Was Andrew Left Right About Valeant Pharmaceuticals Intl Inc.?

Description

After markets closed on Monday, **Valeant Pharmaceuticals Intl Inc.** (TSX:VRX)(NYSE:VRX) announced that it would have to restate its earnings for both 2014 and 2015. The revelation comes in the wake of an ad hoc committee's investigation into Valeant's prior relationship with Philidor.

Without doubt, this will conjure up memories of Andrew Left and his report on Citron Research, in which he claimed that Valeant was likely using Philidor to inflate revenue. So was he right all along?

Mr. Left's report

On October 21, Mr. Left penned a report titled "Valeant: Could this be the Pharmaceutical Enron?" He made some very startling revelations about Valeant and its relationship with Philidor.

"Citron believes [the scheme] is merely for the purpose of phantom sales or stuff the channel, and avoid scrutiny from the auditors," Mr. Left said.

Valeant's shares sunk by nearly 20% that day and have declined further in the four months since.

Not quite the same thing

When a company sells a product to itself (usually done through one or more subsidiaries) and books it as revenue, then this is called channel stuffing. So Mr. Left's suspicions were not to be taken lightly.

As it turns out though, Valeant wasn't using Philidor for this purpose. Instead, the restatement announced Monday evening primarily concerns the timing of revenue. For this reason, earnings per share for 2014 will be restated downwards by US$0.10, and earnings per share in 2015 will be restated upwards by US$0.09.

In fact, investors have largely breathed a sigh of relief. As of this writing, Valeant's shares are up by roughly 9%. This is partly due to the fact that Valeant will be announcing fourth-quarter results on February 29. Previously, this date had not been disclosed, which was raising suspicions about the company and weighing on its share price.

Still plenty of issues

This news still should raise some worries though. After all, it could simply be one part of a broader pattern at Valeant. And it would not be the first company with a habit of aggressively accounting for acquisitions.

Besides, the investigation of Valeant's involvement with Philidor is still not completed, and there could be more revelations. Making matters worse, regulators and politicians have their sights set on Valeant. If anything goes seriously wrong, then the company's US$30 billion debt load could become a major burden.

With all that in mind, Tuesday's rally seems a bit premature. This is still a stock to stay away from.

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