; agree to any restrictions on the ability of restricted subsidiaries to make payments to the Company; create certain liens; enter into transactions with affiliates; designate subsidiaries as unrestricted subsidiaries; and consolidate, merge or sell substantially all of the Company's assets. These covenants are subject to a number of important exceptions and qualifications, including the fall away or revision of certain of these covenants upon The 2020 Notes receiving investment grade credit ratings.

**7.25% Senior Notes Senior Notes due 2022.** On June 8, 2011, we entered into an indenture among the Company, the guarantors named therein and Wells Fargo Bank, National Association, as trustee, which governs the terms of the Company's \$400.0 million aggregate principal amount of 7.25% Senior Notes due 2022 (the 2022 Notes). The 2022 Notes were issued in a private offering exempt from the registration requirements of the Securities Act of 1933, as amended (the Securities Act) to qualified institutional buyers in accordance with Rule 144A and to persons outside of the United States pursuant to Regulation S under the Securities Act. The 2022 Notes are senior unsecured obligations of the Company and are guaranteed on a senior unsecured basis by certain of the Company's domestic subsidiaries. The Company used the net proceeds of the 2022 Notes offering to partially finance the acquisition of AMS, and to pay related fees and expenses.

The 2022 Notes bear interest at a rate of 7.25% per year, accruing from June 8, 2011. Interest on the 2022 Notes is payable semiannually in arrears on January 15 and July 15 of each year, beginning on January 15, 2012. The 2022 Notes will mature on January 15, 2022, subject to earlier repurchase or redemption in accordance with the terms of the indenture governing the 2022 Notes. The indenture governing the 2022 Notes contains covenants that, among other things, restrict the Company's ability and the ability of certain of its restricted subsidiaries to incur

## Edgar Filing: ENDO PHARMACEUTICALS HOLDINGS INC - Form 10-Q

certain additional indebtedness and issue preferred stock; make certain dividends, distributions, investments and other restricted payments; sell certain assets; agree to any restrictions on the ability of restricted subsidiaries to make payments to the Company; create certain liens; enter into transactions with affiliates; designate subsidiaries as

**Table of Contents**

unrestricted subsidiaries; and consolidate, merge or sell substantially all of the Company's assets. These covenants are subject to a number of important exceptions and qualifications, including the fall away or revision of certain of these covenants upon The 2022 Notes receiving investment grade credit ratings.

**16% Non-recourse Notes due 2024.** On August 26, 2008, Indevus closed a private placement to institutional investors of \$105.0 million in aggregate principal amount of 16% non-convertible, non-recourse, secured promissory notes due 2024 (Non-recourse Notes). The Non-recourse Notes were issued by Ledgemont Royalty Sub LLC (Royalty Sub), which was a wholly-owned subsidiary of Indevus at the time of the Non-recourse Note issuance and subsequently became a wholly-owned subsidiary of the Company upon our acquisition of Indevus. As of the Indevus Acquisition Date, the Company recorded these notes at their fair value of approximately \$115.2 million and began amortizing these notes to their face value of \$105.0 million at maturity in 2024.

In August 2009, the Company commenced a cash tender offer for any and all outstanding Non-recourse notes. The purpose of the tender offer was to acquire any and all Notes to reduce our consolidated interest expense. The aggregate principal amount of Non-recourse Notes purchased represented approximately 46% of the \$105 million aggregate principal amount of Non-recourse Notes that were outstanding prior to the Expiration Time. Accordingly, the Company recorded a \$4.0 million gain on the extinguishment of debt, net of transaction costs. The gain was calculated as the difference between the aggregate amount paid to purchase the Non-recourse Notes and their carrying amount.

During the third quarter of 2010, Endo notified the holders of its intent to exercise its option to redeem the remaining \$57 million of principal at 108% of the principal amount for approximately \$62 million (amount excludes accrued and unpaid interest) on November 5, 2010. The Non-recourse Notes were redeemed in November 2010.

**1.75% Convertible Senior Subordinated Notes due 2015.** As discussed in Note 15 to the Condensed Consolidated Financial Statements in Part I, Item 1 of this Report, in April 2008, we issued \$379.5 million in aggregate principal amount of 1.75% Convertible Senior Subordinated Notes due April 15, 2015 (the Convertible Notes) in a private offering for resale to qualified institutional buyers pursuant to Rule 144A under the Securities Act of 1933, as amended.

We received proceeds of approximately \$370.7 million from the issuance, net of the initial purchaser's discount and certain other costs of the offering. Interest is payable semiannually in arrears on each April 15 and October 15 with the first interest payment being made on October 15, 2008. The Convertible Notes will mature on April 15, 2015, unless earlier converted or repurchased by us.

Holders of the Convertible Notes may convert their notes based on a conversion rate of 34.2466 shares of our common stock per \$1,000 principal amount of notes (the equivalent of \$29.20 per share), subject to adjustment upon certain events, only under the following circumstances as described in the Indenture for the Convertible Notes (the Indenture): (1) during specified periods, if the price of our common stock reaches specified thresholds; (2) if the trading price of the Convertible Notes is below a specified threshold; (3) at any time after October 15, 2014; or (4) upon the occurrence of certain corporate transactions. We will be permitted to deliver cash, shares of Endo common stock or a combination of cash and shares, at our election, to satisfy any future conversions of the notes. It is our current intention to settle the principal amount of any conversion consideration in cash.

The Convertible Notes are only included in the dilutive net income per share calculation using the treasury stock method during periods in which the average market price of our common stock was above the applicable conversion price of the Convertible Notes, or \$29.20 per share. In these periods, under the treasury stock method, we calculated the number of shares issuable under the terms of these notes based on the average market price of the stock during the period, and included that number in the total diluted shares outstanding for the period.

We have entered into convertible note hedge and warrant agreements that, in combination, have the economic effect of reducing the dilutive impact of the Convertible Notes. However, we separately analyze the impact of the convertible note hedge and the warrant agreements on diluted weighted average shares outstanding. As a result, the purchases of the convertible note hedges are excluded because their impact would be anti-dilutive. The treasury stock method is applied when the warrants are in-the-money with the proceeds from the exercise of the warrant used to repurchase shares based on the average stock price in the calculation of diluted weighted average shares. Until the warrants are in-the-money, they have no impact to the diluted weighted average share calculation. The total number of shares that could potentially be included if the warrants were exercised is approximately 13 million.

**3.25% Convertible AMS Notes Due 2036 and 4.00% Convertible AMS Notes Due 2041**

As a result of our acquisition of AMS, the Company assumed AMS's 3.25% Convertible Notes due 2036 (the 2036 Notes) and 4.00% Convertible Notes due 2041 (the 2041 Notes and, together with the 2036 Notes, the AMS Notes). In accordance with the indentures governing the AMS Notes, the AMS Notes were immediately convertible upon the closing of Endo's acquisition of AMS. From the AMS Acquisition Date



## Edgar Filing: ENDO PHARMACEUTICALS HOLDINGS INC - Form 10-Q

until the make whole premium on the 2036 Notes expired on August 9, 2011, we paid \$95.7 million to redeem \$61.4 million of the 2036 Notes at a stated premium of 1.5571. From the AMS Acquisition Date until the make whole premium on the 2041 Notes expired on August 1, 2011, we paid \$423.4 million to redeem \$249.9 million of the 2041 Notes at a stated

**Table of Contents**

premium of 1.6940. Our obligation remaining related to the AMS Notes is less than \$1.0 million at September 30, 2011, excluding accrued interest.

**Share Repurchase Program.** Pursuant to our previously announced \$750 million share repurchase plan, we may, from time to time, seek to repurchase our equity in open market purchases, privately-negotiated transactions, accelerated stock repurchase transactions or otherwise. This program does not obligate Endo to acquire any particular amount of common stock. Repurchase activity, if any, will depend on factors such as levels of cash generation from operations, cash requirements for investment in the Company's business, timing and extent of future business development activity, repayment of future debt, if any, current stock price, market conditions and other factors. The share repurchase program may be suspended, modified or discontinued at any time. As a result of a two-year extension approved by the Board of Directors in February 2010, the share repurchase plan is set to expire in April 2012. Pursuant to the existing share repurchase program, we purchased approximately 0.9 million shares of our common stock during the nine month period ended September 30, 2011 totaling \$34.7 million and approximately 2.5 million shares of our common stock during the nine month period ended September 30, 2010 totaling \$59.0 million.

**Marketable Securities.** Beginning in 2008 and continuing through 2011, the securities and credit markets have been experiencing severe volatility and disturbance, increasing risk with respect to certain of our financial assets. As a result of our auction-rate securities rights agreement with UBS (described in more detail below), we have been able to minimize our credit risk losses. On June 30, 2010, we were able to exercise our auction-rate securities rights (the Rights), described below, with UBS and liquidate our remaining UBS auction-rate security portfolio at par value. At September 30, 2011, \$18.8 million of our marketable securities portfolio was invested in auction-rate debt securities with ratings of AAA. Our investment policy seeks to preserve the value of capital, consistent with maximizing return on the Company's investment, while maintaining adequate liquidity and security. This policy specifically prohibits the investment in auction-rate securities as well as the investment in any security that is below investment grade. However, such restrictions were implemented on a prospective basis and did not impact the Company's ability to continue to hold the auction-rate securities it was invested in when the amended investment policy was adopted.

The underlying assets of our auction-rate securities are student loans. Student loans are insured by the Federal Family Education Loan Program, or FFELP.

The Company determined that an income approach (present value technique) that maximizes the use of observable market inputs is the preferred approach to measuring the fair value of our securities. Specifically, the Company used the discount rate adjustment technique to determine an indication of fair value.

To calculate a price for our auction-rate securities, the Company calculates duration to maturity, coupon rates, market required rates of return (discount rate) and a discount for lack of liquidity in the following manner:

The Company identifies the duration to maturity of the auction-rate securities as the time at which principal is available to the investor. This can occur because the auction-rate security is paying a coupon that is above the required rate of return, and the Company treats the security as being called. It can also occur because the market has returned to normal and the Company treats the auctions as having recommenced. Lastly, and most frequently, the Company treats the principal as being returned as prepayment occurs and at the maturity of the security. The initial life used for each remaining security, representing time to maturity, was eight years as of September 30, 2011 and December 31, 2010.

The Company calculates coupon rates based on estimated relationships between the maximum coupon rate (the coupon rate in event of a failure) and market interest rates. The representative coupon rate was 3.80% on September 30, 2011 and 5.10% at December 31, 2010. The Company calculates appropriate discount rates for securities that include base interest rates, index spreads over the base rate, and security-specific spreads. These spreads include the possibility of changes in credit risk over time. The spread over the base rate applied to our securities was 217 basis points at September 30, 2011 and 218 basis points at December 31, 2010.

The Company believes that a market participant would require an adjustment to the required rate of return to adjust for the lack of liquidity. We do not believe it is unreasonable to assume a 150 basis points adjustment to the required rate of return and a term of either three, four or five years to adjust for this lack of liquidity. The increase in the required rate of return decreases the prices of the securities. However, the assumption of a three, four or five-year term shortens the times to maturity and increases the prices of the securities. The Company has evaluated the impact of applying each term and the reasonableness of the range indicated by the results. The Company chose to use a four-year term to adjust for the lack of liquidity as we believe it is the point within the range that is

## Edgar Filing: ENDO PHARMACEUTICALS HOLDINGS INC - Form 10-Q

most representative of fair value. The Company's conclusion is based in part on the fact that the fair values indicated by the results are reasonable in relation to each other given the nature of the securities and current market conditions.

We did not sell any of our remaining auction-rate securities during the nine months ended September 30, 2011. During the nine month period ended September 30, 2010, we sold \$230.3 million of auction-rate securities at par value. Given the uncertainty in the auction-rate securities market, the Company cannot predict when future auctions related to our existing auction-rate securities

**Table of Contents**

portfolio will be successful. However, we do not employ an asset management strategy or tax planning strategy that would require us to sell any of our existing securities at a loss. Furthermore, there have been no adverse changes in our business or industry that could require us to sell the securities at a loss in order to meet working capital requirements.

In October 2008, UBS AG (UBS) made an offer (the UBS Offer) to the Company and other clients of UBS Securities LLC and UBS Financial Services Inc. (collectively, the UBS Entities), pursuant to which the Company received auction-rate securities rights to sell to UBS all auction-rate securities held by the Company as of February 13, 2008 in a UBS account (the Eligible Auction-Rate Securities). The Rights permitted us to require UBS to purchase the Eligible Auction-Rate Securities for a price equal to par value plus any accrued but unpaid dividends or interest beginning on September 30, 2010 and ending on July 2, 2012.

On November 10, 2008, the Company accepted the UBS Offer, awarding the UBS Entities the sole discretion and right to sell or otherwise dispose of, and/or enter orders in the auction process with respect to the Eligible Auction-Rate Securities on the Company's behalf until the expiration date, without prior notification, so long as the Company receives a payment of par value plus any accrued but unpaid dividends or interest upon any sale or disposition. As of June 30, 2010, we exercised the Rights and, on July 1, 2010, received cash for our remaining UBS portfolio at par. Accordingly, as of June 30, 2010, our UBS auction-rate securities were reclassified into a current receivable. The remaining \$18.8 million of our auction-rate securities portfolio, at par-value, is not held in a UBS account and therefore was not subject to the UBS Offer.

As of September 30, 2011, the yields on our long-term auction-rate securities ranged from 0.32% to 0.34%. These yields represent the predetermined maximum reset rates that occur upon auction failures according to the specific terms within each security's prospectus. As of September 30, 2011, the weighted average yields for our long-term auction-rate securities were 0.33%. Total interest recognized on our auction-rate securities during the nine months ended September 30, 2011 and September 30, 2010 was less than \$0.1 million and \$0.6 million, respectively. The issuers have been making interest payments promptly.

At September 30, 2011, the fair value of our auction-rate securities, as determined by applying the above described discount rate adjustment technique, was approximately \$17.4 million, representing an 8%, or \$1.4 million discount from their original purchase price or par value. This compares to approximately \$17.3 million, representing an 8%, or \$1.5 million discount from their original purchase price or par value at December 31, 2010. Had the Company chosen to apply a three or five year term with respect to the liquidity adjustment at September 30, 2011, the resultant discount to the original purchase price or par value would have been \$1.1 million and \$1.7 million, respectively. We believe we have appropriately reflected our best estimate of the assumptions that market participants would use in pricing the assets in a current transaction to sell the asset at the measurement date.

At September 30, 2011 and December 31, 2010, the fair value of our auction-rate securities rights was zero.

**Working Capital.** Working capital increased to \$683.5 million as of September 30, 2011 from \$623.7 million as of December 31, 2010. The components of our working capital as of September 30, 2011 and December 31, 2010 are below:

	September 30, 2011	December 31, 2010
Total current assets	\$ 1,677,104	\$ 1,359,534
Less: Total current liabilities	993,636	735,828
<b>Working capital</b>	<b>\$ 683,468</b>	<b>\$ 623,706</b>

Working capital increased primarily due to the net working capital impact of our June 17, 2011 acquisition of AMS and our operating results.

The following table summarizes our Condensed Consolidated Statements of Cash Flows and liquidity for the nine months ended September 30, 2011 and 2010 (dollars in thousands):

Nine month ended September 30, 2011	Nine month ended September 30, 2010
---	---

Edgar Filing: ENDO PHARMACEUTICALS HOLDINGS INC - Form 10-Q

Net cash flow provided by (used in):		
Operating activities	\$ 418,531	\$ 282,984
Investing activities	(2,367,188)	(115,448)
Financing activities	1,901,717	(101,923)
Effect of foreign exchange rate	397	
Net increase in cash and cash equivalents	(46,543)	65,613
Cash and cash equivalents, beginning of period	466,214	708,462
Cash and cash equivalents, end of period	\$ 419,671	\$ 774,075

**Table of Contents**

	Nine month ended September 30, 2011	Nine month ended September 30, 2010
Current ratio	1.7:1	2.3:1
Days sales outstanding	46	47

**Table of Contents**

**Net Cash Provided by Operating Activities.** Net cash provided by operating activities was \$418.5 million for the nine months ended September 30, 2011 compared to \$283.0 million for the nine months ended September 30, 2010. Significant components of our operating cash flows for the nine months ended September 30, 2011 and 2010 are as follows (in thousands):

	Nine months ended September 30,	
	2011	2010
<b>Cash Flow Data-Operating Activities:</b>		
Consolidated net income	\$ 192,152	\$ 181,287
Depreciation and amortization	169,187	69,859
Stock-based compensation	34,224	16,753
Change in fair value of contingent consideration	(7,458)	2,150
Impairment of long-lived assets	22,691	13,000
Loss on auction-rate securities rights		15,659
Unrealized gain on trading securities		(15,420)
Loss on extinguishment of debt	8,548	
Changes in assets and liabilities which used cash:	(11,748)	(4,470)
Other, net	10,935	4,166
 Net cash provided by operating activities	 \$ 418,531	 \$ 282,984

The increase in net cash provided by operating activities compared to the prior year was primarily attributable to increased consolidated net income in a period of increasing depreciation, amortization, stock-based compensation, and other costs which do not impact net cash provided by operating activities. This increase was partially offset by a decrease in cash inflows during the first nine months of 2011 from changes in assets and liabilities which provided cash, as compared to the first half of 2010.

**Net Cash used in Investing Activities.** Net cash used in investing activities was \$2,367.2 million for the nine months ended September 30, 2011 compared to net cash used in investing activities of \$115.4 million during the same period of 2010. The change is primarily related to net cash paid for acquisitions of \$2,368.4 million.

**Net Cash provided by/used in Financing Activities.** Net cash provided by financing activities was \$1,901.7 million for the nine months ended September 30, 2011 compared to net cash used in financing activities of \$101.9 million during the nine months ended September 30, 2010. The change was primarily a result of our incremental borrowings during the 2011 of \$2,468.0 million, which is net of debt issuance costs of \$81.5 million, partially offset by payments on the AMS Notes of \$519.0 million.

**Research and Development.** Over the past few years, we have incurred significant expenditures related to conducting clinical studies to develop new pharmaceutical products and exploring the value of our existing products in treating disorders beyond those currently approved in their respective labels. We may seek to mitigate the risk in, and expense of, our research and development programs by entering into collaborative arrangements with third parties. However, we intend to retain a portion of the commercial rights to these programs and, as a result, we still expect to spend significant funds on our share of the cost of these programs, including the costs of research, preclinical development, clinical research and manufacturing.

We expect to continue to incur significant levels of research and development expenditures as we focus on the development and advancement of our product pipeline. There can be no assurance that results of any ongoing or future pre-clinical or clinical trials related to these projects will be successful, that additional trials will not be required, that any drug or product under development will receive FDA approval in a timely manner or at all, or that such drug or product could be successfully manufactured in accordance with U.S. current Good Manufacturing Practices, or successfully marketed in a timely manner, or at all, or that we will have sufficient funds to develop or commercialize any of our products.

**Manufacturing, Supply and Other Service Agreements.** We contract with various third-party manufacturers and suppliers to provide us with raw materials used in our products, finished goods, and certain services. Our most significant agreements are with Novartis Consumer Health, Inc., Novartis AG, Teikoku Seiyaku Co., Ltd., Mallinckrodt Inc., Noramco, Inc., Sharp Corporation, and Ventiv Commercial Services, LLC. If, for any reason, we are unable to obtain sufficient quantities of any of the finished goods or raw materials or components required for our products, it could have a material adverse effect on our business, financial condition, results of operations and cash flows. For a complete description of commitments under manufacturing, supply and other service agreements, see Note 12 of the Condensed Consolidated Financial

## Edgar Filing: ENDO PHARMACEUTICALS HOLDINGS INC - Form 10-Q

Statements included in Part I, Item 1 of this Quarterly Report on Form 10-Q.

On March 11, 2011, the northeast coast of Japan experienced a severe earthquake followed by a tsunami, with continuing aftershocks. These geological events have caused significant damage in the region, including severe damage to nuclear power plants, and have impacted Japan's power and other infrastructure as well as its economy. Teikoku Seiyaku Co., Ltd., our sole supplier of Lidoderm<sup>®</sup>, is located in Southeast Japan. The Company does not currently believe these events will have a material impact on its business, results of operations, financial condition or cash flows.



## Table of Contents

**License and Collaboration Agreements.** We have agreed to certain contingent payments in certain of our license, collaboration and other agreements. Payments under these agreements generally become due and payable only upon the achievement of certain developmental, regulatory, commercial and/or other milestones. Due to the fact that it is uncertain if and when these milestones will be achieved, such contingencies have not been recorded in our Condensed Consolidated Balance Sheets. In addition, under certain arrangements, we may have to make royalty payments based on a percentage of future sales of the products in the event regulatory approval for marketing is obtained. From a business perspective, we view these payments favorably as they signify that the products are moving successfully through the development phase toward commercialization. For a complete description of our contingent payments involving our license and collaboration agreements, see Note 8, and Note 12 of the Condensed Consolidated Financial Statements included in Part I, Item 1 of this Quarterly Report on Form 10-Q.

**Acquisitions.** As part of our business strategy, we plan to consider and, as appropriate, make acquisitions of other businesses, products, product rights or technologies. Our cash reserves and other liquid assets may be inadequate to consummate such acquisitions and it may be necessary for us to issue stock or raise substantial additional funds in the future to complete future transactions. In addition, as a result of our acquisition efforts, we are likely to experience significant charges to earnings for merger and related expenses (whether or not our efforts are successful) that may include transaction costs or costs of restructuring activities.

### **AMS**

On June 17, 2011 (the AMS Acquisition Date), the Company completed its acquisition of all outstanding shares of common stock of AMS for approximately \$2.4 billion in aggregate consideration, including \$70.8 million related to existing AMS stock-based compensation awards and certain other amounts, at which time AMS became a wholly-owned subsidiary of the Company. AMS's shares were purchased at a price of \$30.00 per share.

AMS is a worldwide developer and provider of technology solutions to physicians treating men's and women's pelvic health conditions. The AMS business and applicable services include:

#### *Men's Health.*

AMS supplies surgical solutions for the treatment of male urinary incontinence, the involuntary release of urine from the body. The fully implantable AMS 800® system includes an inflatable urethral cuff to restrict flow through the urethra and a control pump that allows the patient to discreetly open the cuff when he wishes to urinate. Since 2000, AMS has also been selling the InVance® sling system, a less-invasive procedure for men with moderate incontinence, and in 2007, AMS released the AdVance® sling system for the treatment of mild to moderate stress urinary incontinence. AMS also offers the UroLume® endoprosthesis stent as a less invasive procedure for patients who may not be good surgical candidates, as well as for men suffering from bulbar urethral strictures.

AMS also supplies penile implants to treat erectile dysfunction, the inability to achieve or maintain an erection sufficient for sexual intercourse, with a series of semi-rigid malleable prostheses and a complete range of more naturally functioning inflatable prostheses, including the AMS 700® MS. AMS has refined its implants over the years with improvements to the AMS 700® series of inflatable prostheses, including the AMS 700 LGX® and the MS Pump®. Another key factor that distinguishes AMS's products is the use of the InhibiZone® antibiotic coating, which received FDA approval in July 2009 for our product claim that InhibiZone® reduces the rate of revision surgery due to surgical infections.

#### *Women's Health.*

AMS offers a broad range of systems, led by Monarc® and MiniArc®, to treat female stress urinary incontinence, which generally results from a weakening of the tissue surrounding the bladder and urethra which can be a result of pregnancy, childbirth and aging. Monarc® incorporates unique helical needles to place a self-fixating, sub-fascial hammock through the obturator foramen. AMS's MiniArc® Single-Incision Sling for stress incontinence was released in 2007 and requires just one incision to surgically place a small sling under the urethra, which minimizes tissue disruption and potential for blood loss, thereby allowing the procedure to be done with less anesthesia on an outpatient basis. In 2010, AMS launched the MiniArc Precise™, which is designed to enhance the ease and accuracy of placement of the MiniArc® device.

AMS also offers solutions for pelvic floor prolapse and other pelvic floor disorders, which may be caused by pregnancy, labor, and childbirth. In 2008, AMS introduced the Elevate® transvaginal pelvic floor repair system, with no external incisions. Using an anatomically designed needle and self-fixating tips, Elevate® allows for safe, simple and precise mesh placement through a single vaginal incision. The posterior system was launched in 2008 and the anterior system was launched in 2009.

#### *BPH Therapy.*

## Edgar Filing: ENDO PHARMACEUTICALS HOLDINGS INC - Form 10-Q

AMS's products can be used to relieve restrictions on the normal flow of urine from the bladder caused by bladder obstructions, generally the result of benign prostatic hyperplasia (BPH) or bulbar urethral strictures. AMS offers men experiencing a physical obstruction of the prostatic urethra an alternative to a transurethral resection of the prostate (TURP), with the GreenLight™ photovaporization of the prostate. This laser therapy is designed to reduce the comorbidities associated with TURP. AMS's GreenLight™ XPS and MoXy™ Liquid Cooled Fiber provide shorter treatment times with similar long-term results compared to other laser systems. The GreenLight™ laser system offers an optimal laser beam that balances vaporization of tissue with coagulation to

**Table of Contents**

prevent blood loss and providing enhanced surgical control compared to other laser systems. AMS also offers the StoneLight® laser and SureFlex™ fiber optics for the treatment of urinary stones. StoneLight® is a lightweight and portable 15-watt holmium laser that offers the right amount of power to effectively fragment most urinary stones. The SureFlex™ fiber optic line is engineered to deliver more energy safely and effectively, even under maximum scope deflection, for high performance holmium laser lithotripsy.

AMS's TherMatr® product is designed for those men not yet to the point of urethral obstruction, but for whom symptomatic relief is desired. It is a less-invasive tissue ablation technique that can be performed in a physician's office using microwave energy delivered to the prostate.

The acquisition of AMS provides Endo scale in its Devices and Services business segment, and the combination of AMS with Endo's existing platform will provide additional cost-effective solutions across the entire urology spectrum.

The operating results of AMS from and including June 18, 2011 are included in the accompanying Condensed Consolidated Statements of Operations. The Condensed Consolidated Balance Sheet as of September 30, 2011 reflects the acquisition of AMS.

The following table summarizes the fair values of the assets acquired and liabilities assumed at the AMS Acquisition Date (in thousands):

	June 17, 2011 (As initially reported)	Measurement period adjustments	June 17, 2011 (As adjusted)
Cash and cash equivalents	\$ 47,289	\$	\$ 47,289
Commercial paper	71,000		71,000
Accounts receivable	73,868		73,868
Other receivables	791		791
Inventories	75,525		75,525
Prepaid expenses and other current assets	7,133		7,133
Income taxes receivable	11,179	(4,022)	7,157
Deferred income taxes	15,360	(829)	14,531
Property and equipment	57,372	(960)	56,412
Other intangible assets	1,390,000		1,390,000
Other assets	4,581		4,581
<b>Total identifiable assets</b>	<b>\$ 1,754,098</b>	<b>\$ (5,811)</b>	<b>\$ 1,748,287</b>
Accounts payable	\$ 9,437	\$	\$ 9,437
Accrued expenses	45,648	150	45,798
Deferred income taxes	507,019	(10,885)	496,134
Long-term debt	520,012	363	520,375
Other liabilities	23,578		23,578
<b>Total liabilities assumed</b>	<b>\$ 1,105,694</b>	<b>\$ (10,372)</b>	<b>\$ 1,095,322</b>
<b>Net identifiable assets acquired</b>	<b>\$ 648,404</b>	<b>\$ 4,561</b>	<b>\$ 652,965</b>
Goodwill	\$ 1,752,427	\$ (5,434)	\$ 1,746,993
<b>Net assets acquired</b>	<b>\$ 2,400,831</b>	<b>\$ (873)</b>	<b>\$ 2,399,958</b>

The above estimated fair values of assets acquired and liabilities assumed are provisional and are based on the information that was available as of the AMS Acquisition Date to estimate the fair value of assets acquired and liabilities assumed. The Company believes that information provides a reasonable basis for estimating the fair values but the Company is waiting for additional information necessary to finalize those amounts, particularly with respect to the estimated fair value of intangible assets, property and equipment, contingent assets and liabilities, and deferred income taxes. Thus, the provisional measurements of fair value reflected are subject to change. Such changes could be significant. The Company expects to finalize the valuation and complete the purchase price allocation as soon as practicable but no later than one year from the AMS Acquisition Date.

## Edgar Filing: ENDO PHARMACEUTICALS HOLDINGS INC - Form 10-Q

The valuation of the intangible assets acquired and related amortization periods are as follows:

	<b>Valuation (in millions)</b>	<b>Amortization Period (in years)</b>
<b>Customer Relationships:</b>		
Men's Health	\$ 97.0	17
Women's Health	49.0	15
BPH	26.0	13

**Table of Contents**

	Valuation (in millions)	Amortization Period (in years)
Total	\$ 172.0	16
<b>Developed Technology:</b>		
Men's Health	\$ 690.0	18
Women's Health	230.0	9
BPH	161.0	18
Total	\$ 1,081.0	16
<b>In Process Research &amp; Development:</b>		
Oracle	\$ 22.0	n/a
Genesis	14.0	n/a
TOPAS	8.0	n/a
Other	22.0	n/a
Total	\$ 66.0	n/a
<b>Tradename:</b>		
AMS	\$ 59.0	n/a
GreenLight	12.0	15
Total	\$ 71.0	n/a
Total other intangible assets	\$ 1,390.0	n/a

The fair value of the developed technology, in-process research and development and customer relationship assets were estimated using a discounted present value income approach. Under this method, an intangible asset's fair value is equal to the present value of the incremental after-tax cash flows (excess earnings) attributable solely to the intangible asset over its remaining useful life. To calculate fair value, the Company used cash flows discounted at rates considered appropriate given the inherent risks associated with each type of asset. The Company believes that the level and timing of cash flows appropriately reflect market participant assumptions. The fair value of the AMS and GreenLight tradenames were estimated using an income approach, specifically known as the relief from royalty method. The relief from royalty method is based on a hypothetical royalty stream that would be received if the Company were to license the AMS or GreenLight tradename. Thus, we derived the hypothetical royalty income from the projected revenues of AMS and GreenLight products, respectively. Cash flows were assumed to extend through the remaining economic useful life of each class of intangible asset.

The \$1,747.0 million of goodwill was assigned to our Devices and Services segment. The goodwill recognized is attributable primarily to strategic and synergistic opportunities across the entire urology spectrum, expected corporate synergies, the assembled workforce of AMS and other factors. Approximately \$17.8 million of goodwill is expected to be deductible for income tax purposes.

Deferred tax assets of \$14.5 million are related primarily to federal net operating loss and credit carryforwards of AMS and its subsidiaries. Deferred tax liabilities of \$496.1 million are related primarily to the difference between the book basis and tax basis of identifiable intangible assets.

The Company recognized \$4.1 million and \$27.3 million of AMS acquisition-related costs that were expensed during the three and nine months ended September 30, 2011, respectively. These costs are included in Acquisition-related items in the accompanying Condensed Consolidated Statements of Operations and are comprised of the following items (in thousands):

Acquisition-related Costs Three months ended September 30,	Acquisition-related Costs Nine months ended September 30, 2011
--	--

Edgar Filing: ENDO PHARMACEUTICALS HOLDINGS INC - Form 10-Q

	2011	
Bank fees	\$	\$ 16,070
Legal, separation, integration, and other costs	4,069	11,263
<b>Total</b>	<b>\$ 4,069</b>	<b>\$ 27,333</b>

The amounts of revenue and net income of AMS included in the Company's Condensed Consolidated Statements of Operations from and including June 18, 2011 to September 30, 2011 are as follows (in thousands, except per share data):

**Table of Contents**

	<b>Revenue and Income included in the Condensed Consolidated Statements of Operations from and including June 18, 2011 to September 30, 2011</b>
Revenue	\$ 158,331
Net loss attributable to Endo Pharmaceuticals Holdings Inc.	\$ (6,527)
Basic and diluted net loss per share	\$ (0.06)

The following supplemental pro forma information presents the financial results as if the acquisition of AMS had occurred on January 1, 2010 for the nine months ended September 30, 2011 and the three and nine months ended September 30, 2010. This supplemental pro forma information has been prepared for comparative purposes and does not purport to be indicative of what would have occurred had the acquisition been made on January 1, 2010, nor are they indicative of any future results.

	<b>Nine months ended September 30, 2011</b>
<b>Pro forma consolidated results (in thousands, except per share data):</b>	
Revenue	\$ 2,165,091
Net income attributable to Endo Pharmaceuticals Holdings Inc.	\$ 130,389
Basic net income per share	\$ 1.12
Diluted net income per share	\$ 1.07

	<b>Three months ended September 30, 2010</b>	<b>Nine months ended September 30, 2010</b>
<b>Pro forma consolidated results (in thousands, except per share data):</b>		
Revenue	\$ 568,285	\$ 1,600,870
Net income attributable to Endo Pharmaceuticals Holdings Inc.	\$ 33,843	\$ 92,610
Basic net income per share	\$ 0.29	\$ 0.80
Diluted net income per share	\$ 0.29	\$ 0.79

These amounts have been calculated after applying the Company's accounting policies and adjusting the results of AMS to reflect factually supportable adjustments that give effect to events that are directly attributable to the AMS Acquisition, including the borrowing under the 2011 Credit Facility, 2019 Notes, and 2022 Notes as well as the additional depreciation and amortization that would have been charged assuming the fair value adjustments primarily to property, plant and equipment, inventory, and intangible assets, had been applied on January 1, 2010, together with the consequential tax effects.

**Qualitest**

On November 30, 2010 (the Qualitest Acquisition Date), Endo completed its acquisition of all of the issued and outstanding capital stock of Generics International (US Parent), Inc. (Qualitest) from an affiliate of Apax Partners, L.P. for approximately \$770.0 million. In addition, Endo paid \$406.8 million to retire Qualitest's outstanding debt and related interest rate swap on November 30, 2010. In connection with the Qualitest acquisition, \$108 million of the purchase price was placed into two separate escrow accounts. One of the escrow accounts was \$8 million, some of which was used to fund working capital adjustments, as defined in the Qualitest Stock Purchase Agreement. This escrow was settled during the third quarter of 2011. There is also a \$100 million escrow account that will be used to fund all claims arising out of or related to the Qualitest acquisition.

## Edgar Filing: ENDO PHARMACEUTICALS HOLDINGS INC - Form 10-Q

In connection with the \$100 million escrow account, to the extent that we are able to realize tax benefits for costs that are funded by the escrow account, we will be required to share these tax benefits with Apax.

Qualitest is a manufacturer and distributor of generic drugs and over-the-counter pharmaceuticals throughout the United States. Qualitest's product portfolio is comprised of 175 product families in various forms including tablets, capsules, creams, ointments, suppositories, and liquids. This acquisition has enabled us to gain critical mass in our generics business while strengthening our pain portfolio through a larger breadth of product offerings.

The operating results of Qualitest from November 30, 2010 are included in the accompanying Condensed Consolidated Statements of Operations. The Consolidated Balance Sheet as of September 30, 2011 and December 31, 2010 reflect the acquisition of Qualitest, effective November 30, 2010, the date the Company obtained control of Qualitest.



**Table of Contents**

The following table summarizes the fair values of the assets acquired and liabilities assumed at the Qualitest Acquisition Date (in thousands):

	November 30, 2010 (As initially reported)	Measurement period adjustments	November 30, 2010 (As adjusted)
Cash and cash equivalents	\$ 21,828	\$	\$ 21,828
Accounts receivable	93,228		93,228
Other receivables	1,483		1,483
Inventories	95,000		95,000
Prepaid expenses and other current assets	2,023	(121)	1,902
Deferred income taxes	63,509	5,457	68,966
Property, Plant and equipment	135,807		135,807
Other intangible assets	843,000	(7,000)	836,000
<b>Total identifiable assets</b>	<b>\$ 1,255,878</b>	<b>\$ (1,664)</b>	<b>\$ 1,254,214</b>
Accounts payable	\$ 27,422	\$	\$ 27,422
Accrued expenses	55,210	3,852	59,062
Deferred income taxes	207,733	1,519	209,252
Long-term debt	406,758		406,758
Other liabilities	9,370	117	9,487
<b>Total liabilities assumed</b>	<b>\$ 706,493</b>	<b>\$ 5,488</b>	<b>\$ 711,981</b>
Net identifiable assets acquired	\$ 549,385	\$ (7,152)	\$ 542,233
Goodwill	\$ 219,986	\$ 7,828	\$ 227,814
<b>Net assets acquired</b>	<b>\$ 769,371</b>	<b>\$ 676</b>	<b>\$ 770,047</b>

The above estimated fair values of assets acquired and liabilities assumed are provisional and are based on the information that was available as of the Qualitest Acquisition Date. The Company believes that information provides a reasonable basis for estimating the fair values but the Company is waiting for additional information necessary to finalize those amounts, particularly with respect to intangible assets, certain liabilities and deferred income taxes. Thus, the provisional measurements of fair value reflected are subject to change. Such changes could be significant. The Company expects to finalize the valuation and complete the purchase price allocation as soon as practicable but no later than one year from the Qualitest Acquisition Date.

The valuation of the intangible assets acquired and related amortization periods are as follows:

	Valuation (in millions)	Amortization Period (in years)
<b>Developed Technology:</b>		
Hydrocodone and acetaminophen	\$ 119.0	17
Oxycodone and acetaminophen	30.0	17
Promethazine	46.0	16
Isosorbide Mononitrate ER	42.0	16
Multi Vitamins	38.0	16
Trazodone	17.0	16
Butalbital, acetaminophen, and caffeine	25.0	16
Triprevifem	16.0	13
Spironolactone	13.0	17

Edgar Filing: ENDO PHARMACEUTICALS HOLDINGS INC - Form 10-Q

Hydrocortisone	34.0	16
Hydrochlorothiazide	16.0	16
Controlled Substances	52.0	16
Oral Contraceptives	8.0	13
Others	162.0	17

Total	\$ 618.0	16
-------	----------	----

**In Process Research & Development:**

Generics portfolio with anticipated 2011 launch	\$ 63.0	n/a
Generics portfolio with anticipated 2012 launch	30.0	n/a

**Table of Contents**

	Valuation (in millions)	Amortization Period (in years)
Generics portfolio with anticipated 2013 launch	17.0	n/a
Generics portfolio with anticipated 2014 launch	88.0	n/a
<b>Total</b>	<b>\$ 198.0</b>	<b>n/a</b>
<b>Tradename:</b>		
Qualitest tradename	\$ 20.0	15
<b>Total</b>	<b>\$ 20.0</b>	<b>15</b>
<b>Total other intangible assets</b>	<b>\$ 836.0</b>	<b>n/a</b>

The fair value of the developed technology assets and in-process research and development assets were estimated using an income approach. Under this method, an intangible asset's fair value is equal to the present value of the incremental after-tax cash flows (excess earnings) attributable solely to the intangible asset over its remaining useful life. To calculate fair value, the Company used probability-weighted cash flows discounted at rates considered appropriate given the inherent risks associated with each type of asset. The Company believes that the level and timing of cash flows appropriately reflect market participant assumptions. Cash flows were generally assumed to extend through the shorter of the patent or estimated useful life of the developed technology or in-process research and development asset. The fair value of the Qualitest tradename was estimated using an income approach, specifically known as the relief from royalty method. The relief from royalty method is based on a hypothetical royalty stream that would be received if the Company were to license the Qualitest tradename. Thus, we derived the hypothetical royalty income from the projected revenues of Qualitest.

The \$227.8 million of goodwill was assigned to our Generics segment. The goodwill recognized is attributable primarily to expected purchasing, manufacturing and distribution synergies as well as their assembled workforce. Approximately \$170.4 million of goodwill is expected to be deductible for income tax purposes.

Deferred tax assets of \$69.0 million are related primarily to federal and state net operating loss and credit carryforwards of Qualitest and its subsidiaries. Deferred tax liabilities of \$209.3 million are related primarily to the difference between the book basis and tax basis of identifiable intangible assets.

The Company recognized \$1.7 million and \$6.3 million of Qualitest acquisition-related costs that were expensed during the three and nine months ended September 30, 2011, respectively. These costs are included in Acquisition-related items in the accompanying Condensed Consolidated Statements of Operations and are comprised of the following items (in thousands):

	Acquisition-related Costs Three months ended September 30, 2011	Acquisition-related Costs Nine months ended September 30, 2011
Bank fees	\$	\$
Legal, separation, integration, and other costs	1,677	6,271
<b>Total</b>	<b>\$ 1,677</b>	<b>\$ 6,271</b>

The following supplemental pro forma information presents the financial results as if the acquisition of Qualitest had occurred on January 1, 2010 for the three and nine months ended September 30, 2010. This supplemental pro forma information has been prepared for comparative purposes and does not purport to be indicative of what would have occurred had the acquisition been made on January 1, 2010, nor are they indicative of any future results.

Edgar Filing: ENDO PHARMACEUTICALS HOLDINGS INC - Form 10-Q

	Three months ended September 30, 2010	Nine months ended September 30, 2010
<b>Pro forma consolidated results (in thousands, except per share data):</b>		
Revenue	\$ 543,799	\$ 1,469,992
Net income attributable to Endo Pharmaceuticals Holdings Inc.	\$ 53,162	\$ 162,949
Basic net income per share	\$ 0.46	\$ 1.40
Diluted net income per share	\$ 0.46	\$ 1.39

**Table of Contents**

These amounts have been calculated after applying the Company's accounting policies and adjusting the results of Qualitest to reflect the additional depreciation and amortization that would have been charged assuming the fair value adjustments primarily to property, plant and equipment and intangible assets, had been applied on January 1, 2010, together with the consequential tax effects.

***Penwest Pharmaceuticals Co.***

On September 20, 2010 (the Penwest Acquisition Date), the Company completed its tender offer for the outstanding shares of common stock of Penwest and on November 4, 2010, we closed this acquisition for approximately \$171.8 million in aggregate cash consideration, at which time Penwest became our wholly-owned subsidiary. On August 22, 2011, Penwest was merged into Endo Pharmaceuticals Inc., at which time Penwest ceased its existence as a separate legal entity.

This transaction contributes to Endo's core pain management franchise and permits us to maximize the value of our oxycodone franchise.

The operating results of Penwest from September 20, 2010 are included in the accompanying Condensed Consolidated Statements of Operations. The Condensed Consolidated Balance Sheets as of September 30, 2011 and December 31, 2010 reflect the acquisition of Penwest, effective September 20, 2010, the date the Company obtained control of Penwest.

The following table summarizes the fair values of the assets acquired and liabilities assumed at the Penwest Acquisition Date (in thousands):

	September 20, 2010 (As initially reported)	Measurement period adjustments	September 20, 2010 (As adjusted)
Cash and cash equivalents	\$ 22,343	\$	\$ 22,343
Marketable securities	800		800
Accounts receivable	10,885	(19)	10,866
Other receivables	132	(1)	131
Inventories	396	11	407
Prepaid expenses and other current assets	716	(223)	493
Deferred income taxes	27,175	2,590	29,765
Property and equipment	1,115	(200)	915
Other intangible assets	111,200		111,200
Other assets	2,104		2,104
<b>Total identifiable assets</b>	<b>\$ 176,866</b>	<b>\$ 2,158</b>	<b>\$ 179,024</b>
Accounts payable	\$ 229	\$	\$ 229
Income taxes payable	347	(187)	160
Penwest shareholder liability	20,815	(20,815)	
Accrued expenses	1,455	87	1,542
Deferred income taxes	39,951	217	40,168
Other liabilities	4,403	117	4,520
<b>Total liabilities assumed</b>	<b>\$ 67,200</b>	<b>\$ (20,581)</b>	<b>\$ 46,619</b>
<b>Net identifiable assets acquired</b>	<b>\$ 109,666</b>	<b>\$ 22,739</b>	<b>\$ 132,405</b>
Goodwill	\$ 37,952	\$ 1,409	\$ 39,361
<b>Net assets acquired</b>	<b>\$ 147,618</b>	<b>\$ 24,148</b>	<b>\$ 171,766</b>

The above estimated fair values of assets acquired and liabilities assumed are based on the information that was available as of the Penwest Acquisition Date. As of September 30, 2011, our measurement period adjustments are complete.

The valuation of the intangible assets acquired and related amortization periods are as follows (in millions):

	Valuation	Amortization Period (in years)
<b>In Process Research &amp; Development:</b>		
Otsuka	\$ 5.5	n/a
A0001	1.6	n/a
Total	\$ 7.1	n/a
<b>Developed Technology:</b>		
Opana® ER	\$ 104.1	10

**Table of Contents**

	Valuation	Amortization Period (in years)
Total	\$ 104.1	10
Total other intangible assets	\$ 111.2	n/a

The fair values of the in-process research and development assets and developed technology asset were estimated using an income approach. To calculate fair value, the Company used probability-weighted cash flows discounted at rates considered appropriate given the inherent risks associated with the asset. The Company believes that the level and timing of cash flows appropriately reflect market participant assumptions. Cash flows were generally assumed to extend through the shorter of the patent or estimated useful life of our developed technology or in-process research and development asset.

The \$39.4 million of goodwill was assigned to our Branded Pharmaceuticals segment. The goodwill recognized is attributable primarily to the control premium associated with our oxymorphone franchise and other factors. None of the goodwill is expected to be deductible for income tax purposes.

Deferred tax assets of \$29.8 million are related primarily to federal net operating loss and credit carryforwards of Penwest. Deferred tax liabilities of \$40.2 million are related primarily to the difference between the book basis and tax basis of the identifiable intangible assets.

The Company recognized \$0.3 million and \$0.5 million of Penwest acquisition-related costs that were expensed during the three and nine months ended September 30, 2011, respectively. The Company also recognized \$6.9 million of Penwest acquisition-related costs that were expensed for both the three and nine month periods ended September 30, 2010. These costs are included in Acquisition-related items in the accompanying Condensed Consolidated Statements of Operations and are comprised of the following items (in thousands):

	Acquisition-related Costs Three and nine months ended September 30, 2010	
Bank fees	\$	3,660
Legal, separation, integration, and other costs		3,255
Total	\$	6,915

Due to the pro forma impacts of eliminating the pre-existing intercompany royalties between Penwest and Endo, which were determined to be at fair value, we have not provided supplemental pro forma information as amounts are not material to the Condensed Consolidated Statements of Operations. We have also considered the impacts of Penwest, since the date we obtained a majority interest, on our Consolidated Statement of Operations and concluded amounts were not material.

***HealthTronics, Inc.***

On July 2, 2010 (the HealthTronics Acquisition Date), the Company completed its initial tender offer for all outstanding shares of common stock of HealthTronics and obtained effective control of HealthTronics. On July 12, 2010, Endo completed its acquisition of HealthTronics for approximately \$214.8 million in aggregate cash consideration for 100% of the outstanding shares, at which time HealthTronics became a wholly-owned subsidiary of the Company. HealthTronics shares were purchased at a price of \$4.85 per HealthTronics Share. In addition, Endo paid \$40 million to retire HealthTronics debt that had been outstanding under its Senior Credit Facility. As a result of the acquisition, the HealthTronics Senior Credit Facility was terminated.

HealthTronics is a provider of healthcare services and manufacturer of medical devices, primarily for the urology community. The HealthTronics business and applicable services include:

*Lithotripsy services.*

## Edgar Filing: ENDO PHARMACEUTICALS HOLDINGS INC - Form 10-Q

HealthTronics provides lithotripsy services, which is a medical procedure where a device called a lithotripter transmits high energy shockwaves through the body to break up kidney stones. Lithotripsy services are provided principally through limited partnerships and other entities that HealthTronics manages, which use lithotripters. In 2010, physician partners used our lithotripters to perform approximately 50,000 procedures in the U.S. While the physicians render medical services, HealthTronics does not. As the general partner of limited partnerships or the manager of other types of entities, HealthTronics also provide services relating to operating its lithotripters, including scheduling, staffing, training, quality assurance, regulatory compliance, and contracting with payors, hospitals, and surgery centers.



**Table of Contents***Prostate treatment services.*

HealthTronics provides treatments for benign and cancerous conditions of the prostate. In treating benign prostate disease, HealthTronics deploys three technologies in a number of its partnerships above: (1) photo-selective vaporization of the prostate (PVP), (2) trans-urethral needle ablation (TUNA), and (3) trans-urethral microwave therapy (TUMT). All three technologies apply an energy source which reduces the size of the prostate gland. For treating prostate and other cancers, HealthTronics uses a procedure called cryosurgery, a process which uses lethal ice to destroy tissue such as tumors for therapeutic purposes. In April 2008, HealthTronics acquired Advanced Medical Partners, Inc., which significantly expanded its cryosurgery partnership base. In July 2009, HealthTronics acquired Endocare, Inc., which manufactures both the medical devices and related consumables utilized by its cryosurgery operations and also provides cryosurgery treatments. The prostate treatment services are provided principally by using equipment that HealthTronics leases from limited partnerships and other entities that HealthTronics manages. Benign prostate disease and cryosurgery cancer treatment services are billed in the same manner as its lithotripsy services under either retail or wholesale contracts. HealthTronics also provides services relating to operating the equipment, including scheduling, staffing, training, quality assurance, regulatory compliance, and contracting.

*Radiation therapy services.*

HealthTronics provided image guided radiation therapy (IGRT) technical services for cancer treatment centers. Its IGRT technical services related to providing the technical (non-physician) personnel to operate a physician practice group's IGRT equipment, leasing IGRT equipment to a physician practice group, providing services related to helping a physician practice group establish an IGRT treatment center, and managing an IGRT treatment center. In September 2011, the IGRT business was sold for approximately \$13.0 million. The impact of this sale was not material to the Company's Condensed Consolidated Statements of Operations.

*Anatomical pathology services.*

HealthTronics provides anatomical pathology services primarily to the urology community. HealthTronics has one pathology lab located in Georgia, which provides laboratory detection and diagnosis services to urologists throughout the United States. In addition, in July 2008, HealthTronics acquired Uropath LLC, now referred to as HealthTronics Laboratory Solutions, which managed pathology laboratories located at Uropath sites for physician practice groups located in Texas, Florida and Pennsylvania. Through HealthTronics Laboratory Solutions, HealthTronics continues to provide administrative services to in-office pathology labs for practice groups and pathology services to physicians and practice groups with its lab equipment and personnel at the HealthTronics Laboratory Solutions laboratory sites.

*Medical products manufacturing, sales and maintenance.*

HealthTronics manufactures and sells medical devices focused on minimally invasive technologies for tissue and tumor ablation through cryoablation, which is the use of lethal ice to destroy tissue, such as tumors, for therapeutic purposes. HealthTronics develops and manufactures these devices for the treatment of prostate and renal cancers and our proprietary technologies also have applications across a number of additional markets, including the ablation of tumors in the lung, liver metastases and palliative intervention (treatment of pain associated with metastases). HealthTronics manufactures the related spare parts and consumables for these devices. HealthTronics also sells and maintains lithotripters and related spare parts and consumables.

The acquisition of HealthTronics reflects Endo's desire to continue expanding our business beyond pain management into complementary medical areas where HealthTronics can be innovative and competitive. We believe this expansion will enable us to be a provider of multiple healthcare solutions and services that fill critical gaps in patient care.

The operating results of HealthTronics from July 2, 2010 are included in the accompanying Condensed Consolidated Statements of Operations. The Condensed Consolidated Balance Sheets as of September 30, 2011 and December 31, 2010 reflect the acquisition of HealthTronics, effective July 2, 2010, the date the Company obtained control of HealthTronics.

The following table summarizes the fair values of the assets acquired and liabilities assumed at the HealthTronics Acquisition Date (in thousands):

	<b>July 2, 2010</b> <b>(As Adjusted)</b>
Cash and cash equivalents	\$ 6,769

Edgar Filing: ENDO PHARMACEUTICALS HOLDINGS INC - Form 10-Q

Accounts receivable	33,388
Other receivables	1,006
Inventories	12,399
Prepaid expenses and other current assets	5,204

**Table of Contents**

	<b>July 2, 2010</b> <b>(As Adjusted)</b>
Deferred income taxes	46,489
Property and equipment	30,687
Other intangible assets	73,124
Other assets	5,210
<b>Total identifiable assets</b>	<b>\$ 214,276</b>
Accounts payable	\$ 3,084
Accrued expenses	20,510
Deferred income taxes	22,376
Long-term debt	43,460
Other liabilities	1,785
<b>Total liabilities assumed</b>	<b>\$ 91,215</b>
Net identifiable assets acquired	\$ 123,061
Noncontrolling interests	\$ (63,227)
Goodwill	\$ 155,009
<b>Net assets acquired</b>	<b>\$ 214,843</b>

The above estimated fair values of assets acquired and liabilities assumed are based on the information that was available as of the HealthTronics Acquisition Date. As of September 30, 2011, our measurement period adjustments are complete.

The valuation of the intangible assets acquired and related amortization periods are as follows:

	<b>Valuation</b> <b>(in millions)</b>	<b>Amortization</b> <b>Period</b> <b>(in years)</b>
Endocare Developed Technology	\$ 46.3	10
HealthTronics Tradename	14.6	15
Service Contract(1)	12.2	n/a
<b>Total</b>	<b>\$ 73.1</b>	<b>n/a</b>

(1) This intangible asset relates to our IGRT business, which was sold in September 2011 for approximately \$13.0 million. Accordingly, the carrying amount of this asset was reduced to zero at the time of sale.

The fair value of the developed technology asset was estimated using a discounted present value income approach. Under this method, an intangible asset's fair value is equal to the present value of the incremental after-tax cash flows (excess earnings) attributable solely to the intangible asset over its remaining useful life. To calculate fair value, the Company used probability-weighted cash flows discounted at rates considered appropriate given the inherent risks associated with each type of asset. The Company believes that the level and timing of cash flows appropriately reflect market participant assumptions. Cash flows were assumed to extend through the patent life of the purchased technology. The fair value of the HealthTronics Tradename was estimated using an income approach, specifically known as the relief from royalty method. The relief from royalty method is based on a hypothetical royalty stream that would be received if the Company were to license the HealthTronics Tradename. Thus, we derived the hypothetical royalty income from the projected revenues of HealthTronics' services.

HealthTronics has investments in partnerships and limited liability companies (LLCs) where we, as the general partner or managing member, exercise effective control. Accordingly, we consolidate various entities where we do not own 100% of the entity in accordance with the accounting consolidation principles. As a result, we are required to fair value the noncontrolling interests as part of our purchase price allocation. To calculate fair value, the Company used historical transactions which represented Level 2 data points within the fair value hierarchy to

## Edgar Filing: ENDO PHARMACEUTICALS HOLDINGS INC - Form 10-Q

calculate applicable multiples of each respective noncontrolling interest in the partnerships and LLCs.

The \$155.0 million of goodwill was assigned to our Devices and Services segment. The goodwill recognized is attributable primarily to strategic and synergistic opportunities across the HealthTronics network of urology partnerships, expected corporate synergies, the assembled workforce of HealthTronics and other factors. Approximately \$33.6 million of goodwill is expected to be deductible for income tax purposes.

**Table of Contents**

Deferred tax assets of \$46.5 million are related primarily to federal net operating loss and credit carryforwards of HealthTronics and its subsidiaries. Deferred tax liabilities of \$22.4 million are related primarily to the difference between the book basis and tax basis of identifiable intangible assets.

The Company recognized \$2.9 million of HealthTronics acquisition-related costs that were expensed during the nine months ended September 30, 2011. There were no acquisition-related costs expensed during the three months ended September 30, 2011. These costs are included in Acquisition-related items in the accompanying Condensed Consolidated Statements of Operations and are comprised of the following items (in thousands):

	<b>Acquisition-related Costs</b>	
	<b>Nine months ended</b>	
	<b>September 30, 2011</b>	
Bank fees	\$	
Legal, separation, integration, and other costs		2,861
<b>Total</b>	<b>\$</b>	<b>2,861</b>

The Company recognized \$15.3 million and \$20.0 million of HealthTronics acquisition-related costs that were expensed during the three and nine months ended September 30, 2010, respectively. These costs are included in Acquisition-related items in the accompanying Condensed Consolidated Statements of Operations and are comprised of the following items (in thousands):

	<b>Acquisition-related Costs</b>	
	<b>Three months ended</b>	
	<b>September</b>	<b>Nine months ended</b>
	<b>30, 2010</b>	<b>September 30, 2010</b>
Bank fees	\$ 5,230	\$ 5,230
Acceleration of outstanding HealthTronics stock-based compensation	7,924	7,924
Legal, separation, integration, and other costs	2,113	6,866
<b>Total</b>	<b>\$ 15,267</b>	<b>\$ 20,020</b>

The following supplemental pro forma information presents the financial results as if the acquisition of HealthTronics had occurred on January 1, 2010 for the nine months ended September 30, 2010. This supplemental pro forma information has been prepared for comparative purposes and does not purport to be indicative of what would have occurred had the acquisition been made on January 1, 2010, nor are they indicative of any future results.

	<b>Nine months ended</b>
	<b>September 30, 2010</b>
<b>Pro forma consolidated results (in thousands, except per share data):</b>	
Revenue	\$ 1,303,728
Net income attributable to Endo Pharmaceuticals Holdings Inc.	\$ 171,180
Basic net income per share	\$ 1.47
Diluted net income per share	\$ 1.46

These amounts have been calculated after applying the Company's accounting policies and adjusting the results of HealthTronics to reflect the additional depreciation and amortization that would have been charged assuming the fair value adjustments primarily to property, plant and equipment, and intangible assets, had been applied on January 1, 2010, together with the consequential tax effects.

**Acquisition-Related Contingent Consideration**

## Edgar Filing: ENDO PHARMACEUTICALS HOLDINGS INC - Form 10-Q

As of September 30, 2011 and December 31, 2010, the fair value of the contingent consideration is \$8.8 million and \$16.1 million, respectively. The material components of this obligation are discussed below.

### *Indevus*

The Indevus Contingent Consideration Agreements were measured and recognized at fair value upon the Indevus Acquisition Date and are required to be re-measured on a recurring basis, with changes to fair value recorded in Acquisition-related items in the accompanying Condensed Consolidated Statements of Operations. The fair values were determined using a probability-weighted

**Table of Contents**

discounted cash flow model, or income approach. This fair value measurement technique is based on significant inputs not observable in the market and thus represents a Level 3 measurement within the fair value hierarchy. The valuation of each Indevus Contingent Consideration Agreement is described in further detail below:

*Aveed™ Contingent Consideration* The range of the undiscounted amounts the Company could pay under the Aveed™ Contingent Cash Consideration Agreement is between zero and approximately \$175.0 million. Under this agreement, there are three scenarios that could potentially lead to amounts being paid to the former stockholders of Indevus. These scenarios are (1) obtaining an Aveed™ With Label approval, (2) obtaining an Aveed™ Without Label approval and (3) achieving the \$125.0 million sales milestone on or prior to the fifth anniversary of the date of the first commercial sale of Aveed™ should the Aveed™ Without Label approval be obtained. The fourth scenario is Aveed™ not receiving approval within three years of the closing of the Offer, which would result in no payment to the former stockholders of Indevus. Each scenario was assigned a probability based on the current regulatory status of Aveed™. The resultant probability-weighted cash flows were then discounted using a discount rate of U.S. Prime plus 300 basis points, which the Company believes is appropriate and is representative of a market participant assumption. Using this valuation technique, the fair value of the contractual obligation to pay the Aveed™ Contingent Consideration was determined to be zero at September 30, 2011, \$7.1 million at December 31, 2010, and \$133.1 million on the Indevus Acquisition Date.

*Octreotide Contingent Consideration* The range of the undiscounted amounts the Company could pay under the Octreotide Contingent Cash Consideration Agreement is between zero and approximately \$91.0 million. Under this agreement, the two scenarios that require consideration are (1) approval of octreotide on or before the fourth anniversary of the closing of the Offer or (2) no octreotide approval on or before the fourth anniversary of the closing of the Offer. Each scenario was assigned a probability based on the current development stage of octreotide. The resultant probability-weighted cash flows were then discounted using a discount rate of U.S. Prime plus 300 basis points, which the Company believes is appropriate and is representative of a market participant assumption. Using this valuation technique, the fair value of the contractual obligation to pay the Octreotide Contingent Consideration was determined to be zero at both September 30, 2011 and December 31, 2010 and \$39.8 million on the Indevus Acquisition Date.

*Valera Contingent Consideration* The range of the undiscounted amounts the Company could pay under the Valera Contingent Cash Consideration Agreement is between zero and approximately \$33.0 million. The fair value of the Valera Contingent Consideration is estimated using the same assumptions used for the Aveed™ Contingent Cash Consideration Agreement and Octreotide Contingent Cash Consideration Agreement, except that the probabilities associated with the Valera Contingent Consideration take into account the probability of obtaining the Octreotide Approval on or before the fourth anniversary of the closing of the Offer. This is due to the fact that the Valera Contingent Consideration will not be paid unless octreotide for the treatment of acromegaly is approved prior to April 18, 2012. Using this valuation technique, the fair value of the contractual obligation to pay the Valera Contingent Consideration was determined to be zero at both September 30, 2011 and December 31, 2010 and \$13.7 million on the Indevus Acquisition Date.

At September 30, 2011, the aggregate fair value of the three Indevus Contingent Consideration Agreements decreased from \$7.1 million at December 31, 2010 to zero at September 30, 2011. This decrease primarily reflects management's current assessment of the probability that it will not be obligated to make contingent consideration payments based on the anticipated timeline for the NDA filings and FDA approvals of Aveed™ and octreotide for the treatment of acromegaly. The decrease in the liability was recorded as a gain and was included in Acquisition-related items in the accompanying Condensed Consolidated Statements of Operations.

As of September 30, 2011, there were no changes to the range of the undiscounted amounts the Company may be required to pay under any of the Indevus Contingent Consideration Agreements.

*Qualitest*

On November 30, 2010 (the Qualitest Acquisition Date), Endo acquired Qualitest, who was party to an asset purchase agreement with Teva Pharmaceutical Industries Ltd (Teva) (the Teva Agreement). Pursuant to this agreement, Qualitest purchased certain pipeline generic products from Teva and could be obligated to pay consideration to Teva upon the achievement of certain future regulatory milestones (the Teva Contingent Consideration).

## Edgar Filing: ENDO PHARMACEUTICALS HOLDINGS INC - Form 10-Q

The range of the undiscounted amounts the Company could pay under the Teva Agreement is between zero and \$12.5 million. The Company is accounting for the Teva Contingent Consideration in the same manner as if it had entered into that arrangement with respect to its acquisition of Qualitest. Accordingly, the fair value was estimated based on a probability-weighted discounted cash flow model, or income approach. The resultant probability-weighted cash flows were then discounted using a discount rate of U.S. Prime plus 300 basis points. This fair value measurement is based on significant inputs not observable in the market and thus represents a Level 3 measurement within the fair value hierarchy. Using this valuation technique, the fair value of the contractual obligation to pay the Teva Contingent Consideration was determined to be \$8.6 million at September 30, 2011 and \$9.0 million at December 31, 2010 and the Qualitest Acquisition Date, respectively.



---

## **Table of Contents**

The decrease from December 31, 2010 to September 30, 2011 primarily reflects changes of our present value assumptions associated with our valuation model. The decrease in the liability was recorded as a gain and is included in Acquisition-related items in the accompanying Condensed Consolidated Statements of Operations.

As of September 30, 2011, there were no changes to the range of the undiscounted amounts the Company may be required to pay under the Teva Agreement.

**Legal Proceedings.** We are subject to various patent, product liability, government investigations and other legal proceedings in the ordinary course of business. Contingent accruals are recorded when we determine that a loss related to a litigation matter is both probable and reasonably estimable. Due to the fact that legal proceedings and other contingencies are inherently unpredictable, our assessments involve significant judgments regarding future events. For a complete description of legal proceedings, see Note 12 of the Condensed Consolidated Financial Statements included in Part I, Item 1 of this Quarterly Report on Form 10-Q.

**Fluctuations.** Our quarterly results have fluctuated in the past, and may continue to fluctuate. These fluctuations may be due to the timing of new product launches, purchasing patterns of our customers, market acceptance of our products, the impact of competitive products and pricing, impairment of intangible assets, separation benefits, business combination transaction costs, upfront, milestone and certain other payments made or accrued pursuant to licensing agreements and changes in the fair value of financial instruments and contingent assets and liabilities recorded as part of a business combination. Further, a substantial portion of our net pharmaceutical product sales are through three wholesale drug distributors who in turn supply our products to pharmacies, hospitals and physicians. Accordingly, we are potentially subject to a concentration of credit risk with respect to our trade receivables.

**Growth Opportunities.** We continue to evaluate growth opportunities including strategic investments, licensing arrangements, acquisitions of businesses, product rights or technologies, and strategic alliances and promotional arrangements which could require significant capital resources. We intend to continue to focus our business development activities on further diversifying our revenue base through product licensing and company acquisitions, as well as other opportunities to enhance stockholder value. Through execution of our business strategy we intend to focus on developing new products through both an internal and a virtual research and development organization with greater scientific and clinical capabilities; expanding the Company's product line by acquiring new products and technologies in existing therapeutic and complementary areas; increasing revenues and earnings through sales and marketing programs for our innovative product offerings and effectively using the Company's resources; and providing additional resources to support our generics business.

**Non-U.S. Operations.** Our operations outside of the United States were not material during the first nine months of 2011. As a result, fluctuations in foreign currency exchange rates did not have a material effect on our financial statements.

**Inflation.** We do not believe that inflation had a material adverse effect on our financial statements for the periods presented.

**Off-Balance Sheet Arrangements.** We have no off-balance sheet arrangements as defined in Item 303(a)(4) of Regulation S-K.

## **CRITICAL ACCOUNTING ESTIMATES**

For a complete discussion of the Company's critical accounting estimates, see "Critical Accounting Estimates" in Item 7 of our Annual Report on Form 10-K for the year ended December 31, 2010, filed with the Securities and Exchange Commission on February 28, 2011.

Additionally, pursuant to our acquisition of AMS in June 2011, our critical accounting policies have been updated to include the following:

**Foreign Currency Translation.** The financial statements for operations outside the United States associated with our recent acquisition of AMS are maintained in their local currency. All assets and liabilities of our international subsidiaries are translated to United States dollars at period-end exchange rates, while elements of the statement of operations are translated at average exchange rates in effect during the year. Translation adjustments arising from the use of differing exchange rates are included in accumulated other comprehensive income in stockholders' equity with the exception of inter-company balances not considered permanently invested which are included in Other income, net. The balance of net cumulative translation losses included in accumulated other comprehensive loss was \$4.3 million at September 30, 2011. Gains and losses on foreign currency transactions are also included in Other income, net.

**Revenue Recognition.** In our Device and Services segment, we recognize revenue generally when services are provided in the case of fees for urology treatments, for managing the operation of our lithotripters and prostate treatment devices, for maintenance services and for anatomical pathology services. In the case of fees for equipment sales, consumable sales and licensing applications, revenues are generally recognized upon delivery or for licensing fees, when the patient is treated. As a result of the acquisition of AMS, we also sell products in this segment through a

## Edgar Filing: ENDO PHARMACEUTICALS HOLDINGS INC - Form 10-Q

direct sales force. A portion of our revenue is generated from consigned inventory or from inventory with field representatives. For these products, revenue is recognized at the time the product has been used

---

## **Table of Contents**

or implanted. For all other transactions, we recognize revenue when title to the goods and risk of loss transfer to our customers providing there are no remaining performance obligations required from us or any matters requiring customer acceptance. In cases where we utilize distributors or ship product directly to the end user, we recognize revenue upon shipment provided all revenue recognition criteria have been met. We record estimated sales returns, discounts and rebates as a reduction of net sales in the period revenue is recognized.

Occasionally, sales of capital equipment have post-sale obligations, such as installation and extended service contracts, which are fulfilled after product shipment, or the delivery of fibers which may be included in the initial sales contract. For each multiple element arrangement, we determine if each element is a separate unit of accounting by ensuring that (1) the element has standalone value to the customer, (2) there is objective evidence of the fair value for the element, and (3) if the arrangement includes a general right of return relative to the delivered item, delivery of the undelivered items is considered probable and in our control. To determine the fair value for each element in an arrangement, we rely primarily upon vendor specific objective evidence (VSOE) of fair value using the price charged when we sell that element separately, we rely upon vendor specific objective evidence of fair value in the form of competitor pricing of the same or interchangeable products. We defer revenue attributable to the post-shipment obligations and recognize such revenue when the obligation is fulfilled.

We provide incentives to customers, including volume based rebates. Customers are not required to provide documentation that would allow us to reasonably estimate the fair value of the benefit received and we do not receive an identifiable benefit in exchange for the consideration. Accordingly, the incentives are recorded as a reduction of revenue.

All of our customers have rights of return for the occasional ordering or shipping error. We maintain an allowance for these returns and reduce reported revenue for expected returns from shipments during each reporting period. This allowance is based on historical and current trends in product returns. This allowance was \$1.7 million at September 30, 2011.

## **RECENT ACCOUNTING PRONOUNCEMENTS**

In December 2010, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update (ASU) 2010-29 on interim and annual disclosure of pro forma financial information related to business combinations. The new guidance clarifies the acquisition date that should be used for reporting the pro forma financial information in which comparative financial statements are presented. It is effective prospectively for business combinations for which the acquisition date is on or after the beginning of the first annual reporting period beginning on or after December 15, 2010. The provisions of this ASU have been incorporated into this filing for our 2011 acquisitions.

In December 2010, the FASB issued ASU 2010-28 on accounting for goodwill. The guidance clarifies the impairment test for reporting units with zero or negative carrying amounts. The guidance is effective for fiscal years and interim periods within those years beginning after December 15, 2011. The adoption is not expected to have a material impact on the Company's Consolidated Financial Statements.

In December 2010, the FASB issued ASU 2010-27 on accounting for the annual fee imposed by the Patient Protection and Affordable Care Act, as amended by the Health Care and Education Reconciliation Act. The new guidance specifies that the liability for the fee should be estimated and recorded in full upon the first qualifying sale with a corresponding deferred cost that is amortized to expense. It is effective on a prospective basis for calendar years beginning after December 31, 2010. We expect this fee will be approximately \$18 million in 2011, which will be charged as an operating expense ratably throughout 2011.

In May 2011, the FASB issued ASU 2011-04 on fair value disclosures. This guidance amends certain accounting and disclosure requirements related to fair value measurements. It is effective on a prospective basis for interim and annual periods beginning after December 15, 2011. Early application is not permitted. The Company is currently evaluating ASU 2011-04 but we do not expect the impact of adoption to be material.

In June 2011, the FASB issued ASU 2011-05 on the presentation of comprehensive income, which amends current comprehensive income guidance. This accounting update eliminates the option to present the components of other comprehensive income as part of the statement of shareholders' equity. Instead, the Company must report comprehensive income in either a single continuous statement of comprehensive income which contains two sections, net income and other comprehensive income, or in two separate but consecutive statements. ASU 2011-05 will be effective for public companies during the interim and annual periods beginning after December 15, 2011 with early adoption permitted. The adoption of ASU 2011-05 will not have an impact on the Company's consolidated financial position, results of operations or cash flows as it only requires a change in the format of the current presentation.

In September 2011, the FASB issued ASU 2011-08 on testing goodwill for impairment, which permits an entity to make a qualitative assessment of whether it is more likely than not that a reporting unit's fair value is less than its carrying value before applying the two-step goodwill impairment model that is currently in place. If it is determined through the qualitative assessment that



## **Table of Contents**

a reporting unit's fair value is more likely than not greater than its carrying value, the remaining impairment steps would be unnecessary. The qualitative assessment is optional, allowing companies to go directly to the quantitative assessment. ASU 2011-08 will be effective for annual and interim goodwill impairment tests performed in fiscal years beginning after December 15, 2011, with early adoption permitted. The Company is currently evaluating ASU 2011-08.

### **Item 3. Quantitative and Qualitative Disclosures about Market Risk.**

For quantitative and qualitative disclosures about market risk, see Item 7A, Quantitative and Qualitative Disclosures about Market Risk, of our annual report on Form 10-K for the year ended December 31, 2010, filed with the Securities and Exchange Commission on February 28, 2011.

In addition, our operations outside of the United States are maintained in their local currency. All assets and liabilities of our international subsidiaries are translated to U.S. dollars at period-end exchange rates. Translation adjustments arising from the use of differing exchange rates are included in accumulated other comprehensive income in stockholders' equity. Gains and losses on foreign currency transactions and short term inter-company receivables from foreign subsidiaries are included in Other (income), net.

The reported results of our foreign operations will be influenced by their translation into U.S. dollars by currency movements against the U.S. dollar. We have entered into various foreign exchange forward contracts to manage a portion of our exposure to foreign exchange rate fluctuations on our forecasted sales to and receivables from certain subsidiaries, denominated in euros, British pounds, Canadian dollars and Australian dollars.

### **Item 4. Controls and Procedures.**

#### ***Evaluation of Disclosure Controls and Procedures***

The Company's management, with the participation of the Company's Chief Executive Officer and Principal Financial Officer, has evaluated the effectiveness of the Company's disclosure controls and procedures, as defined in Rules 13a-15(e) and 15d-15(e) of the Securities Exchange Act of 1934, as of September 30, 2011. Based on that evaluation, the Company's Chief Executive Officer and Principal Financial Officer concluded that the Company's disclosure controls and procedures were effective as of September 30, 2011.

#### ***Changes in Internal Control over Financial Reporting***

The Company acquired Generics International (US Parent), Inc. (Qualitest) and American Medical Systems Holdings, Inc. on November 30, 2010 and June 17, 2011, respectively. The Company began to integrate these acquired companies into its internal control over financial reporting structure subsequent to their respective acquisition dates. As such, there have been changes during the three and nine months ended September 30, 2011 associated with the continued establishment and implementation of internal control over financial reporting with respect to these acquired companies.

There were no other changes in the Company's internal control over financial reporting during the three months ended September 30, 2011 that have materially affected, or are reasonably likely to materially affect, the Company's internal control over financial reporting.

## **PART II**

### **OTHER INFORMATION**

#### **Item 1. Legal Proceedings.**

The disclosures under Note 12. Commitments and Contingencies-Legal Proceedings included in Part I Item I of this Report is incorporated in this Part II, Item 1 by reference.

**Item 1A. Risk Factors**

There have been no material changes to the risk factors that were disclosed in the Company's Quarterly Report on Form 10-Q for the quarter ended June 30, 2011.

**Item 2. Unregistered Sale of Equity Securities and Use of Proceeds.**

None.

**Item 3. Defaults Upon Senior Securities.**

None.

**Item 4. Removed and Reserved.**

**Item 5. Other Information.**

***Corporate Headquarters Lease***

On October 28, 2011, our subsidiary Endo Pharmaceuticals Inc., (the Tenant), entered into a lease agreement with RT/TC Atwater LP, a Delaware limited partnership relating to new Company headquarters consisting of approximately 300,000 square feet of office space located at 1400 Atwater Boulevard, Malvern, Pennsylvania. This lease is guaranteed by the Company.

The term of this lease is one-hundred and forty-four months, which is expected to commence in late 2012, and includes three renewal options, each for an additional sixty (60) month period. The monthly lease rate for the initial year will be \$466,250, and will increase by 2.25% each subsequent year. Under the terms of this lease, the Tenant will have a continuous and recurring right throughout the initial four (4) years of the lease term to lease up to an additional approximately one hundred fifty thousand (150,000) square feet. Additionally, as this is a build-to-suit lease agreement, the Tenant is responsible for all tenant improvement costs, less a tenant improvement allowance of \$45 per square foot times the rentable square footage of the building.

This lease agreement is filed herewith as Exhibit 99.1 and is incorporated herein by reference.

***Executive Employment Agreements***

Effective October 27, 2011 (the Effective Date), the Registrant entered into Executive Employment Agreements with David P. Holveck, the Company's President and Chief Executive Officer, and Ivan P. Gergel, M.D., the Company's Executive Vice President, Research and Development and Chief Scientific Officer. These new agreements supersede Mr. Holveck's and Dr. Gergel's prior agreements in their entirety.

***Mr. David P. Holveck***

The term of Mr. Holveck's new agreement is three years ending on October 27, 2014, unless earlier terminated by either the Company or Mr. Holveck. Under the new agreement, Mr. Holveck is entitled to an annual base salary of \$1,100,000, subject to adjustments at the sole discretion of the Compensation Committee of the Board of Directors (the Compensation Committee) and an annual cash performance bonus opportunity equal to one hundred percent (100%) of his annual base salary for each fiscal year (referred to incentive compensation). The actual annual incentive compensation, if any, paid to Mr. Holveck in any year may be more or less than the target bonus based upon the achievement of certain performance targets set by the Compensation Committee in its sole discretion and such other criteria established by the Compensation Committee. Mr. Holveck is also eligible to earn, as additional compensation for the services rendered pursuant to his employment agreement, long-term equity-based incentives (LTI) in the sole discretion of the Compensation Committee and in an amount approved by the Compensation Committee if the Company and Mr. Holveck achieve certain performance targets set by the Compensation Committee. All such equity based awards are subject to the terms and conditions set forth in the applicable plan and agreements. Mr. Holveck is also entitled to employee benefits, executive benefits, perquisites, reimbursement of expenses and vacation on same basis as other senior executives.

If, during the employment term, Mr. Holveck terminates his new employment agreement for good reason or if the Company terminates Mr. Holveck without cause, Mr. Holveck will be entitled to receive (i) his annual cash incentive compensation, pro-rated for the fiscal year of termination based on the actual achievement of performance goals; (ii) a lump sum equal to two times the sum of (A) Mr. Holveck's base salary

## Edgar Filing: ENDO PHARMACEUTICALS HOLDINGS INC - Form 10-Q

and (B) his target incentive compensation for the fiscal year in which the termination is effective; and (iii) continuation of medical and life insurance benefits for twenty-four (24) months. If the Company terminates his new employment agreement for cause or Mr. Holveck terminates his Employment Agreement without good reason, Mr. Holveck will only receive the compensation that has accrued, but not yet been paid.

Under his new employment agreement, Mr. Holveck is not entitled to a gross up to cover any excise tax that he may owe under Sections 280G and 4999 of the Internal Revenue Code or any other tax gross-up. If Mr. Holveck is entitled to any payment or benefit that would be (in whole or in part) subject to the excise tax imposed under Section 4999 of the Internal Revenue Code or any similar state or local law, his payments will not be grossed up but instead will be reduced to the extent necessary to avoid the excise tax, but only if such reduction will result in a higher after-tax payment to Mr. Holveck. If any excise taxes are owed by Mr. Holveck as a result of his receipt of any excess parachute payments, Mr. Holveck will be responsible for paying all such excise taxes.

Mr. Holveck's new employment agreement also contains covenants not to solicit employees for a period of 24 months after cessation of his employment, not to compete for 18 months after cessation of his employment, nondisparagement, and cooperation in any investigations and litigation.

*Dr. Ivan P. Gergel*

The term of Dr. Gergel's new agreement is three years ending on October 27, 2014, unless earlier terminated by either the Company or Dr. Gergel. Under the new agreement, Dr. Gergel's title has been changed to Executive Vice President, Research and Development and Chief Scientific Officer of the Company. Under the new agreement, Dr. Gergel is entitled to an annual base salary of \$636,000, subject to adjustments at the sole discretion of the Compensation Committee of the Board of Directors (the Compensation Committee) and an annual cash performance bonus opportunity equal to fifty-five percent (55%) of his annual base salary for each fiscal year (referred to as incentive compensation). The actual annual incentive compensation, if any, paid to Dr. Gergel in any year may be more or less than the target bonus based upon the achievement of certain performance targets set by the Compensation Committee in its sole discretion, taking into account the recommendation of the Chief Executive Officer, and such other criteria established by the Compensation Committee. Dr. Gergel is also eligible to earn, as additional compensation for the services rendered pursuant to his employment agreement, long-term equity-based incentives (LTI) in a targeted amount equal to two hundred percent (200%) of his base salary for each fiscal year (or such lesser (including zero) or greater percent of his salary for such fiscal year as is recommended in good faith by the Chief Executive Officer and approved by the Compensation Committee). All such equity based awards are subject to the terms and conditions set forth in the applicable plan and agreements. Dr. Gergel is also entitled to employee benefits, executive benefits, perquisites, reimbursement of expenses and vacation on same basis as other senior executives.

If, during the employment term, Dr. Gergel terminates his new employment agreement for good reason or if the Company terminates Dr. Gergel without cause, Dr. Gergel will be entitled to receive (i) his annual cash incentive compensation pro-rated for the fiscal year of termination based on the actual achievement of performance goals; (ii) a lump sum equal to two times the sum of (A) Dr. Gergel's base salary and (B) his target incentive compensation for the fiscal year in which the termination is effective; and (iii) continuation of medical and life insurance benefits for twenty-four (24) months. If the Company terminates his new employment agreement for cause or Mr. Gergel terminates his new employment agreement without good reason, Mr. Gergel will only receive the compensation that has accrued, but not yet been paid.

Under his new employment agreement, Dr. Gergel is not entitled to a gross up to cover any excise tax that he may owe under Sections 280G and 4999 of the Internal Revenue Code or any other tax gross-up. If Dr. Gergel is entitled to any payment or benefit that would be (in whole or in part) subject to the excise tax imposed under Section 4999 of the Internal Revenue Code or any similar state or local law, his payments will not be grossed up but instead will be reduced to the extent necessary to avoid the excise tax, but only if such reduction will result in a higher after-tax payment to Dr. Gergel. If any excise taxes are owed by Dr. Gergel as a result of his receipt of any excess parachute payments, Dr. Gergel will be responsible for paying all such excise taxes.

Dr. Gergel's new employment agreement also contains covenants not to solicit employees and not to compete, in each case, for a period of 24 months after cessation of his employment, as well as covenants as to nondisparagement and cooperation in any investigations and litigation.

### **Item 6. Exhibits.**

The information called for by this item is incorporated by reference to the Exhibit Index of this Report.

**Table of Contents**

**SIGNATURES**

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

ENDO PHARMACEUTICALS HOLDINGS INC.

(Registrant)

*/s/* DAVID P. HOLVECK  
Name: **David P. Holveck**  
Title: **President and Chief Executive Officer**

**(Principal Executive Officer)**

*/s/* ALAN G. LEVIN  
Name: **Alan G. Levin**  
Title: **Executive Vice President, Chief Financial Officer**

**(Principal Financial Officer)**

*/s/* DANIEL A. RUDIO  
Name: **Daniel A. Rudio**  
Title: **Vice President, Controller and Principal Accounting**

**Officer (Principal Accounting Officer)**

Date: October 31, 2011



**Table of Contents****Exhibit Index****Exhibit**

<b>No.</b>	<b>Title</b>
10.118	Third Amendment, effective July 1, 2011, to the Supply Agreement for Bulk Narcotics Raw Materials, dated as of July 1, 1998, by and between Endo Pharmaceuticals and Mallinckrodt
10.119	Fourth Amendment, effective July 31, 2011, to the Supply Agreement for Bulk Narcotics Raw Materials, dated as of July 1, 1998, by and between Endo Pharmaceuticals and Mallinckrodt
10.120	Fifth Amendment, effective August 31, 2011, to the Supply Agreement for Bulk Narcotics Raw Materials, dated as of July 1, 1998, by and between Endo Pharmaceuticals and Mallinckrodt
10.121	Executive Employment Agreement between Endo and David P. Holveck, dated as of October 27, 2011
10.122	Executive Employment Agreement between Endo and Ivan P. Gergel, dated as of October 27, 2011
10.123	Fifth Amendment, dated as of August 15, 2011, to the License Agreement by and between Endo Pharmaceuticals and Vernalis Development Limited, dated July 14, 2004
10.124	Build to Suit Lease Agreement between Endo Pharmaceuticals Inc. and RT/TC Atwater LP
10.125	First Supplemental Indenture, among Penwest Pharmaceuticals Co. and Generics International (US), Inc., as guaranteeing subsidiaries, Endo, the guarantors named therein and Wells Fargo Bank, National Association, as trustee, dated December 13, 2010, to the Indenture among Endo, the guarantors named therein and Wells Fargo Bank, National Association, as trustee, dated November 23, 2010 (incorporated herein by reference as Exhibit 4.2 to the Form S-4 filed with the Commission on October 14, 2011)
10.126	Second Supplemental Indenture, among Generics Bidco I, LLC, as guaranteeing subsidiary, Endo, the guarantors named therein and Wells Fargo Bank, National Association, as trustee, dated December 21, 2010, to the Indenture among Endo, the guarantors named therein and Wells Fargo Bank, National Association, as trustee, dated November 23, 2010 (incorporated herein by reference as Exhibit 4.3 to the Form S-4 filed with the Commission on October 14, 2011)
10.127	Third Supplemental Indenture, among Ledgemont Royalty Sub LLC, as guaranteeing subsidiary, Endo, the guarantors named therein and Wells Fargo Bank, National Association, as trustee, dated February 17, 2011, to the Indenture among Endo, the guarantors named therein and Wells Fargo Bank, National Association, as trustee, dated November 23, 2010 (incorporated herein by reference as Exhibit 4.4 to the Form S-4 filed with the Commission on October 14, 2011)
10.128	Fourth Supplemental Indenture, among Vintage Pharmaceuticals, LLC, as guaranteeing subsidiary, Endo, the guarantors named therein and Wells Fargo Bank, National Association, as trustee, dated April 5, 2011, to the Indenture among Endo, the guarantors named therein and Wells Fargo Bank, National Association, as trustee, dated November 23, 2010 (incorporated herein by reference as Exhibit 4.5 to the Form S-4 filed with the Commission on October 14, 2011)
10.129	Fifth Supplemental Indenture, among American Medical Systems Holdings, Inc., American Medical Systems, Inc., AMS Research Corporation, AMS Sales Corporation and Laserscope, as guaranteeing subsidiaries, Endo, the guarantors named therein and Wells Fargo Bank, National Association, as trustee, dated June 22, 2011, to the Indenture among Endo, the guarantors named therein and Wells Fargo Bank, National Association, as trustee, dated November 23, 2010 (incorporated herein by reference as Exhibit 4.6 to the Form S-4 filed with the Commission on October 14, 2011)
10.130	Sixth Supplemental Indenture, among American Medical Systems, Inc. and Laserscope, as successor guarantors, Endo, the guarantors named therein and Wells Fargo Bank, National Association, as trustee, dated August 16, 2011, to the Indenture among Endo, the guarantors named therein and Wells Fargo Bank, National Association, as trustee, dated November 23, 2010 (incorporated herein by reference as Exhibit 4.7 to the Form S-4 filed with the Commission on October 14, 2011)
10.131	Seventh Supplemental Indenture, among Generics Bidco II, LLC, Generics International (US Holdco), Inc., Generics International (US Midco), Inc., Generics International (US Parent), Inc., Moores Mill Properties L.L.C., Quartz Specialty Pharmaceuticals, LLC and Wood Park Properties LLC, as guaranteeing subsidiaries, Endo, the guarantors named therein and Wells Fargo Bank, National Association, as trustee, dated September 26, 2011, to the Indenture among Endo, the guarantors named therein and Wells Fargo Bank, National Association, as trustee, dated November 23, 2010 (incorporated herein by reference as Exhibit 4.8 to the Form S-4 filed with the Commission on October 14, 2011)

## Edgar Filing: ENDO PHARMACEUTICALS HOLDINGS INC - Form 10-Q

- 10.132 First Supplemental Indenture, among American Medical Systems Holdings, Inc., American Medical Systems, Inc., AMS Research Corporation, AMS Sales Corporation and Laserscope, as guaranteeing subsidiaries, Endo, the guarantors named therein and Wells Fargo Bank, National Association, as trustee, dated June 17, 2011, to the Indenture among Endo, the guarantors named therein and Wells Fargo Bank, National Association, as trustee, dated June 8, 2011 (incorporated herein by reference as Exhibit 4.11 to the Form S-4 filed with the Commission on October 14, 2011)
- 10.133 Second Supplemental Indenture, among American Medical Systems, Inc. and Laserscope, as successor guarantors, Endo, the guarantors named therein and Wells Fargo Bank, National Association, as trustee, dated August 16, 2011, to the Indenture among Endo, the guarantors named therein and Wells Fargo Bank, National Association, as trustee, dated June 8, 2011 (incorporated herein by reference as Exhibit 4.12 to the Form S-4 filed with the Commission on October 14, 2011)
- 10.134 Third Supplemental Indenture, among Generics Bidco II, LLC, Generics International (US Holdco), Inc., Generics International (US Midco), Inc., Generics International (US Parent), Inc., Moores Mill Properties L.L.C., Quartz Specialty Pharmaceuticals, LLC and Wood Park Properties LLC, as guaranteeing subsidiaries, Endo, the guarantors named therein and Wells Fargo Bank, National Association, as trustee, dated September 26, 2011, to the Indenture among Endo, the guarantors named therein and Wells Fargo Bank, National Association, as trustee, dated June 8, 2011 (incorporated herein by reference as Exhibit 4.13 to the Form S-4 filed with the Commission on October 14, 2011)
- 10.135 First Supplemental Indenture, among American Medical Systems Holdings, Inc., American Medical Systems, Inc., AMS Research Corporation, AMS Sales Corporation and Laserscope, as guaranteeing subsidiaries, Endo, the guarantors named therein and Wells Fargo Bank, National Association, as trustee, dated June 17, 2011, to the Indenture among Endo, the guarantors named therein and Wells Fargo Bank, National Association, as trustee, dated June 8, 2011 (incorporated herein by reference as Exhibit 4.16 to the Form S-4 filed with the Commission on October 14, 2011)
- 10.136 Second Supplemental Indenture, among American Medical Systems, Inc. and Laserscope, as successor guarantors, Endo, the guarantors named therein and Wells Fargo Bank, National Association, as trustee, dated August 16, 2011, to the Indenture among Endo, the guarantors named therein and Wells Fargo Bank, National Association, as trustee, dated June 8, 2011 (incorporated herein by reference as Exhibit 4.17 to the Form S-4 filed with the Commission on October 14, 2011)
- 10.137 Third Supplemental Indenture, among Generics Bidco II, LLC, Generics International (US Holdco), Inc., Generics International (US Midco), Inc., Generics International (US Parent), Inc., Moores Mill Properties L.L.C., Quartz Specialty Pharmaceuticals, LLC and Wood Park Properties LLC, as guaranteeing subsidiaries, Endo, the guarantors named therein and Wells Fargo Bank, National Association, as trustee, dated September 26, 2011, to the Indenture among Endo, the guarantors named therein and Wells Fargo Bank, National Association, as trustee, dated June 8, 2011 (incorporated herein by reference as Exhibit 4.18 to the Form S-4 filed with the Commission on October 14, 2011)
- 21 Subsidiaries of the Registrant
- 31.1 Certification of the President and Chief Executive Officer of Endo pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
- 31.2 Certification of the Chief Financial Officer of Endo pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
- 32.1 Certification of the President and Chief Executive Officer of Endo pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002
- 32.2 Certification of the Chief Financial Officer of Endo pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002
- 101\* The following materials from Endo Pharmaceuticals Holdings Inc. s Quarterly Report on Form 10-Q for the quarter ended September 30, 2011, formatted in XBRL (eXtensible Business Reporting Language): (i) the Condensed Consolidated Balance Sheets, (ii) the Condensed Consolidated Statements of Operations, (iii) the Condensed Consolidated Statements of Cash Flows and (iv) the Notes to Condensed Consolidated Financial Statements.

\* Pursuant to Rule 406T of Regulation S-T, these interactive data files are deemed not filed or part of a registration statement or prospectus for purposes of Sections 11 or 12 of the Securities Act of 1933, as amended, are deemed not filed for purposes of Section 18 of the Securities Exchange Act of 1934, as amended, and otherwise are not subject to liability under those sections.