UNITED THERAPEUTICS Corp
Form 10-Q
October 25, 2017
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UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

FORM 10-Q

(Mark One)

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

For the quarterly period ended September 30, 2017

OR

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

For the transition period from to

Commission file number 0-26301

United Therapeutics Corporation

(Exact Name of Registrant as Specified in Its Charter)

Delaware (State or Other Jurisdiction of Incorporation or Organization)	**52-1984749** (I.R.S. Employer Identification No.)
1040 Spring Street, Silver Spring, MD (Address of Principal Executive Offices)	**20910** (Zip Code)

(301) 608-9292

(Registrant s Telephone Number, Including Area Code)

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

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

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

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

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

If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the Exchange Act. o

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

The number of shares outstanding of the issuer s common stock, par value $.01 per share, as of October 18, 2017 was 43,211,053.

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PART I. FINANCIAL INFORMATION

Item 1. CONSOLIDATED FINANCIAL STATEMENTS

UNITED THERAPEUTICS CORPORATION

CONSOLIDATED BALANCE SHEETS

(In millions, except share data)

	September 30, 2017 (Unaudited)	December 31, 2016
Assets		
Current assets:		
Cash and cash equivalents	$ 1,067.5	$ 1,023.0
Marketable investments	143.2	27.8
Accounts receivable, no allowance for 2017 and 2016	251.8	214.5
Inventories, net	114.4	100.0
Other current assets	62.3	59.5
Total current assets	1,639.2	1,424.8
Marketable investments	338.5	2.3
Goodwill and other intangible assets, net	45.7	33.8
Property, plant and equipment, net	521.7	489.3
Deferred tax assets, net	177.9	178.3
Other non-current assets	213.0	197.1
Total assets	$ 2,936.0	$ 2,325.6
Liabilities and Stockholders Equity		
Current liabilities:		
Accounts payable and accrued expenses	$ 143.3	$ 104.2
Line of credit	250.0	
Share tracking awards plan	145.1	194.8
Other current liabilities	251.0	33.5
Total current liabilities	789.4	332.5
Non-current liabilities	57.5	130.9
Total liabilities	846.9	463.4
Commitments and contingencies		
Temporary equity	19.2	10.9
Stockholders equity:		
Preferred stock, par value $.01, 10,000,000 shares authorized, no shares issued		
Series A junior participating preferred stock, par value $.01, 100,000 shares authorized, no shares issued		
Common stock, par value $.01, 245,000,000 shares authorized, 69,825,916 and 69,340,985 shares issued, and 43,206,700 and 42,965,856 shares outstanding at September 30, 2017 and December 31, 2016, respectively	0.7	0.7
Additional paid-in capital	1,838.6	1,813.5
Accumulated other comprehensive loss	(16.8)	(16.8)
	(2,579.2)	(2,379.6)

Treasury stock, 26,619,216 and 26,375,129 shares at September 30, 2017 and December 31, 2016, respectively				
Retained earnings		2,826.6		2,433.5
Total stockholders equity		2,069.9		1,851.3
Total liabilities and stockholders equity	$	2,936.0	$	2,325.6

See accompanying notes to consolidated financial statements.

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UNITED THERAPEUTICS CORPORATION

CONSOLIDATED STATEMENTS OF OPERATIONS

(In millions, except per share data)

	Three Months Ended September 30, 2017	Three Months Ended September 30, 2016	Nine Months Ended September 30, 2017	Nine Months Ended September 30, 2016
	(Unaudited)		(Unaudited)	
Revenues:				
Net product sales	$ 445.5	$ 408.2	$ 1,260.6	$ 1,189.8
Total revenues	445.5	408.2	1,260.6	1,189.8
Operating expenses:				
Cost of product sales	19.5	23.6	52.7	44.3
Research and development	55.0	45.9	151.0	80.7
Selling, general and administrative	47.2	100.1	171.0	177.3
Estimated loss contingency			210.0	
Total operating expenses	121.7	169.6	584.7	302.3
Operating income	323.8	238.6	675.9	887.5
Other (expense) income:				
Interest expense	(3.3)	(0.5)	(5.5)	(1.7)
Other, net	3.3	1.0	7.7	2.9
Impairment of cost method investment	(3.1)		(49.6)	
Total other (expense) income, net	(3.1)	0.5	(47.4)	1.2
Income before income taxes	320.7	239.1	628.5	888.7
Income tax expense	(44.4)	(77.3)	(229.6)	(285.3)
Net income	$ 276.3	$ 161.8	$ 398.9	$ 603.4
Net income per common share:				
Basic	$ 6.37	$ 3.75	$ 9.00	$ 13.62
Diluted	$ 6.27	$ 3.50	$ 8.83	$ 12.76
Weighted average number of common shares outstanding:				
Basic	43.4	43.2	44.3	44.3
Diluted	44.1	46.2	45.2	47.3

See accompanying notes to consolidated financial statements.

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UNITED THERAPEUTICS CORPORATION

CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME

(In millions)

	Three Months Ended September 30, 2017	Three Months Ended September 30, 2016	Nine Months Ended September 30, 2017	Nine Months Ended September 30, 2016
	(Unaudited)		(Unaudited)	
Net income	$ 276.3	$ 161.8	$ 398.9	$ 603.4
Other comprehensive income:				
Foreign currency translation (losses) gain		(1.0)	0.2	(2.8)
Defined benefit pension plan:				
Actuarial (losses) gain arising during period, net of tax		(1.2)	(0.1)	5.9
Amortization of actuarial gain and prior service cost included in net periodic pension cost, net of tax	0.1	0.1	0.4	0.5
Total defined benefit pension plan, net of tax	0.1	(1.1)	0.3	6.4
Unrealized loss on available-for-sale securities	(0.3)		(0.5)	
Other comprehensive (losses) gain, net of tax	(0.2)	(2.1)		3.6
Comprehensive income	$ 276.1	$ 159.7	$ 398.9	$ 607.0

See accompanying notes to consolidated financial statements.

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UNITED THERAPEUTICS CORPORATION

CONSOLIDATED STATEMENTS OF CASH FLOWS

(In millions)

	Nine Months Ended September 30, 2017	Nine Months Ended September 30, 2016
	(Unaudited)	
Cash flows from operating activities:		
Net income	$ 398.9	$ 603.4
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	23.3	23.8
Share-based compensation benefit	(45.0)	(93.2)
Impairment of cost method investments	49.6	
Estimated loss contingency	210.9	
Other	(9.2)	2.5
Excess tax benefits from share-based compensation		(4.6)
Changes in operating assets and liabilities:		
Accounts receivable	(37.3)	(31.7)
Inventories	(17.0)	(12.9)
Accounts payable and accrued expenses	37.9	13.9
Other assets and liabilities	(52.1)	(21.0)
Net cash provided by operating activities	560.0	480.2
Cash flows from investing activities:		
Purchases of property, plant and equipment	(58.5)	(23.3)
Proceeds from sale of property, plant and equipment	8.3	
Purchases of held-to-maturity and other investments	(51.8)	(0.8)
Maturities of held-to-maturity investments	52.6	78.8
Purchases of available-for-sale investments	(452.6)	
Purchase of investments held at cost	(55.3)	(7.6)
Purchase of investments under the equity method		(2.1)
Consolidation of variable interest entity	0.1	
Intangible assets acquired		(5.2)
Net cash (used in) provided by investing activities	(557.2)	39.8
Cash flows from financing activities:		
Proceeds from line of credit	250.0	
Principal payments of debt		(8.8)
Payments of debt issuance costs	(0.7)	(6.8)
Payments to repurchase common stock	(250.0)	(395.5)
Proceeds from the exercise of stock options	38.2	6.2
Issuance of stock under employee stock purchase plan	4.0	4.3
Excess tax benefits from share-based compensation		4.6
Net cash provided by (used in) financing activities	41.5	(396.0)
Effect of exchange rate changes on cash and cash equivalents	0.2	(2.8)
Net increase in cash and cash equivalents	44.5	121.2
Cash and cash equivalents, beginning of period	1,023.0	831.8
Cash and cash equivalents, end of period	$ 1,067.5	$ 953.0
Supplemental cash flow information:		

Cash paid for interest	$	3.8	$	0.1
Cash paid for income taxes	$	250.6	$	283.7
Non-cash investing and financing activities:				
Non-cash additions to property, plant and equipment	$	7.7	$	3.2
Issuance of common stock upon conversion of convertible notes	$		$	7.5

See accompanying notes to consolidated financial statements.

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UNITED THERAPEUTICS CORPORATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

September 30, 2017

(UNAUDITED)

1. Organization and Business Description

United Therapeutics Corporation is a biotechnology company focused on the development and commercialization of innovative products to address the unmet medical needs of patients with chronic and life-threatening conditions.

We have approval from the U.S. Food and Drug Administration (FDA) to market the following therapies: Remodulin® (treprostinil) Injection (Remodulin), Tyvaso® (treprostinil) Inhalation Solution (Tyvaso), Adcirca® (tadalafil) Tablets (Adcirca), Orenitram® (treprostinil) Extended-Release Tablets (Orenitram) and Unituxin® (dinutuximab) Injection (Unituxin). Our only significant revenues outside the United States are derived from sales of Remodulin in Europe.

As used in these notes to the consolidated financial statements, unless the context otherwise requires, the terms we , us , our , and similar terms refer to United Therapeutics Corporation and its consolidated subsidiaries.

2. Basis of Presentation

The accompanying unaudited consolidated financial statements have been prepared in accordance with the rules and regulations of the U.S. Securities and Exchange Commission (SEC) for interim financial information. Accordingly, they do not include all of the information required by U.S. generally accepted accounting principles (GAAP) for complete financial statements. These consolidated financial statements should be read in conjunction with the audited consolidated financial statements and the accompanying notes to the consolidated financial statements contained in our Annual Report on Form 10-K for the year ended December 31, 2016, as filed with the SEC on February 22, 2017.

In our management s opinion, the accompanying consolidated financial statements contain all adjustments, including normal, recurring adjustments, necessary to fairly present our financial position as of September 30, 2017, statements of operations and statements of comprehensive income for the three- and nine-month periods ended September 30, 2017 and September 30, 2016 and statements of cash flows for the nine-month periods ended September 30, 2017 and September 30, 2016. Interim results are not necessarily indicative of results for an entire year.

Recently Issued Accounting Standards

Accounting Standards Adopted During the Period

In July 2015, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update (ASU) No. 2015-11, *Simplifying the Measurement of Inventory* (ASU 2015-11), which requires that inventory be measured at the lower of cost or net realizable value for entities using first-in, first-out or average cost methods. ASU 2015-11 should be applied prospectively and is effective for fiscal years beginning after December 15, 2016, and for interim periods within those fiscal years. We adopted this standard on January 1, 2017, with no material impact on our financial statements.

In March 2016, the FASB issued ASU No. 2016-09, *Compensation Stock Compensation* (ASU 2016-09), which serves to simplify the accounting for share-based payment transactions. ASU 2016-09 includes guidance on several aspects of the accounting for share-based payments, including the income tax consequences, forfeitures and classification on the statement of cash flows. ASU 2016-09 is effective for fiscal years beginning after December 15, 2016, and for interim periods within those fiscal years. We adopted this standard on January 1, 2017. Upon adoption of ASU 2016-09, we began to recognize excess tax benefits as income tax benefits on our consolidated statements of operations. Previously, we recognized such amounts in additional paid-in capital on our consolidated balance sheets. Additionally, on January 1, 2017, we established an accounting policy election to account for forfeitures of share-based awards when they occur. Upon adoption, we recognized a cumulative-effect adjustment for the removal of the forfeiture estimate with respect to awards that were continuing to vest as of January 1, 2017. The adjustment resulted in a decrease to retained earnings of $5.8 million, which is net of a $3.2 million tax benefit. The guidance also requires that we classify excess tax benefits as an operating activity in our consolidated statements of cash flows, whereas we previously classified such amounts as a financing activity. These amounts are now classified as other in our cash flows from operating activities. We have adopted ASU 2016-09 on a prospective basis and, as such, prior periods have not been adjusted, with the exception of the cumulative-effect adjustment to retained earnings for the removal of the forfeiture estimate, which was adopted on a modified retrospective basis. Refer to Note 7 *Share Tracking Awards Plans,* Note 9 *Stockholders Equity Stock Options* and Note 10 *Income Taxes*.

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Accounting Standards Not Yet Adopted

In May 2014, the FASB issued ASU No. 2014-09, *Revenue from Contracts with Customers* (ASU 2014-09), and subsequent clarifying guidance. This guidance eliminates transaction-specific and industry-specific revenue recognition guidance under current GAAP and replaces it with a principles-based approach for determining revenue recognition. This guidance requires that companies recognize revenue based on the value of transferred goods or services as they occur in accordance with the contract. In addition, disclosure is required about the nature, amount, timing and uncertainty of revenue and cash flows arising from customer contracts, including significant judgments and changes in judgments and assets recognized from costs incurred to obtain or fulfill a contract. The new standard is required to be applied either retrospectively to each prior reporting period presented (full retrospective approach) or retrospectively with the cumulative effect of initial application recognized at the date of initial application (modified retrospective approach). The new standard is effective for reporting periods beginning after December 15, 2017. We have completed the review of our revenue contract portfolio and do not believe adoption of the new standard will have a material impact on the timing or measurement of our revenue. We are finalizing our revenue accounting policy and other revenue-related documentation and implementing changes to our business processes and controls in preparation for adoption of the new standard. We will adopt the requirements of the new standard in the first quarter of 2018 using the modified retrospective method. The modified retrospective method requires companies to recognize the cumulative effect of initially applying the new standard as an adjustment to opening retained earnings.

In January 2016, the FASB issued ASU No. 2016-01, *Financial Instruments Overall: Recognition and Measurement of Financial Assets and Financial Liabilities* (ASU 2016-01), which requires equity investments to be measured at fair value through net income. Equity investments that are accounted for under the equity method are not impacted. ASU 2016-01 provides that equity investments without readily determinable fair values can be valued at cost minus impairment using a simplified impairment assessment that utilizes qualitative assessments. ASU 2016-01 requires separate presentation of the financial assets and liabilities by category and form. ASU 2016-01 should be applied prospectively and will be effective for fiscal years beginning after December 15, 2017, and for interim periods within those fiscal years. We will adopt the requirements of the new standard in the first quarter of 2018 and do not currently expect adoption to have a material impact on our financial statements.

In February 2016, the FASB issued ASU No. 2016-02, *Leases* (ASU 2016-02), which requires that lease assets and lease liabilities be recognized on the balance sheet. ASU 2016-02 also requires additional quantitative and qualitative disclosures that provide the amount, timing, and uncertainty of cash flows relating to lease arrangements. ASU 2016-02 is effective for annual reporting periods beginning after December 15, 2018, using a modified retrospective approach. The modified retrospective approach requires retrospective application to the earliest period presented in the respective financial statements, provides certain practical expedients related to leases that commenced prior to the effective date and allows the use of hindsight when evaluating lease options. Early adoption is permitted. We are currently evaluating the effect of adoption on our financial statements.

In August 2016, the FASB issued ASU No. 2016-15, *Statement of Cash Flows Classification of Certain Cash Receipts and Cash Payments* (ASU 2016-15), which reduces existing diversity in the classification of certain cash receipts and cash payments on the statements of cash flows. ASU 2016-15 is effective for fiscal years beginning after December 15, 2017, and for interim periods within those fiscal years. We will adopt the requirements of the new standard in the first quarter of 2018 and do not currently expect adoption to have a material impact on our financial statements.

In October 2016, the FASB issued ASU No. 2016-16, *Income Taxes Intra-Entity Transfers of Assets Other Than Inventory* (ASU 2016-16), which requires that an entity recognize the income tax consequences of an intra-entity transfer of assets other than inventory when the transfer occurs. ASU 2016-16 is effective for annual reporting periods beginning after December 15, 2017 using a modified retrospective approach through a cumulative adjustment to retained earnings as of the beginning of the period of adoption. We will adopt the requirements of the new standard in the first quarter of 2018 and do not currently expect adoption to have a material impact on our financial statements.

In January 2017, the FASB issued ASU No. 2017-01, *Business Combinations-Clarifying the Definition of a Business* (ASU 2017-01). This update narrows the definition of a business by providing a screen to determine when an integrated set of assets and activities is not a business. The screen specifies that an integrated set of assets and activities is not a business if substantially all of the fair value of the gross assets acquired or disposed of is concentrated in a single asset or a group of similar identifiable assets. ASU 2017-01 should be applied prospectively and is effective for annual reporting periods beginning after December 15, 2017, and for interim periods within those fiscal years. We will adopt the requirements of the new standard in the first quarter of 2018 and do not currently expect adoption to have a material impact on our financial statements.

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In January 2017, the FASB issued ASU No. 2017-04, *Intangibles-Goodwill and Other: Simplifying the Test for Goodwill Impairment* (ASU 2017-04), which simplifies how an entity is required to test goodwill for impairment. A goodwill impairment will be measured by the amount by which a reporting unit s carrying value exceeds its fair value, with the amount of impairment not to exceed the carrying amount of goodwill. ASU 2017-04 is effective for goodwill impairment tests in fiscal years beginning after December 15, 2019, and for interim periods within those fiscal years, and must be adopted on a prospective basis. Early adoption is permitted. We are currently evaluating the effect of adoption on our financial statements.

In March 2017, the FASB issued ASU No. 2017-07, *Compensation-Retirement Benefits* (ASU 2017-07), which improves the presentation of net periodic pension cost and net periodic post-retirement benefit cost. For employers that present a measure of operating income in their statement of income, ASU 2017-07 requires employers to include only the service cost component of net periodic pension cost and net periodic post-retirement benefit cost in operating expense along with other employee compensation costs. Under ASU 2017-07, the service cost component of net benefit cost is eligible for capitalization. Additionally, this update further requires other components of net benefit cost to be included in non-operating expenses. ASU 2017-07 is effective for fiscal years beginning after December 15, 2017, and for interim periods within those fiscal years. An entity is to apply the change in income statement presentation retrospectively, and the change in capitalized benefit cost prospectively. We will adopt the requirements of the new standard in the first quarter of 2018 and do not currently expect adoption to have a material impact on our financial statements.

3. Investments

Available-for-Sale Investments

Marketable investments classified as available-for-sale consisted of the following (in millions):

As of September 30, 2017	**Amortized Cost**	**Gross Unrealized Losses**	**Fair Value**
U.S. government and agency securities	$ 481.0	$ (0.5)	$ 480.5
Total	$ 481.0	$ (0.5)	$ 480.5
Reported under the following captions on the consolidated balance sheet:			
Cash and cash equivalents			$ 28.1
Current marketable investments			115.5
Non-current marketable investments			336.9
Total			$ 480.5

We had no available-for-sale investments as of December 31, 2016.

The following table summarizes the contractual maturities of available-for-sale marketable investments (in millions):

	September 30, 2017	
	Amortized Cost	Fair Value
Due in less than one year	$ 143.7	$ 143.6
Due in one to two years	252.1	251.8
Due in three to five years	85.2	85.1
Total	$ 481.0	$ 480.5

Held-to-Maturity and Other Investments

Our current and long-term marketable investments included $29.3 million and $30.1 million of investments classified as held-to-maturity as of September 30, 2017 and December 31, 2016, respectively. Marketable investments classified as held-to-maturity are comprised of government-sponsored enterprises and corporate notes and bonds. We do not intend to sell these securities, nor is it more likely than not that we will be required to sell them prior to the recovery of their amortized cost basis. Furthermore, we do not believe that these securities expose us to undue market risk or counterparty credit risk. As such, we do not consider these securities to be other than temporarily impaired.

Investments Held at Cost

As of September 30, 2017, we maintain non-controlling equity investments in privately-held companies of approximately $178.9 million in the aggregate. These investments are initially held at cost because we do not have the ability to exercise

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significant influence over these companies and their fair values are not readily determinable. During the three- and nine-month periods ended September 30, 2017, we made payments of $30.2 million and $55.3 million, respectively, for investments held at cost. We include our investments held at cost within other non-current assets on our consolidated balance sheets. These investments are subject to a periodic impairment review and if they are deemed to be other-than-temporarily impaired, the investment is measured and recorded at fair value. During the three-and nine-month periods ended September 30, 2017, we recorded $3.1 million and $49.6 million, respectively, of impairment charges related to our cost method investments in privately-held companies.

Variable Interest Entity

In April 2017, we made a $7.5 million minority investment in a privately-held company. In addition to our investment, we entered into an exclusive license, development and commercialization agreement (the License Agreement) with this company. The License Agreement entitles us to certain control rights that require us to consolidate the balance sheet and results of operations of this company. The control rights relate to additional research and development funding that we may provide to this company over a period of six years. We are also entitled to representation on a joint development committee that approves the company s use of funding provided by us. In April 2017, we provided $5.2 million of financial support to the company. We have the right, at any time and for any reason, to cease our funding of this company s activities.

As of September 30, 2017, our consolidated balance sheet included $9.6 million of cash maintained by this company that can only be used to settle its obligations. Additionally, our consolidated balance sheets included an $8.8 million in-process research and development intangible asset, $3.4 million of goodwill and $8.3 million of preferred stock due to the consolidation of this company. The preferred stock is recorded in temporary equity on our consolidated balance sheets. During the quarter ended September 30, 2017, this company incurred a net loss of $1.5 million. This company s creditors have no recourse against our assets and general credit.

4. Fair Value Measurements

We account for certain assets and liabilities at fair value and classify these assets within a fair value hierarchy (Level 1, Level 2 or Level 3). Our other current assets and our current liabilities have fair values that approximate their carrying values. Assets and liabilities subject to fair value measurements are as follows (in millions):

	As of September 30, 2017			
	Level 1	**Level 2**	**Level 3**	**Balance**
Assets				
Money market funds(1)	$ 641.5	$	$	$ 641.5
Time deposits(2)		25.2		25.2
U.S. government and agency securities(2)		480.5		480.5
Corporate debt securities(2)		4.1		4.1
Total assets	$ 641.5	$ 509.8	$	$ 1,151.3
Liabilities				
Contingent consideration(3)			10.4	10.4
Total liabilities	$	$	$ 10.4	$ 10.4

	As of December 31, 2016			
	Level 1	Level 2	Level 3	Balance
Assets				
Money market funds(1)				