CELGENE CORP /DE/
Form 10-Q
October 29, 2008

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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549
FORM 10-Q

(Mark one)

þ **QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15 (d) OF THE SECURITIES EXCHANGE ACT OF 1934**
For the quarterly period ended September 30, 2008
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 0-16132
CELGENE CORPORATION
(Exact name of registrant as specified in its charter)

Delaware	**22-2711928**
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification Number)
86 Morris Avenue, Summit, NJ	**07901**
(Address of principal executive offices)	(Zip Code)

(908) 673-9000
(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 þ No o

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 þ Accelerated filer o Non-accelerated filer o Smaller reporting company o
(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 o No þ

At October 23, 2008, 458,188,433 shares of Common Stock, par value $.01 per share, were outstanding.

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CELGENE CORPORATION AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF OPERATIONS
(Unaudited)
(Dollars in thousands, except per share amounts)

	Three-Month Periods Ended September 30,		Nine-Month Periods Ended September 30,	
	2008	2007	2008	2007
Revenue:				
Net product sales	$ 567,017	$ 331,169	$ 1,541,556	$ 919,910
Collaborative agreements and other revenue	2,402	4,616	9,960	14,520
Royalty revenue	23,046	14,123	75,011	56,800
Total revenue	592,465	349,908	1,626,527	991,230
Expenses:				
Cost of goods sold (excluding amortization expense)	70,534	34,066	190,452	84,840
Research and development	160,911	130,841	462,650	301,341
Selling, general and administrative	168,607	94,736	485,345	310,669
Amortization of acquired intangible assets	32,833	2,290	77,842	6,755
Acquired in-process research and development			1,740,000	
Total expenses	432,885	261,933	2,956,289	703,605
Operating income (loss)	159,580	87,975	(1,329,762)	287,625
Other income and expense:				
Interest and investment income, net	19,678	28,296	69,281	79,447
Equity in losses of affiliated companies	2,338	1,106	8,761	3,338
Interest expense	512	2,614	3,968	7,913
Other income (expense), net	2,464	732	4,957	(3,345)
Income (loss) before income taxes	178,872	113,283	(1,268,253)	352,476
Income tax provision	42,058	74,450	116,138	201,364
Net income (loss)	$ 136,814	$ 38,833	$ (1,384,391)	$ 151,112
Net income (loss) per common share:				
Basic	$ 0.30	$ 0.10	$ (3.17)	$ 0.40
Diluted	$ 0.29	$ 0.09	$ (3.17)	$ 0.36

Weighted average shares:				
Basic	456,509	383,774	437,206	380,841
Diluted	468,891	432,817	437,206	431,208

See accompanying Notes to Unaudited Consolidated Financial Statements

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CELGENE CORPORATION AND SUBSIDIARIES
CONSOLIDATED BALANCE SHEETS
(Unaudited)
(Dollars in thousands, except per share amounts)

	September 30, 2008	December 31, 2007
Assets		
Current assets:		
Cash and cash equivalents	$ 1,517,120	$ 1,218,273
Marketable securities available for sale	937,050	1,520,645
Accounts receivable, net of allowances of $7,927 and $4,213 at September 30, 2008 and December 31, 2007, respectively	275,409	167,252
Inventory	90,344	49,076
Deferred income taxes	59,808	20,506
Other current assets	144,483	108,669
Total current assets	3,024,214	3,084,421
Property, plant and equipment, net	234,414	197,428
Investment in affiliated companies	18,245	14,422
Intangible assets, net	462,235	92,658
Goodwill	523,617	39,033
Other assets	94,699	183,322
Total assets	$ 4,357,424	$ 3,611,284
Liabilities and Stockholders Equity		
Current liabilities:		
Accounts payable	$ 54,938	$ 37,876
Accrued expenses	329,678	159,220
Income taxes payable	15,541	4,989
Convertible notes		196,555
Current portion of deferred revenue	1,365	7,666
Other current liabilities	47,488	26,625
Total current liabilities	449,010	432,931
Deferred revenue, net of current portion	3,095	60,303
Non-current income taxes payable	257,068	211,307
Other non-current liabilities	59,890	62,799
Total liabilities	769,063	767,340

Commitments and Contingencies

Stockholders Equity:

Preferred stock, $.01 par value per share, 5,000,000 shares authorized; none outstanding at September 30, 2008 and December 31, 2007, respectively		
Common stock, $.01 par value per share, 575,000,000 shares authorized; issued 462,213,553 and 407,150,694 shares at September 30, 2008 and December 31, 2007, respectively	4,622	4,072
Common stock in treasury, at cost; 4,092,612 and 4,026,116 shares at September 30, 2008 and December 31, 2007, respectively	(153,769)	(149,519)
Additional paid-in capital	5,035,170	2,780,849
(Accumulated deficit) retained earnings	(1,259,731)	124,660
Accumulated other comprehensive (loss) income	(37,931)	83,882
Total stockholders equity	3,588,361	2,843,944
Total liabilities and stockholders equity	$ 4,357,424	$ 3,611,284

See accompanying Notes to Unaudited Consolidated Financial Statements

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CELGENE CORPORATION AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF CASH FLOWS
(Unaudited)
(Dollars in thousands)

	Nine-Month Periods Ended September 30,	
	2008	**2007**
Cash flows from operating activities:		
Net (loss) income	$ (1,384,391)	$ 151,112
Adjustments to reconcile net (loss) income to net cash provided by operating activities:		
Depreciation of long-term assets	25,470	15,455
Amortization of intangible assets	78,138	7,047
Provision for accounts receivable allowances	6,642	6,353
Deferred income taxes	(9,770)	(4,334)
Acquired in-process research and development	1,740,000	
Share-based compensation expense	75,650	41,630
Equity in losses of affiliated companies	8,362	2,910
Share-based employee benefit plan expense	7,358	6,436
Other, net	12,434	1,526
Change in current assets and liabilities, excluding the effect of acquisition:		
Accounts receivable	(70,740)	(23,148)
Inventory	(5,799)	(34,480)
Other operating assets	(12,359)	(11,088)
Accounts payable and other operating liabilities	(20,708)	61,162
Income tax payable	26,088	93,085
Deferred revenue	(31)	(2,733)
Net cash provided by operating activities	476,344	310,933
Cash flows from investing activities:		
Proceeds from sales of marketable securities available for sale	981,502	1,462,836
Purchases of marketable securities available for sale	(471,699)	(2,362,302)
Payments for acquisition of business, net of cash acquired	(746,779)	
Capital expenditures	(53,635)	(38,447)
Investment in affiliated companies	(12,185)	(1,621)
Purchases of investment securities	(8,236)	(23,356)
Other	11,528	
Net cash used in investing activities	(299,504)	(962,890)
Cash flows from financing activities:		
Net proceeds from exercise of common stock options and warrants	106,932	136,033

Excess tax benefit from share-based compensation arrangements	59,459	112,614
Net cash provided by financing activities	166,391	248,647
Effect of currency rate changes on cash and cash equivalents	(44,384)	4,630
Net increase (decrease) in cash and cash equivalents	$ 298,847	$ (398,680)
Cash and cash equivalents at beginning of period	$ 1,218,273	$ 1,439,415
Cash and cash equivalents at end of period	$ 1,517,120	$ 1,040,735

See accompanying Notes to Unaudited Consolidated Financial Statements

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CELGENE CORPORATION AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF CASH FLOWS (Continued)
(Unaudited)
(Dollars in thousands)

	Nine-Month Periods Ended September 30,	
	2008	**2007**
Supplemental schedule of non-cash investing and financing activity:		
Change in net unrealized loss on marketable securities available for sale and cash flow hedges	$ 100,527	$ 43,988
Matured shares tendered in connection with stock option exercises	$ (4,250)	$ (6,457)
Conversion of convertible notes	$ 196,543	$ 130
Supplemental disclosure of cash flow information:		
Interest paid	$ 1,640	$ 5,250
Income taxes paid	$ 28,084	$

See accompanying Notes to Unaudited Consolidated Financial Statements

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1. Nature of Business and Summary of Significant Accounting Policies

Nature of Business and Basis of Presentation: Celgene Corporation and its subsidiaries (collectively Celgene or the Company) is a global biopharmaceutical company primarily engaged in the discovery, development and commercialization of innovative therapies designed to treat cancer and immune-inflammatory diseases. On March 7, 2008, the Company acquired all of the outstanding common stock and stock options of Pharmion Corporation, or Pharmion, which prior to the acquisition was a global biopharmaceutical company that acquired, developed and commercialized innovative products for the treatment of hematology and oncology patients, for $2.67 billion in a combination of cash and Celgene common stock. The Company s commercial stage products include REVLIMID®, THALOMID® / Thalidomide, VIDAZA®, ALKERAN® and FOCALIN®. FOCALIN® is sold exclusively to Novartis Pharma AG, or Novartis. The Company also derives revenues from a licensing agreement with Novartis, which entitles it to royalties on FOCALIN XR® and the entire RITALIN® family of drugs, and sales of bio-therapeutic products and services through the Company s Cellular Therapeutics subsidiary.

The accompanying unaudited consolidated financial statements have been prepared from the books and records of the Company pursuant to U.S. generally accepted accounting principles for interim information and the rules and regulations of the Securities and Exchange Commission for reporting on Form 10-Q. Pursuant to such rules and regulations, certain information and footnote disclosures normally included in complete annual financial statements have been condensed or omitted. The consolidated financial statements include the accounts of Celgene Corporation and its subsidiaries. All intercompany transactions and balances have been eliminated. Investments in limited partnerships and interests in which the Company has an equity interest of 50% or less and does not otherwise have a controlling financial interest are accounted for by either the equity or cost method. Certain immaterial reclassifications have been made to the prior period consolidated financial statements in order to conform to the current period presentation. The interim consolidated financial statements should be read in conjunction with the consolidated financial statements and notes thereto included in the Company s Annual Report on Form 10-K for the year ended December 31, 2007.

The preparation of the consolidated financial statements requires management to make estimates and assumptions that affect reported amounts and disclosures. Actual results could differ from those estimates. The Company is subject to certain risks and uncertainties related to product development, regulatory approval, market acceptance, scope of patent and proprietary rights, intense competition, rapid technological change and product liability.

Interim results may not be indicative of the results that may be expected for the full year. In the opinion of management, these financial statements include all normal and recurring adjustments considered necessary for a fair presentation of these interim consolidated financial statements.

Recent Accounting Principles: In September 2006, the Financial Accounting Standards Board, or FASB, issued Statement of Financial Accounting Standards, or SFAS, No. 157, Fair Value Measurements, or SFAS 157, which establishes a framework for measuring fair value and expands disclosures about fair value measurements. The FASB partially deferred the effective date of SFAS 157 for non-financial assets and liabilities that are recognized or disclosed at fair value in the financial statements on a nonrecurring basis to fiscal years beginning after November 15, 2008. The effective date for financial assets and liabilities that are recognized on a recurring basis was January 1, 2008. The Company has determined that its adoption of SFAS 157 on January 1, 2008 for financial assets and liabilities did not have a material impact on its consolidated financial statements. See Note 6 for expanded disclosures required by SFAS 157. The Company is currently evaluating the impact that the adoption of SFAS 157 related to non-financial assets will have, if any, on its consolidated financial statements.

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In February 2007, the FASB issued SFAS No. 159, The Fair Value Option for Financial Assets and Financial Liabilities, or SFAS 159, which provides companies with an option to report selected financial assets and liabilities at fair value. SFAS 159 establishes presentation and disclosure requirements designed to facilitate comparisons between companies that choose different measurement attributes for similar types of assets and liabilities and highlights the effect of a company s choice to use fair value on its earnings. It also requires a company to display the fair value of those assets and liabilities for which it has chosen to use fair value on the face of the balance sheet. SFAS 159 was effective for the Company beginning January 1, 2008 and did not have a material impact on its consolidated financial statements.

In June 2007, the FASB ratified Emerging Issues Task Force, or EITF, Issue No. 07-3, Accounting for Non-Refundable Advance Payments for Goods or Services to be Used in Future Research and Development Activities, or EITF 07-3, which provides that non-refundable advance payments for future research and development activities should be deferred and capitalized until the related goods are delivered or the related services are performed. EITF 07-3 was effective for the Company on a prospective basis beginning January 1, 2008 and did not have a material impact on its consolidated financial statements.

In December 2007, the FASB ratified EITF Issue No. 07-1, Accounting for Collaborative Arrangements Related to the Development and Commercialization of Intellectual Property, or EITF 07-1, which provides guidance on how the parties to a collaborative agreement should account for costs incurred and revenue generated on sales to third parties, how sharing payments pursuant to a collaboration agreement should be presented in the income statement and certain related disclosure requirements. EITF 07-1 will be effective for the Company beginning January 1, 2009 on a retrospective basis. The Company is currently evaluating the impact that the adoption of EITF 07-1 will have, if any, on its consolidated financial statements.

In December 2007, the FASB issued SFAS No. 141R, Business Combinations, or SFAS 141R, which replaces FASB Statement No. 141, Business Combinations, and requires an acquirer to recognize the assets acquired, the liabilities assumed and any noncontrolling interest in the acquiree at the acquisition date, measured at their fair values as of that date, with limited exceptions specified in the Statement. It is effective prospectively to 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, 2008.

In December 2007, the FASB issued SFAS No. 160, Noncontrolling Interests in Consolidated Financial Statements, an Amendment of ARB No. 51, or SFAS 160, which changes the accounting for and reporting of noncontrolling interests (formerly known as minority interests) in consolidated financial statements. SFAS 160 is effective January 1, 2009. Upon implementation, prior periods will be recast for the changes required by SFAS 160. The Company is currently evaluating the impact that the adoption of SFAS 160 will have, if any, on its consolidated financial statements.

In March 2008, the FASB issued SFAS No. 161, Disclosures about Derivative Instruments and Hedging Activities, or SFAS 161, which is intended to improve financial reporting about derivative instruments and hedging activities by requiring enhanced disclosures to enable investors to better understand their effects on an entity s financial position, financial performance and cash flows. It is effective for financial statements issued for fiscal years and interim periods beginning after November 15, 2008, with early adoption encouraged. The Company is currently evaluating the impact that the adoption of SFAS 161 will have, if any, on its consolidated financial statements.

In May 2008, the FASB issued FASB Staff Position, or FSP, No. APB 14-1, Accounting for Convertible Debt Instruments That May Be Settled in Cash upon Conversion (Including Partial Cash Settlement), or FSP APB 14-1, which requires separate accounting for the debt and equity components of convertible debt issuances that have a cash settlement feature permitting settlement partially or fully in cash upon conversion.

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A component of such debt issuances representative of the approximate fair value of the conversion feature at inception should be bifurcated and recorded to equity, with the resulting debt discount amortized to interest expense in a manner that reflects the issuer s nonconvertible, unsecured debt borrowing rate. The requirements for separate accounting must be applied retrospectively to previously issued convertible debt issuances as well as prospectively to newly issued convertible debt issuances, negatively affecting both net income and earnings per share, in financial statements issued for fiscal years beginning after December 15, 2008. Since the Company s past convertible debt issuance did not include a cash settlement feature, it does not expect the adoption of FSP APB 14-1 will have any impact on its consolidated financial statements.

In June 2008, the FASB issued FSP EITF No. 03-6-1, Determining Whether Instruments Granted in Share-Based Payment Transactions Are Participating Securities, or FSP EITF 03-6-1. The FSP addresses whether instruments granted in share-based payment transactions are participating securities prior to vesting and therefore need to be included in the earnings allocation in calculating earnings per share under the two-class method described in SFAS No. 128, Earnings per Share. The FSP requires companies to treat unvested share-based payment awards that have non-forfeitable rights to dividends or dividend equivalents as a separate class of securities in calculating earnings per share. The FSP is effective for fiscal years beginning after December 15, 2008; earlier application is not permitted. Since the Company s past share-based payment awards did not include non-forfeitable rights to dividends or dividend equivalents, it does not expect the adoption of FSP EITF 03-6-1 will have any impact on its consolidated financial statements.

Significant Accounting Policies: The Company s significant accounting policies are described in Note 1 of the Notes to the Consolidated Financial Statements included in its Annual Report on Form 10-K for the year ended December 31, 2007. In addition, the following additional significant accounting policy is now applicable:

Derivatives and Hedging Activities: SFAS No. 133, Accounting for Derivative Instruments and Hedging Activities, or SFAS 133, as amended, requires that all derivative instruments be recognized on the balance sheet at their fair value. Changes in the fair value of derivative instruments are recorded each period in current earnings or other comprehensive income (loss), depending on whether a derivative instrument is designated as part of a hedging transaction and, if it is, the type of hedging transaction. For a derivative to qualify as a hedge at inception and throughout the hedged period, the Company formally documents the nature and relationships between the hedging instruments and hedged item. The Company assesses, both at inception and on an on-going basis, whether the derivative instruments that are used in cash flow hedging transactions are highly effective in offsetting the changes in cash flows of hedged items. The Company assesses hedge ineffectiveness on a quarterly basis and records the gain or loss related to the ineffective portion of derivative instruments, if any, to current earnings. If the Company determines that a forecasted transaction is no longer probable of occurring, it discontinues hedge accounting and any related unrealized gain or loss on the derivative instrument is recognized in current earnings. The Company uses derivative instruments, including those not designated as part of a hedging transaction, to manage its exposure to movements in foreign exchange rates. The use of these derivative instruments modifies the exposure of these risks with the intent to reduce the risk or cost to the Company. The Company does not use derivative instruments for speculative trading purposes and is not a party to leveraged derivatives.

2. Acquisition of Pharmion Corporation

On March 7, 2008, Celgene acquired all of the outstanding common stock and stock options of Pharmion in a transaction accounted for under the purchase method of accounting for business combinations. Under the purchase method of accounting, the assets acquired and liabilities assumed of Pharmion are recorded as of the acquisition date, at their respective fair values, and consolidated with those of Celgene. The reported consolidated financial condition and results of operations of Celgene after completion of the acquisition reflect these fair values. The operating results of Pharmion are included in the Company s consolidated financial statements from the date of acquisition.

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Celgene paid a total purchase price of $2.761 billion to acquire all of the outstanding Pharmion common shares and stock options. Each Pharmion share of common stock (other than shares owned by Celgene or its wholly owned subsidiaries, held in Pharmion s treasury or to which appraisal rights were perfected) were converted into the right to receive (i) 0.8367 shares of common stock of Celgene and (ii) $25.00 in cash. The combination of cash and Celgene stock paid to Pharmion stockholders consisted of $921.0 million in cash and approximately 30.8 million shares of Celgene common stock valued at $1.749 billion. The purchase price included acquisition-related costs of $26.2 million, the fair value of vested Celgene stock options issued of $44.9 million and the cost of Celgene s investment in Pharmion common shares prior to the acquisition.

Prior to the acquisition, Pharmion was a global biopharmaceutical company that acquired, developed and commercialized innovative products for the treatment of hematology and oncology patients. Celgene acquired Pharmion to enhance its portfolio of therapies for patients with life-threatening illnesses worldwide with the addition of Pharmion s marketed products, and several products in development for the treatment of hematological and solid tumor cancers. By combining this new product portfolio with Celgene s existing operational and financial capabilities, Celgene expects to enlarge its global market share through increased product offerings and expanded clinical, regulatory and commercial capabilities.

(Amounts in thousands)

Purchase Price Summary:

Stock issued at fair value	$ 1,749,222
Cash paid	920,805
Acquisition-related costs	26,187
Fully vested stock options issued	44,924
Pharmion shares previously owned	20,212
Total purchase price paid	$ 2,761,350

The acquisition was accounted for using the purchase method of accounting for business combinations and the preliminary purchase price allocation resulted in the following amounts being allocated to the assets acquired and liabilities assumed at the acquisition date based upon their respective fair values.

(Amounts in thousands)	March 7, 2008
Current assets	$ 340,415
Property, plant and equipment	8,404
Developed product rights	510,986
In-process research and development	1,740,000
Other noncurrent assets	304
Assets acquired	2,600,109
Restructuring	(69,000)
Net deferred taxes	(128,352)
Liabilities assumed	(141,748)
Net assets acquired	2,261,009
Goodwill	500,341
Acquisition cost	$ 2,761,350

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The fair value of the acquired identifiable intangible assets consists primarily of developed product rights for the following marketed products at date of acquisition: VIDAZA® IV in the U.S. market, Thalidomide Pharmion in certain foreign markets and other minor commercialized products. The weighted average amortization period for these assets, in total, is 6.5 years. The weighted average amortization period for compassionate use rights is 1.2 years, while the weighted average amortization period for the developed product rights is 7.1 years.

In-process research and development, or IPR&D, represents compounds under development by Pharmion at the date of acquisition that had not yet achieved regulatory approval for marketing in certain markets or had not yet been completed and have no alternative future use. The $1.74 billion estimated fair value of these intangibles was derived using the multi-period excess-earnings method, a form of the income approach. The IPR&D primarily related to development and approval initiatives for VIDAZA® IV in the E.U. market, the oral form of azacitidine in the U.S. and E.U. markets and Thalidomide Pharmion® in the E.U. market. The projected cash flows for valuation purposes were based on key assumptions such as estimates of revenues and operating profits related to the programs considering their stages of development; the time and resources needed to complete the regulatory approval process for the products; and the life of the potential commercialized products and associated risks, including the inherent difficulties and uncertainties in obtaining regulatory approvals.

For VIDAZA® IV in the E.U. market, the related future net cash flows were estimated using a risk-adjusted discount rate of 10.0% and an anticipated regulatory approval date in late 2008 with market exclusivity rights expected to continue through 2019. For the oral form of azacitidine in the United States and European Union, the future net cash flows were estimated using a risk-adjusted discount rate of 11.0% for each market. The anticipated regulatory approval in the European Union was assumed for 2013 with exclusivity continuing through 2023, and the anticipated regulatory approval in the United States was assumed for 2013 with exclusivity continuing through 2018. For Thalidomide Pharmion® in the E.U. market, the future net cash flows were estimated using a risk-adjusted discount rate of 9.5% and an anticipated regulatory approval date in 2008 with exclusivity continuing through 2018.

In accordance with FASB Interpretation No. 4, Applicability of FASB Statement No. 2 to Business Combinations Accounted for by the Purchase Method, the purchase price allocated to IPR&D intangible assets has been expensed to income immediately subsequent to the acquisition because the compounds do not have any alternative future use. This charge is not deductible for tax purposes.

The excess of purchase price over the fair value amounts assigned to the assets acquired and liabilities assumed represents the goodwill amount resulting from the acquisition. The amount allocated to goodwill is preliminary and subject to change, depending on the results of the final purchase price allocation. The Company does not expect any portion of this goodwill to be deductible for tax purposes. The goodwill attributable to the Company s acquisition of Pharmion has been recorded as a noncurrent asset in the Company s Consolidated Balance Sheet and will not be amortized, but is subject to