WATSON PHARMACEUTICALS INC
Form 10-K
February 23, 2009

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

Form 10-K

þ **ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**
For the fiscal year ended December 31, 2008
OR
o **TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**
For the transition period from to

Commission file number 001-13305

WATSON PHARMACEUTICALS, INC.
(Exact name of registrant as specified in its charter)

Nevada	**95-3872914**
(State or other jurisdiction of incorporation or organization)	*(I.R.S. Employer Identification No.)*

311 Bonnie Circle, Corona, CA 92880 - 2882
(Address of principal executive offices, including ZIP code)

(951) 493-5300
(Registrant s telephone number, including area code)

Securities registered pursuant to Section 12(b) of the Act:

Title of Each Class	Name of Each Exchange on Which Registered
Common Stock, $0.0033 par value	New York Stock Exchange

Securities registered pursuant to Section 12(g) of the Act:
None

Indicate by check mark if the registrant is a well known seasoned issuer (as defined in Rule 405 of the Securities Act). Yes þ No o

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act. Yes o No þ

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 if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of Registrant s knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K. 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 (Do not check if a smaller reporting company)	Smaller reporting company o

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

Aggregate market value of Common Stock held by non-affiliates of the Registrant, as of June 30, 2008:
$2,836,945,000 based on the last reported sales price on the New York Stock Exchange

Number of shares of Registrant s Common Stock outstanding on February 18, 2009: 104,627,327

DOCUMENTS INCORPORATED BY REFERENCE

Part III incorporates certain information by reference from the registrant s proxy statement for the 2009 Annual Meeting of Stockholders, to be held on May 8, 2009. Such proxy statement will be filed no later than 120 days after the close of the registrant s fiscal year ended December 31, 2008.

WATSON PHARMACEUTICALS, INC.

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PART I

ITEM 1. *BUSINESS*

Business Overview

Watson Pharmaceuticals, Inc. (Watson , the Company , we , us or our) is a leading specialty pharmaceutical comp engaged in the development, manufacturing, marketing, sale and distribution of generic (off-patent) and brand pharmaceutical products. Our operations are based predominantly in the United States of America (U.S.) and India, with our key commercial market being the U.S. As of December 31, 2008, we marketed approximately 150 generic pharmaceutical product families and 27 brand pharmaceutical product families through our Generic and Brand Divisions, respectively, and distributed approximately 8,000 stock-keeping units (SKUs) through our Distribution Division.

Our principal executive offices are located at 311 Bonnie Circle, Corona, California, 92880. Our Internet website address is www.watson.com. We do not intend this website address to be an active link or to otherwise incorporate by reference the contents of the website into this report. Our annual reports on Form 10-K, quarterly reports on Form 10-Q and current reports on Form 8-K, and all amendments thereto are available free of charge on our Internet website. These reports are posted on our website as soon as reasonably practicable after such reports are electronically filed with the U.S. Securities and Exchange Commission (SEC). The public may read and copy any materials that we file with the SEC at the SEC s Public Reference Room or electronically through the SEC website (www.sec.gov). Within the Investors section of our website, we provide information concerning corporate governance, including our Corporate Governance Guidelines, Board Committee Charters and Composition, Code of Conduct and other information.

Business Description

Prescription pharmaceutical products in the U.S. generally are marketed as either generic or brand pharmaceuticals. Generic pharmaceutical products are bioequivalents of their respective brand products and provide a cost-efficient alternative to brand products. Brand pharmaceutical products are marketed under brand names through programs that are designed to generate physician and consumer loyalty. Through our Distribution Division, we distribute pharmaceutical products, primarily generics, which have been commercialized by us and others, to independent and chain pharmacies and physicians offices. As a result of the differences between the types of products we market and/or distribute and the methods we distribute products, we operate and manage our business as three operating segments: Generic, Brand and Distribution.

Business Strategy

We apply three key strategies to grow our Generic and Brand pharmaceutical businesses: (i) internal development of differentiated and high demand products, (ii) establishment of strategic alliances and collaborations and (iii) acquisition of products and companies that complement our existing portfolio. We believe that our three-pronged strategy will allow us to expand both our brand and generic product offerings. Our Distribution Division distributes products for over 200 suppliers and is focused on providing next-day delivery and responsive service to its customers. Our Distribution Division also distributes a number of Watson generic and brand products. During 2008, the Distribution Division had 12 substantial new product launches.

Based upon business conditions, our financial strength and other factors, we regularly reexamine our business strategies and may change them at anytime. See Item 1A. Risk Factors Risks Related to Our Business in this annual report on Form 10-K (Annual Report).

Generic Segment

Watson is a leader in the development, manufacturing and sale of generic pharmaceutical products. When patents or other regulatory exclusivity no longer protect a brand product, opportunities exist to introduce off-patent or generic counterparts to the brand product. These generic products are bioequivalent to their brand name counterparts and are generally sold at significantly lower prices than the brand product. As such, generic

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pharmaceuticals provide an effective and cost-efficient alternative to brand products. Our portfolio of generic products includes products we have developed internally, products we have licensed from third parties and products we distribute for third parties.

Net revenues in our Generic segment accounted for $1.47 billion or approximately 58% of our total net revenues in 2008.

Generic Strategy

Our Generic business is currently focused on maintaining a leading position within the U.S. generics market by offering a consistent and reliable supply of quality generic products. Our strategy is to develop generic pharmaceuticals that are difficult to formulate or manufacture or will complement or broaden our existing product lines. Since the prices and unit volumes of our brand products will likely decrease upon the introduction of generic alternatives, we also intend to market generic alternatives to our brand products where market conditions and the competitive environment justify such activities. Additionally, we may distribute generic versions of third parties brand products (sometimes known as Authorized Generics) to the extent such arrangements are complementary to our core business.

We have maintained an ongoing effort to enhance efficiencies and reduce costs in our manufacturing operations. Execution of these initiatives will allow us to maintain competitive pricing on our products. We are also looking to leverage our broad product line by expanding our selling and marketing presence outside the U.S. We believe a broader sales and marketing presence will allow us to expand our revenue base and minimize risk. Additionally, we are looking to establish capabilities in developing generic biologics through strategic collaborations or acquisitions.

Our portfolio of approximately 150 Generic pharmaceutical product families includes the following products, which represented 60% of total Generic segment net revenues in 2008:

Watson Generic Product	Comparable Brand Name	Therapeutic Classification
Alendronate Sodium	Fosamax®	Osteoporosis preparation
Bupropion hydrochloride SR	Zyban®	Aid to smoking cessation
Bupropion hydrochloride SR	Wellbutrin SR®	Anti-depressant
Bupropion hydrochloride XL	Wellbutrin XL®	Anti-depressant
Cartia XT®	Cardizem® CD	Anti-hypertensive
Clarithromycin ER	Biaxin® XL	Anti-biotic
Dronabinol	Marinol®	Antiemetic
Fentanyl transdermal system	Duragesic®	Analgesic/narcotic combination
Glipizide ER	Glucotrol® XL	Anti-diabetic
Hydrocodone bitartrate/ acetaminophen	Lorcet®, Vicodin®, Lortab®, Norco®/Anexia	Analgesic
Levora®	Nordette®	Oral contraceptive
Low-Ogestrel®	Lo-Ovral®	Oral contraceptive
Lutera®	Alesse®	Oral contraceptive
Microgestin®/Microgestin® Fe	Loestrin®/Loestrin® Fe	Oral contraceptive
Necon®	Ortho-Novum®, Modicon®	Oral contraceptive
Nicotine polacrilex gum	Nicorette®	Aid to smoking cessation
Omeprazole DR	Prilosec®	Gastrointestinal agent
Oxycodone/acetaminophen	Percocet®	Analgesic

TriNessa™	Ortho Tri-Cyclen®	Oral contraceptive
Trivora®	Triphasil®	Oral contraceptive

Our Generic Division also receives other revenues consisting primarily of royalties and commission revenue. During 2008, we received royalties on GlaxoSmithKline s sales of Wellbutrin XL® 150mg and received royalties on sales by Sandoz Pharmaceutical Corporation (Sandoz), a subsidiary of Novartis AG, of metoprolol succinate 50 mg extended release tablets. Additionally, we promote fentanyl citrate troche on

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behalf of Cephalon, Inc. (Cephalon) and receive commission revenue based on Cephalon s sales. During 2008, we also received a $15.0 million milestone obligation for a 1999 Schein Pharmaceutical, Inc. (Schein) litigation settlement with Barr Pharmaceuticals, Inc. (Barr) related to Cenestin. Other revenue totaled $70.4 million for 2008 or 4.8% of our total Generic segment net revenue.

We predominantly market our generic products to various drug wholesalers, mail order, government and national retail drug and food store chains utilizing 27 sales and marketing professionals. We sell our generic prescription products primarily under the Watson Laboratories and Watson Pharma labels, with the exception of our over-the-counter generic products which we sell under our Rugby® label or under private label.

During 2008, we expanded our generic product line with the launch of 11 generic products. Key launches in 2008 included bupropion hydrochloride XL 150mg tablets, an anti-depressant launched in November 2008; omeprazole 40mg delayed-release capsules, indicated for short-term treatment of active duodenal ulcer, launched in July 2008; dronabinol, indicated to treat nausea and vomiting associated with cancer chemotherapy, launched in June 2008; clarithomycin extended-release tablets, USP in the 500mg strength, an anti-infective launched in January 2008 and galantamine hydrobromide extended-release, indicated for the treatment of Alzheimer s disease, launched in December 2008.

We continue to make progress on our Global Supply Chain Initiative and the transfer of product manufacturing from our New York facility to our Florida, California, and India sites. By the end of 2009, we anticipate one-third of our manufactured volume will be produced from our Goa, India facility. By the end of 2010, we plan to close our New York solid dosage manufacturing and warehouse facilities. Additionally, we continue to implement operational efficiency programs at our manufacturing sites.

Generic Research and Development

During 2008, we took measures to enhance our pipeline of generic products by discontinuing the development of certain products and adding new products to our pipeline. At December 31, 2008, we had approximately 60 Abbreviated New Drug Applications (ANDAs) on file. See the Government Regulation and Regulatory Matters section below for a description of our process for obtaining U.S. Food and Drug Administration (FDA) approval for our products. See also Item 1A. Risk Factors Risks Related to our Business Extensive industry regulation has had, and will continue to have, a significant impact on our business, especially our product development, manufacturing and distribution capabilities. in this Annual Report.

We devote significant resources to the research and development (R&D) of generic products and proprietary drug delivery technologies. We incurred Generic segment R&D expenses of $119 million in 2008, $102 million in 2007 and $84 million in 2006. We are presently developing a number of generic products through a combination of internal and collaborative programs.

Our Generic R&D strategy focuses on the following product development areas:

- off-patent drugs that are difficult to develop or manufacture, or that complement or broaden our existing product lines;
- the development of sustained-release and other drug delivery technologies and the application of these technologies to existing drug forms; and
- using in-house technologies to develop new products.

As of December 31, 2008, we conducted R&D in Corona, California; Davie and Weston, Florida; Copiague, New York; Salt Lake City, Utah; Changzhou City, People s Republic of China; and Ambernath and Mumbai, India.

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Generic Business Development

In December 2008, we acquired a portfolio of generic pharmaceutical products that were divested as a result of the merger between Teva Pharmaceutical Industries, Ltd. (Teva) and Barr. The portfolio consists of 17 products, including 15 FDA-approved products and 2 development-stage products. Key products in the portfolio include cyclosporine capsules and liquid, desmopressin acetate tablets, glipizide/metformin HCI tablets, mirtazapine orally disintegrating tablets and metoclopramide HCI tablets. We acquired the portfolio of existing approved products for an upfront payment of $36.0 million and will make additional payments to Teva if certain milestones are met on the development-stage products. Teva has agreed to supply the products to Watson until manufacturing is transferred to Watson or a third party.

Brand Segment

Newly developed pharmaceutical products normally are patented and, as a result, are generally offered by a single provider when first introduced to the market. We currently market a number of branded products to physicians, hospitals, and other markets that we serve. We classify these patented and off-patent trademarked products as our brand pharmaceutical products. Net revenues in our Brand segment accounted for $455.0 million or approximately 18% of our total net revenues in 2008. Typically, our brand products realize higher profit margins than our generic products.

Our portfolio of 27 Brand pharmaceutical product families includes the following products, which represented 76% of total Brand segment net revenues in 2008:

Watson Brand Product	Active Ingredient	Therapeutic Classification
Androderm®	Testosterone (transdermal patch)	Male hormone replacement
Ferrlecit®	Sodium ferric gluconate in sucrose injection	Hematinic
INFeD®	Iron dextran	Hematinic
Oxytrol®	Oxybutnin (transdermal patch)	Overactive bladder
Trelstar® DEPOT	Triptorelin pamoate injection	Prostate cancer
Trelstar® LA	Triptorelin pamoate injection	Prostate cancer

We market our brand products through approximately 380 sales professionals within our specialized sales and marketing groups. Each of our sales and marketing groups focuses on physicians who specialize in the diagnosis and treatment of particular medical conditions and each group offers products to satisfy the unique needs of these physicians. We believe this focused sales and marketing approach enables us to foster close professional relationships with specialty physicians, as well as cover the primary care physicians who also prescribe in selected therapeutic areas. We generally sell our brand products under the Watson Pharma and the Oclassen® Dermatologics labels.

Our sales and marketing groups have targeted selected specialty therapeutic areas predominately because of their potential growth opportunities and the size of the physician audience. We believe that the nature of these markets and the identifiable base of physician prescribers provide us with opportunities to achieve significant market penetration through our specialized sales forces. We intend to continue to expand our brand product portfolio through internal product development, strategic alliances and acquisitions.

Our Brand segment also receives other revenues consisting of co-promotion revenue and royalties. We promote AndroGel® on behalf of Unimed Pharmaceuticals, Inc., a wholly owned subsidiary of Solvay Pharmaceuticals, Inc.

(Solvay) and other selected products on behalf of third parties. We also record revenue (including the amortization of deferred revenue) relating to our obligation to manufacture and supply Fortamet® and Altoprev® to Sciele Pharma, Inc. (Sciele), a wholly-owned subsidiary of Shionogi & Co., Ltd. Other revenue totaled $58.0 million for 2008 or 12.7% of our total Brand segment net revenue.

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Specialty Products

Our Specialty Products product line focuses on products that we market to urologists, gynecologists and targeted primary care physicians. We actively promote Oxytrol®, Trelstar Depot® and Trelstar® LA (collectively Trelstar®) through this group. We also promote AndroGel® on behalf of Solvay through this group and, in March 2009, we plan to begin co-promoting Femring®, a product for hormone replacement therapy, on behalf of Warner Chilcott Ltd.

In May 2008, we launched Mixject™, a new delivery system for Trelstar® which offers new features that makes preparation, administration and disposal of Trelstar® easier.

In April 2009, we plan to launch Rapaflo™ (silodosin), our selective alpha-blocker for the treatment of the signs and symptoms of benign prostatic hyperplasia (BPH).

In the second quarter of 2009, we plan to launch Gelnique™ (oxybutynin chloride gel) 10%, our topical gel for the treatment of overactive bladder.

Nephrology

Our Nephrology product line consists of products for the treatment of iron deficiency anemia. Our primary products in the Nephrology group are Ferrlecit® and INFeD®, which are indicated for patients undergoing hemodialysis in conjunction with erythropoietin therapy. Regulatory exclusivity on Ferrlecit® ended in August 2004. Additionally, we are currently engaged in an expedited arbitration proceeding to resolve a dispute with Sanofi Aventis concerning, among other things, the expiration date of our rights to market and sell Ferrlecit®. See Item 1A. Risk Factors Risks Related to our Business Loss of revenues from Ferrlecit®, a significant product, could have a material adverse effect on our results of operations, financial condition and cash flows. in this Annual Report. Also refer to *Legal Matters* in NOTE 15 Commitments and Contingencies in the accompanying Notes to Consolidated Financial Statements in this Annual Report.

Brand Research and Development

We devote significant resources to the R&D of brand products and proprietary drug delivery technologies. A number of our brand products are protected by patents and have enjoyed market exclusivity for 5 to 10 years and sometimes even longer. We incurred Brand segment R&D expenses of $51 million in 2008, $42 million in 2007 and $47 million in 2006.

Our Brand R&D strategy focuses on the following product development areas:

- the application of proprietary drug-delivery technology for new product development in specialty areas; and
- the acquisition of mid-to-late development-stage brand drugs.

We are presently developing a number of brand products, some of which utilize novel drug-delivery systems, through a combination of internal and collaborative programs.

During 2008 we filed a New Drug Application (NDA) with the FDA for Rapaflo™, our new alpha-blocker for the treatment of the signs and symptoms of BPH. In October 2008, our NDA was approved and we plan to launch Rapaflo™ in April 2009.

We also filed an NDA for Gelnique™, a topical gel for the treatment of overactive bladder which we believe may provide greater patient acceptance and compliance than current therapies. In January 2009 we received approval of our NDA and we anticipate launching Gelnique™ in the second quarter of 2009. Additional products in the brand pipeline include a six month formulation of Trelstar®, Uracyst, for the treatment of cystitis and a novel oral contraceptive, for the preventation of pregnancy.

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Brand Business Development

In July 2008, Mylan Inc. acquired Watson s 50% joint venture interest in Somerset Pharmaceuticals, Inc. (Somerset). Somerset developed Emsam®, a transdermal patch for the treatment of major depressive disorder, currently marketed in the United States by Bristol-Myers Squibb.

In early 2009, we entered into agreements with Warner Chilcott, Ltd. for our Specialty Products sales force to promote Femring® to gynecologists in the U.S. We also licensed an oral contraceptive from Warner Chilcott Ltd. that is currently in late stage development.

Distribution Segment

Our Distribution business, which consists of our Anda, Anda Pharmaceuticals and Valmed (also known as VIP) subsidiaries (collectively Anda), primarily distributes generic and selected brand pharmaceutical products to independent pharmacies, alternate care providers (hospitals, nursing homes and mail order pharmacies), pharmacy chains and physicians offices. Additionally, we sell to members of buying groups, which are independent pharmacies that band together to enhance their buying power. We believe that we are able to effectively compete in the distribution market, and therefore optimize our market share, based on three critical elements: (i) competitive pricing, (ii) responsive customer service that includes, among other things, next day delivery to the entire U.S. and high levels of inventory for approximately 8,000 SKUs, and (iii) well established telemarketing relationships with our customers, supplemented by our electronic ordering capabilities. While we purchase most of the approximate 8,000 SKUs in our Distribution operations from third party manufacturers, we also utilize these operations for the sale and marketing of our own products, and our collaborative partners products. We are the only U.S. pharmaceutical company that has meaningful distribution operations with direct access to independent pharmacies and we believe that our Distribution operation is a strategic asset in the national distribution of generic and brand pharmaceuticals.

Revenue growth in our Distribution operations will primarily be dependent on the launch of new products, offset by the overall level of net price and unit declines on existing distributed products and will be subject to changes in market share.

In our Distribution operations, we presently distribute products from our facilities in Weston, Florida and Groveport, Ohio. For the year ended December 31, 2008, approximately 60% of our Distribution sales were shipped from our Groveport, Ohio facility and 40% from our Weston, Florida facility, though this percentage can vary. While our Weston, Florida facility is operating at 80% capacity, our 355,000 square foot Ohio distribution center currently operates at approximately 30% capacity, and provides us with additional distribution capacity for the foreseeable future.

Strategic Alliances and Collaborations

Through collaborative agreements and strategic alliances, we develop and manufacture products that are marketed by other pharmaceutical companies, including products that utilize our patented technologies and formulation capabilities. Pursuant to a manufacturing and supply agreement and a license agreement, we supply Fortamet® and Altoprev® to Sciele.

We have a generic product development alliance with Cipla Ltd. (Cipla), the second largest pharmaceutical company in India. Under the terms of the agreement announced in December 2002, we share development responsibilities. Watson is responsible for conducting bioequivalence studies, pursuing regulatory approvals for all developed products and has exclusive U.S. marketing rights for the products. Cipla is responsible for manufacturing products.

In 2004, we entered into an exclusive licensing agreement with Kissei Pharmaceutical Co., Ltd. (Kissei) to develop and market Rapaflo™ for the North American market. The compound was originally developed and launched by Kissei in Japan as Urief® and is marketed in Japan in cooperation with Daiichi Sankyo Pharmaceutical Co., Ltd. for the treatment of the signs and symptoms of BPH.

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In October 2006, we entered into an agreement with Solvay to utilize Watson s Specialty Products sales force to co-promote AndroGel® to urologists in the U.S.

Through a R&D and supply agreement with Takeda Chemical Industries, Ltd. (Takeda), we provide contract R&D and manufacturing services to develop a combination product consisting of Takeda s Actos® (pioglitazone) and our extended-release metformin, which is administered once a day for the treatment of Type 2 diabetes. We are responsible for the formulation and manufacture of this combination product and Takeda is responsible for obtaining regulatory approval of and marketing this combination product, both in the U.S. and in other countries. Takeda submitted an NDA in 2006.

Financial Information About Segments

Watson evaluates the performance of its Generic, Brand and Distribution business segments based on net revenues, gross profit and net contribution. Summarized net revenues, gross profit and contribution information for each of the last three fiscal years, where applicable, is presented in NOTE 12 Operating Segments in the accompanying Notes to Consolidated Financial Statements in this Annual Report.

Customers

In our Generic and Brand operations, we sell our generic and brand pharmaceutical products primarily to drug wholesalers, retailers and distributors, including national retail drug and food store chains, hospitals, clinics, mail order, government agencies and managed healthcare providers such as health maintenance organizations and other institutions. In our Distribution business, we distribute generic and certain select brand pharmaceutical products to independent pharmacies, members of buying groups, alternate care providers (hospitals, nursing homes and mail order pharmacies), pharmacy chains and physicians offices.

Sales to certain of our customers accounted for 10% or more of our annual net revenues during the past three years. The following table illustrates those customers and the respective percentage of our net revenues for which they account:

Customer	2008	2007	2006
McKesson Corporation	11%	12%	17%
Walgreen Co.	11%	11%	8%
AmeriSourceBergen Corp.	9%	9%	13%

Certain of these customers comprise a significant part of the distribution network for pharmaceutical products in the U.S. In recent years, this distribution network has undergone significant consolidation, marked by mergers and acquisitions among wholesale distributors and large retail drug store chains. As a result, a small number of large, wholesale distributors and large chain drug stores control a significant share of the market. We expect that consolidation of drug wholesalers and retailers may adversely impact pricing and create other competitive pressures on drug manufacturers. Our Distribution business competes directly with our large wholesaler customers with respect to the distribution of generic products.

The loss of any of these customers could have a material adverse effect on our business, results of operations, financial condition and cash flows. See Item 1A. Risk Factors Risk Relating to Investing in the Pharmaceutical Industry in this Annual Report.

Competition

The pharmaceutical industry is highly competitive. In our Generic and Brand product operations, we compete with different companies depending upon product categories, and within each product category, upon dosage strengths and drug delivery systems. Such competitors include the major brand name and generic manufacturers of pharmaceutical products. In addition to product development, other competitive factors in the pharmaceutical industry include product quality and price, reputation and service and access to proprietary and technical information. It is possible that developments by others will make our products or technologies noncompetitive or obsolete.

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Competing in the brand product business requires us to identify and bring to market new products embodying technological innovations. Successful marketing of brand products depends primarily on the ability to communicate their effectiveness, safety and value to healthcare professionals in private practice, group practices and managed care organizations. We anticipate that our brand product offerings will support our existing areas of therapeutic focus. Based upon business conditions and other factors, we regularly reevaluate our business strategies and may from time to time reallocate our resources from one therapeutic area to another, withdraw from a therapeutic area or add an additional therapeutic area in order to maximize our overall growth opportunities. Our competitors in brand products include major brand name manufacturers of pharmaceuticals. Based on total assets, annual revenues and market capitalization, our Brand segment is considerably smaller than many of these competitors and other national competitors in the brand product area. Many of our competitors have been in business for a longer period of time, have a greater number of products on the market and have greater financial and other resources than we do. If we directly compete with them for the same markets and/or products, their financial strength could prevent us from capturing a meaningful share of those markets.

We actively compete in the generic pharmaceutical industry. Revenues and gross profit derived from the sales of generic pharmaceutical products tend to follow a pattern based on certain regulatory and competitive factors. As patents and regulatory exclusivity for brand name products expire or are successfully challenged, the first off-patent manufacturer to receive regulatory approval for generic equivalents of such products is generally able to achieve significant market penetration. As competing off-patent manufacturers receive regulatory approvals on similar products, market share, revenues and gross profit typically declines, in some cases dramatically. Accordingly, the level of market share, revenues and gross profit attributable to a particular generic product normally is related to the number of competitors in that product s market and the timing of that product s regulatory approval and launch, in relation to competing approvals and launches. Consequently, we must continue to develop and introduce new products in a timely and cost-effective manner to maintain our revenues and gross profit. In addition to competition from other generic drug manufacturers, we face competition from brand name companies in the generic market. Many of these companies seek to participate in sales of generic products by, among other things, collaborating with other generic pharmaceutical companies or by marketing their own generic equivalent to their brand products as Authorized Generics. Our major competitors in generic products include Teva Pharmaceutical Industries, Ltd., Mylan Inc., Mallinckrodt Pharmaceuticals Generics (a subsidiary of Covidien AG) and Sandoz. See Item 1A. Risk Factors Risks Related to Our Business The pharmaceutical industry is highly competitive. in this Annual Report.

In our Distribution business, we compete with a number of large wholesalers and other distributors of pharmaceuticals, including McKesson Corporation, AmerisourceBergen Corporation and Cardinal Health, Inc., which distribute both brand and generic pharmaceutical products to their customers. These same companies are significant customers of our Generic and Brand pharmaceutical businesses. As generic products generally have higher gross margins than brand products for a pharmaceutical distribution business, each of the large wholesalers, on an increasing basis, are offering pricing incentives on brand products if the customers purchase a large portion of their generic pharmaceutical products from the primary wholesaler. As we do not offer a broad portfolio of brand products to our customers, we are at times competitively disadvantaged and must compete with these wholesalers based upon our very competitive pricing for generic products, greater service levels and our well-established telemarketing relationships with our customers, supplemented by our electronic ordering capabilities. Additionally, generic manufacturers are increasingly marketing their products directly to smaller chains and thus increasingly bypassing wholesalers and distributors. Increased competition in the generic industry as a whole may result in increased price erosion in the pursuit of market share.

Manufacturing, Suppliers and Materials

During 2008, we manufactured many of our own finished products at our plants in Corona, California; Davie, Florida; Goa, India; Carmel, New York; Copiague, New York and Salt Lake City, Utah. As part of an ongoing effort to

optimize our manufacturing operations, we implemented several cost reduction initiatives in 2008, which included the transfer of several solid dosage products from our Carmel, New York facility to our

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Goa, India facility, and the ongoing implementation of our operational excellence program at certain of our U.S. manufacturing facilities.

We have development and manufacturing capabilities for raw material and active pharmaceutical ingredients (API) and intermediate ingredients to support our internal product development efforts in our Goa and Ambernath, India and Changzhou, China facilities. Our Ambernath, India facility also develops and manufactures API for third parties. We also have an equity investment in Scinopharm Taiwan, Ltd., a company that specializes in the development and manufacture of API.

Our manufacturing operations are subject to extensive regulatory oversight and could be interrupted at any time. Our Corona, California facility is currently subject to a consent decree of permanent injunction. See Item 1A. Risk Factors Risks Related to Our Business Extensive industry regulation has had, and will continue to have, a significant impact on our business, especially our product development, manufacturing and distribution capabilities. Also refer to *Legal Matters* in NOTE 15 Commitments and Contingencies in the accompanying Notes to Consolidated Financial Statements in this Annual Report.

We contract with third parties for the manufacture of certain of our products, some of which are currently available only from sole or limited suppliers. These third-party manufactured products include products that have historically accounted for a significant portion of our revenues, such as Ferrlecit ®, bupropion hydrochloride sustained-release tablets and a number of our oral contraceptive products. Third-party manufactured products accounted for approximately 58%, 57% and 58% of our product net revenues in 2008, 2007 and 2006, respectively, and 56%, 56% and 64% of our gross profit in 2008, 2007 and 2006, respectively.

We are dependent on third parties for the supply of the raw materials necessary to develop and manufacture our products, including the API and inactive pharmaceutical ingredients used in our products. We are required to identify the supplier(s) of all the raw materials for our products in the drug applications that we file with the FDA. If raw materials for a particular product become unavailable from an approved supplier specified in a drug application, we would be required to qualify a substitute supplier with the FDA, which would likely interrupt manufacturing of the affected product. To the extent practicable, we attempt to identify more than one supplier in each drug application. However, some raw materials are available only from a single source and, in some of our drug applications, only one supplier of raw materials has been identified, even in instances where multiple sources exist.

In addition, we obtain a significant portion of our raw materials from foreign suppliers. Arrangements with international raw material suppliers are subject to, among other things, FDA regulation, customs clearance, various import duties, foreign currency risk and other government clearances. Acts of governments outside the U.S. may affect the price or availability of raw materials needed for the development or manufacture of our products. In addition, any changes in patent laws in jurisdictions outside the U.S. may make it increasingly difficult to obtain raw materials for R&D prior to the expiration of the applicable U.S. or foreign patents. See Item 1A. Risk Factors Risks Related to Our Business If we are unable to obtain sufficient supplies from key suppliers that in some cases may be the only source of finished products or raw materials, our ability to deliver our products to the market may be impeded. in this Annual Report.

Patents and Proprietary Rights

We believe patent protection of our proprietary products is important to our Brand business. Our success with our brand products will depend, in part, on our ability to obtain, and successfully defend if challenged, patent or other proprietary protection for such products. We currently have a number of U.S. and foreign patents issued or pending. However, the issuance of a patent is not conclusive as to its validity or as to the enforceable scope of the claims of the patent. Accordingly, our patents may not prevent other companies from developing similar or functionally equivalent

products or from successfully challenging the validity of our patents. If our patent applications are not approved or, even if approved, if such patents are circumvented or not upheld in a court of law, our ability to competitively market our patented products and technologies may be significantly reduced. Also, such patents may or may not provide competitive advantages for their respective products or they may be challenged or circumvented by competitors, in which case our ability to commercially market these products may be diminished. From time to time, we may need to obtain licenses to

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patents and other proprietary rights held by third parties to develop, manufacture and market our products. If we are unable to timely obtain these licenses on commercially reasonable terms, our ability to commercially market such products may be inhibited or prevented.

We also rely on trade secrets and proprietary know-how that we seek to protect, in part, through confidentiality agreements with our partners, customers, employees and consultants. It is possible that these agreements will be breached or will not be enforceable in every instance, and we will not have adequate remedies for any such breach. It is also possible that our trade secrets will otherwise become known or independently developed by competitors.

We may find it necessary to initiate litigation to enforce our patent rights, to protect our trade secrets or know-how or to determine the scope and validity of the proprietary rights of others. Litigation concerning patents, trademarks, copyrights and proprietary technologies can often be protracted and expensive and, as with litigation generally, the outcome is inherently uncertain.

Pharmaceutical companies with brand products are increasingly suing companies that produce off-patent forms of their brand name products for alleged patent infringement or other violations of intellectual property rights which may delay or prevent the entry of such a generic product into the market. For instance, when we file an ANDA seeking approval of a generic equivalent to a brand drug, we may certify under the Drug Price Competition and Patent Restoration Act of 1984 (the Hatch-Waxman Act) to the FDA that we do not intend to market our generic drug until any patent listed by the FDA as covering the brand drug has expired, in which case, the ANDA will be approved by the FDA no earlier than the expiration or final finding of invalidity of such patent(s). On the other hand, we could certify that we believe the patent or patents listed as covering the brand drug are invalid and/or will not be infringed by the manufacture, sale or use of our generic form of the brand drug. In that case, we are required to notify the brand product holder or the patent holder that such patent is invalid or is not infringed. If the patent holder sues us for patent infringement within 45 days from receipt of the notice, the FDA is then prevented from approving our ANDA for 30 months after receipt of the notice unless the lawsuit is resolved in our favor in less time or a shorter period is deemed appropriate by a court. In addition, increasingly aggressive tactics employed by brand companies to delay generic competition, including the use of Citizen Petitions and seeking changes to U.S. Pharmacopeia, have increased the risks and uncertainties regarding the timing of approval of generic products.

Litigation alleging infringement of patents, copyrights or other intellectual property rights may be costly and time consuming. See Item 1A. Risk Factors Risks Related to Our Business Third parties may claim that we infringe their proprietary rights and may prevent us from manufacturing and selling some of our products. in this Annual Report.

Because a balanced and fair legislative and regulatory arena is critical to the pharmaceutical industry, we will continue to devote management time and financial resources on government activities. We currently maintain an office and staff a full-time government affairs function in Washington, D.C. that maintains responsibility for keeping abreast of state and federal legislative activities.

Government Regulation and Regulatory Matters

All pharmaceutical manufacturers, including Watson, are subject to extensive, complex and evolving regulation by the federal government, principally the FDA, and to a lesser extent, by the U.S. Drug Enforcement Administration (DEA), Occupational Safety and Health Administration and state government agencies, as well as by varying regulatory agencies in foreign countries where our products or product candidates are being manufactured and/or marketed. The Federal Food, Drug and Cosmetic Act, the Controlled Substances Act and other federal statutes and regulations govern or influence the testing, manufacturing, packing, labeling, storing, record keeping, safety, approval, advertising, promotion, sale and distribution of our products.

FDA approval is required before any dosage form of any new drug, including an off-patent equivalent of a previously approved drug, can be marketed. The process for obtaining governmental approval to manufacture and market pharmaceutical products is rigorous, time-consuming and costly, and the extent to which it may be

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affected by legislative and regulatory developments cannot be predicted. We are dependent on receiving FDA and other governmental approvals prior to manufacturing, marketing and shipping new products. Consequently, there is always the risk the FDA or another applicable agency will not approve our new products, or the rate, timing and cost of obtaining such approvals will adversely affect our product introduction plans or results of operations. See Item 1A. Risk Factors Risks Related to Our Business If we are unable to successfully develop or commercialize new products, our operating results will suffer. and Extensive industry regulation has had, and will continue to have, a significant impact on our business, especially our product development, manufacturing and distribution capabilities. in this Annual Report.

All applications for FDA approval must contain information relating to product formulation, raw material suppliers, stability, manufacturing processes, packaging, labeling and quality control. There are generally two types of applications for FDA approval that would be applicable to our new products:

NDA. We file a NDA when we seek approval for drugs with active ingredients and/or with dosage strengths, dosage forms, delivery systems or pharmacokinetic profiles that have not been previously approved by the FDA. Generally, NDAs are filed for newly developed brand products or for a new dosage form of previously approved drugs.

ANDA. We file an ANDA when we seek approval for off-patent, or generic equivalents of a previously approved drug.

The process required by the FDA before a previously unapproved pharmaceutical product may be marketed in the U.S. generally involves the following:

preclinical laboratory and animal tests;

submission of an investigational new drug application (IND), which must become effective before clinical trials may begin;

adequate and well-controlled human clinical trials to establish the safety and efficacy of the proposed product for its intended use;

submission of a NDA containing the results of the preclinical and clinical trials establishing the safety and efficacy of the proposed product for its intended use; and

FDA approval of a NDA.

Preclinical tests include laboratory evaluation of the product, its chemistry, formulation and stability, as well as animal studies to assess the potential safety and efficacy of the product. For products that require NDA approvals, these preclinical studies and plans for initial human testing are submitted to the FDA as part of an IND, which must become effective before we may begin human clinical trials. The IND automatically becomes effective 30 days after receipt by the FDA unless the FDA, during that 30-day period, raises concerns or questions about the conduct of the trials as outlined in the IND. In such cases, the IND sponsor and the FDA must resolve any outstanding concerns before clinical trials can begin. In addition, an independent Institutional Review Board must provide oversight to review and approve any clinical study at the medical center proposing to conduct the clinical trials.

Human clinical trials are typically conducted in sequential phases:

Phase I. During this phase, the drug is initially introduced into a relatively small number of healthy human subjects or patients and is tested for safety, dosage tolerance, absorption, metabolism, distribution and excretion.

Phase II. This phase involves studies in a limited patient population to identify possible adverse effects and safety risks, to determine the efficacy of the product for specific targeted diseases or conditions, and to determine dosage tolerance and optimal dosage.

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Phase III. When Phase II evaluations demonstrate that a dosage range of the product is effective and has an acceptable safety profile, Phase III trials are undertaken to further evaluate dosage, clinical efficacy and to further test for safety in an expanded patient population at geographically dispersed clinical study sites.

Phase IV. After a drug has been approved by the FDA, Phase IV studies may be conducted to explore additional patient populations, compare the drug to a competitor, or to further study the risks, benefits and optimal use of a drug. These studies may be a requirement as a condition of the initial approval.

The results of product development, preclinical studies and clinical studies are then submitted to the FDA as part of a NDA, for approval of the marketing and commercial shipment of the new product. The NDA drug development and approval process currently averages approximately five to ten years.

FDA approval of an ANDA is required before we may begin marketing an off-patent or generic equivalent of a drug that has been approved under an NDA, or a previously unapproved dosage form of a drug that has been approved under an NDA. The ANDA approval process generally differs from the NDA approval process in that it does not typically require new preclinical and clinical studies; instead, it relies on the clinical studies establishing safety and efficacy conducted for the previously approved NDA drug. The ANDA process, however, typically requires data to show that the ANDA drug is bioequivalent (i.e., therapeutically equivalent) to the previously approved drug. Bioequivalence compares the bioavailability of one drug product with another and, when established, indicates whether the rate and extent of absorption of a generic drug in the body are substantially equivalent to the previously approved drug. Bioavailability establishes the rate and extent of absorption, as determined by the time dependent concentrations of a drug product in the bloodstream needed to produce a therapeutic effect. The ANDA drug development and approval process generally takes less time than the NDA drug development and approval process since the ANDA process does not require new clinical trials establishing the safety and efficacy of the drug product.

Supplemental NDAs or ANDAs are required for, among other things, approval to transfer certain products from one manufacturing site to another and may be under review for a year or more. In addition, certain products may only be approved for transfer once new bioequivalency studies are conducted or other requirements are satisfied.

To obtain FDA approval of both NDAs and ANDAs, our manufacturing procedures and operations must conform to FDA quality system and control requirements generally referred to as current Good Manufacturing Practices (cGMP), as defined in Title 21 of the U.S. Code of Federal Regulations. These regulations encompass all aspects of the production process from receipt and qualification of components to distribution procedures for finished products. They are evolving standards; thus, we must continue to expend substantial time, money and effort in all production and quality control areas to maintain compliance. The evolving and complex nature of regulatory requirements, the broad authority and discretion of the FDA, and the generally high level of regulatory oversight results in the continuing possibility that we may be adversely affected by regulatory actions despite our efforts to maintain compliance with regulatory requirements.

We are subject to the periodic inspection of our facilities, procedures and operations and/or the testing of our products by the FDA, the DEA and other authorities, which conduct periodic inspections to assess compliance with applicable regulations. In addition, in connection with its review of our applications for new products, the FDA conducts pre-approval and post-approval reviews and plant inspections to determine whether our systems and processes comply with cGMP and other FDA regulations. Among other things, the FDA may withhold approval of NDAs, ANDAs or other product applications of a facility if deficiencies are found at that facility. Vendors that supply finished products or components to us that we use to manufacture, package and label products are subject to similar regulation and periodic inspections.

Following such inspections, the FDA may issue notices on Form 483 and Warning Letters that could cause us to modify certain activities identified during the inspection. A Form 483 notice is generally issued at the conclusion of an FDA inspection and lists conditions the FDA investigators believe may violate cGMP or other FDA regulations. FDA guidelines specify that a Warning Letter be issued only for violations of

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regulatory significance for which the failure to adequately and promptly achieve correction may be expected to result in an enforcement action.

Our Corona, California facility is currently subject to a consent decree of permanent injunction. See also Manufacturing, Suppliers and Materials discussion above, Item 1A. Risk Factors Risks Related to Our Business Extensive industry regulation has had, and will continue to have, a significant impact on our business, especially our product development, manufacturing and distribution capabilities. and *Legal Matters* in NOTE 15 Commitments and Contingencies in the accompanying Notes to Consolidated Financial Statements in this Annual Report.

Failure to comply with FDA and other governmental regulations can result in fines, unanticipated compliance expenditures, recall or seizure of products, total or partial suspension of production and/or distribution, suspension of the FDA s review of NDAs, ANDAs or other product application enforcement actions, injunctions and criminal prosecution. Under certain circumstances, the FDA also has the authority to revoke previously granted drug approvals. Although we have internal compliance programs, if these programs do not meet regulatory agency standards or if our compliance is deemed deficient in any significant way, it could have a material adverse effect on us. See Item 1A. Risk Factors Risks Related to Our Business Extensive industry regulation has had, and will continue to have, a significant impact on our business, especially our product development, manufacturing and distribution capabilities. in this Annual Report.

The Generic Drug Enforcement Act of 1992 established penalties for wrongdoing in connection with the development or submission of an ANDA. Under this Act, the FDA has the authority to permanently or temporarily bar companies or individuals from submitting or assisting in the submission of an ANDA, and to temporarily deny approval and suspend applications to market generic drugs. The FDA may also suspend the distribution of all drugs approved or developed in connection with certain wrongful conduct and/or withdraw approval of an ANDA and seek civil penalties. The FDA can also significantly delay the approval of any pending NDA, ANDA or other regulatory submissions under the Fraud, Untrue Statements of Material Facts, Bribery and Illegal Gratuities Policy Act.

Government reimbursement programs include Medicare, Medicaid, TriCare, and State Pharmacy Assistance Programs established according to statute, government regulations and policy. Federal law requires that all pharmaceutical manufacturers, as a condition of having their products receive federal reimbursement under Medicaid, must pay rebates to state Medicaid programs on units of their pharmaceuticals that are dispensed to Medicaid beneficiaries. The required per-unit rebate is currently 11% of the average manufacturer price for products marketed under ANDAs. For products marketed under NDAs, manufacturers are required to rebate the greater of 15.1% of the average manufacturer price, or the difference between the average manufacturer price and the lowest net sales price to a non-government customer during a specified period. In some states, supplemental rebates are additionally required as a condition of including the manufacturer s drug on the state s Preferred Drug List.

The Medicare Prescription Drug, Improvement, and Modernization Act of 2003 (the MMA) requires that manufacturers report data to the Centers for Medicare and Medicaid Services (CMS) on pricing of drugs and biologicals reimbursed under Medicare Part B. These are generally drugs, such as injectable products, that are administered incident to a physician service, and in general are not self-administered. Effective January 1, 2005, average selling price (ASP) became the basis for reimbursement to physicians and suppliers for drugs and biologicals covered under Medicare Part B, replacing the average wholesale price (AWP) provided and published by pricing services. In general, we must comply with all reporting requirements for any drug or biological that is separately reimbursable under Medicare. Watson s Ferrlecit®, INFeD® and Trelstar® products are reimbursed under Medicare Part B and, as a result, we provide ASP data on these products to CMS on a quarterly basis.

Under Part D of the MMA, some Medicare beneficiaries are eligible to obtain subsidized prescription drug coverage from private sector providers. With the January 2006 implementation of the Part D drug benefit, usage of

pharmaceuticals has increased as a result of the expanded access to medicines afforded by the new Medicare prescription drug benefit. However, such sales increases have been offset by increased pricing pressures due to the enhanced purchasing power of the private sector providers who negotiate on behalf of

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Medicare beneficiaries. While it is still difficult to predict the future impact the Medicare prescription drug coverage benefit will have on pharmaceutical companies, it is anticipated that further pricing pressures will continue into 2009 and beyond.

The Deficit Reduction Act of 2005 (DRA) mandated a number of changes in the Medicaid Program. On July 6, 2007, the CMS published the Medicaid Program: Prescription Drugs Final Rule (the Rule) to implement certain sections of the DRA. The Rule provides new requirements for calculating Average Manufacturers Price (AMP) to be used for reimbursing pharmacies that dispense generic drugs under the Medicaid Program, and a schedule to publish monthly and quarterly AMP data on a public web site, beginning in December 2007. The new definition of AMP could significantly reduce pharmacy reimbursement for Medicaid covered drugs, which could adversely impact generic drug manufacturers for a variety of reasons, particularly if pharmacies demand lower prices. The publication of AMP data could disrupt the marketplace for generic drugs because AMP, as calculated under the Rule, does not necessarily represent the actual retail cost of generic drug products. On December 14, 2007, the United States District Court for the District of Columbia issued a preliminary injunction that bars CMS from implementing the Rule, including the AMP data publication provisions and the new requirements for calculating AMP. However, the duration of the injunction is uncertain, and the enforceability of the Rule is still under review by the District Court. If the District or Appellate Court rules in favor of CMS, or if the injunction is lifted and CMS enforces the Rule as currently written, our results of operations, financial condition and cash flows could be materially adversely affected.

There has been enhanced political attention, governmental scrutiny and litigation at the federal and state levels of the prices paid or reimbursed for pharmaceutical products under Medicaid, Medicare and other government programs. See Item 1A. Risk Factors Risks Related to Our Business Investigations of the calculation of average wholesale prices may adversely affect our business. and *Legal Matters* in NOTE 15 Commitments and Contingencies in the accompanying Notes to Consolidated Financial Statements in this Annual Report.

In order to assist us in commercializing products, we have obtained from government authorities and private health insurers and other organizations, such as Health Maintenance Organizations (HMOs) and Managed Care Organizations (MCOs), authorization to receive reimbursement at varying levels for the cost of certain products and related treatments. Third party payers increasingly challenge pricing of pharmaceutical products. The trend toward managed healthcare in the U.S., the growth of organizations such as HMOs and MCOs and legislative proposals to reform healthcare and government insurance programs could significantly influence the purchase of pharmaceutical products, resulting in lower prices and a reduction in product demand. Such cost containment measures and healthcare reform could affect our ability to sell our products and may have a material adverse effect on our business, results of operations, financial condition and cash flows. Due to the uncertainty surrounding reimbursement of newly approved pharmaceutical products, reimbursement may not be available for some of our products. Additionally, any reimbursement granted may not be maintained or limits on reimbursement available from third-party payers may reduce the demand for, or negatively affect the price of, those products.

Federal, state and local laws of general applicability, such as laws regulating working conditions, also govern us. In addition, we are subject, as are all manufacturers generally, to numerous and increasingly stringent federal, state and local environmental laws and regulations concerning, among other things, the generation, handling, storage, transportation, treatment and disposal of toxic and hazardous substances and the discharge of pollutants into the air and water. Environmental permits and controls are required for some of our operations, and these permits are subject to modification, renewal and revocation by the issuing authorities. Our environmental capital expenditures and costs for environmental compliance may increase in the future as a result of changes in environmental laws and regulations or increased manufacturing activities at any of our facilities. We could be adversely affected by any failure to comply with environmental laws, including the costs of undertaking a clean-up at a site to which our wastes were transported.

As part of the MMA, companies are required to file with the U.S. Federal Trade Commission (FTC) and the Department of Justice certain types of agreements entered into between brand and generic pharmaceutical companies related to the manufacture, marketing and sale of generic versions of brand drugs. This

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requirement could affect the manner in which generic drug manufacturers resolve intellectual property litigation and other disputes with brand pharmaceutical companies, and could result generally in an increase in private-party litigation against pharmaceutical companies. The impact of this requirement, and the potential private-party lawsuits associated with arrangements between brand name and generic drug manufacturers, is uncertain and could adversely affect our business. For example, in January 2009 the FTC and the State of California filed a lawsuit against us alleging that our settlement with Solvay related to our ANDA for a generic version of Androgel® is unlawful. In February 2009 several private parties purporting to represent various classes of plaintiffs filed similar lawsuits. Additionally, we have received requests for information, in the form of civil investigative demands or subpoenas, from the FTC, and are subject to ongoing FTC investigations, concerning our settlement with Cephalon related to our ANDA for a generic version of Provigil®, and our agreement with Sandoz to relinquish our Hatch-Waxman Act marketing exclusivity on our ANDA for a 50 mg generic version of Toprol XL®. Any adverse outcome of these investigations or actions could have a material adverse effect on our business, results of operations, financial condition and cash flows. See Item 1A. Risk Factors Risks Related to Our Business Federal regulation of arrangements between manufacturers of brand and generic products could adversely affect our business. Also refer to *Legal Matters* in NOTE 15 Commitments and Contingencies in the accompanying Notes to Consolidated Financial Statements in this Annual Report.

Continuing studies of the proper utilization, safety and efficacy of pharmaceuticals and other health care products are being conducted by industry, government agencies and others. Such studies, which increasingly employ sophisticated methods and techniques, can call into question the utilization, safety and efficacy of previously marketed products and in some cases have resulted, and may in the future result, in the discontinuance of their marketing.

Our Distribution operations and our customers are subject to various regulatory requirements, including requirements from the DEA, FDA, and state boards of pharmacy and city and county health regulators, among others. These include licensing, registration, recordkeeping, security and reporting requirements. In particular, several states and the federal government have begun to enforce anti-counterfeit drug pedigree laws which require the tracking of all transactions involving prescription drugs beginning with the manufacturer, through the supply chain, and down to the pharmacy or other health care provider dispensing or administering prescription drug products. For example, effective July 1, 2006, the Florida Department of Health began enforcement of the drug pedigree requirements for distribution of prescription drugs in the State of Florida. Pursuant to Florida law and regulations, wholesalers and distributors, including our subsidiary, Anda Pharmaceuticals, are required to maintain records documenting the chain of custody of prescription drug products they distribute beginning with the purchase of such products from the manufacturer. These entities are required to provide documentation of the prior transaction(s) to their customers in Florida, including pharmacies and other health care entities. Several other states have proposed or enacted legislation to implement similar or more stringent drug pedigree requirements. In addition, federal law requires that a non-authorized distributor of record must provide a drug pedigree documenting the prior purchase of a prescription drug from the manufacturer or from an authorized distributor of record. In cases where the wholesaler or distributor selling the drug product is not deemed an authorized distributor of record it would need to maintain such records. FDA had announced its intent to impose additional drug pedigree requirements (e.g., tracking of lot numbers and documentation of all transactions) through implementation of drug pedigree regulations which were to have taken effect on December 1, 2006. However, a federal appeals court has issued a preliminary injunction to several wholesale distributors granting an indefinite stay of these regulations pending a challenge to the regulations by these wholesale distributors.

In connection with the acquisition of Andrx Corporation (Andrx) on November 3, 2006 (the Andrx Acquisition), both Watson and Andrx agreed to divest certain overlapping products and abide by the terms of the Decision and Order (the Order) entered by the FTC in December 2006, which includes certain reporting requirements and technical assistance. Failure to abide by the terms of the Order, which expires in December 2016, could result in, among other things, civil penalties.

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Environmental Matters

We are subject to federal, state, local and foreign environmental laws and regulations. We believe that our operations comply in all material respects with applicable environmental laws and regulations in each country where we have a business presence. Although we continue to make capital expenditures for environmental protection, we do not anticipate any significant expenditures in order to comply with such laws and regulations that would have a material impact on our earnings or competitive position. We are not aware of any pending litigation or significant financial obligations arising from current or past environmental practices that are likely to have a material adverse effect on our financial position. We cannot assure you, however, that environmental problems relating to facilities owned or operated by us will not develop in the future, and we cannot predict whether any such problems, if they were to develop, could require significant expenditures on our part. In addition, we are unable to predict what legislation or regulations may be adopted or enacted in the future with respect to environmental protection and waste disposal.

Seasonality

There are no significant seasonal aspects to our business.

Backlog

Due to the relatively short lead-time required to fill orders for our products, backlog of orders is not material to our business.

Employees

As of December 31, 2008, we had approximately 5,070 employees. Of our employees, approximately 670 are engaged in R&D, 1,640 in manufacturing, 990 in quality assurance and quality control, 1,090 in sales, marketing and distribution, and 680 in administration. We believe our relations with our employees are good.

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ITEM 1A. *RISK FACTORS*

CAUTIONARY NOTE REGARDING FORWARD-LOOKING STATEMENTS

Any statements made in this report that are not statements of historical fact or that refer to estimated or anticipated future events are forward-looking statements. We have based our forward-looking statements on management s beliefs and assumptions based on information available to our management at the time these statements are made. Such forward-looking statements reflect our current perspective of our business, future performance, existing trends and information as of the date of this filing. These include, but are not limited to, our beliefs about future revenue and expense levels and growth rates, prospects related to our strategic initiatives and business strategies, including the integration of, and synergies associated with, strategic acquisitions, express or implied assumptions about government regulatory action or inaction, anticipated product approvals and launches, business initiatives and product development activities, assessments related to clinical trial results, product performance and competitive environment, and anticipated financial performance. Without limiting the generality of the foregoing, words such as *may, will, expect, believe, anticipate, intend, could, would, estimate, continue, or pursue,* or the negative or oth thereof or comparable terminology, are intended to identify forward-looking statements. The statements are not guarantees of future performance and involve certain risks, uncertainties and assumptions that are difficult to predict. We caution the reader that these statements are based on certain assumptions, risks and uncertainties, many of which are beyond our control. In addition, certain important factors may affect our actual operating results and could cause such results to differ materially from those expressed or implied by forward-looking statements. We believe the risks and uncertainties discussed under the section entitled Risks Related to Our Business, and other risks and uncertainties detailed herein and from time to time in our SEC filings, may cause our actual results to vary materially than those anticipated in any forward-looking statement.

We disclaim any obligation to publicly update any forward-looking statements, whether as a result of new information, future events or otherwise, except as required by law. This discussion is provided as permitted by the Private Securities Litigation Reform Act of 1995.

Risks Related to Our Business

We operate in a rapidly changing environment that involves a number of risks, some of which are beyond our control. The following discussion highlights some of these risks and others are discussed elsewhere in this annual report. These and other risks could have a material adverse effect on our business, results of operations, financial condition and cash flows.

Risks Associated With Investing In the Business of Watson

Our operating results and financial condition may fluctuate.

Our operating results and financial condition may fluctuate from quarter to quarter and year to year for a number of reasons. The following events or occurrences, among others, could cause fluctuations in our financial performance from period to period:

- development of new competitive products or generics by others;
- the timing and receipt of FDA approvals or lack of approvals;
- difficulties or delays in resolving FDA-observed deficiencies at our manufacturing facilities, which could delay our ability to obtain approvals of pending FDA product applications;

changes in the amount we spend to develop, acquire or license new products, technologies or businesses;

changes in the amount we spend to promote our products;

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delays between our expenditures to acquire new products, technologies or businesses and the generation of revenues from those acquired products, technologies or businesses;

changes in treatment practices of physicians that currently prescribe our products;

changes in reimbursement policies of health plans and other similar health insurers, including changes that affect newly developed or newly acquired products;

changes in laws and regulations concerning reimbursement of pharmaceutical products, including Medicare, Medicaid, and similar state programs;

increases in the cost of raw materials used to manufacture our products;

manufacturing and supply interruptions, including failure to comply with manufacturing specifications;

the effect of economic changes in hurricane and other natural disaster-affected areas;

the impact of third party patents and other intellectual property rights which we may be found to infringe, or may be required to license, and the potential damages or other costs we may be required to pay as a result of a finding that we infringe such intellectual property rights or a decision that we are required to obtain a license to such intellectual property rights;

the mix of products that we sell during any time period;

lower than expected demand for our products;

our responses to price competition;

our ability to successfully integrate and commercialize the products, technologies and businesses we acquire or license, as applicable;

expenditures as a result of legal actions;

market acceptance of our products;

the impairment and write-down of goodwill or other intangible assets;

disposition of our primary products, technologies and other rights;

termination or expiration of, or the outcome of disputes relating to, trademarks, patents, license agreements and other rights;

changes in insurance rates for existing products and the cost of insurance for new products;

general economic and industry conditions, including changes in interest rates affecting returns on cash balances and investments that affect customer demand;

our level of R&D activities;

impairment or write-down of investments;

costs and outcomes of any tax audits or any litigation involving intellectual property, customers or other issues; and

timing of revenue recognition related to licensing agreements and/or strategic collaborations.

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As a result, we believe that period-to-period comparisons of our results of operations are not necessarily meaningful, and these comparisons should not be relied upon as an indication of future performance. The above factors may cause our operating results to fluctuate and adversely affect our financial condition and results of operations.

If we are unable to successfully develop or commercialize new products, our operating results will suffer.

Our future results of operations will depend to a significant extent upon our ability to successfully develop and commercialize new brand and generic products in a timely manner. There are numerous difficulties in developing and commercializing new products, including:

- developing, testing and manufacturing products in compliance with regulatory standards in a timely manner;
- receiving requisite regulatory approvals for such products in a timely manner;
- the availability, on commercially reasonable terms, of raw materials, including API and other key ingredients;
- developing and commercializing a new product is time consuming, costly and subject to numerous factors, including legal actions brought by our competitors, that may delay or prevent the development and commercialization of new products;
- experiencing delays or unanticipated costs; and
- commercializing generic products may be substantially delayed by the listing with the FDA of patents that have the effect of potentially delaying approval of the off-patent product by up to 30 months.

As a result of these and other difficulties, products currently in development by Watson may or may not receive timely regulatory approvals, or approvals at all, necessary for marketing by Watson or other third-party partners. This risk particularly exists with respect to the development of proprietary products because of the uncertainties, higher costs and lengthy time frames associated with research and development of such products and the inherent unproven market acceptance of such products. Additionally, we face heightened risks in connection with our development of extended release or controlled release generic products because of the technical difficulties and regulatory requirements related to such products. If any of our products are not timely approved or, when acquired or developed and approved, cannot be successfully or timely commercialized, our operating results could be adversely affected. We cannot guarantee that any investment we make in developing products will be recouped, even if we are successful in commercializing those products.

Our brand pharmaceutical expenditures may not result in commercially successful products.

Developing and commercializing brand pharmaceutical products is generally more costly than generic products. In the future, we anticipate continuing our product development expenditures for our Brand business segment. For example in November 2008, the FDA accepted for filing an NDA for a six month formulation of our Trelstar® (triptorelin for injection) product for prostate cancer and its review is ongoing. We cannot be sure these or other business expenditures will result in the successful discovery, development or launch of brand products that will prove to be commercially successful or will improve the long-term profitability of our business. If such business expenditures do not result in successful discovery, development or launch of commercially successful brand products our results of operations and financial condition could be materially adversely affected.

Loss of revenues from Ferrlecit®, a significant product, could have a material adverse effect on our results of operations, financial condition and cash flows.

In 2008, Ferrlecit® accounted for approximately 12% of our gross profit.

On March 28, 2008, we received a notice from Sanofi Aventis contending that the distribution agreement and related agreements for Ferrlecit® between certain affiliates of Sanofi Aventis and the Company expire on

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February 18, 2009. Sanofi Aventis also contends it would be entitled to damages and other relief to the extent the Company sells Ferrlecit after February 18, 2009. We contend the distribution agreement and related agreements expire on December 31, 2009. The parties are currently engaged in a binding arbitration proceeding to resolve these disputes. A decision in the arbitration is expected in May 2009. Additionally, the parties are continuing to discuss a possible extension of the distribution agreement and related agreements beyond 2009. However, there can be no assurance that we will be able to negotiate extensions of these agreements on commercially reasonable terms, or at all. Our inability to negotiate extensions of these agreements on commercially reasonable terms, or an adverse finding in the pending arbitration proceeding, could have a material adverse effect on our business, results of operations, financial condition and cash flows.

Even if we succeed in the pending arbitration and/or are able to extend our agreements with Sanofi Aventis beyond 2009, we lost regulatory exclusivity on our Ferrlecit® product in 2004 and, as a result generic applicants became eligible to submit ANDAs for Ferrlecit®. In February 2004, we submitted a Citizen Petition to the FDA requesting that the FDA not approve any ANDA for a generic version of Ferrlecit® until certain manufacturing, physiochemical and safety and efficacy criteria are satisfied. During the third quarter of 2004, we submitted a second Citizen Petition to the FDA requesting that the FDA refuse to accept for substantive review any ANDA referencing Ferrlecit® until the FDA establishes guidelines for determining whether the generic product is the same complex as Ferrlecit®. In October 2006, we submitted a supplement to our Citizen Petition, reiterating our request for the FDA to establish guidelines for determining what data are needed to prove that generic formulations of Ferrlecit® contain the same active complex as Ferrlecit®. We cannot predict whether the FDA will grant or deny our Citizen Petitions or when it may take such action.

In addition to risks associated with generic competition, we are aware of competitors that are developing proprietary products that could compete with Ferrlecit®. These companies may succeed in developing technologies and products that are considered safer or more efficacious, or are less costly than Ferrlecit®.

If a generic version of Ferrlecit® or other competitive product is approved by the FDA and enters the market, our net revenues and profits could significantly decline, which could have a material adverse effect on our results of operations, financial condition and cash flows.

A large percentage of our Ferrlecit® sales are made to dialysis centers. In recent years, there has been significant consolidation of the dialysis business, marked by mergers and acquisitions among dialysis centers. As a result, a small number of customers control a significant share of the injectable iron market in which Ferrlecit® competes. Continued consolidation may adversely impact pricing and create other competitive pressures on suppliers of injectable iron.

During 2008, our largest customer for Ferrlecit® accounted for approximately 37% of our Ferrlecit® sales. During 2008 that customer became the exclusive U.S. licensee of Venofer, a product that directly competes with Ferrlecit®. If we are not able to maintain our Ferrlecit® business with our largest customer, or if we lose any other significant Ferrlecit® customer, our business, results of operations, financial condition and cash flows could be materially adversely affected.

Any acquisitions of technologies, products and businesses, may be difficult to integrate, could adversely affect our relationships with key customers, and/or could result in significant charges to earnings.

We regularly review potential acquisitions of technologies, products and businesses complementary to our business. Acquisitions typically entail many risks and could result in difficulties in integrating operations, personnel, technologies and products. If we are not able to successfully integrate our acquisitions, we may not obtain the advantages and synergies that the acquisitions were intended to create, which may have a material adverse effect on our business, results of operations, financial condition and cash flows, our ability to develop and introduce new

products and the market price of our stock. In addition, in connection with acquisitions, we could experience disruption in our business, technology and information systems, customer or employee base, including diversion of management s attention from our continuing operations. There is also a risk that key employees of companies that we acquire or key employees necessary to successfully commercialize technologies and products that we acquire may seek employment elsewhere, including with our competitors. Furthermore, there may be overlap between the products or customers of Watson and the companies that we

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acquire that may create conflicts in relationships or other commitments detrimental to the integrated businesses. For example, in our Distribution business, our main competitors are McKesson Corporation, AmerisourceBergen Corporation and Cardinal Health, Inc. These companies are significant customers of our Generic and Brand operations and who collectively accounted for approximately 28% of our annual net revenues in 2008. Our activities related to our Distribution business, as well as the acquisition of other businesses that compete with our customers, may result in the disruption of our business, which could harm relationships with our current customers, employees or suppliers, and could adversely affect our expenses, pricing, third-party relationships and revenues.

In addition, as a result of acquiring businesses or products, or entering into other significant transactions, we have experienced, and will likely continue to experience, significant charges to earnings for merger and related expenses. These costs may include substantial fees for investment bankers, attorneys, accountants and financial printing costs and severance and other closure costs associated with the elimination of duplicate or discontinued products, operations and facilities. Charges that we may incur in connection with acquisitions could adversely affect our results of operations for particular quarterly or annual periods.

If we are unsuccessful in our joint ventures and other collaborations, our operating results could suffer.

We have made substantial investments in joint ventures and other collaborations and may use these and other methods to develop or commercialize products in the future. These arrangements typically involve other pharmaceutical companies as partners that may be competitors of ours in certain markets. In many instances, we will not control these joint ventures or collaborations or the commercial exploitation of the licensed products, and cannot assure you that these ventures will be profitable. Although restrictions contained in certain of these programs have not had a material adverse impact on the marketing of our own products to date, any such marketing restrictions could affect future revenues and have a material adverse effect on our operations. Our results of operations may suffer if existing joint venture or collaboration partners withdraw, or if these products are not timely developed, approved or successfully commercialized.

If we are unable to adequately protect our technology or enforce our patents, our business could suffer.

Our success with the brand products that we develop will depend, in part, on our ability to obtain patent protection for these products. We currently have a number of U.S. and foreign patents issued and pending. However, issuance of a patent is not conclusive evidence of its validity or enforceability. We cannot be sure that we will receive patents for any of our pending patent applications or any patent applications we may file in the future, or that our issued patents will be upheld if challenged. For example, in September, 2008, we received notice that Duramed Pharmaceuticals had filed an ANDA seeking to market a generic version of our Oxytrol product, and contending that our patents covering Oxytrol are invalid or not infringed. If our current and future patent applications are not approved or, if approved, our patents are not upheld in a court of law if challenged, it may reduce our ability to competitively exploit our patented products. Also, such patents may or may not provide competitive advantages for their respective products or they may be challenged or circumvented by our competitors, in which case our ability to commercially market these products may be diminished.

We also rely on trade secrets and proprietary know-how that we seek to protect, in part, through confidentiality agreements with our partners, customers, employees and consultants. It is possible that these agreements will be breached or that they will not be enforceable in every instance, and that we will not have adequate remedies for any such breach. It is also possible that our trade secrets will become known or independently developed by our competitors.

If we are unable to adequately protect our technology, trade secrets or propriety know-how, or enforce our patents, our results of operations, financial condition and cash flows could suffer.

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If pharmaceutical companies are successful in limiting the use of generics through their legislative, regulatory and other efforts, our sales of generic products may suffer.

Many pharmaceutical companies increasingly have used state and federal legislative and regulatory means to delay generic competition. These efforts have included:

pursuing new patents for existing products which may be granted just before the expiration of one patent, which could extend patent protection for additional years or otherwise delay the launch of generics;

selling the brand product as an Authorized Generic, either by the brand company directly, through an affiliate or by a marketing partner;

using the Citizen Petition process to request amendments to FDA standards;

seeking changes to U.S. Pharmacopeia, an organization which publishes industry recognized compendia of drug standards;

attaching patent extension amendments to non-related federal legislation;

engaging in state-by-state initiatives to enact legislation that restricts the substitution of some generic drugs, which could have an impact on products that we are developing; and

seeking patents on methods of manufacturing certain API.

If pharmaceutical companies or other third parties are successful in limiting the use of generic products through these or other means, our sales of generic products may decline. If we experience a material decline in generic product sales, our results of operations, financial condition and cash flows will suffer.

If competitors are successful in limiting competition for certain generic products through their legislative, regulatory and litigation efforts, our sales of certain generic products may suffer.

Certain of our competitors have recently challenged our ability to distribute Authorized Generics during the competitors 180-day period of ANDA exclusivity under the Hatch-Waxman Act. Under the challenged arrangements, we have obtained rights to market and distribute under a brand manufacturer s NDA a generic alternative of the brand product. Some of our competitors have challenged the propriety of these arrangements by filing Citizen Petitions with the FDA, initiating lawsuits alleging violation of the antitrust and consumer protection laws, and seeking legislative intervention. The FDA and courts that have considered the subject to date have ruled that there is no prohibition in the Federal Food, Drug, and Cosmetic Act against distributing Authorized Generic versions of a brand drug. However, on February 3, 2009, legislation was introduced in the U.S. Senate that would prohibit the marketing of Authorized Generics during the 180-day period of ANDA exclusivity under the Hatch-Waxman Act. Further, the DRA added provisions to the Medicaid Rebate Program that, effective January 1, 2007, may have the effect of increasing an NDA holder s Medicaid Rebate liability if it permits another manufacturer to market an Authorized Generic version of its brand product. This may affect the willingness of brand manufacturers to continue arrangements, or enter into future arrangements, permitting us to market Authorized Generic versions of their brand products. If so, or if distribution of Authorized Generic versions of brand products is otherwise restricted or found unlawful, our results of operations, financial condition and cash flows could be materially adversely affected.

From time to time we may need to rely on licenses to proprietary technologies, which may be difficult or expensive to obtain.

We may need to obtain licenses to patents and other proprietary rights held by third parties to develop, manufacture and market products. If we are unable to timely obtain these licenses on commercially reasonable terms, our ability to commercially market our products may be inhibited or prevented, which could have a material adverse effect on our business, results of operations, financial condition and cash flows.

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Third parties may claim that we infringe their proprietary rights and may prevent us from manufacturing and selling some of our products.

The manufacture, use and sale of new products that are the subject of conflicting patent rights have been the subject of substantial litigation in the pharmaceutical industry. These lawsuits relate to the validity and infringement of patents or proprietary rights of third parties. We may have to defend against charges that we violated patents or proprietary rights of third parties. This is especially true in the case of generic products on which the patent covering the brand product is expiring, an area where infringement litigation is prevalent, and in the case of new brand products where a competitor has obtained patents for similar products. Litigation may be costly and time-consuming, and could divert the attention of our management and technical personnel. In addition, if we infringe on the rights of others, we could lose our right to develop, manufacture or market products or could be required to pay monetary damages or royalties to license proprietary rights from third parties. For example, in August 2008 the United States District Court for the Southern District of Florida ruled that our naproxen sodium product infringes Elan U.S. Patent Number 5,637,320, and that the infringement was willful. We are also engaged in litigation with Duramed Pharmaceuticals concerning whether our Quasense[tm] product infringes Duramed s U.S. Patent Number RE 39,861, and we continue to manufacture and market our Quasense[tm] product during the pendency of the litigation. Although the parties to patent and intellectual property disputes in the pharmaceutical industry have often settled their disputes through licensing or similar arrangements, the costs associated with these arrangements may be substantial and could include ongoing royalties. Furthermore, we cannot be certain that the necessary licenses would be available to us on commercially reasonable terms, or at all. As a result, an adverse determination in a judicial or administrative proceeding or failure to obtain necessary licenses could prevent us from manufacturing and selling a number of our products, and could have a material adverse effect on our business, results of operations, financial condition and cash flows.

Our distribution operations are highly dependent upon a primary courier service.

Product deliveries within our Distribution business are highly dependent on overnight delivery services to deliver our products in a timely and reliable manner, typically by overnight service. Our Distribution business ships a substantial portion of products via one courier s air and ground delivery service. If the courier terminates our contract with this courier or we cannot renew the courier s contract on favorable terms or enter into a contract with an equally reliable overnight courier to perform and offer the same service level at similar or more favorable rates, our business, results of operations, financial condition and cash flows could be materially adversely affected.

Our distribution operations concentrate on generic products and therefore are subject to the risks of the generic industry.

The ability of our Distribution business to provide consistent, sequential quarterly growth is affected, in large part, by our participation in the launch of new products by generic manufacturers and the subsequent advent and extent of competition encountered by these products. This competition can result in significant and rapid declines in pricing with a corresponding decrease in net sales of our Distribution business. Our margins can also be affected by the risks inherent to the generic industry, which are discussed below under Risks Relating To Investing In the Pharmaceutical Industry .

If we are unable to obtain sufficient supplies from key manufacturing sites or suppliers that in some cases may be the only source of finished products or raw materials, our ability to deliver our products to the market may be impeded.

We are required to identify the supplier(s) of all the raw materials for our products in our applications with the FDA. To the extent practicable, we attempt to identify more than one supplier in each drug application. However, some products and raw materials are available only from a single source and, in some of our drug applications, only one

supplier of products and raw materials or site of manufacture has been identified, even in instances where multiple sources exist. Some of these products have historically accounted

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for a significant portion of our revenues, such as Ferrlecit®, INFed®, bupropion sustained release tablets and a significant number of our oral contraceptive products. From time to time, certain of our manufacturing sites or outside suppliers have experienced regulatory or supply-related difficulties that have inhibited their ability to deliver products and raw materials to us, causing supply delays or interruptions. To the extent any difficulties experienced by our manufacturing sites or suppliers cannot be resolved or extensions of our key supply agreements cannot be negotiated within a reasonable time and on commercially reasonable terms, or if raw materials for a particular product become unavailable from an approved supplier and we are required to qualify a new supplier with the FDA, or if we are unable to do so, our profit margins and market share for the affected product could decrease or be eliminated, as well as delay our development and sales and marketing efforts. Such outcomes could have a material adverse effect on our business, results of operations, financial condition and cash flows.

Our manufacturing sites in India and our arrangements with foreign suppliers are subject to certain additional risks, including the availability of government clearances, export duties, political instability, war, acts of terrorism, currency fluctuations and restrictions on the transfer of funds. For example, we obtain a significant portion of our raw materials from foreign suppliers. Arrangements with international raw material suppliers are subject to, among other things, FDA regulation, customs clearances, various import duties and other government clearances, as well as potential shipping delays due to inclement weather, strikes or other matters outside of our control. Acts of governments outside the U.S. may affect the price or availability of raw materials needed for the development or manufacture of our products. In addition, recent changes in patent laws in jurisdictions outside the U.S. may make it increasingly difficult to obtain raw materials for R&D prior to the expiration of the applicable U.S. or foreign patents.

Our policies regarding returns, allowances and chargebacks, and marketing programs adopted by wholesalers, may reduce our revenues in future fiscal periods.

Consistent with industry practice we, like many generic product manufacturers, have liberal return policies and have been willing to give customers post-sale inventory allowances. Under these arrangements, from time to time, we may give our customers credits on our generic products that our customers hold in inventory after we have decreased the market prices of the same generic products. Therefore, if new competitors enter the marketplace and significantly lower the prices of any of their competing products, we may reduce the price of our product. As a result, we may be obligated to provide significant credits to our customers who are then holding inventories of such products, which could reduce sales revenue and gross margin for the period the credit is provided. Like our competitors, we also give credits for chargebacks to wholesale customers that have contracts with us for their sales to hospitals, group purchasing organizations, pharmacies or other retail customers. A chargeback represents an amount payable in the future to a wholesaler for the difference between the invoice price paid to us by our wholesale customer for a particular product and the negotiated contract price that the wholesaler s customer pays for that product. Although we establish reserves based on our prior experience and our best estimates of the impact that these policies may have in subsequent periods, we cannot ensure that our reserves are adequate or that actual product returns, allowances and chargebacks will not exceed our estimates, which could have a material adverse effect on our results of operations, financial condition, cash flows and the market price of our stock.

Investigations of the calculation of average wholesale prices may adversely affect our business.

Many government and third-party payers, including Medicare, Medicaid, HMOs and MCOs, have historically reimbursed, or continue to reimburse, doctors and others for the purchase of certain prescription drugs based on a drug s AWP. In the past several years, state and federal government agencies have conducted ongoing investigations of manufacturers reporting practices with respect to AWP, in which they have suggested that reporting of inflated AWP s have led to excessive payments for prescription drugs. For example, beginning in July 2002, we and certain of our subsidiaries, as well as numerous other pharmaceutical companies, were named as defendants in various state and federal court actions alleging improper or fraudulent practices related to the reporting of AWP of certain products, and

other improper acts, in order to increase prices and market shares. Additional actions are anticipated. These actions, if successful, could adversely

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affect us and may have a material adverse effect on our business, results of operations, financial condition and cash flows. See *Legal Matters* in NOTE 15 Commitments and Contingencies in the accompanying Notes to Consolidated Financial Statements in this Annual Report.

The design, development, manufacture and sale of our products involves the risk of product liability claims by consumers and other third parties, and insurance against such potential claims is expensive and may be difficult to obtain.

The design, development, manufacture and sale of our products involve an inherent risk of product liability claims and the associated adverse publicity. Insurance coverage is expensive and may be difficult to obtain, and may not be available in the future on acceptable terms, or at all. If the coverage limits for product liability insurance policies are not adequate, a claim brought against Watson, whether covered by insurance or not, could have a material adverse effect on our business, results of operations, financial condition and cash flows.

The loss of our key personnel could cause our business to suffer.

The success of our present and future operations will depend, to a significant extent, upon the experience, abilities and continued services of key personnel. For example, although we have other senior management personnel, a significant loss of the services of Paul Bisaro, our Chief Executive Officer, or other senior executive officers without hiring a suitable successor, could cause our business to suffer. We cannot assure you that we will be able to attract and retain key personnel. We have entered into employment agreements with the majority of our senior executive officers but such agreements do not guarantee that our senior executive officers will remain employed by us for a significant period of time, or at all. We do not carry key-man life insurance on any of our officers.

Rising insurance costs could negatively impact profitability.

The cost of insurance, including workers compensation, product liability and general liability insurance, can increase significantly in a given period and may increase in the future. In response, we may increase deductibles and/or decrease certain lines of coverage to mitigate these costs. These increases, and our increased risk due to increased deductibles and reduced lines of coverage, could have a negative impact on our results of operations, financial condition and cash flows.

Significant balances of intangible assets, including product rights and goodwill acquired, are subject to impairment testing and may result in impairment charges, which will adversely affect our results of operations and financial condition.

A significant amount of our total assets is related to acquired intangibles and goodwill. As of December 31, 2008, the carrying value of our product rights and other intangible assets was approximately $560 million and the carrying value of our goodwill was approximately $868 million.

Our product rights are stated at cost, less accumulated amortization. We determine original fair value and amortization periods for product rights based on our assessment of various factors impacting estimated useful lives and cash flows of the acquired products. Such factors include the product s position in its life cycle, the existence or absence of like products in the market, various other competitive and regulatory issues and contractual terms. Significant adverse changes to any of these factors would require us to perform an impairment test on the affected asset and, if evidence of impairment exists, we would be required to take an impairment charge with respect to the asset. Such a charge could have a material adverse effect on our results of operations and financial condition.

Our other significant intangible assets include acquired core technology and customer relationships, which are intangible assets with definite lives, and the Anda trade name, which is an intangible asset with an indefinite life, as we intend to use the Anda trade name indefinitely.

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Our acquired core technology and customer relationship intangible assets are stated at cost, less accumulated amortization. We determined the original fair value of our other intangible assets by performing a discounted cash flow analysis, which is based on our assessment of various factors. Such factors include existing operating margins, the number of existing and potential competitors, product pricing patterns, product market share analysis, product approval and launch dates, the effects of competition, customer attrition rates, consolidation within the industry and generic product lifecycle estimates. Our other intangible assets with definite lives are tested for impairment when there are significant changes to any of these factors. Our other intangible assets with indefinite lives are tested for impairment annually, or more frequently if there are significant changes to any of the above factors. If evidence of impairment exists, we would be required to take an impairment charge with respect to the impaired asset. Such a charge could have a material adverse effect on our results of operations and financial condition.

Goodwill and our Anda trade name intangible asset are tested for impairment annually and when events occur or circumstances change that could potentially reduce the fair value of the reporting unit or intangible asset. Impairment testing compares the fair value of the reporting unit or intangible asset to its carrying amount. A goodwill or trade name impairment, if any, would be recorded in operating income and could have a material adverse effect on our results of operations and financial condition.

We may need to raise additional funds in the future which may not be available on acceptable terms or at all.

We may consider issuing additional debt or equity securities in the future to fund potential acquisitions or investments, to refinance existing debt, or for general corporate purposes. If we issue equity or convertible debt securities to raise additional funds, our existing stockholders may experience dilution, and the new equity or debt securities may have rights, preferences and privileges senior to those of our existing stockholders. If we incur additional debt, it may increase our leverage relative to our earnings or to our equity capitalization, requiring us to pay additional interest expenses. We may not be able to market such issuances on favorable terms, or at all, in which case, we may not be able to develop or enhance our products, execute our business plan, take advantage of future opportunities, or respond to competitive pressures or unanticipated customer requirements.

Our business could suffer as a result of manufacturing difficulties or delays.

The manufacture of certain of our products and product candidates, particularly our controlled-release products, transdermal products, and our oral contraceptive products, are more difficult than the manufacture of immediate-release products. Successful manufacturing of these types of products requires precise manufacturing process controls, API that conforms to very tight tolerances for specific characteristics and equipment that operates consistently within narrow performance ranges. Manufacturing complexity, testing requirements, and safety and security processes combine to increase the overall difficulty of manufacturing these products and resolving manufacturing problems that we may encounter.

Our manufacturing and other processes utilize sophisticated equipment, which sometimes require a significant amount of time to obtain and install. Our business could suffer if certain manufacturing or other equipment, or a portion or all of our facilities were to become inoperable for a period of time. This could occur for various reasons, including catastrophic events such as earthquake, hurricane or explosion, unexpected equipment failures or delays in obtaining components or replacements thereof, as well as construction delays or defects and other events, both within and outside of our control. Our inability to timely manufacture any of our significant products could have a material adverse effect on our results of operations, financial condition and cash flows.

Our business will continue to expose us to risks of environmental liabilities.

Our product and API development programs, manufacturing processes and distribution logistics involve the controlled use of hazardous materials, chemicals and toxic compounds in our owned and leased facilities. As a result, we are subject to numerous and increasingly stringent federal, state and local environmental laws

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and regulations concerning, among other things, the generation, handling, storage, transportation, treatment and disposal of toxic and hazardous materials and the discharge of pollutants into the air and water. Our programs and processes expose us to risks that an accidental contamination could result in (i) our noncompliance with such environmental laws and regulations and (ii) regulatory enforcement actions or claims for personal injury and property damage against us. If an accident or environmental discharge occurs, or if we discover contamination caused by prior operations, including by prior owners and operators of properties we acquire, we could be liable for cleanup obligations, damages and fines. The substantial unexpected costs we may incur could have a material and adverse effect on our business, results of operations, financial condition, and cash flows. In addition, environmental permits and controls are required for some of our operations, and these permits are subject to modification, renewal and revocation by the issuing authorities. Any modification, revocation or non-renewal of our environmental permits could have a material adverse effect on our ongoing operations, business and financial condition. Our environmental capital expenditures and costs for environmental compliance may increase in the future as a result of changes in environmental laws and regulations or increased development or manufacturing activities at any of our facilities.

Global Economic Conditions Could Harm Us.

Recent global market and economic conditions have been unprecedented and challenging with tighter credit conditions and recession in most major economies continuing into 2009. Continued concerns about the systemic impact of potential long-term and wide-spread recession, energy costs, geopolitical issues, the availability and cost of credit, and the global housing and mortgage markets have contributed to increased market volatility and diminished expectations for western and emerging economies. In the second half of 2008, added concerns fueled by the U.S. government conservatorship of the Federal Home Loan Mortgage Corporation and the Federal National Mortgage Association, the declared bankruptcy of Lehman Brothers Holdings Inc., the U.S. government financial assistance to American International Group Inc., Citibank, Bank of America and other federal government interventions in the U.S. financial system lead to increased market uncertainty and instability in both U.S. and international capital and credit markets. These conditions, combined with volatile oil prices, declining business and consumer confidence and increased unemployment, have contributed to volatility of unprecedented levels.

As a result of these market conditions, the cost and availability of credit has been and may continue to be adversely affected by illiquid credit markets and wider credit spreads. Concern about the stability of the markets generally and the strength of counterparties specifically has led many lenders and institutional investors to reduce, and in some cases, cease to provide credit to businesses and consumers. These factors have lead to a decrease in spending by businesses and consumers alike, and a corresponding decrease in global infrastructure spending. Continued turbulence in the U.S. and international markets and economies and prolonged declines in business consumer spending may adversely affect our liquidity and financial condition, and the liquidity and financial condition of our customers, including our ability to refinance maturing liabilities and access the capital markets to meet liquidity needs.

Risks Relating To Investing In the Pharmaceutical Industry

Extensive industry regulation has had, and will continue to have, a significant impact on our business, especially our product development, manufacturing and distribution capabilities.

All pharmaceutical companies, including Watson, are subject to extensive, complex, costly and evolving regulation by the federal government, principally the FDA and to a lesser extent by the DEA and state government agencies, as well as by varying regulatory agencies in foreign countries where products or product candidates are being manufactured and/or marketed. The Federal Food, Drug and Cosmetic Act, the Controlled Substances Act and other federal statutes and regulations govern or influence the testing, manufacturing, packing, labeling, storing, record keeping, safety, approval, advertising, promotion, sale and distribution of our products.

Under these regulations, we are subject to periodic inspection of our facilities, procedures and operations and/or the testing of our products by the FDA, the DEA and other authorities, which conduct periodic

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inspections to confirm that we are in compliance with all applicable regulations. In addition, the FDA conducts pre-approval and post-approval reviews and plant inspections to determine whether our systems and processes are in compliance with cGMP and other FDA regulations. Following such inspections, the FDA may issue notices on Form 483 and Warning Letters that could cause us to modify certain activities identified during the inspection. A Form 483 notice is generally issued at the conclusion of a FDA inspection and lists conditions the FDA inspectors believe may violate cGMP or other FDA regulations. FDA guidelines specify that a Warning Letter is issued only for violations of regulatory significance for which the failure to adequately and promptly achieve correction may be expected to result in an enforcement action.

Our manufacturing facility in Corona, California (which manufactured products representing approximately 12% of our total product net revenues for 2008) is currently subject to a consent decree of permanent injunction. We cannot assure that the FDA will determine we have adequately corrected deficiencies at our Corona manufacturing site, that subsequent FDA inspections at any of our manufacturing sites will not result in additional inspectional observations at such sites, that approval of any of the pending or subsequently submitted NDAs, ANDAs or supplements to such applications by Watson or our subsidiaries will be granted or that the FDA will not seek to impose additional sanctions against Watson or any of its subsidiaries. The range of possible sanctions includes, among others, FDA issuance of adverse publicity, product recalls or seizures, fines, total or partial suspension of production and/or distribution, suspension of the FDA s review of product applications, enforcement actions, injunctions, and civil or criminal prosecution. Any such sanctions, if imposed, could have a material adverse effect on our business, operating results, financial condition and cash flows. Under certain circumstances, the FDA also has the authority to revoke previously granted drug approvals. Similar sanctions as detailed above may be available to the FDA under a consent decree, depending upon the actual terms of such decree. Although we have instituted internal compliance programs, if these programs do not meet regulatory agency standards or if compliance is deemed deficient in any significant way, it could materially harm our business. Certain of our vendors are subject to similar regulation and periodic inspections.

The process for obtaining governmental approval to manufacture and market pharmaceutical products is rigorous, time-consuming and costly, and we cannot predict the extent to which we may be affected by legislative and regulatory developments. We are dependent on receiving FDA and other governmental or third-party approvals prior to manufacturing, marketing and shipping our products. Consequently, there is always the chance that we will not obtain FDA or other necessary approvals, or that the rate, timing and cost of obtaining such approvals, will adversely affect our product introduction plans or results of operations. We carry inventories of certain product(s) in anticipation of launch, and if such product(s) are not subsequently launched, we may be required to write off the related inventory.

Our Distribution operations and our customers are subject to various regulatory requirements, including requirements from the DEA, FDA, state boards of pharmacy and city and county health regulators, among others. These include licensing, registration, recordkeeping, security and reporting requirements. In particular, several states and the federal government have begun to enforce anti-counterfeit drug pedigree laws which require the tracking of all transactions involving prescription drugs beginning with the manufacturer, through the supply chain, and down to the pharmacy or other health care provider dispensing or administering prescription drug products. For example, effective July 1, 2006, the Florida Department of Health, began enforcement of the drug pedigree requirements for distribution of prescription drugs in the State of Florida. Pursuant to Florida law and regulations, wholesalers and distributors, including our subsidiary, Anda Pharmaceuticals, are required to maintain records documenting the chain of custody of prescription drug products they distribute beginning with the purchase of products from the manufacturer. These entities are required to provide documentation of the prior transaction(s) to their customers in Florida, including pharmacies and other health care entities. Several other states have proposed or enacted legislation to implement similar or more stringent drug pedigree requirements. In addition, federal law requires that a non-authorized distributor of record must provide a drug pedigree documenting the prior purchase of a prescription drug from the manufacturer or from an authorized distributor of record. In cases where the wholesaler or distributor selling the drug product is not deemed an authorized distributor of record it would need to maintain such records. FDA had announced

its intent to impose additional drug pedigree requirements (e.g., tracking of lot numbers

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and documentation of all transactions) through implementation of drug pedigree regulations which were to have taken effect on December 1, 2006. However, a federal appeals court has issued a preliminary injunction to several wholesale distributors granting an indefinite stay of these regulations pending a challenge to the regulations by these wholesale distributors.

Federal regulation of arrangements between manufacturers of brand and generic products could adversely affect our business.

As part of the MMA, companies are required to file with the FTC and the Department of Justice certain types of agreements entered into between brand and generic pharmaceutical companies related to the manufacture, marketing and sale of generic versions of brand drugs. This requirement could affect the manner in which generic drug manufacturers resolve intellectual property litigation and other disputes with brand pharmaceutical companies and could result generally in an increase in private-party litigation against pharmaceutical companies or additional investigations or proceedings by the FTC or other governmental authorities. The impact of this requirement, and the potential private-party lawsuits associated with arrangements between brand name and generic drug manufacturers, is uncertain and could adversely affect our business. For example, in January 2009 the FTC and the State of California filed a lawsuit against us alleging that our settlement with Solvay related to our ANDA for a generic version of Androgel® is unlawful. In February 2009 several private parties purporting to represent various classes of plaintiffs filed similar lawsuits. Additionally, we have received requests for information, in the form of civil investigative demands or subpoenas, from the FTC, and are subject to ongoing FTC investigations, concerning our settlement with Cephalon related to our ANDA for a generic version of Provigil®, and our agreement with Sandoz to relinquish our Hatch-Waxman marketing exclusivity on our ANDA for a 50 mg. generic version of Toprol XL®. Any adverse outcome of these actions or investigations, or actions or investigations related to other settlements we have entered into, could have a material adverse effect on our business, results of operations, financial condition and cash flows.

Healthcare reform and a reduction in the reimbursement levels by governmental authorities, HMOs, MCOs or other third-party payers may adversely affect our business.

In order to assist us in commercializing products, we have obtained from government authorities and private health insurers and other organizations, such as HMOs and MCOs, authorization to receive reimbursement at varying levels for the cost of certain products and related treatments. Third-party payers increasingly challenge pricing of pharmaceutical products. The trend toward managed healthcare in the U.S., the growth of organizations such as HMOs and MCOs and legislative proposals to reform healthcare and government insurance programs could significantly influence the purchase of pharmaceutical products, resulting in lower prices and a reduction in product demand. Such cost containment measures and healthcare reform could affect our ability to sell our products and could have a material adverse effect on our business, results of operations, financial condition and cash flows. Additionally, there is uncertainty surrounding the implementation of the provisions of Part D of the MMA, and the possibility that such provisions will be amended. Depending on how such provisions are implemented or amended, reimbursement may not be available for some of Watson s products. Additionally, any reimbursement granted may not be maintained or limits on reimbursement available from third-party payers may reduce the demand for, or negatively affect the price of, those products and could have a material adverse effect on our business, results of operations, financial condition and cash flows. We may also be subject to lawsuits relating to reimbursement programs that could be costly to defend, divert management s attention and adversely affect our operating results.

The pharmaceutical industry is highly competitive.

We face strong competition in both our Generic and Brand product businesses. The intensely competitive environment requires an ongoing, extensive search for technological innovations and the ability to market products effectively, including the ability to communicate the effectiveness, safety and value of brand products to healthcare professionals

in private practice, group practices and MCOs. Our competitors vary depending upon product categories, and within each product category, upon dosage strengths and drug-delivery systems.

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Based on total assets, annual revenues, and market capitalization, we are smaller than certain of our national and international competitors in the brand product arena. Most of our competitors have been in business for a longer period of time than Watson, have a greater number of products on the market and have greater financial and other resources than we do. If we directly compete with them for the same markets and/or products, their financial strength could prevent us from capturing a profitable share of those markets. It is possible that developments by our competitors will make our products or technologies noncompetitive or obsolete.

Revenues and gross profit derived from the sales of generic pharmaceutical products tend to follow a pattern based on certain regulatory and competitive factors. As patents for brand name products and related exclusivity periods expire, the first generic manufacturer to receive regulatory approval for generic equivalents of such products is generally able to achieve significant market penetration. As competing off-patent manufacturers receive regulatory approvals on similar products or as brand manufacturers launch generic versions of such products (for which no separate regulatory approval is required), market share, revenues and gross profit typically decline, in some cases dramatically. Accordingly, the level of market share, revenue and gross profit attributable to a particular generic product normally is related to the number of competitors in that product s market and the timing of that product s regulatory approval and launch, in relation to competing approvals and launches. Consequently, we must continue to develop and introduce new products in a timely and cost-effective manner to maintain our revenues and gross margins. Additionally, as new competitors enter the market, there may be increased pricing pressure on certain products, which would result in lower gross margins. This is particularly true in the case of certain Asian and other overseas competitors, who may be able to produce products at costs lower than the costs of domestic manufacturers. If we experience substantial competition from Asian or other overseas competitors with lower production costs, our profit margins will suffer.

We also face strong competition in our Distribution business, where we compete with a number of large wholesalers and other distributors of pharmaceuticals, including McKesson Corporation, AmerisourceBergen Corporation and Cardinal Health, Inc., which market both brand and generic pharmaceutical products to their customers. These companies are significant customers of our pharmaceutical business. As generic products generally have higher gross margins for distributors, each of the large wholesalers, on an increasing basis, are offering pricing incentives on brand products if the customers purchase a large portion of their generic pharmaceutical products from the primary wholesaler. As we do not offer a full line of brand products to our customers, we are at times competitively disadvantaged and must compete with these wholesalers based upon our very competitive pricing for generic products, greater service levels and our well-established telemarketing relationships with our customers, supplemented by our electronic ordering capabilities. The large wholesalers have historically not used telemarketers to sell to their customers, but recently have begun to do so. Additionally, generic manufacturers are increasingly marketing their products directly to smaller chains and thus increasingly bypassing wholesalers and distributors. Increased competition in the generic industry as a whole may result in increased price erosion in the pursuit of market share.

Sales of our products may continue to be adversely affected by the continuing consolidation of our distribution network and the concentration of our customer base.

Our principal customers in our Brand and Generic pharmaceutical operations are wholesale drug distributors and major retail drug store chains. These customers comprise a significant part of the distribution network for pharmaceutical products in the U.S. This distribution network is continuing to undergo significant consolidation marked by mergers and acquisitions among wholesale distributors and the growth of large retail drug store chains. As a result, a small number of large wholesale distributors and large chain drug stores control a significant share of the market. We expect that consolidation of drug wholesalers and retailers will increase pricing and other competitive pressures on drug manufacturers, including Watson.

For the year ended December 31, 2008, our three largest customers accounted for 11%, 11% and 9% respectively, of our net revenues. The loss of any of these customers could have a material adverse effect on our business, results of

operations, financial condition and cash flows. In addition, none of our customers are party to any long-term supply agreements with us, and thus are able to change suppliers freely should they wish to do so.

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ITEM 1B. ***UNRESOLVED STAFF COMMENTS***

Not applicable.

ITEM 2. ***PROPERTIES***

We conduct our operations using a combination of owned and leased properties.

Our owned properties consist of facilities used for R&D, manufacturing, distribution (including warehousing and storage) and administrative functions. The following table provides a summary of locations of our significant owned properties:

Location	Primary Use	Segment
Carmel, New York	Manufacturing	Generic
Changzhou City, People s Republic of China	Manufacturing, R&D	Generic
Coleraine, Northern Ireland	Manufacturing	Generic
Copiague, New York	Manufacturing, R&D	Generic
Corona, California	Manufacturing, R&D, Administration	Generic/Brand
Davie, Florida	Manufacturing, R&D, Administration	Generic/Brand
Grand Island, New York	Sales and Marketing, Administration	Distribution
Goa, India	Manufacturing	Generic
Gurnee, Illinois	Distribution	Generic/Brand
Ambernath, India	Manufacturing, R&D	Generic
Salt Lake City, Utah	Manufacturing, R&D	Generic/Brand

Properties that we lease are primarily located throughout the U.S. and include R&D, manufacturing support, distribution (including warehousing and storage), sales and marketing, and administrative facilities. The following table provides a summary of locations of our significant leased properties:

Location	Primary Use	Segment
Brewster, New York	Distribution	Generic/Brand
Davie, Florida	Manufacturing, Administration	Generic/Brand
Groveport, Ohio	Distribution, Administration	Distribution
Morristown, New Jersey	Sales and Marketing, Administration	Generic/Brand
Mt. Prospect, Illinois	Manufacturing support	Generic/Brand
Mumbai, India	Administration, R&D	Generic
Shanghai, People s Republic of China	Sales and Marketing, Administration	Generic
Sunrise, Florida	Distribution, Administration	Generic
Weston, Florida	R&D, Administration	Generic

Weston, Florida	Distribution, Sales and Marketing, Administration	Distribution

Our leased properties are subject to various lease terms and expirations.

We believe that we have sufficient facilities to conduct our operations during 2009. However, we continue to evaluate the purchase or lease of additional properties, or the consolidation of existing properties as our business requires.

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ITEM 3. ***LEGAL PROCEEDINGS***

For information regarding legal proceedings, refer to *Legal Matters* in NOTE 15 Commitments and Contingencies in the accompanying Notes to Consolidated Financial Statements in this Annual Report.

ITEM 4. ***SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS***

No matters were submitted to a vote of security holders during the fourth quarter of the fiscal year ended December 31, 2008.

Executive Officers of the Registrant

Below are our executive officers as of February 23, 2009.

Name	Age	Principal Position with Registrant
Paul M. Bisaro	48	President and Chief Executive Officer
Edward F. Heimers	62	Executive Vice President, President of Brand Division
Thomas R. Russillo	65	Executive Vice President, President of Generic Division
Albert Paonessa, III	48	Executive Vice President, Chief Operating Officer, Distribution Division
David A. Buchen	44	Senior Vice President, General Counsel, and Secretary
Clare Carmichael	49	Senior Vice President, Human Resources
Mark W. Durand	49	Senior Vice President, Chief Financial Officer
Charles D. Ebert, Ph.D.	55	Senior Vice President, Research and Development
Thomas R. Giordano	58	Senior Vice President, Chief Information Officer
Francois A. Menard, Ph.D.	49	Senior Vice President, Generics Research and Development
Gordon Munro, Ph.D.	61	Senior Vice President, Quality Assurance

Paul M. Bisaro

Paul M. Bisaro, age 48, was appointed President and Chief Executive Officer effective September 4, 2007. Prior to joining Watson, Mr. Bisaro was President and Chief Operating Officer of Barr from 1999 to 2007. Between 1992 and 1999, Mr. Bisaro served as General Counsel and from 1997 to 1999 served in various additional capacities including Senior Vice President Strategic Business Development. Prior to joining Barr, he was associated with the law firm Winston & Strawn and a predecessor firm, Bishop, Cook, Purcell and Reynolds from 1989 to 1992. Mr. Bisaro also served as a Senior Consultant with Arthur Andersen & Co. Mr. Bisaro received his undergraduate degree in General Studies from the University of Michigan in 1983 and a Juris Doctor from Catholic University of America in Washington, D.C. in 1989.

Edward F. Heimers

Edward F. Heimers, age 62, has served as Executive Vice President and President of the Brand Division since May 2005. Prior to joining Watson, Mr. Heimers was Senior Vice President, Marketing for Innovex, a contract sales

organization and a division of Quintiles Transnational Corp. from 2000 to 2005. Prior to joining Innovex, he was Senior Vice President, Sales for Novartis Pharmaceuticals Corporation from 1996 to 1999. From 1987 to 1996, Mr. Heimers held various positions, including Senior Vice President, Specialty Products and Senior Vice President, Primary Care Marketing and Sales at Sandoz and from 1978 to 1987 held a number of marketing positions at Schering-Plough. Mr. Heimers received his undergraduate degree in Biology from New York University and a Juris Doctor from Syracuse University.

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Thomas R. Russillo

Thomas R. Russillo, age 65, was appointed Executive Vice President and President of the Generic Division on September 5, 2006. Prior to joining Watson, Mr. Russillo served as a consultant to the Company from February to November, 2006, in connection with the Company s integration planning related to the acquisition of Andrx. From January 2005 until September 1, 2006 Mr. Russillo served as a consultant to various clients in the pharmaceutical industry. From 1990 through 2004, Mr. Russillo served as President, Ben Venue Laboratories, a division of Boehringer Ingelheim. Prior to Ben Venue, he held a number of senior positions with Baxter International, most recently as Managing Director, International Medical Technology. Additionally, he is a past chairman of the National Association of Pharmaceutical Manufacturers and board member for the Generic Pharmaceutical Association. Mr. Russillo received his undergraduate degree in Biology from Fordham University in 1965.

Albert Paonessa III

Albert Paonessa, age 48, joined Watson as our Executive Vice President, Chief Operating Officer of Anda, our Distribution company following our acquisition of Andrx. Mr. Paonessa was appointed Anda Executive Vice President and Chief Operating Officer in August 2005 and had been with Anda since Andrx acquired VIP in March 2000. From March 2000 through January 2002, Mr. Paonessa was Vice President, Operations of VIP. In January 2002, he became Vice President, Information Systems at Anda and in January 2004 was appointed Senior Vice President, Sales at Anda. Mr. Paonessa received a B.A. and a B.S. from Bowling Green State University in 1983.

David A. Buchen

David A. Buchen, age 44, has served as Senior Vice President, General Counsel and Secretary since November 2002. From November 2000 to November 2002, Mr. Buchen served as Vice President and Associate General Counsel. From February 2000 to November 2000, he served as Vice President and Senior Corporate Counsel. From November 1998 to February 2000, he served as Senior Corporate Counsel and as Corporate Counsel. He also served as Assistant Secretary from February 1999 to November 2002. Prior to joining Watson, Mr. Buchen was Corporate Counsel at Bausch & Lomb Surgical (formerly Chiron Vision Corporation) from November 1995 until November 1998 and was an attorney with the law firm of Fulbright & Jaworski, LLP. Mr. Buchen received a B.A. in Philosophy from the University of California, Berkeley in 1985, and a Juris Doctor with honors from George Washington University Law School in 1989.

Clare Carmichael

Clare Carmichael, age 49, was appointed Senior Vice President, Human Resources of Watson effective August 12, 2008. Prior to joining Watson, Ms. Carmichael was Vice President, Human Resources for Schering-Plough Research Institute. Ms Carmichael was Vice President, Human Resources for Eyetech Pharmaceuticals Inc. from 2003 to 2005. She also held positions of increasing responsibility at Pharmacia Corporation until 2003. Ms. Carmichael received a B.A. in Psychology from Rider University in 1981.

Mark W. Durand

Mark W. Durand, age 49, was appointed Senior Vice President, Chief Financial Officer effective November 26, 2007. Prior to joining Watson, Mr. Durand served as Chief Financial Officer and Senior Vice President, Finance and Business Development at Teva North America (Teva NA). Prior to joining Teva NA, he held a number of positions of increasing responsibility at Bristol-Myers Squibb from 1987 to 2004, including Vice President Finance and Business Development and Vice President Specialty Pharmaceuticals. Mr. Durand received a B.S. in Zoology from Duke University in 1981, a M.S. in Biological Sciences from Dartmouth College in 1984 and an M.B.A. from the

University of Chicago in 1986.

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Charles D. Ebert, Ph.D.

Charles D. Ebert, Ph.D., age 55, has served as our Senior Vice President, Research and Development since May 2000. He served as our Senior Vice President, Proprietary Research and Development from June 1999 to May 2000. Before joining Watson, Dr. Ebert served TheraTech, Inc. as Vice President, Research and Development from 1987 to 1992 and as Senior Vice President, Research and Development from 1992 to 1999. Dr. Ebert received a B.S. in Biology from the University of Utah in 1977 and a Ph.D. in Pharmaceutics from the University of Utah in 1981.

Thomas R. Giordano

Thomas R. Giordano, age 58, was appointed Senior Vice President, Chief Information Officer of Watson on December 11, 2006. Mr. Giordano joined Watson following the Company s acquisition of Andrx, where he served as Senior Vice President, Chief Information Officer and Chief Project Management Officer since 2002. Prior to joining Andrx, he was Senior Vice President and Global Chief Information Officer for Burger King Corporation, a subsidiary of Diageo Plc from 1998 to 2001. He has also held the position of Senior Vice President and Chief Information Officer for Racal Data Group and AVEX Electronics. Mr. Giordano received his undergraduate degree in Economics from St. Peters College in New Jersey in 1979, participated in graduate studies at New York University, New York and completed the Information Systems Executive Management Program at Harvard Business School.

Francois A. Menard, Ph.D.

Francois A. Menard, Ph.D, age 49, was appointed Senior Vice President, Generics Research and Development of Watson on February 8, 2008. Prior to joining Watson, Dr. Menard served as Vice President Product Development at Sandoz from 2004 to 2008. Prior to Sandoz, Dr. Menard was Vice President, Research and Development at Ivax Corporation during 2004 and before Ivax Corporation held a number of product development positions of increasing responsibility at Johnson & Johnson from 1996 to 2004. Dr. Menard received a Pharm.D. degree in Industrial Pharmacy from the University of Rennes, France in 1983 and a Ph.D. in Pharmaceutical Sciences from the University of Rhode Island in 1987.

Gordon Munro, Ph.D.

Gordon Munro, Ph.D, age 61, has served as our Senior Vice President, Quality Assurance since June 2004. Prior to joining Watson, Dr. Munro was the Director of Inspection and Enforcement, at the United Kingdom Medicines and Healthcare Products Regulatory Agency from 1997 to 2004, and from 2002 to 2004, he was also Acting Head of Medicines. From 1970 to 1997, he held various positions, including the Director of Quality and Compliance at GlaxoWelcome. Dr. Munro received a B.S. in Pharmacy and a Masters in Analytical Chemistry from the University of Strathclyde, Scotland, and a Ph.D. in Analytical Chemistry from the Council of National Academic Awards.

Our executive officers are appointed annually by the Board of Directors, hold office until their successors are chosen and qualified, and may be removed at any time by the affirmative vote of a majority of the Board of Directors. We have employment agreements with most of our executive officers. There are no family relationships between any director and executive officer of Watson.

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PART II

ITEM 5. *MARKET FOR REGISTRANT S COMMON EQUITY, RELATED STOCKHOLDER MATTERS AND ISSUER PURCHASES OF EQUITY SECURITIES*

Market for Registrant s Common Equity

Our common stock is traded on the New York Stock Exchange under the symbol WPI. The following table sets forth the quarterly high and low share trading price information for the periods indicated:

	High	Low
Year ended December 31, 2008:		
First	$ 29.56	$ 23.90
Second	$ 32.70	$ 25.03
Third	$ 31.38	$ 26.66
Fourth	$ 29.65	$ 20.17
Year ended December 31, 2007:		
First	$ 29.43	$ 25.02
Second	$ 33.28	$ 26.16
Third	$ 33.91	$ 28.77
Fourth	$ 32.53	$ 26.90

As of February 18, 2009, there were approximately 2,900 registered holders of our common stock.

We have not paid any cash dividends since our initial public offering in February 1993, and do not anticipate paying any cash dividends in the foreseeable future.

Recent Sales of Unregistered Securities

There were no unregistered sales of equity securities.

Issuer Purchases of Equity Securities

During the quarter ended December 31, 2008, we repurchased 2,022 shares of our common stock surrendered to the Company to satisfy tax withholding obligations in connection with the vesting of restricted stock issued to employees as follows:

Period	Total Number of Shares Purchased	Average Price Paid per Share	Total Number of Shares Purchased as Part of Publicaly	Approximate Dollar Value of Shares that May Yet Be Purchased Under the Program

				Announced Program
October 1 - 31, 2008		$		
November 1 - 30, 2008	1,031	$	23.78	
December 1 - 31, 2008	991	$	23.62	

Securities Authorized for Issuance Under Equity Compensation Plans

For information regarding securities authorized for issuance under equity compensation plans, refer to NOTE 11 Stockholders Equity in the accompanying Notes to Consolidated Financial Statements in this Annual Report.

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Performance Graph

The following graph compares the cumulative 5-year total return of holders of Watson s common stock with the cumulative total returns of the S&P 500 index and the Dow Jones US Pharmaceuticals index. The graph tracks the performance of a $100 investment in our common stock and in each of the indexes (with reinvestment of all dividends, if any) on December 31, 2003 with relative performance tracked through December 31, 2008.

COMPARISON OF 5 YEAR CUMULATIVE TOTAL RETURN*
Among Watson Pharmaceuticals, The S&P 500 Index
And The Dow Jones US Pharmaceuticals Index

* $100 invested on 12/31/03 in stock & index-including reinvestment of dividends.
Fiscal year ending December 31.

	12/31/03	12/31/04	12/31/05	12/31/06	12/31/07	12/31/08
Watson	**100.00**	**71.33**	**70.67**	**56.59**	**59.00**	**57.76**
S&P 500	**100.00**	**110.88**	**116.33**	**134.70**	**142.10**	**89.53**
Dow Jones US Pharmaceuticals	**100.00**	**91.72**	**90.20**	**103.18**	**107.79**	**88.23**

The stock price performance included in this graph is not necessarily indicative of future stock price performance.

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ITEM 6. ***SELECTED FINANCIAL DATA***

WATSON PHARMACEUTICALS, INC.

FINANCIAL HIGHLIGHTS(1)

	Years Ended December 31,				
	2008	**2007**	**2006(2)**	**2005**	**2004**
	(In thousands, except per share amounts)				
Operating Highlights:					
Net revenues	$ 2,535,501	$ 2,496,651	$ 1,979,244	$ 1,646,203	$ 1,640,551
Gross profit	$ 1,032,679	$ 991,895	$ 745,761	$ 793,789	$ 819,757
Operating income (loss)(1)	$ 358,128	$ 255,660	$ (422,096)	$ 218,512	$ 265,940
Net income (loss)(1)	$ 238,379	$ 141,030	$ (445,005)	$ 138,557	$ 150,018
Basic earnings (loss) per share	$ 2.32	$ 1.38	$ (4.37)	$ 1.32	$ 1.37
Diluted earnings (loss) per share	$ 2.09	$ 1.27	$ (4.37)	$ 1.22	$ 1.26
Weighted average shares outstanding:					
Basic	102,821	102,273	101,761	104,949	109,174
Diluted	117,723	117,039	101,761	120,021	124,727

	At December 31,				
	2008	**2007**	**2006(2)**	**2005**	**2004**
Balance Sheet Highlights:					
Current assets	$ 1,458,417	$ 1,173,776	$ 1,261,676	$ 1,353,543	$ 1,361,136
Working capital	$ 976,422	$ 728,849	$ 571,747	$ 1,107,873	$ 1,105,507
Total assets	$ 3,677,887	$ 3,472,027	$ 3,760,577	$ 3,077,187	$ 3,231,956
Total debt	$ 877,893	$ 905,649	$ 1,231,204	$ 587,935	$ 587,653
Deferred tax liabilities	$ 174,287	$ 178,740	$ 203,860	$ 126,718	$ 141,691
Total stockholders equity	$ 2,108,585	$ 1,849,465	$ 1,680,388	$ 2,100,469	$ 2,230,690

(1) For discussion on comparability of operating income and net income, please refer to financial line item discussion in our Management s Discussion and Analysis of Financial Condition and Results of Operations in this Annual Report.

(2) On November 3, 2006, the Company acquired all the outstanding shares of common stock of Andrx in an all-cash transaction for $25 per share, or total consideration of approximately $1.9 billion.

ITEM 7. ***MANAGEMENT S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS***

Except for the historical information contained herein, the following discussion contains forward-looking statements that are subject to known and unknown risks, uncertainties and other factors that may cause actual results to differ materially from those expressed or implied by such forward-looking statements. We discuss such risks, uncertainties

and other factors throughout this report and specifically under the caption Cautionary Note Regarding Forward-Looking Statements under Item 1A. Risk Factors in this annual report on Form 10-K (Annual Report). In addition, the following discussion of financial condition and results of operations should be read in conjunction with the Consolidated Financial Statements and Notes thereto included elsewhere in this Annual Report.

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EXECUTIVE SUMMARY

Overview of Watson

Watson Pharmaceuticals, Inc. (Watson , the Company , we , us or our) was incorporated in 1985 and is engaged in development, manufacturing, marketing, sale and distribution of brand and off-patent (generic) pharmaceutical products. Watson operates manufacturing, distribution, research and development (R&D), and administrative facilities predominantly in the United States of America (U.S.) and India with our key commercial market being the U.S.

As of December 31, 2008, we marketed approximately 150 generic pharmaceutical product families and 27 brand pharmaceutical product families and distributed approximately 8,000 stock-keeping units (SKUs) through our Distribution business (also known as Anda). Prescription pharmaceutical products in the U.S. are generally marketed as either generic or brand pharmaceuticals.