GANNETT CO INC /DE/
Form 10-K
February 26, 2013

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, DC 20549
FORM 10-K
(Mark One)

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

For the fiscal year ended December 30, 2012

.. 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 1-6961
GANNETT CO., INC.
(Exact name of registrant as specified in its charter)

Delaware	16-0442930
(State or Other Jurisdiction of Incorporation or Organization)	(I.R.S. Employer Identification No.)
7950 Jones Branch Drive, McLean, Virginia	22107-0910
(Address of principal executive offices)	(Zip Code)

Registrant's telephone number, including area code: (703) 854-6000
Securities registered pursuant to Section 12(b) of the Act:

Title of Each Class	Name of Each Exchange on Which Registered
Common Stock, par value $1.00 per share	The New York Stock Exchange

Securities registered pursuant to Section 12(g) of the Act: None
Indicate by check mark if the registrant is well-known seasoned issuer, as defined in Rule 405 of the Securities Act. Yes x No ¨
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 ¨ No x
Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.
Yes x No ¨
Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes x No ¨
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 (Check box if no delinquent filers). ¨
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:

Large accelerated filer	x	Accelerated filer	¨	Non-accelerated filer	..	Smaller reporting company	¨

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

The aggregate market value of the voting common equity held by non-affiliates of the registrant based on the closing sales price of the registrant's Common Stock as reported on The New York Stock Exchange on June 22, 2012, was $3,123,094,828. The registrant has no non-voting common equity.

As of February 3, 2013, 229,626,485 shares of the registrant's Common Stock were outstanding.

DOCUMENTS INCORPORATED BY REFERENCE

The definitive proxy statement relating to the registrant's Annual Meeting of Shareholders to be held on May 7, 2013, is incorporated by reference in Part III to the extent described therein.

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PART I

ITEM 1.BUSINESS

Company Profile

Gannett is a leading international media and marketing solutions company, delivering content and services across an integrated, multiplatform portfolio.

As a digital media leader, the company provides access to content on many different platforms, provides digital marketing services to businesses that help them use digital technology more effectively, and provides Internet-based human resource solutions.

Gannett's rich portfolio of iconic national brands, such as USA TODAY and CareerBuilder, as well as its unique local brands in more than 100 communities, set the company apart and provide a strong brand advantage. Gannett's properties cover a wide range of geographies, demographics and content areas, which combine to form a uniquely powerful and comprehensive portfolio of offerings for consumers and commercial clients alike.

Gannett's connection to, and understanding of, its communities and its local market relationships – many of which have spanned decades – provide the company with strong advantages.

Gannett provides consumers with the information they seek and connects them to their communities of interest through multiple platforms including web sites, mobile and tablet products, print publications and TV stations.

Gannett helps businesses grow by providing marketing solutions that reach and engage their customers across the company's diverse platforms.

The company generates digital revenues through online content subscription fees and advertising in its various digital platforms including more than 130 publishing web sites, 21 TV web sites, the management of social engagement advertising campaigns and customer loyalty programs, a daily coupon and deal business, and online recruitment services. Gannett reaches 54.6 million unique visitors monthly or about 24.7% of the U.S. Internet audience, as measured in December 2012 by comScore Media Metrix, via web sites supported by industry-leading platforms, including CareerBuilder.com, the nation's top human capital solutions site, USATODAY.com and USA TODAY Sports Digital Properties.

Gannett also provides its content through 82 daily U.S. publications, including USA TODAY, a multi-platform news and information media company and the nation's largest-selling daily print publication. In September 2012, USA TODAY celebrated its 30th anniversary, re-launching a new print design format and enhanced digital platforms to provide fresh new ways of interacting with content. The company also publishes about 480 magazines and other non-dailies including USA WEEKEND. Likewise, Gannett subsidiary Newsquest is one of the United Kingdom's leading regional community news providers with 17 daily paid-for titles, more than 200 weekly print products, magazines and trade publications, and a network of web sites. More than 9 million unique users access the Newsquest network of news web sites each month.

In addition, the company operates 23 television stations in 19 U.S. markets with a total market reach of nearly 21 million households, 18.1% of the U.S. population. Each of these stations also operates locally oriented digital platforms offering news, entertainment and advertising content. Through its Captivate subsidiary, which operates video screens in elevators of office buildings and select hotel lobbies across North America, the company's broadcasting group delivers news, information and advertising to a highly desirable demographic in key urban markets.

Many of the company's digital offerings are tightly integrated within its existing infrastructure and publishing or broadcasting product offerings, and reported within the operating results of its Publishing and Broadcasting Segments. In addition, the company also separately reports a Digital Segment which includes stand-alone digital subsidiaries including CareerBuilder, ShopLocal, PointRoll and Reviewed.com.

During 2012, CareerBuilder, the largest online job site in the U.S., continued to grow its reach domestically, expand internationally and enhance its product set. It has a presence in more than 60 markets worldwide, and a focus on technology solutions and niche sites. In 2012, CareerBuilder acquired Economic Modeling Specialists Intl. (EMSI), which specializes in gathering and interpreting vast amounts of labor market data and employment information. The company believes that combining EMSI's "Big Data" expertise with CareerBuilder's leading practices and processes will

enable CareerBuilder to deliver deeper and more targeted employment and labor market information to customers. During 2012, CareerBuilder also continued to grow its global businesses with the acquisitions of Top Language Jobs in the U.K., the leading global online job site for multi-language jobs and candidates, and Ceviu, the leading information technology job board in Brazil.

PointRoll provides online advertisers with rich media marketing services. In October 2012, Gannett acquired Rovion, a rich-media advertising company whose primary product, Ad Composer, includes a self-service technology platform that enables the full development and deployment of rich media and mobile HTML5 ads by clients who do not have coding expertise. Rovion is being integrated into PointRoll's operations and technology platform, which will be leveraged across the entire Gannett network to fulfill the needs of agencies and advertisers. In early 2011, Gannett acquired Reviewed.com, which operates a group of product-review web sites that provide comprehensive and comparative reviews for technology products such as digital cameras, camcorders and high-definition televisions as well as household products and services.

Complementing its core Digital, Publishing and Broadcasting segments, the company has made significant strides accelerating its digital strategy through key investments and partnerships in the online space. These include a partnership investment in the highly successful Classified Ventures, which owns and operates the Cars.com and Apartments.com web sites.

To enhance the company's delivery of these products and platforms, Gannett reorganized its local marketing services efforts in late 2011 and created Gannett Digital Marketing Services (GDMS). GDMS provides a one-stop shop for digital marketing services to help tens of thousands of small and medium-sized businesses use digital technology to more effectively reach their customers. To further expand the scope of its digital marketing products and services, and continue to enhance its robust digital solutions product suite, Gannett acquired BLiNQ Media, which helps companies advertise and engage with consumers on Facebook and other social networks, and Mobestream Media, which, through its Key Ring application, provides a consumer loyalty mobile platform for all major types of smartphones.

Business Transformation and Initiatives: 2012 was a watershed year as Gannett launched a new strategic direction for the company. Gannett laid out a new strategy to return the company to sustainable revenue growth and increased profitability while positioning it for expansion in the digital era.

The company's growth strategy is aimed at achieving three main objectives:

- Enhance its local core news and marketing operations to make its local franchises stronger and its ties with the communities even deeper;
- Leverage its hometown and brand advantages to accelerate growth by entering into or expanding high potential businesses;
- Optimize its assets and maintain a strong financial profile to improve efficiency and effectiveness, allowing the company to self-fund growth while delivering increased shareholder value.

The company also announced a new capital allocation plan, which aims to return over $1.3 billion to shareholders by 2015. As part of that plan, the company increased the annual dividend by 150% to $0.80 per share; and launched a new $300 million share repurchase program in February 2012. Against these targets, in 2012 alone, through the combination of the increase in the company's annual dividend and the new share repurchase program, Gannett paid more than $158 million in dividends to shareholders and repurchased approximately 10.3 million shares for $154 million.

The company is implementing the growth strategy through a plan built to leverage Gannett advantages. These include the company's long history of being a trusted source of relevant, reliable, valued news and information in its markets and the close working relationships the company has with more than 150,000 small to medium-sized businesses.

To implement the strategy, Gannett is committed to revitalizing local and national news and information capabilities while enabling subscribers to access Gannett content across a variety of digital platforms as well as print. The new digital platforms broadened access to content, and also opened new ways for advertisers and marketers to engage with consumers.

Gannett created an integrated national sales organization in 2012 to fully leverage its local-to-national reach, growing national advertising revenues across Gannett's robust publishing and digital businesses.

At the same time, Gannett pursued strategic initiatives in seven primary categories: Digital Relaunch & Mobile; USA TODAY Sports Media Group; Digital Marketing Services; All-Access Content Subscription Model; Gannett Publishing Services; Sourcing; and Space Consolidation.

Gannett made significant progress in implementing its strategy across each of its business segments – Publishing, Broadcast and Digital. Progress on these strategic initiatives is highlighted below:

- The Digital Relaunch and Mobile initiative focused on building out its software and infrastructure for a "One Gannett" platform and creating new award-winning desktop products and mobile apps. Digital teams migrated more than 400 mobile and desktop sites to a single ad server from historically different ad servers. Gannett also created a new digital content management system; built and deployed the U.S. Community Publishing (USCP) online subscription system; and relaunched USA TODAY.com. In addition, the mobile team built and launched over 200 mobile products, including new USCP tablet editions, multiple USA TODAY mobile products for phone and tablet, and the Broadcasting iPad apps. USA TODAY was named Mobile Publisher of the Year by Mobile Marketer, and its new site received the Cutting Edge award from FWA/Adobe.

- USA TODAY Sports Media Group covers sports from the local high school level through college and professional teams and continues to leverage USA TODAY's 30-year relationship with American sports fans by driving growth in the digital sports market. In 2012, USA TODAY Sports Media Group streamlined coverage and became one of the nation's top five digital sports destinations with over 20 million unique visitors each month. Group highlights include:
  - Acquisition of Fantasy Sports Ventures/Big Lead Sports, a leading digital sports site in North America.
  - Rolling out USA TODAY's Sports Pulse digital content syndication to all local markets, which included content from USA TODAY Sports, Gannett's more than 100 local media brands, Sports On Earth (a joint services agreement between USA TODAY Sports and Major League Baseball Advanced Media) and the hundreds of sites within USA TODAY Sports Digital Properties such as thebiglead.com and mixed martial arts site MMAjunkie.com, among others.
  - Increased partnership with UFC and continued expansion of relationships with other league partners such as NASCAR and the PGA Tour.
  - Relaunching USA TODAY's Sports section in print and online.

- Re-branding US PRESSWIRE, its dedicated sports image service providing coverage for nearly 10,000 events each year, to USA TODAY Sports Images.
- Relaunching and re-branding its high school sports web site, highschoolsports.net, as USA TODAY High School Sports (www.usatodayhss.com), which anchors the group's comprehensive national coverage of all boys' and girls' high school sports throughout the country, as well as for the more than 100 local media properties within the company.
- GDMS was created to provide a one-stop shop for digital marketing services to help tens of thousands of small and medium-sized businesses in Gannett markets use digital technology to more effectively reach customers. GDMS enables Gannett sites to deepen their long-standing relationships with advertisers, who see Gannett local media as familiar, knowledgeable and trusted partners.
- By year-end, the planned GDMS roll out was complete and Gannett's local publishing and broadcast markets were offering clients a broad suite of digital services such as daily deals, coupons, loyalty programs, email marketing, search engine optimization and online marketing.
- Gannett completed acquisitions of BLiNQ Media, a company which helps businesses advertise and engage with consumers on Facebook and other social networks, and Mobestream Media, which through its Key Ring application, provides a consumer loyalty mobile platform for all major types of smartphones.
- GDMS expanded DealChicken, its daily deals offering, to 12 new U.S. Community Publishing markets in 2012. DealChicken has been rolled out within 72 markets, helping local area merchants create and expand their brand awareness as well as deliver a loyal following of repeat customers.

USCP continued to transform itself as it successfully implemented the roll-out of its all-access content subscription model for its local media in 78 markets across the U.S. This program makes USCP's unique, local, high-quality content available when and how consumers want it, digitally or in print. The subscription model built on earlier 2010 tests in three markets and 2011 research efforts, offers a variety of options to consumers and advertisers. All subscriptions include full web, mobile, e-Edition and tablet access, with subscription prices that vary according to the frequency of print home delivery. Single-copy print editions continue to be sold at retail outlets. Circulation revenues increased 8% in 2012 at the company's local domestic publishing units driven by the impact of the all-access roll out. The focus in 2013 will shift to enhancing operations and growing digital subscribers.

- 2012 was the first full year of operation of Gannett Publishing Services (GPS), which centralized the circulation, print production and consumer sales and services functions of USCP, USA TODAY, and Gannett Offset divisions under one organizational structure. GPS provides printing services from 43 U.S. locations. This allows Gannett publishers to focus on strengthening the core elements of their local business – which are providing valued news and information, building advertising sales and expanding their strong community ties. GPS also opened up new revenue generation opportunities in third-party production, printing and packaging services as an integrated nationwide business.
- Throughout 2012, Gannett took a number of steps under its sourcing initiative to create greater efficiencies, including driving savings through outsourcing, centralization, renegotiations of vendor contracts and demand management.
- The space consolidation initiative continues to evaluate opportunities to optimize Gannett's real estate portfolio, which include selling older, under utilized buildings and relocating to more efficient office space; reconfiguring space to take advantage of leasing and subleasing opportunities, as well as other options. For example, Gannett's Los Angeles office moved to more efficient space and Chicago offices consolidated locations in 2012. A number of Gannett properties, including those in Westchester, NY, and Des Moines, IA, were put on the market and new, more collaborative-designed leased space is currently under construction. During 2012 alone, Gannett executed 12 real estate transactions, realizing proceeds of nearly $40 million.

Business portfolio: The company operates a diverse business portfolio, established through acquisitions and internal development. Some examples of this diversification are:

- CareerBuilder is the global leader in human capital solutions, helping companies target, attract and retain talent. Its online job site, CareerBuilder.com, is the largest in North America with the most traffic and revenue.
- PointRoll, a leading multi-screen digital advertising and technology company that enables advertisers, agencies and publishers to create, deliver and measure interactive online video, rich media display, mobile and social campaigns.
- ShopLocal, a leader in multichannel shopping and advertising services.

- Reviewed.com, a group of product review web sites that provide comprehensive, comparative reviews of technology and household products and services. Reviewed.com is a key element in the company's consumer media strategy.
- USA WEEKEND, a weekly magazine carried by more than 800 local publishers with an aggregate circulation reach of 22.5 million.
- Clipper Magazine, a direct mail advertising magazine that publishes more than 450 individual market editions under the brands Clipper Magazine, Savvy Shopper and Mint Magazine in 29 states.
- Gannett Government Media, which operates military and defense publications and has expanded into the broadcasting and online arenas. Gannett Government Media collaborates with Gannett Washington, D.C., TV station WUSA to produce "This Week in Defense News" which airs on Sunday mornings.
- Gannett Healthcare Group publishes magazines specializing in news, continuing education opportunities and employment opportunities for nurses and allied health professionals with a combined circulation of 730,000. Its websites, Nurse.com, TodayinPT.com and TodayinOT.com feature news, continuing education opportunities and employment opportunities for allied health professionals. Gannett Healthcare Group also operates Gannett Education, which delivers continuing education opportunities to nurses and allied health professionals and includes ContinuingEducation.com and PearlsReview.com, an online nursing certification and continuing education web site.
- GDMS was established to aggressively maximize scale and further enhance Gannett's product offerings. GDMS, a cross-divisional organization, includes GannettLocal, DealChicken, Clipper's Double-Take Deals, ShopLocal, BLiNQ

Media and Mobestream Media. The new business organization helps the company better leverage its local sales forces across divisions and maximize its ability to build, acquire or partner to deliver the high-quality digital marketing solutions needed to help customers succeed in Gannett markets and beyond. It is also responsible for product fulfillment functions such as building web sites, e-mail marketing, search engine marketing, search engine optimization, daily deals, mobile loyalty and social media marketing; expansion of GannettLocal in building a high-quality telemarketing sales force to work with small customers; and training and integrating the sales forces at the company's 100-plus local media properties.

Strategic Acquisitions: In October 2012, Gannett acquired Rovion. Rovion's primary product, Ad Composer, includes a self-service technology platform that enables the full development and deployment of rich media and mobile HTML5 ads by clients who do not have coding expertise.

In September 2012, Gannett acquired Mobestream Media, developer of the Key Ring consumer rewards mobile platform ("Key Ring") available on all major smartphones. Consumers download the free Key Ring application to scan and store existing loyalty cards, join new rewards programs, get mobile coupons and other promotional offers delivered to their smartphones.

Also in September 2012, CareerBuilder acquired a controlling interest in EMSI. EMSI is an economic software firm that specializes in employment data and labor market analysis. EMSI collects and interprets large amounts of labor data, which is used in work force development and talent strategy.

In August 2012, Gannett completed the acquisition of BLiNQ Media, LLC, a leading global innovator of social engagement advertising solutions for agencies and brands. BLiNQ helps companies advertise and engage with consumers on Facebook and other social networks.
In June 2012, the company acquired Quickish. Quickish is a sports aggregator that offers a summary and a link for sports stories throughout the day.
In April 2012, CareerBuilder acquired two new businesses: Ceviu and Top Language Jobs. Ceviu is the leading information technology job board in Brazil. Top Language Jobs is Europe's number one language specialist recruitment job portal. It operates the largest global network of job boards dedicated to multilingual job seekers looking for work internationally.
In February 2012, the company invested in HotelMe LLC, a company engaged in the business of providing authenticated hotel and lodging travel reviews.
In January 2012, the company acquired the assets of Fantasy Sports Ventures/Big Lead Sports, a leading sports digital site. This business is an important addition to the USA TODAY Sports Media Group, positioning it as one of the top five sports sites on the web.
In previous years, the company also invested in a full complement of digital offerings. For example, in November 2011, the company acquired the mixed martial arts web site, MMAjunkie.com, one of the leading online news destinations for the sport and a content provider for several print, online and TV outlets.
Also in November 2011, the company purchased a minority stake in ShopCo Holdings, LLC (ShopCo). ShopCo provides a common online shopping platform which allows ShopCo advertisers to reach consumers in order to assist them in making informed purchasing decisions.
In September 2011, CareerBuilder acquired JobScout24, which solidified CareerBuilder's position as one of the top three online recruitment sites in Germany.
In August 2011, the company acquired US PRESSWIRE, a global leader in the creation and distribution of premium digital sports images to media companies worldwide. US PRESSWIRE operates within the USA TODAY Sports Media Group and provides daily sports photo coverage for all of the company's publishing and broadcast properties.
In June 2011, the company acquired Nutrition Dimension, which provides continuing education, certification and review programs and other educational content for nutrition, fitness and training professionals.
In May 2011, CareerBuilder acquired JobsCentral, a leading jobs board in Singapore that also has a fast-growing presence in Malaysia.
In January 2011, the company acquired Reviewed.com, a group of product-review web sites that provide comprehensive reviews for technology products such as digital cameras, camcorders and high definition televisions. Its operations have been expanded to cover other household items and consumer services.
In March 2010, CareerBuilder purchased CareerSite.biz, parent of three successful career-related operations in the U.K., two online recruitment niche sites targeted to nursing and rail workers as well as a successful virtual career-fair business.
The company also owns a 23.6% stake in Classified Ventures, a highly successful online business focused on real estate rental and automotive advertising. The company's equity in the earnings of Classified Ventures grew by 25% and 20% in the years 2011 and 2012, respectively.
With these acquisitions and investments, the company has established important business relationships to more broadly leverage its publishing and online assets, as well as products and operations to enhance its online footprint, revenue base and profits.

Digital operations – Publishing and Broadcasting
Gannett Digital's mission is to be the catalyst for revenue growth and innovation by developing products that delight and engage consumers while driving increasing monetization. At its core, Gannett has numerous original content assets, including its national brand, USA TODAY, and more than 100 local print and television brands, as well as a large audience reach. In December 2012, Gannett's total online U.S. Internet audience totaled 54.6 million monthly unique visitors, reaching about 24.7% of the Internet audience, as measured by comScore Media Metrix.
In 2011, Gannett Digital was reorganized into a product development and shared services organization that supports, hosts and manages the key infrastructure for the company's digital operations, including databases, applications,

templates, architecture, user experience, project management, digital video production, mobile and web development, distribution, packaging, ad solutions, and paid content systems.

Following the reorganization, Gannett Digital developed an aggressive roadmap aimed at developing next generation mobile, tablet and browser experiences for Gannett's properties and integrating the company's back-end editorial, publishing and advertising platforms. In 2012, Gannett Digital made significant progress on the roadmap through:

- Building and launching an entirely new platform underlying USATODAY.com, including new publishing tools, content databases and front-end design. The platform was designed to be extended with appropriate modifications to the remainder of Gannett's properties.
- Introducing a new advertising strategy for USATODAY.com focused on higher impact, higher value advertising units in order to drive better results for marketers.
- Training hundreds of journalists on new publishing tools that enable device-specific programming (desktop, tablet, mobile phone).
- Building and launching new or updated mobile and tablet applications for USA TODAY (iPhone 2.0, iPad 3.0, Kindle Fire 2.0, Windows 8), Broadcast (iPad, Android and Kindle) and U.S. Community Publishing (iPhone, Android, HTML5 iPad apps). These product launches, in addition to the robust growth of consumer adoption of mobile phones and tablets, contributed to 20% and 81% year-over-year growth in Gannett-wide mobile/tablet visitors and page views, respectively.
- Building and launching the Video Production Center in Atlanta, housed at WXIA-TV, which enables all Gannett properties to stream live and on-demand video on desktop, mobile phone and tablet. In December 2012, on-demand video views and live video plays across company publishing and broadcast businesses reached 22.8 million, up 65% year over year. Creating and licensing more video content and better promoting video via redesigns drove this growth.
- Converting hundreds of sites to a new ad serving platform across desktop, mobile phone and tablet that will offer Gannett increased capabilities, including better forecasting, improved campaign delivery pacing, and better utilization of inventory.
- Introducing new technologies to improve diagnostic and performance testing of software and implementing a private cloud computing environment to provide greater flexibility for deployment and reconfiguration of services in production.

Additionally in 2012, Gannett Digital supported the roll out of USCP's new all-access content subscription model. Key projects included the development of hundreds of new mobile and phone tablet products, as noted above, and deploying the e-commerce subscription platform associated with USCP's online and mobile sites.

Throughout the year, USA TODAY continued its leadership role in mobile media by developing a broad product portfolio to address established and emerging platforms and devices. Both USA TODAY's iPhone and iPad applications continue to be strong performers in the news category; the latest iPhone application reaches 1.8 million monthly visitors and has over 2.7 million downloads, while the iPad application reaches 1.7 million monthly visitors and has over 4.1 million downloads. In addition to products for Apple's iOS, USA TODAY has also built products for Android systems and Microsoft systems. Gannett Digital's mobile product development successes in 2012 were recognized across the industry: the USA TODAY iPhone 2.0 was awarded "Best User Experience" by Digital Hollywood; "Best Mobile Application" by Editor & Publisher; and USA TODAY was named "Mobile Publisher of the Year" by Mobile Marketer.

Looking ahead to 2013, Gannett Digital will be focused on extending the platforms built in 2012, inclusive of the new publishing tools, content databases, front-end design and ad management to the Broadcast and USCP divisions. Specifically for USCP, the relaunch of their digital platforms is aimed at enhancing the subscriber value and driving digital-only subscriptions. Gannett Digital will also continue to enhance the platforms, including new feature enhancements for USA TODAY, and help develop sponsored content opportunities, Gannett-wide databases and data-driven interactive features.

Video remains a key growth opportunity for Gannett. The Video Production Center will continue to enable more content sharing across the Gannett network (of both internal and external content) and share best practices across the company about video content production and programming. Additionally, the VPC will be building a small studio to enable live webcasting.

Finally, the company's mobile team will be focused on building uniform code bases for iOS, Android and Windows, which can be deployed across all Gannett properties, developing ongoing feature enhancements to existing products and creating new products, including new tablet applications for the USCP properties.

Business Segments: The company has three principal business segments: Publishing, Broadcasting and Digital, which includes CareerBuilder, PointRoll, ShopLocal and Reviewed.com. Operating revenues and income from web sites, mobile and tablet products associated with publishing operations and broadcast stations are reported in the Publishing and Broadcast Segments, respectively.

Financial information for each of the company's reportable segments can be found under Item 7 "Management's Discussion and Analysis of Financial Condition and Results of Operations" and Item 8 "Financial Statements and Supplementary Data" of this Form 10-K.

Publishing/United States

Affiliated web sites of the company's U.S. publications, including USA TODAY, reach 33.5 million unique visitors monthly. The print products reach 11.1 million readers every weekday and 12.7 million readers every Sunday. Together they provide critical news and information from their customers' neighborhoods, across the nation and the globe.

At the end of 2012, the company operated 82 U.S. daily publications, including USA TODAY, and over 480 non-daily local publications in 30 states and Guam. The USCP division and USA TODAY are headquartered in McLean, VA. At the end of 2012, U.S. Publishing had approximately 18,100 full- and part-time employees, including 7,200 employees in the newly formed Gannett Publishing Services.

The company's local publishing operations are managed through the USCP division. These publishing operations are positioned in small and medium sized markets; this geographical diversity is a core strength of the company. A listing of the markets can be found on pages 18 to 23 of this report.

USA TODAY was introduced in 1982 as the country's first national, general-interest daily publication. It is produced at facilities in McLean, VA, and transmitted digitally to offset printing plants around the country. It is printed at Gannett plants in 13 U.S. markets and commercially at offset plants, not owned by Gannett, in 23 other U.S. markets.

In 2012, the USA TODAY brand was re-launched as a multi-platform news and marketing company.

During 2012, USATODAY.com hosted on average 19 million unique visitors, with 75 million visits and 188 million page views per month. Organic search increased more than 28% from 2011 to 2012. USA TODAY mobile traffic page views increased 137.2% year over year, to over 5.2 billion page views in 2012.

All of the company's local publishing operations and affiliated web sites are fully integrated with shared support, sales and service platforms.

Other businesses that complement, support or are managed and reported within the Publishing Segment include: USA WEEKEND, Clipper Magazine, Gannett Government Media, Gannett Healthcare Group, Gannett Publishing Services, Big Lead Sports, USA TODAY Sports Images, USA TODAY High School Sports, and BNQT.

The National Sales Team represents the company's advertising operations working with national advertisers in reaching and engaging local consumers; Gannett Direct Marketing offers direct-marketing services; and Gannett Media Technologies International develops and markets software and other products for the publishing industry and provides technology support for the company's publishing and web operations. Gannett Publishing Services manages the production and other publishing services for all of these businesses and also oversees third-party commercial printing and delivery activities for all U.S. publishing locations.

News, information and editorial matters: In 2012, USCP journalists focused on producing high-value, unique content to support the new all-access content subscription model. Their job was to provide value to readers of all platforms. Among the initiatives designed to deliver value:

- The "Content Evolution" program focused on creating platform-perfect content that serves the needs of key audiences on each platform by time of day, from social media to mobile web, to desktop and the daily print edition. In one example, the Springfield (MO) News-Leader recently began offering the Evening Edition on its mobile web site, summarizing the top stories of the day in digestible bites that make for easy browsing by mobile readers. At The Arizona Republic in Phoenix, a tablet edition – AZ Today – debuted in December as a weekly news magazine. It focuses on telling the week's most compelling stories in depth, with use of photography, video and interactive graphics to create a rich reading experience for evening tablet readers.
- Strategic investments in news-gathering efforts have enhanced local expertise in key coverage areas and raised the overall level of sophistication on digital platforms, particularly in social media, driving value by showcasing the expertise and personalities in its newsrooms.
- Shared Design Studios were created, staffed with top designers from across the country to provide the sophisticated design that print readers demand. The studios now handle all aspects of design for most print publications.
- Nearly all USCP reporters, photographers, videographers and columnists were equipped with smartphones and other devices in early 2012, enabling the company's content-gatherers to write, photograph, shoot and edit video, while connecting with readers over social media in real time. This investment has helped reshape the modern definition of a journalist. It has buttressed Gannett's journalists' competitive edge and allows them to tell stories with greater color and speed than ever before. The smartphones are part of a larger investment to equip journalists with the tools they need to excel at their jobs. They also received an additional 1,800 tablets and other items to reach audiences across multiple platforms. In 2013, journalists will be trained to become advanced video storytellers who deliver compelling content to viewers.
- Smartphones will continue to be an important tool as the company continues to make its publishing systems more efficient and integrated. In 2012, smartphones allowed the company's journalists to publish and share video content across all divisions of the company through the Brightcove app. In 2013, Gannett will enable more content created on smartphones to move directly into its publishing systems allowing for selective syndication for audiences and advertisers around the nation.
- The company's publishing operations organized an aggressive approach to leveraging the viral aspects of social media in 2012. Journalists are using social media to share the work they are doing, source new material and engage with readers in new ways. Gannett began using a social management platform tool that allows better tracking and analysis. This tool enables insights into community conversation trends. By way of example: In November 2012, journalists set up a national, coordinated effort to share breaking news through a 24/7 Super Storm Sandy Social Media Desk. Gannett staff from as many as 18 different markets took shifts to help cover the social media response and publishing for news organizations affected by the storm over a span of three weeks.

Each of these initiatives is designed to promote unique, high-value local content that will drive dramatic transformation.

The company's domestic daily publishing operations received Gannett's wire service in 2012 and subscribe to The Associated Press. Some publishing operations use supplemental news services and syndicated features as well.

The company operates news bureaus in Washington, DC, and four state capitals – Albany, NY; Baton Rouge, LA; Trenton, NJ; and Tallahassee, FL.

In 2012, Gannett publishing operations and journalists received national recognition for their excellent work:

Three newspapers were named finalists in the Pulitzer Prizes in Journalism:

- The Arizona Republic, Phoenix, AZ, was recognized in the Breaking News category for comprehensive coverage of the mass shooting that involved former U.S. Rep. (D-AZ) Gabrielle Giffords. The Arizona Republic was recognized for its exemplary use of journalistic tools to tell an unfolding story.
- The Burlington (VT) Free Press was recognized in the Editorial Writing category. Aki Soga and Michael Townsend were recognized for a campaign that resulted in the state's first reform of open government laws in 35 years.
-

USA TODAY was named in the Explanatory Reporting category. Tom Frank's series explained how state lawmakers pump up their pensions. Frank examined thousands of pages of pension laws from all 50 states to untangle the obscure language behind pension perks.

USA TODAY won the Alfred I. duPont-Columbia Award for investigative multimedia reporting for a report that uncovered hundreds of forgotten lead factories and their health hazards. The award is presented by the Columbia Journalism School.

The Detroit Free Press, MI, won a 2012 National Edward R. Murrow Award for "Living with Murder," a video documentary that explored the toll of homicide in Detroit neighborhoods. Videographer Romain Blanquart, Reporter Suzette Hackney and Deputy Director Photo/Video Kathy Kieliszewski produced the documentary. The awards are presented by the Radio Television Digital News Association and honor excellence in electronic journalism.

Five newspapers were among winners in their circulation categories in the 2012 Associated Press Media Editors (APME) Journalism Excellence Awards competition:

- USA TODAY received a Digital Storytelling and Reporting award for its 14-month investigation, "Ghost Factories: Poison in the Ground," which revealed the locations of long-forgotten factories and the amount of toxic lead left behind.
- The Burlington (VT) Free Press won a First Amendment award, for its investigation of the handling of warrants by the Vermont judiciary, which revealed negligence at every level of the legal system; and a Digital Storytelling and Reporting award, for breaking news coverage during the Occupy Burlington encampment.
- Asbury Park (NJ) Press won a Public Service award for its report on a cluster of suicides by teens and young adults in the Manasquan, NJ area.
- Argus Leader in Sioux Falls, SD, won a Public Service award for "Fighting DUI" about the cost of cracking down on DUIs.
- The News-Press in Fort Myers, FL, won a digital storytelling and reporting award for its package, "Loving Ingrid," about a woman who suffered a traumatic brain injury.

- In addition, The Arizona Republic, AZ, was one of three finalists selected for APME's Innovator of the Year Award. It was cited for the convergence of print, broadcast and online in its web site, AZCentral.

Journalists at five Gannett newspapers were cited in the Society of Professional Journalists Sigma Delta Chi Awards for excellence in journalism.

- Keith Runyon, The Courier-Journal at Louisville, KY, won for "Hospital Merger: A Series of Editorials" in Editorial Writing.
- Candace Page, Burlington (VT) Free Press, won for "Hard lessons of the tweed" in Feature Reporting.
- Douglas Walker and Keith Roysdon, The Star Press at Muncie, IN, won for "For a Child's Sake: The epidemic of child abuse" in Public Service journalism.
- Andrew West, The News-Press Media Group at Fort Myers, FL, won for "Hope for Haiti" in Feature Photography.
- The Burlington (VT) Free Press won for "Occupy Burlington" shooting in Online, Deadline Reporting.

Three Detroit Free Press business reporters, Greg Gardner, Brent Snavely and Chrissie Thompson, won a Gerald Loeb Award for business journalism in the breaking news category for their stories about contract negotiations last year between GM and the UAW.

The Army Times' Sean Naylor won top honors for his investigative series, "The Secret War in Africa," from the Military Reporters and Editors Association.

Writers at four Gannett newspapers won awards in the Society of American Business Editors and Writers (SABEW) 17th Best in Business competition. The awards honor excellence in business and financial journalism across all news platforms:

- Ronald J. Hansen, The Arizona Republic, Phoenix, AZ, won for "Business Taxes" in the Explanatory category.
- Patrick Peterson, FLORIDA TODAY, Brevard, FL, won for "Bright Idea Man" and "Scrap Daddy" in the Feature category.
- Dick Hogan, The News-Press in Fort Myers, FL, won for "Flopping: Fraud Runs Rampant" in the Investigative category.
- Thomas Frank, USA TODAY, won for "Public-Sector Pensions" in the Investigative category.

FLORIDA TODAY in Brevard, FL, won first place for a features web site in The Society for Features Journalism competition for reader engagement.

The Arizona Republic, Phoenix, AZ, was honored by the National Press Club for its breaking news coverage of the Tucson shooting that involved former U.S. Rep. (D-AZ) Gabrielle Giffords.

The Tennessean at Nashville was a finalist in the 2012 Online Journalism awards from the Online News Association for outstanding breaking news coverage of Occupy Nashville.

In Lafayette, IN, Journal and Courier sportswriter Mike Carmin was named recipient of the 2012 Mel Greenberg Media Award from the Women's Basketball Coaches Association.

Audience research: As Gannett's publishing businesses continue their mission to meet consumers' news and information needs anytime, anywhere and in any form, the company remains focused on an audience aggregation strategy. The company considers the reach and coverage of multiple products in its communities and measures the frequency with which consumers interact with each Gannett product.

Results from 2012 studies conducted by Scarborough Research indicate that Gannett local media organizations reach more than seven in 10 adults each week – more than eight in 10 each month. Under the all-access content subscription model rolled out to 78 sites during 2012, more than half of readers access Gannett content on two or more platforms. The company has gathered audience aggregation data for 52 Gannett markets and will continue to add more data in 2013. Aggregated audience data allows advertising sales staff to provide detailed information to advertisers about how best to reach their potential customers and the most effective product combination and frequency. This approach enables the company to increase its total advertising revenue potential while maximizing advertiser effectiveness. Scarborough Research measures 77 of the nation's top markets. In a report on market penetration, the number of adults in a community who access a publication and its related web site, it noted that more than 3 out of 4 adults in the Rochester, NY, market in a given week either read the print version of the Rochester Democrat and Chronicle or

visited its web site (democratandchronicle.com), making it the top-ranked publishing/web operations in the country for integrated audience penetration. Gannett publications also hold the second (Gannett East Wisconsin) and third (The Des Moines Register) positions in the Scarborough Research rankings. These markets are industry leaders because they understand and aggressively pursue different audiences for different platforms - true audience aggregation.

In addition to the audience-based initiative, the company continues to measure customer attitudes, behaviors and opinions to better understand customers' digital use patterns and use focus groups with audiences and advertisers to better determine their needs. In 2009, the USCP research group launched an ongoing longitudinal study to measure audience and sentiment of consumers in key markets. To date, the group has conducted more than 31,000 interviews for the study.

The group also supported the content evolution initiative in 2012 by conducting consumer research in 74 markets to determine the topics readers are most interested in seeing covered in their Gannett local daily newspaper.

Advertising: USCP has advertising departments that sell retail, classified and national advertising across multiple platforms including print, online, mobile, tablet and niche publications. The company has a national ad sales force focused on the largest national advertisers and a separate sales organization to support classified employment sales – the Digital Employment Sales Center. Additionally, GannettLocal provides marketing specialists to small and medium sized businesses, and Gannett Client Solutions groups provide customized marketing solutions. The company also has relationships with outside representative firms that specialize in the sale of national ads.

Retail display advertising is associated with local merchants or locally owned businesses. In addition, retail includes regional and national chains – such as department and grocery stores – that sell in the local market.

Classified advertising includes the major categories of automotive, employment, legal, real estate/rentals and private party consumer-to-consumer business for merchandise and services. Advertising for classified segments is published in the classified sections, in other sections within the publication, on affiliated digital platforms and in niche magazines that specialize in the segment.

National advertising is display advertising principally from advertisers who are promoting national products or brands. Examples are pharmaceuticals, travel, airlines, or packaged goods. Both retail and national ads also include preprints, typically stand-alone multiple page fliers that are inserted in the daily print product.

The division's audience aggregation strategy gives it the ability to deliver specific audiences that advertisers want. Although some advertisers require mass reach, many want to target niche audiences by demographics, geography, consumer buying habits or customer behavior. With Gannett's continued partnership with Yahoo! and enhancement of its digital portfolio with in-house digital marketing services, the company's local media organizations are able to enhance audience delivery for customers by offering behavioral targeting. Whether it is mass reach or a target audience, the company's publishing sites identify an advertiser's key customers and develop advertising schedules that combine products within a site's portfolio to best reach the desired audience with the appropriate frequency.

USCP continues to use online reader panels in 19 markets to measure advertising recall and effectiveness, article response, and identify consumer sentiment and trends. The reader panels include nearly 30,000 opt-in respondents who provide valuable feedback on over 7,800 advertisements and 4,800 news articles. This capability allows markets to provide deeper insights for advertisers and return-on-investment metrics that are in high-demand from customers.

The company's consultative multi-media sales approach has been tailored to all levels of advertisers, from small, locally owned merchants to large, complex businesses. Along with this sales approach, the company has intensified its sales and management training and improved the quality of sales calls. Digital product integration, sales skills and a Gannett five-step consultative sales process were focus areas in 2012 with formal training delivered in all Gannett markets. Front line sales managers in the company's largest 20 markets participated in intensive training to help them coach their sales executives for top performance.

A major company priority is to realign the USCP sales organizations to match customers' needs while creating additional efficiencies to lower the cost of sale. USCP local media organizations designed their sales teams around three general groups of customers: strategic regional, key local and small local controllable accounts. The structure aligns sales and support resources to customers' needs and provides efficient service and affordable packages to smaller accounts and customized, innovative solutions to larger, market-driven clients. The structure includes digital specialists who expand online share in the local market for retail and classified verticals, including Cars.com, Homefinder.com, Apartments.com and CareerBuilder.com. There are also product specialists in larger markets who focus on growing niche advertisers in non-daily publications.

To better serve local customers and win market share, the company created five Gannett Client Solutions Groups. Functioning much like local ad agencies, the groups develop highly designed creative campaigns to give customers a competitive edge in the marketplace. The campaigns are comprehensive and often extend beyond the local media organization's product portfolio, providing a high level of service.

The national ad sales team is responsible for large national retail accounts. These resources give national customers a single point of contact for all Gannett markets, enable Gannett to have more strategic conversations, allow teams to respond better to customers' needs, and focus local sales personnel on advertisers in their local markets they know best.

This national team works with the national sales resources of Digital, Broadcast and USA TODAY to create multi-market, multi-platform solutions for national advertisers scalable across the country.

Ad revenues from affiliated online operations are reported together with revenue from print publishing.

Online operations: The company's local publishing digital platforms showed continued strength in growing audience in 2012, with visitors increasing by 6% year over year as measured internally. More users accessing the full web site on mobile devices and improved search engine optimization for article searches drove the increase.

USCP completed the development and deployment of access management software across 78 local market web sites, allowing subscribers access to all content, while limiting the access of non-subscribers to a small number of articles per month, designed to help them try the services.

In support of the all-access content subscription model, the company invested in a significant expansion of mobile offerings across local markets, including native applications for iPhone and Android smartphones and iPads and tablet-optimized web sites. The mobile audience continued to grow in 2012, ultimately making up 11% of total page views, with mobile web sites and the native iPhone applications leading the way. Through the all-access content subscription model, the company made a clear commitment to provide consumers with the content they most want on the devices they use to access news and information about their local communities. Mobile page views nearly doubled, and mobile visitors increased 45% in 2012 on a year over year basis.

Another key initiative in 2012 was the implementation of a social media content management software tool to ensure the division's journalists and marketing and customer service teams could more effectively manage multiple social media profiles and significantly increase their responsiveness and engagement with consumers.

Gannett continues to enjoy a long standing relationship of trust in the local business community. Its advertising sales staff delivers solutions for its customers and helps small and medium size businesses navigate the increasingly complex and diverse world of digital marketing. In 2012, the company further expanded its GDMS suite of products and continued its partnership with Yahoo! to offer more digital solutions to advertisers. Through this, Gannett is able to offer its customers expanded digital reach.

The overriding objective of USCP's online strategy is to provide compelling content that best serves its customers. A key reason customers turn to a Gannett digital platform is to find local news and information. The credibility of the local media organization, a known and trusted information source, includes its digital platforms (tablet and mobile applications and its web site) and differentiates these online sources from competing online products. This allows Gannett's local media organizations to compete successfully as information providers.

A second objective in the company's online business development is to maximize the natural synergies between the local media organizations and local digital platforms. The local content, customer relationships, news and advertising sales staff, and promotional capabilities are all competitive advantages for Gannett. The company's strategy is to use these advantages to create strong and timely content, sell packaged advertising products that meet the needs of advertisers, operate efficiently and leverage the known and trusted brand of the local media organization.

Gannett Media Technologies International (GMTI) provides technological support and products for the company's domestic local media organizations and Internet activities, including ad software and database management, editorial production and archiving, and web site hosting. In addition, GMTI provides similar services to other media companies.

Non-daily operations: The publication of non-daily products continued to be an important part of Gannett's market strategy for 2012. The company produces non-daily publications in the U.S. including glossy lifestyle magazines, community publications and publications focused on one topic, such as health or cars. The company's strategy for non-daily publications is to appeal to key advertising segments (e.g. affluent women, women with children or young readers). Non-daily products help print operations increase overall impressions and frequency for advertisers looking to reach specific audience segments or in some cases, like community weeklies, provide a lower price point alternative for smaller advertisers with specific geographic targets, thus helping to increase the local media organization's local market share.

Circulation: Detailed information about the circulation of the company's newspapers may be found later in this Form 10-K. In a trend generally consistent with the domestic publishing industry, circulation volume declined. However, year over year circulation revenues increased 5.0% and digital access increased across all publications. USCP has approximately 46,000 digital-only subscribers.

The company's all-access subscription prices are market specific. For example, all-access pricing that includes Monday through Sunday print home delivery ranges from $28 per month per printed bill ($25 EZ Pay) to $14.35 per printed bill ($13 EZ Pay). All-access that includes home delivery of only the Sunday print edition ranges from a high of $17 per printed bill ($15 EZ Pay) to a low of $6 per printed bill ($5 EZ Pay). For USCP publications, all-access subscriptions make up 78% daily (home delivery) and 73% Sunday of total net paid circulation. EZ Pay grew from approximately 50% at the end of 2011 to approximately 60% one year later across Gannett sites, excluding USA TODAY.

More than 70% of the 82 Gannett publications (or 60 publications) had a single copy price increase in 2012. For USCP, single copy represents 13% of daily and 25% of Sunday net paid circulation volume.

The single copy price of USA TODAY at newsstands and vending machines was $1.00 in 2012. Mail subscriptions are available nationwide and abroad, and home, hotel and office delivery is available in many markets. Approximately 76% of its net paid circulation results are from single-copy sales at newsstands, vending machines or provided to hotel guests. The remainder is from home and office delivery, mail, educational and other sales.

At the end of 2012, 71 of the company's domestic daily publications, including USA TODAY, were published in the morning, and 11 were published in the evening.

Production: Product quality and efficiency improvements continue in several areas, as continually improving technology allows for greater speed and accuracy and led to continued consolidation of job functions for all divisions of Gannett now managed by Gannett Publishing Services. That efficiency trend is expected to continue through 2013.

The three Gannett Imaging and Ad Design Centers (GIADC) serve 79 publishing properties, including all USCP dailies except Detroit and Guam. In addition to the USCP sites, USA TODAY and Gannett Broadcast properties are now included. The GIADC also supports projects for Deal Chicken, Gannett Digital and the Client Solutions Group. Fourteen external customers also utilize the GIADC for imaging and/or ad production.

In 2012, the GIADC built 1.2 million ads. Additionally, the GIADC processed over 3.7 million images in 2012 and also created 170 Creative Campaigns as part of a program which allows sales representatives to work directly with a team of highly creative artists to target particular customers and develop a comprehensive multimedia program.

Digital needs continue to evolve rapidly for the company's customers. The GIADC is training in custom rich media utilizing technology offered by two other Gannett companies, PointRoll and Rovion. The GIADC began assuming commercial work in 2012 for external customers and plans to continue this work in 2013.

At the end of 2012, all 82 domestic daily newspapers (including USA TODAY) were printed by the offset process and the majority at 44-inch web and on 45 gram paper. Also at year end, more than 73 percent of its domestic community daily publications were either printed in Gannett-owned facilities that print multiple daily publications or by non-Gannett printers.

Design Studios now handle the layout, design and selection of nation/world content of Gannett's daily newspapers, and the design of Gannett's non-daily print publications. The Design Studios are located in Asbury Park, NJ; Nashville, TN; Louisville, KY; Des Moines, IA; and Phoenix, AZ.

By the end of 2012, almost all USCP and USA TODAY employees were utilizing a common content management system. The common content management system enables communication and collaboration needed to build strong

design remotely. The studios are operationally efficient while enhancing design in publications across the company.

Gannett Publishing Services: Improving the efficiency and reducing the cost associated with the production and distribution of the company's printed products across all divisions remains an important strategic initiative for Gannett. In 2011, GPS was formed to directly manage all of the production and circulation operations of Gannett's 81 domestic community newspapers, USA TODAY and Gannett Offset.

GPS leverages Gannett's existing assets, including employee talent and experience, physical plants and equipment, and its vast national and local distribution networks. The objectives of the new unit are to optimize commercial services, leverage expertise, standardize best practices to optimize efficiency and eliminate duplication. This in turn allows local unit management to focus on growing audience, content and revenue development working with GPS management to focus on consumer sales and the transition of the company's print subscribers to multi-media subscribers on the all-access content subscription model.

GPS is responsible for imaging, ad production, internal and external printing and packaging, internal and external distribution, consumer sales, customer service and direct marketing services. GPS is generating revenue gains from the sale of pre-media services, commercial printing, and third party product delivery. It also is generating cost savings from outsourcing selected production and distribution activities, through standardizing best practices across Gannett's printing and distribution networks and through the elimination of operational redundancies.

Competition: The company's publishing operations and affiliated digital platforms compete with other media for advertising. Publishing operations also compete for circulation and readership against other professional news and information operations and amateur content creators. Very few of the company's publishing operations have daily competitors that are published in the same city. Most of the company's print products compete with other print products published in suburban areas, nearby cities and towns, free-distribution and paid-advertising publications (such as weeklies), and other media, including magazines, television, direct mail, cable television, radio, outdoor advertising, telephone directories, e-mail marketing, web sites and mobile-device platforms.

Digital platforms, which compete for the principal traditional classified advertising revenue streams such as real estate, employment and automotive, have had the most significant impact on the company's revenue results.

The rate of development of opportunities in, and competition from, digital media, including web site, tablet and mobile products, is increasing. Through internal development, content distribution programs, acquisitions and partnerships, the company's efforts to explore new opportunities in the news, information and communications business and in audience generation will keep expanding. The company continues to seek more effective ways to engage with its local communities using all available media platforms and tools.

Environmental regulation: Gannett is committed to protecting the environment. The company's goal is to ensure its facilities comply with federal, state, local and foreign environmental laws and to incorporate appropriate environmental practices and standards in its operations. The company is one of the industry leaders in the use of recycled newsprint, increasing its purchases of newsprint containing recycled content from 42,000 metric tons in 1989 to 198,000 metric tons in 2012. During 2012, 43% of the company's domestic newsprint purchases contained recycled content, with an average recycled content of 42%.

The company's publishing operations use inks, photographic chemicals, solvents and fuels. The use, management and disposal of these substances are sometimes regulated by environmental agencies. The company retains a corporate environmental consultant who, along with internal and outside counsel, oversees regulatory compliance and preventive measures. Some of the company's subsidiaries have been included among the potentially responsible parties in connection with sites that have been identified as possibly requiring environmental remediation. Additional information about these matters can be found in Part I, Item 3, Legal Proceedings, in this Form 10-K.

Raw materials - U.S. & U.K.: Newsprint, which is the basic raw material used in print publication, has been and may continue to be subject to significant price changes from time to time. During 2012, the company's total newsprint consumption was 452,745 metric tons, including consumption by USA WEEKEND, USA TODAY, tonnage at non-Gannett print sites and Newsquest. Newsprint consumption was 7% less than in 2011. The company purchases newsprint from 22 domestic and global suppliers.

In 2012, global newsprint supplies were adequate. The company has and continues to moderate newsprint consumption and expense through press web-width reductions and the use of lighter basis weight paper. The company believes that available sources of newsprint, together with present inventories, will continue to be adequate to supply the needs of its publishing operations.

Newspaper partnerships: The company owns a 19.49% interest in California Newspapers Partnership, which includes 19 daily California newspapers; a 40.64% interest in Texas-New Mexico Newspapers Partnership, which includes six daily newspapers in Texas and New Mexico and four newspapers in Pennsylvania; and a 13.50% interest in Ponderay Newsprint Company in the state of Washington.

Joint operating agencies: The company's publishing subsidiary in Detroit participates in a joint operating agency (JOA). The JOA performs the production, sales and distribution functions for the subsidiary and another publishing company under a joint operating agreement. Operating results for the Detroit JOA are fully consolidated along with a charge for the minority partner's share of profits. Through May 2009, the company also published the Tucson Citizen through the Tucson JOA in which the company held a 50% interest. Because of challenges facing the publishing industry, combined with the difficult economy, particularly in the Tucson area, the company ceased publication of the Tucson Citizen on May 16, 2009. The company retained its online site and 50% partnership interest in the JOA, which provides service to the remaining non-Gannett publication in Tucson. The company's share of results for

the Tucson operations are accounted for under the equity method, and are reported as a net amount in "Equity income in unconsolidated investees, net."

Publishing/United Kingdom

Newsquest produces 17 daily paid-for publications and more than 200 weekly publications, magazines and trade publications in the U.K., as well as associated web sites and a wide range of niche products. Newsquest operates its publishing activities around regional centers to maximize the use of management, finance, printing and personnel resources. This enables the group to offer readers and advertisers a range of attractive products across the market. The clustering of titles and, usually, the publication of a free print product alongside a paid-for print product, allows cross-selling of advertising serving the same or contiguous markets, satisfying the needs of its advertisers and audiences. Newsquest produces free and paid-for print products with quality local editorial content. Newsquest also

distributes a substantial volume of advertising leaflets in the communities it serves. Most of Newsquest's paid-for distribution is outsourced to wholesalers, although direct delivery is employed as well to maximize circulation sales opportunities.

Newsquest's publishing operations are in competitive markets. Their principal competitors include other regional and national newspaper and magazine publishers, other advertising media such as broadcast and billboard, Internet-based news and other information and communication businesses.

Newsquest revenues for 2012 were approximately $484 million, down 5% in local currency reflecting the continuing difficult economy. While print advertising revenue categories declined, digital ad revenues grew by 10% in local currency. As in the U.S., advertising, including ad revenue from online web sites affiliated with the publications, is the largest component of Newsquest's revenue, comprising approximately 69%. Circulation represented 23% of revenue. Printing for third-party newspaper publishers accounts for most of the remainder of revenue.

Recognition for Newsquest's editorial achievements included a variety of Scottish Press Awards won by The Herald, Sunday Herald and Evening Times, which included awards in the following categories: front page, campaign, scoop, reporter, financial journalist, journalist, cartoonist, columnist and young journalist of the year prizes; as well as seven European Newspaper of the Year awards for excellence. In addition, a campaign which seeks to encourage correct grammar and concise writing named the Worcester News as England's top regional daily.

In 2012, the "Queen's Diamond Jubilee" was celebrated across the U.K. A message of thanks on behalf of Queen Elizabeth II was sent to the Telegraph & Argus after copies of six "Diamond Decades Jubilee" commemorative supplements and the shortlist supplement for the publication's "Queen's Jubilee Portrait Competition" were forwarded to her with a letter from the editor. More than 3,500 children from 107 schools entered the "Queen's Jubilee Portrait Competition" competition.

Newsquest newspapers continued to campaign on local issues. For example, The Westmorland Gazette's "Shorter Journeys Longer Lives" campaign culminated in a 2,000-plus people march through the streets of Kendal, U.K. It prompted Britain's Prime Minister to set up a summit meeting to promote "swift and positive" action to bring a radiotherapy unit to Kendal's Westmorland General Hospital. The proposed unit would dramatically trim a 140-mile round trip to the Royal Preston Hospital for 400 local South Cumbrian cancer patients.

In Winchester, the Hampshire Chronicle celebrated 240 years of continuous publishing with a special supplement focusing not only on the history of the paper, but how it is moving forward into the digital age.

Following the successful launch of regional farming products in 2010 and 2011, Three Counties Farmer was launched in 2012. The Newsquest Specialist Media unit successfully launched Reward in June. Reward is a new information product for the workplace benefits sector.
Trials have taken place in three markets for significant changes in cover prices and editorial content, involving two daily products and one weekly product. Initial results are in line with expectations, and Newsquest intends to roll out further changes in selected markets following market research on how to develop its products in those markets.
There were 4,300 Newsquest employees at year end, a decrease of 3% compared to 2011. Efficiency initiatives included the consolidation of a number of back-office functions. Total costs in local currency were 5% lower year-over-year as a result of the range of efficiency measures taken.

Digital operations: Newsquest continues to actively seek to maximize the value of its local media brands through digital channels. Newsquest's most recent data indicated that an average of 9.1 million unique users accessed the Newsquest site network each month during the period July-December 2012.
Newsquest's total digital ad revenue increased by 10% in local currency. Online banner revenues grew by 26%, propelled by improved audiences, increased local resourcing and sales activity. In Scotland, the group's wholly owned market leading recruitment web site, s1, increased revenues by 9% from 2011.

Digital Segment
The Digital business segment includes CareerBuilder, as well as PointRoll, ShopLocal and Reviewed.com. At the end of 2012, the Digital Segment had approximately 2,600 full-time and part-time employees.
CareerBuilder is the global leader in human capital solutions, helping companies target, attract and retain talent. Its online job site, CareerBuilder.com, is the largest in North America with the most traffic and revenue.
Headquartered in Chicago, IL, CareerBuilder at the end of 2012 had approximately 2,200 full-time and part-time employees.
Currently, CareerBuilder operates in the U.S., Europe, Canada, Asia and South America. Its sites, combined with partnerships and acquisitions, give CareerBuilder a presence in more than 60 markets worldwide. CareerBuilder offers everything from employment branding, and talent and compensation intelligence to recruitment solutions. Most of the revenues are generated by its own sales force but substantial revenues are also earned through sales of employment advertising placed with CareerBuilder's owners' affiliated media organizations. It also has a long-term strategic marketing agreement with Microsoft.
In 2012, CareerBuilder acquired EMSI, which collects and interprets large amounts of employment data which is used in workforce development and talent strategy. CareerBuilder plans to leverage the EMSI acquisition to enhance their workforce analytics platform creating an unmatched repository of historical and real-time labor information.
CareerBuilder also continued to grow its global businesses with the acquisitions of Top Language Jobs in the U.K., the leading global online jobsite for multi-language jobs and candidates, and Ceviu, the leading information technology job board in Brazil.
PointRoll is a multi-screen digital advertising technology and services company. PointRoll enables advertisers, agencies, and publishers to create, target, deploy, and optimize digital campaigns in real time across any digital channel including display, rich media, in-stream video, mobile, tablet and more. PointRoll provides the creative tools, analytics and expertise marketers need to effectively

engage consumers and convert them into buyers and brand supporters. Founded in May 2000, PointRoll has been instrumental in the evolution of digital engagement and has evolved beyond the expandable banner ad to offer marketers the ability to find consumers wherever they are across any digital platform and deliver a relevant brand or direct response experience, dramatically improving ad effectiveness while gaining actionable insights. PointRoll is headquartered in King of Prussia, PA, and maintains offices across the U.S. In October 2012, Gannett acquired Rovion. Rovion's primary product, Ad Composer, includes a self-service technology platform that enables the full development and deployment of rich media and mobile HTML5 ads by clients who do not have coding expertise. Rovion is being integrated into PointRoll's operations and technology platform and will be leveraged across the entire Gannett network to fulfill the needs of agencies and advertisers.

ShopLocal, the leader in multi-channel marketing services, offers a complete suite of innovative digital solutions which connect advertisers and consumers, both online and in-store. ShopLocal's industry-leading SmartProduct business solutions (SmartCircular, SmartCatalog and SmartDelivery) enable more than 100 of the nation's top retailers, including Target, Macy's, Home Depot, CVS, Staples, Toys"R"Us, Walgreens, Kohl's and Sears, to deliver highly interactive, targeted and localized promotions to shoppers through use of online circulars, display advertising, search, social media, digital out of home and mobile. ShopLocal is headquartered in Chicago, IL.

Competition: For CareerBuilder, the largest online employment site in North America, the market for online recruitment solutions is highly competitive with a multitude of online and offline competitors. Competitors include other employment related web sites, general classified advertising web sites, professional networking and social networking web sites, traditional media companies, Internet portals, search engines and blogs. The barriers for entry into the online recruitment market are relatively low and new competitors continue to emerge. Recent trends include the rising popularity of professional and social media networking web sites which have gained traction with employer advertisers. The number of niche job boards targeting specific industry verticals has also continued to increase. CareerBuilder's ability to maintain its existing customer base and generate new customers depends to a significant degree on the quality of its services, pricing, product innovation and reputation among customers and potential customers.

For PointRoll, the market for rich media advertising technology solutions is highly competitive with a number of competitors. Competitors include divisions of larger public media and technology companies, and several earlier-stage independent rich media, dynamic ad, video, mobile, and social advertising technology specialists. The barriers to entry in the rich media market are moderate. Recent trends include the shift towards audience-centric, exchange-based media buying, entry of dynamic ad generation specialists, the move towards automated creative design tools, and the shift toward video content online with associated in-stream advertising opportunities. Increasingly, marketers and their agencies are looking for advertising technology providers that can scale across media platforms, including rich media, video and mobile. PointRoll's ability to maintain and grow its customer base and revenue depends largely on its continued product innovation, level of service quality, depth of marketing analytics and ultimately the effectiveness of its rich media advertising and resulting customer satisfaction.

For ShopLocal, the market for digital store promotions is highly competitive and evolving as digital media transforms marketing programs. ShopLocal competitors in the online circular space are few, but very active. Recent trends include a surge in mobile usage driven by smartphone adoption (53% of cell phone users according to comScore) as well as “showrooming” in which the consumer researches prices at other competitive stores while shopping via mobile phone. Media fragmentation continues to challenge retailers and ShopLocal is well positioned to deliver solutions to meet this challenge. ShopLocal’s distribution capabilities allows retailers and brands to distribute any type of deal content to social, advertisements, third-party web sites and any other digitally connected devices.
Regulation and legislation (for digital segment businesses and digital operations associated with publishing and broadcasting businesses): The U.S. Congress has passed legislation which regulates certain aspects of the Internet, including content, copyright infringement, taxation, access charges, liability for third-party activities and jurisdiction. In addition, federal, state, local and foreign governmental organizations have enacted and also are considering other legislative and regulatory proposals that would regulate the Internet. Areas of potential regulation include, but are not limited to, user privacy and intellectual property ownership. With respect to user privacy, the legislative and regulatory proposals would regulate behavioral advertising, which specifically refers to the use of user behavioral data for the creation and delivery of more relevant, targeted Internet advertisements. Some Gannett properties leverage certain aspects of user behavioral data in their solutions.

Broadcasting Segment
Gannett Broadcasting had its best year in history in 2012 with record revenues and record operating income along with significant share growth. Operating revenues finished 25% above last year for the full year. The company benefited from both record Olympic and political revenues this year.
The 2012 Summer Olympic Games were the most viewed television event in U.S. history. More than 219 million Americans tuned into the games, and Gannett local stations helped drive those numbers. KUSA in Denver was the top rated NBC affiliate in adults ages 25 to 54. Gannett stations in Atlanta and Minneapolis were second and third respectively. With Gannett TV stations in St. Louis, Cleveland and Phoenix, six out of the top ten NBC affiliates were Gannett stations. Gannett brought a lot of new major local advertisers into the 2012 Olympics and is already working with them on renewals for the 2014 Sochi Winter Games. Gannett Broadcasting finished the Olympics with $37 million in billing, up 58% from the Beijing Olympics in 2008.
Gannett TV stations have a solid footprint for strong political activity and ended the year with $150 million of political revenue, a company record by a significant margin, leveraged through strong stations and strong local news positions (approximately $4 million of political advertising aired during the Olympics and is included in both the political and Olympic categories).
Digital revenues in the Broadcasting Segment finished up 11%, and retransmission revenues for the year finished 21% above last year.
At the end of 2012, the company’s broadcasting division, headquartered in McLean, VA, included 23 television stations in markets with nearly 21 million households covering 18.1% of the U.S. population. The broadcasting division also includes the Captivate Network.
At the end of 2012, the broadcasting division had approximately 2,600 full-time and part-time employees, approximately 1.1% more than at the end of 2011.

The principal sources of the company’s television revenues are: 1) local advertising focusing on the immediate geographic area of the stations; 2) national advertising; 3) retransmission of the company’s television signals on satellite and cable networks; 4) advertising on the station’s web and tablet and mobile products; and 5) payments by advertisers to television stations for other services, such as the production of advertising material. The advertising revenues derived from a station’s local news programs make up a significant part of its total revenues. Captivate derives its revenue principally from national advertising on video screens in elevators of office buildings and select hotel lobbies. As of year-end, Captivate had over 10,000 video screens located in 25 major cities across North America.
Advertising rates charged by a television station are based on the ability of a station to deliver a specific audience to an advertiser. The larger a station’s ratings in any particular day part, the more leverage a station has in asking for a

price advantage. As the market fluctuates with supply and demand, so does the station's pricing. Almost all national advertising is placed through independent advertising representatives. Local advertising time is sold by each station's own sales force.

Generally, a network provides programs to its affiliated television stations and sells on its own behalf commercial advertising for certain of the available ad spots within the network programs. The company's television stations produce local programming such as news, sports, and entertainment.

For all of its stations, the company is party to network affiliation agreements as well as cable and satellite carriage agreements. The company's 12 NBC-affiliated stations have agreements that expire on Jan. 1, 2017. The agreements for the company's six CBS affiliates expire on Dec. 31, 2015. The company's three ABC affiliates have agreements which expire on Feb. 28, 2014. The company's two MyNetworkTV-affiliated stations have agreements that expire in October 2014.

In 2012, the company completed retransmission negotiations with several providers including cable and satellite operators. All are multi-year agreements that provide the company with significant and steady revenue streams. There are no incremental costs associated with this revenue and therefore all of these revenues contribute directly to operating income. Retransmission revenues are expected to grow significantly in 2013.

As part of the company's growing engagement and innovation with social media, Gannett joined 9 leading television broadcast groups and invested in a long-term commercial partnership with a Silicon Valley-based start-up called ConnecTV. ConnecTV, launched in 2012, is a social television network for TV fans. On Feb. 5, 2012, Gannett entered into a public "Beta" testing period with ConnecTV for the kickoff of Super bowl XLVI. Consumers used the ConnecTV service on their iPads and computers to experience "synced" companion news, polls, player bios and to participate in online chats with other social TV users.

In June 2012, with a significantly improved technology platform and user interface as well as the addition of a core content-development team, ConnecTV "soft launched" its new product with digital promotions and TV spots across the Garnet Media Co., LLC stations, including Belo Corp., Cox Media Group, E.W. Scripps Co., Gannett Broadcasting, Hearst Television Inc., Media General Inc., Meredith Corp., Post-Newsweek Stations Inc., Raycom Media and Schurz. In August 2012, the social TV service was used by 100,000 consumers as its Olympics coverage for the "second" screen rolled out with special companion Games content.

The ConnectTV engineering team also developed a first-ever Ad Sync Network that synchronizes the television advertising experience with companion marketing on the second screen – enabling users to take action on a TV ad that includes the ability to Buy Now, Find the Closest Store, Play Product Videos, Enter a Contest and other "activations" that extend the TV branding experience.

In the fourth quarter of 2012, ConnecTV signed a Charter Programming revenue deal with CBS Television Distribution focused on "Entertainment Tonight" tuned-alerts and co-marketing. This effort also features Entertainment Tonight-ConnecTV co-branded television spots and digital promotion, as well as "Entertainment Tonight" talent appearing in ConnecTV's WATERCOOLER chat venue.

ConnecTV was honored this past year as "The Best Ubiquitous Social TV Network" by the Social TV Summit as its numbers and industry awareness continued to grow.

Programming and production: The costs of locally produced and purchased syndicated programming are a significant portion of television operating expenses. Syndicated programming costs are determined based upon largely uncontrollable market factors, including demand from the independent and affiliated stations within the market. In recent years, the company's television stations have emphasized their locally produced news and entertainment programming in an effort to provide programs that distinguish the stations from the competition, to increase locally responsible programming, and to better control costs.

Gannett TV stations led the way in covering major news events during 2012. Gannett's 12 NBC stations were front and center for the 2012 London Olympics and were home to Super Bowl XLVI. While the company's broadcast markets had no local team in the Super Bowl game, Gannett stations took advantage of the enormous audience and four stations were among the top 10 rated stations (adults ages 25 to 54) for the 2012 Super Bowl: KARE in Minneapolis-St. Paul, MN (No. 3), KUSA in Denver, CO (No. 6), WXIA in Atlanta, GA (No. 8) and WKYC in Cleveland, OH (No. 9).

Maximizing its use of cross-divisional content and resource sharing for the 2012 London Olympics, Gannett Broadcasting sent teams from eight stations to London where they combined forces with USA TODAY to provide the most comprehensive coverage of any local media group. Hundreds of stories produced stateside, combined with hundreds of live shots outside Olympic Stadium, helped Gannett TV stations dominate coverage. Highlights included KUSA in Denver's coverage of hometown four-time gold medalist Missy Franklin and WXIA in Atlanta co-anchoring its morning show from London during the Games. Gannett Broadcasting also teamed with USA TODAY and USCP to provide extensive coverage of Hurricanes Isaac and Sandy. Locally, KUSA led coverage of a tragic movie theater shooting in Aurora, CO, and followed with informative coverage of the worst wild fire season in a decade. KPNX and Republic Media were honored for their coverage of a massive dust storm that blanketed Phoenix, and First Coast News in Jacksonville, FL, produced in-depth coverage of a local high school student who was killed during a confrontation over loud music.

Tampa was the host city of the 2012 Republican Convention and WTSP in Tampa-St. Petersburg, FL, anchored live from the convention for five straight days. WTSP provided hours of extended coverage that included nightly 7 p.m. specials, expanded 11p.m. newscasts, fact-checking political spots and working with USA TODAY to provide a live webcast each day.

With the Democratic Convention in Charlotte, NC, WFMY in Greensboro, NC, anchored its newscasts from the convention as well. Both WTSP's and WFMY's efforts reflect a division-wide commitment to providing informative political coverage to consumers.

Gannett Broadcasting also continued its pursuit of providing innovative, relevant local newscasts to consumers using its "9 Areas of Focus" as a guide. Two areas of particular attention for stations in 2012 were the "Watchdog" and "Advocacy" categories. WUSA in Washington, DC, took on the issue of teenage drinking; WXIA in Atlanta investigated wrongful parking fines; KUSA in Denver showed how dozens of children have been "Failed to Death"; KPNX in Phoenix produced a series called "30 Ways in 30 Days," which highlighted how consumers could help Arizona's children in need; WLTX in Columbia, SC, broke news of the cyber intrusion of the South Carolina Department of Revenue's web site by data thieves and, working with The Greenville (SC) News and USA TODAY, reported the stories of hundreds of thousands of residents who had personal information compromised; WFMY in Greensboro, NC, worked with Guilford County schools to encourage students to read three million books in three

months, and, for the first time, the school district reached its goal; and, as a result of reporting by WMAZ in Macon, GA, a railroad crossing gate was installed where a woman had been killed by a train.

Gannett Broadcasting began rolling out a new graphics and music package at year end, with full implementation expected to be completed in April 2013. Based on feedback from viewers, the new look is clean, sharp and easy to read and uses USA TODAY's signature section color-coding system; news is blue, money is green, sports is red, life is purple.

Gannett Broadcasting stations continue to be recognized by their peers for outstanding work. KARE in Minneapolis-St. Paul and KUSA in Denver won three national Edward R. Murrow awards for locally produced work. In addition, thirty-one regional Edward R. Murrow Awards were presented to Gannett television stations, including three Overall Excellence Awards received by KARE, WGRZ in Buffalo, NY, and KTHV in Little Rock, AR. WXIA in Atlanta was recognized with three National Association of Black Journalists Awards of Excellence in three different categories. Along with the Gannett Graphics Group, six Gannett broadcasting stations, WXIA, WCSH in Portland, ME, KPNX in Phoenix, AZ, WZZM in Grand Rapids, MI, WKYC in Cleveland, OH, and WGRZ won Promax Awards in promotion and marketing and Gannett TV stations across the country combined to win more than 100 AP and Regional Emmy Awards for outstanding journalism. KUSA won its 13th straight Colorado Broadcasters Station of the Year Award, and WUSA was recognized by Mothers Against Drunk Driving (MADD) for its series on teenage drinking.

Competition: In each of its broadcasting markets, the company's stations and affiliated digital platforms compete for revenues with other network-affiliated and independent television and radio broadcasters and with other advertising media, such as cable television, newspapers, magazines, direct mail, out-of-home advertising and Internet media. Other sources of present and potential competition for the company's broadcasting properties include home video and audio recorders and players, direct broadcast satellite, low-power television, radio, video offerings (both wire line and wireless) of telephone companies as well as developing video services. The stations also compete in the emerging local electronic media space, which includes Internet or Internet-enabled devices, handheld wireless devices such as mobile phones and tablets, social media platforms, and digital spectrum opportunities associated with DTV. The company's broadcasting stations compete principally on the basis of their audience share, advertising rates and audience composition.

The Broadcast Segment continues to focus on increasing engagement on all platforms with local customers. As was the case the last several years, Gannett television stations saw very strong growth in digital metrics as the stations' content remains in high demand and product improvements continue to be favorably

received by consumers. Overall in 2012, online visitors increased 20%. Mobile page views are up 195% in 2012, and customers are consuming more content when they visit. Mobile page views per visitor are up 65%, primarily because of the iPhone, Android and Weather apps. Preliminary numbers are positive for the recently launched iPad apps, and the company expects greater consumer adoption with increased tablet penetration.

Video remains the most valuable content from an advertising perspective. On demand video plays increased 33% in 2012 while live video plays increased 500%. This is a result of continued technology improvements, workflow enhancements and viewer demand. Often breaking news happens when people are at work and unable to view a traditional TV. Desktop and mobile video are allowing company broadcast stations to reach consumers no matter where they are, or which device they have available.

Broadcast focused on building engagement in social media in 2012. The synergistic relationship between social media and television is strong. From major sporting events such as the Super Bowl, March Madness and the Olympics to major news events like the shootings in Newtown, CT, and Aurora, CO, to national and local election coverage to entertainment programming such as “The Voice,” social media influenced what people watched, what they shared and what they talked about. Gannett Broadcast Facebook fans increased over 33% in the last half of 2012 and Twitter followers were up over 21%.

Regulation: The company’s television stations are operated under the authority of the Federal Communications Commission (FCC), the Communications Act of 1934, as amended (Communications Act), and the rules and policies of the FCC (FCC Regulations).

Television broadcast licenses are granted for periods of eight years. They are renewable upon application to the FCC and usually are renewed except in rare cases in which a petition to deny, a complaint or an adverse finding as to the licensee’s qualifications results in loss of the license. The company believes it is in substantial compliance with all applicable provisions of the Communications Act and FCC Regulations. Nine of the company’s stations, including two stations with pending renewal applications from 2004, filed for FCC license renewals in 2012. As of Feb. 15, 2013, the renewals remain pending and the company expects the renewals filed in 2012 to be granted in the ordinary course. The company will be filing additional license renewal applications in 2013, including three for stations with pending renewal applications filed in 2005, and anticipate that these applications also will be granted in the ordinary course.

FCC regulation also limits concentration of broadcasting control and regulate network and local programming practices. FCC Regulations governing multiple ownership limit, or in some cases prohibit, the common ownership or control of most communications media serving common market areas (for example, television and radio; television and daily newspapers; or radio and daily newspapers). In addition, the Communications Act includes a national ownership cap under which one company is permitted to serve no more than 39% of all U.S. television households (the company’s 23 television stations currently reach approximately 18.1% of U.S. television households). FCC rules permit common ownership of two television stations in the same market in certain defined circumstances, provided that at least one of the commonly owned stations is not among the market’s top four rated stations at the time of acquisition and at least eight independent media “voices” remain after the acquisition.

FCC regulation prohibits a television station owner from owning a daily newspaper in cases where the station’s contour encompasses the newspaper’s city of publication. In 2007, the FCC granted a permanent waiver authorizing the company’s continued ownership of both KPNX-TV and The Arizona Republic in Phoenix, AZ. The FCC also adopted a waiver standard for the newspaper/broadcast cross-ownership rule, but the pertinent part of the order was vacated on appeal, and thus the waiver standard never went into effect. The appeals court rejected a challenge to the FCC’s retention of the local television ownership rule. In addition, the FCC has commenced a new review of its ownership rules, as it is required to do every four years, and this review may result in additional rule modifications. The FCC has proposed to retain the local television ownership rule (but is seeking comment on a possible waiver standard for smaller markets), and has proposed a modest relaxation of the newspaper/broadcast rule (similar to the waiver standard that the FCC had adopted during the last ownership review that was rejected in court). However, the waiver standard may be of limited value for the company in permitting expanded ownership opportunities, because it contains presumptions that, in the top 20 television markets, common ownership of a television station and a daily newspaper may be permitted only if the station is not one of the top four rated stations; most of the company’s stations are rated number one or two in their markets. The FCC’s notice of proposed rulemaking also seeks comment about

shared services agreements and local news agreements, including whether such arrangements should be attributable for purposes of the ownership rules. An order in this proceeding is expected in 2013.

Congress and the FCC are considering possible changes to the Communications Act and to other FCC regulations, respectively, including the rules concerning retransmission consent (which govern cable and satellite operators' carriage of the signals of the company's stations); the statutory cable and satellite copyright regime; and the rules and policies concerning the specific amount and type of public-interest programming required to be carried by broadcast stations to satisfy their license obligations and requirements concerning the disclosure of such programming efforts. The current retransmission consent rules are working overall. There continues to be few retransmission disputes with virtually all negotiations completed successfully. In addition, as authorized by and pursuant to certain requirements established by Congress in 2012, the FCC is seeking comment on rules to govern a "repacking" of the television spectrum, which may entail the company's stations moving to different channels, having smaller service areas, and /or accepting additional interference.

Employees

At the end of 2012, the company and its subsidiaries had approximately 30,700 full-time and part-time employees including 2,200 for CareerBuilder. At certain operations, headcount reductions were made in 2012 as part of efficiency and consolidation efforts.

Approximately 10% of those employed by the company and its subsidiaries in the U.S. are represented by labor unions. They are represented by 60 local bargaining units, most of which are affiliated with one of seven international unions under collective bargaining agreements. These agreements conform generally with the pattern of labor agreements in the publishing and broadcasting industries. The company does not engage in industry-wide or company-wide bargaining. The company's U.K. subsidiaries bargain with two unions over working practices, wages and health and safety issues only.

The company has a 401(k) Savings Plan, which is available to most domestic non-represented employees and unionized employees who have bargained participation in the plan.

During 2008, substantially all of the participants in the Gannett Retirement Plan (GRP) and the Gannett Supplemental Retirement Plan (SERP) had their benefits under these plans frozen. Amendments were made to the existing Gannett 401(k) Savings Plan (401(k) Plan) and the Gannett Deferred Compensation Plan (DCP). Most participants whose benefits were frozen under the GRP and, if applicable, the SERP received higher matching contributions under the 401(k) Plan. The matching contribution rate generally increased from 50% of the first 6% of compensation that an employee elects to contribute to the plan to 100% of the first 5% of contributed compensation. The company also makes additional employer contributions to the 401(k) Plan on behalf of certain long-service employees. The DCP was amended to provide for Gannett contributions on behalf of certain employees whose benefits under the 401(k) Plan are capped by IRS rules. Participants whose benefits were frozen will have their benefits periodically increased by a cost of living adjustment until benefits commence.

The company provides competitive group life and medical insurance programs for full-time domestic employees at each location. The company pays a substantial portion of these costs and employees contribute the balance.

The company and its subsidiaries have various retirement plans, including plans established under some collective bargaining agreements.

As is the practice in the U.K., Newsquest employees have local staff councils for consultation and communication with local Newsquest management. Newsquest provides its employees with the option to participate in a retirement plan. In October 2010, after discussion with its pension plan trustees and employees, the decision was made to close the Newsquest defined benefit plan to future accrual, effective March 31, 2011. The plan closure was made to reduce pension expenses and funding volatility and was part of a package of measures to address the plan’s deficit. Some of the savings from closing the defined benefit plan were offset by increased membership in Newsquest’s defined contribution plan.

A key initiative for the company is its leadership and diversity program that focuses on finding, developing and retaining the best and the brightest employees, as well as a diverse workforce that reflects the fabric of the communities Gannett serves.

Environmental and Sustainability Initiatives

Gannett is committed to making smart decisions to protect the environment and manage its environmental impact responsibly. Being a good corporate citizen is a core value and the company has taken a number of steps to reduce its environmental impact and underscore its commitment to sustainability.

The company has been an industry pioneer in switching to environmentally-friendly press products, such as low-VOC (Volatile Organic Compound) washes and fountain solutions and citrus-based press cleaners. All colored inks and many black inks the company uses are soy-based rather than petroleum-based, and delivered in reusable containers. Gannett’s waste ink is recycled, either on-site or at the manufacturer’s facility. The company continues to minimize landfill usage by collecting used paper, plastics and other materials for recycling and has substantially reduced water usage by switching to dry methods of photo processing and plate processing.

Gannett has reduced green house emissions by using newsprint vendors who practice sustainability, switching to light-weight newsprint, reducing the size of the newspapers printed, and using recycled and Forest Stewardship Council (FSC)-certified newsprint where available.

The company also is focused on being energy efficient. Its headquarters building received the Leadership in Energy and Environmental Design (LEEDS) EB certification, and the company has relocated many employees in other facilities to newer, more energy efficient offices.

Gannett has installed more energy efficient HVAC systems and appliances in many of its buildings. In 2011-2012 alone, Gannett’s HVAC upgrade program resulted in a reduction of 10.7 million kilowatt hours of annual electricity use. In 2012, Gannett also invested in energy efficient lighting upgrades at two locations. For 2013, Gannett has identified new projects estimated to reduce power consumption further by approximately 2.8 million kilowatt hours annually.

The Gannett Green Operating Employee Group serves as a forum to review and recommend “green” ideas and practices. The group maintains an intranet site that provides an accessible, informative and interactive resource highlighting new and innovative green best practices which help Gannett businesses and properties develop more sustainable operating

practices.

Many of Gannett's media organizations cover environmental and sustainability issues and inspire action. One good example is USA TODAY, which was recognized for “Ghost Factories: Poison in the Ground.” The series won four national awards, including the Alfred I. duPont-Columbia Award from the Columbia Journalism School. The investigative report uncovered hundreds of forgotten lead factories and the toxic lead left behind. The series drew calls for action from seven U.S. senators and led the EPA to re-examine health risks at 464 sites nationwide.

Make A Difference Day, created by USA WEEKEND, is the nation’s largest day of volunteering. For more than 20 years, USA WEEKEND has mobilized millions of people across the U.S. for this National Day of Doing Good. Together with its hundreds of carrier newspapers and longstanding partners Points of Light and Newman’s Own, it rallies millions of people in a single day to help the change communities they live in. Volunteer efforts often include projects such as planting trees or gardens, cleaning up trash, planting sod and other environmentally beneficial tasks.

The Gannett Foundation is a corporate foundation sponsored by the company. Through its Community Grant Program, Gannett Foundation supports non-profit activities in the communities in which Gannett does business and contributes to a variety of charitable causes. One of Gannett Foundation’s community action grant priorities includes environmental conservation.

General Company Information

Gannett was founded by Frank E. Gannett and associates in 1906 and was incorporated in 1923. The company listed shares publicly for the first time in 1967. It reincorporated in Delaware in 1972. Its more than 230 million outstanding shares of common stock are held by approximately 7,960 shareholders of record in all 50 states and several foreign countries. Gannett’s headquarters is in McLean, VA, near Washington, DC.

Mobile and Tablet: Gannett powers more than 400 local mobile and tablet products and also partners with mobile service providers to power news alerts and mobile marketing campaigns. Gannett has also developed and deployed leading applications for iPad, iPhone, Kindle, Android and Windows.

MARKETS WE SERVE

DAILY LOCAL MEDIA ORGANIZATIONS AND AFFILIATED DIGITAL PLATFORMS

State Territory	City	Local media organization/web site	Average 2012 Circulation - Print and Digital Replica and Non-Replica Morning	Afternoon	Sunday	Founded
Alabama	Montgomery	Montgomery Advertiser www.montgomeryadvertiser.com	30,654		39,851	1829
Arizona	Phoenix	The Arizona Republic www.azcentral.com	296,934		516,753	1890
Arkansas	Mountain Home	The Baxter Bulletin www.baxterbulletin.com	8,960			-

Common stock options exercised	-	-	1,000		3,120	-	
Common stock options expensed	-	-	-		-	115,137	
Common stock grants	-	-	-		-	13,623	
Net loss	-	-	-		-	-	
Balances at December 31, 2010	-	$-	40,179,194	$	141,654,375	$3,825,04	

See accompanying notes

CARACO PHARMACEUTICAL LABORATORIES, LTD.
FORM 10-Q

NOTES TO UNAUDITED FINANCIAL STATEMENTS

1. BASIS OF PRESENTATION

The balance sheet as of March 31, 2010 has been derived from our audited financial statements for the year then ended. All other financial statements contained herein are unaudited. In the opinion of management, all adjustments necessary for a fair presentation of such financial statements have been included. Such adjustments consisted only of normal recurring items, with the exception, in first and second quarters of Fiscal 2010, which ended June 30, 2009 and September 30, 2009, respectively, of a write-off of inventory seized by the U.S. Food and Drug Administration ("FDA") and non-recurring income, as discussed below. Interim results are not necessarily indicative of results for the full fiscal year.

The financial statements contained herein should be read in conjunction with the financial statements and notes thereto included in our Annual Report on Form 10-K as of and for the year ended March 31, 2010 of Caraco Pharmaceutical Laboratories, Ltd. ("Caraco," the "Company," or the "Corporation" and which is also referred to as "we," "u or "our").

The accounting policies followed by the Corporation with respect to the unaudited interim financial statements are consistent with those stated in the Corporation's Annual Report on Form 10-K.

2. ORGANIZATION AND NATURE OF BUSINESS

Caraco is a corporation organized under Michigan law in 1984, engaged in the business of developing, licensing, manufacturing, marketing and distributing generic prescription and over-the-counter pharmaceuticals to the nation's largest wholesalers, distributors, chain drugstores and managed care providers, throughout the U.S and Puerto Rico. The Company's primary facility, measuring approximately 222,000 square feet, is located in Detroit, Michigan, which contains our production, research and development and corporate office. In addition, the Company has a packaging facility located in Farmington Hills, Michigan and a leased warehouse, measuring approximately 137,500 square feet, located in Wixom, Michigan for finished goods distribution and storage of inventory.

A generic pharmaceutical is the chemical and therapeutic equivalent of a brand-name drug as to which the patent and/or market exclusivity has expired. Generic pharmaceuticals are well accepted for substitution of brand pharmaceuticals (which substitution is regulated by individual state regulations) as they sell at a discount to the branded product's price and have been determined to be their equivalent in quality and bioavailability.

Our present product portfolio includes 52 prescription products, in 117 strengths, in various package sizes. This represents products we distribute for Sun Pharmaceutical Industries Limited, a specialty pharmaceutical corporation organized under the laws of India ("Sun Pharma") pursuant to two agreements (See "6 Sun Pharmaceutical Industries Limited" below) and Caraco-owned products (those products for which Caraco owns the Abbreviated New Drug Applications ("ANDAs")) manufactured by Sun Pharma or other third parties. This does not include those Caraco-owned products which are manufactured at its facilities, for which the Company has temporarily ceased manufacturing and marketing, due to the enforcement actions of the FDA. The products are intended to treat a variety of disorders including but not limited to the following: hypertension, arthritis, epilepsy, diabetes, depression and pain management.

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Since August 1997, Sun Pharma has contributed equity capital and had advanced us loans. In addition, among other things, Sun Pharma had acted as a guarantor on loans to Caraco, had supplied us with a substantial portion of raw materials for our products, helped us obtain machinery and equipment to enhance our production capacities, transferred certain generic products to us, manufactures certain Caraco-owned products and provides us with qualified technical professionals. Sun Pharma has also provided services as a Clinical Research Organization, ("CRO") by performing certain bio-equivalency studies on our future potential products. Sun Pharma beneficially owns approximately 76% of the outstanding shares of the Company. (See "Current Status of the Corporation" and "Sun Pharmaceutical Industries Limited" below.)

In addition to its substantial relationship with and dependence on Sun Pharma as described above, the Corporation is subject to certain risks associated with companies in the generic pharmaceutical industry. Profitable operations are dependent on the Corporation's ability to market its products at reasonable profit margins. In addition to maintaining profitable operations, the ongoing success of the Corporation will depend, in part, on satisfying the terms of the previously disclosed Consent Decree of Condemnation, Forfeiture and Permanent Injunction ("Consent Decree"), and on its continuing ability to attract and retain key employees, obtain timely approvals of its ANDAs, and develop new products.

3. CURRENT STATUS OF THE CORPORATION

The Company has been actively working with current good manufacturing practice ("cGMP") consultants towards the resumption of manufacturing activities at its facilities. These consultants were appointed by the Company in accordance with the previously disclosed Consent Decree, which the Company entered into with the FDA on September 29, 2009. The Company's remediation efforts towards the resumption of manufacturing and distribution from its facilities are still ongoing, but the Company is unable to predict when such manufacturing and distribution will resume. The Company had previously disclosed its belief that two products would commence manufacture at its Michigan facilities prior to the end of Fiscal 2011. In evaluating and discussing with the cGMP experts the remediation steps completed to date and those yet to be completed, the Company has determined that it will not be able to begin the manufacture and distribution of products by the end of Fiscal Year 2011. As previously disclosed, and is always the case in matters such as these, there is no assurance that the remediation efforts will be successful or result in resolution of the FDA compliance issues.

The FDA approved the Company's work plan on March 17, 2010, and the Company is in the process of implementing the corrective actions and remedial measures as stipulated in the work plan. On June 24, 2010, the FDA notified Caraco that its protocol for third party cGMP certification and batch certification, detailing the activities to be conducted by the cGMP consultants, was acceptable.

On June 25, 2010, the FDA released certain previously seized raw materials which had been opened solely for the purpose of sampling. In September 2010, the FDA released other seized materials, which were disposed of in September 2010, in accordance with the Consent Decree. As a result, the Company is now released from the Bond obligation under the Consent Decree. Accordingly, the Letter of Credit, in the amount of $15 million, which was issued in favor of FDA against this Bond, expired on October 9, 2010, and has not been renewed.

As a result of the previously disclosed FDA actions, there has been a material adverse effect on our current operations and there may be a material adverse effect on our future operations. Under the terms of the Consent Decree, before resuming the manufacture of any product in the Company's facilities, a number of significant steps and processes are required to be completed, and certifications and approvals from both outside experts and the FDA are to be obtained.

All of the Company's prior approved products, together with the new products pending approval from the FDA, will be subject to these same processes, certification and approvals as set forth in the Consent Decree. The Company believes that, even assuming a successful remediation process, it will take significant time before the Company reaches its previous levels of manufacturing in its facilities. We are not able at this time to estimate the cost of these actions, which will be substantial, and once manufacturing resumes, will include the costs of operating our manufacturing facility at volumes well below the facility's capacity. The Consent Decree also requires the Company to abide by certain conditions and restrictions. If the Company violates any portion of Consent Decree, it could incur monetary fines and other penalties.

The Company intends to augment the loss of sales of manufactured products by the sale of Caraco- owned products manufactured at third party sites and through sales of distributed products, which are not impacted by the aforementioned actions of the FDA. However, any disruption in the supplies of the products manufactured by these third party sites due to cGMP issues, changes in the market conditions or any other issues would significantly affect the revenues from such products.

In addition to certain Caraco-owned products manufactured by Sun Pharma and its affiliates, we have transferred certain Caraco-owned products to alternate manufacturing sites of Sun Pharma and its affiliates that would allow the Company to realize revenues from those products. We have filed with the FDA supplements to ANDAs, for its approval, for these transferred products. There is no assurance that such approvals will be granted.

As previously disclosed, on December 3 2010 the Company received a proposal (the "Proposal") from Sun Pharma and Sun Pharma Global, Inc. ("Sun Global") for a going private transaction by which Sun Pharma and Sun Global, and/or one or more of their affiliates, would acquire all of the outstanding shares of the Company's common stock not held by Sun Pharma or Sun Global for $4.75 in cash per share. Subsequently, the Company's Board of Directors authorized the Independent Committee of the Board to:;(1) consider the Proposal including, but not limited to, reviewing (a) whether going private is appropriate for Caraco at this time is advisable or is inadvisable and should be rejected, (b) possible alternatives to the Proposal or opportunities which may be more advantageous to Caraco, and (c) the merits of the Proposal; (2) if deemed advisable, enter into discussions and negotiations with respect to the terms of the Proposal, including the proposed per share purchase price, with Sun Pharma and their advisors; and (3) make recommendations to the Board of Directors and as applicable, to the stockholders as to the Independent Committee's findings. The Independent Committee has also retained William Blair & Company as an independent financial advisor, and Carrington Coleman law firm as independent legal counsel, to assist it in evaluating the Proposal.

As previously disclosed, the Company's two distribution agreements with Sun Pharma have been extended until January 28, 2012, but will each terminate following these extensions. The Company and its Independent Committee of the Board approached Sun Pharma and attempted to negotiate long term renewals for each agreement; however, Sun Pharma exercised its right to end the agreements, following these extensions, on January 28, 2012. During the first six months of calendar 2011, the Company and Sun Pharma will discuss a transition plan to transition the marketing of the products covered by the respective agreements to Sun Pharma and/or its wholly-owned affiliates. Thereafter, if the parties have reached an understanding with respect to the transition plan, the parties will implement the transition plan so that upon the termination of the agreements Sun Pharma and its affiliates will commence marketing of the products. If the parties have not agreed on a transition plan prior to January 28, 2012, the agreements will still terminate on that date.

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During the third quarter ended December 31, 2010 and first nine months of our current fiscal year ("Fiscal 2011") ended December 31, 2010, we generated net sales of $40.4 million and $268.2 million, respectively, as compared to $52.0 million and $178.4 million, respectively, for the corresponding periods of our previous fiscal year ("Fiscal 2010") ended December 31, 2009. During the third quarter and first nine months of Fiscal 2011, sales of Caraco-owned products were $5.7 million and $16.7 million, respectively, as compared to $3.3 million and $18.9 million, respectively, during the corresponding periods of Fiscal 2010. The sales of distributed products during the third quarter and first nine months of Fiscal 2011 were $34.7 million and $251.5 million, respectively, as compared to $48.7 million and $159.5 million, respectively, during the corresponding periods of Fiscal 2010. We earned a gross profit of $3.3 million and $22.4 million during the third quarter and first nine months of Fiscal 2011, respectively, as compared to earning a gross profit of $3.1 million and incurring a gross loss of $4.7 million, respectively, during the corresponding periods of Fiscal 2010. We incurred pre-tax losses of $4.8 million and $5.2 million, respectively, during the third quarter and first nine months of Fiscal 2011, as compared to incurring pre-tax losses of $4.9 and $8.8 million during the respective periods of Fiscal 2010. The Company recorded an income tax benefit of $1.8 million and $1.9 million, respectively, for the third quarter and first nine months of Fiscal 2011, as compared to recording income tax benefits of $1.9 million and $3.0 million during the corresponding periods of Fiscal 2010. We incurred net losses of $3.0 million and $3.3 million, respectively, during the third quarter and first nine months of Fiscal 2011, as compared to incurring net losses of $3.0 million and $5.8 million, respectively, during the corresponding periods of Fiscal 2010. We generated cash from operations in the amount of $2.5 million during the first nine months of Fiscal 2011, as compared to generating cash from operations in the amount of $15.5 million during the corresponding period of Fiscal 2010. At December 31, 2010, we had stockholders' equity of $152.2 million, as compared to stockholders' equity of $155.4 million at March 31, 2010. (See "Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations" for further information).

We filed two ANDAs relating to two products with the FDA during the first nine months of Fiscal 2011. These products have been developed in partnership with other product development and manufacturing companies, one of which is an affiliate. We have not received FDA approval for any ANDAs since the first quarter of Fiscal 2009 and do not expect to receive any approvals for products out of our facilities until we resolve the FDA's concerns as discussed above. The total number of ANDAs pending approval by the FDA as of December 31, 2010 was 33 (including four tentative approvals) relating to 29 products. Out of the 33 ANDAs pending approval, 31 (including four tentative approvals) are from our Detroit, Michigan manufacturing facility and the remaining two are from the manufacturing sites of our partner companies.

4. RECENT ACCOUNTING PRONOUNCEMENTS

In December 2010, the FASB issued an update on (Topic 720) Other Expenses, Relating to Fees paid to the Federal Government by Pharmaceutical Manufacturers, defining how pharmaceutical manufacturers should recognize and classify in their income statements fees mandated by the Patent Protection and Affordable Care Act as amended by the Health Care and Education Reconciliation Act (Accounting Standards Update No. 2010-27). This guidance specifies that liability for the annual fees which will be imposed on the pharmaceutical manufacturers by these acts starting January 2011, based upon the gross receipts from sale of branded prescription drugs to any specified government program or in accordance with coverage under any government program, should be estimated and recorded in full upon the first qualifying sale with a corresponding deferred cost that is amortized to expense using a straight-line method of allocation or any other method which is provides better allocation The amendment is effective for calendar years which begins on January 1, 2011. Management is currently evaluating the impact of the adoption of this amendment on the Corporation's financial statements.

5. COMPUTATION OF LOSS PER SHARE

Loss per share is computed using the weighted average number of common shares outstanding during each period and considers a dual presentation and reconciliation of “basic” and “diluted” per share amounts. Diluted reflects the potential dilution of all common stock equivalents.

The basic and diluted weighted average numbers of common shares outstanding for the third quarter of Fiscal 2011, were both 39,788,933, and were both 39,397,227 for the first nine months of Fiscal 2011. Correspondingly, the basic and diluted weighted average numbers of common shares outstanding for the third quarter of Fiscal 2010, were both 39,090,194, and were both 38,457,176 for the first nine months of Fiscal 2010.

6. SUN PHARMACEUTICAL INDUSTRIES LIMITED

The Company has a long relationship with Sun Pharma, a Mumbai, India based specialty pharmaceutical manufacturing company. In 1997 Sun Pharma made an initial investment of $7.5 million for the purchase of 5.3 million common shares of Caraco. Currently Sun Pharma beneficially owns approximately 76% of the outstanding shares of the Company. The Company and Sun Pharma have entered into various transactions and agreements including those referenced hereunder.

On December 3, 2010, the Company received a Proposal from Sun Pharma and Sun Global for a going private transaction by which Sun Pharma and Sun Global, and/or one or more of their affiliates, would acquire all of the outstanding shares of the Company’s common stock not held by Sun Pharma or Sun Global for $4.75 in cash per share. Subsequently, the Company’s Board of Directors authorized the Independent Committee of the Board to: (1) consider the Proposal including, but not limited to, reviewing (a) whether going private is appropriate for Caraco at this time is advisable or is inadvisable and should be rejected, (b) possible alternatives to the Proposal or opportunities which may be more advantageous to Caraco, and (c) the merits of the Proposal; (2) if deemed advisable, enter into discussions and negotiations with respect to the terms of the Proposal, including the proposed per share purchase price, with Sun Pharma and their advisors; and (3) make recommendations to the Board of Directors and as applicable, to the stockholders as to the Independent Committee's findings. The Independent Committee has also retained William Blair & Company as an independent financial advisor, and the Carrington Coleman law firm as independent legal counsel, to assist it in evaluating the Proposal.

Sun Pharma operates research and development centers in Mumbai and Vadodara in India, where the development work for products is performed.

Sun Pharma and its affiliates supply the Corporation with certain raw materials and formulations, assist in acquiring machinery and equipment to enhance production capacities, and have provided qualified technical professionals who work as Caraco employees. Also, four of the current seven directors of Caraco are, or were, affiliated with Sun Pharma.

The Corporation has also obtained technical and scientific services, including bio-equivalency studies, from the Clinical Research Organization operated by Sun Pharma. The products on which the Company decides to work with Sun Pharma are determined on a case by case basis as mutually agreed upon by both companies.

During the fiscal year ended March 31, 2007 ("Fiscal 2007"), the Corporation entered into a three-year marketing agreement with Sun Pharma, which was reviewed and approved by the Board's Independent Committee. This agreement was renewed for a period of one year in January 2010. Under the agreement, the Corporation purchases selected product formulations offered by Sun Pharma and its affiliates and markets and distributes the same as part of the current product offerings in the U.S., its territories and possessions, including Puerto Rico. Sun Pharma is not obligated to offer Caraco products under this agreement, however, Caraco has the exclusive right to market in the U.S., its territories and possessions, including Puerto Rico, any products offered by Sun Pharma and its affiliates and accepted by Caraco. This agreement has been extended and is currently scheduled to expire on January 28, 2012. The Company and its Independent Committee of the Board approached Sun Pharma and attempted to negotiate a long term renewal for the agreement; however, Sun Pharma exercised its right to end the agreement, following its extension, on January 28, 2012.

During the fiscal year ended March 31, 2008 ("Fiscal 2008"), the Corporation entered into a three-year distribution and sale agreement with Sun Pharma, which was reviewed and approved by the Board's Independent Committee. Under this agreement the Company purchases selected formulations which have been filed under Paragraph IV certification process with the FDA by Sun Pharma and its affiliates and offered for distribution. Paragraph IV certified ("Paragraph IV") products may face litigation challenges with respect to claims of patent infringement. Under the agreement the Company shares in the sales opportunity and shares the litigation risk. The Company is indemnified by Sun Pharma of any risk beyond the percentage agreed to as its profit percentage thereby limiting the Company's exposure. Sun Pharma is not obligated to offer Caraco products under this agreement, however, Caraco has the exclusive right to market in the U.S., its territories and possessions, including Puerto Rico, any products offered by Sun Pharma and accepted by Caraco. The Company markets and distributes the same as part of its current product offerings in the U.S., its territories and possessions, including Puerto Rico. The license granted with respect to a product terminates upon the end of an exclusivity period of 180 days or a non-appealable court decision, or until a third generic manufacturer launches the product, whichever is later, or until a settlement is reached, at which time the product will become part of the standard Caraco-Sun Pharma marketing agreement disclosed above. The Company currently receives a gross profit margin of 8%, or such other percentages as shall be mutually agreed upon. Under the agreement, Sun Pharma and Caraco mutually indemnify each other capped by the fixed margin percentage with respect to damages from infringement. The Company has a right to return the inventory of such products to Sun Pharma if the sale of such products is not allowed by any regulatory authority and Sun Pharma does not file a timely appeal. The Company can also return the inventory, or ask for replacements, under various conditions consistent with normal practices in the pharmaceutical industry. (See "Note 12. Litigation" for disclosure of litigation involving Paragraph IV products). The initial term of the distribution and sale agreement was set to expire on January 29, 2011. This agreement has been extended and is currently scheduled to expire on January 28, 2012. The Company and its Independent Committee of the Board approached Sun Pharma and attempted to negotiate a long term renewal for the agreement; however, Sun Pharma exercised its right to end the agreement, following its extension, on January 28, 2012.

During the third quarter and first nine months of Fiscal 2011, the Corporation made net sales of $34.7 million and $251.5 million, respectively, as compared to $48.7 million and $159.5 million, respectively during the corresponding periods of Fiscal 2010, of the marketed products under the aforesaid agreements.

On July 10, 2009, Caraco entered into an agreement with Alkaloida Chemical Company ZRT, a Hungarian corporation ("Alkaloida") an indirect subsidiary of Sun Pharma, pursuant to which Alkaloida is to provide, with respect to certain products and others agreed upon by the parties, an exclusive, non-transferable license to Caraco to manufacture and market the products in the United States, its territories and possessions, including Puerto Rico. The agreement was approved by Caraco's Independent Committee. No technology for any product has been transferred under this agreement to date. Under the agreement, Caraco is obligated, among other things, to perform all bio-equivalency studies and complete and submit ANDAs to the FDA. Any license for a product would be for a period of five years from the commencement of marketing of the product, and Caraco may extend the license for a further five year period. The agreement terminates five years from the date of approval of the first ANDA, unless renewed or extended for consecutive one year periods.

While Sun Pharma has provided substantial support to Caraco as disclosed above, there can be no assurance that such support will continue, or that the current terms and conditions will remain the same in the future.

7. ACCOUNTING FOR STOCK BASED COMPENSATION

The Company follows the provisions of ASC Topic 718, “Stock Compensation’” which requires employee share-based compensation to be accounted for under the fair value method and requires the use of an option pricing model for estimating the fair value of stock options at the date of grant. The Company estimates the fair value of stock options granted using the Black-Scholes option-pricing model, which requires the Company to estimate the expected term of the stock option grants and expected future stock price volatility over the term. The term represents the expected period of time the Company believes the options will be outstanding based on historical information. Estimates of expected future stock price volatility are based on the historical volatility of the Company’s common stock. The Company calculates the historical volatility as the standard deviation of the differences in the natural logarithms of the weekly stock closing price, adjusted for dividends and stock splits.

For the third quarter and first nine months of Fiscal 2011, the Company has recognized expenses amounting to $37,554 and $115,137, respectively, related to common stock options as compared to $44,147 and $179,725, respectively, for the corresponding periods of Fiscal 2010. As of December 31, 2010, total unrecognized compensation cost related to stock options granted was $92,423. The unrecognized stock option compensation cost is expected to be recognized over a period of approximately two years. The Company granted a total of 15,000 shares of restricted common stock to its Independent Directors during the first nine months of Fiscal 2011, which will vest at the end of each Independent Director’s respective term. The Company amortizes the expense over the vesting period and has recognized expenses amounting to $11,458 and $13,623 during the third quarter and first nine months of Fiscal 2011, respectively, related to these restricted stock grants.

8. COMMON STOCK ISSUANCES

We issued 1,000 shares of common stock to our employees upon exercise of their stock options during the first nine months of Fiscal 2011. The Company granted 15,000 shares of restricted common stock to its Independent Directors during the first nine months of Fiscal 2011, which will vest ratably on the anniversary dates through their remaining respective terms. There were no common stock issuances to Directors or employees during the first nine months of Fiscal 2010.

During the first nine months of Fiscal 2011, Sun Global converted 1,088,000 shares of Series B Preferred Stock into 1,088,000 shares of Common Stock. (See "Part II – Other Information: Item 2. Unregistered Sales of Equity Securities and Use of Proceeds" below).

9. PREFERRED STOCK ISSUANCES

No shares of preferred stock were issued during the first nine months of Fiscal 2011 or Fiscal 2010.

10. SALES AND CUSTOMERS

Net sales decreased during the third quarter and increased during the first nine months of Fiscal 2011, in comparison to the corresponding periods of Fiscal 2010, primarily as a result of lower and higher sales of distributed products, respectively. See "Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations – Third Quarter and First Nine Months Fiscal 2011 Compared to Third Quarter and First Nine Months Fiscal 2010."

As is typical in the U.S. pharmaceutical industry, many of our customers are serviced through their designated wholesalers. During the third quarter and first nine months of Fiscal 2011, shipments to the Company's three largest wholesale customers, Amerisource-Bergen Corporation, McKesson Corporation and Cardinal Health, accounted for approximately 18%, 17% and 15%, respectively, of the Company's total net sales during the third quarter and 13%, 29% and 26%, respectively, of total net sales for the first nine months of Fiscal 2011. During the corresponding periods of Fiscal 2010, shipments to Amerisource-Bergen Corporation, McKesson Corporation and Cardinal Health, accounted for approximately 14%, 11% and 6%, respectively, of the Company's total net sales during the third quarter of Fiscal 2010, and 9%, 7% and 6%, respectively, of total net sales for the first nine months of Fiscal 2010. A part of these net sales include sales to various customers of Caraco that have underlying direct contracts with our Company that are facilitated through our wholesale customers. During the first nine months of Fiscal 2011, sales to CVS Caremark Corporation were insignificant, however during the first nine months of Fiscal 2010, they accounted for approximately 52% of our net sales. A significant portion of the sales to CVS Caremark Corporation are a result of a contract between it and the Company entered into towards the end of Fiscal 2009.

11. DEBT

During the fourth quarter of Fiscal 2009, the Company entered into a term loan of $18 million with RBS Citizens, N.A. d/b/a Charter One Bank ("Charter One Bank"). The loan is secured by a mortgage covering the Company's manufacturing facility and equipment located in Detroit, Michigan. The rate of interest is calculated as LIBOR plus an applicable margin thereto (based upon various leverage levels and current applicable rate is 50 basis points). The aggregate rate applicable to the Company as of December 31, 2010 was 0.8%. (effective rate was 2.91% taking into consideration the Interest Rate SWAP Agreement entered into by the Company details of which are given hereunder). The principal loan payments and accrued interest are payable on a quarterly basis beginning July 2009. The principal is to be repaid in equal quarterly installments of $900,000 for ten quarters through October 2011, and thereafter, if not renewed, the remaining balance of $9 million is due in the subsequent quarter by January 2012. Subsequently, in October 2009 the terms of the loan were modified and we entered into an amended agreement. The amendment adds

to the loan a one year line of credit note for $15 million against which the Company can borrow funds for working capital purposes or can get letters of credit issued. Against this line of credit, the Bank issued an Irrevocable Standby Letter of Credit in an amount of $15 million, in favor of the United States of America, as required to be placed with the FDA in accordance with the Consent Decree, as disclosed above. On October 9, 2010 this Letter of Credit expired and was not renewed, as the Company was released from this obligation under the terms of the Consent Decree. The line of credit carries an interest rate of LIBOR plus 150 basis points, and if letters of credit are issued, the associated fees are 0.7% of such letters of credit on annualized basis. Also, there is an unused fee of 0.25% on an annualized basis to the extent the line remains idle. The outstanding term loan is cross collateralized by all of the Company's fixed assets and cash deposit accounts held with Charter One Bank, equivalent to the amount of outstanding loans. These cash deposits earn interest at prevailing rates applicable to such money market accounts. The Company is continuing discussions with Charter One Bank to allow the release of the cash collateral. Charter One Bank has temporarily suspended the required compliance with the covenants in the loan agreements relating to FDA enforcement actions, and has suspended certain other compliance requirements until April 9, 2011. On or before such date, the Company anticipates either entering into revised agreements or repaying the loan in full.

Currently, as the loan is in technical default due to the FDA enforcement action, the entire outstanding balance has been classified as a short-term liability on the Company's Balance Sheets.

As required pursuant to the terms of the Loan Agreement, the Company has entered into an Interest Rate Swap Agreement with Charter One Bank to hedge the interest rate applicable on the loan. The notional amount for the swap is $12.6 million which will continue to amortize down as principal payments are made on the related debt. The annualized fixed rate of interest as it applies to this agreement is 2.41%. Thus as of December 31, 2010, the effective rate of interest to the Company for the term loan was 2.91% (2.41% swap rate plus applicable margin of 50 basis points). During the third quarter and first nine months of Fiscal 2011 the Company made adjustments of $(93,000) and $40,000, respectively, to record the fair value of this swap agreement, with such amounts included in Interest expense and Accrued expenses. The fair value of this swap agreement at December 31, 2010 was ($371,000).

12. LITIGATION

While it is not possible to determine with any degree of certainty the ultimate outcome of the following legal proceedings, the Company believes that it has meritorious defenses with respect to the claims asserted against it and intends to vigorously defend its position. An adverse outcome in any of these proceedings could have a material adverse effect on the Company's financial position and results of operations.

On June 9, 2005, Novo Nordisk A/S and Novo Nordisk, Inc. ("Novo Nordisk") filed a complaint in the United States District Court for the Eastern District of Michigan alleging that the Company's filing of an ANDA seeking approval to market its generic version of Novo Nordisk's Prandin® (repaglinide) drug product infringed Novo Nordisk's U.S. Patent No. 6,677,358 (the '358 patent). Novo Nordisk seeks an order from the Court which, among other things, directs the FDA not to approve the Company's ANDA any earlier than the claimed expiration date. The Company believes that the '358 patent is invalid, unenforceable and/or will not be infringed by the Company's manufacture, use or sale of the product. The Company believes that it is the first to file an ANDA with a Paragraph IV certification for this drug product and entitled to 180 day exclusivity. On May 26, 2010, the Company received correspondence from the FDA forwarding a letter sent by Sandoz Inc. to the FDA challenging the Company's 180 day exclusivity. The Company responded, and stated to the FDA its position regarding the 180 day exclusivity.

The Company filed a supplemental answer and counterclaim challenging Novo Nordisk's Orange Book use code amendment to Prandin®, which caused the FDA to reject Caraco's request to use a non-infringing generic repaglinide label. On September 25, 2009, the District Court entered an injunction requiring Novo Nordisk to correct its amended use code description for Prandin® on the ground that it does not accurately characterize the referenced method patent. Novo Nordisk then appealed and that injunction was vacated by the Federal Circuit Court of Appeals. The Company's petition for rehearing by the panel and rehearing en banc were denied. The Company has filed a Writ of Certiorari to have the use code issue heard by the United States Supreme Court. Additionally, Caraco is seeking approval for a label that would infringe the '358 patent. The trial regarding the validity and unenforceability of the patent concluded on August 11, 2010. On January 19, 2011, the Court issued a judgment that the '358 patent is invalid because of obviousness, and not enforceable due to inequitable conduct. On January 26, 2011, Novo Nordisk filed a Notice of Appeal of the Court's ruling regarding the '358 patent. The Company has site transferred this product to an affiliate. There is no assurance that the Company will be able to take advantage of what it believes is its 180-day first filer exclusivity with respect to this product.

On May 5, 2009, Wyeth filed a complaint against the Company and Sun Pharma in the United States District Court for the Eastern District of Michigan alleging that the package insert for Sun Pharma's product that is distributed by the Company and which is a generic version of Wyeth's Protonix® (pantoprazole) pharmaceutical product, contains false and misleading statements regarding the active ingredient of that product in violation of federal and state laws. The complaint requested damages, injunctive relief and attorneys' fees and costs. On March 2, 2010, the Court dismissed Wyeth's complaint, without prejudice. On March 31, 2010, Wyeth filed a Notice of Appeal with United States District Court for the Sixth Circuit.

Additionally, Sun Pharma and Wyeth are involved in a separate Paragraph IV product lawsuit in the United States District Court for the District of New Jersey, regarding the validity of the patents in Wyeth's Protonix® (pantoprazole) product. On April 23, 2010, a Jury in the New Jersey patent lawsuit returned a verdict that the patent at issue in that case is not invalid. In the event of a Jury award of damages against Sun Pharma for patent infringement, Caraco's obligation to Sun Pharma for its portion of any such award is capped at its fixed margin percentage, in accordance with the terms of the Distribution and Sale Agreement with Sun Pharma. As a result of the ongoing patent case in the United States District Court for the District of New Jersey, Wyeth, Sun Pharma and the Company agreed to hold the above case regarding the packaging insert in abeyance. The ultimate outcome of the patent litigation cannot be determined at this time.

In 2007, Sun Pharma filed an ANDA to market a generic equivalent of Sanofi-Aventis' Eloxatin® product. The ANDA contains a paragraph IV certification of non-infringement of the patents which support Eloxatin®. Pursuant to the Distribution and Marketing Agreement with Sun Pharma, the Company currently has the right to serve as a distributor for Sun Pharma for this generic product. In July of 2007, Sanofi-Aventis U.S. LLC and certain of its affiliates filed a patent infringement action against Sun Pharma and the Company in the United States District Court for the District of New Jersey. Sanofi-Aventis also filed similar patent infringement actions against other generic manufacturers. The Court consolidated all of these pending actions. Sun Pharma and the Company denied Sanofi-Aventis' allegations and asserted affirmative defenses and counterclaims for invalidity and unenforceability of the relevant patents.

In June 2009, Sun Pharma, the Company and Sanofi-Aventis agreed to a settlement agreement and a license agreement pursuant to which Sun Pharma and the Company are authorized to market, sell and distribute an oxaliplatin product in the United States under certain conditions. In January of 2010, the Company began selling Sun Pharma's FDA-approved generic oxaliplatin product in the United States market, serving as Sun Pharma's distributor.

In March 2010, Sanofi-Aventis announced settlements with all of the other defendants in the pending patent action. Those defendants agreed to stop selling their respective generic oxaliplatin products as of June 30, 2010. Sanofi-Aventis thereafter asserted that Sun Pharma and the Company must also cease selling the generic oxaliplatin product as of June 30, 2010, pursuant to the terms of the license agreement. Sun Pharma and the Company dispute that the license agreement requires Sun Pharma and the Company to stop selling. On April 22, 2010, Sanofi-Aventis obtained a Court judgment which required Sun Pharma and the Company to cease selling generic oxaliplatin from June 30, 2010 until either August 9, 2012 or on occurrence of any event that triggers permission of sales under the license agreement. Sun Pharma and the Company successfully appealed this Court order and are considering their next steps.

On July 17, 2009 and July 23, 2009, two purported class action lawsuits were filed in the United States District Court for the Eastern District of Michigan against the Company and certain of its executive officers. The lawsuits allege securities violations related to the Company's public statements on FDA compliance issues made between May 29, 2008 and June 25, 2009. On November 9, 2009, a Stipulation and Order of Dismissal was entered by the Court dismissing one of the two cases, effectively consolidating the cases. The plaintiffs subsequently filed a consolidated and amended complaint, which also names Sun Pharma as an additional defendant. The defendants then filed a Motion to Dismiss; however, the Court denied the Motion to Dismiss, except as to one count against Sun Pharma.

On November 12, 2010, Hospira, Inc. and Orion Corporation filed a patent infringement suit in the United States District Court for the Eastern District of Michigan against the Company alleging that Caraco's ANDA for dexmedetomidine hydrochloride injection infringes U.S. Patent No. 6,716,867 (the "'867 Patent") that supports the Plaintiffs' drug Precedex®. The complaint asks the court to, among other things, order: (a) that the Company has infringed the '867 Patent; (b) that Caraco's ANDA be approved no earlier than the expiration of the '867 Patent; (c) an injunction against the Company from launching its product; and (d) a grant of attorneys fees.

On December 9, 2010, and subsequent thereto, several purported class action lawsuits were filed in the Wayne Court Circuit Court against the Company, Sun Pharma, Sun Global, and the members of the Board of Directors of the Company, arising out of the previously disclosed proposal by Sun Pharma and Sun Global to acquire all of the shares of the Company's common stock not held by Sun Pharma and Sun Global at a price of $4.75 cash per share. The suits allege breaches of fiduciary duties in relation to the Proposal and Sun Pharma and Sun Global's attempt to take the Company private at an alleged unfair price and with an unfair process. Generally, the complaints ask the Court to: (a) declare the case as a class action; (b) declare that the defendants breached their fiduciary duty; (c) declare that the Proposal is not procedurally and financially fair to the Company's minority shareholders and enjoin the transaction; (d) rule that the Company's Independent Directors are incapable of evaluating the Proposal; and (e) award any damages and attorneys fees.

Additionally, the Company received a shareholder letter dated December 14, 2010, that purports to be on behalf of a shareholder, demanding that the Board of Directors take actions to remedy the alleged breaches of fiduciary duty in connection with the Proposal.

The Company is also currently involved, and from time to time becomes involved, in certain other legal proceedings relating to the conduct of its business, including those pertaining to product liability, contract and employment claims. With respect to product liability claims, we are currently involved in a total of 16 cases, 14 of which involve products alleged to have been manufactured by the Company. The Company carries product liability insurance in an amount it believes is sufficient for its needs. The Company is also a defendant in two product liability cases, where it is alleged that the Company distributed a product manufactured by another party. In those instances, the Company is contractually indemnified by the product manufacturer. While the outcome of any of such proceedings cannot be accurately predicted, the Company does not believe that the ultimate resolution of any of these existing proceedings will have a material adverse effect on the Company's financial condition or liquidity.

13. INVENTORIES

Inventories consist of the following amounts:

	December 31, 2010	March 31, 2010
Raw materials	$ 7,774,185	$ 14,545,370
Goods in transit (Distributed)	8,216,624	28,406,006
Finished goods (Caraco- Owned)	2,163,578	4,460,252
Finished goods (Distributed)	33,897,679	55,771,222
Total Inventories	$ 52,052,066	$ 103,182,850

Total inventories at December 31, 2010 and March 31, 2010 includes materials purchased in the amount of $1,110,800 and $2,249,878, respectively, related to products for which the Company has filed ANDAs that are awaiting approval from the FDA, and the commercial launch of such products will commence once the approvals are received. We do not expect to receive any approvals for products out of our facilities until we resolve the FDA’s concerns as discussed above.

As disclosed above, certain drug products manufactured, work in process, and ingredients held, at the Company's facilities were seized at the direction of the FDA. The estimated cost of such seized inventory was $24.0 million. As stipulated in the Consent Decree, the Company attempted to have the seized inventory released. The Company believed that, except for the raw materials which were opened solely for the purpose of sampling, the estimated value of which was $8.1 million, all other seized inventory would be difficult to recondition. Accordingly, the Company had written off all other seized inventory in the amount of $15.9 million during Fiscal 2010. In accordance with the Consent Decree, on June 25, 2010, the FDA released the raw materials which were opened solely for the purpose of sampling. Subsequently, in September 2010, the FDA released all other seized materials, which were thereafter disposed of by the Company, in accordance with the Consent Decree.

14. INCOME TAXES

The benefit for income taxes is as follows:

	Nine Months Ended	
	Dec. 31, 2010	Dec. 31, 2009
Current (benefit) / expense	$ (2,744,669)	$ 4,982,518
Deferred expense / (benefit)	848,600	(7,990,708)
Total Benefit	$ (1,896,069)	$ (3,008,190)

The benefit for income taxes is different from that which would be obtained by applying the statutory federal income tax rate to income before income taxes. The items causing the difference for the first nine months of Fiscal 2011 and Fiscal 2010, respectively, are as follows:

	Nine Months Ended	
	Dec. 31, 2010	Dec. 31, 2009
Benefit for income taxes at federal statutory rate	$ (1,830,285)	$ (3,078,606)
Permanent items and other	(65,784)	70,416
Income taxes	$ (1,896,069)	$ (3,008,190)

Deferred taxes consist of the following:

	Dec. 31, 2010	March 31, 2010
Deferred tax assets:		
Net operating loss carryforwards	$ 797,631	$ 797,631
Intangibles	22,855,545	24,079,523
Other	544,845	519,554
Total deferred tax assets	$ 24,198,021	$ 25,396,708
Deferred tax liabilities:		
Depreciation	$ 2,950,452	$ 3,298,097
Total deferred tax liabilities	$ 2,950,452	$ 3,298,097
Net deferred tax assets	$ 21,247,569	$ 22,098,611

15. SEGMENT INFORMATION

The Company operates in two reportable segments consisting of (1) Caraco-owned products (those products for which Caraco owns the ANDAs) and (2) those products distributed under various agreements with Sun Pharma and its affiliates. The sales and gross profits earned on these categories of products are as follows:

Fiscal 2011:	Quarter Ended December 31, 2010		Nine Months Ended December 31, 2010	
Category	Net Sales	Gross (Loss) Profit	Net Sales	Gross (Loss) Profit
Caraco-Owned Products	$ 5,706,595	$ (590,962)	$ 16,705,339	$ (1,100,335)
Distributed Products	34,680,214	3,916,598	251,500,076	23,463,115
Total	$ 40,386,809	$ 3,325,636	$ 268,205,415	$ 22,362,780

Fiscal 2010:	Quarter Ended December 31, 2009		Nine Months Ended December 31, 2009	
Category	Net Sales	Gross (Loss) Profit	Net Sales	Gross (Loss) Profit
Caraco-Owned Products	$ 3,322,070	$ (1,124,630)	$ 18,895,700	$ (18,666,990)
Distributed Products	48,667,888	4,209,512	159,540,169	14,004,017
Total	$ 51,989,958	$ 3,084,882	$ 178,435,869	$ (4,662,973)

16. SUBSEQUENT EVENTS

None.

ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

The following discussion and analysis provides information that management believes is relevant to an understanding of the Corporation's results of operations and financial condition. The discussion should be read in conjunction with the financial statements and notes thereto and "Management's Discussion and Analysis of Financial Condition and Results of Operations" included in the Company's 2010 Annual Report on Form 10-K as of and for the year ended March 31, 2010 (the "Annual Report") and the unaudited interim financial statements included in Item 1 of this Quarterly Report on Form 10-Q.

Critical Accounting Policies and Estimates

Our significant accounting policies are described in Note 1 to our financial statements included in our Annual Report. Certain of our accounting policies are particularly important to the portrayal of our financial position and results of operations and require management's subjective judgments. As a result, these judgments are subject to an inherent degree of uncertainty. In applying these policies, management makes estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the dates of the financial statements and the reported amounts of revenues and expenses during the reporting periods. Actual results could differ from those estimates. Significant estimates include, but are not limited to, provisions for estimated customer returns, discounts, rebates and other price adjustments, including customer chargebacks, valuation allowances for deferred tax assets, valuation of overhead components in inventory and the inventory reserves. Our discussion and analysis of our financial condition and results of operations are based on our financial statements, which have been prepared in accordance with accounting principles generally accepted in the United States. There have neither been material changes to our critical accounting policies for the periods presented nor any material quantitative revisions to our critical accounting estimates for the periods presented.

Revenue Recognition

Revenue from product sales, both manufactured and distributed, net of estimated provisions, is recognized when there is persuasive evidence that an arrangement exists, title and risk of ownership have been transferred to the buyer which is assumed to occur when the product reaches its destination, the selling price is fixed or determinable, and collectibility is reasonably probable. Our customers consist primarily of large pharmaceutical wholesalers who sell directly into the retail channel, chain drug stores, distributors, and managed care customers. Provisions for sales discounts, and estimates for chargebacks, rebates, and product returns are established as a reduction of product sales revenue at the time revenues are recognized, based on historical experience and current market trends adjusted to reflect known changes in the factors that impact these reserves. These revenue reductions are reflected as a direct reduction to accounts receivable through an allowance.

The Company makes sales of products under various marketing and distribution agreements. The Company recognizes revenue from such sales in accordance with ASC Topic 605-45, "Principal Agent Considerations." The Company has evaluated the various indicators described under ASC Topic 605-45 and has determined that such revenues should be considered on a gross reporting basis. The factors include the following, which led the Company in making such determination: (1) the title of the goods have been transferred to the Company and the Company assumes all general inventory risks; (2) the Company is the primary obligor in the arrangement. (3) The Company is responsible for the sales process, pricing, marketing and delivery of the products; and (4) the Company is responsible for the collection of receivables and will have to account for bad debt losses if any occur.

Chargebacks

Chargebacks represent our most significant provision against gross accounts receivable and related reduction to gross revenue. Chargebacks are retroactive credits given to our wholesale customers that represent the difference between the lower price they sell (contractual price) to retail, chain stores, and managed care organizations and what we charge the wholesaler. We estimate chargebacks at the time of sale for our wholesale customers. We are currently unable to specifically determine whether the amounts allowed in specific prior periods for chargeback reserves have been over or understated. Wholesaler customers who submit chargebacks to the Company do not reference a specific invoice that the chargeback is related to when the chargeback is submitted to the Company. Thus, we cannot determine the specific period to which the wholesaler's chargeback relates.

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We consider the following factors in the determination of the estimates of chargebacks.

1. The historical data of chargebacks as a percentage of sales, as well as actual chargeback reports received from our primary wholesaler customers.

2. Volume of all products sold to wholesaler customers and the average chargeback rates for the current quarter as compared to the previous quarter and compared to the last six month period.

3. The sales trends and future estimated prices of our products, wholesale acquisition cost (WAC), the contract prices with the retailers, chain stores, managed care organizations (end-users), and our wholesaler customer's contract prices.

4. We utilize remaining inventories on hand at our primary wholesaler customers at the end of the period in the calculation of our estimates.

Such estimated amounts, in addition to certain other deductions, are deducted from our gross sales to determine our net revenues. The amount of actual chargebacks claimed could be either higher or lower than the amounts we accrued. Changes in our estimates, if any, would be recorded in the income statement in the period the change is determined. If we materially over or under estimate the amount that will ultimately be charged back to us by our wholesale customers, there could be a material impact on our financial statements.

Shelf Stock Adjustments

Shelf stock adjustments are credits issued to our customers to reflect decreases in the selling prices of our product. These credits are customary in the industry and are intended to reduce the customers' inventory cost to better reflect current market prices. The determination to grant a shelf stock adjustment to a customer following a price decrease is at our discretion.

Factors considered when recording a reserve for shelf stock adjustments include estimated launch dates of competing products based on market intelligence, estimated decline in market price of our product based on historical experience and input from customers and levels of inventory held by customers at the date of the adjustments as provided by them.

Product returns and other allowances

In the pharmaceutical industry, customers are normally granted the right to return product for credit if the product has not been used prior to its expiration date. Our return policy typically allows product returns for products within a twelve month window from six months prior to the expiration date and up to six months after the expiration date. We estimate the level of sale, what will ultimately be returned pursuant to our return policy, and record a related reserve at the time of sale. These amounts are deducted from our gross sales to determine our net revenues. Our estimates take into consideration historical returns of our products and our future expectations. We periodically review the reserves established for returns and adjust them based on actual experience, if necessary. The primary factors we consider in estimating our potential product returns include shelf life of expiration date of each product and historical levels of expired product returns. In case we become aware of any returns due to product related issues, such information from the customers is used to estimate an additional reserve. The amount of actual product return could be either higher or lower than the amounts we accrued. Changes in our estimates, if any, would be recorded in the income statement in the period the change is determined. If we over or under estimate the quantity of product which will ultimately be returned, there may be a material impact on our financial statements.

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Discounts (trade and prompt payment discounts) are accrued at the end of every reporting period based on the gross sales made to the customers during the period and based on their terms of trade. We review the contracts between the customer and us as well as the historical data and percentages to estimate the discount accrual.

Customer rebates are estimated at every period end, based on direct or indirect purchases. If the purchases are direct, the rebates are recognized when products are purchased and a periodic credit is given. For indirect purchases, the rebates are recognized based on the terms with such customer. Medicaid rebates are estimated based on the historical data we receive from the public sector benefit providers, which is based on the final dispensing of our product by a pharmacy to a benefit plan participant.

Doubtful Accounts

Doubtful accounts are estimated based on the data available from external sources, including information on financial condition of customers. Also, a regular review of past due receivables is done on a quarterly basis to identify and make provision for such receivables not expected to be collected.

Gross Sales and Related Allowances

Our gross sales for the third quarter and first nine months of Fiscal 2011 were $87.9 million and $464.6 million, respectively, as compared to $94.4 million and $308.2 million, respectively, for the corresponding periods of Fiscal 2010. Sales allowances, which include chargebacks, returns, discounts, other customary customer deductions and other sales costs, constituted approximately 54% and 42% of gross sales, respectively, for the third quarter and first nine months of Fiscal 2011 as compared to 45% and 42% of gross sales, respectively, for the corresponding periods of Fiscal 2010. Net sales for the third quarter and first nine months of Fiscal 2011 were $40.4 million and $268.2 million, respectively, as compared to $52.0 million and $178.4 million, respectively, for the corresponding periods of Fiscal 2010.

The following is a roll forward of the provisions for chargebacks, shelf stock adjustments, returns and allowances and estimated doubtful account allowances during Fiscal 2010 and the first nine months of Fiscal 2011 :

($ in Thousands)

	Balances at beginning of period	Allowances created		Credits taken by customers	Balance at the end of period
		Current Period	Prior Period		
For Fiscal 2010					
Chargebacks, rebates & shelf stock adjustments	$ 50,028	$ 203,145	-0-	$ 188,365	$ 64,808
Returns and other allowances	6,555	16,016	-0-	15,104	7,467
Doubtful Accounts	78	53	-0-	-0-	131
For the first nine months of Fiscal 2011					
Chargebacks, rebates & shelf stock adjustments	$ 64,808	$ 183,512	$ 12,584	$ 208,846	$ 52,058
Returns and other allowances	7,467	12,863	-0-	14,687	5,643
Doubtful Accounts	131	-0-	-0-	-0-	131

Research and Development Costs

Series B convertible preferred stock was issued to Sun Pharma and its affiliates under a products agreement between the Corporation and Sun Global dated November 21, 2002, in exchange for the technology of formulation products delivered by Sun Global to the Corporation. Such Products Agreement has been completed with the last technology transfer occurring during the third quarter of Fiscal 2008. Accordingly, no further non-cash research and development expense will be incurred thereunder. The amount of non-cash research and development expense which was incurred for past technology transfers under the Products Agreement was charged to operations and was determined based on the fair value of the preferred shares on the date the respective product formula passed its bio-equivalency studies. The fair value of such shares was based upon a valuation performed by Donnelly Penman & Partners, an independent, third party valuation firm. The exchange of shares was prior to the initial ANDA submission to the FDA.

We were responsible for submission of the ANDAs for these transferred formulations for FDA approval. In our experience, generally the submission of the ANDA to the FDA was approximately thirty days after the receipt of notice that the proposed drug product formula passes its bio-equivalency study and accelerated stability studies. An ANDA contains data related to a generic drug product which is submitted to the FDA for review and approval. The FDA must first determine the completeness of the filing and may deny the filing if it is incomplete. There are various reviews that are completed, including bio-equivalency, chemistry, manufacturing, and labeling. The bio-equivalency of a generic drug product is established by measuring the rate and level of active ingredient(s) in the bloodstream of healthy human subjects over a period of time. These pharmacokinetic parameters and results are compared with the innovator's drug product. The bio-equivalency results of the proposed generic drug product must meet pharmacokinetic standards set forth by the FDA. Accordingly, the generic version of a drug product must generally deliver the same amount of active ingredients into the bloodstream within the same timeframe as that of the innovator drug product. Following an indication that the generic drug product has passed its bio-equivalency study, the generic drug product will undergo reviews for chemistry, manufacturing and labeling. In each case, the FDA has an opportunity to raise questions or comments, or issue a deficiency letter. In the event that one or more deficiency letters are issued by the FDA, the submission of the ANDA may be halted or delayed as necessary to accommodate the correction of any such deficiencies and the completion of any additional reviews required. Minor deficiencies traditionally could delay the approval anywhere from 10 days to 90 days or more. Major deficiencies could stop the evaluation process. A restart of the FDA review process after a major deficiency could take up to as many as 180 days or more. Generally, any deficiencies we have experienced have been minor though at times approvals have faced considerable delays. Based on these delays, the economic benefit may not be realized at its highest potential as the delay could cause our approval to be behind our competition's approval of the same generic product.

Based on the definition and characteristics of an asset, set forth in paragraphs 25 and 26 of Statement of Financial Accounting Concepts No. 6 – Elements of Financial Statements issued by the FASB, the Company did not capitalize the technology formulas transferred, as the probability of the future economic benefit to be derived from such formulations was uncertain at the time of technology transfer.

In addition, we have reported the technology transfers as research and development expenses pursuant to ASC Topic 730, "Research and Development." In connection therewith, the research and development technology transferred by Sun Global under the products agreement was always specific research and development technology for a specific product formula. There were no alternative future uses (in other research and development projects or otherwise) for such products. For example, Caraco has never acquired technology from Sun Global with the purpose of selling such technology and, in fact, has never sold or held for sale any of the technology transferred by Sun Global to a third party. Caraco has always developed the research and development technology into manufactured product for its own business purposes.

Research and development costs settled in cash are charged to expense as incurred.

Short-Term Investments

During the first quarter of Fiscal 2010 the Company invested $10,000,000 in a bank certificate of deposit. In accordance with the term of deposit, in June 2010, the Certificate was renewed for twelve months and earns interest at a rate of 2.7% APY. If such deposit is withdrawn prior to maturity, the Company will earn interest at the applicable LIBOR rate as on the date of such withdrawal.

Intangible Assets

During Fiscal 2009 the Company made cash payments in the amount of $1,456,000 for the purchase of certain assets which included brand products, associated New Drug Applications (“NDAs”) and trademarks and establishment fees for these products. These assets are recorded as intangible assets in the Company’s balance sheet at December 31, 2010. These intangible assets are being amortized equally over a period of 15 years, the period during which the Company expects to receive economic benefits from these intangible assets. The Company recorded $73,000 in amortization expense in each of the first nine-month periods of Fiscal 2011 and Fiscal 2010. The total accumulated amortization related to these intangible assets is $243,000 as of December 31, 2010.

Income Taxes

As part of the process of preparing our financial statements, we are required to estimate our income taxes in each of the jurisdictions in which we operate. We account for income taxes by the liability method. Under this method, deferred income taxes are recognized for tax consequences in future years of differences between the tax bases of assets and liabilities and their financial reporting amounts at each year-end, based on enacted laws and statutory tax rates applicable for the differences that are expected to affect taxable income. In assessing the ability to realize deferred tax assets, the Company considers whether it is more likely than not that some portion or all of the deferred tax assets will not be realized. The ultimate realization of deferred tax assets is dependent upon the generation of future taxable income during the periods in which those temporary differences become deductible. Management considers the scheduled reversal of deferred tax liabilities, projected future taxable income, and tax planning strategies in making this assessment. We had net deferred tax assets of $21.2 million and $22.1 million at December 31, 2010 and March 31, 2010, respectively. Valuation allowances are provided when based upon the weight of available evidence, it is more likely than not that some or all of the deferred tax assets will not be realized. We have recorded an income tax benefit of $1.8 million and $1.9 million for the third quarter and first nine months of Fiscal 2011, respectively, as compared to income tax benefits of $1.9 million and $3.0 million during the third quarter and first nine months of Fiscal 2010, respectively. The income tax benefit for the first nine months of Fiscal 2010 was predominantly due to losses incurred as a result of FDA actions including the seizure of inventory which was written off and destroyed. We have not provided for any valuation allowance as of December 31, 2010 or March 31, 2010. Based upon the level of projected future taxable income over the periods in which these deferred assets are deductible, the Company expects that it is more likely than not that it will realize the benefit of these temporary differences. As of December 31, 2010, we had federal NOLs of approximately $2.3 million, which are restricted by limitations of Internal Revenue Code Section 382, available to reduce future taxable income. The NOLs will expire between 2011 and 2012.

The Company adopted the provisions of ASC 740 dealing with Accounting for Uncertainty in Income Taxes at the beginning of Fiscal 2008. The Company had determined that no adjustments for unrecognized tax benefits were necessary as a result of this adoption. There are no unrecognized tax benefits present at December 31, 2010.

The Company is subject to U.S. federal income tax as well as income tax in certain state jurisdictions. The IRS has initiated an examination of the Company’s tax return for the fiscal year ended March 31, 2009. The Company believes that it has complied with applicable IRS Codes and regulations, for the period under review. The Company’s federal statute of limitations has expired for years prior to 2006.

Inventory

We value inventories at the lower of cost or market. We determine the cost of raw materials, work in process and finished goods using the specific identification cost method. We analyze our inventory levels quarterly and write down inventory that has become obsolete and inventory that has a cost basis in excess of its expected net realizable value. Expired inventory is disposed of and the related costs are written off. Materials acquired solely for research and development ("R&D") are written off in the year of acquisition. Inventory includes material purchased related to products for which the Company has filed ANDAs with the FDA and the commercial launch of such products will commence once the approvals are received. Total inventories at December 31, 2010 and March 31, 2010 include materials purchased in the amount of $1,110,800 and $2,249,878, respectively, related to products for which the Company has filed ANDAs that are awaiting approval from the FDA, and the commercial launch of such products will commence once the approvals are received. We do not expect to receive any approvals for products out of our facilities until we resolve the FDA's concerns as discussed above. The determination of whether or not inventory costs will be realizable requires estimates by management. A critical estimate in this determination is the estimate of the future expected inventory requirements, whereby we compare our internal sales forecasts to inventory on hand. Actual results may differ from those estimates and inventory write-offs may be required. We must also make estimates about the amount of manufacturing overhead to allocate to our finished goods and work in process inventories. Although the manufacturing process is generally similar for our products, we must make judgments as to the portion of costs to allocate to purchased product, work in process and finished goods, and such allocations can vary based upon the composition of these components and the fact that each product produced does not necessarily require the same amount of time or effort for the same production step. Accordingly, the assumptions we make can impact the value of reported inventories and cost of sales.

As disclosed above, certain drug products manufactured, work in process, and ingredients held, at the Company's facilities were seized at the direction of the FDA. The estimated cost of such seized inventory was $24.0 million. As stipulated in the Consent Decree, the Company attempted to have the seized inventory released. The Company believed that, except for the raw materials which were opened solely for the purpose of sampling, the estimated value of which was $8.1 million, all other seized inventory would be difficult to recondition. Accordingly, the Company had written off all other seized inventory in the amount of $15.9 million during Fiscal 2010. In accordance with the Consent Decree, on June 25, 2010, the FDA released the raw materials which were opened solely for the purpose of sampling. Subsequently, in September 2010, the FDA released all other seized materials, which were thereafter disposed of by the Company, in accordance with the Consent Decree.

OVERVIEW

The Company has been actively working with cGMP consultants towards the resumption of manufacturing activities at its facilities. These consultants were appointed by the Company in accordance with the previously disclosed Consent Decree, which the Company entered into with the FDA on September 29, 2009. The Company's remediation efforts towards the resumption of manufacturing and distribution from its facilities are still ongoing, but the Company is unable to predict when such manufacturing and distribution will resume. The Company had previously disclosed its belief that two products would commence manufacture at its Michigan facilities prior to the end of Fiscal 2011. In evaluating and discussing with the cGMP experts the remediation steps completed to date and those yet to be completed, the Company has determined that it will not be able to begin the manufacture and distribution of products by the end of Fiscal Year 2011. As previously disclosed, and is always the case in matters such as these, there is no assurance that the remediation efforts will be successful or result in resolution of the FDA compliance issues.

The FDA approved the Company's work plan on March 17, 2010, and the Company is in the process of implementing the corrective actions and remedial measures as stipulated in the work plan. On June 24, 2010, the FDA notified Caraco that its protocol for third party cGMP certification and batch certification, detailing the activities to be conducted by the cGMP consultants, was acceptable.

On June 25, 2010, the FDA released certain previously seized raw materials which had been opened solely for the purpose of sampling. In September 2010, the FDA released other seized materials, which were disposed of in September 2010, in accordance with the Consent Decree. As a result, the Company is now released from the Bond obligation under the Consent Decree. Accordingly, the Letter of Credit, in the amount of $15 million, which was issued in favor of FDA against this Bond, expired on October 9, 2010, and has not been renewed.

As a result of the previously disclosed FDA actions, there has been a material adverse effect on our current operations and there may be a material adverse effect on our future operations. Under the terms of the Consent Decree, before resuming the manufacture of any product in the Company's facilities, a number of significant steps and processes are required to be completed, and certifications and approvals from both outside experts and the FDA are to be obtained.

All of the Company's prior approved products, together with the new products pending approval from the FDA, will be subject to these same processes, certification and approvals as set forth in the Consent Decree. The Company believes that, even assuming a successful remediation process, it will take significant time before the Company reaches its previous levels of manufacturing in its facilities. We are not able at this time to estimate the cost of these actions, which will be substantial, and once the manufacturing resumes, will include the costs of operating our manufacturing facility at volumes well below the facility's capacity. The Consent Decree also requires the Company to abide by certain conditions and restrictions. If the Company violates any portion of Consent Decree, it could incur monetary fines and other penalties.

The Company intends to augment the loss of sales of manufactured products by the sale of Caraco-owned products manufactured at third party sites and through sales of distributed products, which are not impacted by the aforementioned actions of the FDA. However, any disruption in the supplies of the products manufactured by these third party sites due to cGMP issues, changes in the market conditions or any other issues would significantly affect the revenues from such products.

In addition to certain Caraco-owned products manufactured by Sun Pharma and its affiliates, we have transferred certain Caraco-owned products to alternate manufacturing sites of Sun Pharma and its affiliates that would allow the Company to realize revenues from those products. We have filed with the FDA supplements to ANDAs, for its approval, for these transferred products. There is no assurance that such approvals will be granted.

As previously disclosed, on December 3 2010 the Company received Proposal from Sun Pharma and Sun Global for a going private transaction by which Sun Pharma and Sun Global, and/or one or more of their affiliates, would acquire all of the outstanding shares of the Company's common stock not held by Sun Pharma or Sun Global for $4.75 in cash per share. Subsequently, the Company's Board of Directors authorized the Independent Committee of the Board to: (1) consider the Proposal including, but not limited to, reviewing (a) whether going private is appropriate for Caraco at this time is advisable or is inadvisable and should be rejected, (b) possible alternatives to the Proposal or opportunities which may be more advantageous to Caraco, and (c) the merits of the Proposal; (2) if deemed advisable, enter into discussions and negotiations with respect to the terms of the Proposal, including the proposed per share purchase price, with Sun Pharma and their advisors; and (3) make recommendations to the Board of Directors and as applicable, to the stockholders as to the Independent Committee's findings. The Independent Committee has also retained William Blair & Company as an independent financial advisor, and Carrington Coleman law firm as independent legal counsel, to assist it in evaluating the Proposal.

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As previously disclosed, the Company's two distribution agreements with Sun Pharma have been extended until January 28, 2012, but will each terminate following these extensions. The Company and its Independent Committee of the Board approached Sun Pharma and attempted to negotiate long term renewals for each agreement; however, Sun Pharma exercised its right to end the agreements, following these extensions, on January 28, 2012. During the first six months of calendar 2011, the Company and Sun Pharma will discuss a transition plan to transition the marketing of the products covered by the respective agreements to Sun Pharma and/or its wholly-owned affiliates. Thereafter, if the parties have reached an understanding with respect to the transition plan, the parties will implement the transition plan so that upon the termination of the agreements, Sun Pharma and its affiliates will commence marketing of the products. If the parties have not agreed on a transition plan prior to January 28, 2012, the agreements will still terminate on that date.

During the third quarter ended December 31, 2010 and first nine months of our current fiscal year ("Fiscal 2011") ended December 31, 2010, we generated net sales of $40.4 million and $268.2 million, respectively, as compared to $52.0 million and $178.4 million, respectively, for the corresponding periods of our previous fiscal year ("Fiscal 2010") ended December 31, 2009. During the third quarter and first nine months of Fiscal 2011, sales of Caraco-owned products were $5.7 million and $16.7 million, respectively, as compared to $3.3 million and $18.9 million, respectively, during the corresponding periods of Fiscal 2010. The sales of distributed products during the third quarter and first nine months of Fiscal 2011 were $34.7 million and $251.5 million, respectively, as compared to $48.7 million and $159.5 million, respectively, during the corresponding periods of Fiscal 2010. We earned a gross profit of $3.3 million and $22.4 million during the third quarter and first nine months of Fiscal 2011, respectively, as compared to earning a gross profit of $3.1 million and incurring a gross loss of $4.7 million, respectively, during the corresponding periods of Fiscal 2010. We incurred pre-tax losses of $4.8 million and $5.2 million, respectively, during the third quarter and first nine months of Fiscal 2011, as compared to incurring pre-tax losses of $4.9 and $8.8 million during the respective periods of Fiscal 2010. The Company recorded an income tax benefit of $1.8 million and $1.9 million, respectively, for the third quarter and first nine months of Fiscal 2011, as compared to recording income tax benefits of $1.9 million and $3.0 million during the corresponding periods of Fiscal 2010. We incurred net losses of $3.0 million and $3.3 million, respectively, during the third quarter and first nine months of Fiscal 2011, as compared to incurring net losses of $3.0 million and $5.8 million, respectively, during the corresponding periods of Fiscal 2010. We generated cash from operations in the amount of $2.5 million during the first nine months of Fiscal 2011, as compared to generating cash from operations in the amount of $15.5 million during the corresponding period of Fiscal 2010. At December 31, 2010, we had stockholders' equity of $152.2 million, as compared to stockholders' equity of $155.4 million at March 31, 2010. (See "Third Quarter and First Nine Months Fiscal 2011 Compared to Third Quarter and First Nine Months Fiscal 2010" below for further information).

We filed two ANDAs relating to two products with the FDA during the first nine months of Fiscal 2011. These products have been developed in partnership with other product development and manufacturing companies, one of which is an affiliate. We have not received FDA approval for any ANDAs since the first quarter of Fiscal 2009 and do not expect to receive any approvals for products out of our facilities until we resolve the FDA's concerns as discussed above. The total number of ANDAs pending approval by the FDA as of December 31, 2010 was 33 (including four tentative approvals) relating to 29 products. Out of the 33 ANDAs pending approval, 31 (including four tentative approvals) are out of our Michigan facilities and the remaining two are from our partners' facilities.

FDA COMPLIANCE

As previously disclosed the Company received a warning letter from the Detroit District of the FDA in October 2008, for its manufacturing facility in Detroit, Michigan, to which the Company responded and the Detroit District acknowledged our response on December 22, 2008. The FDA commenced an inspection as a follow-up to the October 2008 warning letter from March 11, 2009 to May 12, 2009. The FDA investigators provided the Company with a list of their observations on FDA Form 483. The FDA's inspection found unresolved violations of cGMP requirements as previously disclosed in our SEC filing on Form 10-K filed June 15, 2009. The Company provided a written response to these observations on June 19, 2009. As previously disclosed on June 25, 2009, at the request of the FDA, drug products manufactured in our facilities were seized. The seizure also included ingredients held at these same facilities as well as work in process. Products distributed by Caraco that are manufactured outside of these facilities were not impacted. In its complaint relating to its seizure, the FDA stated, among other things, that the May 12, 2009 inspection and the Company's written response thereto revealed continuing significant cGMP violations. The FDA also stated that the drug products are adulterated in that the methods used in, and the facilities and controls used for, their manufacture, processing, packing, and/or holding do not conform to and are not operated and administered in conformity with cGMP requirements. As a result of the FDA action, we voluntarily ceased manufacturing operations and instituted an indefinite reduction in our workforce of approximately 430 employees in two phases. The Company has subsequently started recalling some of these employees in conjunction with its efforts to restart its manufacturing activities. This FDA action has resulted and will continue to result in a material adverse effect on our current and near term operations.

On September 29, 2009, Caraco voluntarily entered into a Consent Decree with the FDA regarding the Company's drug manufacturing operations. The Consent Decree provides a series of measures that, when satisfied, will permit Caraco to resume manufacturing and distributing those products that are manufactured in its facilities. The Company is working expeditiously to satisfy the requirements of the Consent Decree and has retained independent cGMP consultants for review of the Company's operations and to facilitate a successful result. The Company in accordance with the Consent Decree has submitted a work plan to the FDA in October 2009 for remedial actions leading to resumption of its manufacturing operations. The FDA approved the Company's work plan on March 17, 2010 after reviewing and suggesting certain modifications. The Company is in the process of implementing the corrective actions and remedial measures as stipulated in the work plan. We intend to continue to work with the FDA to resolve its concerns as effectively and expeditiously as possible. Remediation activities are ongoing with the full knowledge of the cGMP consultants. A protocol for third party certification was submitted to the FDA on May 5, 2010. This protocol details the activities to be conducted by the cGMP consultants. On June 24, 2010, the FDA notified Caraco that the protocol was acceptable.

Under terms of the Consent Decree, Caraco's cessation of manufacturing operations will continue until it receives written notification from independent experts and the FDA that it is in compliance with the Consent Decree and regulations and can resume operations. Caraco-owned products that are manufactured outside of these facilities are not impacted and distribution and marketing of these products continues.

Under the terms of the Consent Decree, before resuming the manufacture of any product in the Company's facilities, a number of significant steps and processes are required to be completed, and certifications and approvals from both outside experts and the FDA are to be obtained.

In evaluating and discussing with the cGMP experts the remediation steps completed to date and those yet to be completed, the Company has determined that it will not be able to begin the manufacture and distribution of products by the end of Fiscal Year 2011. The Company's remediation efforts towards the resumption of manufacturing and distribution from its facilities are still ongoing, but the Company is unable to predict when such manufacturing and distribution will resume. As previously disclosed, and as always is the case in matters such as these, there is no assurance that the remediation efforts will be successful or result in resolution of the FDA compliance issues.

All of the Company's prior approved products, together with the new products pending approval from the FDA, will be subject to these same processes, certification and approvals as set forth in the Consent Decree. The Company believes that, even assuming a successful remediation process, it will take significant time before the Company reaches its previous levels of manufacturing in its facilities.

We have not received FDA approvals for any of our ANDAs since the first quarter of Fiscal 2009. It is unlikely that we will receive any approvals for product out of our facilities until the FDA reviews our remediation response and makes a determination of our status. Further, as stated above, the Company will also require approvals from the FDA for its previously approved ANDAs, as set forth in the Consent Decree.

In accordance with the Consent Decree, we have also provided third party certification to the FDA and requested the release of raw materials which were opened solely for the purpose of sampling. On June 18, 2010, the FDA accepted the raw material certification and had instructed that these materials be released "with the understanding that a defined portion will be destroyed and the remainder will be available for use." Except for the portion which was to be destroyed, approximating $0.3 million, the remainders of these materials, approximating $7.8 million, were released on June 25, 2010. Subsequently in September 2010, all other seized materials (drug products manufactured in our facilities, ingredients including the portion of raw materials amounting to $0.3 million, as mentioned above, and work in process) were released by the FDA and all such materials were disposed of by September 24, 2010 under the supervision of the FDA, in accordance with the Consent Decree.

Third Quarter and First Nine Months Fiscal 2011 Compared to Third Quarter and First Nine Months Fiscal 2010

Net Sales. Net sales for the third quarter and first nine months of Fiscal 2011, ended December 31, 2010, were $40.4 million and $268.2 million, respectively, as compared to $52.0 million and $178.4 million, respectively, for the comparable periods of Fiscal 2010, reflecting decrease of 22% and increase of 50%, respectively. Net sales decreased during the third quarter of Fiscal 2011 as compared to the corresponding period of Fiscal 2010 due to decreased sales of distributed products. Net sales increased during the first nine months of Fiscal 2011, in comparison to the corresponding period of Fiscal 2010, primarily as a result of higher sales of distributed products. Net sales for distributed products were $34.7 million and $251.5 million, respectively, for the third quarter and first nine months of Fiscal 2011, as compared to $48.7 million and $159.5 million, respectively, for the corresponding periods of Fiscal 2010. The sales of distributed products were lower in the third quarter of Fiscal 2011, as compared to the corresponding period of Fiscal 2010, as we stopped shipping certain Paragraph IV products prior to the quarter (see "Note 12. Litigation" for disclosure of litigation involving Paragraph IV products). Sales from such products were included in the third quarter of Fiscal 2010. Net sales of distributed products increased during the first nine months of Fiscal 2011, as compared to corresponding period of last year, primarily due to increased sales of Paragraph IV products, particularly sales of certain Paragraph IV products which were launched by the Company during the fourth quarter of Fiscal 2010 under the Distribution and Sale agreement with Sun Pharma. As previously discussed the sales of such products at these levels were not expected to continue and have not occurred during the third quarter of Fiscal

2011 and are not expected to occur in future periods. Net sales for Caraco-owned products were $5.7 million and $16.7 million, respectively, for the third quarter and first nine months of Fiscal 2011, as compared to $3.3 million and $18.9 million, respectively, for the corresponding periods of Fiscal 2010. The increase in the sales of Caraco-owned products during the third quarter was primarily due to an increase in the number of products being contract manufactured, including certain Caraco-owned products which were acquired as part of the asset purchase agreement with Forest Laboratories, Inc. (“Forest”), as previously disclosed. Sales of Caraco-owned products during first nine months of Fiscal 2011 were lower than those during corresponding period of Fiscal 2010 as we have stopped marketing, effective June 25, 2009, all the products which were being manufactured out of our facilities on account of the FDA actions, as previously discussed, offset in part by higher sales of certain Caraco-owned products which are being contract manufactured, including those which were acquired as part of an asset purchase agreement with Forest which the Company started selling during Fiscal 2010. We were manufacturing and marketing all except two of our approved products, as of June 25, 2009. However, as a result of action taken by the FDA, we have ceased manufacturing operations of the products which we manufacture at our facilities located in the state of Michigan. We continue to generate sales of Caraco-owned products that are manufactured outside of the Company by other manufacturers including Sun Pharma.

Gross Profit. We earned gross profit of $3.3 million and $22.4 million, respectively, in the third quarter and first nine months of Fiscal 2011, as compared to earning a gross profit of $3.1 million and incurring a gross loss of $4.7 million, respectively, during the third quarter and first nine months of Fiscal 2010. The gross profit in the third quarter of Fiscal 2011 is primarily due to mix of products sold. As disclosed above, the sales of Paragraph IV products, which earn a lower gross margin than the Company's other products, were lower in the third quarter of the current fiscal year, as compared to the corresponding period of last fiscal year. The gross profit in the first nine months of Fiscal 2011, as compared to the same period last year, is higher due to the increased level of sales. Also, the gross loss in the first nine months of Fiscal 2010 was, in large part, due to a reserve in the amount of $15.9 million, which we had provided on the inventory seized by the FDA. As disclosed above, due to the actions of the FDA, all shipments of products which were being manufactured at the Company's facilities have ceased effective June 25, 2009, which has led to diminished sales of Caraco-owned products.

The gross profit margin for both the third quarter and first nine months of Fiscal 2011, as a percentage of net sales, was 8%, as compared to 6% and (3%), respectively, during the corresponding periods of Fiscal 2010. As disclosed above, we had created a reserve in the amount of $15.9 million during the first nine months of Fiscal 2010 for the inventory seized by the FDA. Excluding the impact of the inventory reserve, the gross profit margins in the first nine months of Fiscal 2010 was 6%.

The gross profit margin on distributed products was 11% and 9%, respectively, for the third quarter and first nine months of Fiscal 2011, as compared to 9% in both comparable periods of Fiscal 2010. The gross profit margin for Caraco-owned products was (10%) and (7%), respectively, for the third quarter and first nine months of Fiscal 2011, as compared to (33%) and (99%), respectively, for the corresponding periods of Fiscal 2010. Excluding the impact of the inventory reserve, the gross profit margin for Caraco-owned products in the first nine months of Fiscal 2010 was (14%). Caraco-owned product margins have increased in the third quarter primarily due to higher sales of Caraco-owned products including those which were acquired as part of the asset purchase agreement with Forest. The gross margins on Caraco-owned products in first nine months of Fiscal 2011 were higher primarily due to a reserve in the amount of $15.9 million created during the first nine months of Fiscal 2010 for the inventory seized by the FDA. During the first nine months of Fiscal 2011, we wrote off certain seized inventories of approximately $0.3 million as per the undertaking given to the FDA for getting the release of raw material drums which were opened solely for the purpose of sampling. Overall gross profit margins on Caraco-owned products are negative due to high absorption of overheads in relation to the lower levels of sales. During the first nine months of Fiscal 2011 and Fiscal 2010 our overheads were $8.7 million and $12.0 million, respectively. As disclosed above, due to the actions of the FDA, all shipments of products which were being manufactured at the Company's facilities have ceased effective June 25, 2009, which has led to diminished sales of Caraco-owned products. However the Company continues to incur costs to maintain such facilities and to facilitate the resumption of manufacturing operations. The sales and related gross profits generated from the Distribution and Sale Agreement dated January 29, 2008 and the marketing agreement dated January 19, 2007 (see Note 6 - Sun Pharmaceutical Industries Limited) are recognized under distributed products which we segregate from sales of Caraco-owned products and are accordingly disclosed in Note 15 of Notes to Financial Statements under Segment Reporting.

Selling, General and Administrative Expenses. Selling, general and administrative ("SG&A") expenses during the third quarter and first nine months of Fiscal 2011 were $6.6 million and $20.4 million, respectively, as compared to $5.4 million and $15.9 million, respectively, during the corresponding periods of Fiscal 2010, representing increases of 22% and 28%, respectively. SG&A expenses were higher during the third quarter of Fiscal 2011 as compared to the corresponding period of Fiscal 2010 predominantly due to certain customer related adjustments recorded during the period. SG&A expenses were higher during the first nine months of Fiscal 2011 due to customer related adjustments and the recording of additional expenses primarily related to professional consultation fees pertaining to FDA issues and royalties related to certain Caraco-owned products which were acquired as part of the asset purchase agreement with Forest SG&A expenses, as a percentage of net sales were 20% and 8%, respectively, for the third quarter and first nine months of Fiscal 2011, as compared to 10% and 9%, respectively, for the corresponding periods of Fiscal 2010. SG&A expenses, as a percentage of sales, were high during the third quarter of Fiscal 2011 primarily due to lower net sales during the period.

Research and Development Expenses. Total R&D expenses incurred for the third quarter and first nine months of Fiscal 2011 were $1.7 million and $7.8 million, respectively, as compared to $2.8 million and $8.3 million, respectively, during the corresponding periods of Fiscal 2010. The R&D expenses during the first nine months of Fiscal 2010 were reduced by the reimbursement of a certain amount relating to certain product litigation costs as part of a settlement agreement, as previously disclosed. R&D expenses continues to be further decreased since the Company ceased manufacturing operations, as the Company has focused primarily on FDA remediation.

Net Other Income (Expense). We earned net other income of $0.2 million and $0.6 million during the third quarter and first nine months of Fiscal 2011, respectively, as compared to net other income of $0.1 million during both corresponding periods of Fiscal 2010.

Income Taxes. We recorded income tax benefits of $1.8 million and $1.9 million, respectively, during the third quarter and first nine months of Fiscal 2011, as compared to recording income tax benefits of $1.9 million and $3.0 million during the corresponding periods of Fiscal 2010.

Results of Operations. We incurred pre-tax losses of $4.8 million and $5.2 million, respectively, during the third quarter and first nine months of Fiscal 2011, as compared to pre-tax losses of $4.9 million and $8.8 million during the corresponding periods of Fiscal 2010. We incurred net losses of $3.0 million and $3.3 million, respectively, for the third quarter and first nine months of Fiscal 2011, as compared to incurring net losses of $3.0 million and $5.8 million, respectively, during the corresponding periods of Fiscal 2010.

Liquidity and Capital Resources We generated cash from operations in the amount of $2.5 million during the first nine months of Fiscal 2011, as compared to generating cash from operations in the amount of $15.5 million during the corresponding period of Fiscal 2010. The cash flow from operations was lower in the first nine months of Fiscal 2011, primarily due to the decrease in accounts payable balances, offset by decreases in accounts receivable and inventory balances, and lower net loss. Accounts receivable decreased by $97.5 million during the first nine months of Fiscal 2011, and as of December 31, 2010 balances payable to customers net, was $2.8 million, as compared to accounts receivable net, of $94.7 million at the end of Fiscal 2010. Accounts receivable is equivalent to (6) days sales outstanding ("DSO") as of December 31, 2010 versus 154 days as of March 31, 2010. The negative level of DSO at December 31, 2010 is temporary and is mainly due to the reserves which have been created for likely credits to be received from our customers for price adjustments and increased chargebacks for certain products which were earlier sold, and also due to timing of payments made by the wholesale customers. The wholesale customers make payment for invoices on gross sales, however, a deduction for chargebacks will be made by these wholesale customers as they continue to sell to retail chain stores and managed care organizations with whom we have contractual pricing. The Company believes that it has provided adequate reserves for chargeback deductions which are likely to be taken by the wholesale customers in subsequent periods. The lower level in DSO is also due to lower levels of sales in the current period and collection of receivable balances from certain customers with whom we have entered into agreements which included special payment terms. The collections of the related accounts receivable balances from these previous period sales were spread over an extended period which ended in the third quarter of Fiscal 2011. Based on the third quarter cost of sales, which is most representative of current sales activity, inventory levels at December 31, 2010 were equivalent to 129 days on hand, and similarly, based on the fourth quarter of Fiscal 2010 cost of sales, inventory levels at March 31, 2010 were equivalent to 182 days on hand. The decrease in inventory levels is primarily due to higher levels of sales in the first nine months of Fiscal 2011 of certain distributed products for which the Company was carrying the inventory in previous periods and currently does not carry any inventory for such products. The inventory, as of March 31, 2010, included high levels of inventory of Paragraph IV products to support the anticipated sales which occurred in the current fiscal year. Also during the third quarter of Fiscal 2011 the Company wrote-off certain inventory of such Paragraph IV products amounting to $29.5 million, and recovered the cost from Sun Pharma in accordance with the terms of Distribution and Sale Agreement.

During the first quarter of Fiscal 2010 the Company had invested $10.0 million in a bank certificate of deposit which was renewed in June 2010 for twelve months in accordance with the terms of the deposit, and earns interest at a rate of 2.7% APY. If such deposit is withdrawn prior to maturity, the Company will earn interest at the applicable LIBOR rate as on the date of such withdrawal.

As disclosed above the FDA actions and the Company's voluntary cessation of production at its facilities had a material adverse affect on our current operations and there may be a material adverse affect on our future operations. The Company initiated a reduction in various expenses in an effort to bring its expenses in line with its current levels of sales and other activities. The sales of distributed products and certain Caraco-owned products made by other manufacturers are expected to continue and contribute to the cash flows. Also, the Company has entered into an agreement with Forest which, to date, has provided three additional products to the Company's product portfolio, and such products have begun generating incremental revenues under Caraco-owned product sales. We expect additional products will be added to our portfolio as a result of this agreement. The Company owns seven products that are manufactured outside of the Company by other manufacturers including Sun Pharma and its affiliates. The Company has filed supplements to ANDAs, for FDA approval, for the transfer of certain Caraco-owned products to Sun Pharma

and its affiliates that would allow the Company to realize revenues from these products. There is no assurance that such approvals will be granted. As of December 31, 2010, we have $54 million in cash and another $10 million in short-term investments, including the proceeds from a loan in the amount of $12.6 million, currently classified as a short term liability. The Company believes that its cash flow from operations and cash balances will continue to support its ongoing business requirements. However, because of, among other things, decreased customer confidence resulting in lower sales, as well as the uncertainty of resumption in manufacturing activities, future costs of FDA compliance and associated costs, various litigation proceedings (see “Note 12. Litigation”) and the expiration of the marketing agreement and Distribution and Sale agreement, on January 28, 2012, both signed with Sun Pharma, there can be no assurance of this belief.

At December 31, 2010, we had working capital of $89.1 million, compared to working capital of $89.3 million at March 31, 2010.

During Fiscal 2009 the Company entered into a term loan of $18 million with Charter One Bank. The loan is secured by a mortgage covering the Company's manufacturing facility and equipment located in Detroit, Michigan. The rate of interest is calculated as LIBOR plus an applicable margin thereto (based upon various leverage levels and current applicable rate is 50 basis points). The aggregate rate applicable to the Company as of December 31, 2010 was 0.8% (effective rate was 2.91% taking into consideration the Interest Rate SWAP Agreement entered into by the Company details of which are given hereunder). The principal loan payments and accrued interest are payable on a quarterly basis beginning July 2009. The principal is to be repaid in equal quarterly installments of $900,000 for ten quarters through October 2011, and thereafter, if not renewed, the remaining balance of $9 million is due in the subsequent quarter by January 2012. Subsequently, in October 2009 the terms of the loan were modified and we entered into an amended agreement. The amendment adds to the loan a one year line of credit note for $15 million against which the Company can borrow funds for working capital purposes or can get letters of credit issued. Against this line of credit, the Bank issued an Irrevocable Standby Letter of Credit in an amount of $15 million, in favor of the United States of America, as required to be placed with the FDA in accordance with the Consent Decree, as disclosed above. On October 9, 2010 this Letter of Credit expired and was not renewed, as the Company was released from this obligation under the terms of the Consent Decree. The line of credit carries an interest rate of LIBOR plus 150 basis points, and if letters of credit are issued, the associated fees are 0.7% of such letters of credit on annualized basis. Also, there is an unused fee of 0.25% on an annualized basis to the extent the line remains idle. The outstanding term loan is cross collateralized by all of the Company's fixed assets and cash deposit accounts held with Charter One Bank, equivalent to the amount of outstanding loans. These cash deposits earn interest at prevailing rates applicable to such money market accounts. The Company is continuing discussions with Charter One Bank to allow the release of the cash collateral. Charter One Bank has temporarily suspended the required compliance with the covenants in the loan agreements relating to FDA enforcement actions, and has suspended certain other compliance requirements until April 9, 2011. On or before such date, the Company anticipates either entering into revised agreements or repaying the loan in full. Currently, as the loan is in technical default due to the FDA enforcement action, the entire outstanding balance has been classified as a short-term liability on its Balance Sheets.

As required pursuant to the terms of the Loan Agreement, the Company has entered into an Interest Rate Swap Agreement with Charter One Bank to hedge the interest rate applicable on the loan. The notional amount for the swap is $12.6 million which will continue to amortize down as principal payments are made on the related debt. The annualized fixed rate of interest as it applies to this agreement is 2.41%. Thus as of December 31, 2010, the effective rate of interest to the Company for the term loan was 2.91% (2.41% swap rate plus applicable margin of 50 basis points). The Company has made provisions to record the fair value of this swap agreement, which was ($0.4) million at December 31, 2010.

Future Outlook

As previously disclosed, on December 3, 2010, the Company received a Proposal from Sun Pharma and Sun Global for a going private transaction by which Sun Pharma and Sun Global, and/or one or more of their affiliates, would acquire all of the outstanding shares of the Company’s common stock not held by Sun Pharma or Sun Global for $4.75 in cash per share. Subsequently, the Company’s Board of Directors authorized the Independent Committee of the Board to: (1) consider the Proposal including, but not limited to, reviewing (a) whether going private is appropriate for Caraco at this time is advisable or is inadvisable and should be rejected, (b) possible alternatives to the Proposal or opportunities which may be more advantageous to Caraco, and (c) the merits of the Proposal; (2) if deemed advisable, enter into discussions and negotiations with respect to the terms of the Proposal, including the proposed per share purchase price, with Sun Pharma and their advisors; and (3) make recommendations to the Board of Directors and as applicable, to the stockholders as to the Independent Committee's findings. The Independent Committee has also retained William Blair & Company as an independent financial advisor, and the Carrington Coleman law firm as independent legal counsel, to assist it in evaluating the Proposal.

We voluntarily entered into a Consent Decree with the FDA regarding the Company's drug manufacturing operations. The Consent Decree provides a series of measures that, when satisfied, will permit Caraco to resume manufacturing and distributing those products that are manufactured in its facilities. We continue to focus on improving support to, and emphasis on, quality assurance, quality control, and manufacturing areas in order to continually improve the performance of our quality system. We have hired external cGMP consultants who have experience in assisting manufacturers with FDA compliance issues. These consultants have reviewed all of our systems, procedures, reporting structures, and processes, as well as reviewed training on risk management and overall cGMP. As part of this comprehensive process we have evaluated our internal and external cGMP audit programs, and will make any improvements that we believe to be necessary to improve these programs. Caraco continues to obtain assistance and guidance wherever required from the quality group of Sun Pharma to improve its quality systems. Though near term sales of Caraco-owned products face challenges, we are in the process of remediation and intend to effect the changes required to improve our performance on sales of these products, on a long-term basis. The Company’s remediation efforts towards the resumption of manufacturing and distribution from its facilities are still ongoing, but the Company is unable to predict when such manufacturing and distribution will resume. As previously disclosed, and as always is the case in matters such as these, there is no assurance that the remediation efforts will be successful or result in resolution of the FDA compliance issues.

The Company submitted a work plan to the FDA in October 2009 for remedial actions leading to resumption of its manufacturing operations. The FDA approved the Company’s work plan on March 17, 2010 after reviewing and suggesting certain modifications. The Company is in the process of implementing the corrective actions and remedial measures as stipulated in the work plan. On June 24, 2010, the FDA notified Caraco that its protocol for third party cGMP certification, detailing the activities to be conducted by the cGMP consultants, was acceptable. We intend to continue to work with the FDA to resolve its concerns as effectively and expeditiously as possible.

Under the terms of the Consent Decree, before resuming the manufacture of any product in the Company's manufacturing facilities, a number of significant steps and processes are required to be completed, and certifications and approvals from both outside experts and the FDA are to be obtained. All of the Company's prior approved products, together with the new products pending approval from the FDA, will be subject to these same processes, certification and approvals as set forth in the Consent Decree.

In evaluating and discussing with the cGMP experts the remediation steps completed to date and those yet to be completed, the Company has determined that it will not be able to begin the manufacture and distribution of products by the end of Fiscal Year 2011. The Company believes that, even assuming a successful remediation process, it will take significant time before the Company reaches its previous levels of manufacturing in its facilities. We are not able at this time to estimate the cost of these actions, which will be substantial, and once the manufacturing resumes, will include the costs of operating our manufacturing facility at volumes well below the facility's capacity. The Consent Decree also requires the Company to abide by certain conditions and restrictions. If the Company violates any portion of the Consent Decree, it could incur monetary fines and other penalties.

The Company intends to augment the loss of sales of manufactured products by the sale of Caraco-owned products manufactured at third party sites and through sales of distributed products. Caraco-owned products that are manufactured outside of these facilities are not impacted by the aforementioned actions of the FDA. However, any disruption in supplies of the products manufactured at these third party sites due to cGMP issues, changes in market conditions or any other issues would significantly impact the revenues from such products.

Our current focus remains on resumption of manufacturing and quality assurance. Currently we are utilizing part of our R&D team to help with technical validations and compliance initiatives and will continue to do so in the near term. As a result, our R&D expense has declined in periods subsequent to the cessation of manufacturing due to the actions of the FDA. Development of products at third party sites, currently in process by our partner companies will continue. Our production capacity is in place, which should support the business for years to come once we overcome our current obstacles.

Currently, we have 33 ANDAs pending approval at the FDA (including four tentative approvals) relating to 29 products. Out of the 33 ANDAs pending approval, 31 (including four tentative approvals) are filed from our Michigan facilities and the remaining two are filed from the manufacturing sites of our partner companies, one of which is an affiliate. We continue to upgrade our facilities, and expand our customer base. We now have 16 products, that we market (including Caraco-owned products being manufactured by other parties, including Sun Pharma, and those distributed under various agreements with Sun Pharma), whose market share is ranked third or higher against the same products of our generic competitors. We are focused on products that are currently in our portfolio and are yet to realize their full market potential. The total portfolio consists of 52 products.

In addition to certain Caraco-owned products manufactured by Sun Pharma and its affiliates, we have also transferred certain Caraco-owned products to alternate manufacturing sites of Sun Pharma and its affiliates that would allow the Company to realize revenues from those products. We have filed with the FDA supplements to ANDAs, for its approval, for these transferred products. There is no assurance that such approvals will be granted.

Should pricing pressures become more severe than anticipated; the result may be reduced growth rates and gross margins. Management has worked, and will continue to work, diligently to counter the pricing pressures through increased sales volumes, improved market share on existing products, expansion of our customer base, improved productivity, and increased cost reductions.

The FDA's action and the Company's voluntary cessation of manufacturing have had, and are expected to continue to have, a material adverse effect on operations and operating results. At December 31, 2010, the Company had $54 million in cash and $10 million in short-term investments including the proceeds from a loan in the amount of $12.6 million. The Company believes that its cash flow from operations and cash balances will continue to support its ongoing business requirements including working capital requirements, funding of potential litigation expenses relating to Paragraph IV certification and financing of further capital investments. However, because, among other things, of the uncertainty of future costs of FDA compliance and associated costs, there can be no assurance of this belief.

The Company has decreased its internal development of new products. Beginning in Fiscal 2007, we entered into seven definitive agreements with various companies, one of which is an affiliate, to develop eight additional ANDAs for Caraco and provide additional opportunities for the future development of products. These agreements contain, both milestone payments to be paid in cash and profit sharing based upon future sales for a defined period, for certain products and only milestone payments in cash without any obligation to share profits in the future for other products. However we have terminated two agreements earlier entered for three of these products. This brings the total number of products being developed by such companies to five. During the first nine months of Fiscal 2011, the Company filed ANDAs with the FDA for two of these products.

As previously mentioned, in Fiscal 2007 we entered into a definitive agreement to market Sun Pharma ANDAs that are either approved or awaiting approval at the FDA. Accordingly, we continue to market a number of these products which are categorized as distributed products. This agreement was renewed in January 2010, for a period of one year, and was further extended until January 28, 2012, on which date it will terminate. The Company and its Independent Committee of the Board approached Sun Pharma and attempted to negotiate a long term renewal for the agreement; however, Sun Pharma exercised its right to end the agreement, following the extension, on January 28, 2012.

In addition, on January 29, 2008, the Company executed a distribution and sale agreement with Sun Pharma. This agreement covers certain mutually agreed upon products that have been filed or will be filed with the FDA with a Paragraph IV certification. A Paragraph IV certification states that the filer believes that it either does not infringe the patent or believes that the patent is invalid. Paragraph IV certified products face litigation challenges with respect to claims of patent infringement. Sun Pharma is not obligated to offer Caraco products under this agreement, however, Caraco has the exclusive right to market in the U.S., its territories and possessions, including Puerto Rico, any products offered by Sun Pharma and accepted by Caraco. Under the agreement, the Company participates in the sales opportunity on the products, and also shares the litigation risks to a limited extent based on percentage. If such claims are successful, however, they could have a material adverse effect on the Company. We have been marketing several products under this agreement including Pantoprazole sodium DR tablets and Oxaliplatin. See "Note 12. Litigation." The initial term of the Distribution and Sale agreement was set to expire on January 29, 2011 and has been extended until January 28, 2012, on which date it will terminate. The Company and its Independent Committee of the Board approached Sun Pharma and attempted to negotiate a long term renewal for this agreement; however, Sun Pharma exercised its right to end the agreement, following the extension, on January 28, 2012.

Currently our revenues are highly dependent on these agreements as we have ceased all manufacturing activities due to the actions of the FDA. Once these agreements are terminated, the Company would incur significantly higher losses and such non-renewal would have a material adverse effect on its results of operations. The future termination of these agreements may also result in loss of sales of distributed products prior to the termination, and thus may have material adverse effect on the Company's results of operations.

The Company's goals for the remainder of Fiscal 2011 include:

- Compliance with Consent Decree.
- Continue working towards resumption of manufacturing activities in conformance with FDA guidelines, the work plan approved by the FDA and the Consent Decree.
- Discuss transition plan for transfer of products to Sun Pharma, currently marketed under distribution agreements with Sun Pharma, scheduled to expire in January 2012.
- Increase cGMP training to accommodate staff and compliance.
- Increase market share for certain existing products and recently introduced products.
- Enhanced customer reach and satisfaction.
- Leverage distribution and marketing core competencies by marketing third party products through in-licensing agreements.
- Increase revenue and cash by marketing ANDAs owned by Sun Pharma, and the prompt introduction of new products to the market.
- Research alternate product development sources and product licenses such as in licensing authorized generics from brand innovator companies and acquisitions of ANDAs from competitor manufacturers both domestically and abroad.
- Increase management training and development.

Forward Looking Statements

This report, other than the historical financial and business information, may contain forward-looking statements within the meaning of Section 27A of the Securities Act of 1933 and Section 21E of the Securities Exchange Act of 1934. Without limitation, the words "believes," "plans," "expects," and similar expressions are intended to identify forward-looking statements. Those statements include statements regarding our intent, belief, and current expectation. These statements are not guarantees of future performance and are subject to risks and uncertainties that cannot be predicted or quantified. Consequently, actual results could differ materially from those expressed or implied by such forward-looking statements.

Such risks and uncertainties include, but are not limited to: (i) that the information is of a preliminary nature and may be subject to further adjustment; (ii) not obtaining FDA approval for new products or delays in receiving FDA approvals; (iii) governmental restrictions on the sale of certain products; (iv) dependence on key personnel; (v) development by competitors of new or superior products or cheaper products or new technology for the production of products or the entry into the market of new competitors; (vi) market and customer acceptance and demand for new

pharmaceutical products; (vii) availability of raw materials in a timely manner, at competitive prices, and in required quantities; (viii) timing and success of product development and launch; (ix) integrity and reliability of the Company's data; (x) lack of success in attaining full compliance with regard to regulatory and cGMP compliance; (xi) inability to achieve successful remediation efforts; (xii) dependence on limited customer base; (xiii) occasional credits to certain customers reflecting price reductions on products previously sold to them and still available as shelf-stock; (xiv) possibility of an incorrect estimate of charge-backs and the impact of such an incorrect estimate on net sales, gross profit and net income; (xv) dependence on few products generating majority of sales; (xvi) product liability claims for which the Company may be inadequately insured; (xvii) subjectivity in judgment of management in applying certain significant accounting policies derived based on historical experience, terms of contracts, our observations of trends of industry, information received from our customers and other sources, to estimate revenues, accounts receivable allowances including chargebacks, rebates, income taxes, values of assets and inventories; (xviii) litigation involving claims of patent infringement; (xix) litigation involving claims for royalties and/or options relating to a prior contract for one product, (xx) material litigation from product recalls, (xxi) the purported class action lawsuits alleging federal securities laws violations, (xxii) delays in returning the Company's products to market, including loss of market share, (xxiii) excessive dependency for revenues on the marketing agreement and distribution and sale agreement, both signed with Sun Pharma; (xxiv) excessive dependency on Sun Pharma and other third parties for manufacture of Caraco-owned products; (xxv) inability to successfully transfer Caraco-owned products; and (xxvi) other risks identified in this report and identified from time to time in our reports and registration statements filed with the Securities and Exchange Commission (see Item 1A hereof and our Annual Report on Form 10-K for the year ended March 31, 2010, Part I, Item 1A, for more detailed discussion of such risks). These forward-looking statements represent our judgment as of the date of this report. We disclaim, however, any intent or obligation to update our forward-looking statements.

ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

Refer to “Item 7A. Quantitative and Qualitative Disclosures About Market Risk” in our Annual Report on Form 10-K for the year ended March 31, 2010 and “Note 11. Debt” above for a discussion of our market risk.

ITEM 4. CONTROLS AND PROCEDURES

a. The term “disclosure controls and procedures” is defined in Rules 13a-15(e) and 15d-15(e) of the Securities Exchange Act of 1934 (the “Exchange Act”). These rules refer to the controls and other procedures of a company that are designed to ensure that information required to be disclosed by a company in the reports that it files under the Exchange Act is recorded, processed, summarized and reported within required time periods. Our Chief Executive Officer and our interim Chief Financial Officer have evaluated the effectiveness of our disclosure controls and procedures as of the end of the period covered by this report (the “Evaluation Date”), and have concluded that, as of the Evaluation Date, our disclosure controls and procedures are effective in providing them with material information relating to the Company known to others within the Company which is required to be included in our periodic reports filed under the Exchange Act.

b. There has been no change in the Company's internal control over financial reporting that occurred during the third quarter of Fiscal 2011 that materially affected, or is reasonably likely to materially affect, the Company's internal control over financial reporting. The Company has engaged an outside firm to support its internal audit function.

PART II -- OTHER INFORMATION

ITEM 1. LEGAL PROCEEDINGS

The information presented in Note 12 of Part I, Notes to Financial Statements, is incorporated herein by reference.

ITEM 2. UNREGISTERED SALES OF EQUITY SECURITES AND USE OF PROCEEDS

During the first nine months of Fiscal 2011, 1,088,000 shares of Series B Preferred Stock previously issued to Sun Global were converted into 1,088,000 shares of Caraco common stock and issued to Sun Global.

All shares of Caraco common stock issued by the Company as set forth above were issued pursuant to exemptions from registration under Section 4(2) of the Securities Act of 1933.

ITEM 6. EXHIBITS

10.34 Fourth Amendment to Loan Agreement with RBS Citizens N.A. dated January 7, 2011.

10.35 Certificate of Suspension of Loan Covenants between Caraco and RBS Citizens N.A. dated January 7, 2011.

31.1 Certification of Chief Executive Officer

31.2 Certification of Interim Chief Financial Officer.

32.1 Certification pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.

SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

CARACO PHARMACEUTICAL LABORATORIES, LTD.

Date: February 9, 2011

By: /s/ GP. Singh Sachdeva
GP. Singh Sachdeva
Chief Executive Officer

Date: February 9, 2011

By: /s/ Mukul Rathi
Mukul Rathi
Interim Chief Financial Officer

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