

PDL BIOPHARMA, INC.
Form 10-Q
April 30, 2010
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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

(Mark One)

Quarterly report pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934
For the quarterly period ended March 31, 2010

OR

Transition report pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934
For transition period from _____ to _____

Commission File Number: 000-19756

PDL BIOPHARMA, INC.

(Exact name of registrant as specified in its charter)

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Delaware
(State or other jurisdiction of
incorporation or organization)

94-3023969
(I.R.S. Employer
Identification Number)

932 Southwood Boulevard

Incline Village, Nevada 89451

(Address of principal executive offices and Zip Code)

(775) 832-8500

(Registrant's telephone number, including area code)

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes No

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes No

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

Large accelerated filer

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 Exchange Act). Yes No

As of April 28, 2010, there were 119,674,377 shares of the Registrant's Common Stock outstanding.

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We own or have rights to certain trademarks, trade names, copyrights and other intellectual property used in our business, including PDL BioPharma and the PDL logo, each of which is considered a trademark. All other company names, product names, trade names and trademarks included in this Quarterly Report are trademarks, registered trademarks or trade names of their respective owners.

Table of Contents**PART I. FINANCIAL INFORMATION****ITEM 1. FINANCIAL STATEMENTS****PDL BIOPHARMA, INC.****CONDENSED CONSOLIDATED STATEMENTS OF INCOME****(Unaudited)****(In thousands, except per share amounts)**

	Three Months Ended March 31,	
	2010	2009
Revenues:		
Royalties	\$ 62,061	\$ 62,298
License and other		324
Total revenues	62,061	62,622
General and administrative expenses	9,410	4,693
Operating income	52,651	57,929
Interest and other income, net	80	336
Interest expense	(12,527)	(3,574)
Income before income taxes	40,204	54,691
Income tax expense	14,197	17,234
Net income	\$ 26,007	\$ 37,457
Net income per basic share	\$ 0.22	\$ 0.31
Net income per diluted share	\$ 0.15	\$ 0.23
Cash dividends declared per common share	\$ 1.00	\$ 1.00
Shares used to compute income per basic and diluted share:		
Shares used to compute income per basic share	119,525	119,327
Shares used to compute income per diluted share	184,308	172,570

See accompanying notes.

Table of Contents**PDL BIOPHARMA, INC.****CONDENSED CONSOLIDATED BALANCE SHEETS****(In thousands, except per share amounts)**

	March 31, 2010 (Unaudited)	December 31, 2009 (Note 1)
Assets		
Current assets:		
Cash and cash equivalents	\$ 319,674	\$ 303,227
Receivables from licensees	150	1,050
Deferred tax assets		1,271
Prepaid and other current assets	14,292	10,288
Total current assets	334,116	315,836
Property and equipment, net	137	171
Long-term deferred tax assets	8,350	10,396
Other assets	15,648	12,008
Total assets	\$ 358,251	\$ 338,411
Liabilities and Stockholders Deficit		
Current liabilities:		
Accounts payable	\$ 685	\$ 370
Accrued compensation	1,954	2,206
Accrued interest	2,567	8,812
Other accrued liabilities	6,573	2,292
Deferred revenue	1,500	1,600
Dividend payable	119,974	386
Current portion of convertible notes payable	199,978	199,998
Current portion of non-recourse notes payable	84,386	77,852
Total current liabilities	417,617	293,516
Convertible notes payable	228,000	228,000
Non-recourse notes payable	202,993	222,148
Other long-term liabilities	10,700	10,700
Total liabilities	859,310	754,364
Commitments and contingencies (Note 12)		
Stockholders deficit:		
Preferred stock, par value \$0.01 per share, 10,000 shares authorized; no shares issued and outstanding		
Common stock, par value \$0.01 per share, 250,000 shares authorized; 119,526 and 119,523 shares issued and outstanding at March 31, 2010 and December 31, 2009, respectively	1,195	1,195
Additional paid-in capital	(201,325)	(83,850)
Accumulated deficit	(307,291)	(333,298)
Accumulated other comprehensive income	6,362	
Total stockholders deficit	(501,059)	(415,953)

Total liabilities and stockholders' deficit	\$ 358,251	\$ 338,411
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See accompanying notes.

Table of Contents**PDL BIOPHARMA, INC.****CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS****(Unaudited)****(In thousands)**

	Three Months Ended March 31,	
	2010	2009
Cash flows from operating activities		
Net income	\$ 26,007	\$ 37,457
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation expense	34	887
Amortization of convertible notes offering costs	501	585
Amortization of non-recourse notes offering costs	1,881	
Stock-based compensation expense	188	196
Tax benefit from stock-based compensation arrangements	1,989	12,792
Net excess tax benefit from stock-based compensation	(2,217)	(18,056)
Deferred income taxes	277	3,623
Changes in assets and liabilities:		
Receivables from licensees	900	12,876
Prepaid and other current assets	(285)	(33)
Other assets	47	
Accounts payable	315	(2,431)
Accrued liabilities	(2,601)	(20,083)
Deferred revenue	(100)	(100)
Net cash provided by operating activities	26,936	27,713
Cash flows from investing activities		
Purchase of property and equipment		(33)
Net cash used in investing activities		(33)
Cash flows from financing activities		
Proceeds from issuance of common stock, net of cancellations		256
Payments for debt issuance costs		(327)
Repayment of non-recourse notes	(12,621)	
Cash dividend paid	(85)	
Net excess tax benefit from stock-based compensation	2,217	18,056
Net cash provided by (used in) financing activities	(10,489)	17,985
Net increase in cash and cash equivalents	16,447	45,665
Cash and cash equivalents at beginning of the period	303,227	129,058
Cash and cash equivalents at end of the period	\$ 319,674	\$ 174,723

See accompanying notes.

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PDL BIOPHARMA, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

March 31, 2010

(Unaudited)

1. Summary of Significant Accounting Policies

Basis of Presentation

The accompanying unaudited Condensed Consolidated Financial Statements have been prepared in accordance with U.S. generally accepted accounting principles for interim financial information. The financial statements include all adjustments consisting only of normal recurring adjustments that the management of PDL BioPharma, Inc. (PDL, we or our) believes are necessary for a fair presentation of the periods presented. These interim financial results are not necessarily indicative of results expected for the full fiscal year or for any subsequent interim period.

The accompanying Condensed Consolidated Financial Statements and related financial information should be read in conjunction with the audited Consolidated Financial Statements and the related notes thereto for the year ended December 31, 2009, included in our Annual Report on Form 10-K filed with the U.S. Securities and Exchange Commission (SEC). The Condensed Consolidated Balance Sheet at December 31, 2009 has been derived from the audited Consolidated Financial Statements at that date.

Principles of Consolidation

Beginning in November 2009, the Consolidated Financial Statements include the accounts of PDL and its wholly-owned subsidiary, QHP Royalty Sub LLC (QHP). For the period from January to November 2009, we had no wholly owned subsidiaries. All intercompany transactions are eliminated in consolidation.

Table of Contents**PDL BIOPHARMA, INC.****NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)****March 31, 2010****(Unaudited)*****Foreign Currency Hedging Contracts***

We hedge certain foreign currency exposures related to our licensees' product sales with foreign currency exchange forward contracts and foreign currency exchange option contracts. In general, these contracts are intended to offset the underlying foreign currency market risk in our royalty revenues. Our exposure to credit risk from these contracts is a function of currency exchange rates and, therefore, varies over time. We limit the credit risk that our counterparty to these contracts may be unable to perform by transacting with a major bank, and for which we monitor the exposure in the context of current market conditions. We mitigated the risk of loss by entering into a netting agreement with our counterparty that provides for net settlement should our counterparty default on the forward and options contracts prior to maturity. Therefore, our overall risk of loss in the event of counterparty default is limited to the amount of any unrecognized gains on outstanding contracts net of any unrecognized losses on outstanding contracts at the date of default. We do not enter into speculative foreign currency transactions. We have designated the foreign currency contracts as cash flow hedges. At the inception of the hedging relationship and on a quarterly basis, we assess hedge effectiveness. The aggregate unrealized gain or loss on the effective component of our foreign currency exchange contracts net of estimated taxes is recorded in stockholders' deficit as accumulated other comprehensive income. Gains or losses on cash flow hedges are recognized as license and other revenue in the same period that the hedged transaction (royalty revenue) impacts earnings.

Customer Concentration

The following table summarizes revenues from our licensees' products which individually accounted for 10% or more of our total revenues for the three months ended March 31, 2010 and 2009:

Licensees	Product Name	Three Months Ended March 31,	
		2010	2009
Genentech, Inc. (Genentech)	Avastin®	27%	22%
	Herceptin®	38%	26%
	Lucentis®	12%	7%
MedImmune, LLC (MedImmune) ⁽¹⁾	Synagis®		27%
Elan Corporation, Plc (Elan)	Tysabri®	14%	11%

- (1) In December 2009, we sent a letter to MedImmune stating that it is in breach of its obligations under the license agreement, canceling the license agreement and revoking any licenses and rights granted therein. In February 2010, MedImmune made a royalty payment to an escrow account created *pendente lite* (while the litigation is pending). We do not expect to receive additional payments from MedImmune unless and until the lawsuit is resolved in our favor.

2. Stock-Based Compensation

Stock-based compensation expense for employees and directors for the three months ended March 31, 2010 and 2009 was as follows:

**Three Months Ended
March 31,**

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(In thousands)	2010	2009
General and administrative expenses	\$ 188	\$ 184
Income tax effect	(66)	(64)
Stock-based compensation expense included in net income	\$ 122	\$ 120

During the three months ended March 31, 2010, approximately 1.3 million of fully vested stock options with an average exercise price of \$20.36 were forfeited and expired unexercised.

3. Net Income per Share

We compute basic net income per share using the weighted-average number of shares of common stock outstanding during the periods presented less the weighted-average number of shares of restricted stock that are subject to repurchase. We compute diluted net income per share using the sum of the weighted-average number of common and common equivalent shares outstanding. Common equivalent shares used in the computation of diluted net income per share result from the assumed exercise of stock options, the issuance of restricted stock and the assumed conversion of our 2.00% Convertible Senior Notes (the 2012 Notes) and our 2.75% Convertible Subordinated Notes (the 2023 Notes), including both the effect of adding back interest expense and the inclusion of the underlying shares using the if-converted method. The adjusted conversion rate for the 2012 Notes is 128.318 shares per \$1,000 principal amount

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NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

March 31, 2010

(Unaudited)

of 2012 Notes, or a conversion price of approximately \$7.79 per share, effective March 16, 2010. The adjusted conversion rate for the 2023 Notes is 177.1594 shares per \$1,000 principal amount of 2023 Notes, or a conversion price of approximately \$5.64 per share, effective March 16, 2010. Following is a reconciliation of the numerators and denominators of the basic and diluted net income per share computations for the three months ended March 31, 2010 and 2009: