

Pacira Pharmaceuticals, Inc.
Form 10-Q
October 27, 2015

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10-Q

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

For the Quarterly Period Ended September 30, 2015

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: 001-35060

PACIRA PHARMACEUTICALS, INC.
(Exact Name of Registrant as Specified in its Charter)

Delaware
(State or Other Jurisdiction of
Incorporation or Organization)

51-0619477
(I.R.S. Employer
Identification No.)

5 Sylvan Way, Suite 300
Parsippany, New Jersey, 07054
(Address and Zip Code of Principal Executive Offices)

(973) 254-3560
(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

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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

Smaller reporting company

(Do not check if a 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 October 25, 2015, 36,757,420 shares of the registrant’s common stock, \$0.001 par value per share, were outstanding.

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PACIRA PHARMACEUTICALS, INC.
QUARTERLY REPORT ON FORM 10-Q
FOR THE QUARTER ENDED SEPTEMBER 30, 2015

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PART I — FINANCIAL INFORMATION

Item 1. FINANCIAL STATEMENTS

PACIRA PHARMACEUTICALS, INC.
CONSOLIDATED BALANCE SHEETS

(Unaudited)

(In thousands, except share and per share amounts)

	September 30, 2015	December 31, 2014 (Note 2)
ASSETS		
Current assets:		
Cash and cash equivalents	\$ 30,522	\$ 37,520
Restricted cash	—	1,509
Short-term investments	115,916	119,138
Accounts receivable, net	25,919	22,366
Inventories, net	56,132	29,263
Prepaid expenses and other current assets	4,611	4,461
Total current assets	233,100	214,257
Long-term investments	17,921	24,431
Fixed assets, net	86,323	60,632
Goodwill	28,888	23,761
Intangibles, net	161	403
Other assets	2,595	2,588
Total assets	\$ 368,988	\$ 326,072
LIABILITIES AND STOCKHOLDERS' EQUITY		
Current liabilities:		
Accounts payable	\$ 8,471	\$ 6,758
Accrued expenses	30,295	28,311
Convertible senior notes	104,907	103,100
Current portion of royalty interest obligation	—	276
Current portion of deferred revenue	1,426	1,426
Income taxes payable	312	139
Total current liabilities	145,411	140,010
Deferred revenue	8,439	9,508
Other liabilities	6,125	5,409
Total liabilities	159,975	154,927
Commitments and contingencies (Note 12)		
Stockholders' equity:		
Preferred stock, par value \$0.001; 5,000,000 shares authorized; none issued and outstanding at September 30, 2015 and December 31, 2014	—	—
Common stock, par value \$0.001, 250,000,000 shares authorized; 36,735,981 shares issued and outstanding at September 30, 2015; 36,150,620 shares issued and outstanding at December 31, 2014	37	36

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Additional paid-in capital	514,796	481,334
Accumulated deficit	(305,791)	(310,145)
Accumulated other comprehensive loss	(29)	(80)
Total stockholders' equity	209,013	171,145
Total liabilities and stockholders' equity	\$ 368,988	\$ 326,072

See accompanying condensed notes to consolidated financial statements.

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CONSOLIDATED STATEMENTS OF OPERATIONS

(Unaudited)

(In thousands, except per share amounts)

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2015	2014	2015	2014
Revenues:				
Net product sales	\$61,150	\$50,920	\$176,297	\$132,697
Collaborative licensing and development revenue	357	357	1,069	930
Royalty revenue	706	771	2,310	2,249
Total revenues	62,213	52,048	179,676	135,876
Operating expenses:				
Cost of goods sold	15,901	20,391	52,409	58,472
Research and development	5,893	4,425	15,509	14,844
Selling, general and administrative	35,310	28,217	101,490	75,643
Total operating expenses	57,104	53,033	169,408	148,959
Income (loss) from operations	5,109	(985)	) 10,268	(13,083)
Other (expense) income:				
Interest income	171	134	504	237
Interest expense	(1,905)	) (2,037)	) (5,842)	) (6,222)
Royalty interest obligation	—	(73)	) (71)	) (330)
Loss on extinguishment of debt	—	—	(51)) —
Other, net	(8)	) (43)	) (82)	) (120)
Total other expense, net	(1,742)	) (2,019)	) (5,542)	) (6,435)
Income (loss) before income taxes	3,367	(3,004)	) 4,726	(19,518)
Income tax expense	(281)	) —	(372)) —
Net income (loss)	\$3,086	\$ (3,004)	) \$4,354	\$ (19,518)
Net income (loss) per share:				
Basic net income (loss) per common share	\$0.08	\$ (0.08)	) \$0.12	\$ (0.56)
Diluted net income (loss) per common share	\$0.08	\$ (0.08)	) \$0.11	\$ (0.56)
Weighted average common shares outstanding:				
Basic	36,663	35,943	36,460	35,039
Diluted	41,043	35,943	41,422	35,039

See accompanying condensed notes to consolidated financial statements.

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CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME (LOSS)(Unaudited)
(In thousands)

	Three Months Ended		Nine Months Ended	
	September 30,		September 30,	
	2015	2014	2015	2014
Net income (loss)	\$3,086	\$(3,004	) \$4,354	\$(19,518)
Other comprehensive income (loss):				
Net unrealized gain (loss) on investments	(2	) 39	51	3
Total other comprehensive income (loss)	(2	) 39	51	3
Comprehensive income (loss)	\$3,084	\$(2,965	) \$4,405	\$(19,515)

See accompanying condensed notes to consolidated financial statements.

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CONSOLIDATED STATEMENT OF STOCKHOLDERS' EQUITY

FOR THE NINE MONTHS ENDED SEPTEMBER 30, 2015

(Unaudited)
(In thousands)

	Common Stock		Additional	Accumulated	Accumulated	Other	Total
	Shares	Amount	Paid-In Capital	Deficit	Comprehensive	Income (Loss)	
Balances at December 31, 2014	36,151	\$36	\$481,334	\$(310,145)	\$(80)		\$171,145
Exercise of stock options	521	1	8,797	—	—		8,798
Shares issued under employee stock purchase plan	20	—	1,195	—	—		1,195
Stock-based compensation	—	—	23,640	—	—		23,640
Issuance of common stock upon conversion of convertible senior notes	44	—	3,930	—	—		3,930
Retirement of equity component of convertible senior notes	—	—	(4,100)	—	—		(4,100)
Net unrealized gain on investments	—	—	—	—	51		51
Net income	—	—	—	4,354	—		4,354
Balances at September 30, 2015	36,736	\$37	\$514,796	\$(305,791)	\$(29)		\$209,013

See accompanying condensed notes to consolidated financial statements.

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CONSOLIDATED STATEMENTS OF CASH FLOWS(Unaudited)
(In thousands)

	Nine Months Ended September 30,	
	2015	2014 (Note 2)
Operating activities:		
Net income (loss)	\$4,354	\$(19,518)
Adjustments to reconcile net income (loss) to net cash provided by operating activities:		
Depreciation of fixed assets and amortization of intangibles	8,356	7,328
Amortization of unfavorable lease obligation and debt issuance costs	361	365
Amortization of debt discount	3,080	3,104
Loss on extinguishment of debt	51	—
Loss on disposal of fixed assets	—	157
Stock-based compensation	23,640	17,199
Changes in operating assets and liabilities:		
Restricted cash	1,509	(196)
Accounts receivable, net	(3,553)	(5,927)
Inventories, net	(26,869)	(8,105)
Prepaid expenses and other assets	(647)	(696)
Accounts payable and accrued expenses	2,034	9,560
Royalty interest obligation	(276)	(641)
Other liabilities	990	2,142
Deferred revenue	(1,069)	7,070
Net cash provided by operating activities	11,961	11,842
Investing activities:		
Purchases of fixed assets	(32,146)	(14,161)
Purchases of short-term investments	(125,197)	(140,410)
Sales of short-term investments	134,984	68,016
Purchases of long-term investments	—	(24,465)
Payment of contingent consideration	(5,127)	(11,720)
Net cash used in investing activities	(27,486)	(122,740)
Financing activities:		
Proceeds from follow-on public offering, net	—	110,407
Proceeds from exercise of stock options and warrants	8,798	5,732
Proceeds from shares issued under employee stock purchase plan	1,195	—
Conversion of principal and equity component of convertible senior notes	(1,466)	—
Net cash provided by financing activities	8,527	116,139
Net (decrease) increase in cash and cash equivalents	(6,998)	5,241
Cash and cash equivalents, beginning of period	37,520	12,515
Cash and cash equivalents, end of period	\$30,522	\$17,756
Supplemental cash flow information:		
Cash paid for interest, including royalty interest obligation	\$4,224	\$4,873
Cash paid for income taxes	\$199	\$—
Non-cash investing and financing activities:		

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Issuance of stock from conversion of convertible senior notes	\$3,930	\$—
Purchases of fixed assets accrued but not paid	\$1,660	\$616

See accompanying condensed notes to consolidated financial statements.

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PACIRA PHARMACEUTICALS, INC.
CONDENSED NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited)

NOTE 1—DESCRIPTION OF BUSINESS

Pacira Pharmaceuticals, Inc. and its subsidiaries (collectively, the “Company” or “Pacira”) is a specialty pharmaceutical company focused on the development, commercialization and manufacture of proprietary pharmaceutical products, based on its proprietary DepoFoam[®] extended release drug delivery technology, for use primarily in hospitals and ambulatory surgery centers. The Company’s lead product, EXPAREL[®] (bupivacaine liposome injectable suspension), which consists of bupivacaine encapsulated in DepoFoam, was approved by the United States Food and Drug Administration, or FDA, on October 28, 2011 and launched commercially in April 2012. DepoFoam is also the basis for the Company’s other FDA-approved commercial product, DepoCyt(e), which the Company manufactures for its commercial partners.

Pacira is subject to risks common to companies in similar industries and stages of development, including, but not limited to, competition from larger companies, reliance on revenue from few customers and products, reliance on a single manufacturing site, new technological innovations, dependence on key personnel, reliance on third-party service providers and sole source suppliers, protection of proprietary technology and compliance with government regulations.

NOTE 2—SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Basis of Presentation and Principles of Consolidation

These interim consolidated financial statements have been prepared in accordance with generally accepted accounting principles in the United States of America, or GAAP, and in accordance with the rules and regulations of the Securities and Exchange Commission for interim reporting. Pursuant to these rules and regulations, certain information and footnote disclosures normally included in complete annual financial statements have been condensed or omitted. Therefore, these interim consolidated financial statements should be read in conjunction with the audited annual consolidated financial statements and notes thereto included in the Company’s Annual Report on Form 10-K for the year ended December 31, 2014.

The consolidated financial statements at September 30, 2015, and for the three and nine months ended September 30, 2015 and 2014, are unaudited, but include all adjustments (consisting of only normal recurring adjustments) which, in the opinion of management, are necessary to present fairly the financial information set forth herein in accordance with GAAP. The consolidated balance sheet as of December 31, 2014 has been derived from the audited consolidated financial statements included in the Company’s Annual Report on Form 10-K for the year ended December 31, 2014. The consolidated financial statements as presented reflect certain reclassifications from previously issued financial statements to conform to the current year presentation. The consolidated financial statements include the accounts of the Company and its wholly-owned subsidiaries. Intercompany accounts and transactions have been eliminated in consolidation.

The results of operations for the interim periods are not necessarily indicative of results that may be expected for any other interim period or for the full year.

Concentration of Major Customers

The Company's customers are national and regional wholesalers of pharmaceutical products as well as commercial, collaborative and licensing partners. The Company sells EXPAREL through a drop-ship program under which orders are processed through wholesalers (including AmerisourceBergen Health Corporation, Cardinal Health, Inc. and McKesson Drug Company) without the wholesaler ever taking physical possession of the product. Shipments of EXPAREL are sent directly to individual accounts, such as hospitals, ambulatory surgery centers and individual doctors. The table below includes the percentage of revenue comprised by the Company's three largest customers (i.e., wholesalers or commercial partners) in each period presented:

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	Three Months Ended		Nine Months Ended	
	September 30,		September 30,	
	2015	2014	2015	2014
Largest customer	33%	34%	32%	33%
Second largest customer	29%	29%	30%	29%
Third largest customer	27%	24%	28%	23%
	89%	87%	90%	85%

Recent Accounting Pronouncements

In May 2014, the Financial Accounting Standards Board, or FASB, issued Accounting Standards Update, or ASU, 2014-09, Revenue from Contracts with Customers, which requires that an entity recognize the amount of revenue to which it expects to be entitled for the transfer of promised goods or services to its customers. In order to achieve this core principle, an entity should apply the following steps: (1) identify the contract(s) with a customer; (2) identify the performance obligations in the contract; (3) determine the transaction price; (4) allocate the transaction price to the performance obligations in the contract; and (5) recognize revenue when (or as) the entity satisfies a performance obligation. In August 2015, the FASB issued Accounting Standards Update 2015-14, Revenue from Contracts with Customers: Deferral of the Effective Date. This latest standard defers the effective date of revenue standard ASU 2014-09 by one year and permits early adoption on a limited basis. This update will replace existing revenue recognition guidance under GAAP when it becomes effective for the Company beginning January 1, 2018, with early adoption permitted in the first quarter of 2017. The updated standard will permit the use of either the retrospective or cumulative effect transition method. The Company is continuing to evaluate the impact of these updates on its consolidated financial statements.

In April 2015, the FASB issued ASU 2015-03, Interest—Imputation of Interest, which requires that debt issuance costs related to a recognized debt liability be presented in the balance sheet as a direct deduction from the carrying amount of the related debt liability instead of being presented as an asset. Debt disclosures will include the face amount of the debt liability and the effective interest rate. The update requires retrospective application and represents a change in accounting principle. The update is effective for fiscal years beginning after December 15, 2015. Early adoption is permitted for financial statements that have not been previously issued. The adoption of ASU 2015-03 is not expected to have a material impact on the Company's consolidated financial statements.

In July 2015, the FASB issued ASU 2015-11, Inventory (Topic 330): Simplifying the Measurement of Inventory. The standard requires entities to measure most inventory "at the lower of cost and net realizable value," thereby simplifying the current guidance under which an entity must measure inventory at the lower of cost or market (market in this context is defined as one of three different measures, one of which is net realizable value). The standard is effective for the Company prospectively beginning January 1, 2017. The adoption of ASU 2015-11 is not expected to have a material impact on the Company's consolidated financial statements.

NOTE 3—INVENTORIES

The components of inventories are as follows (in thousands):

	September 30,	December 31,
	2015	2014
Raw materials	\$16,096	\$9,263
Work-in-process	8,866	8,617
Finished goods	31,170	11,383
Total	\$56,132	\$29,263

NOTE 4—FIXED ASSETS

Fixed assets, summarized by major category, consist of the following (in thousands):

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	September 30, 2015	December 31, 2014
Machinery and laboratory equipment	\$31,682	\$29,697
Leasehold improvements	30,213	26,350
Computer equipment and software	4,037	3,754
Office furniture and equipment	1,484	1,001
Construction in progress	44,009	19,944
Total	111,425	80,746
Less: accumulated depreciation	(25,102	) (20,114
Fixed assets, net	\$86,323	\$60,632

For the three months ended September 30, 2015 and 2014, depreciation expense was \$2.8 million and \$2.3 million, respectively. For the three months ended September 30, 2015 and 2014, capitalized interest on the construction of manufacturing sites was \$0.2 million and \$0.1 million, respectively.

For the nine months ended September 30, 2015 and 2014, depreciation expense was \$8.1 million and \$6.7 million, respectively. For the nine months ended September 30, 2015 and 2014, capitalized interest on the construction of manufacturing sites was \$0.6 million and \$0.3 million, respectively.

NOTE 5—GOODWILL AND INTANGIBLE ASSETS

In March 2007, the Company acquired from SkyePharma Holding, Inc., or Skyepharma, its California operating subsidiary, referred to herein as the Acquisition. The Company's goodwill arose in April 2012 from a contingent milestone payment to Skyepharma in connection with the Acquisition. The Acquisition was accounted for under Statement of Financial Accounting Standards 141, Accounting for Business Combinations, which was the effective GAAP standard at the Acquisition date. In connection with the Acquisition, the Company agreed to certain earn-out payments based on a percentage of net sales of EXPAREL collected and certain other yet-to-be-developed products, as well as milestone payments for EXPAREL, as follows:

- (i) \$10.0 million upon the first commercial sale in the United States (met April 2012);
- (ii) \$4.0 million upon the first commercial sale in a major EU country (United Kingdom, France, Germany, Italy and Spain);
- (iii) \$8.0 million when annual net sales collected reach \$100.0 million (met September 2014);
- (iv) \$8.0 million when annual net sales collected reach \$250.0 million; and
- (v) \$32.0 million when annual net sales collected reach \$500.0 million.

All earn-out payments are treated as additional costs of the Acquisition and, therefore, are recorded as goodwill if and when each contingency is resolved. The first milestone was met in April 2012, resulting in a \$10.0 million payment to Skyepharma. The Company recorded this payment net of a \$2.0 million contingent consideration liability recognized at the time of the Acquisition, resulting in \$8.0 million recorded as goodwill. In September 2014, the Company made an \$8.0 million milestone payment to Skyepharma in connection with achieving \$100.0 million of annual EXPAREL net sales collected. For purposes of meeting future milestone payments, annual net sales are measured on a rolling quarterly basis. Cumulatively through September 30, 2015, the Company has recorded an additional \$12.9 million as goodwill for earn-out payments which are based on a percentage of net sales of EXPAREL collected.

The change in the carrying value of goodwill is summarized as follows (in thousands):

	Carrying Value of Goodwill
Balance at December 31, 2014	\$23,761

Percentage payments on collections of net sales of EXPAREL	5,127
Balance at September 30, 2015	\$28,888

Intangible assets, net, consist of core technology, developed technology and trademarks and trade names acquired in the Acquisition and are summarized as follows (in thousands):

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	September 30, 2015			December 31, 2014			
	Gross Carrying Value	Accumulated Amortization	Intangible Assets, Net	Gross Carrying Value	Accumulated Amortization	Intangible Assets, Net	Estimated Useful Life
Amortizable intangible assets:							