ACETO CORP
Form 10-Q
May 10, 2013

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

FORM 10-Q

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

For the quarterly period ended March 31, 2013
Commission file number 000-04217

ACETO CORPORATION
(Exact name of registrant as specified in its charter)

New York (State or other jurisdiction of incorporation or organization)	11-1720520 (I.R.S. Employer Identification Number)

4 Tri Harbor Court, Port Washington, NY 11050
(Address of principal executive offices)

(516) 627-6000
(Registrant's telephone number, including area code)

www.aceto.com
(Registrant's website address)

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

Yes x No o

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate website, if any, every interactive data file required to be submitted and posted pursuant to Rule 405 of Regulation S-T (section 232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files).

Yes x No o

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

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

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).

Yes o No x

The registrant had 27,393,375 shares of common stock outstanding as of May 6, 2013.

ACETO CORPORATION AND SUBSIDIARIES
QUARTERLY REPORT FOR THE PERIOD ENDED MARCH 31, 2013

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PART I. FINANCIAL INFORMATION
Item 1. Financial Statements

ACETO CORPORATION AND SUBSIDIARIES
CONDENSED CONSOLIDATED BALANCE SHEETS
(in thousands, except per-share amounts)

	March 31, 2013 (unaudited)	June 30, 2012
ASSETS		
Current assets:		
Cash and cash equivalents	$35,423	$24,862
Investments	1,655	1,518
Trade receivables, less allowance for doubtful accounts (March, $846; June, $887)	95,904	74,744
Other receivables	4,495	2,979
Inventory	86,681	84,687
Prepaid expenses and other current assets	3,068	2,231
Deferred income tax asset, net	1,260	948
Total current assets	228,486	191,969
Property and equipment, net	11,631	11,705
Property held for sale	4,058	3,752
Goodwill	33,512	33,495
Intangible assets, net	41,296	45,251
Deferred income tax asset, net	4,684	4,719
Other assets	9,615	8,389
TOTAL ASSETS	$333,282	$299,280
LIABILITIES AND SHAREHOLDERS' EQUITY		
Current liabilities:		
Current portion of long-term debt	$7,464	$6,713
Accounts payable	50,220	42,007
Accrued expenses	33,476	24,921
Total current liabilities	91,160	73,641
Long-term debt	36,404	39,052
Long-term liabilities	14,159	12,943
Environmental remediation liability	6,370	5,633
Deferred income tax liability	20	8
Total liabilities	148,113	131,277
Commitments and contingencies (Note 6)		
Shareholders' equity:		
Common stock, $.01 par value, 40,000 shares authorized; 27,386 and 26,937 shares issued and outstanding at March 31, 2013 and June 30,		

2012, respectively	274	269
Capital in excess of par value	67,885	64,071
Retained earnings	114,758	102,344
Accumulated other comprehensive income	2,252	1,319
Total shareholders’ equity	185,169	168,003
TOTAL LIABILITIES AND SHAREHOLDERS’ EQUITY	$333,282	$299,280

See accompanying notes to condensed consolidated financial statements and accountants’ review report.

ACETO CORPORATION AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF INCOME
(unaudited and in thousands, except per-share amounts)

	Nine Months Ended March 31, 2013	Nine Months Ended March 31, 2012
Net sales	$376,575	$333,439
Cost of sales	302,835	272,121
Gross profit	73,740	61,318
Selling, general and administrative expenses	47,769	41,678
Operating income	25,971	19,640
Other income (expense):		
Interest expense	(1,570)	(2,067)
Interest and other income, net	1,906	1,878
	336	(189)
Income before income taxes	26,307	19,451
Income tax provision	9,381	6,451
Net income	$16,926	$13,000
Net income per common share	$0.63	$0.49
Diluted net income per common share	$0.62	$0.49
Weighted average shares outstanding:		
Basic	26,956	26,558
Diluted	27,342	26,747

See accompanying notes to condensed consolidated financial statements and accountants' review report.

ACETO CORPORATION AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF INCOME
(unaudited and in thousands, except per-share amounts)

	Three Months Ended March 31, 2013	2012
Net sales	$150,871	$ 121,415
Cost of sales	119,344	99,260
Gross profit	31,527	22,155
Selling, general and administrative expenses	19,781	14,581
Operating income	11,746	7,574
Other (expense) income:		
Interest expense	(492)	(656)
Interest and other income, net	333	630
	(159)	(26)
Income before income taxes	11,587	7,548
Income tax provision	3,994	2,169
Net income	$7,593	$ 5,379
Net income per common share	$0.28	$ 0.20
Diluted net income per common share	$0.28	$ 0.20
Weighted average shares outstanding:		
Basic	27,108	26,634
Diluted	27,485	26,870

See accompanying notes to condensed consolidated financial statements and accountants' review report.

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ACETO CORPORATION AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME
(unaudited and in thousands)

	Nine Months Ended March 31,		Three Months Ended March 31,	
	2013	2012	2013	2012
Net income	$16,926	$13,000	$7,593	$5,379
Other comprehensive income:				
Foreign currency translation adjustments	824	(3,514)	(1,487)	1,327
Change in fair value of interest rate swaps	109	(102)	56	1
Comprehensive income	$17,859	$9,384	$6,162	$6,707

See accompanying notes to condensed consolidated financial statements and accountants’ review report.

ACETO CORPORATION AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
(unaudited and in thousands)

	Nine Months Ended March 31, 2013	2012
Operating activities:		
Net income	$16,926	$13,000
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	5,203	5,184
Provision for doubtful accounts	61	140
Non-cash stock compensation	1,353	881
Deferred income taxes	(268)	457
Earnings on equity investment in joint venture	(1,748)	(1,602)
Contingent consideration	2,840	-
Changes in assets and liabilities:		
Investments-trading securities	-	475
Trade accounts receivable	(20,791)	(2,457)
Other receivables	(1,591)	1,964
Inventory	(1,576)	(6,036)
Prepaid expenses and other current assets	(790)	(659)
Other assets	617	607
Accounts payable	7,959	3,282
Accrued expenses and other liabilities	9,222	(5,403)
Net cash provided by operating activities	17,417	9,833
Investing activities:		
Purchases of investments	(1,152)	(1,138)
Sales of investments	1,029	-
Payments received on notes receivable	-	350
Purchases of property and equipment, net	(902)	(692)
Payments for intangible assets	(563)	(726)
Net cash used in investing activities	(1,588)	(2,206)
Financing activities:		
Payment of cash dividends	(4,481)	(2,661)
Proceeds from exercise of stock options	1,961	198
Excess tax benefit on stock option exercises and restricted stock	427	32
Payment of deferred consideration	(1,470)	(1,500)
Repayment of bank loans	(8,897)	(4,698)
Borrowings of bank loans	7,000	-
Net cash used in financing activities	(5,460)	(8,629)
Effect of exchange rate changes on cash	192	(1,051)
Net increase (decrease) in cash	10,561	(2,053)
Cash at beginning of period	24,862	28,664
Cash at end of period	$35,423	$26,611

See accompanying notes to condensed consolidated financial statements and accountants' review report.

ACETO CORPORATION AND SUBSIDIARIES
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(unaudited and in thousands, except per-share amounts)

(1) Basis of Presentation

The condensed consolidated financial statements of Aceto Corporation and subsidiaries (“Aceto” or the “Company”) included herein have been prepared by the Company and reflect all adjustments (consisting solely of normal recurring adjustments) necessary to present fairly the financial position, results of operations and cash flows for all periods presented. Interim results are not necessarily indicative of results which may be achieved for the full year.

The preparation of financial statements in conformity with U.S. generally accepted accounting principles (GAAP) requires management to make estimates and assumptions that affect the reported amounts of assets, liabilities, revenues and expenses reported in those financial statements. These judgments can be subjective and complex, and consequently actual results could differ from those estimates and assumptions. The Company’s most critical accounting policies relate to revenue recognition; royalty income; partnered products; allowance for doubtful accounts; inventories; goodwill and other indefinite-lived intangible assets; long-lived assets; environmental and other contingencies; income taxes; and stock-based compensation.

These condensed consolidated financial statements do not include all disclosures associated with consolidated financial statements prepared in accordance with GAAP. Accordingly, these statements should be read in conjunction with the Company’s consolidated financial statements and notes thereto contained in the Company’s Form 10-K for the year ended June 30, 2012.

(2) Stock-Based Compensation

At the annual meeting of shareholders of the Company, held on December 6, 2012, the Company’s shareholders approved the amended and restated Aceto Corporation 2010 Equity Participation Plan (the “Plan”). Under the Plan, grants of stock options, restricted stock, restricted stock units, stock appreciation rights, and stock bonuses (collectively, “Stock Awards”) may be made to employees, non-employee directors and consultants of the Company, including the chief executive officer, chief financial officer and other named executive officers. The maximum number of shares of common stock of the Company that may be issued pursuant to Stock Awards granted under the Plan will not exceed, in the aggregate, 5,250 shares.

During fiscal year 2012, the Company granted 217 stock options to employees at an exercise price equal to the market value of the common stock on the date of grant, determined in accordance with the Plan. These options vest over three years and have a term of ten years from the date of grant. Compensation expense was determined using the Black-Scholes option pricing model. Total compensation expense related to stock options for the nine months ended March 31, 2013 and 2012 was $246 and $250, respectively and $83 and $79 for the three months ended March 31, 2013 and 2012, respectively. As of March 31, 2013, the total unrecognized compensation cost related to option awards is $325.

In order to determine the fair value of stock options on the date of grant, the Company uses the Black-Scholes option-pricing model, including an estimate of forfeiture rates. Inherent in this model are assumptions related to expected stock-price volatility, risk-free interest rate, expected life and dividend yield. The Company uses an expected stock-price volatility assumption that is a combination of both historical volatility, calculated based on the daily closing prices of its common stock over a period equal to the expected life of the option and implied volatility, utilizing market data of actively traded options on Aceto’s common stock, which are obtained from public data sources. The Company believes that the historical volatility of the price of its common stock over the expected life of the option is a reasonable indicator of the expected future volatility and that implied volatility takes into consideration market expectations of how future volatility might differ from historical volatility. Accordingly, the Company believes a combination of both historical and implied volatility provides the best estimate of the future volatility of the market price of its common stock. The risk-free interest rate is based on U.S. Treasury issues with a term equal to the expected life of the option. The Company uses historical data to estimate expected dividend yield, expected life and forfeiture rates. The fair values of the options granted in fiscal year 2012 were estimated based on the following weighted average assumptions:

	Nine months ended March 31, 2012	
Expected life	5.7 years	
Expected volatility	48.10	%
Risk-free interest rate	1.59	%
Dividend yield	3.24	%

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ACETO CORPORATION AND SUBSIDIARIES
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(unaudited and in thousands, except per-share amounts)

There were no stock options granted in the nine months ended March 31, 2013.

During the nine months ended March 31, 2013, the Company granted 120 shares of restricted common stock to its employees that vest over three years and 25 shares of restricted common stock to its non-employee directors, which vest over one year. In addition, the Company also issued a target grant of 84 performance-vested restricted stock units, which grant could be as much as 126 if certain performance criteria and market conditions are met. Performance-vested restricted stock units will cliff vest 100% at the end of the third year following grant in accordance with the performance metrics set forth in the applicable employee performance-vested restricted stock unit grant.

During the year ended June 30, 2012, the Company granted 103 shares of restricted common stock to its employees that vest over three years and 38 shares of restricted common stock to its non-employee directors, which vest over one year. In addition, the Company also issued a target grant of 49 performance-vested restricted stock units, which grant could be as much as 73 if certain performance criteria and market conditions are met. Performance-vested restricted stock units will cliff vest 100% at the end of the third year following grant in accordance with the performance metrics set forth in the applicable employee performance-vested restricted stock unit grant.

For the three and nine months ended March 31, 2013, the Company recorded stock-based compensation expense of approximately $361 and $1,097 respectively, related to restricted common stock and restricted stock units. For the three and nine months ended March 31, 2012, the Company recorded stock-based compensation expense of approximately $203 and $623, respectively, related to restricted common stock and restricted stock units. As of March 31, 2013, the total unrecognized compensation cost related to restricted stock awards and units is approximately $2,204.

(3) Common Stock

On May 9, 2013, the Company's board of directors declared a regular quarterly dividend of $0.055 per share to be distributed on June 25, 2013 to shareholders of record as of June 14, 2013.

On February 7, 2013, the Company's board of directors declared a regular quarterly dividend of $0.055 per share which was paid on March 26, 2013 to shareholders of record as of March 15, 2013.

On December 6, 2012, the Company's board of directors declared a regular quarterly dividend of $0.055 per share which was paid on December 28, 2012 to shareholders of record as of December 17, 2012.

On September 6, 2012, the Company's board of directors declared a regular quarterly dividend of $0.055 per share which was paid on September 28, 2012 to shareholders of record as of September 17, 2012.

ACETO CORPORATION AND SUBSIDIARIES
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(unaudited and in thousands, except per-share amounts)

(4) Net Income Per Common Share

Basic income per common share is based on the weighted average number of common shares outstanding during the period. Diluted income per common share includes the dilutive effect of potential common shares outstanding. The following table sets forth the reconciliation of weighted average shares outstanding and diluted weighted average shares outstanding:

	Nine months ended March 31,		Three months ended March 31,	
	2013	2012	2013	2012
Weighted average shares outstanding	26,956	26,558	27,108	26,634
Dilutive effect of stock options and restricted stock awards and units	386	189	377	236
Diluted weighted average shares outstanding	27,342	26,747	27,485	26,870

There were 566 and 1,571 common equivalent shares outstanding as of March 31, 2013 and 2012, respectively, that were not included in the calculation of diluted income per common share for the nine months ended March 31, 2013 and 2012, respectively, because their effect would have been anti-dilutive. There were 545 and 1,250 common equivalent shares outstanding as of March 31, 2013 and 2012, respectively, that were not included in the calculation of diluted income per common share for the three months ended March 31, 2013 and 2012, respectively, because their effect would have been anti-dilutive.

(5) Debt

Long-term debt

	March 31, 2013	June 30, 2012
Revolving bank loans	$ 14,000	$ 11,000
Term bank loans	26,250	31,000
Mortgage	3,618	3,765
	43,868	45,765
Less current portion	7,464	6,713
	$ 36,404	$ 39,052

ACETO CORPORATION AND SUBSIDIARIES
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(unaudited and in thousands, except per-share amounts)
Credit Facilities

On December 31, 2010, the Company entered into a Credit Agreement (the "Credit Agreement") with two U.S. financial institutions. Aceto may borrow, repay and reborrow during the period ending December 31, 2015, up to but not exceeding at any one time outstanding $40,000 (the "Revolving Loans"). The Revolving Loans may be (i) Adjusted LIBOR Loans (as defined in the Credit Agreement), (ii) Alternate Base Rate Loans (as defined in the Credit Agreement) or (iii) a combination thereof. As of March 31, 2013, the Company borrowed Revolving Loans aggregating $14,000, which loans are Adjusted LIBOR Loans at an interest rate of 2.06% at March 31, 2013. The Credit Agreement also allows for the borrowing of up to $40,000 (the "Term Loan"). The Company borrowed a Term Loan of $40,000 on December 31, 2010. The Term Loan interest may be payable as an (i) Adjusted LIBOR Loan, (ii) Alternate Base Rate Loan, or (iii) a combination thereof. As of March 31, 2013, the remaining amount outstanding under the original amortizing Term Loan is $26,250 and is payable as an Adjusted LIBOR Loan at an interest rate of 2.06% at March 31, 2013. The Term Loan is payable as to principal in twenty (20) consecutive quarterly installments, which commenced on March 31, 2011 and will continue on each June 30, September 30 and December 31st thereafter, each in the amount set forth below opposite the applicable installment, provided that the final payment on the Term Loan Maturity Date (as defined in the Credit Agreement) shall be in an amount equal to the then outstanding unpaid principal amount of the Term Loan:

Installment	Amount
1 through 8	$ 1,500
9 through 12	$ 1,750
13 through 16	$ 2,000
17 through 20	$ 3,250

As such, the Company has classified $7,250 of the Term Loan as short-term in the consolidated balance sheet at March 31, 2013. The Credit Agreement also provides that commercial letters of credit shall be issued to provide the primary payment mechanism in connection with the purchase of any materials, goods or services by the Company in the ordinary course of business. The Company had open letters of credit of approximately $47 and $199 as of March 31, 2013 and June 30, 2012, respectively. The terms of these letters of credit are all less than one year. No material loss is anticipated due to non-performance by the counterparties to these agreements.

The Credit Agreement provides for a security interest in all personal property of the Company. The Credit Agreement contains several financial covenants including, among other things, maintaining a minimum level of debt service. The Company is also subject to certain restrictive covenants, including, among other things, covenants governing liens, limitations on indebtedness, limitations on cash dividends, guarantees, sale of assets, sales of receivables, and loans and investments. The Company was in compliance with all covenants at March 31, 2013.

Mortgage

On June 30, 2011, the Company entered into a mortgage payable for $3,947 on its new corporate headquarters, in Port Washington, New York. This mortgage payable is secured by the land and building and is being amortized over a period of 20 years. The mortgage payable bears interest at 5.92% and matures on June 30, 2021.

(6) Commitments, Contingencies and Other Matters

The Company and its subsidiaries are subject to various claims which have arisen in the normal course of business. The impact of the final resolution of these matters on the Company's results of operations in a particular reporting period is not known. Management is of the opinion, however, that the ultimate outcome of such matters will not have a material adverse effect upon the Company's financial condition or liquidity.

On October 29, 2012, a lawsuit was filed in the United Kingdom by United Phosphorous Limited ("UPL") against Aceto Agricultural Chemicals Corporation ("AACC"), a wholly-owned subsidiary of the Company. In the lawsuit, UPL alleges, among other things, that AACC breached a 1995 agreement regarding European sales of a potato sprout suppression product, by selling the product in Europe. UPL claims damages of approximately £4,500 (approximately US $7,200) plus an unspecified amount of additional damages. While the impact of the resolution of the matter, including any legal and other associated costs, on the Company's consolidated results of operations in a particular reporting period is not known at this time, after a detailed review and careful analysis of the allegations, AACC strongly denies the allegations, believes that UPL's claims are without merit and intends to vigorously defend the lawsuit.

ACETO CORPORATION AND SUBSIDIARIES
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(unaudited and in thousands, except per-share amounts)

In fiscal years 2011, 2009, 2008 and 2007, the Company received letters from the Pulvair Site Group, a group of potentially responsible parties (PRP Group) who are working with the State of Tennessee (the State) to remediate a contaminated property in Tennessee called the Pulvair site. The PRP Group has alleged that Aceto shipped hazardous substances to the site which were released into the environment. The State had begun administrative proceedings against the members of the PRP Group and Aceto with respect to the cleanup of the Pulvair site and the PRP Group has begun to undertake cleanup. The PRP Group is seeking a settlement of approximately $1,700 from the Company for its share to remediate the site contamination. Although the Company acknowledges that it shipped materials to the site for formulation over twenty years ago, the Company believes that the evidence does not show that the hazardous materials sent by Aceto to the site have significantly contributed to the contamination of the environment and thus believes that, at most, it is a de minimus contributor to the site contamination. Accordingly, the Company believes that the settlement offer is unreasonable. The impact of the resolution of this matter on the Company's results of operations in a particular reporting period is not known. However, management believes that the ultimate outcome of this matter will not have a material adverse effect on the Company's financial condition or liquidity.

The Company has environmental remediation obligations in connection with Arsynco, Inc. (Arsynco), a subsidiary formerly involved in manufacturing chemicals located in Carlstadt, New Jersey, which was closed in 1993 and is currently held for sale. Based on continued monitoring of the contamination at the site and the approved plan of remediation, the Company received an estimate from an environmental consultant stating that the costs of remediation could be between $9,000 and $10,800. Remediation commenced in fiscal 2010, and as of March 31, 2013 and June 30, 2012, a liability of $7,400 and $7,566, respectively, is included in the accompanying condensed consolidated balance sheets for this matter. In accordance with GAAP, management believes that the majority of costs incurred to remediate the site will be capitalized in preparing the property which is currently classified as held for sale. An appraisal of the fair value of the property by a third-party appraiser supports the assumption that the expected fair value after the remediation is in excess of the amount required to be capitalized. However, these matters, if resolved in a manner different from those assumed in current estimates, could have a material adverse effect on the Company's financial condition, operating results and cash flows when resolved in a future reporting period.

In connection with the environmental remediation obligation for Arsynco, in July 2009, the Company entered into a settlement agreement with BASF Corporation (BASF), the former owners of the Arsynco property. In accordance with the settlement agreement, BASF paid for a portion of the prior remediation costs and going forward, will co-remediate the property with the Company. In accordance with the contract, BASF paid $550 related to past response costs and will pay a proportionate share of the future remediation costs. Accordingly, the Company recorded a gain of $550 in fiscal 2009. This $550 gain relates to the partial reimbursement of costs of approximately $1,200 that the Company previously expensed. The Company also recorded an additional receivable from BASF, with an offset against property held for sale, representing its estimated portion of the future remediation costs. The balance of this receivable for future remediation costs as of March 31, 2013 and June 30, 2012 is $3,330 and $3,405, respectively, which is included in the accompanying condensed consolidated balance sheets.

In March 2006, Arsynco received notice from the EPA of its status as a PRP under the Comprehensive Environmental Response, Compensation and Liability Act (CERCLA) for a site described as the Berry's Creek Study Area. Arsynco is one of over 150 PRPs which have potential liability for the required investigation and remediation of the site. The estimate of the potential liability is not quantifiable for a number of reasons, including the difficulty in determining the extent of contamination and the length of time remediation may require. In addition, any estimate of liability must also consider the number of other PRPs and their financial strength. Based on prior practice in similar situations, it is possible that the State may assert a claim for natural resource damages with respect to the Arsynco site itself, and either the federal government or the State (or both) may assert claims against Arsynco for natural resource damages in connection with Berry’s Creek; any such claim with respect to Berry’s Creek could also be asserted against the approximately 150 PRPs which the EPA has identified in connection with that site. Any claim for natural resource damages with respect to the Arsynco site itself may also be asserted against BASF, the former owners of the Arsynco property. In September 2012, Arsynco entered into an agreement with three of the other PRPs that had previously been impleaded into New Jersey Department of Environmental Protection, et al. v. Occidental Chemical Corporation, et al., Docket No. ESX-L-9868-05 (the “NJDEP Litigation”) and were considering impleading Arsynco into same. Arsynco entered into agreement to avoid impleader. Pursuant to agreement, Arsynco agreed to (1) a tolling period that would not be included when computing the running of any statute of limitations that might provide a defense to the NJDEP Litigation; (2) the waiver of certain issue preclusion defenses in the NJDEP Litigation; and (3) arbitration of certain potential future liability allocation claims if the other parties to the agreement are barred by a court of competent jurisdiction from proceeding against Arsynco. Since an amount of the liability cannot be reasonably estimated at this time, no accrual is recorded for these potential future costs. The impact of the resolution of this matter on the Company’s results of operations in a particular reporting period is not known. However, management believes that the ultimate outcome of this matter will not have a material adverse effect on the Company’s financial condition or liquidity.

ACETO CORPORATION AND SUBSIDIARIES
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(unaudited and in thousands, except per-share amounts)

A subsidiary of the Company markets certain agricultural protection products which are subject to the Federal Insecticide, Fungicide and Rodenticide Act (FIFRA). FIFRA requires that test data be provided to the EPA to register, obtain and maintain approved labels for pesticide products. The EPA requires that follow-on registrants of these products compensate the initial registrant for the cost of producing the necessary test data on a basis prescribed in the FIFRA regulations. Follow-on registrants do not themselves generate or contract for the data. However, when FIFRA requirements mandate that new test data be generated to enable all registrants to continue marketing a pesticide product, often both the initial and follow-on registrants establish a task force to jointly undertake the testing effort. The Company is presently a member of several such task force groups, which requires payments for such memberships. In addition, in connection with its agricultural protection business, the Company plans to acquire product registrations and related data filed with the United States Environmental Protection Agency to support such registrations and other supporting data for several products. The acquisition of these product registrations and related data filed with the United States Environmental Protection Agency as well as payments to various task force groups could approximate $4,661 through fiscal 2014, of which $0 and $242 has been accrued as of March 31, 2013 and June 30, 2012, respectively.

On December 31, 2010, the Company acquired certain assets of Rising Pharmaceuticals, Inc. (“Rising”), a New Jersey based company that markets and distributes generic prescription and over the counter pharmaceutical products to leading wholesalers, chain drug stores, distributors, mass market merchandisers and others under its own label, throughout the United States. The purchase agreement provides for the payment of additional contingent consideration equal to one-half of the three year cumulative Rising earnings before interest, taxes, depreciation and amortization in excess of $32,100, up to a maximum of $6,000. As of March 31, 2013, the Company has accrued $4,811 related to this contingent consideration. In the third quarter of fiscal 2013, the Company recorded additional contingent consideration of $2,840, which is included in selling, general and administrative expenses in the accompanying condensed consolidated statements of income for the three and nine months ended March 31, 2013. Any necessary future adjustments to this amount will be recorded as an income statement charge at that time.

(7) Fair Value Measurements

GAAP defines fair value as the price that would be received to sell an asset or paid to transfer a liability in an orderly fashion between market participants at the measurement date. GAAP establishes a fair value hierarchy for those instruments measured at fair value that distinguishes between assumptions based on market data (observable inputs) and the Company’s assumptions (unobservable inputs). The hierarchy consists of three levels:

Level 1 – Quoted market prices in active markets for identical assets or liabilities;

Level 2 – Inputs other than Level 1 inputs that are either directly or indirectly observable; and

Level 3 – Unobservable inputs that are not corroborated by market data.

On a recurring basis, Aceto measures at fair value certain financial assets and liabilities, which consist of cash equivalents, investments and foreign currency contracts. The Company classifies cash equivalents and investments within Level 1 if quoted prices are available in active markets. Level 1 assets include instruments valued based on quoted market prices in active markets which generally include corporate equity securities publicly traded on major exchanges. Time deposits are very short-term in nature and are accordingly valued at cost plus accrued interest, which approximates fair value, and are classified within Level 2 of the valuation hierarchy. The Company uses foreign currency forward contracts (futures) to minimize the risk caused by foreign currency fluctuation on its foreign currency receivables and payables by purchasing futures with one of its financial institutions. Futures are traded on regulated U.S. and international exchanges and represent commitments to purchase or sell a particular foreign currency at a future date and at a specific price. Aceto's foreign currency derivative contracts are classified within Level 2 as the fair value of these hedges is primarily based on observable forward foreign exchange rates. At March 31, 2013 the Company had foreign currency contracts outstanding that had a notional amount of $64,484. Unrealized losses on hedging activities for the nine months ended March 31, 2013 and 2012 was $218 and $221, respectively, and are included in interest and other income, net, in the condensed consolidated statements of income. The contracts have varying maturities of less than one year.

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Pursuant to the requirements of the Credit Agreement, the Company is required to deliver Hedging Agreements (as defined in the Credit Agreement) fixing the interest rate on not less than $20,000 of the Term Loan. Accordingly, in March 2011, the Company entered into an interest rate swap for a notional amount of $20,000, which has been designated as a cash flow hedge. The expiration date of this interest rate swap is December 31, 2015. The unrealized loss to date associated with this derivative, which is recorded in accumulated other comprehensive income in the condensed consolidated balance sheet at March 31, 2013, is $318. Aceto's interest rate swap is classified within Level 2 as the fair value of this hedge is primarily based on observable interest rates.

As of March 31, 2013 and June 30, 2012, the Company had $4,811 and $1,779, respectively, of contingent consideration that was recorded at fair value in the Level 3 category, which related to the acquisition of Rising, which was completed during fiscal 2011. The contingent consideration was calculated using the present value of a probability weighted income approach. The changes in contingent consideration relates to accrued interest expense of $192 and additional contingent consideration of $2,840 for the Rising acquisition, recorded in the third quarter of fiscal 2013.

During the fourth quarter of each year, the Company evaluates goodwill and indefinite-lived intangibles for impairment at the reporting unit level using an undiscounted cash flow model using Level 3 inputs. Additionally, on a nonrecurring basis, the Company uses fair value measures when analyzing asset impairment. Long-lived assets and certain identifiable intangible assets are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. If it is determined such indicators are present and the review indicates that the assets will not be fully recoverable, based on undiscounted estimated cash flows over the remaining amortization periods, their carrying values are reduced to estimated fair value. Measurements based on undiscounted cash flows are considered to be Level 3 inputs.

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The following tables summarize the valuation of the Company's financial assets and liabilities which were determined by using the following inputs at March 31, 2013 and June 30, 2012:

	Fair Value Measurements at March 31, 2013 Using			
	Quoted Prices in Active Markets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Total
Cash equivalents:				
Time deposits	-	$837	-	$837
Investments:				
Time deposits	-	1,655	-	1,655
Foreign currency contracts-liabilities (1)	-	216	-	216
Derivative liability for interest rate swap (2)	-	318	-	318
Contingent consideration (2)	-	-	$ 4,811	4,811

(1) Included in "Accrued expenses" in the accompanying Condensed Consolidated Balance Sheet as of March 31, 2013.
(2) Included in "Long-term liabilities" in the accompanying Condensed Consolidated Balance Sheet as of March 31, 2013.

	Fair Value Measurements at June 30, 2012 Using			
	Quoted Prices in Active Markets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Total
Cash equivalents:				
Time deposits	-	$814	-	$814
Investments:				
Time deposits	-	1,518	-	1,518

Foreign currency contracts-assets (3)	-	138	-	138
Foreign currency contracts-liabilities (4)	-	661	-	661
Derivative liability for interest rate swap (5)	-	427	-	427
Contingent consideration (5)	-	-	$ 1,779	1,779

(3) Included in “Other receivables” in the accompanying Condensed Consolidated Balance Sheet as of June 30, 2012.
(4) Included in “Accrued expenses” in the accompanying Condensed Consolidated Balance Sheet as of June 30, 2012.
(5) Included in “Long-term liabilities” in the accompanying Condensed Consolidated Balance Sheet as of June 30, 2012.

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The carrying values of all financial instruments classified as a current asset or current liability are deemed to approximate fair value because of the short maturity of these instruments. The fair values of the Company's notes receivable and short-term and long-term bank loans were based upon current rates offered for similar financial instruments to the Company.

(8) Recent Accounting Pronouncements

In June 2011, the Financial Accounting Standards Board (the "FASB") issued Accounting Standards Update ("ASU") 2011-05, "Presentation of Comprehensive Income", which eliminates the option to report other comprehensive income and its components in the statement of changes in stockholders' equity and requires an entity to present the total of comprehensive income, the components of net income and the components of other comprehensive income either in a single continuous statement or in two separate but consecutive statements. This pronouncement is effective for fiscal years, and interim periods within those years, beginning after December 15, 2011. In December 2011, the FASB issued ASU 2011-12 "Comprehensive Income (Topic 220): Deferral of the Effective Date for Amendments to the Presentation of Reclassifications of Items Out of Accumulated Other Comprehensive Income in Accounting Standards Update No. 2011-05" . ASU 2011-12 deferred certain aspects of ASU 2011-05. The new guidance is effective for fiscal years, and interim periods within those years, beginning after December 15, 2011. The Company adopted this guidance in this first quarter of fiscal 2013. As this guidance only amends the presentation of the components of comprehensive income, the adoption did not have an impact on the Company's consolidated financial statements.

In September 2011, the FASB issued ASU 2011-08, "Intangibles-Goodwill and Other (Topic 350): Testing Goodwill for Impairment", to allow entities to use a qualitative approach to test goodwill for impairment. ASU 2011-08 permits an entity to first perform a qualitative assessment to determine whether it is more likely than not that the fair value of a reporting unit is less than its carrying value. If it is concluded that this is the case, it is necessary to perform the currently prescribed two-step goodwill impairment test. Otherwise, the two-step goodwill impairment test is not required. ASU 2011-08 is effective for the Company in fiscal 2013 and earlier adoption is permitted. The Company adopted ASU 2011-08 at the beginning of fiscal 2013. This adoption did not have a material impact on the Company's consolidated financial statements.

In July 2012, the FASB issued ASU 2012-02, "Testing Indefinite-Lived Intangible Assets for Impairment (the revised standard)" , which allows companies the option to perform a qualitative assessment to determine whether further impairment testing of indefinite-lived intangible assets is necessary. Under this guidance, an entity is required to perform a quantitative impairment test if qualitative factors indicate that it is more likely than not that indefinite-lived intangible assets are impaired. The qualitative factors are consistent with the guidance established for goodwill impairment testing and include identifying and assessing events and circumstances that would most significantly impact, individually or in the aggregate, the carrying value of the indefinite-lived intangible assets. The revised standard is effective for the Company in fiscal 2014 and early adoption is permitted. The adoption of ASU 2012 -02 is not expected to have a material impact on the Company's consolidated financial statements.

In October 2012, the FASB issued ASU 2012-04, "Technical Corrections and Improvements." ASU 2012-04 contains certain technical corrections and conforming fair value amendments to the FASB Accounting Standards Codification. The amendments that do not have transition guidance were effective upon issuance. The amendments that are subject to the transition guidance will be effective for fiscal periods beginning after December 15, 2012. The adoption of ASU 2012-04 will not have a material impact on the Company's consolidated financial statements.

(9) Segment Information

The Company's business is organized along product lines into three principal segments: Human Health, Pharmaceutical Ingredients and Performance Chemicals. In fiscal 2012, the Company reconfigured and renamed its three business segments to more accurately reflect the scope of its business activities. As such, the Company has recasted the segment information as if the composition of its reportable segments had existed in the prior period presented.

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Human Health - includes finished dosage form generic drugs and nutraceutical products.

Pharmaceutical Ingredients – includes pharmaceutical intermediates and active pharmaceutical ingredients (APIs).

Performance Chemicals - The Performance Chemicals segment is made up of two product groups: Specialty Chemicals and Agriculture Protection Products. Specialty chemicals includes a variety of chemicals which make plastics, surface coatings, textiles, fuels and lubricants perform to their designed capabilities. Dye and pigment intermediates are used in the color-producing industries such as textiles, inks, paper, and coatings. Organic intermediates are used in the production of agrochemicals. In addition, Aceto is a supplier of diazos and couplers to the paper, film and electronics industries.

Agricultural Protection Products includes herbicides, fungicides and insecticides that control weed growth as well as control the spread of insects and other microorganisms that can severely damage plant growth. The Agricultural Protection Products segment also includes a sprout inhibitor for potatoes and an herbicide for sugar cane.

The Company's chief operating decision maker evaluates performance of the segments based on net sales, gross profit and income before income taxes. Unallocated corporate amounts are deemed by the Company as administrative, oversight costs, not managed by the segment managers. The Company does not allocate assets by segment because the chief operating decision maker does not review the assets by segment to assess the segments' performance, as the assets are managed on an entity-wide basis.

Nine Months Ended March 31, 2013 and 2012:

	Human Health	Pharmaceutical Ingredients	Performance Chemicals	Unallocated Corporate	Consolidated Totals
2013					
Net sales	$ 92,559	$ 142,169	$ 141,847	$ -	$ 376,575
Gross profit	28,062	25,429	20,249	-	73,740
Income (loss) before income taxes	12,760	12,432	8,391	(7,276)	26,307
2012					
Net sales	$ 78,243	$ 121,537	$ 133,659	$ -	$ 333,439
Gross profit	22,860	18,654	19,804	-	61,318
Income (loss) before income taxes	9,836	5,839	7,940	(4,164)	19,451

Three Months Ended March 31, 2013 and 2012:

	Human Health	Pharmaceutical Ingredients	Performance Chemicals