SCHERING PLOUGH CORP
Form 10-Q
October 29, 2009

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

Form 10-Q

þ **QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**
For the quarterly period ended September 30, 2009

Commission file number 1-6571

SCHERING-PLOUGH CORPORATION
(Exact name of registrant as specified in its charter)

New Jersey	**22-1918501**
State or other jurisdiction of incorporation or organization	*(I.R.S. Employer identification No.)*
2000 Galloping Hill Road, Kenilworth, NJ	**07033**
(Address of principal executive offices)	*Zip Code*

Registrant s telephone number, including area code:
(908) 298-4000

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 þ No o

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes þ 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 þ Accelerated filer o Non-accelerated filer o Smaller reporting company o
(Do not check if a smaller reporting company)

Indicate whether the registrant is a shell company (as defined in Rule 12b-2 of the Act). Yes o No þ

Common Shares Outstanding as of September 30, 2009: 1,639,151,392

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Item 1. ***Financial Statements***

SCHERING-PLOUGH CORPORATION AND SUBSIDIARIES

STATEMENTS OF CONDENSED CONSOLIDATED OPERATIONS

(Unaudited)
(Amounts in millions, except per share figures)

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2009	**2008**	**2009**	**2008**
Net sales	$ 4,499	$ 4,576	$ 13,539	$ 14,154
Cost of sales	1,719	1,737	4,738	5,782
Selling, general and administrative	1,511	1,660	4,629	5,208
Research and development	913	893	2,580	2,679
Other expense/(income), net	102	(39)	297	189
Special, merger and acquisition-related charges	29	101	133	218
Equity income	(387)	(434)	(1,157)	(1,444)
Income before income taxes	612	658	2,319	1,522
Income tax expense	97	44	328	133
Net income	515	614	1,991	1,389
Preferred stock dividends	38	38	113	113
Net income available to common shareholders	$ 477	$ 576	$ 1,878	$ 1,276
Diluted earnings per common share	$ 0.29	$ 0.35	$ 1.13	$ 0.78
Basic earnings per common share	$ 0.29	$ 0.35	$ 1.14	$ 0.78
Dividends per common share	$ 0.065	$ 0.065	$ 0.195	$ 0.195

The accompanying notes are an integral part of these Condensed Consolidated Financial Statements.

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SCHERING-PLOUGH CORPORATION AND SUBSIDIARIES

STATEMENTS OF CONDENSED CONSOLIDATED CASH FLOWS

(Unaudited)
(Amounts in millions)

	Nine Months Ended September 30,	
	2009	**2008**
Operating Activities:		
Net income	$ 1,991	$ 1,389
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	929	1,813
Accrued share-based compensation	135	170
Special, merger and acquisition-related charges and payments	(54)	115
Gain on sale of divested products		(160)
Changes in assets and liabilities:		
Accounts receivable	(179)	(132)
Inventories	(129)	(135)
Prepaid expenses and other assets	120	(22)
Accounts payable	28	16
Other liabilities	(217)	(479)
Net cash provided by operating activities	2,624	2,575
Investing Activities:		
Capital expenditures	(522)	(542)
Dispositions of property and equipment	48	33
Contributions to benefit-related trusts	(367)	
Proceeds from divested products, net	23	241
Purchases of short-term investments	(2,035)	
Maturities of short-term investments	1,554	27
Other, net	(10)	(3)
Net cash used for investing activities	(1,309)	(244)
Financing Activities:		
Payments of long-term debt	(71)	(791)
Cash dividends paid to common shareholders	(318)	(317)
Cash dividends paid to preferred shareholders	(113)	(113)
Net change in short-term borrowings	(122)	(207)
Stock option exercises	167	15
Other, net		(3)
Net cash used for financing activities	(457)	(1,416)

Effect of exchange rates on cash and cash equivalents	81	(35)
Net increase in cash and cash equivalents	939	880
Cash and cash equivalents, beginning of period	3,373	2,279
Cash and cash equivalents, end of period	$ 4,312	$ 3,159

The accompanying notes are an integral part of these Condensed Consolidated Financial Statements.

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SCHERING-PLOUGH CORPORATION AND SUBSIDIARIES

CONDENSED CONSOLIDATED BALANCE SHEETS

(Unaudited)
(Amounts in millions, except per share figures)

	September 30, 2009	December 31, 2008
ASSETS		
Current Assets:		
Cash and cash equivalents	$ 4,312	$ 3,373
Short-term investments	487	5
Accounts receivable, net	3,127	2,816
Inventories	3,459	3,114
Deferred income taxes	578	435
Prepaid expenses and other current assets	1,203	1,228
Total current assets	13,166	10,971
Property, plant and equipment	11,012	10,440
Less accumulated depreciation	4,088	3,607
Property, net	6,924	6,833
Goodwill	2,879	2,778
Other intangible assets, net	5,981	6,154
Other assets	1,597	1,381
Total assets	$ 30,547	$ 28,117
LIABILITIES AND SHAREHOLDERS EQUITY		
Current Liabilities:		
Accounts payable	$ 1,709	$ 1,677
Short-term borrowings and current portion of long-term debt	185	245
Income taxes	232	183
Accrued compensation	967	1,010
Other accrued liabilities	1,996	2,078
Total current liabilities	5,089	5,193
Long-term Liabilities:		
Long-term debt, net of current portion	8,033	7,931
Deferred income taxes	1,523	1,551
Other long-term liabilities	3,002	2,913
Total long-term liabilities	12,558	12,395
Commitments and contingent liabilities (Note 17)		
Shareholders Equity:		

2007 Mandatory convertible preferred shares $1 par value; $250 per share face value; issued: 10 at September 30, 2009 and December 31, 2008		2,500		2,500
Common shares authorized: 2,400, $.50 par value; issued: 2,132 at September 30, 2009 and 2,118 at December 31, 2008		1,066		1,059
Paid-in capital		5,340		5,045
Retained earnings		10,737		9,181
Accumulated other comprehensive loss		(1,360)		(1,913)
Total		18,283		15,872
Less treasury shares: 493 at September 30, 2009 and 492 at December 31, 2008; at cost		5,383		5,343
Total shareholders equity		12,900		10,529
Total liabilities and shareholders equity	$	30,547	$	28,117

The accompanying notes are an integral part of these Condensed Consolidated Financial Statements.

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SCHERING-PLOUGH CORPORATION AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited)

1. BASIS OF PRESENTATION

These unaudited Condensed Consolidated Financial Statements of Schering-Plough Corporation and subsidiaries (Schering-Plough), have been prepared pursuant to the rules and regulations of the Securities and Exchange Commission (SEC) for reporting on Form 10-Q. Certain information and disclosures normally included in financial statements prepared in accordance with U.S. Generally Accepted Accounting Principles have been condensed or omitted pursuant to such SEC rules and regulations. These statements should be read in conjunction with the accounting policies and notes to the consolidated financial statements included in Schering-Plough s 2008 10-K.

In the opinion of Schering-Plough s management, these financial statements reflect all adjustments necessary, including normal recurring accruals, for a fair presentation of the statements of operations, cash flows and financial position for the interim periods presented.

Third quarter and nine months ended September 30, 2008, income tax expense has been revised from the prior year 10-Q which reflected an overstatement of income tax expense relating to the accounting for the purchase of Organon BioSciences N.V. (OBS). This change resulted in a reduction of income tax expense and a corresponding increase in net income and net income available to common shareholders of $25 million for the third quarter of 2008 and $74 million for the nine months ended September 30, 2008, along with an associated increase in per share amounts.

In November 2007, Schering-Plough acquired OBS, a company that discovers, develops and manufactures human prescription and animal health products.

Schering-Plough has evaluated all subsequent events through October 29, 2009, the date of filing of this 10-Q.

Impact of Recently Issued Accounting Standards

In June 2009, the Financial Accounting Standards Board (FASB) issued guidance which is included in the Codification in FASB Accounting Standards Codification (ASC) 105, Generally Accepted Accounting Principles. This guidance modifies the Generally Accepted Accounting Principles (GAAP) hierarchy by establishing only two levels of GAAP, authoritative and nonauthoritative accounting literature. Effective July 2009, the FASB ASC, also known collectively as the Codification, is considered the single source of authoritative U.S. accounting and reporting standards, except for additional authoritative rules and interpretive releases issued by the SEC. This guidance is effective for financial statements issued for reporting periods that end after September 15, 2009. Where possible, FASB references have been replaced with ASC references.

As of January 1, 2009, Schering-Plough implemented the transition guidance related to FASB Staff Position (FSP) Emerging Issues Task Force (EITF) 03-6-1, Determining Whether Instruments Granted in Share-Based Payment Transactions Are Participating Securities , which is included in the codification in ASC 260-10, Earnings Per Share (ASC 260-10). ASC 260-10 requires Schering-Plough to treat unvested deferred stock units as participating securities in accordance with the two-class method in the calculation of both basic and diluted earnings per share. ASC 260-10 must be applied retrospectively. The effect of the retrospective application of ASC 260-10 was not material to Schering-Plough s earnings per share in 2008, 2007 or 2006.

As of June 30, 2009, Schering-Plough implemented FASB ASC 825-10-65-1, Financial Instruments (ASC 825-10-65-1). ASC 825-10-65-1 provides disclosure about fair value of financial instruments in interim as well as in annual financial statements. This guidance is effective for periods ending after June 15, 2009. In the second quarter of 2009, Schering-Plough implemented this guidance. See Note 13, Financial Instruments.

Effective January 1, 2008, the Company adopted FASB ASC 820-10, Fair Value Measurements and Disclosures (ASC 820-10) with respect to its financial assets and liabilities. In February 2008, the FASB issued updated guidance related to fair value measurements, which is included in the Codification in ASC 820-10, Fair Value Measurements and Disclosures (see Note 14, Fair Value Measurements). The updated guidance provided a one year deferral of the effective date of ASC 820-10 for non-financial assets and non-financial liabilities, except those that are recognized or disclosed in the financial statements at fair value at least annually.

SCHERING-PLOUGH CORPORATION AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

The implementation of the non-financial items measured on a non-recurring basis did not have a material impact on Schering-Plough s condensed consolidated financial statements.

In December 2007, the FASB issued guidance which is included in the Codification in ASC 808, Collaborative Arrangements (ASC 808), which is effective for calendar-year companies beginning January 1, 2009. ASC 808 clarified the manner in which costs, revenues and sharing payments made to, or received by, a partner in a collaborative arrangement should be presented in the income statement and set forth certain disclosures that should be required in the partners financial statements. The implementation of this standard did not have a material impact on Schering-Plough s condensed consolidated financial statements. Schering-Plough has a number of collaborative arrangements. For collaborative arrangements, sales are generally included in Net sales and payments to collaboration partners are classified in the statement of condensed consolidated operations based on their nature in Cost of sales or Research and development, as appropriate.

In December 2007, the FASB issued guidance which is included in the Codification in ASC 805, Business Combination (ASC 805). For calendar-year companies, the standard is applicable to new business combinations occurring on or after January 1, 2009. ASC 805 requires an acquiring entity to recognize all the assets acquired and liabilities assumed in a transaction at the acquisition-date fair value with limited exceptions. Most significantly, ASC 805 requires that acquisition costs generally be expensed as incurred, certain acquired contingent liabilities be recorded at fair value, and acquired in-process research and development be recorded at fair value as an indefinite-lived intangible asset at the acquisition date. The implementation of this standard did not have a material impact on Schering-Plough s condensed consolidated financial statements.

In December 2007, the FASB issued guidance which is included in the Codification in ASC 810-10-65-1, Consolidation (ASC 810-10-65-1), which is effective for calendar-year companies beginning January 1, 2009. This standard revised the accounting treatment for noncontrolling minority interests of partially-owned subsidiaries. The standard establishes new accounting and reporting standards for the noncontrolling interest in a subsidiary and for the deconsolidation of a subsidiary. The implementation of this standard did not have a material impact on Schering-Plough s condensed consolidated financial statements.

In March 2008, the FASB issued issued guidance which is included in the Codification in ASC 815-10, Derivatives and Hedging. This guidance is effective for calendar-year companies beginning January 1, 2009. The guidance enhances required disclosures regarding derivatives and hedging activities. The implementation of this standard did not have a material impact on Schering-Plough s condensed consolidated financial statements.

In April 2008, the FASB issued ASC 350, Intangibles-Goodwill and Other (ASC 350). ASC 350 amends the factors that should be considered in developing renewal or extension assumptions used to determine the useful life of a recognized intangible asset. ASC 350 is effective for calendar-year companies beginning January 1, 2009. The requirement for determining useful lives must be applied prospectively to intangible assets acquired after the effective date and the disclosure requirements must be applied prospectively to all intangible assets recognized as of, and subsequent to, the effective date. The implementation of this standard did not have a material impact on Schering-Plough s condensed consolidated financial statements.

In April 2009, the FASB issued updated guidance related to business combinations, which is included in the Codification in ASC 805-20, Business Combinations Identifiable Assets, Liabilities and Any Noncontrolling Interest

(ASC 805-20). ASC 805-20 amends the provisions in ASC 805 for the initial recognition and measurement, subsequent measurement and accounting, and disclosures for assets and liabilities arising from contingencies in business combinations. ASC 805-20 is effective for contingent assets or contingent liabilities acquired in business combinations for which the acquisition date is on or after the beginning of the first annual reporting period beginning on or after December 15, 2008. The implementation of this standard did not have a material impact on Schering-Plough s condensed consolidated financial statements.

In May 2009, the FASB issued guidance which is included in the Codification in ASC 855, Subsequent Events (ASC 855). This guidance establishes the accounting and disclosure of events that occur after the balance sheet date but before financial statements are issued or are available to be issued. It requires the disclosure of the date through which an entity has evaluated subsequent events and the basis for that date. This guidance is effective for interim or annual financial periods ending after June 15, 2009, and as such, became effective for the

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SCHERING-PLOUGH CORPORATION AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

Company on June 30, 2009. The implementation of this standard did not have a material impact on Schering-Plough s condensed consolidated financial statements.

In June 2009, the FASB issued Statement of Financial Accounting Standards (SFAS) No. 166, Accounting for Transfers of Financial Assets, an amendment of SFAS No. 140 (SFAS 166), which has not yet been codified in the ASC. SFAS 166 amends SFAS No. 140 to improve the relevance, representational faithfulness, and comparability of the information that a reporting entity provides in its financial reports about a transfer of financial assets; the effects of a transfer on its financial position, financial performance, and cash flows; and a transferor s continuing involvement in transferred financial assets. This Statement is effective as of the beginning of each reporting entity s first annual reporting period that begins after November 15, 2009, for interim periods within that first annual reporting period, and for interim and annual reporting periods thereafter. Earlier application is prohibited. The recognition and measurement provisions of this Statement shall be applied to transfers that occur on or after the effective date. Schering-Plough is currently assessing the impact of the adoption of SFAS 166.

In June 2009, the FASB issued SFAS No. 167, Amendments to FASB Interpretation No. 46(R) (SFAS 167), which has not yet been codified in the ASC. SFAS 167 amends certain requirements of FASB Interpretation No. 46 (revised December 2003), Consolidation of Variable Interest Entities, to improve financial reporting by enterprises involved with variable interest entities and to provide more relevant and reliable information to users of financial statements. This Statement is effective as of the beginning of each reporting entity s first annual reporting period that begins after November 15, 2009, for interim periods within that first annual reporting period, and for interim and annual reporting periods thereafter. Earlier application is prohibited. Schering-Plough is currently assessing the impact of the adoption of SFAS 167.

In August 2009, the FASB issued Accounting Standards Update (ASU) No. 2009-05, Fair Value Measurements and Disclosures (Topic 820) (ASU 2009-05). ASU 2009-05 provided amendments to ASC 820-10, Fair Value Measurements and Disclosures Overall, for the fair value measurement of liabilities. ASU 2009-05 provides clarification that in circumstances in which a quoted price in an active market for the identical liability is not available, a reporting entity is required to measure fair value using certain techniques. ASU 2009-05 also clarifies that when estimating the fair value of a liability, a reporting entity is not required to include a separate input or adjustment to other inputs relating to the existence of a restriction that prevents the transfer of a liability. ASU 2009-05 also clarifies that both a quoted price in an active market for the identical liability at the measurement date and the quoted price for the identical liability when traded as an asset in an active market when no adjustments to the quoted price of the asset are required are Level 1 fair value measurements. The new guidance is effective for interim and annual periods beginning after August 27, 2009, and applies to all fair-value measurements of liabilities required by GAAP. Schering-Plough is currently assessing the impact of the adoption of ASU 2009-05.

In October 2009, the FASB issued ASU 2009-13, Multiple-Deliverable Revenue Arrangements, (amendments to FASB ASC Topic 605, Revenue Recognition) (ASU 2009-13). ASU 2009-13 requires entities to allocate revenue in an arrangement using estimated selling prices of the delivered goods and services based on a selling price hierarchy. The amendments eliminate the residual method of revenue allocation and require revenue to be allocated using the relative selling price method. ASU 2009-13 should be applied on a prospective basis for revenue arrangements entered into or materially modified in fiscal years beginning on or after June 15, 2010, with early adoption permitted. Schering-Plough is currently assessing the impact of the adoption of ASU 2009-13.

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SCHERING-PLOUGH CORPORATION AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

2. PRODUCTIVITY TRANSFORMATION PROGRAM

Schering-Plough s Productivity Transformation Program (PTP) is designed to reduce and avoid costs and increase productivity.

The following table summarizes activities reflected in the condensed consolidated financial statements related to the Productivity Transformation Program, for the nine months ended September 30, 2009:

	Charges Included in						
	Cost of Sales	Research and Development	Special, Merger and Acquisition-Related Charges	Total Charges	Cash Payments	Non-cash Charges /(Credits)	Accrued Liability
	(Dollars in millions)						
Accrued liability at January 1, 2009							$ 155
Employee termination costs	$	$	$ 98	$ 98	$ (156)	$	(58)
Asset write-offs	5			5		5	
Inventory write-offs	38			38		38	
Accelerated depreciation	12	2		14		14	
Foreign exchange and other						(4)	(4)
Total	$ 55	$ 2	$ 98	$ 155	$ (156)	$ 53	
Accrued liability at September 30, 2009							$ 93

For the three months ended September 30, 2009, special, merger and acquisition-related costs totaled $29 million, of which $24 million related to employee termination costs and $5 million related to the planned merger with Merck & Co., Inc (Merck). Planned merger costs are not included in the table above. For the nine months ended September 30, 2009, special, merger and acquisition-related costs totaled $133 million, of which $98 million related to employee termination costs and $35 million related to the planned merger with Merck.

The following table summarizes activities reflected in the condensed consolidated financial statements related to the Productivity Transformation Program, for the nine months ended September 30, 2008:

	Special, and Acquisition-Related Charges	Total Charges	Cash Payments	Non-cash Charges	Accrued Liability
			(Dollars in millions)		
Accrued liability at January 1, 2008					$ 174
Employee termination costs	$ 177	$ 177	$ (197)	$ 32	12
Accrued liability at September 30, 2008					$ 186

For the three months ended September 30, 2008, special and acquisition-related charges totaled $101 million ($93 million of employee termination costs and $8 million related to OBS integration activities). For the nine months ended September 30, 2008, special and acquisition-related charges totaled $218 million ($177 million of employee termination costs and $41 million to OBS integration activities).

3. EQUITY INCOME

In May 2000, Schering-Plough and Merck entered into two separate sets of agreements to jointly develop and market certain products in the U.S. including (1) two cholesterol-lowering drugs and (2) an allergy/asthma drug. In December 2001, the cholesterol agreements were expanded to include all countries of the world except Japan. In general, the companies agreed that the collaborative activities under these agreements would operate in a virtual joint venture to the maximum degree possible by relying on the respective infrastructures of the two

SCHERING-PLOUGH CORPORATION AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

companies. These agreements generally provide for equal sharing of development costs and for co-promotion of approved products by each company.

The cholesterol agreements provide for Schering-Plough and Merck to jointly develop and commercialize ezetimibe in the cholesterol management field:

i. as a once-daily monotherapy (managed as ZETIA in the U.S. and Asia and EZETROL in Europe);

ii. in co-administration with various approved statin drugs; and

iii. as a fixed-combination tablet of ezetimibe and simvastatin (Zocor), Merck s cholesterol-modifying medicine. This combination medication (ezetimibe/simvastatin) is managed as VYTORIN in the U.S. and as INEGY in many international countries.

ZETIA/EZETROL (ezetimibe) and VYTORIN/INEGY (the combination of ezetimibe/simvastatin) are approved for use in the U.S. and have been launched in many international markets.

Schering-Plough utilizes the equity method of accounting in recording its share of activity from the Merck/Schering-Plough cholesterol joint venture. As such, Schering-Plough s net sales do not include the sales of the joint venture. The cholesterol joint venture agreements provide for the sharing of operating income generated by the joint venture based upon percentages that vary by product, sales level and country. In the U.S. market, Schering-Plough receives a greater share of profits on the first $300 million of annual ZETIA sales. Above $300 million of annual ZETIA sales, Merck and Schering-Plough generally share profits equally. Schering-Plough s allocation of the joint venture income is increased by milestones recognized. Further, either company s share of the joint venture s income from operations is subject to a reduction if that company fails to perform a specified minimum number of physician details in a particular country. The companies agree annually to the minimum number of physician details by country.

The companies bear the costs of their own general sales forces and commercial overhead in marketing joint venture products around the world. In the U.S., Canada and Puerto Rico, the cholesterol agreements provide for a reimbursement to each company for physician details that are set on an annual basis, and in Italy, a contractual amount is included in the profit sharing calculation that is not reimbursed. In the U.S., Canada and Puerto Rico this amount is equal to each company s agreed physician details multiplied by a contractual fixed fee. Schering-Plough reports these amounts as part of equity income from the cholesterol joint venture. These amounts do not represent a reimbursement of specific, incremental and identifiable costs for Schering- Plough s detailing of the cholesterol products in these markets. In addition, these amounts are not reflective of Schering-Plough s sales effort related to the joint venture as Schering-Plough s sales force and related costs associated with the joint venture are generally estimated to be higher.

Costs of the joint venture that the companies contractually share are a portion of manufacturing costs, specifically identified promotion costs (including direct-to-consumer advertising and direct and identifiable out-of-pocket promotion) and other agreed upon costs for specific services such as market support, market research, market expansion, a specialty sales force and physician education programs.

Certain specified research and development expenses are generally shared equally by Schering-Plough and Merck.

The unaudited financial information below presents summarized combined financial information for the Merck/Schering-Plough cholesterol joint venture for the three and nine months ended September 30, 2009 and 2008:

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2009	2008	2009	2008
	(Dollars in millions)			
Net sales	$ 1,029	$ 1,102	$ 3,007	$ 3,487
Cost of sales	43	41	128	145
Income from operations	746	777	2,116	2,413

SCHERING-PLOUGH CORPORATION AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

Amounts related to physician details, among other expenses, that are invoiced by Schering-Plough and Merck in the U.S., Canada and Puerto Rico are deducted from income from operations of the cholesterol joint venture.

Schering-Plough s share of the cholesterol joint venture s income from operations for the three and nine months ended September 30, 2009 was $357 million and $1.1 billion, respectively. For the three and nine months ended September 30, 2008, Schering-Plough s share of the cholesterol joint venture s income from operations were $393 million and $1.3 billion, respectively. Included in Schering-Plough s share of income from operations is income of $19 million and $83 million, for the three and nine months ended September 30, 2008, respectively, related to the termination of a respiratory joint venture with Merck. In the U.S. market, Schering-Plough receives a greater share of income from operations on the first $300 million of annual ZETIA sales. As a result, Schering-Plough s share of the cholesterol joint venture s income from operations is generally higher in the first quarter than in subsequent quarters.

The following information provides a summary of the components of Schering-Plough s equity income from the cholesterol joint venture for the three and nine months ended September 30, 2009 and 2008:

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2009	2008	2009	2008
	(Dollars in millions)			
Schering-Plough s share of income from operations	$ 357	$ 393	$ 1,064	$ 1,288
Contractual amounts for physician details	35	49	108	172
Elimination of intercompany profit and other, net	(5)	(8)	(15)	(16)
Total equity income from cholesterol joint venture	$ 387	$ 434	$ 1,157	$ 1,444

At September 30, 2009 and December 31, 2008, Schering-Plough had net receivables (including undistributed income) from the Merck/Schering-Plough Joint Venture of $75 million and $130 million, respectively.

Equity income from the joint venture excludes any profit arising from transactions between Schering-Plough and the joint venture until such time as there is an underlying profit realized by the joint venture in a transaction with a party other than Schering-Plough or Merck.

Due to the virtual nature of the cholesterol joint venture, Schering-Plough incurs substantial costs, such as selling, general and administrative costs, that are not reflected in Equity income and are borne by the overall cost structure of Schering-Plough. These costs are reported on their respective line items in the statements of condensed consolidated operations and are not separately identifiable. The cholesterol agreements do not provide for any jointly owned facilities and, as such, products resulting from the joint venture are manufactured in facilities owned by either Schering-Plough or Merck.

Schering-Plough and Merck are developing a single-tablet combination of ezetimibe and atorvastatin as a treatment for elevated cholesterol levels.

In April 2008, the Merck/Schering-Plough joint venture received a not-approvable letter from the U.S. Food and Drug Administration (FDA) for the proposed fixed combination of loratadine/montelukast. During the second quarter of 2008 the respiratory joint venture was terminated in accordance with the agreements. This action has no impact on the cholesterol joint venture.

See Note 17, Legal, Environmental and Regulatory Matters, Litigation and Investigations relating to the Merck/Schering-Plough Cholesterol Joint Venture, for additional information.

SCHERING-PLOUGH CORPORATION AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

4. SHARE-BASED COMPENSATION

A summary of the options, deferred stock units and performance-based deferred stock units granted during the three and nine months ended September 30, 2009 and 2008 is as follows:

Number of Underlying Shares in Thousands	Three Months Ended September 30, 2009 Underlying Shares	Weighted-Average Grant-Date Fair Value	2008 Underlying Shares	Weighted-Average Grant-Date Fair Value	Nine Months Ended September 30, 2009 Underlying Shares	Weighted-Average Grant-Date Fair Value	2008 Underlying Shares	Weighted-Average Grant-Date Fair Value
Stock options	9	$ 8.53	13	$ 6.58	7,829	$ 7.67	13,597	$ 5.35
Deferred stock units	9	25.55	64	19.79	4,618	22.89	4,772	18.93
Performance-based deferred stock units					1,043	27.93	1,064	19.35
Total Awards	18		77		13,490		19,433	

Options generally become exercisable in equal annual installments over a three-year period. The deferred stock units generally vest at the end of a three-year period from the date they were granted. The performance-based deferred stock units vest at the end of a three-year performance period if specific pre-established levels of performance, market conditions and service are met.

The weighted-average assumptions used in the Black-Scholes option pricing model for the three and nine months ended September 30, 2009 and 2008, were as follows:

	Three Months Ended September 30, 2009	2008	Nine Months Ended September 30, 2009	2008
Dividend yield	1.1%	1.1%	1.1%	1.1%
Volatility	40.6%	37.0%	41.5%	31.4%
Risk-free interest rate	2.4%	3.2%	1.9%	2.8%
Expected term of options (in years)	4.5	4.5	4.5	4.5

Total compensation expense related to stock options, deferred stock units and performance-based deferred stock units for the three and nine months ended September 30, 2009 was $53 million and $135 million, respectively. Total compensation expense related to stock options, deferred stock units and performance-based deferred stock units for

the three and nine months ended September 30, 2008 was $52 million and $171 million, respectively.

At September 30, 2009, the total remaining unrecognized compensation cost related to the performance-based deferred stock units granted in 2009 amounted to $23 million, which will be amortized over the weighted-average remaining requisite service period of 2.25 years. The remaining unrecognized compensation cost for the performance-based deferred stock units may vary each reporting period based on changes in the expected achievement of performance measures.

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SCHERING-PLOUGH CORPORATION AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

5. OTHER EXPENSE/(INCOME), NET

The components of other expense/(income), net are as follows:

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2009	2008	2009	2008
	(Dollars in millions)			
Interest cost incurred	$ 119	$ 140	$ 348	$ 428
Less: amount capitalized on construction	(6)	(4)	(16)	(14)
Interest expense	113	136	332	414
Interest income	(6)	(19)	(17)	(58)
Foreign exchange (gains)/losses	(5)	4	(18)	10
Gain on sales of assets		(160)		(177)
Total other expense/(income), net	$ 102	$ (39)	$ 297	$ 189

In September 2008, Schering-Plough completed its previously announced divestitures of certain Animal Health products as required by regulatory agencies in the U.S. and Europe in connection with the acquisition of OBS. As a result of these divestitures, Schering-Plough recognized a gain of $160 million ($149 million after tax). In addition, during the nine months ended September 30, 2008, Schering-Plough recognized a gain of $17 million ($12 million after tax) on the sale of a manufacturing site. These gains were included in Gain on sales of assets. Net cash proceeds from the divested animal health products were $210 million.

During 2008, Schering-Plough participated in health care refinancing programs adopted by local government fiscal authorities in a major European market. During the three and nine months ended September 30, 2008, Schering-Plough transferred $47 million of its trade accounts receivables owned by a foreign subsidiary to third-party financial institutions without recourse. The transfer of trade accounts receivable qualified as sales of accounts receivable under SFAS No. 140, Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities. For the three and nine months ended September 30, 2008, the transfer of these trade accounts receivable did not have a material impact on Schering-Plough s Statements of Condensed Consolidated Operations. Cash flows from these transactions are included in the change in accounts receivable in operating activities.

6. INCOME TAXES

Schering-Plough reported a U.S. Net Operating Loss (NOL) carryforward of approximately $1.3 billion on its 2008 tax return, which will be available to offset future U.S. taxable income, in varying amounts, through 2028.

This U.S. NOL carryforward could be materially reduced after examination of Schering-Plough s income tax returns by the Internal Revenue Service (IRS). Schering-Plough continues to maintain a valuation allowance against its U.S. deferred tax assets, as management cannot conclude that it is more likely than not the benefit of the U.S. net deferred tax assets can be realized.

SCHERING-PLOUGH CORPORATION AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

7. RETIREMENT PLANS AND OTHER POST-RETIREMENT BENEFITS

Schering-Plough has defined benefit pension plans covering eligible employees in the U.S. and certain foreign countries. In addition, Schering-Plough provides post-retirement medical and life insurance benefits primarily to its eligible U.S. retirees and their dependents through its post-retirement benefit plans.

The components of net pension expense were as follows:

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2009	2008	2009	2008
	(Dollars in millions)			
Service cost	$ 54	$ 54	$ 157	$ 162
Interest cost	61	58	177	176
Expected return on plan assets	(59)	(59)	(172)	(178)
Amortization, net	11	7	32	20
Settlement	1		1	
Net pension expense	$ 68	$ 60	$ 195	$ 180

The components of other post-retirement benefits expense were as follows:

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2009	2008	2009	2008
	(Dollars in millions)			
Service cost	$ 6	$ 7	$ 18	$ 21
Interest cost	9	10	27	29
Expected return on plan assets	(2)	(3)	(8)	(9)
Amortization, net	(1)	1	(3)	3
Net other post-retirement benefits expense	$ 12	$ 15	$ 34	$ 44

For the three and nine months ended September 30, 2009, Schering-Plough made regular contributions of $30 million and $216 million, respectively, to its retirement plans. For the three and nine months ended September 30, 2008,

Schering-Plough contributed $57 million and $153 million, respectively, to its retirement plans. Schering-Plough expects to make regular contributions of approximately $40 million to its retirement plans during the remainder of 2009.

In addition, in 2009 Schering-Plough contributed an aggregate of $367 million of cash equivalents to non-qualified trusts designated to fund certain pension and other employee benefit payments related to the planned combination with Merck. These amounts are included in Other assets in the Condensed Consolidated Balance Sheets. Further, Schering-Plough expects to fund certain deferred compensation plan requirements in the approximate amount of $170 million during the remainder of 2009.

8. EARNINGS PER COMMON SHARE

As of January 1, 2009, Schering-Plough began to treat unvested deferred stock units as participating securities in accordance with the two-class method in the calculation of both basic and diluted earnings per share. This was also applied retrospectively. The effect of the retrospective application of this method was not material to Schering-Plough s earnings per share in 2008.

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SCHERING-PLOUGH CORPORATION AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

The following tables summarize the components of basic and diluted earnings per common share computations.

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2009	2008	2009	2008
	(Dollars in millions)			
Reconciliation of undistributed earnings:				
Net income available to common shareholders	$ 477	$ 576	$ 1,878	$ 1,276
Less: Dividends on common stock	106	106	318	317
Less: Dividends on unvested participating securities	1	1	4	3
Undistributed earnings(1)	$ 370	$ 469	$ 1,556	$ 956

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2009	2008	2009	2008
	(Dollars and shares in millions)			
Basic earnings per common share computation:				
Net income available to common shareholders	$ 477	$ 576	$ 1,878	$ 1,276
Less: Dividend equivalents on unvested participating securities	1	1	4	3
Less: Undistributed earnings allocated to unvested participating securities(1)	4	5	17	11
Undistributed earnings allocated to common shareholders	$ 472	$ 570	$ 1,857	$ 1,262
EPS denominator:				
Weighted-average shares outstanding for basic earnings per common share	1,637	1,626	1,632	1,623
Basic earnings per common share	$ 0.29	$ 0.35	$ 1.14	$ 0.78

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2009	2008	2009	2008
	(Dollars and shares in millions)			

Diluted earnings per common share computation:				
Net income available to common shareholders	$ 477	$ 576	$ 1,878	$ 1,276
Add: Preferred stock dividends(3)				
Less: Dividend equivalents on unvested participating securities	1	1	4	3
Less: Undistributed earnings allocated to unvested participating securities(1)	4	5	17	11
	$ 472	$ 570	$ 1,857	$ 1,262
EPS denominator calculation:				
Weighted-average shares outstanding for basic earnings per common share	1,637	1,626	1,632	1,623
Dilutive effect of options(2)	12	2	7	3
Dilutive effect of preferred shares(3)				
Weighted-average shares outstanding for diluted earnings per common share	1,649	1,628	1,639	1,626
Diluted earnings per common share	$ 0.29	$ 0.35	$ 1.13	$ 0.78

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SCHERING-PLOUGH CORPORATION AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

. (1) For the three and nine months ended September 30, 2009, 17 million of unvested outstanding deferred stock units and performance-based deferred stock units are considered participating securities. For the three and nine months ended September 30, 2008, 18 million of unvested outstanding deferred stock units and performance-based deferred stock units are considered participating securities. The undistributed earnings are allocated to both common shares and unvested participating securities in computing the earnings per share under the two-class method.

(2) For the three and nine months ended September 30, 2009, 34 million and 38 million, respectively, of equivalent common shares issuable under Schering-Plough s stock incentive plans were excluded from the computation of diluted EPS because their effect would have been antidilutive. For the three and nine months ended September 30, 2008, 54 million and 53 million, respectively, of equivalent common shares issuable under Schering-Plough s stock incentive plans were excluded from the computation of diluted EPS because their effect would have been antidilutive.

(3) For the three and nine months ended September 30, 2009, approximately 88 million and 89 million of common shares, obtainable upon conversion of Schering-Plough s 2007 mandatory convertible preferred stock were excluded from the computation of diluted earnings per share because their effect would have been antidilutive. For the three months and nine months ended September 30, 2008 approximately 91 million common shares, obtainable upon conversion of the 2007 mandatory convertible preferred stock were excluded from the computation of diluted earnings per share because their effect would have been antidilutive.

9. COMPREHENSIVE INCOME

Comprehensive income is comprised of the following:

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2009	2008	2009	2008
	(Dollars in millions)			
Net income	$ 515	$ 614	$ 1,991	$ 1,389
Foreign currency translation adjustment	341	(732)	535	(282)
Unrealized gain (loss) on investments available for sale	8	(10)	18	(15)
Total comprehensive income/(loss)	$ 864	$ (128)	$ 2,544	$ 1,092

10. INVENTORIES

Inventories consisted of the following:

	September 30, 2009	December 31, 2008
	(Dollars in millions)	
Finished products	$ 1,126	$ 1,212
Goods in process	1,948	1,428
Raw materials and supplies	622	679
Total inventories and inventory classified in other non-current assets	$ 3,696	$ 3,319

For the nine months ended September 30, 2008, $840 million of amortization of the fair value step-up recorded as part of the OBS acquisition are included in Depreciation and amortization in the condensed consolidated statements of cash flows.

Included in Other assets (non-current) at September 30, 2009 and December 31, 2008 was $237 million and $205 million, respectively, of inventory not expected to be sold within one year.

11. GOODWILL AND OTHER INTANGIBLE ASSETS

Goodwill was $2,879 million at September 30, 2009 as compared to $2,778 million at December 31, 2008. The increase was due to foreign currency translation.

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SCHERING-PLOUGH CORPORATION AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

The components of other intangible assets, net are as follows:

	September 30, 2009			December 31, 2008		
	Gross Carrying Amount	Accumulated Amortization	Net	Gross Carrying Amount	Accumulated Amortization	Net
	(Dollars in millions)					
Patents	$ 3,983	$ 725	$ 3,258	$ 3,803	$ 418	$ 3,385
Trademarks and other	2,854	294	2,560	2,756	180	2,576
Licenses and other	806	643	163	796	603	193
Total other intangible assets	$ 7,643	$ 1,662	$ 5,981	$ 7,355	$ 1,201	$ 6,154

These intangible assets are amortized on the straight-line method over their respective useful lives. The residual value of intangible assets is estimated to be zero. Amortization expense for the three months ended September 30, 2009 and 2008 was $139 million and $148 million, respectively and $401 million and $439 million for the nine months ended September 30, 2009 and 2008, respectively. Annual amortization expenses related to these intangible assets for the years 2009 to 2013 is expected to be approximately $535 million.

12. BORROWINGS

Schering-Plough s outstanding borrowings at September 30, 2009 and December 31, 2008 were as follows:

	September 30, 2009	December 31, 2008
	(Dollars in millions)	
Short-term		
Short-term borrowings and current portion of long-term debt	$ 184	$ 244
Current portion of capital leases	1	1
Total short-term borrowings and current portion of long-term debt	$ 185	$ 245
Long-term		
5.00% senior unsecured Euro-denominated notes due 2010	$ 732	$ 698
Floating rate Euro-denominated term loan due 2012	659	698
5.30% senior unsecured notes due 2013	1,248	1,247
5.375% senior unsecured Euro-denominated notes due 2014	2,194	2,090
6.00% senior unsecured notes due 2017	996	995
6.50% senior unsecured notes due 2033	1,143	1,143

6.55% senior unsecured notes due 2037		994		994
Capital leases		21		19
Other long-term borrowings		46		47
Total long-term borrowings, net of current portion	$	8,033	$	7,931

The decrease in the Floating rate Euro-denominated term loan due 2012 was due to an early principal repayment of Euro 50 million in the first quarter of 2009. No prepayment penalty was incurred relating to this principal repayment. The other changes in outstanding Euro-denominated borrowings at September 30, 2009 were due to foreign currency translation on Euro-denominated debt balances.

13. FINANCIAL INSTRUMENTS

The table below presents the carrying values and estimated fair values for certain of Schering-Plough s financial instruments at September 30, 2009 and December 31, 2008. Estimated fair values were determined based on market prices, where available, or dealer quotes. The carrying values of all other financial instruments, including cash and cash equivalents, approximated their estimated fair values at September 30, 2009 and December 31, 2008.

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NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

	September 30, 2009		December 31, 2008	
	Carrying Value	Estimated Fair Value	Carrying Value	Estimated Fair Value
	(Dollars in millions)			
ASSETS:				
Short-term investments	$ 487	$ 487	$ 5	$ 5
Long-term investments(1)	557	557	157	157
LIABILITIES:				
Short-term borrowings and current portion of long-term debt	$ 185	$ 185	$ 245	$ 245
Long-term debt	8,033	8,926	7,931	7,891

(1) Long-term investments, which are included in other non-current assets, primarily consist of cash, debt and equity securities held in non-qualified trusts to fund employee benefit obligations. The related employee benefit obligations are included as liabilities in the condensed consolidated balance sheets. These assets can only be used to fund the related employee benefit obligations.

14. FAIR VALUE MEASUREMENTS

Schering-Plough s condensed consolidated balance sheet at September 30, 2009 includes the following assets that are measured at fair value on a recurring basis:

	Total Fair Value at September 30, 2009	Quoted Prices in Active Markets for Identical Assets and Liabilities (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
	(Dollars in millions)			
Assets				
Securities held for employee compensation	$ 115	$ 115	$	$
Other	10	7	3	
Total assets	$ 125	$ 122	$ 3	$

At September 30, 2009 there were no liabilities that were subject to fair value measurement.

The majority of Schering-Plough s assets measured at fair value on a recurring basis are measured using unadjusted quoted prices in active markets for identical items (Level 1) as inputs, multiplied by the number of units held at the balance sheet date. As of September 30, 2009, assets with fair values measured using significant other observable inputs (Level 2) include measurements using quoted prices for identical items in markets that are not active and measurements using inputs that are derived principally from or corroborated by observable market data.

15. SEGMENT DATA

Schering-Plough has three reportable segments: Prescription Pharmaceuticals, Animal Health and Consumer Health Care. The segment sales and profit data that follow are consistent with Schering-Plough s current management reporting structure. The Prescription Pharmaceuticals segment discovers, develops, manufactures and markets human pharmaceutical products. The Animal Health segment discovers, develops, manufactures and markets animal health products. The Consumer Health Care segment develops, manufactures and markets over-the-counter, foot care and sun care products, primarily in the U.S.

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SCHERING-PLOUGH CORPORATION AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

Net sales by segment:

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2009	2008	2009	2008
	(Dollars in millions)			
Prescription Pharmaceuticals	$ 3,548	$ 3,539	$ 10,515	$ 10,798
Animal Health	669	759	1,976	2,299
Consumer Health Care				