

ALKERMES INC  
Form 10-Q  
August 14, 2006

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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 June 30, 2006**
- 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 1-14131**

**ALKERMES, INC.**

*(Exact name of registrant as specified in its charter)*

**PENNSYLVANIA**

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

**23-2472830**

*(I.R.S. Employer Identification No.)*

**88 Sidney Street, Cambridge, MA**

*(Address of principal executive offices)*

**02139-4234**

*(Zip Code)*

**Registrant's telephone number including area code:**

**(617) 494-0171**

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

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

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, or a non-accelerated filer. See definition of "accelerated filer and large accelerated filer" in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer  Accelerated filer  Non-accelerated filer

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

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The number of shares outstanding of each of the issuer's classes of common stock was:

<b>Class</b>	<b>As of July 31, 2006</b>
Common Stock, \$.01 par value	100,922,394
Non-Voting Common Stock, \$.01 par value	382,632

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**ALKERMES, INC. AND SUBSIDIARIES**

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**Table of Contents****PART 1. FINANCIAL INFORMATION****Item 1. *Unaudited Condensed Consolidated Financial Statements:*****ALKERMES, INC. AND SUBSIDIARIES****CONDENSED CONSOLIDATED BALANCE SHEETS**

	<b>June 30, 2006</b>	<b>March 31, 2006</b>
	<b>(In thousands, except share and per share amounts)</b>	
<b>ASSETS</b>		
<b>CURRENT ASSETS:</b>		
Cash and cash equivalents	\$ 107,923	\$ 33,578
Investments short-term	260,616	264,389
Receivables	41,353	39,802
Inventory, net	11,378	7,341
Prepaid expenses and other current assets	4,802	2,782
Total current assets	426,072	347,892
<b>PROPERTY, PLANT AND EQUIPMENT:</b>		
Land	301	301
Building and improvements	21,186	20,966
Furniture, fixtures and equipment	63,752	61,086
Equipment under capital lease	464	464
Leasehold improvements	45,971	45,842
Construction in progress	27,158	23,555
	158,832	152,214
Less: accumulated depreciation and amortization	(42,586)	(39,297)
Property, plant and equipment net	116,246	112,917
RESTRICTED INVESTMENTS long-term	5,145	5,145
OTHER ASSETS	10,290	11,209
TOTAL ASSETS	\$ 557,753	\$ 477,163
<b>LIABILITIES, REDEEMABLE CONVERTIBLE PREFERRED STOCK AND SHAREHOLDERS EQUITY</b>		
<b>CURRENT LIABILITIES:</b>		
Accounts payable and accrued expenses	\$ 28,992	\$ 36,141

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Accrued interest	2,985	3,239
Accrued restructuring costs	855	852
Unearned milestone revenue current portion	56,320	83,338
Deferred revenue current portion	200	200
Convertible subordinated notes current portion	676	676
Long-term debt current portion	1,239	1,214
<b>Total current liabilities</b>	<b>91,267</b>	<b>125,660</b>
<b>NON-RECOURSE RISPERDAL CONSTA SECURED 7% NOTES</b>	<b>154,427</b>	<b>153,653</b>
<b>CONVERTIBLE SUBORDINATED NOTES LONG-TERM PORTION</b>		<b>124,346</b>
<b>LONG-TERM DEBT</b>	<b>1,200</b>	<b>1,519</b>
<b>UNEARNED MILESTONE REVENUE LONG-TERM PORTION</b>	<b>124,319</b>	<b>16,198</b>
<b>DEFERRED REVENUE LONG-TERM PORTION</b>	<b>700</b>	<b>750</b>
<b>OTHER LONG-TERM LIABILITIES</b>	<b>6,677</b>	<b>6,821</b>
<b>TOTAL LIABILITIES</b>	<b>378,590</b>	<b>428,947</b>
<b>REDEEMABLE CONVERTIBLE PREFERRED STOCK, par value, \$0.01 per share; authorized and issued, 1,500 shares at June 30, 2006 and March 31, 2006 (at liquidation preference)</b>	<b>15,000</b>	<b>15,000</b>
<b>COMMITMENTS AND CONTINGENCIES</b>		
<b>SHAREHOLDERS EQUITY:</b>		
Capital stock, par value, \$0.01 per share; authorized, 4,550,000 shares (includes 2,997,000 shares of preferred stock); issued, none		
Common stock, par value, \$0.01 per share; authorized, 160,000,000 shares; 101,041,464 and 91,744,680 shares issued, 100,906,834 and 91,744,680 shares outstanding at June 30, 2006 and March 31, 2006, respectively	1,010	917
Nonvoting common stock, par value, \$0.01 per share; authorized 450,000 shares; issued and outstanding, 382,632 shares at June 30, 2006 and March 31, 2006	4	4
Treasury stock, at cost (134,630 and 0 shares at June 30, 2006 and March 31, 2006, respectively)	(2,627)	
Additional paid-in capital	798,084	664,596
Deferred compensation		(374)
Accumulated other comprehensive income	1,398	1,064
Accumulated deficit	(633,706)	(632,991)
<b>Total shareholders equity</b>	<b>164,163</b>	<b>33,216</b>
<b>TOTAL LIABILITIES, REDEEMABLE CONVERTIBLE PREFERRED STOCK AND SHAREHOLDERS EQUITY</b>	<b>\$ 557,753</b>	<b>\$ 477,163</b>

The accompanying notes are an integral part of these unaudited condensed consolidated financial statements.

**Table of Contents****ALKERMES, INC. AND SUBSIDIARIES****CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS**

	<b>Three Months Ended June 30, 2006</b>	<b>Three Months Ended June 30, 2005</b>
	<b>(In thousands, except per share amounts)</b>	
<b>REVENUES:</b>		
Manufacturing revenues	\$ 22,193	\$ 13,983
Royalty revenues	5,139	3,604
Research and development revenue under collaborative arrangements	14,464	7,251
Net collaborative profit	9,742	
<b>Total revenues</b>	<b>51,538</b>	<b>24,838</b>
<b>EXPENSES:</b>		
Cost of goods manufactured	9,338	4,517
Research and development	25,863	21,622
Selling, general and administrative	16,530	8,952
<b>Total expenses</b>	<b>51,731</b>	<b>35,091</b>
<b>OPERATING LOSS</b>	<b>(193)</b>	<b>(10,253)</b>
<b>OTHER INCOME (EXPENSE):</b>		
Interest income	4,335	1,631
Interest expense	(5,473)	(5,169)
Derivative loss related to convertible subordinated notes		(266)
Other income (expense), net	787	320
<b>Total other income (expense)</b>	<b>(351)</b>	<b>(3,484)</b>
<b>LOSS BEFORE INCOME TAXES</b>	<b>(544)</b>	<b>(13,737)</b>
<b>INCOME TAXES</b>	<b>171</b>	
<b>NET LOSS</b>	<b>\$ (715)</b>	<b>\$ (13,737)</b>
<b>LOSS PER COMMON SHARE, BASIC AND DILUTED</b>	<b>\$ (0.01)</b>	<b>\$ (0.15)</b>
<b>WEIGHTED AVERAGE NUMBER OF COMMON SHARES OUTSTANDING, BASIC AND DILUTED</b>	<b>93,784</b>	<b>90,410</b>

The accompanying notes are an integral part of these unaudited condensed consolidated financial statements.



**Table of Contents****ALKERMES, INC. AND SUBSIDIARIES****CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS**

	<b>Three Months Ended June 30, 2006</b>	<b>Three Months Ended June 30, 2005</b>
	<b>(In thousands)</b>	
<b>CASH FLOWS FROM OPERATING ACTIVITIES:</b>		
Net loss	\$ (715)	\$ (13,737)
Adjustments to reconcile net loss to net cash provided by operating activities:		
Depreciation and amortization	2,826	2,578
Stock-based compensation	8,347	58
Other non-cash charges	1,215	1,303
Derivative loss related to convertible subordinated notes		266
Gain on investments	(846)	(308)
Loss on sale of equipment	5	
Changes in assets and liabilities:		
Receivables	(1,551)	(9,004)
Inventory, prepaid expenses and other current assets	(5,401)	(776)
Accounts payable, accrued expenses and accrued interest	(7,370)	1,006
Accrued restructuring costs	(159)	(322)
Unearned milestone revenue	81,103	160,000
Deferred revenue	(50)	100
Other long-term liabilities	18	108
Net cash provided by operating activities	77,422	141,272
<b>CASH FLOWS FROM INVESTING ACTIVITIES:</b>		
Additions to property, plant and equipment	(6,160)	(5,301)
Proceeds from the sale of equipment		1
Purchases of short and long-term investments	(63,374)	(326,173)
Sales and maturities of short and long-term investments	67,096	165,431
Decrease in other assets	14	18
Net cash used in investing activities	(2,424)	(166,024)
<b>CASH FLOWS FROM FINANCING ACTIVITIES:</b>		
Proceeds from issuance of common stock	2,268	351
Payment of debt	(294)	(273)
Purchase of treasury stock	(2,627)	
Net cash (used in) provided by financing activities	(653)	78
<b>NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS</b>	<b>74,345</b>	<b>(24,674)</b>

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CASH AND CASH EQUIVALENTS	Beginning of period	33,578	47,485
CASH AND CASH EQUIVALENTS	End of period	\$ 107,923	\$ 22,811
SUPPLEMENTARY INFORMATION:			
Cash paid for interest		\$ 4,511	\$ 2,057
Noncash activities:			
Conversion of 2.5% convertible subordinated notes into common stock		\$ 125,000	\$

The accompanying notes are an integral part of these unaudited condensed consolidated financial statements.

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**ALKERMES, INC. AND SUBSIDIARIES**

**NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**

**1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES**

***Basis of Presentation***

The accompanying condensed consolidated financial statements of Alkermes, Inc. (the Company or Alkermes) for the three months ended June 30, 2006 and 2005 are unaudited and have been prepared on a basis substantially consistent with the audited financial statements for the year ended March 31, 2006. In the opinion of management, the condensed consolidated financial statements include all adjustments that are necessary to present fairly the results of operations for the reported periods. The Company's condensed consolidated financial statements are prepared in conformity with accounting principles generally accepted in the United States of America (commonly referred to as GAAP).

These financial statements should be read in conjunction with the Company's audited consolidated financial statements and notes thereto which are contained in the Company's Annual Report on Form 10-K/A for the year ended March 31, 2006, filed with the Securities and Exchange Commission (SEC).

The results of the Company's operations for any interim period are not necessarily indicative of the results of the Company's operations for any other interim period or for a full fiscal year.

***Principles of Consolidation*** The unaudited condensed consolidated financial statements include the accounts of Alkermes, Inc. and its wholly-owned subsidiaries: Alkermes Controlled Therapeutics, Inc. (ACT I); Alkermes Controlled Therapeutics, Inc. II (ACT II); Alkermes Acquisition Corp.; Alkermes Europe, Ltd.; Advanced Inhalation Research, Inc. (AIR); and RC Royalty Sub LLC (Royalty Sub). Intercompany accounts and transactions have been eliminated. The assets of Royalty Sub are not available to satisfy obligations of Alkermes and its subsidiaries, other than the obligations of Royalty Sub including Royalty Sub's non-recourse RISPERDAL CONSTA secured 7% notes (the Non-Recourse 7% Notes).

***Use of Estimates*** The preparation of the Company's unaudited condensed consolidated financial statements in conformity with GAAP necessarily requires management to make estimates and assumptions that affect the following: (1) reported amounts of assets and liabilities; (2) disclosure of contingent assets and liabilities at the date of the unaudited condensed consolidated financial statements; and (3) the reported amounts of revenues and expenses during the reporting period. Actual results could differ from these estimates.

***New Accounting Pronouncements***

Effective April 1, 2006, the Company adopted the provisions of Statement of Financial Accounting Standards (SFAS) No. 151, *Inventory Costs* (SFAS 151), which amends Accounting Research Bulletin (ARB) No. 43, Chapter 4, *Inventory Pricing*, to clarify the accounting for idle facility expense, freight, handling costs and waste (spoilage). Adoption of SFAS 151 did not have a material impact on the unaudited condensed consolidated financial statements.

Effective April 1, 2006, the Company adopted the provisions of SFAS No. 123(R), *Share-Based Payment* (SFAS 123R). See Note 8.

In July 2006, the Financial Accounting Standards Board (FASB) issued FASB Interpretation (FIN) No. 48, *Accounting for Uncertainty in Income Taxes* (FIN No. 48), an interpretation of SFAS No. 109, *Accounting for Income Taxes*. FIN No. 48 clarifies the accounting for uncertainty in income taxes recognized in a company's financial

statements and prescribes a recognition threshold and measurement process for financial statement recognition and measurement of a tax position taken or expected to be taken in a tax return. FIN No. 48 also provides guidance on derecognition, classification, interest and penalties, accounting in interim periods, disclosure and transition and will become effective for the Company on April 1, 2007. The Company is in the process of evaluating the impact of adoption of FIN No. 48.

**Table of Contents****ALKERMES, INC. AND SUBSIDIARIES****NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)****2. COMPREHENSIVE LOSS**

Comprehensive loss for the three months ended June 30, 2006 and 2005 is as follows:

<b>(In thousands)</b>	<b>Three Months Ended June 30, 2006</b>	<b>Three Months Ended June 30, 2005</b>
Net loss	\$ (715)	\$ (13,737)
Unrealized gain on marketable securities	334	136
Comprehensive loss	\$ (381)	\$ (13,601)

**3. LOSS PER COMMON SHARE**

Basic loss per common share was calcul