

MENTOR CORP /MN/  
Form 10-Q  
February 06, 2008

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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 December 28, 2007**

**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 No. 001-31744**

**MENTOR CORPORATION**

(Exact Name of Registrant as Specified in its Charter)

Minnesota

(State or other jurisdiction of  
incorporation or organization)

41-0950791

(IRS Employer Identification No.)

**201 Mentor Drive, Santa Barbara, California 93111**

(Address of principal executive offices) (Zip Code)

**(805) 879-6000**

(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 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 ☒

As of February 1, 2008 there were approximately 33,737,437 Common Shares, \$.10 par value per share, outstanding.

**MENTOR CORPORATION  
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Mentor Corporation  
Consolidated Balance Sheets  
(Unaudited)

| (in thousands)              | <b>December 31,<br/>2007</b> | March 31,<br>2007 |
|-----------------------------|------------------------------|-------------------|
| <b>Assets</b>               |                              |                   |
| Current assets:             |                              |                   |
| Cash and cash equivalents   | \$ 74,961                    | \$ 371,525        |
| Marketable securities       | 31,686                       | 116,215           |
| Accounts receivable, net    | 72,385                       | 65,419            |
| Inventories                 | 46,697                       | 38,073            |
| Deferred income taxes       | 26,353                       | 25,892            |
| Prepaid income taxes        | 9,789                        | 13,495            |
| Prepaid expenses and other  | 7,994                        | 6,761             |
| Total current assets        | 269,865                      | 637,380           |
| Property and equipment, net | 48,610                       | 34,683            |
| Intangible assets, net      | 32,067                       | 15,963            |
| Goodwill, net               | 46,197                       | 12,644            |
| Other assets                | 6,681                        | 9,098             |
| Total assets                | \$ 403,420                   | \$ 709,768        |

See notes to consolidated financial statements.

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Mentor Corporation  
Consolidated Balance Sheets  
(Unaudited)

| (in thousands, except share data)                           | December 31,<br>2007 | March 31,<br>2007 |
|-------------------------------------------------------------|----------------------|-------------------|
| <b>Liabilities and shareholders' equity</b>                 |                      |                   |
| Current liabilities:                                        |                      |                   |
| Accounts payable and accrued liabilities                    | \$ 38,709            | \$ 32,147         |
| Sales returns                                               | 14,881               | 18,590            |
| Accrued compensation                                        | 17,917               | 14,022            |
| Deferred revenue                                            | 12,443               | 11,863            |
| Dividends payable                                           | 6,745                | 8,481             |
| Product liability reserves                                  | 7,322                | 6,555             |
| Short-term debt                                             | 1,076                |                   |
| Warranty reserve                                            | 2,393                | 2,989             |
| Interest payable                                            | 2,063                | 1,031             |
| Accrued royalties                                           | 250                  | 230               |
| Other                                                       | 14,108               | 16,823            |
| Total current liabilities                                   | 117,907              | 112,731           |
| Long-term accrued liabilities                               | 15,606               | 12,169            |
| Convertible subordinated notes                              | 150,000              | 150,000           |
| Other long-term debt                                        | 2,735                |                   |
| Commitments and contingencies                               |                      |                   |
| Shareholders' equity:                                       |                      |                   |
| Common stock, \$.10 par value:                              |                      |                   |
| Authorized - 150,000,000 shares; issued and outstanding     |                      |                   |
| 33,725,599 shares at December 31, 2007;                     |                      |                   |
| 42,400,483 shares at March 31, 2007;                        | 3,373                | 4,240             |
| Preferred stock, \$.01 par value:                           |                      |                   |
| Authorized - 25,000,000 shares; none issued and outstanding |                      |                   |
| Accumulated other comprehensive income                      | 22,630               | 11,342            |
| Retained earnings                                           | 91,169               | 419,286           |
| Total shareholders' equity                                  | 117,172              | 434,868           |
| Total liabilities and shareholders' equity                  | \$ 403,420           | \$ 709,768        |

See notes to consolidated financial statements.

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Mentor Corporation  
Consolidated Statements of Income  
Three Months Ended December 31, 2007 and 2006  
(Unaudited)

| (in thousands, except per share data)                                                 | <b>2007</b>      | 2006      |
|---------------------------------------------------------------------------------------|------------------|-----------|
| Net sales                                                                             | <b>\$ 92,860</b> | \$ 75,309 |
| Cost of sales                                                                         | <b>26,138</b>    | 18,925    |
| Gross profit                                                                          | <b>66,722</b>    | 56,384    |
| Selling, general, and administrative                                                  | <b>38,884</b>    | 32,356    |
| Research and development                                                              | <b>9,690</b>     | 7,780     |
|                                                                                       | <b>48,574</b>    | 40,136    |
| Operating income from continuing operations                                           | <b>18,148</b>    | 16,248    |
| Interest expense                                                                      | <b>(1,249)</b>   | (1,426)   |
| Interest income                                                                       | <b>1,071</b>     | 6,346     |
| Other income (expense), net                                                           | <b>(452)</b>     | (281)     |
| Income from continuing operations before income taxes                                 | <b>17,518</b>    | 20,887    |
| Income taxes                                                                          | <b>5,406</b>     | 6,137     |
| Income from continuing operations                                                     | <b>12,112</b>    | 14,750    |
| Loss from discontinued operations, net of tax benefit of \$94 and \$596, respectively | <b>(170)</b>     | (1,102)   |
| Loss on sale of discontinued operations, net of tax benefit of \$13                   |                  | (20)      |
| Net income                                                                            | <b>\$ 11,942</b> | \$ 13,628 |
| Basic earnings (loss) per share                                                       |                  |           |
| Continuing operations                                                                 | <b>\$ 0.36</b>   | \$ 0.35   |
| Discontinued operations                                                               | <b>(0.01)</b>    | (0.03)    |
| Basic earnings per share                                                              | <b>0.36</b>      | 0.33      |
| Diluted earnings (loss) per share                                                     |                  |           |
| Continuing operations                                                                 | <b>\$ 0.32</b>   | \$ 0.32   |
| Discontinued operations                                                               | <b>(0.01)</b>    | (0.03)    |
| Diluted earnings per share                                                            | <b>0.32</b>      | 0.29      |
| Dividends per share                                                                   | <b>\$ 0.20</b>   | \$ 0.18   |

|                                                 |               |        |
|-------------------------------------------------|---------------|--------|
| Weighted average shares outstanding             |               |        |
| Basic                                           | <b>33,602</b> | 41,916 |
| Diluted                                         | <b>39,848</b> | 49,144 |
| See notes to consolidated financial statements. |               |        |

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Mentor Corporation  
Consolidated Statements of Income  
Nine Months Ended December 31, 2007 and 2006  
(Unaudited)

|                                                                                                               |                   |            |
|---------------------------------------------------------------------------------------------------------------|-------------------|------------|
| (in thousands, except per share data)                                                                         | <b>2007</b>       | 2006       |
| Net sales                                                                                                     | <b>\$ 273,814</b> | \$ 221,654 |
| Cost of sales                                                                                                 | <b>72,842</b>     | 59,491     |
| Gross profit                                                                                                  | <b>200,972</b>    | 162,163    |
| Selling, general, and administrative                                                                          | <b>108,326</b>    | 90,792     |
| Research and development                                                                                      | <b>32,207</b>     | 24,654     |
|                                                                                                               | <b>140,533</b>    | 115,446    |
| Operating income from continuing operations                                                                   | <b>60,439</b>     | 46,717     |
| Interest expense                                                                                              | <b>(4,160)</b>    | (4,707)    |
| Interest income                                                                                               | <b>7,218</b>      | 16,233     |
| Other income (expense), net                                                                                   | <b>(1,421)</b>    | 494        |
| Income from continuing operations before income taxes                                                         | <b>62,076</b>     | 58,737     |
| Income taxes                                                                                                  | <b>18,191</b>     | 17,490     |
| Income from continuing operations                                                                             | <b>43,885</b>     | 41,247     |
| (Loss) income from discontinued operations, net of tax (benefit) expense of (\$152) and \$2,760, respectively | <b>(275)</b>      | 1,342      |
| (Loss) gain on sale of discontinued operations, net of taxes of (\$5) and \$138,341, respectively             | <b>(12)</b>       | 222,162    |
| Net income                                                                                                    | <b>\$ 43,598</b>  | \$ 264,751 |
| Basic earnings (loss) per share                                                                               |                   |            |
| Continuing operations                                                                                         | <b>\$ 1.22</b>    | \$ 0.98    |
| Discontinued operations                                                                                       | <b>(0.01)</b>     | 5.33       |
| Basic earnings per share                                                                                      | <b>1.21</b>       | 6.32       |
| Diluted earnings (loss) per share                                                                             |                   |            |
| Continuing operations                                                                                         | <b>\$ 1.09</b>    | \$ 0.89    |
| Discontinued operations                                                                                       | <b>(0.01)</b>     | 4.57       |
| Diluted earnings per share                                                                                    | <b>1.08</b>       | 5.46       |

|                                                 |    |               |    |        |
|-------------------------------------------------|----|---------------|----|--------|
| Dividends per share                             | \$ | <b>0.60</b>   | \$ | 0.54   |
| Weighted average shares outstanding             |    |               |    |        |
| Basic                                           |    | <b>36,033</b> |    | 41,898 |
| Diluted                                         |    | <b>42,499</b> |    | 48,948 |
| See notes to consolidated financial statements. |    |               |    |        |

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Mentor Corporation  
Consolidated Statements of Cash Flows  
Nine Months Ended December 31, 2007 and 2006  
(Unaudited)

| (in thousands)                                                          | 2007      | 2006      |
|-------------------------------------------------------------------------|-----------|-----------|
| <b>Operating Activities:</b>                                            |           |           |
| Income from continuing operations                                       | \$ 43,885 | \$ 41,247 |
| Adjustments to derive cash flows from continuing operating activities:  |           |           |
| Depreciation                                                            | 6,024     | 5,640     |
| Amortization                                                            | 3,734     | 1,889     |
| Deferred income taxes                                                   | (2,527)   | 3,477     |
| Non-cash compensation                                                   | 9,128     | 8,203     |
| Tax benefit from exercise of stock options                              | 2,054     | 8,465     |
| Excess tax benefits from equity compensation                            | (2,256)   |           |
| Loss on sale of assets                                                  | 29        | 162       |
| Loss (gain) on long-term marketable securities, net                     | (28)      | 132       |
| Cash provided by (used in) changes in operating assets and liabilities: |           |           |
| Accounts receivable                                                     | (1,151)   | (2,351)   |
| Inventories                                                             | 3,360     | (725)     |
| Other current assets                                                    | 2,869     | 285       |
| Accounts payable and accrued liabilities                                | 4,503     | 3,933     |
| Income taxes payable                                                    |           | (5,137)   |
| Net cash provided by continuing operating activities                    | 69,624    | 65,220    |
| Net cash used for discontinued operating activities                     | (287)     | (95,111)  |
| Net cash provided by (used for) operating activities                    | 69,337    | (29,891)  |
| <b>Investing Activities:</b>                                            |           |           |
| Purchases of property and equipment                                     | (13,683)  | (4,435)   |
| Purchases of intangibles                                                |           | (3,505)   |
| Purchases of marketable securities                                      | (44,150)  | (65,609)  |
| Sales of marketable securities                                          | 128,294   | 53,666    |
| Acquisition, net of cash acquired                                       | (53,437)  |           |
| Proceeds from the sale of the urology business                          |           | 458,066   |
| Other, net                                                              |           | 5         |
| Net cash provided by continuing investing activities                    | 17,024    | 438,188   |
| Net cash used for discontinued investing activities                     |           | (50)      |
| Net cash provided by investing activities                               | 17,024    | 438,138   |
| <b>Financing Activities:</b>                                            |           |           |
| Repurchase of common stock                                              | (367,701) | (88,198)  |
| Proceeds from exercise of stock options and ESPP                        | 4,982     | 22,194    |
| Excess tax benefits from equity compensation                            | 2,256     |           |

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|                                                              |                  |            |
|--------------------------------------------------------------|------------------|------------|
| Dividends paid                                               | <b>(22,780)</b>  | (22,842)   |
| Repayments under line of credit agreements                   | <b>(420)</b>     | (14,000)   |
| Net cash used for continuing financing activities            | <b>(383,663)</b> | (102,846)  |
| Net cash used for financing activities                       | <b>(383,663)</b> | (102,846)  |
| Effect of currency exchange rates of continuing operations   | <b>738</b>       | 413        |
| Effect of currency exchange rates of discontinued operations |                  | (120)      |
| (Decrease) increase in cash and cash equivalents             | <b>(296,564)</b> | 305,694    |
| Cash and cash equivalents at beginning of year               | <b>371,525</b>   | 98,713     |
| Cash and cash equivalents at end of period                   | <b>\$ 74,961</b> | \$ 404,407 |

See notes to consolidated financial statements.

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**MENTOR CORPORATION**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**  
**December 31, 2007**

**Note A Business Activity**

Mentor Corporation was incorporated in April 1969. Unless the context indicates otherwise, when we refer to Mentor, we, us, our, or the Company in these notes, we are referring to Mentor Corporation and its subsidiaries on a consolidated basis. Presently, the Company develops, manufactures, licenses and markets a range of products serving the aesthetic and general surgery markets, including plastic and reconstructive surgery.

Historically, the Company's products were categorized into three primary segments:

Aesthetic and General Surgery This segment includes surgically implantable breast implants for plastic and reconstructive surgery, capital equipment and consumables used for soft tissue aspiration or body contouring (liposuction), and facial rejuvenation products including various types of products for skin restoration.

Surgical Urology This segment includes surgically implantable prostheses for the treatment of impotence, surgically implantable incontinence products, urinary care products, and brachytherapy seeds for the treatment of prostate cancer.

Clinical and Consumer Healthcare This segment includes catheters and other products for the management of urinary incontinence and retention.

On June 2, 2006, the Company completed a transaction for the sale of the Surgical Urology and the Clinical and Consumer Healthcare segments (together referred to as the Urology Business) to Coloplast A/S (Coloplast). Please see Note P and Note R to the consolidated financial statements for further information.

**Note B Summary of Significant Accounting Policies**

The consolidated financial statements include the accounts of the Company and all of its subsidiaries in which a controlling interest is maintained. All intercompany accounts and transactions have been eliminated.

**Basis of Presentation**

The financial information for the three and nine months ended December 31, 2007 and 2006 is unaudited, but in the opinion of management includes all adjustments (consisting only of normally recurring accruals, unless otherwise indicated) that the Company considers necessary for a fair presentation of the results of operations for this period. Interim results are not necessarily indicative of results for the full fiscal year. The balance sheet at March 31, 2007 has been derived from the audited financial statements as of that date, but does not include all of the information and notes required by accounting principles generally accepted in the United States for complete financial statements.

**Use of Estimates**

Financial statements prepared in accordance with accounting principles generally accepted in the United States require management to make estimates and judgments that affect amounts and disclosures reported in the financial statements. Actual results could differ from those estimates.

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**Revenue Recognition**

The Company recognizes product revenue, net of discounts, returns, rebates, and taxes collected from customers in accordance with Statement of Financial Accounting Standards ( SFAS ) No. 48, Revenue Recognition When the Right of Return Exists, and Staff Accounting Bulletin ( SAB ) No. 104, Revenue Recognition. As required by these standards, revenue is recorded when persuasive evidence of a sales arrangement exists, delivery has occurred, the buyer's price is fixed or determinable, contractual obligations have been satisfied, and collectibility is reasonably assured. These requirements are met, and sales and related cost of sales are recognized upon the shipment of products, or in the case of consignment inventories, upon the notification of usage by the customer. The Company records estimated reductions to revenue for customer programs and other volume-based incentives. Should the actual level of customer participation in these programs differ from those estimated, additional adjustments to revenue may be required. The Company also allows credit for products returned within its policy terms. The Company records an allowance for estimated returns at the time of sale based on historical experience, recent gross sales levels, any notification of pending returns and other relevant information. Should the actual returns differ from those estimated, additional adjustments to revenue and cost of sales may be required.

The Company has current and long term deferred revenue, which include funds received in connection with purchases of the Company's Enhanced Advantage Limited Warranty program for breast implants. The fees received in connection with the Enhanced Advantage Limited Warranty are deferred and recognized evenly over the life of the warranty term.

**Warranty Reserves**

The Company offers limited warranty coverage on some of its products (see Note G for details). While the Company engages in extensive product quality programs and processes, including actively monitoring and evaluating the quality of our component and raw material suppliers, the limited warranty obligation is affected by reported rates of warranty claims and levels of financial assistance specified in the limited warranties. Should actual patient claim rates reported differ from the Company's estimates and/or changes in claim rates result in revised actuarial assumptions, additional adjustments to the estimated limited warranty liability may be required. These adjustments would be included in cost of sales. The Company's limited warranty programs may be modified in the future in response to the competitive market environment. Such changes may impact the amount and timing of the associated revenue and expense for these programs.

**Product Liability Reserves**

The Company has product liability reserves for product-related claims to the extent those claims may result in litigation expenses, settlements or judgments within the Company's self-insured retention limits. The Company has also established additional reserves, through its wholly-owned captive insurance company, for estimated liabilities for product-related claims based on actuarially determined estimated liabilities taking into account its excess insurance coverages. The actuarial valuations are based on historical information and certain assumptions about future events. Product liability costs are recorded in selling, general and administrative expenses as they are directly under the control of its General Counsel and other general and administrative staff and are directly impacted by the Company's overall risk management strategy; or in the case of products related to discontinued operations, including urology products or ophthalmic products, product liability costs are recorded in discontinued operations. Should actual product liability experience differ from the estimates and assumptions used to develop these reserves, subsequent changes in reserves will be recorded in selling, general and administrative expenses, and may affect the Company's operating results in future periods.

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**Employee Stock-Based Payments**

The Company has employee compensation plans under which various types of stock-based instruments have been granted. These instruments principally include stock options, restricted stock and performance units. As of December 31, 2007, these plans have instruments outstanding that might require the issuance of 4.9 million shares of common stock to its employees and directors. Stock-based awards under the Company's employee compensation plans are made with authorized, but unissued, shares reserved for this purpose.

Effective April 1, 2006, the Company adopted the fair value recognition provisions of SFAS No. 123(R), "Share-Based Payment". In addition to recognizing compensation expense related to restricted stock and performance units, SFAS No. 123(R) also requires the Company to recognize compensation expense related to the estimated fair value of stock options and other equity based compensation instruments. The Company adopted SFAS No. 123(R) using the modified-prospective-transition method. Under that transition method, compensation expense recognized subsequent to adoption includes: (a) compensation cost for all share-based payments granted prior to, but not yet vested, as of April 1, 2006, based on the values estimated in accordance with the original provisions of SFAS No. 123, and (b) compensation cost for all share-based payments granted subsequent to April 1, 2006 based on the grant-date fair values estimated in accordance with the provisions of SFAS No. 123(R).

**Effects of Recent Accounting Pronouncements**

In September 2006, the Financial Accounting Standards Board (FASB) issued SFAS No. 157, "Fair Value Measurements". This statement defines fair value, establishes a framework for measuring fair value in generally accepted accounting principles (GAAP), and expands disclosure about fair value measurements. This statement applies under other accounting pronouncements that require or permit fair value measurements. Accordingly, this statement does not require any new fair value measurements. This statement is effective for fiscal years beginning after November 15, 2007, and interim periods within those fiscal years. The Company is currently evaluating the requirements of SFAS No. 157 and has not yet determined the impact on the Company's consolidated financial statements.

In July 2006, the FASB issued FASB Interpretation No. 48, "Accounting for Uncertainty in Income Taxes" an interpretation of FASB Statement No. 109 (FIN 48), which became effective for the Company as of April 1, 2007. FIN 48 clarifies the accounting for uncertainty in income taxes by prescribing rules for recognition, measurement and classification in the financial statements of tax positions taken or expected to be taken in a tax return.

For tax benefits to be recognized under FIN 48, a tax position must be more-likely-than-not to be sustained upon examination by taxing authorities. The amount recognized is measured as the largest amount of benefit that is greater than fifty percent likely of being realized upon ultimate settlement. As of April 1, 2007, the gross amount of the Company's liabilities for unrecognized tax benefits (UTBs) was approximately \$4.6 million and accrued interest related to these UTBs totaled approximately \$0.6 million. Virtually all of this balance of \$4.6 million of UTBs (net of the federal benefit on state taxes), if recognized, would affect the Company's annual effective tax rate. The cumulative effect of applying the recognition and measurement provisions upon adoption of FIN 48 was not material.

FIN 48 also provides guidance on the balance sheet classification of liabilities for UTBs as either current or non-current depending on the expected timing of payments. Upon adoption of FIN 48, the Company reclassified approximately \$1.4 million and \$3.8 million of UTBs and related accrued interest from prepaid income taxes payable to current and non-current liabilities, respectively.

As of adoption of FIN 48, the Company believed that it was reasonably possible that our liabilities for UTBs may decrease by \$0.6 million to \$1.6 million within the succeeding twelve months due to potential tax settlements and resolution of tax issues and examinations.

Interest and penalties related to UTBs are classified as a component of our provision for income taxes.

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In February 2007, FASB issued SFAS No. 159, The Fair Value Option for Financial Assets and Liabilities including an amendment of FASB Statement No. 115 ( SFAS 159 ). SFAS 159 permits entities to choose to measure certain financial assets and liabilities at fair value. Unrealized gains and losses, arising subsequent to adoption, are reported in earnings. The Company is required to adopt SFAS 159 for the first fiscal year beginning after November 15, 2007. The Company is currently evaluating if it will elect the fair value option for any of its eligible financial instruments and other items.

In June 2007, FASB ratified Emerging Issues Task Force Issue No. 07-3, Accounting for Nonrefundable Advance Payments for Goods or Services Received for Use in Future Research and Development Activities ( EITF No. 07-3 ). EITF No. 07-3 requires that nonrefundable advance payments for goods and services that will be used or rendered in future research and development activities pursuant to executory contractual arrangements should be deferred and recognized as an expense in the period that the related goods are delivered or services are performed. The Company will adopt EITF No. 07-3 in the first quarter of fiscal 2009, and it is not expected to have a material impact on the Company's results of operations or financial position.

In December 2007, FASB ratified Emerging Issues Task Force Issue No. 07-1, Accounting for Collaborative Arrangements . EITF No. 07-1 requires a company in a collaborative arrangement to present the results of activities for which it acts as the principal on a gross basis and to report any payments received from (made to) other collaborators based on other applicable generally accepted accounting principles (GAAP) or, in the absence of other applicable GAAP, based on analogy to authoritative literature or a reasonable, rational, and consistently applied accounting policy election. The Company is required to adopt EITF No. 07-1 for annual periods beginning after December 15, 2008. The Company is currently evaluating the requirements of EITF No. 07-1 and has not yet determined the impact on the Company's consolidated financial statements.

**Note C Interim Reporting**

The Company's three quarterly interim reporting periods are each thirteen-week periods ending on the Friday nearest the end of the third calendar month of each calendar quarter. The fiscal year end remains March 31<sup>st</sup>. To facilitate ease of presentation, each interim period is shown as if it ended on the last day of the appropriate calendar month. The actual dates for each of the three interim quarter ends are shown below:

|                | Fiscal 2008        | Fiscal 2007        |
|----------------|--------------------|--------------------|
| First Quarter  | June 29, 2007      | June 30, 2006      |
| Second Quarter | September 28, 2007 | September 29, 2006 |
| Third Quarter  | December 28, 2007  | December 29, 2006  |

The accompanying unaudited consolidated financial statements for the three and nine months ended December 31, 2007 and 2006 have been prepared in accordance with accounting principles generally accepted in the United States for interim financial information and with instructions to Form 10-Q and Article 10 of Regulation S-X. Accordingly, they do not include all of the information and notes required by accounting principles generally accepted in the United States for complete financial statements.

The consolidated financial statements should be read in conjunction with the Company's Annual Report on Form 10-K for the year ended March 31, 2007.

**Note D Cash Equivalents, Marketable Securities, and Long-Term Marketable Securities and Investments**

All highly liquid investments with maturities of three months or less at the date of purchase are considered to be cash equivalents.

The Company considers its marketable securities available-for-sale as defined in SFAS No. 115, Accounting for Certain Investments in Debt and Equity Securities. Available-for-sale securities are reported at fair market value. Realized gains and losses, and declines in value considered to be other than temporary, are included in income. The cost of securities sold is based on the specific identification method. Unrealized gains and losses are excluded from income, and are reported as a net amount in Accumulated Other Comprehensive Income in Shareholders' Equity. The Company's short-term marketable securities consist primarily of state and municipal government and government agency obligations, Federal Home Loan Bank and Mortgage Association bonds, and investment-grade corporate obligations, including commercial paper.



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Cash and available-for-sale investments at December 31, 2007 were as follows:

| (in thousands)                            | <b>Adjusted<br/>Cost</b> | <b>Gross<br/>Unrealized<br/>Gains</b> | <b>Gross<br/>Unrealized<br/>Losses</b> | <b>Estimated<br/>Fair<br/>Value</b> |
|-------------------------------------------|--------------------------|---------------------------------------|----------------------------------------|-------------------------------------|
| Cash balances                             | \$ 56,315                | \$                                    | \$                                     | \$ 56,315                           |
| Money market funds                        | 18,646                   |                                       |                                        | 18,646                              |
| U.S. Government and agency obligations    | 16,799                   | 6                                     | (1)                                    | 16,804                              |
| State and Municipal agency obligations    | 14,596                   |                                       |                                        | 14,596                              |
| Corporate debt securities                 | 285                      | 1                                     |                                        | 286                                 |
| <br>Total available-for-sale investments  | <br>\$ 106,641           | <br>\$ 7                              | <br>\$ (1)                             | <br>\$ 106,647                      |
| <br>Included in cash and cash equivalents | <br>\$ 74,961            | <br>\$                                | <br>\$                                 | <br>\$ 74,961                       |
| Included in current marketable securities | 31,680                   | &nbs                                  |                                        |                                     |