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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 MARCH 31, 2013**

**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: 001-14758**

# QUESTCOR PHARMACEUTICALS, INC.
**(Exact name of Registrant as specified in its charter)**

| **CALIFORNIA** | **33-0476164** |
|---|---|
| **(State or other jurisdiction of incorporation or organization)** | **(I.R.S. Employer of Identification No.)** |

**1300 North Kellogg Drive, Suite D**
**Anaheim, CA 92807**
**(Address of Principal Executive Offices)**

**(714) 786-4200**
**(Registrant's Telephone Number, Including Area Code)**

Indicate by check mark whether the Registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter prior 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 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 | x | Accelerated filer | o |
| Non-accelerated filer | o (Do not check if a smaller reporting company) | Smaller reporting company | o |

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

As of March 31, 2013 there were 59,554,145 shares of the Registrant’s common stock, no par value per share, outstanding.

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# PART I. FINANCIAL INFORMATION

## ITEM 1. FINANCIAL STATEMENTS

**QUESTCOR PHARMACEUTICALS, INC.**
**CONDENSED CONSOLIDATED BALANCE SHEETS**
**(In thousands, except share information)**
**(unaudited)**

| | March 31, 2013 | December 31, 2012 |
|---|---|---|
| **ASSETS** | | |
| Current assets: | | |
| Cash and cash equivalents | $ 75,404 | $ 80,608 |
| Short-term investments | 78,020 | 74,705 |
| Total cash, cash equivalents and short-term investments | 153,424 | 155,313 |
| Accounts receivable, net of allowances for doubtful accounts of $379 and $0 at March 31, 2013 and December 31, 2012, respectively | 59,278 | 61,417 |
| Inventories, net of allowances of $1,205 and $52 at March 31, 2013 and December 31, 2012, respectively | 16,786 | 9,909 |
| Prepaid expenses and other current assets | 6,485 | 4,900 |
| Deferred tax assets | 5,464 | 5,737 |
| Total current assets | 241,437 | 237,276 |
| Property and equipment, net | 35,742 | 2,073 |
| Purchased technology, net | 700 | 1,493 |
| Goodwill | 20,597 | — |
| Intangibles, net | 33,992 | — |
| Deposits and other assets | 1,766 | 70 |
| Deferred tax assets | 11,519 | 11,519 |
| Total assets | $ 345,753 | $ 252,431 |
| **LIABILITIES AND SHAREHOLDERS' EQUITY** | | |
| Current liabilities: | | |
| Accounts payable | $ 14,630 | $ 13,069 |
| Accrued compensation | 6,089 | 21,300 |
| Sales-related reserves | 25,830 | 37,376 |
| Dividend payable | 14,751 | — |
| Current portion of contingent consideration in conjunction with acquisition of BioVectra | 4,485 | — |
| Income taxes payable | 13,003 | 7,360 |
| Current portion of long-term debt | 1,680 | — |
| Other accrued liabilities | 13,827 | 11,294 |
| Total current liabilities | 94,295 | 90,399 |
| Long-term debt, less current portion | 16,062 | — |
| Contingent consideration in conjunction with acquisition of BioVectra | 25,747 | — |
| Non current deferred tax liability | 11,736 | — |
| Other non current liabilities | 2,211 | 203 |
| Total liabilities | 150,051 | 90,602 |
| Shareholders' equity: | | |
| Preferred stock, no par value, 5,334,285 shares authorized; none outstanding | — | — |
| Common stock, no par value, 105,000,000 shares authorized, 59,554,145 and 58,544,206 shares issued and outstanding at March 31, 2013 and December 31, 2012, respectively | 26,692 | 15,938 |
| Retained earnings | 170,164 | 145,851 |
| Accumulated other comprehensive (loss) income | (1,154) | 40 |
| Total shareholders' equity | 195,702 | 161,829 |
| Total liabilities and shareholders' equity | $ 345,753 | $ 252,431 |

See accompanying notes.

**QUESTCOR PHARMACEUTICALS, INC.**

**CONDENSED CONSOLIDATED STATEMENTS OF INCOME AND COMPREHENSIVE INCOME**
**(In thousands, except net income per share data)**
**(unaudited)**

| | Three Months Ended March 31, | |
|---|---|---|
| | **2013** | **2012** |
| **Revenue** | | |
| Pharmaceutical net sales | $ 126,771 | $ 95,968 |
| Contract manufacturing net sales | 8,358 | — |
| Total net sales | 135,129 | 95,968 |
| Cost of sales (exclusive of amortization of purchased technology) | 16,189 | 5,520 |
| Gross profit | 118,940 | 90,448 |
| Operating expenses: | | |
| Selling and marketing | 35,461 | 21,716 |
| General and administrative | 12,548 | 5,442 |
| Research and development | 10,793 | 5,665 |
| Depreciation and amortization | 1,070 | 290 |
| Impairment of purchased technology | 719 | — |
| Total operating expenses | 60,591 | 33,113 |
| Income from operations | 58,349 | 57,335 |
| Interest and other (expense) income, net | (342) | 216 |
| Foreign currency transaction loss | (488) | — |
| Income before income taxes | 57,519 | 57,551 |
| Income tax expense | 18,455 | 19,008 |
| Net income | $ 39,064 | $ 38,543 |
| Change in unrealized gains or losses on available-for-sale securities, net of related tax effects and changes in foreign currency translation adjustments. | (1,194) | 91 |
| Comprehensive income | $ 37,870 | $ 38,634 |
| | | |
| Net income per share: | | |
| Basic | $ 0.68 | $ 0.61 |
| Diluted | $ 0.65 | $ 0.58 |
| Shares used in computing net income per share: | | |
| Basic | 57,857 | 63,491 |
| Diluted | 60,271 | 66,471 |
| | | |
| Dividends declared per share of common stock | $ 0.25 | $ — |

See accompanying notes.

**QUESTCOR PHARMACEUTICALS, INC.**
**CONDENSDED CONSOLIDATED STATEMENTS OF CASH FLOWS**
**(In thousands)**
**(unaudited)**

| | Three Months Ended March 31, | |
|---|---|---|
| | **2013** | **2012** |
| **OPERATING ACTIVITIES** | | |
| Net income | $ 39,064 | $ 38,543 |
| Adjustments to reconcile net income to net cash provided by operating activities: | | |
| Share-based compensation expense | 6,148 | 2,296 |
| Deferred income taxes | 411 | 67 |
| Amortization of investments | 182 | 546 |
| Depreciation and amortization | 2,137 | 290 |
| Impairment of purchased technology and goodwill | 719 | — |
| Loss on disposal of property and equipment | 21 | — |
| Changes in operating assets and liabilities, net of business acquisition: | | |
| Accounts receivable | 8,718 | (13,557) |
| Inventories | 4,637 | (298) |
| Prepaid income taxes | — | 760 |
| Prepaid expenses and other current assets | (198) | (272) |
| Accounts payable | (384) | 1,985 |
| Accrued compensation | (15,211) | (6,519) |
| Sales-related reserves | (11,546) | (354) |
| Income taxes payable | 5,643 | 17,556 |
| Contingent consideration | 505 | — |
| Other accrued liabilities | 538 | (13) |
| Other non-current liabilities | 68 | (120) |
| Net cash flows provided by operating activities | 41,452 | 40,910 |
| **INVESTING ACTIVITIES** | | |
| Purchase of property and equipment | (562) | (302) |
| Purchase of short-term investments | (33,539) | (71,074) |
| Proceeds from maturities of short-term investments | 30,038 | 32,235 |
| Acquisition of BioVectra, net of cash acquired | (46,692) | — |
| Deposits and other assets | — | 4 |
| Net cash flows used in investing activities | (50,755) | (39,137) |
| **FINANCING ACTIVITIES** | | |
| Repayment of funded long-term debt | (304) | — |
| Repayment of other long-term debt | (119) | — |
| Income tax benefit realized from share-based compensation plans | 1,991 | 1,380 |
| Issuance of common stock, net | 2,615 | 956 |
| Repurchase of common stock | — | (28,987) |
| Net cash flows provided by / (used in) financing activities | 4,183 | (26,651) |
| Effect of cash on changes in exchange rates | (84) | — |
| **Decrease in cash and cash equivalents** | (5,204) | (24,878) |
| Cash and cash equivalents at beginning of period | 80,608 | 88,469 |
| **Cash and cash equivalents at end of period** | $ 75,404 | $ 63,591 |
| **Supplemental Disclosures of Cash Flow Information:** | | |
| Cash paid for interest | $ 182 | $ 7 |
| Cash paid for income taxes | $ 9,707 | $ 32 |

| | | |
|---|---|---|
| **Supplemental Disclosures of Investing and Financing Activities:** | | |
| Dividend payable | $ 14,751 | $ — |
| **In conjunction with the acquisition of BioVectra at January 18, 2013:** | | |
| Incremental fair value of assets acquired, net | $ 80,698 | |
| Less: fair value of contingent consideration | (30,383) | |
| | 50,315 | |
| Loss on foreign exchange rate | 488 | |
| Total cash paid for acquisition of BioVectra | $ 50,803 | |

See accompanying notes.

## QUESTCOR PHARMACEUTICALS, INC.

## CONDENSED CONSOLIDATED STATEMENTS OF SHAREHOLDERS' EQUITY

| (in thousands, except per share data) | Common Stock | | Retained Earnings | Accumulated Other Comprehensive Gain (Loss) | Total Shareholders' Equity |
|---|---|---|---|---|---|
| | Shares | Amount | | | |
| Balances at December 31, 2012 | 58,544,206 | $ 15,938 | $ 145,851 | $ 40 | $ 161,829 |
| Stock compensation for equity incentives and restricted common stock granted to employees | 658,344 | 6,148 | | | 6,148 |
| Issuance of common stock pursuant to employee stock purchase plan | 47,035 | 1,026 | | | 1,026 |
| Dividends declared on shares of common stock | | | (14,751) | | (14,751) |
| Issuance of common stock upon exercise of stock options | 310,283 | 1,738 | | | 1,738 |
| Repurchase of common stock | — | — | — | — | — |
| Cancellation of shares related to tax liability | (5,723) | (149) | | | (149) |
| Income tax benefit realized from share-based compensation plans | | 1,991 | | | 1,991 |
| Comprehensive income (loss): | | | | | |
| Net unrealized gain on investments | | | | (5) | (5) |
| Foreign currency translation adjustments | | | | (1,189) | (1,189) |
| Net income | | | 39,064 | | 39,064 |
| Total comprehensive income | — | — | — | — | 37,870 |
| Balances at March 31, 2013 | 59,554,145 | $ 26,692 | $ 170,164 | $ (1,154) | $ 195,702 |

See accompanying notes.

**QUESTCOR PHARMACEUTICALS, INC.**

**NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**
**(unaudited)**

## 1. The Company

Questcor Pharmaceuticals, Inc. ("we", "our", "us", or the "Company") is a biopharmaceutical company primarily focused on the treatment of patients with serious, difficult-to-treat autoimmune and inflammatory disorders. We also supply specialty contract manufacturing services to the global pharmaceutical and biotechnology industry through our wholly-owned subsidiary, BioVectra Inc. Our primary product is H.P. Acthar® Gel (repository corticotropin injection), or Acthar, an injectable drug that is approved by the U.S. Food and Drug Administration, or FDA, for the treatment of 19 indications. Of the 19 FDA approved indications, we currently generate substantially all of our pharmaceutical net sales from the use of Acthar in connection with the following indications:

- Nephrotic Syndrome (NS): Acthar is indicated “to induce a diuresis or a remission of proteinuria in the nephrotic syndrome without uremia of the idiopathic type or that due to lupus erythematosus.” According to the National Kidney Foundation, nephrotic syndrome can result from several idiopathic type kidney disorders, including idiopathic membranous nephropathy, focal segmental glomerulosclerosis, IgA nephropathy and minimal change disease. Nephrotic syndrome can also occur due to lupus erythematosus. In this Form 10-Q, the terms “nephrotic syndrome” and “NS” refer only to the proteinuria in nephrotic syndrome conditions that are covered by the Acthar label of approved indications.
- Multiple Sclerosis (MS): Acthar is indicated “for the treatment of acute exacerbations of multiple sclerosis in adults. Controlled clinical trials have shown H.P. Acthar Gel to be effective in speeding the resolution of acute exacerbations of multiple sclerosis. However, there is no evidence that it affects the ultimate outcome or natural history of the disease.”
- Infantile Spasms (IS): Acthar is indicated “as monotherapy for the treatment of infantile spasms in infants and children under 2 years of age.” We continue to support this vulnerable patient population. We believe that a significant percentage of the $305 million in free drug that we have provided from September 2007 through March 31, 2013, has been used to treat IS. We support the IS community through other initiatives. In February 2012, we were awarded the first-ever Corporate Citizenship Award presented by the Child Neurology Foundation. This award honors our long-term commitment to support the child neurology community as well as our specific efforts to fund education and research related to IS.
- Rheumatology Related Conditions: Acthar is approved for the following rheumatology related conditions: (i) Collagen Diseases: Acthar is indicated "during an exacerbation or as maintenance therapy in selected cases of systemic lupus erythematosus, systemic dermatomyositis (polymyositis)" and (ii) Rheumatic Disorders: Acthar is indicated as "adjunctive therapy for short-term administration (to tide the patient over an acute episode or exacerbation) in: Psoriatic arthritis, Rheumatoid arthritis, including juvenile rheumatoid arthritis (selected cases may require low-dose maintenance therapy), and Ankylosing spondylitis."

We continue to explore the possible use of Acthar to provide therapeutic benefit to patients suffering from other serious, difficult-to-treat autoimmune and inflammatory disorders that are included on the Acthar label . In addition, we are exploring the possibility of pursuing FDA approval for additional indications not currently on the Acthar label, for other serious, difficult-to-treat autoimmune and inflammatory disorders.

In order to improve outcomes for patients with difficult-to-treat autoimmune and inflammatory disorders, we are expanding our research to better understand the mechanism(s) of action of Acthar as well as the pharmacology of Acthar across and within each indication. We are also conducting studies to expand our understanding of why Acthar acts differently than steroids and potentially other melanocortin peptides.

***Acquisition of BioVectra Inc.***

On January 18, 2013, we completed our acquisition of BioVectra Inc. BioVectra is located in Prince Edward Island, Canada, and is a supplier of specialty contract manufacturing services to the global pharmaceutical and biotechnology industry. BioVectra manufactures active pharmaceutical ingredients, or API, chemical intermediates, and bioprocessing reagents. BioVectra has been our manufacturing partner for the API in Acthar since April, 2003. BioVectra's facilities are staffed by 178 employees including chemists, engineers and technicians.

We acquired 100% of the issued and outstanding shares of BioVectra for $50.3 million utilizing cash on hand. The former shareholders of BioVectra could receive additional cash consideration of C$50.0 million based on BioVectra's financial results over the next three years, which consideration is payable annually with a final true-up payment in the third year. Contingent

consideration in conjunction with the acquisition of BioVectra of $30.4 million was recorded on our condensed consolidated balance sheet at the acquisition date. Any differences between our estimate and actual payments or subsequent adjustments will be recorded in interest and other (expense) income, net.

As of March 31, 2013, there were no changes in the recognized amount or range of outcomes for the contingent consideration recognized as a result of our acquisition of BioVectra. As of March 31, 2013, the estimated value of the contingent consideration of $30.2 million has been recorded as a liability in our condensed consolidated balance sheets ($4.5 million has been recorded as the current portion of the contingent consideration).

For the three months ended March 31, 2013, we recorded $0.2 million of acquisition-related expenses associated with the BioVectra acquisition within general and administrative expenses in our condensed consolidated statements of income and comprehensive income.

The acquisition was recorded by allocating the estimated value of consideration paid by us for the BioVectra acquisition to the assets acquired including intangible assets, and liabilities assumed, based on their estimated fair values at the acquisition date in accordance with the acquisition method of accounting. We are in the process of finalizing the estimated amounts shown below and such amounts are provisional measurements that are subject to change.

The following table reflects the fair value of consideration transferred at the acquisition date (in thousands):

| | | |
|---|---|---|
| *Allocation of Purchase Price*: | | |
| Current assets excluding inventory | $ | 11,362 |
| Inventory | | 11,774 |
| Property and equipment | | 35,221 |
| Other non-current assets | | 1,708 |
| Current deferred tax asset | | 141 |
| Intangibles | | 35,581 |
| Goodwill | | 21,022 |
| Current liabilities | | (5,230) |
| Non-current liabilities, excluding long-term debt | | (1,994) |
| Non-current deferred tax liability | | (12,012) |
| Long-term debt | | (16,875) |
| Total net assets acquired | $ | 80,698 |
| | | |
| Cash consideration paid to BioVectra shareholders | $ | 50,315 |
| Estimated fair value of contingent considerations | | 30,383 |
| Total purchase consideration | $ | 80,698 |

The following unaudited pro forma financial information for the three months ended March 31, 2013 and 2012 presents the combined results of operations of Questcor and the BioVectra acquisition described above, as if the acquisition had occurred as of January 1 of the year prior to acquisition. The unaudited pro forma financial information is not intended to represent or be indicative of the Company's consolidated results of operations or financial condition that would have been reported had these acquisitions been completed as of the beginning of the periods presented and should not be taken as indicative of the Company's future consolidated results of operations or financial condition. Pro forma adjustments are tax-effected at the applicable statutory tax rates.

| | Three Months Ended March 31, | |
|---|---|---|
| | **2013** | **2012** |
| Net sales | $ 136,986 | $ 102,677 |
| Net income | $ 38,454 | $ 36,472 |

The above pro forma results could change if the provisional measurements change.

## 2. Summary of Significant Accounting Policies

***Basis of Presentation***

The condensed consolidated financial statements include the accounts of the Company and our wholly-owned subsidiaries. All significant inter-company accounts and transactions have been eliminated in consolidation. In the opinion of the Company's management, all adjustments (consisting of normal recurring adjustments) considered necessary for the fair presentation of interim financial information have been included.

The financial statements of our subsidiaries with functional currencies other than the U.S. dollar are translated into U.S. dollars using period-end exchange rates for assets and liabilities, historical exchange rates for shareholders' equity and weighted average exchange rates for operating results. Translation gains and losses are included in accumulated other comprehensive income in stockholders' equity. Foreign currency transaction gains and losses are included in the results of operations in our condensed consolidated statements of income and comprehensive income.

***Use of Estimates***

The preparation of financial statements in conformity with U.S generally accepted accounting principles, or GAAP, requires us to make estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes. Actual results could materially differ from those estimates. Our significant estimates include our estimates for sales-related reserves, impairment of intangibles, deferred tax assets and tax liabilities and share-based compensation, among others.

***Revenue Recognition***

We recognize revenue in accordance with Accounting Standards Codification 605, “Revenue Recognition-Products,” or ASC 605. Pursuant to ASC 605, we recognize revenue when we have persuasive evidence that an arrangement, agreement or contract exists, when title for our product and risk of loss have passed to our customer, the price we charge for our product is fixed or is readily determinable, and we are reasonably assured of collecting the amounts owed under the resulting receivable. We do not require collateral from our customers. In order to ensure that patients who need Acthar are able to obtain it regardless of ability to pay, we support the patient assistance programs administered by the National Organization of Rare Disorders, or NORD, and the Chronic Disease Fund by providing free drug with a commercial value of over $305 million to patients since September 2007 through March 31, 2013. We do not recognize any revenue from the Acthar free drug program.

In the U.S., our exclusive customer for Acthar is CuraScript Specialty Distributor, or CuraScript SD. For our sales to CuraScript SD, a sale of Acthar occurs when CuraScript SD accepts a shipment of Acthar based on its order of Acthar from Integrated Commercial Services, which we have engaged to act as our exclusive agent for commercial shipment of Acthar to CuraScript SD. We sell Acthar at a discount from our list price to CuraScript SD, which then sells Acthar primarily to approximately 12 specialty pharmacy companies, including CuraScript Specialty Pharmacy, or CuraScript SP, and to many hospitals.

International sales of our products are immaterial.

*Net Sales*

We record net sales after establishing reserves for the following:

- Medicaid rebates;
- TRICARE retail program rebates;
- Medicare Part D Coverage Gap Discount Program rebates;
- Chargebacks due to other government programs;
- Questcor-sponsored co-pay assistance programs;
- Exchanges, which have historically been immaterial; and
- Other deductions, such as payment discounts.

We currently provide our products to Medicaid participants under an agreement with the Centers for Medicare & Medicaid Services, or CMS. Under this agreement, states are eligible to receive rebates from us for Medicaid patients in

accordance with CMS regulations. For the three months ended March 31, 2012, the rebate amount equaled 100% of the Average Manufacturers' Price, or AMP, which approximates the amount we charge to CuraScript SD. During the three months ended March 31, 2013, the rebate amount in the Medicaid system was reset from 100% of the AMP of Acthar to the basic 23.1% of AMP. States have historically provided us with rebate invoices for their Medicaid Fee for Service reimbursements between 60 and 90 days after the end of the calendar quarter in which our products were provided. Certain states are taking longer to submit their initial rebate invoices for the Medicaid Managed Care utilization that became rebate eligible on March 23, 2010, as a result of the enactment of the Patient Protection and Affordable Care Act and the Health Care and Education Reconciliation Act of 2010, or the Health Care Reform Acts.

We estimate the end of period liability and the sales reserve needed for Medicaid rebates, TRICARE retail program rebates, Medicare Part D Coverage Gap Discount Program rebates, or Coverage Gap Discount rebates (commonly referred to as the Medicare Part D "donut hole"), and chargebacks due to other government programs.

Our resulting total sales reserve for the quarter includes the sum of the Medicaid sales reserve, the TRICARE sales reserve, the Coverage Gap Discount reserve, the chargeback sales reserve, co-pay assistance payments, and payment discounts provided.

Significant judgment is inherent in the selection of assumptions and the interpretation of historical experience as well as the identification of external and internal factors affecting the determination of our reserves for Medicaid rebates and other government program rebates and chargebacks. We believe that the assumptions used to determine these sales reserves are reasonable considering known facts and circumstances. However, our Medicaid rebates and other government program rebates and chargebacks could materially differ from our reserve amounts because of, among other factors, unanticipated changes in prescription trends or patterns in the states' submissions of Medicaid claims, adjustments to the amount of product in the distribution channel, or if our estimates of the number of Medicaid patients treated with Acthar, or the number of vials used by such patients, are incorrect. If actual Medicaid rebates, or other government program rebates and chargebacks, are materially different from our estimates, we would account for such differences as a change in estimate in the period in which they become known. If actual future payments for such reserves exceed the estimates we made at the time of sale, our consolidated financial position, results of operations and cash flows may be negatively impacted.

*Total Sales-related Reserves*

At March 31, 2013 and December 31, 2012, sales-related reserves included in the accompanying condensed consolidated balance sheets were as follows (in thousands):

| | March 31, 2013 | December 31, 2012 |
|---|---|---|
| Medicaid rebates | $ 22,237 | $ 33,921 |
| Tricare rebates | 3,190 | 3,222 |
| Medicare Part D Coverage Gap Discount Program rebates | 205 | 194 |
| Government chargebacks | 38 | 38 |
| Other discounts | 160 | 1 |
| Total | $ 25,830 | $ 37,376 |

The following table summarizes the activity in the account for sales-related reserves for Medicaid rebates (in thousands):

| | 2013 | 2012 |
|---|---|---|
| Balance at January 1 | $ 33,921 | $ 29,874 |
| Actual Medicaid payments for sales made in prior year | (17,712) | (14,138) |
| Actual Medicaid payments for sales made in current year | — | — |
| Current Medicaid provision for sales made in prior year | (3) | — |
| Current Medicaid provision for sales made in current year | 6,031 | 13,312 |
| Balance at March 31 | $ 22,237 | $ 29,048 |

The following table summarizes the activity in the account for sales-related reserves for TRICARE rebates (in thousands):

| | 2013 | 2012 |
|---|---|---|
| Balance at January 1 | $ 3,222 | $ 4,095 |
| Actual TRICARE payments for sales made in prior year | (1,571) | (571) |
| Actual TRICARE payments for sales made in current year | — | — |
| Current TRICARE provision for sales made in prior year | — | — |
| Current TRICARE provision for sales made in current year | 1,539 | 1,077 |
| Balance at March 31 | $ 3,190 | $ 4,601 |

***Product Exchanges and Returns***

Acthar has a shelf life of 18 months from the date of manufacture. We authorize Acthar exchanges for expiring and expired product in accordance with our stated return policy, which allows CuraScript SD to return product within one month of its expiration date and for a period up to three months after such product has reached its expiration date. Product exchanges have been insignificant since we began utilizing the services of CuraScript SD to distribute Acthar.

For our contract manufactured finished goods sold through our BioVectra subsidiary, we warrant that our products conform to the applicable product specifications. Each product is shipped with a Certificate of Analysis stating the conditions and results of product performance tests. Our customers must determine the suitability of our product. We do not accept liability for any incidental, direct or indirect consequential or contingent damages arising out of the use, result of use, or the inability to use our products. Should any of our products fail to meet its described specifications for reasons other than misuse or mishandling, at our option, we will either replace the product free of charge or refund the purchase price. We reserve the right to deny a return when the date of the invoice is greater than 30 days from the return request date, or for any other reason as covered by our warranty.

***Concentration of Credit Risk***

Financial instruments that subject us to a significant concentration of credit risk principally consist of cash and cash equivalents, short-term investments and accounts receivable. We invest our cash in high credit quality government and corporate debt instruments and believe the financial risks associated with these instruments are minimal.

Cash and cash equivalents are maintained at financial institutions and, at times, balances may exceed federally insured limits. We have never experienced any losses related to these balances. Beginning January 1, 2013, all of our non-interest bearing cash balances were insured up to $250,000 per depositor at each financial institution. We did not have any non-interest-bearing amounts on deposit in excess of federally insured limits at March 31, 2013.

We extend credit to our customer, CuraScript SD, which accounts for approximately 94% of our gross product sales and 85% of our accounts receivable. We have not experienced material credit losses on our customer accounts.

***Inventories***

We state inventories, net of allowances, at the lower of cost or market value. For our Acthar product, cost is determined by the first-in, first-to-expire method. For our production materials and supplies, work-in-process and finished goods at our contract manufacturer, cost is determined on an average cost basis.

We review inventory periodically for slow-moving or obsolete status. We adjust our inventory if we do not expect to recover the cost of inventory. We would record a reserve to adjust inventory to its net realizable value when any of the following occur: (i) a product is close to expiration and we do not expect it to be sold, (ii) a product has reached its expiration date or (iii) we do not expect a product to be saleable. In determining the reserves for these products, we consider factors such as the amount of inventory on hand and its remaining shelf life, and current and expected market conditions, including management forecasts and levels of competition. We have evaluated the current level of inventory considering historical trends and other factors, and based on our evaluation, have recorded adjustments to reflect inventory at its net realizable value. These adjustments are estimates, which could vary significantly from actual results if future economic conditions, customer demand, competition or other relevant factors differ from expectations. These estimates require us to assess the future demand for our products in order to categorize the status of such inventory items as slow-moving, obsolete or in excess-of-need. These future estimates are subject to the ongoing accuracy of our forecasts of market conditions, industry trends, competition and other factors. Differences between our estimated reserves and actual inventory adjustments have been immaterial, and we account for such adjustments in the current period as a change in estimate.

The components of inventory are as follows (in thousands):

| | March 31, 2013 | December 31, 2012 |
|---|---|---|
| Raw material | $ 9,125 | $ 9,271 |
| Work-in-process | 2,135 | — |
| Intermediates | 1,568 | — |
| Finished goods | 5,163 | 690 |
| | 17,991 | 9,961 |
| Less: Reserve for obsolescence | 1,205 | 52 |
| | $ 16,786 | $ 9,909 |

Included in inventories at March 31, 2013 is $9.2 million held at BioVectra, in Canada.

***Property, Plant and Equipment***

Equipment and leasehold improvements and related accumulated depreciation and amortization are as follows (in thousands):

| | March 31, 2013 | December 31, 2012 |
|---|---|---|
| Equipment (including manufacturing, laboratory and office) | $ 48,174 | $ 3,466 |
| Building | 14,450 | — |
| Land | 454 | — |
| Leasehold improvements | 1,446 | 1,349 |
| | 64,524 | 4,815 |
| Less accumulated depreciation and amortization | (28,782) | (2,742) |
| | $ 35,742 | $ 2,073 |

Total depreciation and amortization expense amounted to $1.3 million and $0.2 million for the three months ended March 31, 2013 and 2012 respectively. The increase in depreciation and amortization expense was due to the amortization on the intangibles acquired in conjunction with the acquisition of BioVectra. We depreciate our property and equipment and amortize our leasehold improvements using the straight-line method of depreciation. Included in property and equipment at March 31, 2013 is $33.7 million held at BioVectra, in Canada.

***Supply Concentration Risks***

Acthar is derived from the extraction and purification of porcine pituitary glands through complicated processes, and is difficult to manufacture. Acthar bulk concentrate, the API used in Acthar, is processed at our BioVectra subsidiary, in several stages to produce a highly purified raw material for formulation. We have a supply agreement with Cangene bioPharma, Inc., or Cangene, to manufacture commercial quantities of Acthar finished product. Currently, Cangene is our sole source supplier of Acthar finished product. Additionally, we use a sole source provider for potency testing. The processes used to manufacture and test Acthar are complex and subject to FDA inspection and approval. Acthar finished product has a shelf life of 18 months from the date of manufacture.

***Cash Equivalents and Short-Term Investments***

We consider highly liquid investments with maturities from the date of purchase of three months or less to be cash equivalents. We classify available-for-sale debt instruments with maturities at the date of purchase of greater than three months as short-term investments.

We carry available-for-sale securities at fair value, with the unrealized gains and losses, if any, reported in the Condensed Consolidated Statements of Income and Comprehensive Income. If we deem the decline in value to be other-than-temporary and we intend to sell such securities before their full cost can be recovered, we write down such securities to fair value and we charge the loss to net realized losses on investments. We use significant judgment in the determination of when an other-than-temporary decline in value has occurred. We evaluate our investment securities for other-than-temporary declines based on

quantitative and qualitative factors. As of March 31, 2013, none of our investments had an other-than-temporary decline in valuation, and no other-than-temporary losses were recognized during the three months ended March 31, 2013 and 2012, respectively. We base the cost of securities sold on the specific identification method. We include realized gains and losses, if any, in the accompanying Condensed Consolidated Statements of Income and Comprehensive Income, in Interest and Other Income.

A summary of cash and cash equivalents and short-term investments, classified as available-for-sale, and carried at fair value is as follows (in thousands):

| | Amortized Cost | Gross Unrealized Gain | Gross Unrealized (Loss) | Estimated Fair Value |
|---|---|---|---|---|
| **March 31, 2013** | | | | |
| Cash and cash equivalents | $ 4,492 | $ — | $ — | $ 4,492 |
| Short-term investments: | | | | |
| Certificates of deposit | $ 720 | $ 1 | | $ 721 |
| Corporate bonds | 46,689 | 24 | (8) | 46,705 |
| Government-sponsored enterprises | 28,589 | 12 | (2) | 28,599 |
| Municipal bonds | 1,994 | 1 | — | 1,995 |
| | $ 77,992 | $ 38 | $ (10) | $ 78,020 |
| **December 31, 2012** | | | | |
| Cash and cash equivalents | $ 7,740 | $ — | $ — | $ 7,740 |
| Short-term investments: | | | | |
| Certificates of deposit | $ 720 | $ 2 | $ — | $ 722 |
| Corporate bonds | 47,857 | 29 | (8) | 47,878 |
| Government-sponsored enterprises | 24,699 | 13 | — | 24,712 |
| Municipal bonds | 1,395 | 1 | (3) | 1,393 |
| | $ 74,671 | $ 45 | $ (11) | $ 74,705 |

The amortized cost and fair value of short-term investment securities at March 31, 2013, by contractual maturity, are as follows (in thousands):

| | Amortized Cost | Estimated Fair Value |
|---|---|---|
| Due in one year or less | $ 48,229 | $ 48,247 |
| Due after one through two years | 29,763 | 29,773 |
| Total short-term investments | $ 77,992 | $ 78,020 |

As of March 31, 2013, the average contractual maturity of our short-term investments was approximately 14 months.

As of March 31, 2013, we had the following available-for-sale securities that were in an unrealized loss position but were not deemed to be other-than-temporarily impaired (in thousands):

| | Less Than 12 Months | | 12 Months or Greater | |
|---|---|---|---|---|
| | Gross Unrealized Losses | Estimated Fair Value | Gross Unrealized Losses | Estimated Fair Value |
| Corporate bonds | $ (8) | $ 16,497 | $ — | $ 355 |
| Government-sponsored enterprises | — | — | (2) | 11,003 |
| Municipal bonds | — | 564 | — | 205 |
| Total | $ (8) | $ 17,061 | $ (2) | $ 11,563 |

The gross unrealized losses reported above for March 31, 2013 were caused by general fluctuations in market interest rates from the respective purchase date of these securities through March 31, 2013. No significant facts or circumstances have occurred to indicate that these unrealized losses are related to any deterioration in the creditworthiness of the issuers of the

marketable securities we own. Based on our review of these securities, including our assessment of the duration and severity of the related unrealized losses, we have not recorded any other-than-temporary impairments on these investments. For the three months ended March 31, 2013, we did not realize any gains or losses.

***Fair Value of Financial Instruments***

Our financial instruments include cash and cash equivalents, short-term investments, accounts receivable, accounts payable, dividends payable and accrued liabilities. We believe that the fair value of these financial instruments approximate the reported carrying amounts.

***Fair Value Measurements***

We account for fair value measurements under Accounting Standards Codification 820 “Fair Value Measurements and Disclosures,” or ASC 820, which defines fair value as the exchange price that would be received for an asset or paid to transfer a liability (an exit price) in the principal or most advantageous market for the asset or liability in an orderly transaction between market participants at the measurement date. ASC 820 establishes a three-level fair value hierarchy that prioritizes the inputs used to measure fair value. This hierarchy requires entities to maximize the use of observable inputs and minimize the use of unobservable inputs. The three levels of inputs used to measure fair value are as follows:

- Level 1 – Quoted prices in active markets for identical assets or liabilities.
- Level 2 – Observable inputs other than quoted prices included in Level 1, such as quoted prices for similar assets and liabilities in active markets; quoted prices for identical or similar assets and liabilities in markets that are not active; or other inputs that are observable or can be corroborated by observable market data.
- Level 3 – Unobservable inputs that are supported by little or no market activity and that are significant to the fair value of the assets or liabilities. This includes certain pricing models, discounted cash flow methodologies and similar techniques that use significant unobservable inputs.

We have segregated all assets and liabilities measured at fair value on a recurring basis (at least annually) into the most appropriate level within the fair value hierarchy based on the inputs used to determine the fair value at the measurement date in the table below. As of March 31, 2013, assets and liabilities measured at fair value on a recurring basis are summarized below (in thousands):

| | | Basis of Fair Value Measurements | | | |
|---|---|---|---|---|---|
| **Balance Sheet Classification** | | **Balance at March 31, 2013** | **Level 1** | **Level 2** | **Level 3** |
| Cash and cash equivalents | Cash and cash equivalents | $ 4,492 | $ 4,492 | $ — | $ — |
| Short-term investments | Certificates of deposit | 721 | 721 | — | — |
| Short-term investments | Corporate bonds | 46,705 | 46,705 | — | — |
| Short-term investments | Government-sponsored enterprises | 28,599 | 28,599 | — | — |
| Short-term investments | Municipal bonds | 1,995 | 1,995 | — | — |
| | Total assets | $ 82,512 | $ 82,512 | $ — | $ — |
| | | | | | |
| Current liabilities | Current portion of contingent consideration | 4,485 | — | — | 4,485 |
| Non-current liabilities | Contingent consideration | 25,747 | — | — | 25,747 |
| | Total liabilities | $ 30,232 | $ — | $ — | $ 30,232 |

The fair value of contingent consideration in conjunction with the acquisition of BioVectra was determined to be Level 3 under the fair value hierarchy. The following table presents the fair value, valuation technique and related unobservable input for the Level 3 measurements:

| | Fair Value | Valuation Technique | Unobservable Input | Rate |
|---|---|---|---|---|
| Contingent consideration estimate | $ 30,232 | Probability weighted discounted future cash flows | Discount rate | 5% |

Investment securities are exposed to various risk factors, such as interest rate, market and credit risk. Due to the level of risk associated with certain investment securities and the level of uncertainty related to changes in the value of investment securities, it is possible that changes in these risk factors in the near term could have an adverse material impact on our results of operations or shareholders' equity.

The following table represents a roll forward of the fair value of Level 3 instruments, comprised solely of the contingent consideration, including the current portion of the contingent consideration:

| | March 31, 2013 |
|---|---|
| Balance at beginning of period | $ — |
| Amounts acquired or issued | 30,383 |
| Changes in fair value | (151) |
| Balance at end of period | $ 30,232 |

Certain assets and liabilities are measured at fair value on a nonrecurring basis. In other words, the instruments are not measured at fair value on an ongoing basis but are subject to fair value adjustments only in certain circumstances (for example, when there is evidence of impairment).

Our product, Doral® (quazepam), is indicated for the treatment of insomnia characterized by difficulty in falling asleep, frequent nocturnal awakenings, and/or early morning awakenings. At March 31, 2013, we determined that a portion of the value of our purchased technology associated with the acquisition of Doral was impaired. This determination was based on a signed purchase agreement for the disposition of Doral subsequent to March 31, 2013. Based on the agreement, we will not recover $0.7 million as of March 31, 2013. See "Subsequent Events" for further details. There were no other assets or liabilities measured at fair value on a nonrecurring basis during the three months ended March 31, 2013 and 2012, respectively.

***Long-term Debt***

*Funded long-term debt*

Our subsidiary, BioVectra, has a supply agreement with a customer to supply a pharmaceutical product for a period of 10 years. Per the supply agreement, BioVectra financed and constructed a facility for the manufacturing of the pharmaceutical product to be supplied under the agreement. BioVectra entered into a term loan agreement with Prince Edward Island Century 2000 Fund Inc. to finance $14.8 million of the construction costs of the facility. The term loan has an interest rate of 4%, is due in full by February 2022 and is secured by certain of our BioVectra assets. Under the supply agreement, the customer agreed to reimburse BioVectra for the quarterly financing payments of $450,743 during the term of the loan.

| | March 31, 2013 |
|---|---|
| 4% Term Loan, due February 2022, payable in quarterly installments of $450,743 including principal and interest | $ 13,642 |
| Less: Current Portion | 1,233 |
| Funded long-term debt, less current portion | $ 12,409 |

*Long-term debt*

Our subsidiary, BioVectra, has a 3.3% term loan. The loan is payable monthly and was due April 2013; however, the lender has provided a letter indicating that it will not demand payment prior to April 1, 2014, as long as the loan remains in good-standing. The loan is secured with BioVectra accounts receivable and inventory.

| | March 31, 2013 |
|---|---|
| 3.3% Term Loan, due April 2013, payable in monthly installments of $49,466 including principal and interest | $ 4,100 |
| Less: Current Portion | 447 |
| Funded long-term debt, less current portion | $ 3,653 |

***Share-based Compensation***

We recognize compensation expense for all share-based awards made to employees and directors. The fair value of share-based awards is estimated at grant date using an option pricing model and the portion that is ultimately expected to vest is recognized as compensation cost over either (1) the requisite service period or (2) the performance period.

Since share-based compensation is recognized only for those awards that are ultimately expected to vest, we have applied an estimated forfeiture rate to unvested awards for the purpose of calculating compensation cost. These estimates will be revised, if necessary, in future periods if actual forfeitures differ from estimates. Changes in forfeiture estimates impact compensation cost in the period in which the change in estimate occurs.

We use the Black-Scholes option-pricing model to estimate the fair value of share-based awards. The determination of fair value using the Black-Scholes option-pricing model is affected by our stock price as well as assumptions regarding a number of complex and subjective variables, including expected stock price volatility, risk-free interest rate, expected dividends and projected employee stock option behaviors. We estimate the expected term based on the contractual term of the awards and employees' exercise and expected post-vesting termination behavior.

We use the intrinsic method to account for restricted stock awards. The restricted stock awards are valued based on the closing stock price on the date of grant and amortized ratably over the life of the award.

Additionally, we are required to disclose in our consolidated statements of cash flows the income tax effects resulting from share-based payment arrangements. We adopted the simplified method to calculate the beginning balance of the additional paid-in capital, or APIC, pool of excess tax benefits, and to determine the subsequent effect on the APIC pool and consolidated statements of cash flows of the tax effects of employee share-based compensation awards.

At March 31, 2013, we had $64.4 million of total unrecognized compensation cost related to unvested stock options and unvested restricted awards, which is expected to be recognized over a remaining weighted average vesting period of approximately 2.5 years.

Share-based compensation cost is summarized below (in thousands):

| | Three Months Ended March 31, | |
|---|---|---|
| | 2013 | 2012 |
| Selling and marketing | $ 2,454 | $ 1,046 |
| General and administrative | 2,538 | 464 |
| Research and development | 1,156 | 786 |
| Total | $ 6,148 | $ 2,296 |

***Net Income Per Share***

Basic net income per share applicable to common shareholders is computed by dividing the net income for the period by the weighted average number of common shares outstanding during the period. Diluted net income per share is computed by dividing the net income for the period by the weighted average number of common and common equivalents shares, such as stock options and restricted stock outstanding during the period. Diluted earnings for our common shareholders per common stock considers the impact of potentially dilutive securities and excludes the impact of potential common shares related to our stock options and restricted stock in periods in which the option exercise or conversion price is greater than the average market price of our common stock during the period.

The following table presents the amounts used in computing basic and diluted net income per share applicable to common shareholders for the three months ended March 31, 2013 and 2012 and the effect of dilutive potential common shares on the number of shares used in computing dilutive net income per share applicable to common shareholders. Diluted potential

common shares resulting from the assumed exercise of outstanding stock options and restricted stock are determined based on the treasury stock method (in thousands, except per share amounts).

| | Three Months Ended March 31, | |
|---|---|---|
| | 2013 | 2012 |
| Net income applicable to common shareholders | $ 39,064 | $ 38,543 |
| Shares used in computing net income per share applicable to common shareholders: | | |
| Basic | 57,857 | 63,491 |
| Effect of dilutive potential common shares: | | |
| Stock options | 2,288 | 2,958 |
| Restricted stock | 126 | 22 |
| Diluted | 60,271 | 66,471 |
| Net income per share applicable to common shareholders: | | |
| Basic | $ 0.68 | $ 0.61 |
| Diluted | $ 0.65 | $ 0.58 |

The following table presents the amounts excluded from the computation of diluted net income per share applicable to common shareholders for the three months ended March 31, 2013 and 2012 as the inclusion of these securities would have been anti-dilutive (in thousands):

| | Three Months Ended March 31, | |
|---|---|---|
| | 2013 | 2012 |
| Stock options | 2,068 | 590 |
| Restricted stock awards | 78 | — |

Basic and diluted net income per share also takes into consideration the two-class method. Under the two-class method, undistributed net income is allocated to common stock and unvested participating securities based on their respective rights to share in dividends. We have determined that restricted stock awards represent participating securities and, therefore, require the use of the two-class method for the calculation of basic and diluted earnings per share. The following table sets forth the calculation of unallocated undistributed earnings, both basic and diluted, using the two-class method for amounts attributable to our common stock and our restricted stock awards (in thousands):

| | Three months ended March 31, | |
|---|---|---|
| | 2013 | 2012 |
| Net income applicable to common shareholders | $ 39,064 | $ 38,543 |
| Less: Dividends declared | 14,751 | — |
| Undistributed earnings | $ 24,313 | $ 38,543 |
| | | |
| Common stock undistributed earnings | 23,878 | 38,500 |
| Unvested restricted stock award undistributed earnings | 435 | 43 |
| Total undistributed earnings | $ 24,313 | $ 38,543 |

***Dividend Program***

During September 2012, our Board of Directors adopted a policy to pay a regular quarterly dividend in such amounts as the Board of Directors may determine from time to time. The Board of Directors declared an initial quarterly cash dividend of $0.20 per common share to all shareholders of record at the close of business on October 31, 2012. In December 2012, we announced an accelerated cash dividend of $0.20 per share to all shareholders of record at the close of business on December 14, 2012. The accelerated dividend was in lieu of any quarterly dividend we otherwise would have declared in the first quarter

of 2013. In February 2013, we announced an increase in our quarterly cash dividend from $0.20 per share to $0.25 per share, with such increase occurring with the quarterly cash dividend paid on April 30, 2013.

***Purchased Technology, Goodwill and Intangibles***

Purchased technology consists of the following (in thousands):

| | March 31, 2013 | December 31, 2012 |
|---|---|---|
| Purchased technology | $ 4,386 | $ 4,386 |
| Less accumulated amortization | (3,686) | (2,893) |
| | $ 700 | $ 1,493 |

Purchased technology at March 31, 2013 and December 31, 2012 consists of our acquisition costs for Doral. Amortization expense for purchased technology totaled $0.1 million for the three months ended March 31, 2013 and $0.3 million for the year ended December 31, 2012. At March 31, 2013, we determined that a portion of the value of our purchased technology associated with the acquisition of Doral was impaired. Subsequent to March 31, 2013, we entered into a purchase agreement to sell Doral. The agreed upon purchase price was $0.7 million. Based on the purchase agreement, we will not recover $0.7 million of the remaining asset value as of March 31, 2013. As of December 31, 2012, we had not yet made this determination.

Goodwill and intangibles acquired in conjunction with the acquisition of BioVectra, consists of the following (in thousands):

| | March 31, 2013 | December 31, 2012 |
|---|---|---|
| Acquired intangibles | $ 34,768 | $ — |
| Less accumulated amortization | (776) | — |
| Acquired intangibles, net | $ 33,992 | $ — |
| Goodwill | $ 20,597 | $ — |

The following table summarizes the changes in the carrying amount of goodwill (in thousands):

| | |
|---|---|
| Balance at December 31, 2012 | $ — |
| Goodwill resulting from the acquisition of BioVectra | 21,022 |
| Currency translation | (425) |
| Balance at March 31, 2013 | $ 20,597 |

The following table summarizes the changes in the carrying amount of intangibles (in thousands):

| | |
|---|---|
| Balance at December 31, 2012 | $ — |
| Intangibles resulting from the acquisition of BioVectra | 35,581 |
| Amortization expense | (776) |
| Currency translation | (813) |
| Balance at March 31, 2013 | $ 33,992 |

Amortization expense for BioVectra's intangibles totaled $0.8 million for the three months ended March 31, 2013. The estimated annual amortization expense for intangible assets is approximately $2.3 million in 2013, $3.4 million in 2014, $3.4 million in 2015, $3.2 million in 2016 and $3.0 million in 2017 and $10.7 million thereafter. Amortizable intangible assets are amortized over 8 to 10 years (9 years average). Customer relationships are amortized on an accelerated basis over their useful lives.

***Commitments and Contingencies***

BioVectra receives funding from the Atlantic Canada Opportunities Agency (“ACOA”) which is contingently repayable on a royalty basis upon sales of commercialized products resulting from 4 projects. In the event that the products are not

commercialized under the program or do not continue to generate revenues, the royalty agreement will be terminated without future obligation to BioVectra. Royalties paid under this agreement in the quarter ended March 31, 2013 were immaterial.

We operate in a highly regulated industry. We are subject to the regulatory authority of the SEC, the FDA and numerous other federal, state and foreign governmental agencies including state attorney general offices, which have become more active in investigating the business practices of pharmaceutical companies.

As permitted under California law and in accordance with our Amended and Restated Bylaws, we indemnify our officers and directors for certain events or occurrences while the officer or director is or was serving at our request in such capacity. The potential future indemnification limit is to the fullest extent permissible under California law. However, we have a director and officer insurance policy that limits our exposure and may enable us to recover a portion of any future amounts paid. We believe the fair value of these indemnification agreements in excess of applicable insurance coverage is minimal. Accordingly, we have no liabilities recorded for these agreements as of March 31, 2013 and December 31, 2012.

Glenridge Litigation

In June 2011, Glenridge Pharmaceuticals LLC, or Glenridge, filed a lawsuit against us in the Superior Court of California, Santa Clara County, alleging that we had underpaid royalties to Glenridge, in connection with the timing of the impact of various offsets in the calculation of net sales. We are defending this lawsuit vigorously. In October 2012, a Judge of the Superior Court denied Glenridge's motion for summary judgment on its claims. In March 2013, Glenridge amended its complaint and added causes of action for breach of contract and breach of the implied covenant of good faith and fair dealing. In April 2013, we filed our answer to this amended complaint.

In August 2012, we filed a separate lawsuit in the Superior Court of California, Orange County, against the three principals of Glenridge, as well as Glenridge, challenging the enforceability of our agreement with Glenridge, and alleging breach of fiduciary duty, as well as aiding and abetting of the breach, by the principals. In November 2012, a Judge of the Superior Court of California, Orange County, transferred this lawsuit to the Superior Court of California, Santa Clara County. In February 2013, a Judge of the Superior Court denied Glenridge's motion to stay this lawsuit in favor of the accounting lawsuit described in the immediately preceding paragraph. We have filed a motion for summary judgment on issues related to the fiduciary duty claim. A hearing on the motion is likely to occur in July 2013.

USAO Investigation

On September 21, 2012, we became aware of an investigation by the United States Attorney's Office for the Eastern District of Pennsylvania (the "USAO") regarding our promotional practices. Following our September 24, 2012 announcement of this investigation, we received a subpoena from the USAO for information relating to our promotional practices. We are cooperating with the USAO with regard to this investigation.

Putative Class Action Securities Litigation

On September 26, 2012, a putative class action lawsuit was filed against us and certain of our officers and directors in the United States District Court for the Central District of California, captioned *John K. Norton v. Questcor Pharmaceuticals, et al.*, No. SACv12-1623 DMG (FMOx). The complaint purports to be brought on behalf of shareholders who purchased our common stock between April 26, 2011 and September 21, 2012. The complaint generally asserts that we and certain of our officers and directors violated sections 10(b) and/or 20(a) of the Securities Exchange Act of 1934, as amended, or the Exchange Act, by making allegedly false and/or misleading statements concerning the clinical evidence to support the use of Acthar for indications other than infantile spasms, the promotion of the sale and use of Acthar in the treatment of MS and nephrotic syndrome, reimbursement for Acthar from third-party insurers, and our outlook and potential market growth for Acthar. The complaint seeks damages in an unspecified amount and equitable relief against the defendants. This lawsuit has been consolidated with four subsequently-filed actions asserting similar claims under the caption: *In re Questcor Securities Litigation*, No. CV 12-01623 DMG (FMOx). On January 4, 2013, the district court issued an order appointing the West Virginia Investment Management Board and Plumbers & Pipefitters National Pension Fund as Lead Plaintiffs in the consolidated securities action. In March 2013, the Lead Plaintiffs filed a consolidated amended complaint for the consolidated securities action. We will be filing a motion to dismiss the consolidated amended complaint in May 2013.

Federal Shareholder Derivative Litigation

On October 4, 2012, another alleged shareholder filed a derivative lawsuit in the United States District Court for the Central District of California captioned *Gerald Easton v. Don M. Bailey, et al.*, No. SACV12-01716 DOC (JPRx). The suit asserts claims substantially identical to those asserted in the *do Valle* derivative action described below against the same defendants. This lawsuit has been consolidated with five subsequently-filed actions asserting similar claims under the caption:

*In re Questcor Shareholder Derivative Litigation, CV 12-01716 DMG (FMOx)*. In March 2013, the parties entered into a stipulation to stay the consolidated federal derivative lawsuit, pending resolution of the motion to dismiss the consolidated securities action.

State Shareholder Derivative Litigation

On October 2, 2012, an alleged shareholder filed a derivative lawsuit purportedly on behalf of the Company against certain of our officers and directors in the Superior Court of the State of California, Orange County, captioned *Monika do Valle v. Virgil D. Thompson, et al.*, No. 30-2012-00602258-CU-SL-CXC. The complaint asserts claims for breach of fiduciary duty, abuse of control, mismanagement and waste of corporate assets arising from substantially similar allegations as those contained in the *Norton* case described above, as well as from allegations relating to sales of our common stock by the defendants and repurchases of our common stock. The complaint seeks an unspecified sum of damages and equitable relief. On October 24, 2012, an alleged shareholder filed a derivative lawsuit purportedly on behalf of the Company against certain of our officers and directors in the Superior Court of the State of California, Orange County, captioned *Jones v. Bailey, et al.*, Case No. 30-2012-00608001-CU-MC-CXC. The suit asserts claims substantially identical to those asserted in the *do Valle* derivative action. In January 2013, a Judge of the Superior Court held a hearing with regard to our motion to stay these state shareholder derivative actions in favor of the putative federal securities class action and federal shareholder derivative action. On February 19, 2013, the court issued a final ruling granting our motion to stay the state derivative actions until the putative federal securities and federal derivative actions are resolved.

Put Options Securities Action

In March 2013, individual traders of put options filed a securities complaint in the United States District Court for the Central District of California captioned David *Taban, et al. v. Questcor Pharmaceuticals, Inc.*, No. SACV13-0425. The complaint generally asserts claims against us and certain of our officers and directors for violations of the Exchange Act and for state law fraud and fraudulent concealment based on allegations similar to those asserted in the *Norton* case described above. The complaint seeks compensatory damages in an amount equal to $5 million and punitive damages of an unspecified amount.

***Segment Reporting***

We have historically operated in one business segment. On January 18, 2013, we acquired 100% of the issued and outstanding shares of BioVectra Inc. We now manage our operations through two operating segments which are defined by our separate companies - Questcor and BioVectra. Each segment is operated as an independent business under its own management team, and has responsibility for its commercial activities, operations, and research and development activities related to its products. We intend to have BioVectra continue to operate independently under its existing management team for the foreseeable future.

Questcor is headquartered in Anaheim, California, and is a biopharmaceutical company focused on the treatment of patients with serious, difficult-to-treat autoimmune and inflammatory disorders. Questcor's primary product is H.P. Acthar® Gel (repository corticotropin injection), an injectable drug that is approved by the FDA for the treatment of 19 indications. Of these 19 indications, Questcor currently generates substantially all of its net sales from four indications: the treatment of proteinuria in idiopathic types of nephrotic syndrome, the treatment of acute exacerbations of multiple sclerosis in adults, the treatment of certain rheumatology-related conditions, and the treatment of infantile spasms in children under two years of age.

BioVectra is located in Prince Edward Island, Canada, operating from three facilities. BioVectra is a supplier of contract manufacturing services to the global pharmaceutical and biotechnology industry. BioVectra manufactures active pharmaceutical ingredients (API's), chemical intermediates, and bioprocessing reagents, and is our manufacturing partner for the API in our H.P. Acthar® Gel (repository corticotropin injection). BioVectra is proficient in synthetic organic chemistry, natural extraction of bioactive compounds, PEGylation and conjugation chemistry, and fermentation of chemical and biologic molecules. BioVectra has submitted 10 product filings, including ANDA, DMF, VMF, and CMC section preparations for both the FDA and Health Canada. These filings have been made for both synthetic and biologic molecules, and include a human injectable API, as well as a final drug product.

Segment results are presented in the same manner as we present our operations internally to make operating decisions and assess performance. Net income is the primary responsibility of segment operating management and therefore all activities remain in the segment in which incurred for performance assessment by our chief operating decision maker.

For the three months ended March 31, 2013 and 2012, information regarding our net sales and net income for our operating segments is as follows (in millions):

| | Questcor | BioVectra | Intersegment Eliminations | Consolidated |
|---|---|---|---|---|
| **Net Sales** | | | | |
| For the three months ended March 31, 2013 | $ 126,771 | $ 8,385 | $ (27) | $ 135,129 |
| For the three months ended March 31, 2012 | $ 95,968 | $ — | $ — | $ 95,968 |
| **Net Income** | | | | |
| For the three months ended March 31, 2013 | $ 40,824 | $ (1,755) | $ (5) | $ 39,064 |
| For the three months ended March 31, 2012 | $ 38,543 | $ — | $ — | $ 38,543 |

For the three months ended March 31, 2013 and 2012, information regarding total assets for our operating segments is as follows (in millions):

| | Questcor | BioVectra | Intersegment Eliminations | Consolidated |
|---|---|---|---|---|
| **Total Assets** | | | | |
| March 31, 2013 | $ 314,337 | $ 112,176 | $ (80,760) | $ 345,753 |
| December 31, 2012 | $ 252,431 | $ — | $ — | $ 252,431 |

As discussed above, our purchase of BioVectra occurred in the first quarter of 2013. For more detailed information regarding the assets acquired through our stock purchase of BioVectra, refer to Note 1 - Company - Acquisition of BioVectra Inc.

***Income Taxes***

We account for income taxes under the provisions of Accounting Standards Codification, 740 “Income Taxes,” or ASC 740. We make certain estimates and judgments in determining income tax expense for financial statement purposes. These estimates and judgments occur in the calculation of certain tax assets and liabilities, which arise from differences in the timing of recognition of revenue and expense for tax and financial statement purposes. These differences result in deferred tax assets and liabilities, which are included in our consolidated balance sheets.

As part of the process of preparing our consolidated financial statements, we are required to estimate income taxes in each of the jurisdictions in which we operate. This process involves estimating our tax exposure under the most current tax laws and assessing temporary and/or permanent differences resulting from differing treatment of items for tax and accounting purposes, which may result in uncertain tax positions.

We regularly assess the likelihood that we will be able to recover our deferred tax assets, which is ultimately dependent on us generating future taxable income. We consider all available evidence, both positive and negative, including historical levels of income, expectations and risks associated with estimates of future taxable income and ongoing prudent and feasible tax planning strategies in assessing the need for a valuation allowance. If it is not considered “more likely than not” that we will recover our deferred tax assets, we will increase our provision for taxes by recording a valuation allowance against the deferred tax assets that we estimate will not ultimately be recoverable.

***Equity Transactions***

On February 29, 2008, our Board of Directors approved a stock repurchase plan that provides for the repurchase of up to 7 million shares of our common stock. Stock repurchases under this plan may be made through either open market or privately negotiated transactions in accordance with all applicable laws, rules and regulations. On May 29, 2009 and May 10, 2012, our Board of Directors increased the stock repurchase plan authorization by an additional 6.5 million shares and 5 million shares, respectively. On September 28, 2012, our Board of Directors increased the remaining shares authorized under the stock repurchase plan to 7 million shares. This authorization included the 3.2 million shares previously outstanding from previous authorizations.

During the three months ended March 31, 2012, we used $29.0 million of our cash to repurchase 798,285 shares of our common stock. During the three months ended March 31, 2013, we did not repurchase any shares of our common stock. Under this share repurchase plan, we have repurchased a total of 16.0 million shares of our common stock for $309.9 million through March 31, 2013, at an average price of $19.37 per share. As of March 31, 2013, there are approximately 6.3 million shares authorized remaining under our stock repurchase plan. Additionally, we have repurchased 6.2 million shares outside of the approved share repurchase plan, for $30.3 million at an average purchase price of $4.93 per share. Total shares repurchased were 22.2 million for $340.3 million at an average price of $15.36 per share.

Total share-based compensation costs, related to both stock options and restricted stock awards, for the three months ended March 31, 2013 and 2012 were $6.1 million and $2.3 million, respectively. For the three months ended March 31, 2013, we granted options to employees and non-employee directors to purchase 202,750 shares of our common stock at a weighted average exercise price of $26.47 per share. During the first quarter of 2012, we issued 255,000 performance-based options. These performance-based options include a one-time performance achievement, followed by a time-based vesting of an additional 12 months, should the performance be achieved. During the quarter ended June 30, 2012, we determined that the liability associated with the achievement of the one-time performance milestone was reasonably estimable and probable. As such, we recorded share-based compensation costs related to these performance-based options.

In addition to stock options, we may also grant restricted stock awards to certain employees. For the three months ended March 31, 2013 and 2012, we issued 666,203 and 33,440 restricted stock awards, respectively. For the three months ended March 31, 2013, we issued 471,453 shares of restricted stock to executive officers and certain other employees and issued 194,750 shares of performance-based restricted stock awards. These performance-based restricted stock awards include a one-time performance achievement and vest according to the degree at which the performance milestone was achieved. At March 31, 2013, we were unable to determine achievement of the milestone, thus have not recorded any stock-based compensation expense associated with such grants. The total share-based compensation costs for the three months ended March 31, 2013 and 2012 included $2.1 million and $128,833, respectively, related to restricted stock awards issued in prior periods. On October 18, 2012, we made our annual equity grant to all eligible employee other than executive officers and certain other employees. We issued 692,375 shares of restricted stock to 324 employees. The restricted stock awards are intended to replace the annual grant of stock options that typically occur subsequent to fiscal year end. These restricted stock awards are subject to 4 year vesting and have an intrinsic value of $25.76 per share of restricted stock.

***Subsequent Events***

Subsequent to March 31, 2013, we completed the sale of our U.S. manufacturing, marketing and distribution rights to Doral® (quazepam).

We evaluated subsequent events that have occurred after March 31, 2013, and determined that there were no other events or transactions occurring during this reporting period that require recognition or disclosure in our consolidated financial statements.

## ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

Except for the historical information contained herein, the following discussion contains forward-looking statements that involve risks and uncertainties. Our actual results could differ materially from those discussed herein. Factors that could cause or contribute to such differences include, but are not limited to, those discussed in this section, in Item 1A "Risk Factors" of Part II of this Quarterly Report, those discussed in our Annual Report on Form 10-K for the year ended December 31, 2012, including Item 1 "Business of Questcor," and Item 1A "Risk Factors" of Part I of that Annual Report, as well as factors discussed in any documents incorporated by reference therein.

### *Overview*

We are biopharmaceutical company focused on the treatment of patients with serious, difficult-to-treat autoimmune and inflammatory disorders. We also supply specialty contract manufacturing services to the global pharmaceutical and biotechnology industry through our wholly-owned subsidiary, BioVectra Inc. Our primary product is H.P. Acthar® Gel (repository corticotropin injection), or Acthar, an injectable drug that is approved by the U.S. Food and Drug Administration, or FDA, for the treatment of 19 indications. Of these 19 indications, we currently generate substantially all of our pharmaceutical net sales from the use of Acthar in connection with the following indications:

- Nephrotic Syndrome (NS): Acthar is indicated "to induce a diuresis or a remission of proteinuria in the nephrotic syndrome without uremia of the idiopathic type or that due to lupus erythematosus." According to the National Kidney Foundation, nephrotic syndrome can result from several idiopathic type kidney disorders, including idiopathic membranous nephropathy, focal segmental glomerulosclerosis, IgA nephropathy and minimal change disease. Nephrotic syndrome can also occur due to lupus erythematosus. In this Form 10-Q, the terms "nephrotic syndrome" and "NS" refer only to the proteinuria in nephrotic syndrome conditions that are covered by the Acthar label of approved indications.
- Multiple Sclerosis (MS): Acthar is indicated "for the treatment of acute exacerbations of multiple sclerosis in adults. Controlled clinical trials have shown H.P. Acthar Gel to be effective in speeding the resolution of acute exacerbations of multiple sclerosis. However, there is no evidence that it affects the ultimate outcome or natural history of the disease."
- Infantile Spasms (IS): Acthar is indicated "as monotherapy for the treatment of infantile spasms in infants and children under 2 years of age." We continue to support this vulnerable patient population. We believe that a significant percentage of the $305 million in free drug that we have provided from September 2007 through March 31, 2013, has been used to treat IS. We support the IS community through other initiatives. In February 2012, we were awarded the first-ever Corporate Citizenship Award presented by the Child Neurology Foundation. This award honors our long-term commitment to support the child neurology community as well as our specific efforts to fund education and research related to IS.
- Rheumatology Related Conditions: Acthar is approved for the following rheumatology related conditions: (i) Collagen Diseases: Acthar is indicated "during an exacerbation or as maintenance therapy in selected cases of systemic lupus erythematosus, systemic dermatomyositis (polymyositis)" and (ii) Rheumatic Disorders: Acthar is indicated as "adjunctive therapy for short-term administration (to tide the patient over an acute episode or exacerbation) in: Psoriatic arthritis, Rheumatoid arthritis, including juvenile rheumatoid arthritis (selected cases may require low-dose maintenance therapy), and Ankylosing spondylitis."

Our research and development program is focused on: (i) the evaluation of the use of Acthar for certain on-label indications; (ii) the investigation of other potential uses of Acthar for indications not currently FDA approved; and (iii) the expansion of our understanding of how Acthar works in the human body (pharmacology), and ultimately, its mechanism(s) of action in the disease states for which it is currently used, or may be used in the future. We manage contract research organizations to conduct our in-house discovery programs, which include the following:

- On-Label Development. We continue to explore additional markets for other on-label indications. Our on-label, in-house clinical development efforts include the following:
    - Nephrotic Syndrome (NS). We are the sponsor of a Phase 4 clinical trial evaluating Acthar for the treatment of proteinuria associated with treatment-resistant idiopathic membranous nephropathy (IMN), which commenced patient dosing in the fourth quarter of 2011.

- Systemic Lupus Erythematosus (SLE). We are conducting Phase 4 clinical trials evaluating Acthar for the treatment of SLE and randomized our first patient in January 2013.

- Other Indications, Not On-Label. We are exploring the possibility of pursuing FDA approval for indications not currently on the Acthar label involving other serious, difficult-to-treat autoimmune and inflammatory disorders with high unmet medical need. Our in-house research and development efforts with respect to the use of Acthar to treat conditions that are not on the label of approved indications for Acthar include the following:

  - Diabetic Nephropathy (DN). We reached agreement with the FDA with respect to our investigational new drug application, or IND, for a small Company-sponsored study to evaluate the safety and efficacy of Acthar in treating DN.

  - Amyotrophic Lateral Sclerosis (ALS). We are evaluating the potential clinical benefit that Acthar may provide for the treatment of ALS (commonly referred to as Lou Gehrig's disease). In April 2013, we received a Notice of Allowance from the FDA for our IND relating to a proof-of-concept trial of Acthar in ALS, which we are in the process of initiating.

- Pharmacology. We are conducting in-house non-clinical and clinical pharmacology studies:

  - We seek to expand our understanding of the mechanism(s) of action of Acthar as well as the pharmacology of Acthar across and within each indication. We are also conducting studies to expand our understanding of why Acthar acts differently than steroids and potentially other melanocortin peptides.

We supplement our own research and development activities through third-party collaborations, including investigator initiated studies, which include the following:

- On-Label Development. On-label, third-party clinical development efforts include the following:

  - Nephrotic Syndrome (NS). We are supporting clinical nephrology investigator-initiated studies evaluating: (i) the safety and efficacy of Acthar in IMN; (ii) the safety and efficacy of Acthar in proteinuria in nephrotic syndrome due to focal segmental glomerular sclerosis (FSGS); and (iii) the safety and efficacy of Acthar in treating proteinuria in treatment-resistant nephrotic syndrome (including IMN, FSGS, IgA nephropathy and minimal change disease).

  - Infantile Spasms (IS). We are supporting an investigator-initiated study aimed at establishing quality of care indicators for IS.

- Other Indications, Not On-Label. We are supporting third-party research and development efforts with respect to the use of Acthar to treat conditions that are not on the label of approved indications for Acthar which include the following:

  - Multiple Sclerosis - Pulse Therapy. We are supporting a clinical investigator-initiated study, examining pulse administration of Acthar in multiple sclerosis in conjunction with disease-modifying therapy to evaluate the possible disease modifying effects of Acthar.

  - Cognitive Protection/Autism. We are supporting a preclinical investigator-initiated study, to determine whether Acthar has protective effects in an animal model of epilepsy with concomitant autism-related cognitive dysfunction.

  - Traumatic Brain Injury (TBI): We are supporting a preclinical investigator-initiated study, to determine whether Acthar has protective effects in an animal model of TBI.

- Pharmacology. We are supporting third-party non-clinical and clinical pharmacology studies:

- Multiple Sclerosis. We are supporting an investigator-initiated study, evaluating the immune modulating effects of Acthar applied to serum from multiple sclerosis patients and an investigator-initiated study evaluating neuroprotective properties of adrenocorticotropic hormone that are relevant to multiple sclerosis.

We derive net sales of Acthar from our sales of vials to CuraScript Specialty Distributor, or CuraScript SD, which in turn sells Acthar primarily to specialty pharmacies. These specialty pharmacies place orders with CuraScript SD based on their respective levels of sales and inventory practices. End-user demand for Acthar results from physicians writing prescriptions to patients for the treatment of NS, MS exacerbations, IS, rheumatology related conditions and various other conditions. Physicians do not purchase Acthar for resale to patients. Instead, patients purchase Acthar directly from specialty pharmacies after receiving a prescription and, typically, after arranging for third party reimbursement (government or commercial insurance) - most often after satisfying a prior authorization requirement imposed by their insurance carrier. Alternatively, if a patient is uninsured or under-insured, they may receive Acthar under a Questcor sponsored patient assistance program, administered by the National Organization of Rare Disorders.

Healthcare provider understanding of Acthar is facilitated by our experienced team of sales representatives and managers. We have an active compliance program led by our chief compliance officer who is dedicated exclusively to compliance and who reports directly to our Chief Executive Officer and to the Compliance Committee of our Board of Directors. Our compliance program is based on the Office of Inspector General's guidance relating to the following elements of an effective compliance program: (i) written policies and procedures, (ii) compliance officer and compliance committee, (iii) effective training and communication, (iv) effective lines of communication, (v) monitoring and auditing, (vi) enforcement and disciplinary guidelines, and (vii) corrective action process.

***Recent Developments***

On January 18, 2013, we completed our acquisition of BioVectra. BioVectra is located in Prince Edward Island, Canada, and is a supplier of specialty contract manufacturing services to the global pharmaceutical and biotechnology industry. BioVectra manufactures active pharmaceutical ingredients (API), chemical intermediates, and bioprocessing reagents. BioVectra has been our manufacturing partner for the API in Acthar since April, 2003. BioVectra's facilities are staffed by 178 employees including chemists, engineers and technicians.

We acquired 100% of the issued and outstanding shares of BioVectra utilizing cash on hand. The former shareholders of BioVectra could receive additional cash consideration based on BioVectra's financial results over the next three years, which consideration is payable annually with a final true-up payment in the third year.

***Results of Operations***

*Three months ended March 31, 2013 compared to the three months ended March 31, 2012:*

***Recorded Net Sales***

| | Three Months Ended March 31, | | | |
|---|---|---|---|---|
| | 2013 | 2012 | Increase | % Change |
| | (in $000's) | | | |
| **Pharmaceutical sales** | $ 137,378 | $ 111,348 | $ 26,030 | 23 % |
| Less sales reserves: | | | | |
| Provision for Medicaid rebates | 6,028 | 13,312 | (7,284) | (55)% |
| Provision for chargebacks | 46 | 64 | (18) | (28)% |
| Provision for Coverage Gap Discount | 217 | 125 | 92 | 74 % |
| Provision for TRICARE | 1,539 | 1,077 | 462 | 43 % |
| Co-payment assistance and other | 2,777 | 802 | 1,975 | 246 % |
| Total sales reserves | 10,607 | 15,380 | (4,773) | (31)% |
| **Total pharmaceutical net sales** | 126,771 | 95,968 | 30,803 | 32 % |
| **Total contract manufacturing net sales** | 8,358 | — | 8,358 | — % |
| **Total net sales** | $ 135,129 | $ 95,968 | $ 39,161 | 41 % |

Net sales for the three months ended March 31, 2013 and 2012 were comprised primarily of net sales of Acthar and, for the quarter ended only March 31, 2013, net sales from BioVectra. Net sales of Acthar for the three months ended March 31, 2013 increased 32% to $126.7 million as compared to $95.9 million during the same period in 2012. Net sales of Acthar for the three months ended March 31, 2013 resulted primarily from increased unit demand from CuraScript SD, our distributor for Acthar. We shipped 4,830 vials for the three months ended March 31, 2013 as compared to 4,111 vials shipped for the three months ended March 31, 2012. While we do not receive complete information regarding prescriptions by therapeutic area, we believe increased demand from CuraScript SD was driven by the expanded usage of Acthar by nephrologists in the treatment of NS and by rheumatologists in the treatment of dermatomyositis, polymyositis, systemic lupus erythematosus, and rheumatoid arthritis, as well as continued prescribing by neurologists in the treatment of MS and IS. This increased unit demand relative to the three months ended March 31, 2012 was partially offset by the negative impact of the introduction of a new reimbursement support center, distribution channel disruption associated with establishing a lower Medicaid rebate for Acthar and the timing of two Acthar orders that were received and filled at the end of fourth quarter 2012.

Our net sales of Acthar are also impacted by the amount of our sales reserves, which are deducted from revenue in the calculation of net sales. During the three months ended March 31, 2013 and 2012, the largest component of our sales reserves related to our provision for Medicaid rebates. This provision is impacted by two factors. First, the rebate amount for Acthar affects our provision for Medicaid rebates. During the three months ended March 31, 2012, the Medicaid rebate amount equaled 100% of the Average Manufacturer Price, or AMP, of Acthar which approximates the amount we charge to CuraScript SD. As such, we did not generate any net sales in connection with Medicaid business. During the first quarter of 2013, the Medicaid rebate amount for Acthar was reset in the Medicaid system from 100% of the AMP of Acthar to the basic rebate amount of 23.1% of AMP. Second, our business mix across therapeutic areas affects our provision for Medicaid rebates since the percentage of patients that are enrolled in Medicaid varies by therapeutic area. Specifically, a lower percentage of adults are enrolled in Medicaid than are infants. As such, growth in our non-IS sales relative to IS sales has resulted in an overall lower percentage of sales being attributable to patients enrolled in Medicaid. For the three months ended March 31, 2013, we recorded a provision of 7.3% of our gross revenue for sales-related reserves, a decrease from the 13.8% in the three months ended March 31, 2012.

We believe that over half of our growth in net sales of Acthar from the three months ended March 31, 2012 to the three months ended March 31, 2013 was due to increased vial shipments, with the remainder of our net sales growth being due to the increase in the percentage of our product sales that are not subject to Medicaid rebates as described above, as well as increased product pricing. However, it is difficult to ascribe the sources of net sales growth to these individual factors as the factors might not be independent.

We believe that Acthar represents a promising potential therapy for patients suffering from the difficult-to-treat, on-label medical conditions for which we currently promote Acthar. However, there is limited awareness of Acthar amongst physicians who practice in the relevant medical specialties, due in part to Acthar being under-invested in by its previous owners. As such, we have expanded our sales force across multiple on-label therapeutic areas in order to increase our ability to educate physicians about Acthar's potential benefit to their patients. Most recently, we significantly expanded our Rheumatology Sales Force by expanding this group from an initial team of 12 Acthar specialists to 55 specialists. This expansion was initiated during the fourth quarter of 2012 and hiring and training was completed in February 2013. It is unclear whether this will continue to result in increased net sales. The process of significantly expanding a sales force in the biopharmaceutical industry is complex. We modify and re-allocate individual sales territories across our enlarged sales force, which can cause temporary disruptions in our selling efforts. Additionally, while the cost of our new sales representatives impacts our operating expenses immediately, there can be a delay in the expected ability of our new representatives to increase our net sales due to the time it takes for us to train the new representatives and for the new representatives to establish professional relationships with prescribing physicians within their territories.

Acthar orders may be affected by several factors, including inventory levels at specialty and hospital pharmacies, greater use of patient assistance programs, the overall pattern of usage by the health care community, including Medicaid and government-supported entities, the use of alternative therapies, and the reimbursement policies of insurance companies. Our specialty distributor ships Acthar to specialty pharmacies and hospitals to meet end user demand. We track our own Acthar shipments daily, but those shipments vary compared to end user demand and because of changes in inventory levels at specialty pharmacies and hospitals. As a result of the variation in order patterns, in channel inventory levels may be positively or negatively affected. Due in part to distribution channel disruption associated with establishing a lower Medicaid rebate for Acthar and the timing of two Acthar orders that were received and filled at the end of fourth quarter 2012, we believe that channel inventory was reduced during the quarter ended March 31, 2013, but we do not have complete visibility into the inventory levels at the various specialty pharmacies in our distribution channel.

Net sales for BioVectra were $8.4 million representing 6.2% of total net sales. Because we acquired BioVectra on January 18, 2013, there were no comparable sales in the same period 2012.

***Cost of Sales and Gross Profit***

| | Three Months Ended March 31, | | | |
|---|---|---|---|---|
| | 2013 | 2012 | Increase/ (Decrease) | % Change |
| | (in $000's) | | | |
| Cost of sales | $ 16,189 | $ 5,520 | $ 10,669 | 193% |
| Gross profit | $ 118,940 | $ 90,448 | $ 28,492 | 32% |
| Gross margin | 94% | 94% | | |

Cost of sales was $16.2 million for the three months ended March 31, 2013, as compared to $5.5 million for the three months ended March 31, 2012. Our gross margin and gross profit was 94%, or $118.9 million, respectively, for the three months ended March 31, 2013, as compared to 94%, or $90.4 million, respectively, for the three months ended March 31, 2012.

Cost of sales for the three months ended March 31, 2013 primarily included costs associated with the sale of Acthar ($8.0 million or 50% of the total costs) and costs associated with our manufacturing activity at BioVectra ($8.2 million or 50% of the total costs). We include in cost of sales direct material costs, manufacturing labor, indirect manufacturing costs including plant supplies, packaging, warehousing and distribution, royalties, product liability insurance, quality control (which primarily includes product stability and potency testing), quality assurance, depreciation of manufacturing equipment and facilities and reserves for excess or obsolete inventory.

The increase in gross profit dollars is due to continued growth in vials sold for all of our indications. The increase in cost of sales was primarily due to the following: (1) the inclusion of BioVectra manufacturing costs as of January 18, 2013 (which included unexpected manufacturing costs for additional external testing and additional repair and maintenance costs on a new production plant), (2) an increase in Acthar net sales, (3) an increase in the cost for outside product potency testing, (4) an increase in royalties on Acthar net sales, offset by a decrease in the proportionate amount of distribution costs relative to Acthar net sales.

We continue to expect our cost of sales, in absolute dollars, to increase in future periods due to the inclusion of BioVectra, increased costs associated with outside product potency testing, product stability testing and, in the event of increased net sales,

higher royalty payments. The manufacturing process for Acthar is complex and problems may arise during manufacturing for a variety of reasons, including equipment malfunction, failure to follow specific protocols and procedures, problems with raw materials, natural disasters, and environmental factors.

***Selling and Marketing***

| | Three Months Ended March 31, | | Increase/ (Decrease) | % Change |
|---|---|---|---|---|
| | 2013 | 2012 | | |
| | (in $000's) | | | |
| Selling and marketing expense | $ 35,461 | $ 21,716 | $ 13,745 | 63% |

Selling and marketing expenses were $35.5 million for the three months ended March 31, 2013, as compared to $21.7 million for the three months ended March 31, 2012. The increase of $13.7 million in 2013 as compared to 2012 is due primarily to increases in headcount-related costs and costs associated with our expanded sales and marketing effort. We include in sales and marketing expenses headcount-related costs, promotional costs and physician program costs. We have expanded our sales force and expect selling and marketing expenses to increase in future periods.

***General and Administrative***

| | Three Months Ended March 31, | | Increase/ (Decrease) | % Change |
|---|---|---|---|---|
| | 2013 | 2012 | | |
| | (in $000's) | | | |
| General and administrative expense | $ 12,548 | $ 5,442 | $ 7,106 | 131% |

General and administrative expenses were $12.5 million for the three months ended March 31, 2013, as compared to $5.4 million for the three months ended March 31, 2012. We include in general and administrative expenses headcount-related costs, including stock-based compensation expense, legal and accounting expenses. The increase of $7.1 million in 2013 as compared to 2012 is due primarily to increased headcount and headcount-related costs to support our growth, and increased legal costs.

***Research and Development***

| | Three Months Ended March 31, | | Increase/ (Decrease) | % Change |
|---|---|---|---|---|
| | 2013 | 2012 | | |
| | (in $000's) | | | |
| Research and development | $ 10,793 | $ 5,665 | $ 5,128 | 91% |

Research and development expenses were $10.8 million in the three months ended March 31, 2013, as compared to $5.7 million for the three months ended March 31, 2012. The increase in research and development expenses for the three months ended March 31, 2013 as compared to the same period in 2012 was primarily due to increases in headcount and headcount-related costs to continue and expand our various research and development programs, including with the following clinical studies: (1) the initiation of our Phase 4 dose response clinical trial for idiopathic membranous nephropathy, (2) the initiation of our pilot safety and efficacy study of Acthar in patients with diabetic nephropathy, and (3) the initiation of our study exploring the efficacy, safety and pharmacodynamics of Acthar in system lupus erythematosus. Costs included in research and development also include costs associated with the funding of medical research projects to better understand the therapeutic benefit of Acthar in current and new therapeutic applications, product development efforts and regulatory compliance activities.

We manage and evaluate our research and development expenditures generally by the type of costs incurred. We generally classify and separate research and development expenditures into amounts related to medical affairs, regulatory, product development and manufacturing costs. Such categories include the following types of costs:

- Medical Affairs Costs - Medical affairs costs, which include activities related to medical information in support of Acthar and its related indications.
- Regulatory Costs - Regulatory costs, which include compliance and all FDA interactions.
- Product Development Costs - Product development costs, which include contract research organization costs and study monitoring costs.
- Manufacturing Costs - Manufacturing costs, which include costs related to production scale-up and validation, raw material qualification and stability studies.

For the three months ended March 31, 2013, approximately 43% of our research and development expenditures were for medical affair costs, 4% was spent on regulatory costs, 41% was spent on product development costs, and approximately 12% was spent on manufacturing costs.

For the three months ended March 31, 2012, approximately 40% of our research and development expenditures were for medical affair costs, 9% was spent on regulatory costs, 44% was spent on product development costs, and approximately 7% was spent on manufacturing costs.

We continue to invest in Acthar through the expansion of our product development efforts. We manage contract research organizations to conduct our in-house discovery programs. We are the sponsor of a Phase 4 clinical trial evaluating Acthar for the treatment of proteinuria associated with treatment-resistant idiopathic membranous nephropathy (IMN), which commenced patient dosing in the fourth quarter of 2011. We are conducting Phase 4 clinical trials evaluating Acthar for the treatment of SLE and randomized our first patient in January 2013. We are also exploring the possibility of pursuing FDA approval for indications not currently on the Acthar label involving other serious, difficult-to-treat autoimmune and inflammatory disorders with high unmet medical need. We reached agreement with the FDA with respect to our investigational new drug application, or IND, for a small Company-sponsored study to evaluate the safety and efficacy of Acthar in treating diabetic nephropathy. We are evaluating the potential clinical benefit that Acthar may provide for the treatment of ALS (commonly referred to as Lou Gehrig's disease). In April 2013, we received a Notice of Allowance from the FDA for our IND relating to a proof-of-concept trial of Acthar in ALS, which we are in the process of initiating. These programs will result in a significant increase in research and development expense throughout 2013.

The expenditures that will be necessary to execute our development plans are subject to numerous uncertainties, which may affect our research and development expenditures and capital resources. For instance, the duration and the cost of clinical trials may vary significantly depending on a variety of factors including a trial's protocol, the number of patients in the trial, the duration of patient follow-up, the number of clinical sites in the trial, and the length of time required to enroll suitable patient subjects. Even if earlier results are positive, we may obtain different results in later stages of development, including failure to show the desired safety or efficacy, which could impact our development expenditures for a particular indication. Although we spend a considerable amount of time planning our development activities, we may be required to deviate from our plan based on new circumstances or events or our assessment from time to time of a particular indication's market potential, other product opportunities and our corporate priorities. Any deviation from our plan may require us to incur additional expenditures or accelerate or delay the timing of our development spending. Furthermore, as we obtain results from trials and review the path toward regulatory approval, we may elect to discontinue development of certain indications or product candidates, in order to focus our resources on more promising indications or candidates. As a result, the amount or ranges of cost and timing to complete our product development programs and each future product development program is not estimable.

***Share-based compensation costs.*** Total share-based compensation costs, related to stock options and restricted stock awards, for the three months ended March 31, 2013 and 2012 were $6.1 million and $2.3 million, respectively. For the three months ended March 31, 2013, we granted options to employees and non-employee directors to purchase 202,750 shares of our common stock at a weighted average exercise price of $26.47 per share. During the first quarter of 2012, we issued 255,000 performance-based options. These performance-based options include a one-time performance achievement, followed by a time-based vesting of an additional 12 months, should the performance be achieved. It was determined during 2012 the one-time performance milestone was achieved.

Our equity incentive award plan is broad-based and every Questcor full-time employee and certain Questcor part-time employees are eligible to receive a grant. The increase in our share-based compensation is due to the increase in Questcor employees from 185 on March 31, 2012 to 329 employees on March 31, 2013, offset by the decrease in the weighted average stock price from $37.21 in the quarter ended March 31, 2012 to $28.96 in the quarter ended March 31, 2013.

In addition to stock options, we may also grant restricted stock awards to certain employees. For the three months ended March 31, 2013 and 2012, we issued 666,203 and 33,440 restricted stock awards, respectively. For the three months ended March 31, 2013, we issued 471,453 shares of restricted stock to executive officers and certain other employees and issued 194,750 shares of performance-based restricted stock awards. These performance-based restricted stock awards include a one-time performance achievement and vest according to the degree at which the performance milestone was achieved. At March 31, 2013, we were unable to determine achievement of the milestone, thus have not recorded any stock-based compensation expense associated with such grants. The total share-based compensation costs for the three months ended March 31, 2013 and 2012 included $2.1 million and $128,833, respectively, related to restricted stock awards issued in prior periods. On October 18, 2012, we made our annual equity grant to all eligible employee other than executive officers and certain other employees. We issued 692,375 shares of restricted stock to 324 employees. The restricted stock awards are intended to replace the annual grant of stock options that typically occur subsequent to fiscal year end. These restricted stock awards are subject to 4 year vesting and have an intrinsic value of $25.76 per share of restricted stock.

The following table sets forth our share-based compensation costs for the three months ended March 31, 2013 and 2012, respectively (in thousands):

| | Three Months Ended March 31, | |
|---|---|---|
| | 2013 | 2012 |
| Selling and marketing | $ 2,454 | $ 1,046 |
| General and administrative | 2,538 | 464 |
| Research and development | 1,156 | 786 |
| Total | $ 6,148 | $ 2,296 |

***Depreciation and amortization.*** Depreciation and amortization expense for the three months ended March 31, 2013 was $2.1 million, as compared to $0.3 million for the three months ended March 31, 2012. The increase in depreciation and amortization expense of $1.8 million as compared to 2012 was due primarily to the related amortization expense of the purchased intangibles in conjunction with the acquisition of BioVectra.

***Income tax expense.*** Income tax expense for the three months ended March 31, 2013 was $18.5 million, as compared to $19.0 million for the three months ended March 31, 2012. The decrease in income tax expense of $0.5 million in 2013 as compared to 2012 was primarily due to the extension of the research and development tax credit that occurred in the first quarter of 2013. Our foreign earnings attributable to the BioVectra acquisition will be permanently reinvested in such foreign jurisdiction and, therefore, no deferred tax liabilities for U.S. income taxes have been provided for on any undistributed earnings.

***Liquidity and Capital Resources***

Cash and cash equivalents, short term investments and working capital as of March 31, 2013 and December 31, 2012 were as follows (in thousands):

**Financial Assets:**

| | March 31, 2013 | December 31, 2012 |
|---|---|---|
| Cash and cash equivalents | $ 75,404 | $ 80,608 |
| Short term investments | 78,020 | 74,705 |
| Cash, cash equivalents and short term investments | $ 153,424 | $ 155,313 |

**Select measures of liquidity and capital resources:**

| | March 31, 2013 | December 31, 2012 |
|---|---|---|
| Current assets | $ 241,437 | $ 237,276 |
| Current liabilities | 94,295 | 90,399 |
| Working Capital | $ 147,142 | $ 146,877 |
| Current ratio | 2.56 | 2.62 |

Until required for use in our business or returned to shareholders through our dividend, share repurchase program or other method, we invest our cash reserves in money market funds and high quality commercial, corporate and U.S. government and agency bonds in accordance with our investment policy. The objective of our investment policy is to preserve capital, provide liquidity consistent with forecasted cash flow requirements, maintain appropriate diversification and generate returns relative to these investment objectives and prevailing market conditions.

The slight decrease in cash, cash equivalents and short-term investments was primarily due to the acquisition of BioVectra during the quarter, offset by our net sales and the related cash generated from operations. The increase in our working capital was primarily due to increases in inventory (due primarily to the acquisition of BioVectra), decreases in accrued compensation and sales-related reserves (due to the pay out of the corporate bonus pool and the reduction in our Medicaid rebate percent, respectively), offset by the increase in our dividend payable and income taxes payable. We expect to maintain increased amounts of inventory as compared to historical averages as a result of the acquisition of BioVectra.

Our collection terms on our accounts receivable relating to sales of Acthar to CuraScript SD are net 30 days. CuraScript SD represents approximately 85% of our accounts receivable and 94% of our net sales.

We expect continued growth in our research and development expenses. However, we anticipate that cash generated from operations and our existing cash, cash equivalents and short-term investments should provide us adequate resources to fund our operations as currently planned for the foreseeable future.

**Cash Flows**

**Change in cash and cash equivalents:**

| (in $000's) | Three Months Ended March 31, 2013 | 2012 | Increase/ (Decrease) |
|---|---|---|---|
| Net cash flows provided by operating activities | $ 41,452 | $ 40,910 | $ 542 |
| Net cash flows provided by investing activities | (50,755) | (39,137) | (11,618) |
| Net cash flows used in financing activities | 4,183 | (26,651) | 30,834 |
| Impact of exchange rates on cash flows | (84) | — | (84) |
| Net change in cash and cash equivalents | $ (5,204) | $ (24,878) | $ 19,674 |

*Operating Activities*

The components of cash flows from operating activities, as reported on our Consolidated Statement of Cash Flows, are as follows:

- Our reported net income, adjusted for non-cash items, including share-based compensation expense, deferred income taxes, amortization of investments, depreciation and amortization, impairment of purchased technology and goodwill, and loss on disposal of property and equipment was $48.7 million and $41.7 million for the three months ended March 31, 2013 and 2012, respectively.

- Net cash outflow due to changes in operating assets and liabilities was $7.2 million for the three months ended March 31, 2013 and $0.8 million for the three months ended March 31, 2012. The $7.2 million change in operating assets and liabilities primarily relates to a decrease in accrued compensation of $15.2 million as a result of the 2012 corporate bonus pool payout during the quarter, a decrease in sales related reserves of $11.5 million due to the favorable change in our Medicaid rebate rate, offset by a decrease in our accounts receivable of $8.7 million due to a reduction in net sales quarter over quarter and a decrease in inventory of $4.6 million.

*Investing Activities*

The components of cash flows from investing activities consisted of the following:

- Acquisition of BioVectra, net of cash acquired of $46.7 million;
- Purchases of property and equipment of $0.6 million;
- Purchases of short term investments of $33.5 million; and
- Maturities of short term investments of $30.0 million.

*Financing Activities*

Net cash flows from financing activities reflected the following:

- the income tax benefit realized on our share-based compensation plans of $2.0 million; and
- the proceeds from issuance of common stock related to the exercise of stock options of $2.6 million

On January 18, 2013, we acquired 100% of the issued and outstanding shares of BioVectra for $50.3 million, but paid $50.8 million, which includes a loss on foreign exchange rate of $0.5 million, plus up to an additional C$50.0 million in cash tied to the future performance of BioVectra.

Our subsidiary, BioVectra, has a supply agreement with a customer to supply a pharmaceutical product for a period of 10 years. Per the supply agreement, BioVectra financed and constructed a facility for the manufacturing of the pharmaceutical product to be supplied under the agreement. BioVectra entered into a term loan agreement with Prince Edward Island Century 2000 Fund Inc. to finance $14.8 million of the construction costs of the facility. The term loan has an interest rate of 4%, is due in full by February 2022 and is secured by certain of our BioVectra assets. Under the supply agreement, the customer agreed to reimburse BioVectra for the quarterly financing payments of $450,743 during the term of the loan.

We review our level of liquidity and anticipated cash needs for the business on an ongoing basis, and consider whether to return additional capital to our shareholders as well as alternative methods to return capital. Historically, our primary method of returning capital to shareholders has been open market share repurchases and dividend payments. Since the beginning of 2008, we have repurchased a total of 22.2 million shares of our common stock under our stock repurchase plan for $340.3 million through March 31, 2013, at an average price of $15.36 per share. As of March 31, 2013, there are 6.3 million shares authorized remaining under our stock repurchase plan.

## ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

The primary objective of our investment policy is to preserve principal while at the same time maximizing the income we receive from our investments without significantly increasing risk. Some of the securities that we have invested in have had market risk. This means that a change in prevailing interest rates may cause the principal amount of the investment to fluctuate. For example, if we hold a security that was issued with a fixed interest rate at the then-prevailing rate and the prevailing interest rate later increases, the principal amount of our investment probably will decline. In an attempt to limit interest rate risk, we follow guidelines to limit the average and longest single maturity dates. Our investments include money market accounts, government-sponsored enterprises, certificates of deposit and municipal bonds. None of our investments are in auction rate securities. Seeking to minimize credit risk, we place our investments with high quality issuers and follow internally developed guidelines to limit the amount of credit exposure to any one issuer.

As a result of our foreign operations, we face exposure to movements in foreign currency exchange rates, primarily the Canadian dollar to the U.S. dollar. The current exposures arise primarily from cash, accounts receivable, intercompany receivables and payables, and product sales denominated in foreign currencies. Both positive and negative impacts to our international product sales from movements in foreign currency exchange rates are partially mitigated by the natural, opposite impact that foreign currency exchange rates have on our international operating expenses.

## ITEM 4. CONTROLS AND PROCEDURES

### (a) Evaluation of Disclosure Controls and Procedures

We maintain disclosure controls and procedures that are designed to ensure that information required to be disclosed in our reports filed pursuant to the Exchange Act, is recorded, processed, summarized and reported within the time periods specified in the Securities and Exchange Commission's, or SEC, rules and forms and that such information is accumulated and communicated to our management, including our Chief Executive Officer (principal executive officer) and Chief Financial Officer (principal financial and accounting officer), as appropriate, to allow for timely decisions regarding required disclosure.

In designing and evaluating the disclosure controls and procedures, management recognizes that any controls and procedures, no matter how well designed and operated, can provide only reasonable assurance of achieving the desired control objectives, and management is required to apply its judgment in evaluating the cost-benefit relationship of possible controls and procedures. Our disclosure controls and procedures were designed to provide reasonable assurance that the controls and procedures would meet their objectives.

As required by Exchange Act Rule 13a-15(b), we carried out an evaluation, under the supervision and with the participation of our management, including our Chief Executive Officer (principal executive officer) and Chief Financial Officer (principal financial and accounting officer), of the effectiveness of the design and operation of our disclosure controls and procedures as of the end of the quarter covered by this quarterly report on Form 10-Q. Based on the foregoing, our Chief Executive Officer (principal executive officer) and Chief Financial Officer (principal financial and accounting officer) concluded that our disclosure controls and procedures were effective as of March 31, 2013.

There has been no change in our internal controls over financial reporting during our most recent fiscal quarter that has materially affected, or is reasonably likely to affect materially, our internal controls over financial reporting.

## PART II. OTHER INFORMATION

### ITEM 1. LEGAL PROCEEDINGS

We operate in a highly regulated industry. We are subject to the regulatory authority of the SEC, the FDA and numerous other federal and state governmental agencies including state attorney general offices, which have become more active in investigating the business practices of pharmaceutical companies.

Glenridge Litigation

In June 2011, Glenridge Pharmaceuticals LLC, or Glenridge, filed a lawsuit against us in the Superior Court of California, Santa Clara County, alleging that we had underpaid royalties to Glenridge, in connection with the timing of the impact of various offsets in the calculation of net sales. We are defending this lawsuit vigorously. In October 2012, a Judge of the Superior Court denied Glenridge's motion for summary judgment on its claims. In March 2013, Glenridge amended its complaint and added causes of action for breach of contract and breach of the implied covenant of good faith and fair dealing. In April 2013, we filed our answer to this amended complaint.

In August 2012, we filed a separate lawsuit in the Superior Court of California, Orange County, against the three principals of Glenridge, as well as Glenridge, challenging the enforceability of our agreement with Glenridge, and alleging breach of fiduciary duty, as well as aiding and abetting of the breach, by the principals. In November 2012, a Judge of the Superior Court of California, Orange County, transferred this lawsuit to the Superior Court of California, Santa Clara County. In February 2013, a Judge of the Superior Court denied Glenridge's motion to stay this lawsuit in favor of the accounting lawsuit described in the immediately preceding paragraph. We have filed a motion for summary judgment on issues related to the fiduciary duty claim. A hearing on the motion is likely to occur in July 2013.

USAO Investigation

On September 21, 2012, we became aware of an investigation by the United States Attorney's Office for the Eastern District of Pennsylvania (the "USAO") regarding our promotional practices. Following our September 24, 2012 announcement of this investigation, we received a subpoena from the USAO for information relating to our promotional practices. We are cooperating with the USAO with regard to this investigation.

Putative Class Action Securities Litigation

On September 26, 2012, a putative class action lawsuit was filed against us and certain of our officers and directors in the United States District Court for the Central District of California, captioned *John K. Norton v. Questcor Pharmaceuticals, et al.*, No. SACv12-1623 DMG (FMOx). The complaint purports to be brought on behalf of shareholders who purchased our common stock between April 26, 2011 and September 21, 2012. The complaint generally asserts that we and certain of our officers and directors violated sections 10(b) and/or 20(a) of the Securities Exchange Act of 1934, as amended, or the Exchange Act, by making allegedly false and/or misleading statements concerning the clinical evidence to support the use of Acthar for indications other than infantile spasms, the promotion of the sale and use of Acthar in the treatment of MS and nephrotic syndrome, reimbursement for Acthar from third-party insurers, and our outlook and potential market growth for Acthar. The complaint seeks damages in an unspecified amount and equitable relief against the defendants. This lawsuit has been consolidated with four subsequently-filed actions asserting similar claims under the caption: *In re Questcor Securities Litigation*, No. CV 12-01623 DMG (FMOx). On January 4, 2013, the district court issued an order appointing the West Virginia Investment Management Board and Plumbers & Pipefitters National Pension Fund as Lead Plaintiffs in the consolidated securities action. In March 2013, the Lead Plaintiffs filed a consolidated amended complaint for the consolidated securities action. We will be filing a motion to dismiss the consolidated amended complaint in May 2013.

Federal Shareholder Derivative Litigation

On October 4, 2012, another alleged shareholder filed a derivative lawsuit in the United States District Court for the Central District of California captioned *Gerald Easton v. Don M. Bailey, et al.*, No. SACV12-01716 DOC (JPRx). The suit asserts claims substantially identical to those asserted in the *do Valle* derivative action described below against the same defendants. This lawsuit has been consolidated with five subsequently-filed actions asserting similar claims under the caption: *In re Questcor Shareholder Derivative Litigation, CV 12-01716 DMG (FMOx)*. In March 2013, the parties entered into a stipulation to stay the consolidated federal derivative lawsuit, pending resolution of the motion to dismiss the consolidated securities action.

State Shareholder Derivative Litigation

On October 2, 2012, an alleged shareholder filed a derivative lawsuit purportedly on behalf of the Company against certain of our officers and directors in the Superior Court of the State of California, Orange County, captioned *Monika do Valle v. Virgil D. Thompson, et al.*, No. 30-2012-00602258-CU-SL-CXC. The complaint asserts claims for breach of fiduciary duty, abuse of control, mismanagement and waste of corporate assets arising from substantially similar allegations as those contained in the *Norton* case described above, as well as from allegations relating to sales of our common stock by the defendants and repurchases of our common stock. The complaint seeks an unspecified sum of damages and equitable relief. On October 24, 2012, an alleged shareholder filed a derivative lawsuit purportedly on behalf of the Company against certain of our officers and directors in the Superior Court of the State of California, Orange County, captioned *Jones v. Bailey, et al.*, Case No. 30-2012-00608001-CU-MC-CXC. The suit asserts claims substantially identical to those asserted in the *do Valle* derivative action. In January 2013, a Judge of the Superior Court held a hearing with regard to our motion to stay these state shareholder derivative actions in favor of the putative federal securities class action and federal shareholder derivative action. On February 19, 2013, the court issued a final ruling granting our motion to stay the state derivative actions until the putative federal securities and federal derivative actions are resolved.

Put Options Securities Action

In March 2013, individual traders of put options filed a securities complaint in the United States District Court for the Central District of California captioned David *Taban, et al. v. Questcor Pharmaceuticals, Inc.*, No. SACV13-0425. The complaint generally asserts claims against us and certain of our officers and directors for violations of the Exchange Act and for state law fraud and fraudulent concealment based on allegations similar to those asserted in the *Norton* case described above. The complaint seeks compensatory damages in an amount equal to $5 million and punitive damages of an unspecified amount.

We believe that the probability of unfavorable outcome or loss related to this litigation and an estimate of the amount or range of loss, if any, from an unfavorable outcome are not determinable at this time. Responding to government investigations, defending any claims raised, and any resulting fines, restitution, damages and penalties, settlement payments or administrative actions, as well as any related actions brought by stockholders or other third parties, could have a material impact on our reputation, business and financial condition and divert the attention of our management from operating our business.

## ITEM 1A. RISK FACTORS

Information about material risks related to our business, financial condition and results of operations for the quarterly period ended March 31, 2013 does not materially differ from that described in Part I, Item 1A of our Annual Report on Form 10-K for the year ended December 31, 2012, as filed with the SEC on February 27, 2013.

**ITEM 2. UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS**

Not applicable.

**ITEM 3. DEFAULTS UPON SENIOR SECURITIES**

Not applicable.

**ITEM 4. MINE SAFETY DISCLOSURE**

Not applicable.

**ITEM 5. OTHER INFORMATION**

Not applicable.

**ITEM 6. EXHIBITS**

| Exhibit No | Description |
|---|---|
| 31.1 | Certification of Principal Executive Officer Pursuant to Rule 13a-14(a)/15d-14(a) of the Securities Exchange Act of 1934. |
| 31.2 | Certification of Principal Financial Officer Pursuant to Rule 13a-14(a)/15d-14(a) of the Securities Exchange Act of 1934. |
| 32.1 | Certification of Principal Executive Officer Pursuant to Rule 13a-14(b)/15d-14(b) of the Securities Exchange Act of 1934 and 18 U.S.C. Section 1350. |
| 32.2 | Certification of Principal Financial Officer Pursuant to Rule 13a-14(b)/15d-14(b) of the Securities Exchange Act of 1934 and 18 U.S.C. Section 1350. |
| 101 .INS* | XBRL Instance Document |
| 101.SCH* | XBRL Taxonomy Extension Schema Document |
| 101.CAL* | XBRL Taxonomy Extension Calculation Linkbase Document |
| 101.DEF* | XBRL Taxonomy Extension Definition Linkbase Document |
| 101.LAB* | XBRL Taxonomy Extension Label Linkbase Document |
| 101.PRE* | XBRL Taxonomy Extension Presentation Linkbase Document |

* Furnished herewith.

**SIGNATURES**

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned hereunto duly authorized.

QUESTCOR PHARMACEUTICALS, INC.

Date: May 2, 2013 By: /s/ Don M. Bailey

**Don M. Bailey**
**President and Chief Executive Officer**
**(Principal Executive Officer)**

By: /s/ Michael H. Mulroy

**Michael H. Mulroy**
**Chief Financial Officer and General Counsel**
**(Principal Financial and Accounting Officer)**

## Exhibit Index

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|---|---|
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| 101.PRE* | XBRL Taxonomy Extension Presentation Linkbase Document |

* Furnished herewith.

**Exhibit 31.1**

**CERTIFICATION**

I, Don M. Bailey, certify that:

1. I have reviewed this quarterly report on Form 10-Q of Questcor Pharmaceuticals, Inc.;

2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;

3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;

4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:

    a. Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;

    b. Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;

    c. Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and

    d. Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and

5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):

    a. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):

    b. Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: May 2, 2013

/s/ Don M. Bailey

Don M. Bailey
President and Chief Executive Officer
(Principal Executive Officer)

**Exhibit 31.2**

**CERTIFICATION**

I, Michael H. Mulroy, certify that:

1. I have reviewed this quarterly report on Form 10-Q of Questcor Pharmaceuticals, Inc.;

2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;

3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;

4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:

    a. Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;

    b. Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;

    c. Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and

    d. Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and

5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):

    a. All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and

    b. Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: May 2, 2013

/s/ Michael H. Mulroy

Michael H. Mulroy
Chief Financial Officer
(Principal Accounting Officer)

**Exhibit 32.1**

**CERTIFICATION**

I, Don M. Bailey, hereby certify pursuant to Rule 13a-14(b) or Rule 15d-14(b) of the Securities Exchange Act of 1934 and 18 U.S.C. Section 1350, that the Quarterly Report of Questcor Pharmaceuticals, Inc. on Form 10-Q for the quarterly period ended March 31, 2013 fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934 and that information contained in such Quarterly Report on Form 10-Q for the period ended March 31, 2013 fairly presents in all material respects the financial condition and results of operations of Questcor Pharmaceuticals, Inc.

May 2, 2013 /s/ Don M. Bailey

Don M. Bailey
President and Chief Executive Officer
(Principal Executive Officer)

This certification accompanies the Quarterly Report on Form 10-Q pursuant to Rule 13a-14(b) or Rule 15d-14(b) under the Securities Exchange Act of 1934 and 18 U.S.C. Section 1350 and shall not be deemed filed by Questcor Pharmaceuticals, Inc. for purposes of Section 18 of the Securities Exchange Act of 1934.

**Exhibit 32.2**

**CERTIFICATION**

I, Michael H. Mulroy, hereby certify pursuant to Rule 13a-14(b) or Rule 15d-14(b) of the Securities Exchange Act of 1934 and 18 U.S.C. Section 1350, that the Quarterly Report of Questcor Pharmaceuticals, Inc. on Form 10-Q for the quarterly period ended March 31, 2013 fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934 and that information contained in such Quarterly Report on Form 10-Q for the period ended March 31, 2013 fairly presents in all material respects the financial condition and results of operations of Questcor Pharmaceuticals, Inc.

May 2, 2013 /s/ Michael H. Mulroy

Michael H. Mulroy
Chief Financial Officer
(Principal Accounting Officer)

This certification accompanies the Quarterly Report on Form 10-Q pursuant to Rule 13a-14(b) or Rule 15d-14(b) under the Securities Exchange Act of 1934 and 18 U.S.C. Section 1350 and shall not be deemed filed by Questcor Pharmaceuticals, Inc. for purposes of Section 18 of the Securities Exchange Act of 1934.