PERNIX THERAPEUTICS HOLDINGS, INC.
Form 10-Q
May 15, 2012

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, DC 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: March 31, 2012

o Transition report pursuant to section 13 or 15(d) of the Securities Exchange Act of 1934

For the transition period from: _____ to _____

001-14494
Commission File Number

PERNIX THERAPEUTICS HOLDINGS, INC.
(Exact name of Registrant as specified in its charter)

Maryland	33-0724736
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification Number)
10003 Woodloch Forest Drive, The Woodlands, TX	77380
(Address of principal executive offices)	(Zip Code)

(832) 934-1825
(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 report(s)) and (2) has been subject to such filing requirements for the past 90 days. Yes þ No ¨ .

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

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 definitions of “large accelerated filer,” “accelerated filer,” and “smaller reporting company” in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer	o	Accelerated filer	o
Non-accelerated filer (Do not check if a smaller reporting company)	o	Smaller reporting company	þ

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

On May 11, 2012, there were 29,068,163 shares outstanding of the Registrant’s common stock, par value $0.01 per share.

PERNIX THERAPEUTICS HOLDINGS, INC.
Quarterly Report on Form 10-Q
For the Three Months Ended March 31, 2012

INDEX

PART I. FINANCIAL INFORMATION

PART II. INFORMATION

Cautionary Statement Regarding Forward-Looking Statements

The Private Securities Litigation Reform Act of 1995 provides a "safe harbor" for forward-looking statements to encourage companies to provide prospective information, so long as those statements are identified as forward-looking and are accompanied by meaningful cautionary statements identifying important factors that could cause actual results to differ materially from those discussed in the statement. We desire to take advantage of these "safe harbor" provisions with regard to the forward-looking statements in this Form 10-Q and in the documents that are incorporated herein by reference. These forward-looking statements reflect our current views with respect to future events and financial performance. Specifically, forward-looking statements may include:

- projections of revenues, expenses, income, income per share and other performance measures;
- statements regarding expansion of operations, including entrance into new markets and development of products; and
- statements preceded by, followed by or that include the words "estimate," "plan," "project," "forecast," "intend," "expect," "anticipate," "believe," "seek," "target" or similar expressions.

These forward-looking statements express our best judgment based on currently available information and we believe that the expectations reflected in our forward-looking statements are reasonable.

By their nature, however, forward-looking statements often involve assumptions about the future. Such assumptions are subject to risks and uncertainties that could cause actual results to differ materially from those described in the forward-looking statements. As such, we cannot guarantee you that the expectations reflected in our forward-looking statements will actually be achieved. Actual results may differ materially from those in the forward-looking statements due to, among other things, the following factors:

- changes in general business, economic and market conditions;
- volatility in the securities markets generally or in the market price of our stock specifically; and
- the risks outlined in the section entitled "Risk Factors" contained in our Annual Report on Form 10-K for the fiscal year ended December 31, 2011.

We caution you not to place undue reliance on any forward-looking statements, which speak only as of the date of this Form 10-Q. Except as required by law, we do not undertake any obligation to publicly update or release any revisions to these forward-looking statements to reflect any events or circumstances after the date hereof or to reflect the occurrence of unanticipated events.

PART I. FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS

PERNIX THERAPEUTICS HOLDINGS, INC.
CONDENSED CONSOLIDATED BALANCE SHEETS

	March 31, 2012 (unaudited)	December 31, 2011
ASSETS		
Current assets:		
Cash and cash equivalents	$39,201,515	$ 34,551,180
Accounts receivable, net	16,401,767	20,601,360
Inventory, net	5,040,631	6,261,162
Prepaid expenses and other current assets	1,672,289	2,144,203
Pepaid taxes	807,174	
Deferred income taxes	4,057,000	4,552,000
Total current assets	67,180,376	68,109,905
Property and equipment, net	1,057,105	911,948
Other assets:		
Investments	5,869,320	4,451,831
Intangible assets, net	12,664,454	8,876,504
Other long-term assets	213,783	213,783
Total assets	$86,985,038	$ 82,563,971
LIABILITIES		
Current liabilities:		
Accounts payable	$2,249,872	$ 2,987,913
Accrued personnel expense	1,371,517	2,044,121
Accrued allowances	14,905,179	17,006,409
Income taxes payable		585,931
Other accrued expenses	2,024,198	1,565,918
Contracts payable	3,415,725	1,290,000
Line of Credit	6,000,000	6,000,000
Total current liabilities	29,966,491	31,480,292
Long-term liabilities:		
Contracts payable	300,000	600,000
Deferred income taxes	1,425,000	860,000
Total liabilities	31,691,491	32,940,292
Commitments and contingencies		
STOCKHOLDERS' EQUITY		
Common stock, $.01 par value, 90,000,000 shares authorized, 28,423,482 and 27,820,004 issued, and 26,350,672 and 25,749,137 outstanding at March 31, 2012 and December 31, 2011, respectively	263,507	257,491
Treasury stock, at cost (2,072,810 and 2,070,867 shares held at March 31, 2012 and December 31, 2011, respectively)	(3,772,410)	(3,751,890)

Additional paid-in capital	33,655,001	30,185,292
Retained earnings	23,034,581	21,843,418
Other comprehensive income	2,112,868	1,089,368
Total stockholders' equity	55,293,547	49,623,679
Total liabilities and stockholders' equity	$86,985,038	$ 82,563,971

See accompanying notes to condensed consolidated financial statements.

PERNIX THERAPEUTICS HOLDINGS, INC.
CONDENSED CONSOLIDATED STATEMENTS OF INCOME AND COMPREHENSIVE INCOME
(Unaudited)

	Three Months Ended March 31,	
	2012	2011
Net revenues	$14,482,025	$10,094,975
Costs and expenses:		
Cost of product sales	4,690,583	1,956,040
Selling, general and administrative expenses	6,824,262	5,219,740
Research and development expense	70,006	106,158
Loss from the operations of the joint venture with SEEK	240,195	330,000
Royalties expense, net		261,400
Depreciation and amortization expense	638,072	493,285
Total costs and expenses	12,463,118	8,366,623
Income from operations	2,018,907	1,728,352
Other income (expense):		
Other expense	(4,807)	
Interest expense, net	(39,937)	(30,177)
Total other income, net	(44,744)	(30,177)
Income before income taxes	1,974,163	1,698,175
Income tax provision	783,000	723,000
Net income	$1,191,163	$975,175
Unrealized gain on securities, net of income tax of approximately $634,000	1,023,500	
Comprehensive income	$2,214,663	$975,175
Net income per share, basic	$0.05	$0.04
Net income per share, diluted	$0.04	$0.04
Weighted-average common shares, basic	25,921,139	22,652,394
Weighted-average common shares, diluted	26,473,364	23,141,524

See accompanying notes to condensed consolidated financial statements.

PERNIX THERAPEUTICS HOLDINGS, INC.

CONDENSED CONSOLIDATED STATEMENTS OF STOCKHOLDERS' EQUITY

(Unaudited)

	Common Stock	Additional Paid-In Capital	Treasury Stock	Retained Earnings	Accumulated Other Comprehensive income	Total
Balance at December 31, 2011	257,491	30,185,292	(3,751,890)	21,843,418	1,089,368	49,623,679
Stock-based compensation	2,881	493,317				496,198
Issuance of stock options for services from non-employees		188,365				188,365
Issuance of common stock, net of stock withheld for income tax liability	471	257,380	(20,520)			237,331
Income tax benefit on stock based awards		133,000				133,000
Issuance of common stock upon additional public offering, net of issuance costs of $185,871	2,664	2,397,647				2,400,311
Net income				1,191,163		1,191,163
Unrealized gain on securities, net					1,023,500	1,023,500
Balance at March 31, 2012	$ 263,507	$ 33,655,001	$ (3,772,410)	$ 23,034,581	$ 2,112,868	$ 55,293,547

See accompanying notes to condensed consolidated financial statements.

PERNIX THERAPEUTICS HOLDINGS, INC.
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
(Unaudited)

	Three months ended March 31,	
	2012	2011
Cash flows from operating activities:		
Net income	$ 1,191,163	$ 975,175
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation	26,022	21,958
Amortization	612,050	471,327
Deferred income tax benefit	425,816	(978,000)
Loss on disposal of assets	4,807	
Stock compensation expense	496,198	211,275
Expense from stock options issued in exchange for services	188,365	
Loss from the operations of the joint venture with SEEK	240,195	330,000
Changes in operating assets and liabilities:		
Accounts receivable	4,199,593	3,441,855
Inventory	1,220,531	48,374
Prepaid expenses and other assets	471,915	(297,717)
Accounts payable	(738,041)	(1,457,421)
Income taxes	(1,393,105)	(92,478)
Accrued expenses	(2,115,784)	2,337,867
Net cash from operating activities	4,829,725	5,012,215
Cash flows from investing activities:		
Payments received on notes receivable		56,667
Acquisition of gastroenterology product license	(2,400,000)	
Purchase of equipment	(20,261)	(75,284)
Net cash from investing activities	(2,420,261)	(18,617)
Cash flows from financing activities:		
Proceeds from line of credit		1,000,000
Payment on contracts payable	(330,000)	(1,300,000)
Proceeds from issuance of stock in additional offering, net of issuance costs of $185,871	2,400,310	
Tax benefit on stock-based awards	133,000	
Proceeds from issuance of stock, net of stock withheld for payment of income tax liability	37,561	
Net cash from financing activities	2,240,871	(300,000)
Net increase in cash and cash equivalents	4,650,335	4,693,598
Cash and cash equivalents, beginning of period	34,551,180	8,260,059
Cash and cash equivalents, end of period	$ 39,201,515	$ 12,953,657
Supplemental disclosure:		
Cash paid for income taxes	$ 1,297,725	$ 1,793,529
Accrued 2011 bonus paid in unrestricted common stock	$ 199,770	$
Interest paid during the period	$ 53,297	$ 36,143
Non-cash transaction		

Acquisition of Omeclamox® license - contract payable	$ 2,000,000	$

See accompanying notes to condensed consolidated financial statements.

PERNIX THERAPEUTICS HOLDINGS, INC.
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
FOR THE THREE MONTHS ENDED MARCH 31, 2012
(Unaudited)

Note 1. Company Overview

Pernix is a specialty pharmaceutical company focused on the sales, marketing and development of branded and generic pharmaceutical products for pediatric and adult indications in a variety of therapeutic areas. We expect to continue to execute our growth strategy which involves the horizontal integration of our branded prescription, generic and OTC businesses. We manage a portfolio of branded and generic prescription products and theobromine, a non-codeine, cough suppressant product candidate in development. Our branded products for the pediatrics market include CEDAX®, an antibiotic for middle ear infections, NATROBA™, a topical treatment for head lice marketed under an exclusive co-promotion agreement with ParaPRO, LLC, REZYST IM™, a proprietary probiotic blend to promote dietary management and a family of prescription treatments for cough and cold (BROVEX®, ALDEX® and PEDIATEX®). The Company promotes its branded products through an established U.S. sales force. Pernix also markets generic products through its wholly-owned subsidiary, Macoven Pharmaceuticals. Founded in 1996, the Company is based in The Woodlands, TX.

Registered Direct Offering. On July 27, 2011, the Company completed an underwritten registered direct offering of 4,000,000 shares of common stock pursuant to the terms of that certain underwriting agreement dated July 21, 2011 by and among the Company, the selling stockholders named therein and the underwriters named on Schedule I thereto, for whom Stifel, Nicolaus & Company, Incorporated acted as representative. As provided in the underwriting agreement, (i) the Company sold an aggregate of 3,000,000 shares of its common stock, and (ii) the selling stockholders sold 1,000,000 shares of common stock. The public offering price was $7.00 per share, and the underwriters purchased the shares subject to the offering at a price of $6.58 per share. The offering was led by Aisling Capital and OrbiMed Advisors, LLC. Net proceeds from the sale of the shares of common stock sold by the Company, after underwriting discounts and commissions and offering expenses, were approximately $19.3 million. The offering was made pursuant to an effective shelf registration statement filed with the Securities and Exchange Commission on May 31, 2011.

Controlled Equity Offering. On February 10, 2012, the Company entered into a controlled equity offering sales agreement (the “Sales Agreement”) with Cantor Fitzgerald & Co. (“Cantor”) pursuant to which the Company could issue and sell shares of its common stock having an aggregate offering price of up to $25,000,000 from time to time through Cantor, acting as agent, but in no event more than 5,000,000 shares of common stock. Sales of the Company's common stock through Cantor were be made on the NYSE Amex by means of ordinary brokers’ transactions at market prices, in block transactions or as otherwise agreed by Cantor and the Company. Cantor used its commercially reasonable efforts to sell the Company's common stock from time to time, based upon the Company's instructions (including any price, time or size limits or other customary parameters or conditions the Company may impose). The Company paid Cantor a commission rate of 3.0% of the gross sales price per share of any common stock sold through Cantor as agent under the Sales Agreement. The Company has also reimbursed Cantor for certain expenses incurred in connection with entering into the Sales Agreement and has provided Cantor with customary indemnification rights. The Company will use the proceeds of this financing to provide funding for future acquisitions and for general corporate purposes. As of March 31, 2012, the Company has sold 266,400 shares of common stock under this controlled equity program for total net proceeds of approximately $2.5 million after deducting commissions. See Note 12, Subsequent Events, for further discussion.

5

Note 2. Basis of Presentation and Summary of Significant Accounting Policies

Interim Financial Statements

The accompanying unaudited condensed consolidated financial statements have been prepared in accordance with generally accepted accounting principals in the United States ("GAAP") and with the instructions to Form 10-Q and Rule 10-01 of Regulation S-X. Certain information and footnote disclosures normally included in financial statements prepared in accordance with GAAP have been condensed or omitted. These 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, 2011.

In the opinion of management, the accompanying unaudited condensed consolidated financial statements include all adjustments (consisting of normal recurring adjustments) necessary for a fair presentation of these financial statements. Operating results for the three-month period ended March 31, 2012 are not necessarily indicative of the results for future periods or the full year.

Principles of Consolidation

The condensed consolidated financial statements include the accounts of Pernix's wholly-owned subsidiaries: Pernix Therapeutics, LLC, GTA GP, Inc., GTA LP, Inc., Gaine, Inc. and Macoven Pharmaceuticals, LLC. Transactions between and among the Company and its consolidated subsidiaries are eliminated.

Management's Estimates and Assumptions

The preparation of condensed consolidated financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the condensed consolidated financial statements and the reported amounts of revenues and expenses during the period. Actual results could differ from those estimates. The Company reviews all significant estimates affecting the condensed consolidated financial statements on a recurring basis and records the effect of any necessary adjustments prior to their issuance. Significant estimates of the Company include: revenue recognition, sales allowances such as returns on product sales, government program rebates, customer coupon redemptions, wholesaler/pharmacy discounts, product service fees, rebates and chargebacks, sales commissions, amortization, depreciation, stock-based compensation, the determination of fair values of assets and liabilities in connection with business combinations, and deferred income taxes.

Equity Method of Accounting

For the periods presented, the Company's investment in the joint venture with SEEK is accounted for at cost and adjusted for the Company's share (46%) of the joint venture's undistributed earnings or losses.

Revenue Recognition

The Company's consolidated net revenues represent the Company's net product sales and collaboration revenues. The following table sets forth the categories of the Company's net revenues (in thousands) for the three months ended March 31, 2012 and 2011.

	Three Months Ended March 31,

	(in thousands)	
	2012	2011
Gross product sales	$ 20,268	$ 18,252
Sales allowances	(6,283)	(9,323)
Net product sales	13,985	8,929
Co-promotion and other revenue	497	1,166
Net revenues	$ 14,482	$ 10,095

The Company records all of its revenue from product sales and co-promotion agreements when realized or realizable and earned. Revenue is realized or realizable and earned when all of the following criteria are met: (1) persuasive evidence of an arrangement exists; (2) delivery has occurred or services have been rendered; (3) the seller's price to the buyer is fixed or determinable; and (4) collectability is reasonably assured. The Company records revenue from product sales when the customer takes ownership and assumes risk of loss (free-on-board destination). Royalty revenue is recognized upon shipment from the manufacturer to the purchaser. Co-promotion revenue is recognized in the period in which the product subject to the arrangement is sold. At the time of sale, estimates for a variety of sales deductions, such as returns on product sales, government program rebates, price adjustments and prompt pay discounts are recorded.

The Company relies on certain materials used in its development and manufacturing processes, most of which are procured from a single source. The Company purchases its pharmaceutical ingredients from a limited number of suppliers. The failure of a supplier, including a subcontractor, to deliver on schedule could delay or interrupt the development or commercialization process and thereby adversely affect the Company's operating results. In addition, a disruption in the commercial supply of or a significant increase in the cost of the active pharmaceutical ingredient ("API") from any of these sources could have a material adverse effect on the Company's business, financial position and results of operations.

The Company's customers consist of drug wholesalers, retail drug stores, mass merchandiser and grocery store pharmacies in the United States. The Company primarily sells its products directly to large national drug wholesalers, which in turn resell the products to smaller or regional wholesalers, retail pharmacies, chain drug stores, and other third parties. The following tables list the Company's customers that individually comprised greater than 10% of total gross product sales for the three months ended March 31, 2012 and 2011, or 10% of total accounts receivable as of March 31, 2012 and December 31, 2011.

	Gross Product Sales Three Months Ended March 31,	
	2012	2011
Cardinal Health, Inc.	33%	44%
McKesson Corporation	24%	26%
AmerisourceBergen Drug Corporation	17%	14%
Morris & Dickson Co., LLC	11%	7%
Total	85%	91%

	Accounts Receivable	
	March 31, 2012	December 31, 2011
Cardinal Health, Inc.	37%	30%
McKesson Corporation	23%	32%
Walgreens	14%	8%
AmerisourceBergen Drug Corporation	13%	8%
Total	87%	78%

Net Revenues

Product Sales

The Company recognizes revenue from its product sales in accordance with its revenue recognition policy discussed above. The Company sells its products primarily to large national wholesalers, which have the right to return the products they purchase. The Company is required to estimate the amount of future returns at the time of revenue recognition. The Company recognizes product sales net of estimated allowances for product returns, government program rebates, price adjustments, and prompt pay discounts.

Product Returns

Consistent with industry practice, the Company offers contractual return rights that allow its customers to return the majority of its products within an 18-month period, commencing from six months prior to and up to twelve months subsequent to the product expiration date. The Company's products have a 24 to 36-month expiration period from the date of manufacture. The Company adjusts its estimate of product returns if it becomes aware of other factors that it believes could significantly impact its expected returns. These factors include its estimate of inventory levels of its products in the distribution channel, the remaining shelf life of the product, review of consumer consumption data as reported by external information management companies, actual and historical return rates for expired lots, the forecast of future sales of the product, competitive issues such as new product entrants and other known changes in sales trends. The Company estimated returns at 5% to 10% of sales of branded products during the first quarter of 2012. This estimate is based upon historical data and other facts and circumstances that may impact future expected returns to derive an average return percentage of our products. Under our co-promotion arrangement with ParaPRO, certain returns of Natroba sold within the first year of launch may be reimbursed by ParaPRO up to 65%. The Company estimated returns at 5% - 7% on sales of generic products on sales during the first quarter of 2012 depending on assumptions and/or facts and circumstances existing for certain products. The returns reserve may be adjusted as we accumulate sales history and returns experience on this portfolio of products. The Company reviews and adjusts these reserves quarterly.

Government Program Rebates

The liability for Medicaid, Medicare and other government program rebates is estimated based on historical and current rebate redemption and utilization rates contractually submitted by each state's program administrator and assumptions regarding future Medicaid utilization for each product.

Price Adjustments

The Company's estimates of price adjustments, which include customer rebates, service fees, chargebacks, and other fees and discounts, are based on our estimated mix of sales to various third-party payors who are entitled, either contractually or statutorily, to discounts from the listed prices of our products and contracted service fees with our wholesalers. In the event that the sales mix to third-party payors or the contract fees paid to the wholesalers are different from the Company's estimates, the Company may be required to pay higher or lower total price adjustments and/or incur chargebacks that differ from its original estimates and such difference may be significant.

The Company's estimates of discounts are applied pursuant to the contracts negotiated with certain customers and are primarily based on sales volumes. The Company, from time to time, offers certain promotional product-related incentives to its customers. These programs include sample cards to retail consumers, certain product incentives to pharmacy customers and other sales stocking allowances. For example, the Company has initiated coupon programs for certain of its promoted products whereby the Company offers a point-of-sale subsidy to retail consumers. The Company estimates its liabilities for these coupon programs based on redemption information provided by a third party claims processing organization. The Company accounts for the costs of these special promotional programs as price adjustments, resulting in a reduction in gross revenue.

Any price adjustments that are not contractual or are non-recurring but that are offered at the time of sale or when a specific triggering event occurs, such as sales stocking allowances or price protection adjustments, are recorded as a reduction in revenue when the sales order is recorded or when the triggering event occurs. These allowances may be offered at varying times throughout the year or may be associated with specific events such as a new product launch, the reintroduction of a product or product price changes.

Prompt Payment Discount

The Company typically requires its customers to remit payments within the first 30 days for branded products and within 60 to 120 days for generics, depending on the customer and the products purchased. The Company offers wholesale distributors a prompt payment discount if they make payments within these deadlines. This discount is generally 2%, but may be higher in some instances due to product launches and/or industry expectations. Because the Company's wholesale customers typically take the prompt pay discount, we accrue 100% of prompt pay discounts. These discounts are based on the gross amount of each invoice at the time of our original sale to them. Earned discounts are applied at the time of payment. This allowance is recorded as a reduction of accounts receivable.

See Note 8, Other Revenue Sharing Arrangements, for further discussion of co-promotion and other revenue sharing arrangements.

Earnings per Share

Earnings per common share is presented under two formats: basic earnings per common share and diluted earnings per common share. Basic earnings per common share is computed by dividing net income attributable to common shareholders by the weighted average number of common shares outstanding during the period. Diluted earnings per common share is computed by dividing net income by the weighted average number of common shares outstanding during the period, plus the potentially dilutive impact of common stock equivalents (i.e. stock options). Dilutive common share equivalents consist of the incremental common shares issuable upon exercise of stock options.

The following table sets forth the computation of basic and diluted net income per share:

	Three Months Ended March 31,	
	2012	2011
Numerator:		
Net income	$ 1,191,163	$ 975,175
Denominator:		
Weighted-average common shares, basic	25,921,139	22,652,394
Dilutive shares	552,225	489,130
Weighted-average common shares, diluted	26,473,364	23,141,524
Net income per share, basic	$ 0.05	$ 0.04
Net income per share, diluted	$ 0.04	$ 0.04

Total outstanding options at March 31, 2012 are 1,980,499. Options not included above of 1,428,274 are anti-dilutive as of March 31, 2012. See Note 9, Employee Equity Compensation, for information regarding the Company's outstanding options.

Investments in Marketable Securities and Other Comprehensive Income

The Company holds investment marketable equity securities as available-for-sale and the change in the market value gives rise to other comprehensive income. The components of other comprehensive income are recorded in the consolidated statements of income and comprehensive income, net of the related income tax effect.

On October 5, 2011, the Company acquired 2.6 million shares of TherapeuticsMD for a purchase price of $1.0 million, or $0.38 per share, representing approximately 3.2% of TherapeuticsMD's outstanding common stock at that time. The Company's purchase was contingent upon TherapeuticsMD's acquisition of VitaMedMD, which occurred on October 4, 2011. The Company has applied a 30% discount to the quoted market value of its TherapeuticsMD stock, which represents the Company's estimate of the discount for lack of marketability for its non-controlling interest. In connection with the Company's purchase of shares of TherapeuticsMD, the Company also entered into a software license agreement with VitaMedMD pursuant to which VitaMedMD granted the Company an exclusive license to use certain of its physician, patient and product data gathering software in the field of pediatric medicine for a period of five years for a monthly fee of $21,700. Cooper Collins, the Company's Chief Executive Officer, serves on the board of TherapeuticsMD.

As of March 31, 2012

TherapeuticsMD Common Stock	Cost	Appreciation	Discount	Fair Value
2,631,579 shares	$ 1,000,000	$ 5,315,789	$ (1,894,737)	$ 4,421,052

Reclassifications

Certain reclassifications have been made to prior period amounts in our consolidated statements of income to conform to the current period presentation. These reclassifications related to the classification of cost of samples as a selling expense instead of including in cost of goods had no effect on net income as previously reported.

Recent Accounting Pronouncements

There have been no other recent accounting pronouncements that have not yet been adopted by us that are expected to have a material impact on our condensed consolidated financial statements from the accounting pronouncements previously disclosed in our Annual Report on Form 10-K for the year ended December 31, 2011.

Note 3. Accounts Receivable

Accounts receivable consist of the following:

	March 31, 2012	December 31, 2011
Trade accounts receivable	$ 15,297,616	$ 18,844,320
Less allowance for prompt pay discounts	(339,695)	(393,174)
Total trade receivables	14,957,921	18,451,146
Receivables from third parties – revenue sharing arrangements	1,371,419	2,146,214
Other miscellaneous receivables	72,427	4,000
Total account receivables	$ 16,401,767	$ 20,601,360

As of March 31, 2012 and December 31, 2011, no receivables were outstanding for longer than the agreed upon payment terms. The net amount of accounts receivable was considered collectible and no allowance for doubtful accounts was recorded.

Note 4. Investment in Joint Venture

On December 17, 2010, the Company entered into a Joint Venture Agreement (the “JV Agreement”) with SEEK, a United Kingdom drug discovery group, to form a joint venture structured as a private company limited by shares incorporated in the United Kingdom (the “JV”). The purpose of the JV is to develop and obtain regulatory approval in both Europe and the United States for products utilizing the JV's intellectual property. Pernix contributed approximately $1.5 million to the JV, in consideration for 50% of the voting interest and approximately 46% of the total economic interest in the JV. On September 26, 2011, the Company funded an additional $1.0 million in cash to the JV for continuing operations.

Below is the condensed balance sheet of the JV:

Condensed Balance Sheet as of: (unaudited) (in thousands)	March 31, 2012	December 31, 2011
Cash and other current assets	$ 947	$ 1,512
Intellectual property and other rights (including capitalized development costs)	1,719	1,719
Total assets	$ 2,666	$ 3,231
Equity	$ 2,666	$ 3,231

	For the three months ended March 31, 2012	2011
Loss from operations of the joint venture with SEEK	$ 240	$ 330

Theobromine development costs were approximately $512,000 for the three months ended March 31, 2012. The Company recorded approximately 46% of these development costs, or $240,000 for the three months ended March 31, 2012, in loss from operations of our JV.

For additional information, see Note 12, Subsequent Events, for further discussion.

Note 5. Intangible Assets

License of Gastroenterology Product. In January 2012, the Company entered into a license and supply agreement with a private company for a new FDA-approved prescription product to treat gastroenterology disease. Under the terms of the agreement, the Company obtained exclusive marketing rights to Omeclamox® in the United States. The Company paid an up-front license fee of $2.0 million and will pay an additional fee of $2.0 million upon commercial launch of the product. In addition to these license fees, the agreement calls for the Company to pay royalties and milestone payments based on the sales of the product. Pernix is currently establishing a gastroenterology sales force and plans to launch Omeclamox-Pak® in the summer of 2012. Omeclamox-Pak® is a triple combination medication taken orally to treat Helicobacter pylori (H. pylori) infection and eradicate duodenal ulcer disease in adults.

Intangible assets consist of the following:

	Life	March 31, 2012	December 31, 2011
Patents	12 - 15 years	$ 1,442,000	$ 1,442,000
Brand – CEDAX	8 years	3,887,000	3,887,000
Product licenses	1 – 10 years	4,520,000	120,000
Non-compete and supplier contract – Macoven	2 - 7 years	5,194,571	5,194,571
Trademark rights – BROVEX	Indefinite	238,758	238,758
Goodwill	Indefinite	1,406,591	1,406,591
		16,688,920	12,288,920
Accumulated amortization		(4,024,466)	(3,412,416)
Total		$ 12,664,454	$ 8,876,504

Estimated amortization expense related to intangible assets with definite lives for each of the five succeeding years and thereafter is as follows:

	Amount
2012 (April – December)	$ 1,113,000
2013	1,505,000
2014	1,505,000
2015	1,505,000
2016	1,505,000
Thereafter	3,886,105
Total	$ 11,019,105

Amortization expense is approximately $612,000 and $471,000 for the three months ended March 31, 2012 and 2011, respectively. See Note 12, Subsequent Events, for further discussion.

Note 6. Accrued Allowances

Accrued allowances consist of the following:

	March 31, 2012	December 31, 2011
Accrued returns allowance	$ 4,865,195	$ 5,712,500
Accrued price adjustments	5,176,641	5,450,619
Accrued government program rebates	4,863,343	5,843,290
Total	$ 14,905,179	$ 17,006,409

Note 7. Lines of Credit

On September 8, 2010, the Company entered into a Loan Agreement (the "Loan Agreement") with Regions Bank ("Regions"). The Loan Agreement provides for a $5 million secured revolving line of credit (the "RLOC") and a $5 million secured guidance line of credit (the "GLOC" and together with the RLOC, the "Loans"). The RLOC may be used to fund working capital needs and the GLOC may be used for acquisitions approved by Regions. The Loans mature on September 8, 2012 and bear interest at LIBOR plus 2.5%.

The Loan Agreement contains customary restrictive covenants and events of default, including breaches of representations and warranties and breaches of covenants. As of March 31, 2012, the Company was in compliance with all financial covenants.

In consideration for Regions entering into the Loan Agreement, the Company granted Regions a first priority security interest in substantially all of its assets except for all patents owned by Pernix as well as certain trademarks. Regions is also entitled to a first priority security interest on any intellectual property assets acquired with proceeds from the GLOC.

The outstanding balances under the GLOC and the RLOC were $5,000,000 and $1,000,000, respectively, as of March 31, 2012 and December 31, 2011.

Note 8. Other Revenue Sharing Arrangements

Collaboration Arrangements

The Company enters into collaborative arrangements to develop and commercialize drug candidates. Collaborative activities might include research and development, marketing and selling (including promotional activities and physician detailing), manufacturing, and distribution. These collaborations often require royalty or profit share payments, contingent upon the occurrence of certain future events linked to the success of the product. Revenues related to products sold by the Company pursuant to these arrangements are included in product sales, while other sources of revenue such as royalties and profit share receipts are included in collaboration, royalty and other revenue as further discussed below. Operating expenses for costs incurred pursuant to these arrangements are reported in their respective expense line item.

In March 2012, we entered into a product development agreement with a private company for a prescription product for the pediatrics market. Under the terms of the agreement, Pernix obtained exclusive marketing rights to this late-stage development product in the United States, and Pernix will pay the costs related to the development of the product. Pernix expects to invest approximately $6 million over an estimated 36-month period for development and regulatory expenses related to this product candidate, and Pernix's development partner will manage the development program. Pernix and its development partner expect to commence pivotal phase III studies in the next 12 months.

Co-promotion Agreements

The Company seeks to enter into co-promotion agreements to enhance the promotional efforts and sales of products. The Company may enter into co-promotion agreements whereby it obtains rights to market other parties' products in return for certain commissions or percentages of revenue on the sales Pernix generates. Alternatively, Pernix may enter into co-promotion agreements with respect to its products whereby it grants another party certain rights to market or otherwise promote one or more of its products. Typically, the Company will enter into this type of

co-promotion arrangement when a particular product is not aligned with its product focus or it lacks sufficient sales force representation in a particular geographic area. Co-promotion revenue is included in net revenues. Expense from co-promotion agreements is included in cost of goods sold.

In addition to the co-promotion agreement that the Company has with ParaPRO, the Company also has a Supply and Distribution Agreement. The cost that the Company pays for NATROBA pursuant to the Supply and Distribution Agreement with ParaPRO is significantly higher than the direct manufacturing cost that the Company pays on the other products in our portfolio which impacts our gross profit margin on product sales. NATROBA was launched in August 2011.

	Three Months Ended March 31 ,	
	2012	2011
Pernix Consolidated Gross Margin - including Natroba	68%	N/A
Pernix Consolidated Gross Margin - excluding Natroba	73%	81%

Note 9. Employee Compensation and Benefits

Stock Options

The Company's 2009 Stock Incentive Plan (the "2009 Plan") was approved concurrent with its merger with GTA on March 9, 2010. The maximum number of shares that can be offered under this plan is 5,000,000. Incentives may be granted under the 2009 Plan to eligible participants in the form of (a) incentive stock options, (b) non-qualified stock options, (c) restricted stock, (d) restricted stock units ("RSU"), (e) stock appreciation rights ("SARs") and (f) other stock-based awards.

As of March 31, 2012, approximately 208,333 options remain outstanding that were issued to current officers and directors under prior incentive plans of GTA. The remaining average contractual life of these options is approximately eleven months.

The Company currently uses the Black-Scholes-Merton option pricing model to determine the fair value of its stock options. The determination of the fair value of stock-based payment awards on the date of grant using an option pricing model is affected by the Company's stock price, as well as assumptions regarding a number of complex and subjective variables. These variables include the Company's expected stock price volatility over the term of the awards, actual employee exercise behaviors, risk-free interest rate and expected dividends.

The following table shows the weighted average of the assumptions used to value stock options on the date of grant, as follows:

	Three Months Ended March 31, 2012
Weighted average expected stock price volatility	65.0%
Estimated dividend yield	0.0%
Risk-free interest rate	1.2%
Expected life of option (in years)	6.0
Weighted average fair value per share	5.52

The Company has not paid and does not anticipate paying cash dividends; therefore, the expected dividend rate is assumed to be 0%. The expected stock price volatility for the stock options is based on historical volatility of a representative peer group of comparable companies selected using publicly available industry and market capitalization data. The risk-free rate was based on the U.S. Treasury yield curve in effect at the time of grant commensurate with the expected life assumption. The expected life of the stock options granted was estimated based on the historical exercise patterns over the option lives.

The following table shows the option activity, described above, during the three months ended March 31, 2012:

Option Shares	Shares	Average Exercise Price
Outstanding at December 31, 2011(1)	1,848,491	$ 4.55
Granted	170,000	9.36
Exercised	(25,826)	2.25

Cancelled	(12,166)		4.41
Expired			
Outstanding at March 31, 2012	1,980,499	$	4.99
Vested and exercisable, end of period	507,996	$	4.09

(1)Includes 460,000 options granted to ParaPRO, LLC on August 3, 2011, that vest over seven years, pursuant to the commercial terms of the co-promotion arrangement between the Company and ParaPRO for the marketing and sale of Natroba. For additional information, see Note 8, Other Revenue Sharing Arrangements.

The following table shows the details by range of exercise price for the total options outstanding at March 31, 2012:

	Options Outstanding			Options Exercisable	
Range of Exercise Price ($)		Shares	Remaining Contractual Life (years)	Shares	Price ($)
1.94 - 2.20		25,833	.9	25,833	2.00
3.31 – 4.20	(1)	1,361,166	7.6	453,831	3.90
6.10		193,500	9.4		
7.90 – 9.02		300,000	9.7	13,333	7.90
10.13 – 10.35		100,000	9.5	14,999	10.14
		1,980,499	8.06	507,996	4.09

(1)Includes 460,000 options granted to ParaPRO, LLC on August 3, 2011, that vest over seven years, pursuant to the commercial terms of the co-promotion arrangement between the Company and ParaPRO for the marketing and sale of Natroba. For additional information, see Note 8, Other Revenue Sharing Arrangements.

As of March 31, 2012, the aggregate intrinsic value of 507,996 options outstanding and exercisable was approximately $2,511,000.

As of March 31, 2012, there was approximately $2,930,000 of total unrecognized compensation cost related to unvested stock options issued to employees and directors of the Company, which is expected to be recognized ratably over a weighted-average period of 2.3 years.

Restricted Stock

Amendment to Employment Agreement . On March 23, 2012, the Company, Macoven and John McMahon, Macoven's Vice President of Product Sales, entered into an amendment to Mr. McMahon's amended and restated employment agreement pursuant to which all provisions relating to quarterly bonuses and a bonus pool were removed. The amendment also provided for the issuance of 165,000 shares of restricted stock pursuant to the Company's 2009 Amended and Restated Stock Incentive Plan with certain volume limitations on the sale of such shares after vesting.

Also on March 23, 2012, in connection with the amendment to Mr. McMahon's agreement, the Company granted Michael Venters, Macoven's Executive Vice President of Corporate Development, 85,000 shares of restricted stock pursuant to the Company's 2009 Amended and Restated Stock Incentive Plan with the same volume limitations as Mr. McMahon. Both grants vest in equal installments on each of the first three anniversaries of the date of grant.

Director Compensation. On March 22, 2012, each non-executive director received a grant of options to purchase 10,000 shares of our common stock and a grant of 10,000 shares of restricted stock. The options and restricted stock each vest one-third per year on the first three anniversaries of the grant date. The options were granted at the market price of $9.02, the closing market price on March 21, 2012. In addition, our Board approved a $5,000 increase in the annual cash compensation of the non-executive Chairman.

15

The following table shows the Company's nonvested restricted stock outstanding at March 31, 2012:

Restricted Stock Shares	Shares	Weighted Average Grant Date Fair Value
Nonvested at December 31, 2011	120,002	$ 6.56
Granted	290,000	8.61
Vested	(48,335)	6.11
Forfeited		
Nonvested at March 31, 2012	361,667	$ 8.27

During the three months ended March 31, 2012, 290,000 restricted common shares were issued as described above. Approximately $2,905,000 of total unrecognized compensation expense related to unvested restricted stock is expected to be recognized over a weighted-average period of 2.8 years.

Employee Stock Purchase Plan

Effective July 22, 2010, the Company adopted the 2010 Employee Stock Purchase Plan to provide substantially all employees an opportunity to purchase shares of its common stock through payroll deduction, up to 10% of eligible compensation with a $25,000 maximum deferral. Semi-annually (on May 1st and November 1st), participant account balances may be used to purchase shares of stock at the lesser of 85 percent of the fair market value of shares at the beginning or ending of such six-month period. The Employee Stock Purchase Plan expires on July 22, 2020. A total of 1,000,000 shares are available for purchase under this plan. Compensation expense related to the Employee Stock Purchase Plan and included in the table below for the three months ended March 31, 2012 was approximately $22,000.

Stock-Based Compensation Expense

The following table shows the approximate amount of total stock-based compensation expense recognized for employees and non-employees:

	Three Months Ended March 31,	
	2012	2011
Employees	$ 338,000	$ 145,000
Non-employees/Directors	158,000	66,000
Total	$ 496,000	$ 211,000

Note 10. Income Taxes

The income tax provision consisted of the income tax expense (benefit) for the three months ended March 31, 2012 and 2011, as presented in the table below.

	Three Months Ended March 31,	
	2012	2011
Current:		
Federal	$ 310,000	$ 1,458,000
State	47,000	243,000
	357,000	1,701,000