UNITED STATES SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

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

FOR THE QUARTERLY PERIOD ENDED MARCH 31, 2013

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

FOR THE TRANSITION PERIOD FROM TO .

Commission File No. 001-31298

LANNETT COMPANY, INC.

(Exact Name of Registrant as Specified in its Charter)

State of Delaware	**23-0787699**
(State of Incorporation)	(I.R.S. Employer I.D. No.)

9000 State Road

Philadelphia, PA 19136

(215) 333-9000

(Address of principal executive offices and telephone number)

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Exchange Act during the past 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 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 x No o

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See the definitions of large accelerated filer, accelerated filer and smaller reporting company in Rule 12b-2 of the Exchange Act. (Check one):

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

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12B-12 of the Exchange Act). Yes x No o

Indicate the number of shares outstanding of each class of the registrant s common stock, as of the latest practical date.

Class	**Outstanding as of April 30, 2013**
Common stock, par value $0.001 per share	28,683,685

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PART I. FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS

LANNETT COMPANY, INC. AND SUBSIDIARIES

CONSOLIDATED BALANCE SHEET

(In thousands, except share and per share data)	(Unaudited) March 31, 2013	June 30, 2012
ASSETS		
Current Assets		
Cash and cash equivalents	$ 33,066	$ 22,562
Investment securities	5,906	6,667
Trade accounts receivable (net of allowance of $84 and $124, respectively)	39,810	42,212
Inventories, net	32,847	27,064
Prepaid income taxes	213	2,120
Deferred tax assets	5,253	4,833
Other current assets	1,851	1,023
Total Current Assets	118,946	106,481
Property, plant and equipment, net	39,288	37,068
Intangible assets, net	3,017	4,429
Deferred tax assets	8,024	9,069
Other assets	956	1,171
TOTAL ASSETS	$ 170,231	$ 158,218
LIABILITIES		
Current Liabilities		
Accounts payable	$ 15,709	$ 17,989
Accrued expenses	2,053	1,518
Accrued payroll and payroll related	5,347	3,198
Current portion of long-term debt	657	648
Rebates, chargebacks and returns payable	16,550	17,039
Total Current Liabilities	40,316	40,392
Long-term debt, less current portion	6,125	6,513
TOTAL LIABILITIES	46,441	46,905
Commitment and Contingencies, See notes 13 and 14		
SHAREHOLDERS EQUITY		
Common stock - authorized 50,000,000 shares, par value $0.001; issued 29,103,931 and 28,594,437 shares, respectively; outstanding, 28,668,052 and 28,252,192 shares, respectively	29	29
Additional paid-in capital	102,702	99,515
Retained earnings	22,990	13,236
Accumulated other comprehensive loss	(79)	(63)
Treasury stock at cost 435,879 and 342,245 shares, respectively	(2,034)	(1,594)
Total Shareholders Equity Attributable to Lannett Company, Inc.	123,608	111,123

Noncontrolling Interest		182		190
TOTAL SHAREHOLDERS EQUITY		123,790		111,313
TOTAL LIABILITIES AND SHAREHOLDERS EQUITY	$	170,231	$	158,218

The accompanying notes to the consolidated financial statements are an integral part of these statements.

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LANNETT COMPANY, INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF OPERATIONS

(UNAUDITED)

(In thousands, except share and per share data)	**Three months ended March 31, 2013**	**2012**	**Nine months ended March 31, 2013**	**2012**
Net sales	$ 39,022	$ 30,688	$ 110,880	$ 87,300
Cost of sales	23,321	19,276	67,105	58,789
Amortization of intangible assets	471	471	1,412	1,409
Product royalties	60	50	146	168
Gross profit	15,170	10,891	42,217	26,934
Research and development expenses	5,229	2,911	12,565	7,850
Selling, general, and administrative expenses	5,245	5,616	16,571	14,780
Operating income	4,696	2,364	13,081	4,304
Other income (expense):				
Foreign currency gain (loss)		(3)	3	(6)
Gain on sale of assets	93		51	4
Realized gain on investments	353	361	449	215
Unrealized gain (loss) on investments	185	105	394	(46)
Litigation settlement			1,250	
Interest and dividend income	22	28	84	117
Interest expense	(59)	(64)	(194)	(214)
	594	427	2,037	70
Income before income tax expense	5,290	2,791	15,118	4,374
Income tax expense	1,327	1,057	5,353	1,788
Net income	3,963	1,734	9,765	2,586
Less net income attributable to noncontrolling interest	(16)	(16)	(11)	(53)
Net income attributable to Lannett Company, Inc.	$ 3,947	$ 1,718	$ 9,754	$ 2,533
Basic earnings per common share - Lannett Company, Inc.	$ 0.14	$ 0.06	$ 0.34	$ 0.09
Diluted earnings per common share - Lannett Company, Inc.	$ 0.14	$ 0.06	$ 0.34	$ 0.09
Basic weighted average common shares outstanding	28,490,175	28,571,062	28,371,189	28,509,595
Diluted weighted average common shares outstanding	29,115,941	28,719,669	28,644,831	28,668,281

The accompanying notes to the consolidated financial statements are an integral part of these statements.

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LANNETT COMPANY, INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME

(UNAUDITED)

(In thousands)	Three months ended March 31, 2013	Three months ended March 31, 2012	Nine months ended March 31, 2013	Nine months ended March 31, 2012
Net Income	$ 3,963	$ 1,734	$ 9,765	$ 2,586
Foreign currency translation adjustments	(53)	(7)	(16)	(41)
Unrealized holding loss on securities		(1)		(3)
Tax effect		1		1
Total Other Comprehensive Loss, net of tax	(53)	(7)	(16)	(43)
Comprehensive Income	3,910	1,727	9,749	2,543
Less: Total Comprehensive Income attributable to noncontrolling interest	(16)	(16)	(11)	(53)
Comprehensive Income attributable to Lannett Company Inc.	$ 3,894	$ 1,711	$ 9,738	$ 2,490

The accompanying notes to the consolidated financial statements are an integral part of these statements.

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LANNETT COMPANY, INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENT OF CHANGES IN SHAREHOLDERS EQUITY

(UNAUDITED)

	Shareholders Equity Attributable to Lannett Company, Inc.								
	Common Stock								
(In thousands)	**Shares Issued**	**Amount**	**Additional Paid-In Capital**	**Retained Earnings**	**Accumulated Other Comprehensive Loss**	**Treasury Stock**	**Shareholders Equity Attributable to Lannett Co., Inc.**	**Noncontrolling Interest**	**Total Shareholders Equity**
Balance, July 1, 2012	28,594	$ 29	$ 99,515	$ 13,236	$ (63)	$ (1,594)	$ 111,123	$ 190	$ 111,313
Shares issued in connection with share-based compensation plans	510		1,995				1,995		1,995
Share-based compensation			1,192				1,192		1,192
Purchase of treasury stock						(440)	(440)		(440)
Other comprehensive income, net of income tax					(16)		(16)		(16)
Distribution to noncontrolling interest								(19)	(19)
Net income				9,754			9,754	11	9,765
Balance, March 31, 2013	29,104	$ 29	$ 102,702	$ 22,990	$ (79)	$ (2,034)	$ 123,608	$ 182	$ 123,790

The accompanying notes to the consolidated financial statements are an integral part of these statements.

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LANNETT COMPANY, INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENT OF CASH FLOWS

(UNAUDITED)

(In thousands)	**Nine months ended March 31, 2013**	**2012**
OPERATING ACTIVITIES:		
Net income	$ 9,765	$ 2,586
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	4,622	4,206
Deferred tax expense	625	1,371
Share-based compensation expense	1,192	1,659
Gain on sale of assets	(51)	(4)
Realized gain on investments	(449)	(215)
Unrealized (gain) loss on investments	(394)	46
Gain on litigation settlement	(1,250)	
Proceeds from litigation settlement	1,250	
Other noncash expenses	12	10
Changes in assets and liabilities which provided (used) cash:		
Trade accounts receivable	2,402	(4,035)
Inventories	(5,783)	(1,073)
Prepaid income taxes	1,907	431
Prepaid expenses and other assets	(395)	(559)
Accounts payable	(2,280)	(2,624)
Accrued expenses	535	(184)
Rebates, chargebacks and returns payable	(489)	1,830
Accrued payroll and payroll related	2,149	1,225
Net cash provided by operating activities	13,368	4,670
INVESTING ACTIVITIES:		
Purchases of property, plant and equipment	(5,889)	(4,186)
Proceeds from sale of property, plant and equipment	279	7
Proceeds from sale of investment securities	17,646	32,639
Purchase of investment securities	(16,041)	(18,662)
Net cash provided by (used in) investing activities	(4,005)	9,798
FINANCING ACTIVITIES:		
Repayments of debt	(379)	(401)
Proceeds from issuance of stock	1,995	191
Purchase of treasury stock	(440)	(479)
Tax shortfall on stock options exercised		(7)
Distribution to noncontrolling interests	(19)	(19)
Net cash provided by (used in) financing activities	1,157	(715)
Effect of foreign currency rates on cash and cash equivalents	(16)	(41)
NET INCREASE IN CASH AND CASH EQUIVALENTS	10,504	13,712
CASH AND CASH EQUIVALENTS, BEGINNING OF PERIOD	22,562	5,277

CASH AND CASH EQUIVALENTS, END OF PERIOD	$	33,066	$	18,989
SUPPLEMENTAL DISCLOSURE OF CASH FLOW INFORMATION -				
Interest paid	$	194	$	213
Income taxes paid (refunded)	$	2,821	$	(7)

The accompanying notes to the consolidated financial statements are an integral part of these statements.

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LANNETT COMPANY, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - UNAUDITED

(In thousands, unless otherwise noted and per share data)

Note 1. Interim Financial Information

The accompanying unaudited financial statements have been prepared in accordance with U.S. generally accepted accounting principles for presentation of interim financial statements and with the instructions to Form 10-Q and Article 10 of Regulation S-X. Accordingly, the unaudited financial statements do not include all the information and footnotes necessary for a comprehensive presentation of the financial position, results of operations, and cash flows for the periods presented. In the opinion of management, the unaudited financial statements include all the normal recurring adjustments that are necessary for a fair presentation of the financial position, results of operations, and cash flows for the periods presented. Operating results for the three and nine months ended March 31, 2013 are not necessarily indicative of the results that may be expected for the fiscal year ending June 30, 2013. You should read these unaudited financial statements in combination with the other Notes in this section; Management s Discussion and Analysis of Financial Condition and Results of Operations appearing in Item 2; and the Financial Statements, including the Notes to the Financial Statements, included in our Annual Report on Form 10-K for the fiscal year ended June 30, 2012.

Note 2. Summary of Significant Accounting Policies

Lannett Company, Inc., a Delaware corporation, and subsidiaries (the Company or Lannett), develop, manufacture, package, market, and distribute finished dosage forms of drugs as well as manufacture active pharmaceutical ingredients. The Company manufactures solid oral dosage forms, including tablets and capsules, topical and oral solutions, and is pursuing partnerships and contracts for the development and production of other dosage forms, including ophthalmic, nasal and injectable products.

The Company is engaged in an industry which is subject to considerable government regulation related to the development, manufacture, and marketing of pharmaceutical products. In the normal course of business, the Company periodically responds to inquiries or engages in administrative and judicial proceedings involving regulatory authorities, particularly the Food and Drug Administration (FDA) and the Drug Enforcement Agency (DEA).

Use of Estimates The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, the disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

Principles of Consolidation The consolidated financial statements include the accounts of the operating parent company, Lannett Company, Inc., and its wholly owned subsidiaries, as well as the consolidation of Cody LCI Realty, LLC (Realty), a variable interest entity. See Note 12 regarding the consolidation of this variable interest entity. All intercompany accounts and transactions have been eliminated.

Foreign Currency Translation The local currency is the functional currency of the Company s foreign subsidiary. Assets and liabilities of the foreign subsidiary are translated into U.S. dollars at the period-end currency exchange rate and revenues and expenses are translated at an average currency exchange rate for the period. The resulting translation adjustment is recorded in a separate component of shareholders equity and changes to such are included in comprehensive income. Exchange adjustments resulting from transactions denominated in foreign currencies are recognized in the consolidated statements of operations.

Reclassifications Certain prior year amounts have been reclassified to conform to the current year financial statement presentation.

Revenue Recognition The Company recognizes revenue when its products are shipped. At this point, title and risk of loss have transferred to the customer and provisions for estimates, including rebates, promotional adjustments, price adjustments, returns, chargebacks, and other potential adjustments are reasonably determinable. Accruals for these provisions are presented in the consolidated financial statements as rebates, chargebacks and returns payable and reductions to net sales. The change in the reserves for various sales adjustments may not be proportionally equal to the change in sales because of changes in both the product and the customer mix. Increased sales to wholesalers will generally require additional accruals as they are the primary recipient of chargebacks and rebates. Incentives offered to secure sales vary from product to product. Provisions for estimated rebates and promotional credits are estimated based upon contractual terms. Provisions for other customer credits, such as price adjustments, returns, and chargebacks, require management to make subjective judgments on customer mix. Unlike branded innovator drug companies, Lannett does not use information about product levels in distribution channels from third-party sources, such as IMS and Wolters Kluwer, in estimating future returns and other credits. Lannett calculates a chargeback/rebate rate based on contractual terms with its customers and applies this rate to customer sales.

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LANNETT COMPANY, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - UNAUDITED

(In thousands, unless otherwise noted and per share data)

Chargebacks The provision for chargebacks is the most significant and complex estimate used in the recognition of revenue. The Company sells its products directly to wholesale distributors, generic distributors, retail pharmacy chains, and mail-order pharmacies. The Company also sells its products indirectly to independent pharmacies, managed care organizations, hospitals, nursing homes, and group purchasing organizations, collectively referred to as indirect customers. Lannett enters into agreements with its indirect customers to establish pricing for certain products. The indirect customers then independently select a wholesaler from which to actually purchase the products at these agreed-upon prices. If the price paid by indirect customers is lower than the price paid by the wholesaler, Lannett will provide credit, called a chargeback, to the wholesaler for the difference between the contractual price paid by the indirect customers and the wholesaler purchase price. The provision for chargebacks is based on expected sell-through levels by the Company s wholesale customers to the indirect customers and estimated wholesaler inventory levels. As sales to the large wholesale customers, such as Cardinal Health, AmerisourceBergen, and McKesson increase (decrease), the reserve for chargebacks will also generally increase (decrease). However, the size of the increase (decrease) depends on the product mix and the amount of those sales that end up at indirect customers with which the Company has specific chargeback agreements. The Company continually monitors the reserve for chargebacks and makes adjustments when management believes that expected chargebacks on actual sales may differ from actual chargeback reserves.

Rebates Rebates are offered to the Company s key chain drug store, distributor and wholesaler customers to promote customer loyalty and increase product sales. These rebate programs provide customers with rebate credits upon attainment of pre-established volumes or attainment of net sales milestones for a specified period. Other promotional programs are incentive programs offered to the customers. As a result of the Patient Protection and Affordable Care Act (PPACA) enacted in the U.S. in March 2010, the Company participates in a new cost-sharing program for certain Medicare Part D beneficiaries designed primarily for the sale of brand drugs and certain generic drugs if their FDA approval was granted under a New Drug Application (NDA) or 505(b) NDA versus an Abbreviated New Drug Application (ANDA). Because our drugs used for the treatment of thyroid deficiency and our Morphine Sulfate Oral Solution product were each approved by the FDA as a 505(b)(2) NDA, they are considered branded drugs for purposes of the PPACA. Drugs purchased under this program during Medicare Part D coverage gap (commonly referred to as the donut hole) result in additional rebates. At the time of shipment, the Company estimates reserves for rebates and other promotional credit programs based on the specific terms in each agreement. The reserve for rebates increases (decreases) as sales to certain wholesale and retail customers increase (decrease). However, since these rebate programs are not identical for all customers, the size of the reserve will depend on the mix of customers that are eligible to receive rebates.

Returns Consistent with industry practice, the Company has a product returns policy that allows customers to return product within a specified period prior to and subsequent to the product s lot expiration date in exchange for a credit to be applied to future purchases. The Company s policy requires that the customer obtain pre-approval from the Company for any qualifying return. The Company estimates its provision for returns based on historical experience, changes to business practices, and credit terms. While such experience has allowed for reasonable estimations in the past, history may not always be an accurate indicator of future returns. The Company continually monitors the provisions for returns and makes adjustments when management believes that actual product returns may differ from established reserves. Generally, the reserve for returns increases (decreases) as net sales increase (decrease). The reserve for returns is included in the rebates, chargebacks and returns payable account on the balance sheet.

Other Adjustments Other adjustments consist primarily of price adjustments, also known as shelf-stock adjustments, which are credits issued to reflect decreases in the selling prices of the Company s products that customers have remaining in their inventories at the time of the price reduction. Decreases in selling prices are discretionary decisions made by management to reflect competitive market conditions. Amounts recorded for estimated shelf stock adjustments are based upon specified terms with direct customers, estimated declines in market prices, and estimates of inventory held by customers. The Company regularly monitors these and other factors and evaluates the reserve as additional information becomes available. Other adjustments are included in the rebates, chargebacks and returns payable account on the balance sheet.

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LANNETT COMPANY, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - UNAUDITED

(In thousands, unless otherwise noted and per share data)

Reserve Activity March 31, 2013 vs. March 31, 2012

The following tables identify the reserve for each major category of revenue allowance and a summary of the activity for the nine months ended March 31, 2013 and 2012:

For the nine months ended March 31, 2013

(In thousands) **Reserve Category**	**Chargebacks**	**Rebates**	**Returns**	**Other**	**Total**
Reserve Balance as of July 1, 2012	$ 7,063	$ 4,436	$ 5,540	$	$ 17,039
Actual credit issued related to sales recorded in prior fiscal years	(6,586)	(4,434)	(2,521)	(66)	(13,607)
Reserve or (reversal) charged during Fiscal 2013 related to sales in prior fiscal years	(463)	139		66	(258)
Reserve charged to net sales during Fiscal 2013 related to sales recorded in Fiscal 2013	52,006	17,467	3,363	2,801	75,637
Actual credit issued related to sales recorded in Fiscal 2013	(45,542)	(13,918)		(2,801)	(62,261)
Reserve Balance as of March 31, 2013	$ 6,478	$ 3,690	$ 6,382	$	$ 16,550

For the nine months ended March 31, 2012

(In thousands) **Reserve Category**	**Chargebacks**	**Rebates**	**Returns**	**Other**	**Total**
Reserve Balance as of July 1, 2011	$ 5,497	$ 2,925	$ 5,142	$	$ 13,564
Actual credit issued related to sales recorded in prior fiscal years	(5,350)	(3,084)	(3,426)	(152)	(12,012)
Reserve or (reversal) charged during Fiscal 2012 related to sales in prior fiscal years	(54)	158		152	256

Reserve charged to net sales during Fiscal 2012 related to sales recorded in Fiscal 2012	50,392	15,405	3,567	488	69,852
Actual credit issued related to sales recorded in Fiscal 2012	(44,092)	(11,686)		(488)	(56,266)
Reserve Balance as of March 31, 2012	$ 6,393	$ 3,718	$ 5,283	$	$ 15,394

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LANNETT COMPANY, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - UNAUDITED

(In thousands, unless otherwise noted and per share data)

The total reserve for chargebacks, rebates, returns and other adjustments decreased from $17,039 at June 30, 2012 to $16,550 at March 31, 2013. The decrease in the chargeback reserve is due primarily to a decrease in inventory levels at wholesale distribution centers as a result of increased gross sales to indirect customers during the first nine months of Fiscal 2013 as compared to Fiscal 2012. The decrease in the rebate reserve is due to the timing of rebates processed during the first nine months of Fiscal 2013 as compared to Fiscal 2012. The increase in the return reserve is primarily related to the increase in gross sales during Fiscal 2013. The activity in the Other category for the period ended March 31, 2013 includes shelf-stock, shipping and other sales adjustments.

When the Company and a customer enter into an agreement for the supply of a product, the customer will generally continue to purchase the product, stock its warehouse(s), and resell the product to its own customers. The Company ships its products to the warehouses of its wholesale and retail chain customers. The Company s customer will reorder the product as its warehouse is depleted. The Company generally has no minimum size orders for its customers. Additionally, most warehousing customers prefer not to stock excess inventory levels due to the additional carrying costs and inefficiencies created by holding excess inventory. As such, the Company s customers continually reorder the Company s products. It is common for the Company s customers to order the same products on a monthly basis. For generic pharmaceutical manufacturers, it is critical to ensure that customers warehouses are adequately stocked with its products. This is important due to the fact that multiple generic competitors may compete for the consumer demand for a given product. Availability of inventory ensures that a manufacturer s product is considered. Otherwise, retail prescriptions would be filled with competitors products. For this reason, the Company periodically offers incentives to its customers to purchase its products. These incentives are generally up-front discounts off its standard prices at the beginning of a generic campaign launch for a newly-approved or newly-introduced product, or when a customer purchases a Lannett product for the first time. Customers generally inform the Company that such purchases represent an estimate of expected resale for a period of time. This period of time is generally up to three months. The Company records this revenue, net of any discounts offered and accepted by its customers at the time of shipment. The Company s products generally have either 24 months or 36 months of shelf-life at the time of manufacture. The Company monitors its customers purchasing trends to attempt to identify any significant lapses in purchasing activity. If the Company observes a lack of recent activity, inquiries will be made to such customer regarding the success of the customer s resale efforts. The Company attempts to minimize any potential return (or shelf-life issues) by maintaining an active dialogue with the customers.

The products that the Company sells are generic versions of brand named drugs. The consumer markets for such drugs are well-established markets with many years of historically-confirmed consumer demand. Such consumer demand may be affected by several factors, including alternative treatments and costs, etc. However, the effects of changes in such consumer demand for the Company s products, like generic products manufactured by other generic companies, are gradual in nature. Any overall decrease in consumer demand for generic products generally occurs over an extended period of time. This is because there are thousands of doctors, prescribers, third-party payers, institutional formularies and other buyers of drugs that must change prescribing habits and medicinal practices before such a decrease would affect a generic drug market. If the historical data the Company uses and the assumptions management makes to calculate its estimates of future returns, chargebacks, and other credits do not accurately approximate future activity, its net sales, gross profit, net income and earnings per share could change. However, management believes that these estimates are reasonable based upon historical experience and current conditions.

Cash and cash equivalents The Company considers all highly liquid securities purchased with original maturities of 90 days or less to be cash equivalents. Cash equivalents are stated at cost, which approximates market value, and consist of certificates of deposit that are readily converted to cash. The Company maintains cash and cash equivalents with several major financial institutions.

Accounts Receivable The Company performs ongoing credit evaluations of its customers and adjusts credit limits based upon payment history and the customer s current credit worthiness, as determined by a review of current credit information. The Company continuously monitors collections and payments from its customers and maintains a provision for estimated credit losses based upon historical experience and any specific customer collection issues that have been identified. While such credit losses have historically been within both the Company s expectations and the provisions established, the Company cannot guarantee that it will continue to experience the same credit loss rates that it has in the past.

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LANNETT COMPANY, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - UNAUDITED

(In thousands, unless otherwise noted and per share data)

Inventories The Company values its inventory at the lower of cost (determined by the first-in, first-out method) or market, regularly reviews inventory quantities on hand, and records a provision for excess and obsolete inventory based primarily on remaining product shelf-life and estimated forecasts of product demand. The Company s estimates of future product demand may fluctuate, in which case estimated required reserves for excess and obsolete inventory may increase or decrease. If the Company s inventory is determined to be overvalued, the Company reduces the inventory value and recognizes such costs in cost of goods sold at the time of such determination. Likewise, if inventory is determined to be undervalued, the Company may have recognized excess cost of goods sold in previous periods and would recognize such additional operating income at the time of sale.

Property, Plant and Equipment Property, plant and equipment balances are stated at cost. Depreciation is provided for by the straight-line method for financial reporting purposes over the estimated useful lives of the assets. Depreciation expense for the three months ended March 31, 2013 and 2012 was $1,060 and $934, respectively. Depreciation expense for the nine months ended March 31, 2013 and 2012 was $3,210 and $2,797, respectively.

Investment Securities The Company s investment securities consist of publicly traded equity securities, which are classified as trading. Investment securities are recorded at fair value based on quoted market prices. For trading investments, unrealized holding gains and losses are recorded on the consolidated statements of operations. No gains or losses on investment securities are realized until they are sold or a decline in fair value is determined to be other-than-temporary. The Company reviews its investment securities and determines whether the investments are other-than-temporarily impaired. If the investments are deemed to be other-than-temporarily impaired, the investments are written down to their then current fair market value with a new cost basis being established. There were no securities determined by management to be other-than-temporarily impaired during the nine months ended March 31, 2013 or the fiscal year ended June 30, 2012.

Shipping and Handling Costs The cost of shipping products to customers is recognized at the time the products are shipped, and is included in cost of sales.

Research and Development Research and development costs are expensed as incurred.

Intangible Assets Indefinite-lived and definite-lived intangible assets are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount of the asset may not be recoverable. Definite-lived intangible assets are amortized over the estimated useful lives, generally for periods ranging from 10 to 15 years. The Company continually evaluates the reasonableness of the useful lives of these assets.

Impairments An impairment loss is measured as the excess of the asset s carrying value over its fair value, calculated using a discounted future cash flow method. Our discounted cash flow models are highly reliant on various assumptions which are considered level 3 inputs, including estimates of future cash flow (including long-term growth rates), discount rates, and expectations about the amount and timing of cash flows and the probability of achieving the estimated cash flows.

Advertising Costs The Company charges advertising costs to operations as incurred. Advertising expense for the nine months ended March 31, 2013 and 2012 was $13 and $26, respectively.

Income Taxes The Company accounts for income taxes in accordance with FASB ASC 740. Deferred tax assets and liabilities are determined based on the difference between the financial statement and tax bases of assets and liabilities as measured by the enacted tax rates which will be in effect when these differences reverse. Deferred tax expense/(benefit) is the result of changes in deferred tax assets and liabilities. The Company may recognize the tax benefit from an uncertain tax position claimed on a tax return only if it is more likely than not that the tax position will be sustained on examination by the taxing authorities, based on the technical merits of the position. The tax benefits recognized in the financial statements from such a position are measured based on the largest benefit that has a greater than 50% likelihood of being realized upon ultimate settlement. The authoritative standards issued by the FASB also provide guidance on de-recognition, classification, interest and penalties on income taxes, accounting in interim periods and requires increased disclosures. The factors used to assess the likelihood of realization are the Company s forecast of future taxable income and available tax planning strategies that could be implemented to realize the net deferred tax assets. Failure to achieve forecasted taxable income in applicable tax jurisdictions could affect the ultimate realization of deferred tax assets and could result in an increase in the Company s effective tax rate on future earnings.

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(In thousands, unless otherwise noted and per share data)

Medical Indication Information The Company operates one business segment - generic pharmaceuticals; accordingly the Company aggregates its financial information for all products and reports one reporting segment. The following table identifies the Company s net product sales by medical indication for the three and nine months ended March 31, 2013 and 2012:

(In thousands) Medical Indication	For the Three Months Ended March 31, 2013	For the Three Months Ended March 31, 2012	For the Nine Months Ended March 31, 2013	For the Nine Months Ended March 31, 2012
Antibiotic	$ 3,496	$ 1,662	$ 6,267	$ 4,798
Cardiovascular	6,988	6,050	21,356	11,512
Gallstone	1,390	1,419	4,676	4,286
Glaucoma	1,627	993	4,608	3,093
Gout	1,776	110	2,907	482
Migraine Headache	1,299	1,442	3,995	4,601
Obesity	1,074	979	3,488	2,570
Pain Management	4,980	4,043	14,752	14,609
Thyroid Deficiency	14,024	12,543	42,135	36,788
Other	2,368	1,447	6,696	4,561
Total	$ 39,022	$ 30,688	$ 110,880	$ 87,300

Concentration of Market and Credit Risk The following table identifies products which accounted for at least 10% of net sales in either of the three and nine month periods ended March 31, 2013 and 2012.

	For the Three Months Ended March 31, 2013	For the Three Months Ended March 31, 2012	For the Nine Months Ended March 31, 2013	For the Nine Months Ended March 31, 2012
Product 1	36%	41%	38%	42%
Product 2	12%	11%	11%	4%
Product 3	10%	6%	9%	9%

The following table identifies customers which accounted for at least 10% of net sales in either of the three and nine month periods ended March 31, 2013 and 2012, respectively.

For the Three Months Ended March 31, 2013	For the Three Months Ended March 31, 2012	For the Nine Months Ended March 31, 2013	For the Nine Months Ended March 31, 2012

Customer A	16%	16%	16%	18%
Customer B	11%	10%	12%	11%
Customer C	10%	9%	10%	12%
Customer D	9%	11%	8%	10%

At March 31, 2013 and June 30, 2012, four customers accounted for 68% and 66%, respectively of the Company s accounts receivable balances, respectively. Credit terms are offered to customers based on evaluations of the customers financial condition. Generally, collateral is not required from customers. Accounts receivable payment terms vary and outstanding balances are stated in the financial statements net of an allowance for doubtful accounts. Individual balances remaining outstanding longer than the payment terms are considered past due. The Company determines its allowance by considering a number of factors, including the length of time trade accounts receivable are past due, the Company s previous loss history, the customer s current ability to pay its obligation to the Company, and the condition of the general economy and the industry as a whole. The Company writes-off accounts receivable when they are determined to have become uncollectible.

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Share-based Compensation Share-based compensation costs are recognized over the vesting period based on the fair value of the instrument on the date of grant less an estimate for forfeitures. The Company uses the Black-Scholes valuation model to determine the fair value of stock options and the share price on the grant date to value restricted stock. The fair value model includes various assumptions, including the expected volatility, expected life of the awards, and risk-free interest rates. These assumptions involve inherent uncertainties based on market conditions which are generally outside the Company s control. Changes in these assumptions could have a material impact on share-based compensation costs recognized in the financial statements.

Note 3. New Accounting Standards

In June 2011, the FASB issued authoritative guidance which allows an entity the option to present the total of comprehensive income, the components of net income, and the components of other comprehensive income either in a single continuous statement of comprehensive income or in two separate but consecutive statements. In both options, an entity is required to present each component of net income along with total net income, each component of other comprehensive income along with a total for other comprehensive income, and a total amount for comprehensive income. This guidance eliminates the option to present the components of other comprehensive income as part of the statement of changes in stockholders equity. This guidance does not change the items that must be reported in other comprehensive income or when an item of other comprehensive income must be reclassified to net income. This authoritative guidance must be applied retrospectively, and is effective for fiscal years and interim periods within those years, beginning after December 15, 2011. In December 2011, the FASB issued an update deferring the effective date for amendments to the presentation of reclassifications of items out of accumulated other comprehensive income. The adoption of this guidance by the Company on July 1, 2012 did not have a significant impact on the Company s consolidated financial statements as it only requires a change in the format of the presentation.

In July 2012, the FASB issued authoritative guidance which allows an entity the option to first assess qualitative factors to determine whether the existence of events and circumstances indicates that it is more likely than not that an indefinite-lived intangible asset is impaired. If, after assessing the totality of events and circumstances, an entity concludes that it is not more likely than not that the indefinite-lived intangible asset is impaired, then the entity is not required to take further action. An entity also has the option to bypass the qualitative assessment for any indefinite-lived intangible asset in any period and proceed directly to performing the quantitative impairment test. An entity will be able to resume performing the qualitative assessment in any subsequent period. The amendments are effective for annual and interim impairment tests performed for fiscal years beginning after September 15, 2012. Early adoption is permitted, including for annual and interim impairment tests performed as of a date before July 27, 2012, if a public entity s financial statements for the most recent annual or interim period have not yet been issued or, for nonpublic entities, have not yet been made available for issuance. The Company adopted this guidance effective July 1, 2012. The adoption of this guidance by the Company did not have a significant impact on the Company s consolidated financial statements.

In February 2013, the FASB issued authoritative guidance which requires an entity to provide information about the amounts reclassified out of accumulated other comprehensive income by component. In addition, an entity is required to present, either on the face of the statement where net income is presented or in the notes, significant amounts reclassified out of accumulated other comprehensive income by the respective line items of net income but only if the amount reclassified is required under U.S. GAAP to be reclassified to net income in its entirety in the same reporting period. For other amounts not required under U.S. GAAP to be reclassified in their entirety to net income, an entity is required to cross-reference to other disclosures required under U.S. GAAP that provide additional detail about those amounts. This authoritative guidance is effective for reporting periods beginning after December 15, 2012. The adoption of this guidance by the Company did not have a significant impact on the Company s consolidated financial statements.

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Note 4. Inventories

Inventories at March 31, 2013 and June 30, 2012 consist of the following:

(In thousands)		**March 31, 2013**		**June 30, 2012**
Raw Materials	$	15,693	$	11,351
Work-in-process		3,362		4,805
Finished Goods		11,778		9,130
Packaging Supplies		2,014		1,778
	$	32,847	$	27,064

The preceding amounts are net of excess and obsolete inventory reserves of $1,190 and $1,472 at March 31, 2013 and June 30, 2012, respectively.

Recently, the FDA increased its efforts to force companies to file and seek FDA approval for GRASE or Grandfathered products. GRASE products are those old drugs that do not require prior approval from FDA in order to be marketed because they are generally recognized as safe and effective based on published scientific literature. Similarly, Grandfathered products are those which entered the market before the passage of the 1906 Act, the 1938 Act or the 1962 amendments to the Act. Efforts have included issuing notices to discontinue marketing certain products to companies currently producing these products. Lannett currently manufactures and markets one product that is considered GRASE or a Grandfathered product, C-Topical Solution. An additional GRASE product, Oxycodone HCl Oral Solution (Oxycodone) was manufactured and marketed through October 2012. In July 2012 the FDA issued notice forcing all companies who manufactured Oxycodone to remove it from the market by October 2012 and to file an application seeking FDA approval . The Company had $445 and $1,703 of net inventory value of other Grandfathered products at March 31, 2013 and June 30, 2012, respectively.

Note 5. Property, Plant and Equipment

Property, plant and equipment at March 31, 2013 and June 30, 2012 consist of the following:

(In thousands)	**Useful Lives**		**March 31, 2013**	**June 30, 2012**
Land		$	1,279	