

RESPIRONICS INC  
Form 10-Q  
February 09, 2006  
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**UNITED STATES**  
**SECURITIES AND EXCHANGE COMMISSION**

WASHINGTON, D. C. 20549

**FORM 10-Q**

(Mark One)

**Quarterly Report pursuant to section 13 or 15(d) of the Securities Exchange Act of 1934**

for the quarterly period ended December 31, 2005

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. 000-16723

**RESPIRONICS, INC.**

(Exact name of registrant as specified in its charter)

Delaware  
(State or other jurisdiction of  
incorporation or organization)

25-1304989  
(I.R.S. Employer  
Identification Number)

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**1010 Murry Ridge Lane**  
**Murrysville, Pennsylvania**  
(Address of principal executive offices)

**15668-8525**  
(Zip Code)

**724-387-5200**

(Registrant's Telephone Number, including area code)

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

Indicate by check mark whether the registrant 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 January 31, 2006, there were 79,488,430 shares of Common Stock of the registrant outstanding, of which 6,990,315 were held in treasury.

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**RESPIRONICS, INC.**

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**Review Report of Independent Registered Public Accounting Firm**

Board of Directors

Respironics, Inc. and Subsidiaries

We have reviewed the accompanying consolidated balance sheet of Respironics, Inc. and Subsidiaries as of December 31, 2005, and the related consolidated statements of operations for the three-month and six-month periods ended December 31, 2005 and 2004, and the condensed consolidated statements of cash flows for the six-month periods ended December 31, 2005 and 2004. These interim financial statements are the responsibility of the Company's management.

We conducted our reviews in accordance with standards of the Public Company Accounting Oversight Board (United States). A review of interim financial information consists principally of applying analytical procedures to financial data, and making inquiries of persons responsible for financial and accounting matters. It is substantially less in scope than an audit conducted in accordance with the auditing standards of the Public Company Accounting Oversight Board, which will be performed for the full year with the objective of expressing an opinion regarding the financial statements taken as a whole. Accordingly, we do not express such an opinion.

Based on our reviews, we are not aware of any material modifications that should be made to the accompanying consolidated financial statements referred to above for them to be in conformity with U.S. generally accepted accounting principles.

We have previously audited, in accordance with standards of the Public Company Accounting Oversight Board (United States), the consolidated balance sheet of Respironics, Inc. and Subsidiaries as of June 30, 2005, and the related consolidated statements of operations, shareholders equity, and cash flows for the year then ended not presented herein, and in our report dated September 7, 2005 we expressed an unqualified opinion on those consolidated financial statements. In our opinion, the information set forth in the accompanying consolidated balance sheet as of June 30, 2005 is fairly stated, in all material respects, in relation to the consolidated balance sheet from which it has been derived.

/s/ Ernst & Young LLP

Pittsburgh, Pennsylvania

February 9, 2006

**Table of Contents****CONSOLIDATED BALANCE SHEETS****RESPIRONICS, INC. AND SUBSIDIARIES**

	(Unaudited) December 31 2005	June 30 2005
	<u>                    </u>	<u>                    </u>
<b>ASSETS</b>		
<b>CURRENT ASSETS</b>		
Cash and cash equivalents	\$ 250,303,943	\$ 234,632,280
Trade accounts receivable	174,378,593	153,479,117
Inventories	102,691,192	96,314,972
Prepaid expenses and other current assets	18,866,006	11,930,547
Deferred income tax benefits	41,228,981	39,767,465
	<u>                    </u>	<u>                    </u>
<b>TOTAL CURRENT ASSETS</b>	587,468,715	536,124,381
<b>PROPERTY, PLANT AND EQUIPMENT</b>		
Land	4,367,855	4,387,557
Buildings	24,427,197	23,088,982
Production and office equipment	288,794,890	279,156,393
Leasehold improvements	10,019,923	9,386,856
	<u>                    </u>	<u>                    </u>
	327,609,865	316,019,788
Less allowances for depreciation and amortization	201,002,525	188,643,863
	<u>                    </u>	<u>                    </u>
	126,607,340	127,375,925
<b>OTHER ASSETS</b>	51,539,055	48,318,790
<b>GOODWILL</b>	173,907,722	166,627,295
	<u>                    </u>	<u>                    </u>
<b>TOTAL ASSETS</b>	<u>\$ 939,522,832</u>	<u>\$ 878,446,391</u>
<b>LIABILITIES AND SHAREHOLDERS' EQUITY</b>		
<b>CURRENT LIABILITIES</b>		
Accounts payable	\$ 62,277,319	\$ 57,474,169
Accrued expenses and other current liabilities	123,597,772	123,136,829
Current portion of long-term obligations	16,284,691	17,411,475
	<u>                    </u>	<u>                    </u>
<b>TOTAL CURRENT LIABILITIES</b>	202,159,782	198,022,473
<b>LONG-TERM OBLIGATIONS</b>	28,322,454	29,240,901
<b>OTHER NON-CURRENT LIABILITIES</b>	22,590,577	23,537,406
<b>SHAREHOLDERS' EQUITY</b>		
Common Stock, \$.01 par value; authorized 100,000,000 shares; issued 79,285,882 shares at December 31, 2005 and 78,689,442 shares at June 30, 2005; outstanding 72,295,567 shares at December 31, 2005 and 71,698,913 shares at June 30, 2005	792,859	786,894
Additional capital	299,339,998	278,764,548
Accumulated other comprehensive loss	(9,280,455)	(4,873,567)
Retained earnings	437,036,966	394,407,777
Treasury stock	(41,439,349)	(41,440,041)
	<u>                    </u>	<u>                    </u>
<b>TOTAL SHAREHOLDERS' EQUITY</b>	686,450,019	627,645,611

TOTAL LIABILITIES AND SHAREHOLDERS EQUITY	<u>\$ 939,522,832</u>	<u>\$ 878,446,391</u>
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See notes to consolidated financial statements.

**Table of Contents****CONSOLIDATED STATEMENTS OF OPERATIONS (UNAUDITED)****RESPIRONICS, INC. AND SUBSIDIARIES**

	Three-month periods ended December 31		Six-month periods ended December 31	
	2005	2004	2005	2004
Net sales	\$ 257,901,418	\$ 225,929,127	\$ 498,123,729	\$ 425,365,731
Cost of goods sold	115,169,252	103,151,583	222,712,286	195,213,405
	142,732,166	122,777,544	275,411,443	230,152,326
General and administrative expenses (excluding acquisition earn-out expenses)	39,556,803	34,808,895	79,807,802	65,097,270
Acquisition earn-out expenses	752,290	876,686	2,052,529	1,551,686
Sales, marketing and commission expenses	50,687,026	41,966,518	101,192,997	82,874,550
Research and development expenses	12,962,179	10,991,169	27,031,829	20,389,999
Contribution to foundation		1,500,000	1,500,000	1,500,000
Restructuring and acquisition-related expenses	224,133	2,290,312	1,313,166	4,425,477
Other (income) expense, net	(76,649)	(1,690,677)	(6,013,904)	(1,833,670)
	104,105,782	90,742,903	206,884,419	174,005,312
<b>INCOME BEFORE INCOME TAXES</b>	38,626,384	32,034,641	68,527,024	56,147,014
Income taxes	14,573,601	11,965,112	25,897,835	20,886,690
<b>NET INCOME</b>	\$ 24,052,783	\$ 20,069,529	\$ 42,629,189	\$ 35,260,324
Basic earnings per share	\$ 0.33	\$ 0.28	\$ 0.59	\$ 0.50
Basic shares outstanding	72,160,067	70,582,744	72,014,449	70,366,090
Diluted earnings per share	\$ 0.33	\$ 0.28	\$ 0.58	\$ 0.49
Diluted shares outstanding	73,540,297	71,984,940	73,452,853	71,901,968

See notes to consolidated financial statements.

**Table of Contents****CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS (UNAUDITED)****RESPIRONICS, INC. AND SUBSIDIARIES**

	Six-month periods ended December 31	
	2005	2004
<b>OPERATING ACTIVITIES</b>		
Net income	\$ 42,629,189	\$ 35,260,324
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	22,005,348	22,352,129
Stock-based compensation	5,878,551	
Excess tax benefits from share-based payment arrangements	(4,571,520)	1,741,434
Gain on sale of investment	(4,398,274)	
Changes in operating assets and liabilities:		
Accounts receivable	(20,899,477)	(6,349,345)
Inventories	(6,376,220)	(3,435,249)
Other operating assets and liabilities	(2,385,120)	1,612,513
<b>NET CASH PROVIDED BY OPERATING ACTIVITIES</b>	<b>31,882,477</b>	<b>51,181,806</b>
<b>INVESTING ACTIVITIES</b>		
Proceeds from sale of investment	5,488,097	
Purchase of property, plant and equipment	(24,867,180)	(30,926,024)
Acquisition of businesses, net of cash acquired	(9,068,398)	(47,414,750)
Additional purchase price for previously acquired businesses	(3,696,866)	(1,956,769)
<b>NET CASH USED BY INVESTING ACTIVITIES</b>	<b>(32,144,347)</b>	<b>(80,297,543)</b>
<b>FINANCING ACTIVITIES</b>		
Excess tax benefits from share-based payment arrangements	4,571,520	
Net increase in borrowings	1,229,977	4,324,822
Issuance of common stock	10,132,036	10,563,860
<b>NET CASH PROVIDED BY FINANCING ACTIVITIES</b>	<b>15,933,533</b>	<b>14,888,682</b>
<b>INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS</b>	<b>15,671,663</b>	<b>(14,227,055)</b>
Cash and cash equivalents at beginning of period	234,632,280	192,445,866
<b>CASH AND CASH EQUIVALENTS AT END OF PERIOD</b>	<b>\$ 250,303,943</b>	<b>\$ 178,218,811</b>

See notes to consolidated financial statements.



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**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)**

**RESPIRONICS, INC. AND SUBSIDIARIES**

**December 31, 2005**

**NOTE A BASIS OF PRESENTATION**

The accompanying unaudited condensed consolidated financial statements have been prepared in accordance with U.S. generally accepted accounting principles for interim financial information and with the instructions to Form 10-Q and Article 10 of Regulation S-X. Accordingly, they do not include all of the information and footnotes required by U.S. generally accepted accounting principles for complete financial statements. In the opinion of management, all adjustments (consisting of normal recurring accruals) considered necessary for a fair presentation have been included. Operating results for the three-month and six-month periods ended December 31, 2005 are not necessarily indicative of the results that may be expected for the year ended June 30, 2006. The amounts and information as of June 30, 2005 set forth in the consolidated balance sheet and notes to the consolidated financial statements that follow were derived from the Company's Annual Report on Form 10-K for the year ended June 30, 2005. For further information, refer to the consolidated financial statements and footnotes thereto included in the Company's Annual Report on Form 10-K for the year ended June 30, 2005.

On April 20, 2005, the Company's Board of Directors declared a two-for-one stock split of the Company's common stock, payable in the form of a 100% stock dividend. On June 1, 2005, one additional share of common stock was distributed for each share held of record on May 9, 2005. An amount equal to the par value of the shares issued was transferred from the additional capital account to the common stock account. All references to number of shares, except shares authorized, and to per share information in the consolidated financial statements have been adjusted to reflect the stock split on a retroactive basis.

Certain amounts in the June 30, 2005 financial statements were reclassified to conform with the presentation in the current period.

**NOTE B STOCK OPTION AND PURCHASE PLANS**

At December 31, 2005, the Company has two active employee stock option plans, the 2000 Stock Incentive Plan and the 2006 Stock Incentive Plan, and one employee stock purchase plan. The 2000 Incentive Stock Option Plan and the employee stock purchase plan are described more fully in Note M in the Company's June 30, 2005 consolidated financial statements. The 2000 Stock Incentive Plan provides for the issuance of up to 3,276,000 shares for grant to eligible employees, consultants, and non-employee directors for a period of up to ten years at option prices not less than the fair market value at the time of grant. As of December 31, 2005, 443,000 shares were reserved and available to be granted pursuant to the 2000 Incentive Stock Option Plan. The 2006 Stock Incentive Plan was approved by shareholders on November 15, 2005, and provides for the issuance of up to 5,019,000 shares to be granted to eligible employees, consultants, and non-employee directors for a period of up to ten years at option prices not less than the fair market value at the time of grant. As of December 31, 2005, no shares have been granted from the 2006 Stock Incentive Plan. The Company may satisfy the awards upon exercise under both plans with either newly-issued or treasury shares.

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In December 2004, the Financial Accounting Standards Board ( FASB ) issued Statement Number 123 (Revised 2004) Share-Based Payment ( FASB 123(R) ), which is a revision of FASB Statement No. 123, Accounting for Stock-Based Compensation ( FASB 123 ). FASB 123(R) replaces FASB 123, and supersedes Accounting Principles Board Opinion No. 25, Accounting for Stock Issued to Employees ( APB 25 ). FASB 123(R) requires that all stock-based compensation be recognized as expenses in the financial statements and that such expenses are measured at the fair value of the award.

The Company adopted FASB 123(R) on July 1, 2005 using the modified prospective method, which resulted in the recognition of stock compensation expenses in the consolidated statement of operations during the three-

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month and six-month periods ended December 31, 2005. Under the modified prospective method, prior period financial statements have not been restated, and the stock-based compensation expenses recorded in the consolidated statement of operations after adoption of FAS 123(R) includes both new share-based awards and the remaining service period of awards that had been included in pro forma disclosures in prior periods. Stock-based compensation expenses in the three-month and six-month periods ended December 31, 2005 was \$3,105,000 (\$2,208,000 after tax, or \$0.03 per share) and \$5,879,000 (\$4,217,000 after tax, or \$0.06 per share). For the three-month period ended December 31, 2005 stock-based compensation expense is comprised of \$2,914,000 attributable to stock options and \$192,000 is attributable to the employee stock purchase plan. For the six-month period ended December 31, 2005, stock-based compensation expense is comprised of \$5,521,000 attributable to stock options and \$357,000 attributable to the employee stock purchase plan. As of December 31, 2005, the total unrecognized stock-based compensation expenses related to non-vested stock awards was \$25,670,000, which will be recognized over a weighted-average period of 2.06 years.

FASB 123(R) also requires that excess tax benefits related to stock option exercises be reflected as a component of financing cash flows instead of operating cash flows. For the six-month period ended December 31, 2005, the adoption of FASB 123(R) resulted in cash flows provided by financing activities of \$4,572,000, which reduced cash flows provided by operating activities by the same amount.

The following table summarizes the Company's stock option information as of, and for the six-month period ended December 31, 2005:

**Option  
Shares**

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