

Consolidated Financial Statements and Report of  
Independent Certified Public Accountants

**United States Pharmacopeial  
Convention and Subsidiaries**

June 30, 2009, 2008, 2007, 2006 and 2005

# United States Pharmacopeial Convention and Subsidiaries

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## United States Pharmacopeial Convention and Subsidiaries

### Consolidated Statements of Financial Position

<i>June 30,</i>	<b>2009</b>	<b>2008</b>	<b>2007</b>	<b>2006</b>	<b>2005</b>
<b>Assets</b>					
<b>Current Assets</b>					
Cash and Cash Equivalents	\$ 9,449,686	\$ 4,194,068	\$ 6,626,965	\$ 8,129,417	\$ 6,910,589
Accounts Receivable:					
Reference Standards and Publications	8,858,943	8,141,158	7,726,439	7,135,866	5,563,137
Cooperative Agreements and Grants	475,630	407,343	1,089,678	1,021,612	819,319
Inventory	66,748,409	70,726,999	52,146,746	44,176,164	42,992,098
Prepaid Expenses and Other Assets	2,178,169	2,519,129	2,383,871	1,459,107	1,851,001
<b>Total Current Assets</b>	<b>87,710,837</b>	<b>85,988,697</b>	<b>69,973,699</b>	<b>61,922,166</b>	<b>58,136,144</b>
<b>Other Assets</b>					
Investments	63,819,341	75,849,835	83,840,549	69,984,295	64,029,768
Trustee Held Cash For Construction	—	—	9,448,146	48,552,944	68,740,007
Property and Equipment - Net	111,807,523	118,157,278	25,932,167	24,456,793	22,950,345
Construction In Process - Real Estate	—	—	75,952,594	29,257,387	6,712,332
Other Assets	3,623,470	3,958,509	3,907,048	3,365,141	3,672,787
Interest Rate Swap Agreement	—	—	45,137	372,711	—
<b>Total Other Assets</b>	<b>179,250,334</b>	<b>197,965,622</b>	<b>199,125,641</b>	<b>175,989,271</b>	<b>166,105,239</b>
<b>Total Assets</b>	<b>\$ 266,961,171</b>	<b>\$ 283,954,319</b>	<b>\$ 269,099,340</b>	<b>\$ 237,911,437</b>	<b>\$ 224,241,383</b>
<b>Liabilities and Net Assets</b>					
<b>Current Liabilities</b>					
Accounts Payable and Accrued Expenses	\$ 12,097,733	\$ 17,399,406	\$ 15,035,629	\$ 16,366,580	\$ 13,387,377
Revolving Line of Credit	2,000,000	4,000,000	—	—	—
Current Portion of Long Term Debt	4,377,158	—	—	—	—
Leases Payable Short Term	24,621	29,819	—	—	—
Deferred Revenue	3,254,922	3,411,730	3,798,808	3,733,281	3,339,943
<b>Total Current Liabilities</b>	<b>21,754,434</b>	<b>24,840,955</b>	<b>18,834,437</b>	<b>20,099,861</b>	<b>16,727,320</b>
<b>Long-term Liabilities</b>					
Interest Rate Swap Agreement	—	6,515,646	—	—	8,113,467
Leases Payable Long-term	16,204	42,611	—	—	—
Long-term Debt - 2004 and 2006 Bonds	—	97,595,000	97,595,000	87,495,000	87,495,000
Long-term Debt - 2008 Bonds	98,650,000	—	—	—	—
Long-term Debt - Term Loan	—	1,017,694	—	—	—
Long-term Taxable Loan	13,170,000	—	—	—	—
<b>Total Long-term Liabilities</b>	<b>111,836,204</b>	<b>105,170,951</b>	<b>97,595,000</b>	<b>87,495,000</b>	<b>95,608,467</b>
<b>Total Liabilities</b>	<b>133,590,638</b>	<b>130,011,906</b>	<b>116,429,437</b>	<b>107,594,861</b>	<b>112,335,787</b>
<b>Net Assets - Unrestricted</b>	<b>133,370,533</b>	<b>153,942,413</b>	<b>152,669,903</b>	<b>130,316,576</b>	<b>111,905,596</b>
<b>Total Liabilities and Net Assets</b>	<b>\$ 266,961,171</b>	<b>\$ 283,954,319</b>	<b>\$ 269,099,340</b>	<b>\$ 237,911,437</b>	<b>\$ 224,241,383</b>

The accompanying notes are an integral part of these statements.

## United States Pharmacopeial Convention and Subsidiaries

### Consolidated Statements of Activities and Changes in Net Assets

<i>Year ended June 30</i>	<b>2009</b>	<b>2008</b>	<b>2007</b>	<b>2006</b>	<b>2005</b>
<b>Operating Revenue</b>					
Reference Standards	\$ 89,883,005	\$ 80,587,095	\$ 69,545,308	\$ 58,431,105	\$ 49,349,502
Publications	14,029,135	13,786,675	13,067,604	12,759,541	12,629,966
Other	850,175	3,148,368	3,267,241	3,181,021	4,020,665
Total Compendial Activities	<u>104,762,315</u>	<u>97,522,138</u>	<u>85,880,153</u>	<u>74,371,667</u>	<u>66,000,133</u>
Verification Programs	1,393,508	1,266,377	920,902	756,231	1,000,408
Pharmacopeial Education	710,283	750,660	510,195	477,379	476,583
Other	301,592	205,569	327,822	266,736	200,215
Total Allied Compendial Activities	<u>2,405,383</u>	<u>2,222,606</u>	<u>1,758,919</u>	<u>1,500,346</u>	<u>1,677,206</u>
USAID Grant	4,034,226	4,118,926	3,765,815	3,068,462	2,527,479
Other	438,608	171,398	30,546	38,904	—
Total Non-Compendial Activities	<u>4,472,833</u>	<u>4,290,324</u>	<u>3,796,361</u>	<u>3,107,366</u>	<u>2,527,479</u>
Contributed Reference Standards	52,825,043	57,600,969	11,772,541	8,912,384	12,116,668
Contributed Services	11,397,040	10,909,721	8,957,073	7,002,805	6,908,309
<b>Total Operating Revenue</b>	<b><u>175,862,614</u></b>	<b><u>172,545,758</u></b>	<b><u>112,165,047</u></b>	<b><u>94,894,568</u></b>	<b><u>89,229,795</u></b>
<b>Expenses</b>					
Compendial Activities	160,861,291	149,408,075	92,453,879	84,478,542	71,972,980
Allied Compendial Activities	2,997,705	4,538,233	2,543,815	1,821,209	2,096,182
Non-Compendial Activities	5,560,000	4,160,445	5,762,807	4,545,502	4,316,038
<b>Total Expenses</b>	<b><u>169,418,996</u></b>	<b><u>158,106,753</u></b>	<b><u>100,760,501</u></b>	<b><u>90,845,253</u></b>	<b><u>78,385,200</u></b>
<b>Increase in Net Assets from Operations</b>	<b>6,443,619</b>	<b>14,439,005</b>	<b>11,404,546</b>	<b>4,049,315</b>	<b>10,844,595</b>
Investment Income	(12,127,997)	(2,630,381)	11,084,817	6,117,748	3,387,494
Change in Interest Rate Swap Agreement Valuation	(7,220,336)	(6,560,783)	(327,574)	8,486,178	(8,113,467)
Bond and Swap Interest Expense	(2,783,988)	(3,614,623)	—	—	—
Bond Liquidity and Remarketing Fees	(100,413)	(214,547)	—	—	—
Bond Debt Amortization	(3,710,472)	(171,764)	—	—	—
Letter of Credit	(259,409)	—	—	—	—
Line of Credit	(165,575)	—	—	—	—
Taxable Loan	(214,602)	—	—	—	—
Other Expense	(70,395)	(170,194)	(35,518)	(114,928)	(225,315)
Foreign Currency Exchange Gain (Loss)	(1,152,024)	195,797	227,056	(127,333)	—
Unrealized Gain (Loss) on Derivatives	789,712	—	—	—	—
<b>Change in Net Assets</b>	<b>(20,571,881)</b>	<b>1,272,510</b>	<b>22,353,327</b>	<b>18,410,980</b>	<b>5,893,307</b>
<b>Net Assets, beginning of year</b>	<b><u>153,942,413</u></b>	<b><u>152,669,903</u></b>	<b><u>130,316,576</u></b>	<b><u>111,905,596</u></b>	<b><u>106,012,289</u></b>
<b>Net Assets, end of year</b>	<b>\$ 133,370,533</b>	<b>\$ 153,942,413</b>	<b>\$ 152,669,903</b>	<b>\$ 130,316,576</b>	<b>\$ 111,905,596</b>

The accompanying notes are an integral part of these statements.

## United States Pharmacopeial Convention and Subsidiaries

### Consolidated Statements of Cash Flows

<i>Year ended June 30,</i>	<b>2009</b>	<b>2008</b>	<b>2007</b>	<b>2006</b>	<b>2005</b>
<b>(Decrease) Increase in Cash and Cash Equivalents</b>					
<b>Cash Flows from Operating Activities</b>					
Change in net assets	\$ (20,571,880)	\$ 1,272,510	\$ 22,353,327	\$ 18,410,980	\$ 5,893,306
Adjustments to reconcile change in net assets to net cash from operating activities:					
Depreciation	8,496,994	7,486,541	5,121,021	3,918,699	3,942,968
(Gain) Loss on disposal of property and equipment	9,267	8,267	(438)	24,803	104,614
Net realized and unrealized gain on investment	14,180,523	4,994,019	(8,917,229)	(4,663,595)	(1,801,112)
Unrealized loss (gain) on interest rate swap valuation	(6,515,646)	6,560,783	327,574	(8,486,178)	8,113,467
Revenue from contributed reference standards	(52,825,043)	(26,931,741)	(11,772,541)	(8,912,384)	(12,116,668)
Cost of goods sold from contributed reference standards	9,320,026	10,654,196	5,452,485	9,315,037	5,707,070
Reserve for Slow Moving Inventory	11,574,227	2,172,524	—	—	—
Revenue from contributed services	(11,397,040)	(10,909,721)	(8,957,073)	(7,002,805)	(6,908,309)
Expenses from contributed services	11,397,040	10,909,721	8,957,073	7,002,805	6,908,309
Changes in operating assets and liabilities:					
Accounts receivable	(786,072)	267,615	(658,639)	(1,775,022)	493,703
Inventory	35,909,380	(4,475,232)	(1,650,526)	(1,586,720)	(1,893,533)
Prepaid expenses and other assets	340,959	(135,257)	(924,764)	391,894	(448,402)
Other assets	335,039	(51,459)	(343,125)	123,526	(163,232)
Accounts payable and accrued expenses	(5,301,674)	2,363,778	(1,330,951)	2,979,203	634,652
Deferred revenue	(156,808)	(387,078)	65,527	393,339	(121,682)
<b>Net Cash (Used in) Provided by Operating Activities</b>	<b>(5,990,708)</b>	<b>3,799,466</b>	<b>7,721,721</b>	<b>10,133,582</b>	<b>8,345,151</b>
<b>Cash Flows from Investing Activities</b>					
Proceeds from sales of investments	107,509,337	126,111,770	106,996,683	40,551,981	110,686,117
Purchases of investments	(109,659,366)	(123,115,075)	(111,935,707)	(41,842,913)	(114,237,301)
Proceeds from sale of property and equipment	—	904	—	—	2,500
Purchases of property and equipment	(2,156,505)	(23,768,229)	(6,373,725)	(5,449,951)	(5,075,419)
Construction in process - real estate	—	—	(46,496,422)	(22,360,935)	(4,777,708)
<b>Net Cash Used in Investing Activities</b>	<b>(4,306,534)</b>	<b>(20,770,630)</b>	<b>(57,809,171)</b>	<b>(29,101,818)</b>	<b>(13,401,811)</b>
<b>Cash Flows from Financing Activities</b>					
Proceeds from issuance of long-term debt	115,179,465	1,017,694	10,100,000	—	87,495,000
Payments of debt financing costs	—	—	(619,801)	—	(3,635,417)
Payments on long-term debt	(97,595,000)	—	—	—	(9,033,333)
Deposits to trustee held cash for construction	—	—	(10,100,000)	—	(72,628,589)
Line of Credit	(2,000,000)	4,000,000	—	—	—
Lease Payable	(31,605)	72,427	—	—	—
Withdrawals from trustee held cash for construction	—	9,448,146	49,204,799	20,187,064	3,888,582
<b>Net Cash Provided by Investing Activities</b>	<b>15,552,860</b>	<b>14,538,267</b>	<b>48,584,998</b>	<b>20,187,064</b>	<b>6,086,243</b>
<b>Net Increase (Decrease) in Cash and Cash Equivalents</b>	<b>5,255,618</b>	<b>(2,432,897)</b>	<b>(1,502,452)</b>	<b>1,218,828</b>	<b>1,029,583</b>
<b>Cash and Cash Equivalents, beginning of year</b>	<b>4,194,068</b>	<b>6,626,965</b>	<b>8,129,417</b>	<b>6,910,589</b>	<b>5,881,006</b>
<b>Cash and Cash Equivalents, end of year</b>	<b>\$ 9,449,686</b>	<b>\$ 4,194,068</b>	<b>\$ 6,626,965</b>	<b>\$ 8,129,417</b>	<b>\$ 6,910,589</b>

The accompanying notes are an integral part of these statements.

# United States Pharmacopeial Convention and Subsidiaries

Notes to Consolidated Financial Statements—Continued

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June 30, 2009, 2008, 2007, 2006 and 2005

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## NOTE A—ORGANIZATION AND SIGNIFICANT ACCOUNTING POLICES

### *Organization*

The United States Pharmacopeial Convention (USPC), established in 1820, is a not-for profit organization whose purpose is to promote the public health by establishing and disseminating officially recognized standards of quality and authoritative information for the use of medicines and health care technologies by health care professionals, patients and consumers. Initially founded to ensure that consumers receive medicines of the highest possible quality, strength, and purity in the United States, today's Pharmacopeia provides standards for more than 4,200 drugs and dosage forms for medicines and dietary supplements. USPC's standards-setting role also has grown to include development of authoritative information on the use of medicines and dietary supplements, as well as reporting and prevention programs regarding product problems and medication errors, which seek to reduce such occurrences and benefit consumers nationwide.

On May 27, 2005, USPC formed United States Pharmacopeia – India Private Limited (USP India), a private company held under India law through two intermediate holding companies.

On June 13, 2006, USPC formed a new wholly owned subsidiary in China called United States Pharmacopeia Research and Development (Shanghai) Corporation Limited (USP China). USP China began operations during 2007.

On September 21, 2007, USPC formed a new wholly owned subsidiary in Brazil called United States Farmacopeia Brasil Ltda (USP Brazil) located in Sao Paulo, Brazil. As of June 30, 2009, this subsidiary is in full operation.

USP India, USP China, and USP Brazil are wholly owned subsidiaries of USP Holding and USP Holding International, disregarded entities for federal income tax purposes of USPC.

On August 23, 2006, USPC entered into a definitive purchase agreement with the National Academy of Sciences(NAS) for the purchase of the Food Chemicals Codex (FCC), including full and complete ownership of NAS work including copyrights to ensure USP's world-wide exclusive right to manufacture, print, publish, sell, and distribute the FCC beginning with the Sixth Edition. USPC also received all rights and interest in the publication name including any trademarks or service marks beginning with the Sixth Edition.

On November 20, 2007, USPC entered into a strategic, sales, product management, and support agreement with Quantros, Inc. where Quantros would provide the product management, operational, support, marketing and sales responsibilities for the USPC MEDMARX program for all MEDMARX customers under the terms and conditions of the agreement. The term of the agreement will be five years with an option to renew the agreement for a subsequent five year period. Under this agreement, USPC will receive royalties on all MEDMARX product renewals and all new sales of the MEDMARX product. In addition, USPC will receive a referral fee on all Quantros customers who convert to their own SRM product from the MEDMARX product. USPC will pay Quantros a one-time service fee equal to 25 percent of USPC's deferred revenue associated with MEDMARX customers at closing.

# United States Pharmacopeial Convention and Subsidiaries

Notes to Consolidated Financial Statements—Continued

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*June 30, 2009, 2008, 2007, 2006 and 2005*

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## NOTE A— ORGANIZATION AND SIGNIFICANT ACCOUNTING POLICES—Continued

### *Principles of Consolidation*

The consolidated financial statements include the accounts of USPC and USP India, USP China, and USP Brazil (collectively “USPC”). All significant inter-company transactions have been eliminated.

### *Basis of Presentation*

The accompanying consolidated financial statements have been prepared on the accrual basis of accounting.

### *Cash and Cash Equivalents*

For financial statement purposes, USPC considers highly liquid debt instruments with a maturity of three months or less when purchased, except for amounts held in investment brokerage accounts, to be cash equivalents. USPC maintains cash balances, which may exceed Federally insured limits. USPC feels that their exposure to this credit risk is limited.

### *Inventory*

USPC maintains an inventory of finished reference standards, publications, and bulk raw materials. Most bulk raw materials are contributed to USPC. Contributed reference standards are valued at an average price for bulk inventory, and are determined on a moving average method. Inventories of publications are valued at the lower of cost or market using a moving average method.

### *Contributions*

USPC records contributions in accordance with SFAS No. 116, *Accounting for Contributions Received and Contributions Made*. Contributions of services are recognized by USPC if the services received require specialized skills, are provided by individuals possessing those skills and would typically need to be purchased if not provided by donation. Contributions of materials are recognized as revenues and gains in the period received and as assets, decreases of liabilities, or expenses depending on the form of benefits received. Contributions received are measured at their estimated fair value and are reported as unrestricted support based on the absence of donor imposed restrictions.

# United States Pharmacopeial Convention and Subsidiaries

Notes to Consolidated Financial Statements—Continued

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June 30, 2009, 2008, 2007, 2006 and 2005

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## NOTE A— ORGANIZATION AND SIGNIFICANT ACCOUNTING POLICES—Continued

### *Investments*

USPC reports investments in accordance with SFAS No. 124, *Accounting for Certain Investments Held by Not-for-Profit Organizations*. Investments in equity securities with readily determinable fair values and all investments in debt securities are reported at fair value based upon market prices with gains and losses included in the statements of activities, unless their use is temporarily or permanently restricted by explicit donor stipulations or by law. The alternative investments, which are not readily marketable, are carried at estimated fair values as provided by the investment managers. USPC reviews and evaluates the values provided by the investment managers and agrees with the valuation methods and assumptions used in determining the fair value of the alternative investments. Those estimated fair values may differ significantly from the values that would have been used had a ready market for these securities existed.

### *Property and Equipment*

Property and equipment includes items exceeding \$2,500 and are stated at cost. Depreciation and amortization is computed using the straight-line method over the estimated useful lives of the assets of three to fifty years.

### *Debt Financing Costs*

On November 1, 2008 USPC refinanced the Maryland Economic Development Corporation (MEDCO) 2004 and 2006 series bonds with MEDCO Series 2008 Bonds A and B. In fiscal year 2009 USPC incurred debt financing costs of \$987,322. The costs were incurred for legal, underwriter, advisory and other fees associated with the debt incurred under the MEDCO 2008 Bond Series A and B issuance. The debt financing costs are being amortized over the 30 year life of the debt using the interest method. Amortization for the year ending June 30, 2009 was \$29,943.

On November 19, 2008 USPC entered into an Interest Rate Cap agreement in conjunction with the issuance of the MEDCO 2008 Bond Series A and B. The Interest Rate Cap limits the effective interest rate that can be assessed against the MEDCO 2008 Bond Series A and B to a maximum of 5%. The Interest Rate Cap issuance costs of \$1,438,000 will be amortized over five years. Amortization for the year ending June 30, 2009 was \$167,767.

### *Derivative Instruments*

On December 11, 2003, USPC entered into an interest rate swap agreement that is a derivative financial instrument and is accounted for in accordance with Statement of Financial Accounting Standards No. 133, *Accounting for Derivative Instruments and Hedging Activities* (SFAS No. 133). USPC's objective in entering into the interest rate swap agreement, which became effective September 1, 2004, was to, effectively, convert its variable interest rate debt under the Maryland Economic Development Corporation Multi-Modal Revenue Bonds to a fixed rate. The instrument issued is designated as a fair value hedge with a notional amount that mirrors the principal amount of the debt over its 30 year life.

On November 18, 2008 the Interest Rate Swap Agreement was terminated between USPC and Ambac Financial Services, LLC. At termination the outstanding fair market value of the Swap Agreement was \$13,850,000. USPC refinanced the outstanding fair market value with a five year taxable loan.

# United States Pharmacopeial Convention and Subsidiaries

Notes to Consolidated Financial Statements—Continued

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June 30, 2009, 2008, 2007, 2006 and 2005

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## NOTE A— ORGANIZATION AND SIGNIFICANT ACCOUNTING POLICES—Continued

### *Derivative Instruments - Continued*

In November 2008, USPC entered into two interest rate cap agreements that are derivative financial instruments. The instruments each have a notional amount of \$49,325,000 at a rate of 5%. The agreements are scheduled to expire December 2013. The fair value of the instruments was \$789,712 at June 30, 2009 and is included in other assets in the statement of financial position.

### *Accounts Receivable*

The face amount of accounts receivable is reduced by an allowance for doubtful accounts. The allowance for doubtful accounts reflects the best estimate of probable losses determined principally on the basis of historical experience, specific allowances for known troubled accounts, and future business trends for USPC.

### *Revenue Recognition*

Revenue from the sale of publications and their related supplements is recognized as income during the fiscal year in which the publications or supplements are distributed. Subscriptions for print products are sold on an annual basis. Recognition of revenue occurs in the month in which the products are distributed. Revenue from on-line subscription products is recognized uniformly over the subscription period.

Revenue from conference and meetings is recognized as income in the year when the conference or meeting takes place.

Revenue from cost-type contracts is recognized as costs are incurred on the basis of direct costs plus allowable indirect costs.

Revenue recognized on contracts for which billings have not been presented to customers at year-end is reflected in the accounts receivable – cooperative agreements classification on the statement of financial position.

Revenue from fixed-price contracts is recognized under the percentage-of-completion method of accounting, with costs and estimated profits included in contract revenue as work is performed. If actual and estimated costs to complete a contract indicate a loss, provision is made currently for the anticipated loss on the contract.

Revenue from advance royalties is recognized as income on a monthly basis according to the terms specified in the contract.

### *Allocation of Expenses*

USPC is organized into departmental cost centers. Each department's expenses are allocated directly and indirectly to the public health programs supported by USPC.

# United States Pharmacopeial Convention and Subsidiaries

Notes to Consolidated Financial Statements—Continued

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June 30, 2009, 2008, 2007, 2006 and 2005

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## NOTE A— ORGANIZATION AND SIGNIFICANT ACCOUNTING POLICES—Continued

### *Income Taxes*

USPC is exempt from Federal income taxes under the provisions of Section 501(c)(3) of the Internal Revenue Code. USPC is, however, subject to tax on its unrelated business income. For the years, ended June 30, 2009, 2008, 2007, 2006, and 2005 there was no provision for income taxes since USPC had no unrelated business activities. In addition, USPC's wholly owned subsidiaries, USP India, USP Brazil, and USP China, are subject to local country taxes per India, Brazil and China tax regulations.

### *Convention*

USPC holds a convention of its membership every five years to adopt resolutions, and elect a Council of Experts and Board of Trustees. The next meeting is expected to occur in March 2010. The cost of the meeting, currently estimated at \$1.5 million, is accrued ratably over each five-year period. Such accrual in advance of actually incurring costs associated with the meeting or the conduct of the meeting is not in accordance with generally accepted accounting principles. However, management believes that the ratable accrual prevents the erratic impact of cost recognition every five years in its financial statements, is more meaningful to its financial statement users and, on an annual basis, is not material to its financial statements. The total amount accrued as of June 30, 2009, 2008, 2007, 2006 and 2005 was \$1,278,162, \$ 975,000, \$ 675,000, \$375,000 and \$75,000, respectively.

### *Management Estimates*

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

### *Foreign Currency Translation*

The consolidated financial statements and transactions of USPC's foreign subsidiaries are generally maintained in the relevant local currency. Where local currencies are used, assets and liabilities are translated at current exchange rates in effect at the date on the consolidated statement of financial position. Revenue and expenses are translated at the average exchange rate for each period. Gains and losses from foreign currency transactions are included in change in net assets.

### *Advertising*

Advertising costs are charged to marketing expense when incurred. Advertising expense for 2009, 2008, 2007, 2006 and 2005 was \$22,764, \$120,303, \$274,737, \$265,076 and \$267,435, respectively.

# United States Pharmacopeial Convention and Subsidiaries

## Notes to Consolidated Financial Statements—Continued

June 30, 2009, 2008, 2007, 2006 and 2005

### NOTE B—ACCOUNTS RECEIVABLE— COOPERATIVE AGREEMENTS AND GRANTS

The Accounts receivable - cooperative agreements and grants consist of unbilled recoverable amounts under contracts in progress with U.S. Government units and non-federal organizations. At June 30, 2009, 2008, 2007, 2006 and 2005, the components of accounts receivable - cooperative agreements and grants by customers were as follows:

June 30,	2009	2008	2007	2006	2005
Unbilled receivable:					
U.S. Agency for International Development	\$ 291,800	\$ 361,441	\$ 889,642	\$ 994,388	\$ 801,309
Centers for Medicare and Medicaid Services	—	—	151,036	23,004	—
Booz Allen Hamilton	—	—	—	4,220	—
Management Sciences for Health	106,032	—	—	—	—
PSI (Population Services International)	23,698	45,902	—	—	—
World Health Organization	54,100	—	—	—	—
DHHS Agency for Healthcare Research and Quality	—	—	49,000	—	—
UNC Center for Education and Research On Therapeutics	—	—	—	—	18,010
Total cooperative agreements and grants Receivable	\$475,630	\$407,343	\$1,089,678	\$1,021,612	\$ 819,319

For the years ended June 30, 2009, 2008, 2007, 2006 and 2005, USP recognized revenue from U.S. government agencies of \$4,034,226, \$4,452,282, \$4,193,797, \$3,232,185 and \$3,307,271, respectively, of which revenue recognized from the U.S. Agency for International Development contracts was \$4,034,226, \$4,153,318, \$3,731,423, \$3,068,461 and \$2,527,479, respectively.

### NOTE C—INVENTORY

At June 30, 2009, 2008, 2007, 2006 and 2005, inventory consisted of the following:

June 30,	2009	2008	2007	2006	2005
Reference standards					
Finished goods	\$ 34,478,782	\$ 25,776,825	\$ 21,725,144	\$ 18,362,049	\$ 14,301,959
Work in process	3,888,491	3,677,117	619,739	1,188,805	1,612,750
Raw material	38,928,486	43,103,814	29,514,723	25,339,349	26,895,779
Reserve	(11,574,227)	(2,208,834)	(10,145)	(1,018,958)	—
Publications					
Finished goods	1,026,877	378,077	297,285	304,919	181,610
Total	\$ 66,748,409	\$ 70,726,999	\$ 52,146,746	\$ 44,176,164	\$ 42,992,098

## United States Pharmacopeial Convention and Subsidiaries

Notes to Consolidated Financial Statements—Continued

June 30, 2009, 2008, 2007, 2006 and 2005

### NOTE C—INVENTORY—Continued

USPC, through research, experimentations and other proper methods, develops officially recognized reference standards. Once it is established that such materials' identity, strength, and purity may be accurately determined, USPC sells the reference standards along with publications revealing such formulas and results. Materials for use in establishing reference standards are either purchased by USPC or contributed by pharmaceutical manufacturers. Purchased inventories are recorded at cost. Approximately 84% of inventory value is contributed. Contributed reference standards materials are valued at the estimated market value at receipt. For the years ended June 30, 2009, 2008, 2007, 2006 and 2005, USP recognized revenue in contributed reference standard materials of \$52,825,043, \$57,600,969, \$11,772,541, \$8,912,384 and \$12,116,668, respectively.

USPC has established a formal inventory reserve for slow moving finished goods inventory. The replacement of inventory may take considerable time and due to technical requirements, USPC may package product to last for a period of seven years so it is important that these long lead times to replenish stock are maintained. It was deemed this reserve would exclude any product that was in its first two years of release for sale. In addition, given that the inventory for reference materials must be maintained when there is a monograph need, it was determined that a seven year target inventory level is appropriate, based on sales levels. This reserve will be reviewed routinely and adjusted based on sales and inventory levels.

### NOTE D— INVESTMENTS

At June 30, 2006 and 2005, USP's investments, by type, consisted of the following:

June 30,	2009		2008		2007	
	Cost	Market	Cost	Market	Cost	Market
Money market	\$6,362,840	\$6,362,840	\$1,934,373	\$1,934,725	\$2,435,176	\$2,435,176
Corporate bonds	26,373,234	24,177,687	20,335,601	19,060,077	20,691,180	19,779,406
International bonds	651,034	638,485	188,114	181,924	188,114	184,311
Equity funds	18,950,966	17,391,978	32,294,695	34,480,516	38,710,629	48,898,803
Govt. obligations	6,504,568	6,625,837	5,293,558	5,326,747	5,848,929	5,745,326
Mortgage-backed securities	1,904,896	1,805,402	6,433,089	6,715,040	6,846,398	6,797,527
Alternative investments	7,920,000	6,501,164	7,920,000	7,920,000	—	—
Vanguard 457(b) plan	—	315,948	—	230,806	—	—
	<u>\$68,667,538</u>	<u>\$63,819,341</u>	<u>\$74,399,430</u>	<u>\$75,849,835</u>	<u>\$74,720,426</u>	<u>\$83,840,549</u>

## United States Pharmacopeial Convention and Subsidiaries

Notes to Consolidated Financial Statements—Continued

*June 30, 2009, 2008, 2007, 2006 and 2005*

### NOTE D— INVESTMENTS—Continued

June 30,	2006		2005	
	Cost	Market	Cost	Market
Money market	1,788,766	1,788,766	2,305,720	2,305,720
Corporate bonds	16,415,493	15,732,841	14,575,435	14,729,217
International bonds	103,730	101,464	271,877	265,985
Equity funds	37,272,185	42,122,028	34,985,068	35,890,687
Govt. obligations	4,117,030	4,008,307	3,489,344	3,848,870
Mortgage-backed securities	6,381,794	6,230,889	7,087,536	6,989,289
	66,078,998	69,984,295	62,714,980	64,029,768

Investment income is comprised of the following for the years ended June 30:

June 30,	2009	2008	2007	2006	2005
Interest and dividend income	\$ 2,345,862	\$ 2,830,782	\$ 2,594,834	\$ 1,816,989	\$ 1,811,840
Net realized and unrealized gains and losses	(14,180,523)	(4,994,019)	8,917,229	4,663,595	1,801,112
Investment expenses	(293,336)	(467,144)	(427,246)	(362,836)	(225,458)
Total investment income	\$ (12,127,997)	\$ (2,630,381)	\$ 11,084,817	\$ 6,117,748	\$ 3,387,494

# United States Pharmacopeial Convention and Subsidiaries

Notes to Consolidated Financial Statements—Continued

*June 30, 2009, 2008, 2007, 2006 and 2005*

## NOTE E—PROPERTY AND EQUIPMENT

USP property and equipment at June 30, 2009, 2008, 2007, 2006 and 2005 consists of:

<i>June 30,</i>	<b>2009</b>		
	<b>Cost</b>	<b>Accumulated Depreciation</b>	<b>Net</b>
Land	\$ 1,086,609	\$ —	\$ 1,086,609
Buildings and improvements	109,500,360	(14,701,667)	94,798,693
Furniture and equipment	21,622,244	(10,911,857)	10,710,387
Computer hardware and software	15,253,766	(12,899,816)	2,353,950
Construction in progress – Twinbrook Land	2,857,884	—	2,857,884
Total	\$ 150,320,863	\$ (38,513,340)	\$ 111,807,523
<i>June 30,</i>	<b>2008</b>		
	<b>Cost</b>	<b>Accumulated Depreciation</b>	<b>Net</b>
Land	\$ 1,086,609	\$ —	\$ 1,086,609
Buildings and improvements	107,187,220	(11,124,923)	96,062,297
Furniture and equipment	27,954,486	(11,010,476)	16,944,010
Computer hardware and software	18,506,258	(15,531,949)	2,974,309
Construction in progress – Twinbrook Land	1,090,053	—	1,090,053
Total	\$ 155,824,626	\$ (37,667,348)	\$ 118,157,278
<i>June 30,</i>	<b>2007</b>		
	<b>Cost</b>	<b>Accumulated Depreciation</b>	<b>Net</b>
Land	\$ 1,086,609	\$ —	\$ 1,086,609
Buildings and improvements	20,718,462	(8,539,884)	12,178,578
Furniture and equipment	16,635,083	(8,955,080)	7,680,003
Computer hardware and software	17,972,408	(12,985,431)	4,986,977
Total	\$ 56,412,562	\$ (30,480,395)	\$ 25,932,167

## United States Pharmacopeial Convention and Subsidiaries

Notes to Consolidated Financial Statements—Continued

*June 30, 2009, 2008, 2007, 2006 and 2005*

### NOTE E—PROPERTY AND EQUIPMENT—Continued

<i>June 30,</i>	<b>2006</b>		
	<b>Cost</b>	<b>Accumulated Depreciation</b>	<b>Net</b>
Land	\$ 1,086,609	\$ —	\$ 1,086,609
Buildings and improvements	19,849,647	(7,732,337)	12,117,311
Furniture and equipment	13,278,316	(7,865,195)	5,413,121
Computer hardware and software	15,838,924	(9,999,172)	5,839,752
Total	\$ 50,053,496	\$ (25,596,704)	\$ 24,456,793
 <i>June 30,</i>	<b>2005</b>		
	<b>Cost</b>	<b>Accumulated Depreciation</b>	<b>Net</b>
Land	\$ 1,086,609	\$ —	\$ 1,086,609
Buildings and improvements	19,540,347	(7,142,049)	12,398,298
Furniture and equipment	11,823,024	(8,231,585)	3,591,439
Computer hardware and software	13,392,633	(7,518,634)	5,873,999
Total	\$ 45,842,613	\$ (22,892,268)	\$ 22,950,345

## United States Pharmacopeial Convention and Subsidiaries

Notes to Consolidated Financial Statements—Continued

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*June 30, 2009, 2008, 2007, 2006 and 2005*

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### NOTE F—LONG-TERM DEBT

On November 30, 2008, USPC issued \$98,650,000 under the Maryland Economic Development Corporation (MEDCO) Series 2008 Note Series 2008A and B bonds. Proceeds of the borrowing was used to refinance the \$87,495,000 under Series 2004 Note Series 2004A and B, \$10,100,000 Series 2006 Note from MEDCO, and issuance costs of \$1,055,000. The note is collateralized by a springing mortgage on the real estate and a security interest in all of USPC's receipts derived from its ownership, operation, or leasing of the facilities. The agreement provides that effective December 31, 2008, USPC must meet specific financial covenants, the most significant of which are:

- a. Maintain a Debt Service Coverage of 1.10 to 1
- b. Maintain a Liquidity Coverage of .45 to 1

Total interest incurred on the 2008 Bond Payable for the year ending June 30, 2009 was \$2,783,988. The bond carries a variable interest rate not to exceed 5%. The interest rate will be determined by the Remarketing Agent as the lowest rate of interest which would result in the bond's market value equal to principal plus accrued interest taking into account prevailing market conditions. The bond requires interest only payments through June 30, 2013 with scheduled annual principal payments commencing July 1, 2014. Final payment on the note is due July 1, 2038.

On November 1, 2008 USPC borrowed \$15,000,000 under a Term Loan Agreement with Bank of America, N.A. The proceeds of the loan were used to refinance the fair market value at the time of termination of the Interest Rate Swap (\$13,850,000) and Interest Rate Cap premiums (\$1,438,000). The Term Loan carries a variable interest rate of LIBOR plus 1.60%. The note has scheduled annual principal payments commencing on July 1, 2009 with the final payment due July 1, 2013. Total interest incurred as of June 30, 2009 was \$214,602.

In May 2008, USP entered into a Term Loan with Bank of America in the amount of \$1,100,000 that represents the initial amount for the purchase of adjacent two acres of land that is next door to USPC's new building located in Rockville. In 2009, the term loan was increased to \$2,547,158. This term loan will be used to finance the initial land deposit, related due diligence, and legal costs. The amount outstanding at June 30, 2009 is \$2,547,158 and the interest rate charged is LIBOR plus 0.5%.

There are covenant requirements associated with these loans which USPC was in compliance with as of June 30, 2009.

## United States Pharmacopeial Convention and Subsidiaries

Notes to Consolidated Financial Statements—Continued

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*June 30, 2009, 2008, 2007, 2006 and 2005*

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### NOTE F—LONG-TERM DEBT-Continued

Minimum future maturities and sinking fund requirements under long-term debt are as follows:

<i>Year ending June 30,</i>	<b>Principal Amount</b>
2010	\$ 6,377,158
2011	3,065,000
2012	3,215,000
2013	3,365,000
2014	3,525,000
Thereafter	<u>98,650,000</u>
Total	<u>\$ 118,197,158</u>

In September 2009, USPC settled on the purchase of land adjacent to its Rockville headquarters for a purchase price of \$9,250,000. The purchase was financed through a term loan for up to \$10,600,000 which is expected to be repaid from the issuance of a Maryland Economic Development Organization three year bank qualified tax exempt bond to finance construction of a building extension. The term loan will bear interest at a floating rate of the 30 day LIBOR rate plus 0.5% and will require interest only payments with the principal due at maturity. The maturity date of the loan is the earlier of the closing of the associated tax exempt bonds or five years from the date of issuance. The tax exempt bond is expected to have a fixed rate of interest of 2.27%.

# United States Pharmacopeial Convention and Subsidiaries

Notes to Consolidated Financial Statements—Continued

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*June 30, 2009, 2008, 2007, 2006 and 2005*

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## NOTE G— COMMITMENTS AND CONTINGENCIES

### *Leases*

In May 2004, USPC entered into a non-cancelable operating lease for warehouse space in Rockville, Maryland for a term of approximately ten years with two options of five years each. Rent payments are based on a beginning annual value of \$64,715 increased annually by multiplying the effective minimum rent by one and three hundredths (1.03). USPC is also responsible for a proportionate share of the operating costs of the building and real property taxes. USPC received twenty-two months of discounted rent under the lease. Minimum rent payments required under the lease are recognized as rent expense on the straight-line basis over the term of the lease.

In July 2004, USPC entered into a non-cancelable operating lease for temporary office space in Rockville, Maryland for a term of twenty-six months. This lease was amended in March 2006 to extend the lease term to thirty-three months and add to this lease additional office space that was formerly subleased. In September 2007, this lease was amended for the third time to reduce the size of the original premises, extend the term of the lease, and amend certain other terms and conditions. This amendment brought leased premises down to only 13,742 square feet with the base rent approximately \$36,000 per month. The term of this third amendment is for a period of five years expiring on September 30, 2012.

In October 2005, USP Holding entered into an operating lease for office space in Basel, Switzerland. The lessor has been notified of USPC's intention to renew the lease for an additional term of five years. The renewal option expires in September 2015. Rent payments are approximately \$2,342 per month for the life of the lease.

In December 2005, USP India entered into an operating lease for office and lab space in Hyderabad, India for a term of three years. Rent payments are approximately \$17,200 per month. The lease was renewed in 2009 for an additional three years, dating back to the original termination date of November 2008. The renewed lease will terminate in November 2011.

In June 2008, USP India entered into a cancelable operating lease agreement with ICICI Knowledge Park for 4.17 acres of land for future site expansion. This lease agreement is for a period of 33 years and is renewable for another 18 years. All sums paid are being expensed out over the term of the lease.

In April 2006, USP Holding entered into an operating lease for office and lab space in Shanghai, China for a term of three years. In April 2009, this lease was renewed for three years, expiring in March 2012. Rent payments are approximately \$8,170 per month for the life of the lease (based on 1,025 square meters of total floor area leased). USP Holding may terminate the lease at any time by giving at least three months of notice and also paying liquidation damages equal to three month's rent.

In October 2007, USP Brazil entered into a non-cancelable lease for laboratory and office space in Sao Paulo (Alphaville), Brazil. The lease is for a term of five years and will terminate in September 2012. Monthly lease payments are approximately \$26,000 and can be adjusted annually according to the monthly percentage variance of the IPCA-IBGE rate in Brazil every October. The company may terminate the lease with at least sixty days written notice and with paying liquidated damages equal to three months rent.

Rent expense for the years ended June 30, 2009, 2008, 2007, 2006 and 2005 was \$1,230,513, \$1,912,520, \$2,105,622, \$1,843,881 and \$1,405,641 respectively.

# United States Pharmacopeial Convention and Subsidiaries

Notes to Consolidated Financial Statements—Continued

June 30, 2009, 2008, 2007, 2006 and 2005

## NOTE G—COMMITMENTS AND CONTINGENCIES—Continued

### *Leases—Continued*

Minimum future rental payments under these non-cancelable leases are as follows:

<i>Year ending June 30,</i>	<b>Amount</b>
2010	\$ 1,176,460
2011	1,231,347
2012	1,118,961
2013	323,044
2014	149,004
Thereafter	40,346
Total	<u>\$ 4,039,162</u>

### *Health and Retirement Plans*

USPC sponsors a defined contribution plan that covers substantially all US based employees of USP. These employees are eligible for the plan after working for at least 1000 hours in a plan year, completing one year of service and attaining age twenty-one. USPC contributes an amount equal to 10 percent of each employee's compensation of such plan year. USPC pension expense for the years ended June 30, 2009, 2008, 2007, 2006 and 2005 was \$3,859,572, \$3,494,482, \$2,744,550, \$2,488,371 and \$2,248,196, respectively.

USPC established a deferred compensation plan on July 1, 2007 in accordance with the requirements under the Internal Revenue Code Section 457(b). Participation in the plan is limited to employees who hold positions of Vice President or higher. Participants may contribute the lesser of 100% of compensation or the maximum dollar amount permitted of \$ 16,500 for 2009, as well as an additional \$5,500 if participants over age 50. Participants are fully vested in the Plan upon entry. For the years ending June 30, 2009 and 2008, the market value was \$315,948 and \$230,806 respectively.

USPC's U.S. group health benefits are self-insured for claims up to \$150,000, per participant per plan year. USPC carries stop-loss coverage for claims in excess of \$150,000 per participant, per plan year, and also aggregate stop loss for multiple claims in excess of 125% of expected total claims in a plan year.

### *Line of Credit*

On August 25, 2004, USPC entered into a revolving line of credit with its bank in the amount of \$5,000,000 for temporary seasonal cash flow needs. Under the terms of this agreement, interest is payable at LIBOR plus .5 percent on a monthly basis. During June 2008, this promissory note was amended to increase the revolving credit line from the \$5,000,000 up to \$10,000,000. The interest rate continues at LIBOR plus 0.5 percent. At June 30, 2009, USP had an outstanding balance of \$ 2,000,000 on this revolving line of credit.

This new line of credit has a cleanup period where for a period of 30 consecutive days during any fiscal year, USPC must fully pay down the balance of this line so that no principal or interest is outstanding.

# United States Pharmacopeial Convention and Subsidiaries

Notes to Consolidated Financial Statements—Continued

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June 30, 2009, 2008, 2007, 2006 and 2005

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## NOTE H—CONTRIBUTING SERVICES

The utilization of volunteers is fundamental to USP's mission and Product development. These volunteers are composed of health care practitioners, academicians, and other professionals. The value of these volunteer services has been computed by multiplying the average number of hours per volunteer with the number of volunteers and a rate per hour equal to that of a qualified employee who would have been paid for their services.

June 30,	2009	2008	2007	2006	2005
Value of Contributed Services	\$ 11,397,040	\$ 10,909,721	\$ 8,957,073	\$7,002,805	\$6,908,309
Number of Contributing Volunteers	717	720	710	538	664

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## NOTE I—SUBSEQUENT EVENT

In May 2009, the Financial Accounting Standards Board issued Statement 165, *Subsequent Events*, to incorporate the accounting and disclosure requirements for subsequent events into U.S. generally accepted accounting principles. Statement 165 introduces new terminology, defines a date through which management must evaluate subsequent events, and lists the circumstances under which an entity must recognize and disclose events or transactions occurring after the statement of financial position date. USPC adopted Statement 165 as of June 30, 2009, which was the required effective date.

USPC evaluated its June 30, 2009 financial statements for subsequent events through November 12, 2009, the date the financial statements were available to be issued. Other than the event noted below, USPC is not aware of any subsequent events which would require recognition or disclosure in the financial statements.

As disclosed in Note F, on September 16, 2009, USPC settled on the purchase of two acres of land adjacent to its Rockville headquarters for a purchase price of \$9,250,000. The purchase was financed through a term loan for up to \$10,600,000.