ADVANCED MEDICAL OPTICS INC
Form 10-Q
November 02, 2004

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**UNITED STATES**
**SECURITIES AND EXCHANGE COMMISSION**
**WASHINGTON, D.C. 20549**

**FORM 10-Q**

**(Mark One)**

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

**For the quarterly period ended September 24, 2004**

or

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

**For the transition period from to .**

**COMMISSION FILE NUMBER 001-31257**

**ADVANCED MEDICAL OPTICS, INC.**

(Exact name of registrant as specified in its charter)

| | |
|---|---|
| **Delaware**<br>(State or other jurisdiction of incorporation or organization) | **33-0986820**<br>(I.R.S. Employer Identification No.) |
| **1700 E. St. Andrew Place**<br>**Santa Ana, California**<br>(Address of principal executive offices) | **92705**<br>(Zip Code) |

Registrant s telephone number, including area code **714/247-8200**

Indicate by a check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.

Yes x No o

Indicate by check mark whether the registrant is an accelerated filer (as defined in Rule 12b-2 of the Exchange Act).

Yes x No o

As of October 27, 2004, there were 36,712,987 shares of common stock outstanding.

ADVANCED MEDICAL OPTICS, INC.
FORM 10-Q FOR THE QUARTER ENDED SEPTEMBER 24, 2004

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PART I FINANCIAL INFORMATION

Item 1. Financial Statements

Advanced Medical Optics, Inc.

Unaudited Condensed Consolidated Statements of Operations

(In thousands, except per share data)

| | Three Months Ended | | Nine Months Ended | |
|---|---|---|---|---|
| | September 24, 2004 | September 26, 2003 | September 24, 2004 | September 26, 2003 |
| Net sales | $198,366 | $151,152 | $ 517,414 | $434,464 |
| Cost of sales | 88,894 | 57,045 | 212,577 | 163,763 |
| Gross profit | 109,472 | 94,107 | 304,837 | 270,701 |
| Selling, general and administrative | 88,533 | 67,600 | 236,620 | 205,106 |
| Research and development | 11,830 | 9,256 | 31,043 | 26,996 |
| In-process research and development | 28,100 | | 28,100 | |
| Operating income (loss) | (18,991) | 17,251 | 9,074 | 38,599 |
| Non-operating expense (income): | | | | |
| Interest expense | 8,377 | 5,888 | 19,327 | 20,442 |
| Unrealized gain on derivative instruments | (304) | (341) | (830) | (59) |
| Other, net | 4,708 | 17,896 | 127,977 | 17,161 |
| | 12,781 | 23,443 | 146,474 | 37,544 |
| Earnings (loss) before income taxes | (31,772) | (6,192) | (137,400) | 1,055 |
| Provision (benefit) for income taxes | (64) | (2,528) | 2,103 | 443 |
| Net earnings (loss) | $ (31,708) | $ (3,664) | $(139,503) | $ 612 |
| Net earnings (loss) per share : | | | | |
| Basic | $ (0.89) | $ (0.13) | $ (4.36) | $ 0.02 |

| | | | | |
|---|---|---|---|---|
| Diluted | $ (0.89) | $ (0.13) | $ (4.36) | $ 0.02 |
| Weighted average number of shares outstanding: | | | | |
| Basic | 35,711 | 29,110 | 31,977 | 28,962 |
| Diluted | 35,711 | 29,110 | 31,977 | 29,274 |

See accompanying notes to unaudited condensed consolidated financial statements.

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Advanced Medical Optics, Inc.

Unaudited Condensed Consolidated Balance Sheets
(In thousands)

| | September 24, 2004 | December 31, 2003 |
|---|---|---|
| ASSETS | | |
| Current assets | | |
| Cash and equivalents | $ 34,098 | $ 46,104 |
| Trade receivables, net | 180,919 | 130,423 |
| Inventories | 90,665 | 41,596 |
| Other current assets | 35,922 | 34,369 |
| Total current assets | 341,604 | 252,492 |
| Property, plant and equipment, net | 108,556 | 68,136 |
| Other assets | 36,146 | 34,635 |
| Intangibles, net | 134,157 | 369 |
| Goodwill | 360,798 | 105,713 |
| Total assets | $ 981,261 | $ 461,345 |
| LIABILITIES AND STOCKHOLDERS EQUITY | | |
| Current liabilities | | |
| Current portion of long-term debt | $ 2,050 | $ 2,328 |
| Accounts payable | 71,863 | 35,605 |
| Accrued compensation | 29,526 | 24,507 |
| Other accrued expenses | 64,314 | 52,861 |
| Total current liabilities | 167,753 | 115,301 |
| Long-term debt, net of current portion | 566,392 | 233,611 |
| Other liabilities | 53,535 | 19,241 |
| Stockholders equity: | | |
| Preferred stock, $.01 par value; authorized 5,000,000 shares; none issued | | |
| Common stock, $.01 par value; authorized 120,000,000 shares; issued 36,602,060 and 29,378,599 shares | 366 | 294 |
| Additional paid-in capital | 300,173 | 54,064 |
| Retained earnings (accumulated deficit) | (114,522) | 24,981 |
| Accumulated other comprehensive income | 7,587 | 13,868 |
| Less treasury stock, at cost (1,379 and 997 shares) | (23) | (15) |

| | | |
|---|---|---|
| Total stockholders equity | 193,581 | 93,192 |
| Total liabilities and stockholders equity | $ 981,261 | $ 461,345 |

See accompanying notes to unaudited condensed consolidated financial statements.

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Advanced Medical Optics, Inc.

Unaudited Condensed Consolidated Statements of Cash Flows
(In thousands)

| | Nine Months Ended | |
|---|---|---|
| | **September 24, 2004** | **September 26, 2003** |
| Cash flows provided by operating activities: | | |
| Net earnings (loss) | $(139,503) | $ 612 |
| Non cash items included in net earnings (loss): | | |
| Amortization and write-off of original issue discount and debt issuance costs | 9,860 | 9,140 |
| Amortization and write-off of net realized gain on interest rate swaps | (3,466) | (2,498) |
| Depreciation and amortization | 14,970 | 11,618 |
| In-process research and development | 28,100 | |
| Loss on exchange of convertible senior subordinated notes | 110,729 | |
| Loss on investments and assets | 748 | 639 |
| Unrealized gain on derivative instruments | (830) | (59) |
| Expense of compensation plan | 152 | 64 |
| Changes in assets and liabilities, net of effect of acquisition: | | |
| Trade receivables, net | (52,279) | (5,477) |
| Inventories | 3,055 | 3,538 |
| Other current assets | (1,715) | 4,533 |
| Accounts payable | 36,400 | 533 |
| Accrued expenses and other liabilities | 3,625 | (5,725) |
| Other non-current assets | (1,885) | (5,491) |
| Net cash provided by operating activities | 7,961 | 11,427 |
| Cash flows from investing activities: | | |
| Acquisition of business, net of cash acquired | (456,709) | |
| Additions to property, plant and equipment | (9,018) | (6,157) |
| Proceeds from the sale of property, plant and equipment | 35 | 264 |
| Additions to capitalized internal-use software | (739) | (172) |
| Additions to demonstration and bundled equipment | (5,104) | (5,363) |
| Net cash used in investing activities | (471,535) | (11,428) |
| Cash flows from financing activities: | | |
| Proceeds from issuance of convertible senior subordinated notes | 350,000 | 140,000 |
| Borrowings under term loans | 250,000 | 22,376 |
| Repayment of long-term debt | (138,236) | (205,000) |
| Financing related costs | (16,553) | (7,316) |
| Proceeds from the issuance of common stock | 5,087 | 2,898 |
| Net proceeds from settlement of interest rate swaps | | 582 |
| Purchase of treasury stock | (8) | (120) |

| | | |
|---|---|---|
| Net cash provided by (used in) financing activities | 450,290 | (46,580) |
| Effect of exchange rates on cash and equivalents | 1,278 | 1,212 |
| Net decrease in cash and equivalents | (12,006) | (45,369) |
| Cash and equivalents at beginning of period | 46,104 | 80,578 |
| Cash and equivalents at end of period | $ 34,098 | $ 35,209 |
| Supplemental non-cash financing activity | | |
| Exchange of convertible notes into common stock | $ 126,558 | $ |

See accompanying notes to unaudited condensed consolidated financial statements.

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Advanced Medical Optics, Inc.

Notes to Unaudited Condensed Consolidated Financial Statements

Note 1: Basis of Presentation

In the opinion of management, the accompanying unaudited condensed consolidated financial statements contain all adjustments necessary (consisting only of normal recurring accruals) to present fairly the financial information contained therein. These statements do not include all disclosures required by accounting principles generally accepted in the United States of America for annual financial statements and should be read in conjunction with the audited consolidated financial statements of the Company for the year ended December 31, 2003. The results of operations for the three and nine months ended September 24, 2004 are not necessarily indicative of the results to be expected for the year ending December 31, 2004.

All material intercompany balances have been eliminated.

Certain reclassifications of prior year amounts have been made to conform with current year presentation.

*Stock-Based Compensation*

The Company measures stock-based compensation for option grants to employees and members of the board of directors using the intrinsic value method. Restricted stock awards are valued based on the market price of a share of nonrestricted stock on the grant date. No compensation expense has been recognized for stock-based incentive compensation plans other than for restricted stock awards. Had compensation expense for the Company s stock options and employee stock purchase plans been recognized based upon the fair value for awards granted, the Company s net earnings (loss) would have been decreased (increased) to the following pro forma amounts (in thousands, except per share data):

| | **Three Months Ended** | | **Nine Months Ended** | |
|---|---|---|---|---|
| | **September 24, 2004** | **September 26, 2003** | **September 24, 2004** | **September 26, 2003** |
| Net earnings (loss): | | | | |
| As reported | $(31,708) | $ (3,664) | $(139,503) | $ 612 |
| Stock-based compensation expense included in reported net earnings (loss), net of tax | 43 | 23 | 99 | 38 |
| Stock-based compensation expense determined under fair value based method, net of tax | (2,419) | (1,122) | (4,720) | (3,720) |
| Pro forma | $(34,084) | $ (4,763) | $(144,124) | $ (3,070) |

Earnings (loss) per share:

| | | | | |
|---|---|---|---|---|
| As reported: | | | | |
| Basic | $ (0.89) | $ (0.13) | $ (4.36) | $ 0.02 |
| Diluted | $ (0.89) | $ (0.13) | $ (4.36) | $ 0.02 |
| Pro forma Basic and Diluted | $ (0.95) | $ (0.16) | $ (4.51) | $ (0.11) |

These pro forma effects are not indicative of future amounts. The Company expects to grant additional awards in the future.

*Acquired In-Process Research and Development*

Costs to acquire in-process research and development (IPR&D) projects and technologies which have no alternative future use and which have not reached technological feasibility at the date of acquisition are expensed as incurred (see Note 2, Acquisition of Pfizer Inc. Surgical Ophthalmic Business ).

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Advanced Medical Optics, Inc.
Notes to Unaudited Condensed Consolidated Financial Statements (continued)

*Recently Adopted and Issued Accounting Standards*

In March 2004, the Emerging Issues Task Force finalized its consensus on EITF Issue 03-6, Participating Securities and the Two-Class Method Under FASB Statement No. 128, Earnings Per Share (EITF 03-6). EITF 03-6 clarifies what constitutes a participating security and requires the use of the two-class method for computing basic earnings per share when participating convertible securities exist. EITF 03-6 is effective for fiscal periods beginning after March 31, 2004. Adoption of EITF 03-6 did not have an effect on our consolidated financial statements.

In September 2004, the Emerging Issues Task Force finalized its consensus on EITF Issue No. 04-8, The Effect of Contingently Convertible Debt on Diluted Earnings Per Share (EITF 04-8). EITF 04-8 addresses when the dilutive effect of contingently convertible debt with a market price trigger should be included in diluted earnings per share (EPS). Under EITF 04-8, the market price contingency should be ignored and these securities should be treated as non-contingent, convertible securities and always included in the diluted EPS computation. EITF 04-8 requires these securities be included in diluted EPS using either the if-converted method or the net share settlement method, depending on the conversion terms of the security. EITF 04-8 is effective for all periods ending after December 15, 2004 and is to be applied by retrospectively restating previously reported EPS. The Company expects to irrevocably elect to cash settle the principal amount of the Notes (as defined in Note 4) and thus, the dilutive effect of the Notes would be calculated under the net share settlement method. Adoption of EITF 04-8 would not have an impact on reported EPS for the three and nine months ended September 24, 2004 or the three months ended September 26, 2003 as we reported a loss for all such periods. Adoption of EITF 04-8 would not have an impact on reported EPS for the nine months ended September 26, 2003 or the year ended December 31, 2003, as the impact of the Existing Notes (as defined in Note 4) is antidilutive.

Note 2: Acquisition of Pfizer Inc. Surgical Ophthalmic Business

On June 26, 2004, pursuant to a stock and asset purchase agreement dated as of April 21, 2004, the Company completed the purchase of Pfizer Inc. s surgical ophthalmic business for $450 million in cash (Acquisition). Pfizer s surgical ophthalmic business manufactured and marketed surgical devices for the eyes. The Company acquired ophthalmic surgical products and certain manufacturing and research and development facilities located in Uppsala, Sweden, Groningen, Netherlands and Bangalore, India. The products acquired include the *Healon*® line of viscoelastic products used in ocular surgery, the *CeeOn*® and *Tecnis*® intraocular lenses and the *Baerveldt*® glaucoma shunt.

The primary reason for the Acquisition is to strengthen the Company s position in the global ophthalmic surgical industry by expanding its product portfolio and its manufacturing and research and development expertise.

The Acquisition has been accounted for as a purchase business combination. Under the purchase method of accounting, the assets acquired and liabilities assumed are recorded at the date of acquisition at their respective fair values.

The results of operations of the Acquisition have been included in the accompanying unaudited condensed consolidated statements of operations from the date of acquisition. The total estimated cost of the Acquisition is as follows (in thousands):

| | |
|---|---|
| Cash consideration to Pfizer Inc. | $450,000 |

| | |
|---|---|
| Direct costs | 7,399 |
| Cash acquired | (690) |
| Total purchase price | $456,709 |

The above purchase price has been preliminarily allocated based on an estimate of the fair values of assets acquired and liabilities assumed. The final valuation of net assets is expected to be completed as soon as possible, but no later than one year from the acquisition date in accordance with generally accepted accounting principles.

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Advanced Medical Optics, Inc.
Notes to Unaudited Condensed Consolidated Financial Statements (continued)

The purchase price has been allocated based on management s estimates as follows (in thousands):

| | |
|---|---|
| Inventories | $ 52,411 |
| Other current assets | 350 |
| Property, plant and equipment | 39,066 |
| Intangible assets | 135,900 |
| In-process research and development | 28,100 |
| Goodwill | 258,812 |
| Current liabilities | (14,601) |
| Non-current liabilities | (655) |
| Non-current deferred tax liability | (42,674) |
| Net assets acquired | $456,709 |

Of the $135.9 million of acquired intangible assets, $121.0 million was assigned to developed technology rights that have a weighted-average useful life of approximately 12.7 years and $14.9 million was assigned to a trademark with a useful life of approximately 13.5 years. Approximately $11.6 million of the goodwill is expected to be deductible for tax purposes. A history of operating margins and profitability, a strong scientific employee base and a strong presence in the viscoelastic market were among the factors that contributed to a purchase price resulting in the recognition of goodwill.

*In-process research and development*

Approximately $28.1 million of the purchase price represents the estimated fair value of projects that, as of the acquisition date, had not reached technological feasibility and had no alternative future use. Accordingly, this amount was immediately expensed in the unaudited condensed consolidated statements of operations for the three and nine months ended September 24, 2004. The estimated fair value assigned to IPR&D is comprised of the following projects (in thousands):

| | Value of IPR&D Acquired |
|---|---|
| Tecnis® Monofocal | $ 1,600 |
| Tecnis® Multifocal | 26,500 |
| Total | $28,100 |

The estimated fair value of these projects was determined based on a discounted cash flow model. For each project, the estimated after-tax cash flows were probability weighted to take into account the stage of completion and the risks surrounding the successful development and commercialization. These cash flows were then discounted to a present value using a discount rate of 14.5%. In addition, solely for the purposes of estimating the fair value of these IPR&D projects, the following assumptions were made:

Revenue that is reasonably likely to result from the approved and unapproved, potential uses of identifiable intangible assets that includes the estimated number of units to be sold, estimated selling prices, estimated market penetration and estimated market share and year-over-year growth rates over the product cycles;

Regulatory approval for the Tecnis® monofocal lens in Japan is expected in 2005, based on results of current trials. Management also estimates that the Tecnis® multifocal lens will receive its PMA in the U.S. from the FDA in 2007, with approval in Japan in 2008. The time frame and clinical roadmaps for the devices are based on management s estimates;

Remaining developmental R&D and sustaining engineering expenses once commercialized were also estimated by management according to internal planning estimates;

Cost of goods sold was assumed to be similar to the current commercialized versions of Tecnis® lenses and includes a direct distribution cost burden; and

Advanced Medical Optics, Inc.
Notes to Unaudited Condensed Consolidated Financial Statements (continued)

Margins for the promotion, marketing, and sales expenses were assumed at the same level as those for commercialized IOL and viscoelastic franchises and include assumed increases in staffing required to realize estimated worldwide sales expectations.

The major risks and uncertainties associated with the timely and successful completion of these projects consist of the ability to confirm the safety and efficacy of the technology based on the data from clinical trials and obtaining necessary regulatory approvals. In addition, no assurance can be given that the underlying assumptions used to forecast the cash flows or the timely and successful completion of such projects will materialize, as estimated. For these reasons, among others, actual results may vary significantly from the estimated results.

The following unaudited pro forma information assumes the Acquisition occurred on January 1, 2003. These unaudited pro forma results have been prepared for informational purposes only and do not purport to represent what the results of operations would have been had the Acquisition occurred as of the date indicated, nor of future results of operations. The unaudited pro forma results for the nine months ended September 24, 2004 and for the three and nine months ended September 26, 2003 are as follows (in thousands, except per share data):

| | Nine Months Ended September 24, 2004 | Three Months Ended September 26, 2003 | Nine Months Ended September 26, 2003 |
|---|---|---|---|
| Net sales | $ 592,291 | $ 183,572 | $ 547,942 |
| Net earnings (loss) | 31,493 (1) | (5,070) (2) | 8,169 (3) |
| Earnings (loss) per share: | | | |
| Basic (4) | $ 0.81 | $ (0.14) | $ 0.23 |
| Diluted (5) | $ 0.77 | $ (0.14) | $ 0.23 |

(1) The unaudited pro forma information for the nine months ended September 24, 2004 excludes the following non-recurring charges: incremental cost of sales of $14.1 million from the sale of acquired inventory adjusted to fair value; a $28.1 million in-process research and development charge; a charge of $5.2 million for the write-off of debt issuance costs, one-time commitment fee and original issue discount, net of the recognition of realized gains on interest rate swaps; and early debt extinguishment costs of $126.2 million. The unaudited pro forma information also reflects a $2.3 million decrease in depreciation and amortization related to the estimated fair value of property, plant and equipment and identifiable intangible assets and a $9.7 million increase in interest expense resulting from the recapitalization to fund the Acquisition.

(2) The unaudited pro forma information for the three months ended September 26, 2003 reflects a net $0.6 million decrease in depreciation and amortization related to the estimated fair value of property, plant and equipment and identifiable intangible assets and a $2.4 million increase in interest expense resulting from the recapitalization to fund the Acquisition.

(3) The unaudited pro form information for the nine months ended September 26, 2003 reflects a $1.8 million increase in depreciation and amortization related to the estimated fair value of property, plant and equipment and identifiable intangible assets and a $9.5 million increase in interest expense resulting from the recapitalization to fund the Acquisition.

(4) The weighted average number of shares outstanding used for computation of basic earnings (loss) per share for each of the periods presented include an additional 6.8 million shares exchanged for approximately $126.6 million

aggregate principal amount of 3½% convertible senior subordinated notes (see Note 4).

(5) The weighted average number of shares outstanding used for computation of diluted earnings per share for the nine months ended September 24, 2004 includes the aggregate dilutive effect of approximately 2.2 million shares for stock options and the remaining 3½% convertible senior subordinated notes. The weighted average number of shares outstanding used for computation of diluted earnings per share for the nine months ended September 26, 2003 includes the dilutive effect of approximately 0.3 million shares for stock options.

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Advanced Medical Optics, Inc.
Notes to Unaudited Condensed Consolidated Financial Statements (continued)

Note 3: Composition of Certain Financial Statement Captions

The components of inventories were as follows:

| (In thousands) | September 24, 2004 | December 31, 2003 |
|---|---|---|
| Finished goods, including inventory on consignment with customers of $9,420 and $6,696 in 2004 and 2003, respectively | $ 73,814 | $ 37,255 |
| Work in process | 5,268 | 1,056 |
| Raw materials | 11,583 | 3,285 |
| | $ 90,665 | $ 41,596 |

The components of amortizable intangibles and goodwill were as follows:

*Intangibles*

| | September 24, 2004 | | December 31, 2003 | |
|---|---|---|---|---|
| (In thousands) | Gross Amount | Accumulated Amortization | Gross Amount | Accumulated Amortization |
| Amortized Intangible Assets: | | | | |
| Technology Rights | $121,000 | $(2,388) | $ | $ |
| Trade Name | 14,900 | (276) | | |
| Licensing | 4,590 | (3,950) | 3,940 | (3,940) |
| Trademarks | 572 | (291) | 572 | (203) |
| | $141,062 | $(6,905) | $4,512 | $(4,143) |

The technology rights and trade name were acquired in the Acquisition (see Note 2).

Amortization expense of intangible assets for the three and nine months ended September 24, 2004 was $2.7 million and $2.8 million, respectively. Amortization expense of intangible assets for the three and nine months ended September 26, 2003 was immaterial. Amortization expense is expected to be approximately $5.3 million in 2004, $10.7 million in 2005, 2006 and 2007 and $10.5 million in 2008.

*Goodwill*

| **(In thousands)** | **September 24, 2004** | **December 31, 2003** |
|---|---|---|
| Goodwill: | | |
| United States | $ 12,783 | $ 12,783 |
| Japan | 27,007 | 28,144 |
| Manufacturing operations | 321,008 | 64,786 |
| | $360,798 | $105,713 |

The change in goodwill is due to goodwill acquired in the Acquisition (see Note 2) and foreign currency fluctuations.

Note 4: Debt and Interest Rate Swap Agreements

On June 22, 2004, the Company issued $350.0 million of 2½% convertible senior subordinated notes due July 15, 2024 (Notes). Interest on the Notes is payable on January 15 and July 15 of each year, commencing on January 15, 2005. The Notes are convertible into 19.9045 shares of AMO s common stock for each $1,000 principal amount of Notes (conversion price of approximately $50.24 per share), subject to adjustment. The Notes may be converted, at the option of the holders, on or prior to the final maturity date under certain circumstances, including:

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Advanced Medical Optics, Inc.
Notes to Unaudited Condensed Consolidated Financial Statements (continued)

during any fiscal quarter commencing after September 24, 2004, if the closing sale price per share of AMO s common stock exceeds 130% of the conversion price for at least 20 trading days in the 30 consecutive trading day period ending on the last trading day of the preceding fiscal quarter;

during the five business days after any five consecutive trading day period in which the trading price of the Notes for each day was less than 95% of the conversion value of the Notes; provided that holders may not convert their Notes in reliance on this provision after July 15, 2019, if on any trading day during such trading period the closing sale price per share of AMO s common stock was between 100% and 130% of the then current conversion price;

upon the occurrence of specified ratings events with respect to the Notes. This conversion feature represents an embedded derivative. However, based on the de minimis value associated with this feature, no value has been assigned at issuance and at September 24, 2004;

if the Notes have been called for redemption;

if a fundamental change occurs; or

upon the occurrence of specified corporate events.

Upon conversion, the Company has the right to deliver, in lieu of shares of common stock, cash or a combination of cash and shares of common stock. Under the indenture for the Notes, the Company may irrevocably elect to satisfy in cash the conversion obligation with respect to the principal amount of the Notes and expects to make such election prior to December 31, 2004.

The Company may redeem some or all of the Notes for cash, on or after January 20, 2010, for a price equal to 100% of the principal amount plus accrued and unpaid interest, including contingent interest, if any, to but excluding the redemption date.

The Notes contain put options, which may require the Company to repurchase all or a portion of the Notes on January 15, 2010, July 15, 2014, and July 15, 2019 at a repurchase price of 100% of the principal amount plus accrued and unpaid interest, including contingent interest, if any, to but excluding the repurchase date. The Company may choose to pay the repurchase price in cash, shares of common stock or a combination of cash and shares of common stock.

Beginning with the six-month interest period commencing January 15, 2010, holders of the Notes will receive contingent interest payments during any six-month interest period if the trading price of the Notes for each of the five trading days ending on the second trading day immediately preceding the first day of the applicable six-month interest period equals or exceeds 120% of the principal amount of the Notes. The contingent interest payable will equal 0.25% of the average trading price of $1,000 principal amount of Notes during the five trading days immediately preceding the first day of the applicable six-month interest period. This contingent interest payment feature represents an embedded derivative. However, based on the de minimis value associated with this feature, no value has been assigned at issuance and at September 24, 2004.

On or prior to January 15, 2010, upon the occurrence of a fundamental change, under certain circumstances, the Company will pay a make whole premium on Notes converted in connection with, or tendered for repurchase upon, the fundamental change. The make whole premium will be payable, in the same form of consideration into which the

Company s common stock has been exchanged or converted, on the repurchase date for the Notes after the fundamental change, both for Notes tendered for repurchase and for Notes converted in connection with the fundamental change. The amount of the make whole premium, if any, will be based on the Company s stock price on the effective date of the fundamental change. This make whole premium feature represents an embedded derivative. However, based on the de minimis value associated with this feature, no value has been assigned at issuance and at September 24, 2004.

On June 25, 2004, the Company amended and re