

NUVASIVE INC
Form 10-Q
November 04, 2011
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UNITED STATES SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

(Mark One)

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

For the quarterly period ended September 30, 2011

OR

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

For the transition period from _____ to _____

Commission file number 000-50744

NUVASIVE, INC.

(Exact name of registrant as specified in its charter)

Delaware
(State or other jurisdiction of
incorporation or organization)

33-0768598
(I.R.S. Employer
Identification No.)

7475 Lusk Boulevard

San Diego, CA 92121

(Address of principal executive offices, including zip code)

(858) 909-1800

(Registrant's telephone number, including area code)

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(Former name, former address and former fiscal year, if changed since last report)

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

Yes No

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate website, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files).

Yes 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 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 Accelerated filer Non-accelerated filer Smaller reporting company

(Do not check if a smaller reporting company)

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

As of October 28, 2011, there were 42,244,073 shares of the registrant's common stock outstanding.

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NUVASIVE, INC.

QUARTERLY REPORT ON FORM 10-Q

September 30, 2011

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	September 30, 2011 (Unaudited)	December 31, 2010
ASSETS		
Current assets:		
Cash and cash equivalents	\$ 220,943	\$ 92,597
Short-term marketable securities	151,363	86,458
Accounts receivable, net	78,637	76,632
Inventory	122,588	107,577
Deferred tax assets	4,425	4,425
Prepaid expenses and other current assets	5,100	4,082
Total current assets	583,056	371,771
Property and equipment, net	118,125	102,165
Long-term marketable securities	46,593	50,635
Intangible assets, net	100,044	107,121
Goodwill	103,070	103,070
Deferred tax assets, non-current	76,260	52,033
Restricted cash and investments	68,463	5,529
Other assets	19,187	9,705
Total assets	\$ 1,114,798	\$ 802,029
LIABILITIES AND STOCKHOLDERS' EQUITY		
Current liabilities:		
Accounts payable and accrued liabilities	\$ 52,191	\$ 58,995
Accrued payroll and related expenses	17,872	17,266
Litigation liability	101,200	
Acquisition-related liabilities	33,628	32,715
Total current liabilities	204,891	108,976
Senior Convertible Notes	427,974	230,000
Long-term acquisition-related liabilities		326
Deferred tax liabilities	3,685	3,685
Other long-term liabilities	13,088	12,810
Commitments and contingencies		
Noncontrolling interests	11,015	11,877
Stockholders' equity:		
Preferred stock, \$0.001 par value; 5,000 shares authorized, none outstanding		
Common stock, \$0.001 par value; 120,000 and 70,000 shares authorized at September 30, 2011 and December 31, 2010, respectively; 39,904 and 39,528 issued and outstanding at September 30, 2011 and December 31, 2010, respectively	40	40
Additional paid-in capital	625,387	545,114

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Accumulated other comprehensive income (loss)	(54)	616
Accumulated deficit	(171,228)	(111,415)
Total stockholders' equity	454,145	434,355
Total liabilities and stockholders' equity	\$ 1,114,798	\$ 802,029

See accompanying notes to unaudited condensed consolidated financial statements.

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NUVASIVE, INC.

UNAUDITED CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS

(in thousands, except per share data)

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2011	2010	2011	2010
Revenue	\$ 132,880	\$ 120,262	\$ 390,312	\$ 348,933
Cost of goods sold (excluding amortization of purchased technology)	26,015	21,580	75,049	62,037
Gross profit	106,865	98,682	315,263	286,896
Operating expenses:				
Sales, marketing and administrative	85,482	77,717	254,025	230,104
Research and development	10,092	10,085	31,119	31,989
Amortization of intangible assets	1,504	1,342	4,241	4,047
Litigation award	101,200		101,200	
Total operating expenses	198,278	89,144	390,585	266,140
Interest and other expense, net:				
Interest income	257	200	591	567
Interest expense	(7,276)	(1,668)	(10,962)	(5,005)
Other income (expense), net	1,726	(6)	2,303	81
Total interest and other expense, net	(5,293)	(1,474)	(8,068)	(4,357)
(Loss) income before income tax expense	(96,706)	8,064	(83,390)	16,399
Income tax (benefit) expense	(29,031)	(40)	(22,715)	1,399
Consolidated net (loss) income	\$ (67,675)	\$ 8,104	\$ (60,675)	\$ 15,000
Net loss attributable to noncontrolling interests	\$ (123)	\$ (438)	\$ (862)	\$ (1,353)
Net (loss) income attributable to NuVasive, Inc.	\$ (67,552)	\$ 8,542	\$ (59,813)	\$ 16,353
Net (loss) income per share attributable to NuVasive, Inc.:				
Basic	\$ (1.69)	\$ 0.22	\$ (1.50)	\$ 0.42
Diluted	\$ (1.69)	\$ 0.21	\$ (1.50)	\$ 0.40
Weighted average shares outstanding:				
Basic	39,892	39,394	39,766	39,180
Diluted	39,892	40,396	39,766	40,389

See accompanying notes to unaudited condensed consolidated financial statements.

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NUVASIVE, INC.

UNAUDITED CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

(in thousands)

	Nine Months Ended September 30,	
	2011	2010
Operating activities:		
Consolidated net (loss) income	\$ (60,675)	\$ 15,000
Adjustments to reconcile net (loss) income to net cash provided by operating activities:		
Depreciation and amortization	24,847	27,404
Stock-based compensation	23,789	21,304
Allowance for excess and obsolete inventory	4,642	1,682
Allowance for doubtful accounts and sales return reserves, net of write offs	1,261	(1,039)
Accretion of contingent consideration	587	570
Amortization of debt issuance costs	2,588	1,120
Amortization of debt discount	3,076	
Gain recognized on change in fair value of derivatives	(2,387)	
Deferred income tax expense	6,238	
Other non-cash adjustments	3,545	2,924
Changes in operating assets and liabilities, net of effects from acquisitions:		
Accounts receivable	(3,152)	(11,465)
Inventory	(19,933)	(10,043)
Prepaid expenses and other assets	(1,061)	(3,878)
Accounts payable and accrued liabilities	504	6,502
Litigation liability	101,200	
Accrued payroll and related expenses	584	(5,973)
Income taxes payable	(32,237)	(186)
Net cash provided by operating activities	53,416	43,922
Investing activities:		
Purchases of property and equipment	(39,435)	(36,622)
Purchases of marketable securities	(244,209)	(150,045)
Sales of marketable securities	124,205	142,313
Purchases of restricted investments	(4,535)	
Payment for specific rights in connection with supply agreement, net of refund received	(5,000)	
Other assets	(1,100)	(659)
Net cash used in investing activities	(170,074)	(45,013)
Financing activities:		
Proceeds from the sale of warrants	47,898	
Proceeds from the issuance of convertible debt, net of issuance costs	391,334	
Purchase of convertible note hedges	(80,097)	
Repurchase of 2013 Senior Convertible Notes	(118,702)	
Proceeds from the issuance of common stock	4,461	12,768
Other assets	(349)	(7,722)
Tax benefits related to stock-based compensation awards	638	1,118
Net cash provided by financing activities	245,183	6,164
Effect of exchange rate changes on cash	(179)	104

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Increase in cash and cash equivalents	128,346	5,177
Cash and cash equivalents at beginning of period	92,597	65,413
Cash and cash equivalents at end of period	\$ 220,943	\$ 70,590

See accompanying notes to unaudited condensed consolidated financial statements.

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NuVasive, Inc.

Notes to Unaudited Condensed Consolidated Financial Statements

1. Description of Business and Basis of Presentation

Description of Business

NuVasive[®], Inc. (the Company or NuVasive) was incorporated in Delaware on July 21, 1997. The Company is focused on developing minimally disruptive surgical products and procedures for the spine. The Company began commercializing its products in 2001. Its currently-marketed product portfolio is focused on applications for spine fusion surgery. Its principal product offering includes a minimally disruptive surgical platform called Maximum Access Surgery, or MAS[®], as well as a growing offering of biologics, cervical and motion preservation products. In the spine surgery market, the Company's currently-marketed products are primarily used to enable access to the spine and to perform restorative and fusion procedures in a minimally disruptive fashion. The Company also focuses significant research and development efforts on expanding its MAS product platform, advancing the applications of its unique technology to additional procedures, and developing motion preservation products. The Company dedicates significant resources toward training spine surgeons on its unique technology and products.

The Company's primary business model is to loan its MAS systems to surgeons and hospitals who purchase disposables and implants for use in individual procedures. In addition, for larger customers, the Company's proprietary nerve monitoring systems, MaXcess[®] and surgical instrument sets are placed with hospitals for an extended period at no up-front cost to them. The Company also offers a range of bone allograft in patented saline packaging, disposables and spine implants, which include its branded CoRoent[®] products and fixation devices such as rods, plates and screws. Implants and disposables are shipped from the Company's inventories. The Company sells an immaterial quantity of MAS instrument sets, MaXcess and nerve monitoring systems to hospitals.

Basis of Presentation

The accompanying unaudited condensed consolidated financial statements have been prepared pursuant to the rules and regulations of the Securities and Exchange Commission (SEC). Pursuant to these rules and regulations, the Company has condensed or omitted certain information and footnote disclosures it normally includes in its annual consolidated financial statements prepared in accordance with accounting principles generally accepted in the United States (GAAP). In the opinion of management, the consolidated financial statements include all adjustments necessary, which are of a normal and recurring nature, for the fair presentation of the Company's financial position and of the results of operations and cash flows for the periods presented.

The accompanying unaudited condensed consolidated financial statements as of September 30, 2011 and December 31, 2010 and for the three and nine months ended September 30, 2011 and 2010 include the accounts of the Company and its wholly owned subsidiaries, as well as the accounts of a variable interest entity, Progentix Orthobiology, B.V. (Progentix), which is consolidated pursuant to existing guidance issued by the Financial Accounting Standards Board (FASB). All significant intercompany accounts and transactions have been eliminated in consolidation.

These financial statements should be read in conjunction with the audited consolidated financial statements and notes thereto for the year ended December 31, 2010 included in NuVasive's Annual Report on Form 10-K filed with the SEC. Operating results for the three and nine months ended September 30, 2011 are not necessarily indicative of the results that may be expected for any other interim period or for the full year. The balance sheet at December 31, 2010 has been derived from the audited financial statements at that date, but does not include all of the information and footnotes required by GAAP for complete financial statements.

Change in Accounting Estimate

During the first quarter of 2011, the Company completed a review of the estimated useful life of its surgical instrument sets. Based on historical useful life information, as well as forecasted product life cycles and demand expectations, the useful life of certain surgical instrument sets was extended from three to four years. In accordance with authoritative guidance, this was accounted for as a change in accounting estimate and was made on a prospective basis effective January 1, 2011. For the three and nine months ended September 30, 2011, depreciation expense, which is included in sales, marketing and administrative expenses, was lower by approximately \$1.2 million and \$5.0 million, respectively, than it would have been had the useful life of these assets not been extended. The effect of this change on basic and diluted earnings per share for the three and nine months ended September 30, 2011 was \$0.02 and \$0.09 per share, respectively.

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Reclassifications and Adjustments

Certain reclassifications have been made to the prior year condensed consolidated financial statements to conform to the current year presentation.

During the three months ended June 30, 2011, the Company identified an immaterial error in the consolidated financial statements for the year ended December 31, 2010 related to the accrual of payroll expenses. Based on a quantitative and qualitative analysis of the error as required by authoritative guidance, management concluded that the correction, which increased expenses by approximately \$1.3 million in the nine months ended September 30, 2011, had no material impact on any of the Company's previously issued financial statements, would be immaterial to the expected full year results for 2011 and had no effect on the trend of financial results. Of the \$1.3 million, approximately \$1.0 million and \$0.3 million was charged to sales, marketing and administrative expenses and research and development expenses, respectively.

2. Significant Accounting Policies

Derivative Financial Instruments

On June 28, 2011, the Company issued \$402.5 million principal amount of 2.75% Senior Convertible Notes due 2017 (the 2017 Notes). Prior to September 28, 2011, the 2017 Notes were settleable only in cash. On September 28, 2011, stockholder approval was obtained to increase the number of the Company's authorized shares of common stock from 70 million to 120 million. Prior to obtaining stockholder approval, in accordance with authoritative guidance, the cash conversion feature of the 2017 Notes (the 2017 Notes Embedded Conversion Derivative) required bifurcation from the 2017 Notes and was accounted for as a derivative liability.

In connection with the issuance of the 2017 Notes, the Company entered into convertible note hedge transactions (the 2017 Hedge) entitling the Company to purchase up to 9,553,096 shares of the Company's common stock at an initial stock price of \$42.13 per share, each of which is subject to adjustment. Prior to obtaining the stockholder approval to increase the number of the Company's authorized shares of common stock discussed above, the 2017 Hedge was settleable only in cash. In accordance with authoritative guidance, the 2017 Hedge was accounted for as a derivative asset.

In accordance with authoritative guidance, upon obtaining stockholder approval to increase the number of authorized shares of the Company's common stock, as the Company can now settle the 2017 Notes in cash, stock, or a combination thereof, solely at the Company's election, the derivative liability and asset were marked to fair value and reclassified to stockholders' equity.

During the three and nine months ended September 30, 2011, the Company recognized non-cash income of approximately \$2.4 million related to the net change in the fair values of the derivative liability and asset. This \$2.4 million consists of a \$39.5 million gain related to the change in the fair value of the derivative liability and a loss of \$37.1 million related to the change in fair value of the derivative asset. Gains and losses are included as a component of other income (expense), net.

Recently Adopted Accounting Standards

Fair Value Measurements Disclosures

Effective January 1, 2011, the Company adopted the FASB's updated guidance related to fair value measurements and disclosures, which requires a reporting entity to disclose separately information related to purchases, sales, issuances, and settlements in the reconciliation for fair value measurements using significant unobservable inputs, or Level 3, to be included in the rollforward of activity. The guidance is effective for interim or annual financial reporting periods beginning after December 15, 2010. The Company has updated its disclosures to comply with the updated guidance; however, adoption of the updated guidance did not have an impact on the Company's consolidated results of operations or financial position.

Table of Contents**3. Investment in Progentix Orthobiology, B.V.**

In 2009, the Company completed the purchase of forty percent (40%) of the capital stock of Progentix, a company organized under the laws of the Netherlands, from existing shareholders (the Progentix Shareholders) pursuant to a Preferred Stock Purchase Agreement for \$10 million in cash (the Initial Investment). Concurrent with the Initial Investment, NuVasive and Progentix also entered into a Senior Secured Facility Agreement, whereby Progentix may borrow up to \$5.0 million from NuVasive to fund ongoing clinical and regulatory efforts (the Loan). At September 30, 2011, the Company had advanced Progentix the full \$5.0 million in accordance with the Loan Agreement. The Loan accrues interest at a rate of six percent (6%) per year. Other than its obligations under the Loan Agreement, NuVasive is not obligated to provide additional funding, nor has any additional funding been provided, to Progentix.

Also concurrent with the Preferred Stock Purchase Agreement, NuVasive, Progentix and the Progentix Shareholders entered into an Option Purchase Agreement, as amended (the Option Agreement), whereby NuVasive may be obligated (the Put Option), upon the achievement of an annual sales run rate on Progentix products in excess of a specified amount between June 14, 2011 and June 13, 2013 (the Option Period), to purchase the remaining sixty percent (60%) of capital stock of Progentix from its shareholders (the Remaining Shares) for an amount up to \$35.0 million, subject to certain reductions, payable in a combination of cash and NuVasive common stock, at NuVasive's sole discretion. In accordance with the Option Agreement, NuVasive has the right to purchase the Remaining Shares (the Call Option) during the Option Period for an amount up to \$35.0 million, subject to certain reductions, payable in a combination of cash and NuVasive common stock, at NuVasive's sole discretion. Also in accordance with the Option Agreement, an option expired in June 2011 that could have required NuVasive to purchase the Remaining Shares and make additional milestone-related payments totaling up to \$70.0 million, subject to certain adjustments. NuVasive and Progentix also entered into a Distribution Agreement, as amended, whereby Progentix appointed NuVasive as its exclusive distributor for certain Progentix products. The Distribution Agreement will be in effect for a term of ten years unless terminated earlier in accordance with its terms.

In accordance with authoritative guidance, the Company has determined that Progentix is a variable interest entity (VIE) as it does not have the ability to finance its activities without additional subordinated financial support and its equity investors will not absorb their proportionate share of expected losses and will be limited in the receipt of the potential residual returns of Progentix. Additionally, pursuant to this guidance, NuVasive is considered its primary beneficiary as NuVasive has both (1) the power to direct the economically significant activities of Progentix and (2) the obligation to absorb losses of, or the right to receive benefits from, Progentix. Accordingly, the financial position and results of operations of Progentix have been included in the Company's consolidated financial statements from the date of the Initial Investment. The liabilities recognized as a result of consolidating Progentix do not represent additional claims on the Company's general assets. The creditors of Progentix have claims only on the assets of Progentix, which are not material, and the assets of Progentix are not available to NuVasive.

Pursuant to authoritative guidance, the equity interests in Progentix not owned by the Company, which includes shares of both common and preferred stock, are reported as noncontrolling interests on the consolidated balance sheet of the Company. The preferred stock represents 18% of the noncontrolling equity interests and provides for a cumulative 8% dividend, if and when declared by Progentix's Board of Directors. As the rights and conversion features of the preferred stock are substantially the same as those of the common stock, the preferred stock is classified as noncontrolling interest and shares in the allocation of the losses incurred by Progentix. Losses incurred by Progentix are charged to the Company and to the noncontrolling interest holders based on their ownership percentage. The Remaining Shares and the Option Agreement that was entered into between NuVasive, Progentix and the Progentix Shareholders are not considered to be freestanding financial instruments as defined by authoritative guidance. Therefore the Remaining Shares and the Option Agreement are accounted for as a combined unit on the consolidated financial statements as a redeemable noncontrolling interest that was initially recorded at fair value and classified as mezzanine equity.

Total assets and liabilities of Progentix as of September 30, 2011 included in the accompanying condensed consolidated balance sheet are as follows (*in thousands*):

Total current assets	\$ 834
Identifiable intangible assets, net	15,455
Goodwill	12,654
Other long-term assets	422
Accounts payable & accrued expenses	470
Other long-term liabilities	553
Deferred tax liabilities, net	3,685
Noncontrolling interests	11,015

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The following is a reconciliation of equity (net assets) attributable to the noncontrolling interests (*in thousands*):

Noncontrolling interests at December 31, 2010	\$ 11,877
Net loss attributable to the noncontrolling interests	(862)
Noncontrolling interests at September 30, 2011	\$ 11,015

4. Balance Sheet Reserves

The balances of the reserves for accounts receivable and inventory are as follows (*in thousands*):

	September 30, 2011	December 31, 2010
Reserves for accounts receivable and sales returns	\$ 3,533	\$ 2,573
Reserves for excess and obsolete inventory	11,324	6,682

The Company's inventory consists primarily of purchased finished goods, which includes specialized implants and disposables, and is stated at the lower of cost or market determined by a weighted average cost method. The Company reviews the components of its inventory on a periodic basis for excess, obsolete or impaired inventory, and records a reserve for the identified items.

5. Marketable Securities and Fair Value Measurements

Marketable securities consist of certificates of deposit, corporate debt securities, commercial paper, U.S. government treasury securities and securities of government-sponsored entities. The Company classifies all securities as available-for-sale, as the sale of such securities may be required prior to maturity to implement management strategies. These securities are carried at fair value, with the unrealized gains and losses reported as a component of other comprehensive income in stockholders' equity until realized. A decline in the market value of any marketable security below cost that is determined to be other-than-temporary will result in a revaluation of its carrying amount to fair value. The impairment is charged to earnings and a new cost basis for the security is established. No such impairment charges were recorded for any period presented.

Realized gains and losses from the sale of marketable securities, if any, are determined on a specific identification basis. Realized gains and losses and declines in value judged to be other-than-temporary, if any, on available-for-sale securities are included in other income or expense on the consolidated statements of operations. Realized gains and losses during the periods presented were immaterial. Premiums and discounts are amortized or accreted over the life of the related security as an adjustment to yield using the straight-line method and are included in interest income on the consolidated statements of operations. Interest and dividends on securities classified as available-for-sale are included in interest income on the consolidated statements of operations.

The composition of marketable securities is as follows (*in thousands, except years*):

	Contractual Maturity (in Years)	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
September 30, 2011:					
Classified as current assets					
Certificates of deposit	Less than 1	\$ 777	\$ 1	\$	\$ 778
Corporate notes	Less than 1	21,206	9	(1)	21,214
Commercial paper	Less than 1	9,997			9,997
U.S. government treasury securities	Less than 1	34,760	5	(1)	34,764
Securities of government-sponsored entities	Less than 1	84,618	4	(12)	84,610

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Short-term marketable securities		151,358	19	(14)	151,363
Classified as non-current assets					
Corporate notes	1 to 2	5,075	3		5,078
Securities of government-sponsored entities	1 to 2	41,506	17	(8)	41,515
Long-term marketable securities		46,581	20	(8)	46,593
Classified as restricted investments					
U.S. government treasury securities	Less than 1 to 2	12,030	11		12,041
Securities of government-sponsored entities	Less than 1 to 2	50,716	22	(13)	50,725
Restricted investments		62,746	33	(13)	62,766
Total marketable securities at September 30, 2011		\$ 260,685	\$ 72	\$ (35)	\$ 260,722

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	Contractual				
	Maturity		Gross	Gross	Fair
	(in Years)	Amortized	Unrealized	Unrealized	Value
		Cost	Gains	Losses	
December 31, 2010:					
Classified as current assets					
Certificates of deposit	Less than 1	\$ 938	\$ 1	\$ (1)	\$ 938
Corporate notes	Less than 1	12,076	3		12,079
U.S. government treasury securities	Less than 1	16,550	12	(1)	16,561
Securities of government-sponsored entities	Less than 1	56,870	24	(14)	56,880
Short-term marketable securities		86,434	40	(16)	86,458
Classified as non-current assets					
Certificates of deposit	1 to 2	456			456
Corporate notes	1 to 2	3,123		(9)	3,114
U.S. government treasury securities	1 to 2	4,023			4,023
Securities of government-sponsored entities	1 to 2	43,056	6	(20)	43,042
Long-term marketable securities		50,658	6	(29)	50,635
Total marketable securities at December 31, 2010		\$ 137,092	\$ 46	\$ (45)	\$ 137,093

As of September 30, 2011, the Company had no significant investment positions that were in an unrealized loss position. The Company reviews its investments to identify and evaluate investments that have an indication of possible other-than-temporary impairment. Factors considered in determining whether a loss is other-than-temporary include the length of time and extent to which fair value has been less than the cost basis, the financial condition and near-term prospects of the investee, and the Company's intent and ability to hold the investment for a period of time sufficient to allow for any anticipated recovery in market value. The Company maintains an investment portfolio of various holdings, types and maturities. The Company does not have derivative financial investments. The Company places its cash investments in instruments that meet high credit quality standards, as specified in its investment policy guidelines. These guidelines also limit the amount of credit exposure to any one issue, issuer or type of instrument.

The Company measures certain assets and liabilities in accordance with authoritative guidance which requires fair value measurements be classified and disclosed in one of the following three categories:

Level 1: Quoted prices (unadjusted) in active markets that are accessible at the measurement date for assets or liabilities.

Level 2: Observable prices that are based on inputs not quoted on active markets, but corroborated by market data.

Level 3: Unobservable inputs are used when little or no market data is available.

Assets and liabilities are classified based on the lowest level of input that is significant to the fair value measurements. The Company reviews the fair value hierarchy classification on a quarterly basis. Changes in the ability to observe valuation inputs may result in a reclassification of levels for certain assets or liabilities within the fair value hierarchy. The Company did not have any transfers of assets and liabilities between Level 1 and Level 2 of the fair value measurement hierarchy during the nine months ended September 30, 2011. The Company had one transfer from Level 3 of the fair value measurement hierarchy, as the liability became fixed during the nine months ended September 30, 2011.

The fair values of the Company's assets and liabilities at September 30, 2011, which are measured at fair value on a recurring basis, were determined using the following inputs (*in thousands*):

	Quoted Price Significant Other		
	Active	Observable	Significant
	Market	Inputs	Unobservable
	Total	(Level 2)	Inputs (Level 3)
Marketable Securities and Restricted Investments:			