

CONMED CORP  
Form 10-Q  
August 09, 2011

UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

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

For the quarterly period ended  
June 30, 2011

Commission File Number  
0-16093

CONMED CORPORATION  
(Exact name of the registrant as specified in its charter)

New York  
(State or other jurisdiction of  
incorporation or organization)

16-0977505  
(I.R.S. Employer  
Identification No.)

525 French Road, Utica, New York  
(Address of principal executive offices)

13502  
(Zip Code)

(315) 797-8375  
(Registrant's telephone number, including area code)

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 ☒ 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 shorter period that the registrant was required to submit and post such files). ☒

Edgar Filing: CONMED CORP - Form 10-Q

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 definition of “accelerated filer”, “large accelerated filer” and “smaller reporting company” in Rule 12b-2 of the Exchange Act (Check one).

Large accelerated filer ☐ 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 Exchange Act).

Yes ☐ No ☒

The number of shares outstanding of registrant's common stock, as of July 27, 2011 is 28,569,319 shares.

---

CONMED CORPORATION  
QUARTERLY REPORT ON FORM 10-Q  
FOR THE QUARTER ENDED JUNE 30, 2011

PART I FINANCIAL INFORMATION

| Item Number               |   | Page |
|---------------------------|---|------|
| <u>Item 1.</u>            | <u>Financial Statements (unaudited)</u>   |      |
|                           | <u>- Consolidated Condensed Statements of Income for the three and six month periods ended June 30, 2010 and 2011</u> | 1    |
|                           | <u>- Consolidated Condensed Balance Sheets as of December 31, 2010 and June 30, 2011</u>                              | 2    |
|                           | <u>- Consolidated Condensed Statements of Cash Flows for the six months ended June 30, 2010 and 2011</u>              | 3    |
|                           | <u>- Notes to Consolidated Condensed Financial Statements</u>   | 4    |
| <u>Item 2.</u>            | <u>Management's Discussion and Analysis of Financial Condition and Results of Operations</u>                          | 15   |
| <u>Item 3.</u>            | <u>Quantitative and Qualitative Disclosures About Market Risk</u>   | 32   |
| <u>Item 4.</u>            | <u>Controls and Procedures</u>  | 32   |
| PART II OTHER INFORMATION |   |      |
| <u>Item 1.</u>            | <u>Legal Proceedings</u>  | 32   |
| <u>Item 6.</u>            | <u>Exhibits</u>   | 33   |
| <u>Signatures</u>         |   | 34   |

Table of Contents

## PART I FINANCIAL INFORMATION

## Item 1.

CONMED CORPORATION  
CONSOLIDATED CONDENSED STATEMENTS OF INCOME  
(Unaudited, in thousands except per share amounts)

|   | Three Months Ended<br>June 30, |           | Six Months Ended<br>June 30, |           |
|---|--------------------------------|-----------|------------------------------|-----------|
|   | 2010                           | 2011      | 2010                         | 2011      |
| Net sales                               | \$181,086                      | \$183,236 | \$357,451                    | \$366,686 |
| Cost of sales                           | 87,403                         | 91,781    | 171,973                      | 179,515   |
| Gross profit                            | 93,683                         | 91,455    | 185,478                      | 187,171   |
| Selling and administrative expense      | 71,494                         | 67,862    | 142,046                      | 137,940   |
| Research and development expense        | 6,441                          | 6,797     | 14,123                       | 14,478    |
| Other expense                           | 970                            | 98        | 970                          | 792       |
|   | 78,905                         | 74,757    | 157,139                      | 153,210   |
| Income from operations                  | 14,778                         | 16,698    | 28,339                       | 33,961    |
| Loss on early extinguishment<br>of debt | 79                             | -         | 79                           | -         |
| Amortization of debt discount           | 1,056                          | 1,113     | 2,108                        | 2,207     |
| Interest expense                        | 1,771                          | 1,707     | 3,520                        | 3,512     |
| Income before income taxes              | 11,872                         | 13,878    | 22,632                       | 28,242    |
| Provision for income taxes              | 4,566                          | 5,198     | 8,007                        | 10,567    |
| Net income                              | \$7,306                        | \$8,680   | \$14,625                     | \$17,675  |
| Per share data:                         |                                |           |                              |           |
| Net Income                              |                                |           |                              |           |
| Basic                                   | \$.25                          | \$.31     | \$.50                        | \$.62     |
| Diluted                                 | .25                            | .30       | .50                          | .61       |
| Weighted average common shares          |                                |           |                              |           |
| Basic                                   | 29,100                         | 28,448    | 29,125                       | 28,356    |

|         |        |        |        |        |
|---------|--------|--------|--------|--------|
| Diluted | 29,295 | 28,883 | 29,342 | 28,820 |
|---------|--------|--------|--------|--------|

See notes to consolidated condensed financial statements.

Table of Contents

CONMED CORPORATION  
CONSOLIDATED CONDENSED BALANCE SHEETS  
(Unaudited, in thousands except share and per share amounts)

|  | December<br>31,<br>2010 | June 30,<br>2011 |
|--|-------------------------|------------------|
| <b>ASSETS</b>  |                         |                  |
| Current assets:  |                         |                  |
| Cash and cash equivalents  | \$12,417                | \$24,331         |
| Accounts receivable, net   | 145,350                 | 152,695          |
| Inventories  | 172,796                 | 169,254          |
| Deferred income taxes  | 8,476                   | 8,824            |
| Prepaid expenses and other current assets  | 11,153                  | 13,078           |
| Total current assets   | 350,192                 | 368,182          |
| Property, plant and equipment, net   | 140,895                 | 140,792          |
| Deferred income taxes  | 2,009                   | 2,354            |
| Goodwill   | 295,068                 | 294,874          |
| Other intangible assets, net   | 190,091                 | 186,868          |
| Other assets   | 7,518                   | 7,095            |
| Total assets   | \$985,773               | \$1,000,165      |
|  |                         |                  |
| <b>LIABILITIES AND SHAREHOLDERS' EQUITY</b>  |                         |                  |
| Current liabilities:   |                         |                  |
| Current portion of long-term debt  | \$110,433               | \$144,065        |
| Accounts payable   | 21,692                  | 20,981           |
| Accrued compensation and benefits  | 28,411                  | 23,060           |
| Income taxes payable   | 973                     | 1,267            |
| Other current liabilities  | 18,357                  | 20,974           |
| Total current liabilities  | 179,866                 | 210,347          |
| Long-term debt   | 85,182                  | 30,644           |
| Deferred income taxes  | 106,046                 | 114,671          |
| Other long-term liabilities  | 28,116                  | 27,794           |
| Total liabilities  | 399,210                 | 383,456          |
| <b>Commitments and contingencies</b>   |                         |                  |
| <b>Shareholders' equity:</b>   |                         |                  |
| Preferred stock, par value \$ .01 per share;<br>authorized 500,000 shares; none outstanding  | -                       | -                |
| Common stock, par value \$ .01 per share;<br>100,000,000 shares authorized; 31,299,203 shares<br>issued in 2010 and 2011, respectively | 313                     | 313              |
| Paid-in capital  | 319,406                 | 319,259          |

Edgar Filing: CONMED CORP - Form 10-Q

|   |           |             |
|---|-----------|-------------|
| Retained earnings   | 354,020   | 371,365     |
| Accumulated other comprehensive loss  | (15,861 ) | (10,710 )   |
| Less: 3,077,377 and 2,741,168 shares of common stock<br>in treasury, at cost in 2010 and 2011, respectively | (71,315 ) | (63,518 )   |
| Total shareholders' equity  | 586,563   | 616,709     |
| Total liabilities and shareholders' equity  | \$985,773 | \$1,000,165 |

See notes to consolidated condensed financial statements.

Table of Contents

CONMED CORPORATION  
CONSOLIDATED CONDENSED STATEMENTS OF CASH FLOWS  
(Unaudited, in thousands)

|  | Six months ended<br>June 30, |           |
|--|------------------------------|-----------|
|  | 2010                         | 2011      |
| Cash flows from operating activities:  |                              |           |
| Net income   | \$14,625                     | \$17,675  |
| Adjustments to reconcile net income<br>to net cash provided by operating activities: |                              |           |
| Depreciation   | 8,449                        | 8,983     |
| Amortization of debt discount  | 2,108                        | 2,207     |
| Amortization, all other  | 10,024                       | 9,857     |
| Stock-based compensation expense   | 2,082                        | 2,232     |
| Deferred income taxes  | 7,239                        | 8,981     |
| Loss on early extinguishment of debt   | 79                           | -         |
| Sale of accounts receivable to<br>(collections on behalf of) purchaser               | (29,000 )                    | -         |
| Increase (decrease) in cash flows<br>from changes in assets and liabilities:         |                              |           |
| Accounts receivable  | 8,718                        | (4,541 )  |
| Inventories  | (16,167 )                    | 78        |
| Accounts payable   | 6,100                        | 2,309     |
| Income taxes payable   | (125 )                       | 143       |
| Accrued compensation and benefits  | 90                           | (5,684 )  |
| Other assets   | (2,884 )                     | (2,226 )  |
| Other liabilities  | (5,815 )                     | 209       |
|  | (9,102 )                     | 22,548    |
| Net cash provided by operating activities  | 5,523                        | 40,223    |
| Cash flows from investing activities:  |                              |           |
| Purchases of property, plant and equipment   | (7,163 )                     | (8,576 )  |
| Payments related to business acquisitions  | (5,157 )                     | (72 )     |
| Net cash used in investing activities  | (12,320 )                    | (8,648 )  |
| Cash flows from financing activities:  |                              |           |
| Net proceeds from common stock issued<br>under employee plans                        | 789                          | 5,495     |
| Repurchase of treasury stock   | (9,471 )                     | -         |
| Payments on senior credit agreement  | (10,675 )                    | (22,675 ) |
| Payments on mortgage notes   | (404 )                       | (438 )    |
| Proceeds from secured borrowings, net  | 31,000                       | -         |
| Payments on senior subordinated notes  | (2,933 )                     | -         |
| Net change in cash overdrafts  | (2,068 )                     | (3,148 )  |
| Net cash provided by<br>(used in) financing activities                               | 6,238                        | (20,766 ) |
| Effect of exchange rate changes  |                              |           |



|  |          |          |
|--|----------|----------|
| on cash and cash equivalents                         | (1,049 ) | 1,105    |
| Net increase (decrease) in cash and cash equivalents | (1,608 ) | 11,914   |
| Cash and cash equivalents at beginning of period     | 10,098   | 12,417   |
| Cash and cash equivalents at end of period           | \$8,490  | \$24,331 |

See notes to consolidated condensed financial statements.

Table of Contents

CONMED CORPORATION  
NOTES TO CONSOLIDATED CONDENSED FINANCIAL STATEMENTS  
(Unaudited, in thousands except per share amounts)

## Note 1 – Operations

CONMED Corporation (“CONMED”, the “Company”, “we” or “us”) is a medical technology company with an emphasis on surgical devices and equipment for minimally invasive procedures and monitoring. The Company’s products serve the clinical areas of arthroscopy, powered surgical instruments, electrosurgery, cardiac monitoring single-uses, endosurgery and endoscopic technologies. They are used by surgeons and physicians in a variety of specialties including orthopedics, general surgery, gynecology, neurosurgery, and gastroenterology.

## Note 2 - Interim financial information

The accompanying unaudited consolidated condensed financial statements have been prepared in accordance with generally accepted accounting principles for interim financial information and with the instructions to Form 10-Q and Article 10 of Regulation S-X. Accordingly, they do not include all of the information and footnotes required by generally accepted accounting principles for annual financial statements. Results for the period ended June 30, 2011 are not necessarily indicative of the results that may be expected for the year ending December 31, 2011.

The consolidated condensed financial statements and notes thereto should be read in conjunction with the financial statements and notes for the year ended December 31, 2010 included in our Annual Report on Form 10-K.

## Note 3 – Comprehensive income

Comprehensive income consists of the following:

|   | Three months ended<br>June 30, |          | Six months ended<br>June 30, |          |
|---|--------------------------------|----------|------------------------------|----------|
|   | 2010                           | 2011     | 2010                         | 2011     |
| Net income  | \$7,306                        | \$8,680  | \$14,625                     | \$17,675 |
| Other comprehensive income:                         |                                |          |                              |          |
| Pension liability, net of<br>income tax             | 207                            | 266      | 414                          | 497      |
| Cash flow hedging gain (loss),<br>net of income tax | 858                            | 271      | 1,464                        | (775 )   |
| Foreign currency<br>translation adjustment          | (5,786 )                       | 1,585    | (7,354 )                     | 5,429    |
| Comprehensive income                                | \$2,585                        | \$10,802 | \$9,149                      | \$22,826 |



Table of Contents

Accumulated other comprehensive income (loss) consists of the following:

|  | Cash Flow<br>Hedging<br>Loss | Pension<br>Liability | Cumulative<br>Translation<br>Adjustments | Accumulated<br>Other<br>Comprehensive<br>Income (loss) |
|--|------------------------------|----------------------|--|--|
| Balance, December 31, 2010                   | \$(1,245 )                   | \$(18,482 )          | \$ 3,866                                 | \$ (15,861 )   |
| Pension liability,<br>net of income tax      | -                            | 497                  | -  | 497  |
| Cash flow hedging loss,<br>net of income tax | (775 )                       | -                    | -  | (775 )   |
| Foreign currency translation<br>adjustments  | -                            | -                    | 5,429                                    | 5,429  |
| Balance, June 30, 2011                       | \$(2,020 )                   | \$(17,985 )          | \$ 9,295                                 | \$ (10,710 )   |

#### Note 4 – Fair value of financial instruments

We enter into derivative instruments for risk management purposes only. We operate internationally and, in the normal course of business, are exposed to fluctuations in interest rates, foreign exchange rates and commodity prices. These fluctuations can increase the costs of financing, investing and operating the business. We use forward contracts, a type of derivative instrument, to manage certain foreign currency exposures.

By nature, all financial instruments involve market and credit risks. We enter into forward contracts with major investment grade financial institutions and have policies to monitor the credit risk of those counterparties. While there can be no assurance, we do not anticipate any material non-performance by any of these counterparties.

**Foreign Currency Forward Contracts.** We hedge forecasted intercompany sales denominated in foreign currencies through the use of forward contracts. We account for these forward contracts as cash flow hedges. To the extent these forward contracts meet hedge accounting criteria, changes in their fair value are not included in current earnings but are included in accumulated other comprehensive loss. These changes in fair value will be recognized into earnings as a component of sales when the forecasted transaction occurs. The notional contract amounts for forward contracts outstanding at June 30, 2011 which have been accounted for as cash flow hedges totaled \$99.6 million. Net realized gains (losses) recognized for forward contracts accounted for as cash flow hedges approximated \$1.3 million and (\$2.3 million) for the three months ended June 30, 2010 and 2011, respectively and \$2.2 million and (\$3.5 million) for the six months ended June 30, 2010 and 2011, respectively. Net unrealized losses on forward contracts outstanding, which have been accounted for as cash flow hedges and which have been included in other comprehensive income, totaled \$2.0 million at June 30, 2011. These unrealized losses and any subsequent changes in fair value will be recognized in the consolidated statements of operations in 2011 and 2012 as the related forward

contracts mature and gains and losses are realized.

Table of Contents

We also enter into forward contracts to exchange foreign currencies for United States dollars in order to hedge our currency transaction exposures on intercompany receivables denominated in foreign currencies. These forward contracts settle each month at month-end, at which time we enter into new forward contracts. We have not designated these forward contracts as hedges and have not applied hedge accounting to them. The notional contract amounts for forward contracts outstanding at June 30, 2011 which have not been designated as hedges totaled \$38.0 million. Net realized gains (losses) recognized in connection with those forward contracts not accounted for as hedges approximated \$1.0 million and (\$0.6 million) for the three months ended June 30, 2010 and 2011, respectively, offsetting gains (losses) on our intercompany receivables of (\$0.1 million) and \$0.4 million for the three months ended June 30, 2010 and 2011, respectively. Net realized gains (losses) recognized in connection with those forward contracts not accounted for as hedges approximated \$1.3 million and (\$1.6 million) for the six months ended June 30, 2010 and 2011, respectively, offsetting gains (losses) on our intercompany receivables of (\$0.8 million) and \$1.6 million for the six months ended June 30, 2010 and 2011, respectively. These gains and losses have been recorded in selling and administrative expense in the consolidated statements of operations.

We record these forward foreign exchange contracts at fair value; the following table summarizes the fair value for forward foreign exchange contracts outstanding at June 30, 2011:

|  | Asset<br>Balance Sheet<br>Location | Fair<br>Value | Liabilities<br>Balance Sheet<br>Location | Fair<br>Value | Net<br>Fair<br>Value |
|--|------------------------------------|---------------|--|---------------|----------------------|
| Derivatives designated as hedged instruments:      |                                    |               |  |               |                      |
| Foreign Exchange Contracts                         | Other current liabilities          | \$ (135 )     | Other current liabilities                | \$ 3,339      | \$ 3,204             |
| Derivatives not designated as hedging instruments: |                                    |               |  |               |                      |
| Foreign Exchange Contracts                         | Other current liabilities          | -             | Other current liabilities                | 89            | 89                   |
| Total derivatives                                  |                                    | \$ (135 )     |  | \$ 3,428      | \$ 3,293             |

Our forward foreign exchange contracts are subject to a master netting agreement and qualify for netting in the consolidated balance sheets. Accordingly, we have recorded the net fair value of \$3.3 million in other current liabilities.

**Fair Value Disclosure.** Financial Accounting Standards Board (“FASB”) guidance defines fair value and establishes a framework for measuring fair value and related disclosure requirements. This guidance applies when fair value measurements are required or permitted. The guidance indicates, among other things, that a fair value measurement assumes that the transaction to sell an asset or transfer a liability occurs in the principal market for the asset or liability or, in the absence of a principal market, the most advantageous market for the asset or liability. Fair value is defined based upon an exit price model.



Table of Contents

As of June 30, 2011, we do not have any significant non-recurring measurements of nonfinancial assets and nonfinancial liabilities.

**Valuation Hierarchy.** A valuation hierarchy was established for disclosure of the inputs to the valuations used to measure fair value. This hierarchy prioritizes the inputs into three broad levels as follows. Level 1 inputs are quoted prices (unadjusted) in active markets for identical assets or liabilities. Level 2 inputs are quoted prices for similar assets and liabilities in active markets, quoted prices for identical or similar assets in markets that are not active, inputs other than quoted prices that are observable for the asset or liability, including interest rates, yield curves and credit risks, or inputs that are derived principally from or corroborated by observable market data through correlation. Level 3 inputs are unobservable inputs based on our own assumptions used to measure assets and liabilities at fair value. A financial asset or liability's classification within the hierarchy is determined based on the lowest level input that is significant to the fair value measurement.

**Valuation Techniques.** Liabilities carried at fair value and measured on a recurring basis as of June 30, 2011 consist of forward foreign exchange contracts and two embedded derivatives associated with our 2.50% convertible senior subordinated notes (the "Notes"). The value of the forward foreign exchange contracts was determined within Level 2 of the valuation hierarchy and is listed in the table above. The value of the two embedded derivatives associated with the Notes was determined within Level 2 of the valuation hierarchy and was not material either individually or in the aggregate to our financial position, results of operations or cash flows.

The carrying amounts reported in our balance sheets for cash and cash equivalents, accounts receivable, accounts payable and long-term debt excluding the Notes approximate fair value. The fair value of the Notes approximated \$111.7 million and \$112.8 million at December 31, 2010 and June 30, 2011, respectively, based on their quoted market price. During the quarter ended June 30, 2010, we repurchased and retired \$3.0 million of the Notes for \$2.9 million and recorded a loss on the early extinguishment of debt of \$0.1 million.

#### Note 5 - Inventories

Inventories consist of the following:

|                 | December<br>31,<br>2010 | June 30,<br>2011 |
|-----------------|-------------------------|------------------|
| Raw materials   | \$49,038                | \$44,603         |
| Work-in-process | 15,460                  | 17,343           |
| Finished goods  | 108,298                 | 107,308          |
| Total           | \$172,796               | \$169,254        |

#### Note 6 – Earnings per share

Basic earnings per share ("basic EPS") is computed by dividing net income by the weighted average number of common shares outstanding for the reporting period. Diluted earnings per share ("diluted EPS") gives effect to all dilutive potential shares outstanding resulting from employee stock options, restricted stock units and stock appreciation rights ("SARs") during the period. The following table sets forth the computation of basic and diluted earnings per share for the three and six months ended June 30, 2010 and 2011.





Table of Contents

|  | Three months ended<br>June 30, |         | Six months ended<br>June 30, |          |
|--|--------------------------------|---------|------------------------------|----------|
|  | 2010                           | 2011    | 2010                         | 2011     |
| Net income                                       | \$7,306                        | \$8,680 | \$14,625                     | \$17,675 |
| Basic – weighted average shares<br>outstanding   | 29,100                         | 28,448  | 29,125                       | 28,356   |
| Effect of dilutive potential<br>securities       | 195                            | 435     | 217                          | 464      |
| Diluted – weighted average<br>shares outstanding | 29,295                         | 28,883  | 29,342                       | 28,820   |
| Net Income                                       |                                |         |                              |          |
| Basic  | \$.25                          | \$.31   | \$.50                        | \$.62    |
| Diluted  | .25                            | .30     | .50                          | .61      |

The shares used in the calculation of diluted EPS exclude options and SARs to purchase shares where the exercise price was greater than the average market price of common shares for the period. Shares excluded from the calculation of diluted EPS aggregated 1.5 million and 1.4 million for the three and six months ended June 30, 2010, respectively. Shares excluded from the calculation of diluted EPS aggregated 0.6 million and 0.7 million for the three and six months ended June 30, 2011, respectively. The shares used in the calculation of diluted EPS also exclude potential shares issuable under the Notes. Upon conversion of the Notes, the holder of each Note will receive the conversion value of the Note payable in cash up to the principal amount of the Note and CONMED common stock for the Note's conversion value in excess of such principal amount. As of June 30, 2011, our share price has not exceeded the conversion price of the Notes, therefore the conversion value was less than the principal amount of the Notes. Accordingly, under the net share settlement method, there were no potential shares issuable under the Notes to be used in the calculation of diluted EPS. The maximum number of shares we may issue with respect to the Notes is 5,750,000.

## Note 7 – Goodwill and other intangible assets

The changes in the net carrying amount of goodwill for the six months ended June 30, 2011 are as follows:

|   |           |
|---|-----------|
| Balance as of January 1, 2011   | \$295,068 |
| Adjustments to goodwill resulting from<br>business acquisitions finalized | -         |
| Foreign currency translation  | (194 )    |
| Balance as of June 30, 2011   | \$294,874 |

Total accumulated impairment losses (associated with our CONMED Endoscopic Technologies operating unit) aggregated \$46,689 at December 31, 2010 and June 30, 2011.

Table of Contents

Goodwill associated with each of our principal operating units is as follows:

|                       | December<br>31,<br>2010 | June 30,<br>2011 |
|-----------------------|-------------------------|------------------|
| CONMED Electrosurgery | \$ 16,645               | \$ 16,645        |
| CONMED Endosurgery    | 42,439                  | 42,439           |
| CONMED Linvatec       | 175,682                 | 175,488          |
| CONMED Patient Care   | 60,302                  | 60,302           |
| Balance               | \$295,068               | \$294,874        |

Other intangible assets consist of the following:

|                                     | December 31, 2010           |                             | June 30, 2011               |                             |
|-------------------------------------|-----------------------------|-----------------------------|-----------------------------|-----------------------------|
|                                     | Gross<br>Carrying<br>Amount | Accumulated<br>Amortization | Gross<br>Carrying<br>Amount | Accumulated<br>Amortization |
| Amortized intangible assets:        |                             |                             |                             |                             |
| Customer relationships              | \$127,594                   | \$ (40,801 )                | \$127,594                   | \$ (42,957 )                |
| Patents and other intangible assets | 47,178                      | (32,224 )                   | 47,208                      | (33,317 )                   |
| Unamortized intangible assets:      |                             |                             |                             |                             |
| Trademarks and tradenames           | 88,344                      | -                           | 88,340                      | -                           |
|                                     | \$263,116                   | \$ (73,025 )                | \$263,142                   | \$ (76,274 )                |

Other intangible assets primarily represent allocations of purchase price to identifiable intangible assets of acquired businesses. The weighted average amortization period for intangible assets which are amortized is 31 years. Customer relationships are being amortized over a weighted average life of 34 years. Patents and other intangible assets are being amortized over a weighted average life of 15 years.

Amortization expense related to intangible assets which are subject to amortization totaled \$1,528 and \$3,051 in the three and six months ended June 30, 2010, respectively, and \$1,626 and \$3,249 in the three and six months ended June 30, 2011, respectively, and is included in selling and administrative expense on the consolidated condensed statements of income.

The estimated amortization expense for the year ending December 31, 2011, including the six month period ended June 30, 2011 and for each of the five succeeding years is as follows:

Edgar Filing: CONMED CORP - Form 10-Q

|      |       |
|------|-------|
| 2011 | 6,077 |
| 2012 | 6,023 |
| 2013 | 5,796 |
| 2014 | 5,369 |
| 2015 | 4,734 |
| 2016 | 4,619 |

Table of Contents

## Note 8 — Guarantees

We provide warranties on certain of our products at the time of sale. The standard warranty period for our capital and reusable equipment is generally one year. Liability under service and warranty policies is based upon a review of historical warranty and service claim experience. Adjustments are made to accruals as claim data and historical experience warrant.

Changes in the carrying amount of service and product warranties for the six months ended June 30, are as follows:

|                          | 2010     | 2011     |
|--------------------------|----------|----------|
| Balance as of January 1, | \$3,383  | \$3,363  |
| Provision for warranties | 1,669    | 2,247    |
| Claims made              | (1,740 ) | (2,082 ) |
| Balance as of June 30,   | \$3,312  | \$3,528  |

## Note 9 – Pension plan

Net periodic pension costs consist of the following:

|  | Three months ended<br>June 30, |          | Six months ended<br>June 30, |          |
|--|--------------------------------|----------|------------------------------|----------|
|  | 2010                           | 2011     | 2010                         | 2011     |
| Service cost                                     | \$44                           | \$70     | \$88                         | \$141    |
| Interest cost on projected<br>benefit obligation | 1,006                          | 664      | 2,012                        | 1,759    |
| Expected return on plan assets                   | (1,003 )                       | (1,132 ) | (2,007 )                     | (2,189 ) |
| Net amortization and deferral                    | 328                            | 423      | 657                          | 789      |
| Net periodic pension cost                        | \$375                          | \$25     | \$750                        | \$500    |

We are required and expect to make \$2.1 million in contributions to our pension plan in 2011. We contributed \$0.5 million during the second quarter of 2011 and expect to contribute the remaining \$1.6 million during the second half of 2011.

## Note 10 – Other expense

Other expense consists of the following:

| Three months ended<br>June 30, | Six months ended<br>June 30, |
|--------------------------------|------------------------------|
|--------------------------------|------------------------------|

Edgar Filing: CONMED CORP - Form 10-Q

|                                    | 2010  | 2011 | 2010  | 2011  |
|------------------------------------|-------|------|-------|-------|
| Administrative consolidation costs | 970   | \$98 | 970   | \$792 |
| Other expense                      | \$970 | \$98 | \$970 | \$792 |

Table of Contents

During 2011, we consolidated certain administrative functions in our Utica, New York facility. For the three and six months ending June 30, 2011, we incurred \$0.1 million and \$0.8 million, respectively, in related costs consisting principally of severance charges.

During the second quarter of 2010, we incurred \$1.0 million in restructuring costs associated with the consolidation of administrative functions in our CONMED Linvatec division.

## Note 11 — Business Segments and Geographic Areas

CONMED conducts its business through five principal operating segments, CONMED Endoscopic Technologies, CONMED Endosurgery, CONMED Electrosurgery, CONMED Linvatec and CONMED Patient Care. We believe each of our segments are similar in the nature of their products, production processes, customer base, distribution methods and regulatory environment. Our CONMED Endosurgery, CONMED Electrosurgery and CONMED Linvatec operating segments also have similar economic characteristics and therefore qualify for aggregation. Our CONMED Patient Care and CONMED Endoscopic Technologies operating units do not qualify for aggregation since their economic characteristics do not meet the criteria for aggregation as a result of the lower overall operating margin in these segments.

CONMED Endosurgery, CONMED Electrosurgery and CONMED Linvatec consist of a single aggregated segment comprising a complete line of endo-mechanical instrumentation for minimally invasive laparoscopic procedures, electrosurgical generators and related surgical instruments, arthroscopic instrumentation for use in orthopedic surgery and small bone, large bone and specialty powered surgical instruments. CONMED Patient Care product offerings include a line of vital signs and cardiac monitoring products as well as suction instruments & tubing for use in the operating room. CONMED Endoscopic Technologies product offerings include a comprehensive line of minimally invasive endoscopic diagnostic and therapeutic instruments used in procedures which require examination of the digestive tract.

The following is net sales information by product line and reportable segment:

|   | Three months ended<br>June 30, |           | Six months ended<br>June 30, |           |
|---|--------------------------------|-----------|------------------------------|-----------|
|   | 2010                           | 2011      | 2010                         | 2011      |
| Arthroscopy   | 74,821                         | 70,646    | 147,075                      | 146,065   |
| Powered Surgical Instruments                        | 35,769                         | 38,255    | 70,758                       | 76,291    |
| CONMED Linvatec                                     | 110,590                        | 108,901   | 217,833                      | 222,356   |
| CONMED Electrosurgery                               | 23,965                         | 26,053    | 47,048                       | 49,625    |
| CONMED Endosurgery                                  | 17,143                         | 19,133    | 34,223                       | 37,031    |
| CONMED Linvatec, Endosurgery,<br>and Electrosurgery | 151,698                        | 154,087   | 299,104                      | 309,012   |
| CONMED Patient Care                                 | 17,461                         | 16,636    | 34,620                       | 33,260    |
| CONMED Endoscopic Technologies                      | 11,927                         | 12,513    | 23,727                       | 24,414    |
| Total   | \$181,086                      | \$183,236 | \$357,451                    | \$366,686 |



Table of Contents

Total assets, capital expenditures, depreciation and amortization information are impracticable to present by reportable segment because the necessary information is not available.

The following is a reconciliation between segment operating income and income before income taxes:

|   | Three months ended<br>June 30, |          | Six months ended<br>June 30, |          |
|---|--------------------------------|----------|------------------------------|----------|
|   | 2010                           | 2011     | 2010                         | 2011     |
| CONMED Endosurgery, Electrosurgery and Linvatec | \$21,271                       | \$20,529 | \$38,527                     | \$44,804 |
| CONMED Patient Care                             | 1,200                          | (999 )   | 1,546                        | (1,735 ) |
| CONMED Endoscopic Technologies                  | (237 )                         | 355      | (38 )                        | 165      |
| Corporate                                       | (7,456 )                       | (3,187 ) | (11,696 )                    | (9,273 ) |
| Income from Operations                          | 14,778                         | 16,698   | 28,339                       | 33,961   |
| Loss on early extinguishment<br>of debt         | 79                             | -        | 79                           | -        |
| Amortization of debt discount                   | 1,056                          | 1,113    | 2,108                        | 2,207    |
| Interest expense                                | 1,771                          | 1,707    | 3,520                        | 3,512    |
| Income before income taxes                      | \$11,872                       | \$13,878 | \$22,632                     | \$28,242 |

## Note 12 – Legal proceedings

From time to time, we are a defendant in certain lawsuits alleging product liability, patent infringement, or other claims incurred in the ordinary course of business. Likewise, from time to time, the Company may receive a subpoena from a government agency such as the Equal Employment Opportunity Commission, Occupational Safety and Health Administration, the Department of Labor, the Treasury Department, and other federal and state agencies or foreign governments or government agencies. These subpoenas may or may not be routine inquiries, or may begin as routine inquiries and over time develop into enforcement actions of various types. The product liability claims are generally covered by various insurance policies, subject to certain deductible amounts, maximum policy limits and certain exclusions in the respective policies or required as a matter of law. In some cases we may be entitled to indemnification by third parties. When there is no insurance coverage, as would typically be the case primarily in lawsuits alleging patent infringement or in connection with certain government investigations, or indemnification obligations of a third party, we establish reserves sufficient to cover probable losses associated with such claims. We do not expect that the resolution of any pending claims or investigations will have a material adverse effect on our financial condition, results of operations or cash flows. There can be no assurance, however, that future claims or investigations, or the costs associated with responding to such claims or investigations, especially claims and investigations not covered by insurance, will not have a material adverse effect on our financial condition, results of operations or cash flows.

Manufacturers of medical products may face exposure to significant product liability claims. To date, we have not experienced any product liability claims that are material to our financial statements or condition, but any such claims arising in the future could have a material adverse effect on our business or results of operations. We currently maintain commercial product liability insurance of \$25 million per incident and \$25 million in the aggregate annually, which we believe is adequate. This coverage is on a claims-made basis. There can be no assurance that claims will not exceed insurance coverage, that the carriers will be solvent or that such insurance will be available to us in the

future at a reasonable cost.

## Table of Contents

Our operations are subject, and in the past have been subject, to a number of environmental laws and regulations governing, among other things, air emissions, wastewater discharges, the use, handling and disposal of hazardous substances and wastes, soil and groundwater remediation and employee health and safety. In some jurisdictions environmental requirements may be expected to become more stringent in the future. In the United States certain environmental laws can impose liability for the entire cost of site restoration upon each of the parties that may have contributed to conditions at the site regardless of fault or the lawfulness of the party's activities. While we do not believe that the present costs of environmental compliance and remediation are material, there can be no assurance that future compliance or remedial obligations would not have a material adverse effect on our financial condition, results of operations or cash flows.

### Note 13 – New accounting pronouncements

In October 2009, the FASB issued new guidance for arrangements with multiple deliverables under which a company is required to use its best estimate of selling price for the deliverables in an arrangement when vendor specific objective evidence or third party evidence of the selling price is not available. We adopted the updated guidance, including the requirement for expanded qualitative and quantitative disclosures, effective January 1, 2011. The implementation of this new guidance did not have a material impact on our consolidated financial statements.

In May 2011, the FASB issued new authoritative guidance to provide a consistent definition of fair value and ensure that fair value measurements and disclosure requirements are similar between GAAP and International Financial Reporting Standards. This guidance changes certain fair value measurement principles and enhances the disclosure requirements for fair value measurements. This guidance is effective for interim and annual periods beginning after December 15, 2011 and is applied prospectively. We are currently evaluating the impact such guidance will have on our consolidated financial statements.

In June 2011, the FASB amended its guidance on the presentation of comprehensive income in financial statements to improve the comparability, consistency and transparency of financial reporting and to increase the prominence of items that are recorded in other comprehensive income. The new accounting guidance requires entities to report components of comprehensive income in either (1) a continuous statement of comprehensive income or (2) two separate but consecutive statements. This guidance is effective for interim and annual periods beginning after December 15, 2011. We do not believe this guidance will have a material impact on our consolidated financial statements.

Table of Contents

## Note 14 – Restructuring

We incurred the following restructuring costs:

|   | Three months ended<br>June 30,<br>2010 |       | Six months ended<br>June 30,<br>2011 |         |
|---|--|-------|--------------------------------------|---------|
| New plant/facility consolidation costs        | \$992                                  | \$986 | \$1,559                              | \$1,740 |
| Restructuring costs included in cost of sales | \$992                                  | \$986 | \$1,559                              | \$1,740 |
| Administrative consolidation costs            | \$970                                  | \$98  | \$970                                | \$792   |
| Restructuring costs included in other expense | \$970                                  | \$98  | \$970                                | \$792   |

During 2010 and 2011, we continued our operational restructuring plan which includes the transfer of additional production lines from Utica, New York, Largo, Florida and Goleta, California to our manufacturing facility in Chihuahua, Mexico. We incurred \$1.0 million and \$1.6 million in costs associated with the restructuring during the three and six months ending June 30, 2010. We incurred \$1.0 million and \$1.7 million in the three and six months ending June 30, 2011. These costs were charged to cost of goods sold and include severance and other charges associated with the transfer of production to Mexico.

Restructuring costs included in other expense are described more fully in Note 10.

Table of Contents

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

Forward-Looking Statements

In this Report on Form 10-Q, we make forward-looking statements about our financial condition, results of operations and business. Forward-looking statements are statements made by us concerning events that may or may not occur in the future. These statements may be made directly in this document or may be "incorporated by reference" from other documents. Such statements may be identified by the use of words such as "anticipates", "expects", "estimates", "intends" and "believes" and variations thereof and other terms of similar meaning.

Forward-Looking Statements are not Guarantees of Future Performance

Forward-looking statements involve known and unknown risks, uncertainties and other factors, including those that may cause our actual results, performance or achievements, or industry results, to be materially different from any future results, performance or achievements expressed or implied by such forward-looking statements. Such factors include those identified under "Risk Factors" in our Annual Report on Form 10-K for the year-ended December 31, 2010 and the following, among others:

- general economic and business conditions;
- changes in foreign exchange and interest rates;
- cyclical customer purchasing patterns due to budgetary and other constraints;
  - changes in customer preferences;
  - competition;
  - changes in technology;
- the introduction and acceptance of new products;
- the ability to evaluate, finance and integrate acquired businesses, products and companies;
  - changes in business strategy;
  - the availability and cost of materials;
- the possibility that United States or foreign regulatory and/or administrative agencies may initiate enforcement actions against us or our distributors;
  - future levels of indebtedness and capital spending;
- quality of our management and business abilities and the judgment of our personnel;
  - the availability, terms and deployment of capital;

- the risk of litigation, especially patent litigation as well as the cost associated with patent and other litigation; and
- changes in regulatory requirements.

See “Management’s Discussion and Analysis of Financial Condition and Results of Operations” below and “Risk Factors” and “Business” in our Annual Report on Form 10-K for the year-ended December 31, 2010 for a further discussion of these factors. You are cautioned not to place undue reliance on these forward-looking statements, which speak only as of the date hereof. We do not undertake any obligation to publicly release any revisions to these forward-looking statements to reflect events or circumstances after the date of this Quarterly Report on Form 10-Q or to reflect the occurrence of unanticipated events.

Table of Contents

## Overview:

CONMED Corporation (“CONMED”, the “Company”, “we” or “us”) is a medical technology company with six principal product lines. These product lines and the percentage of consolidated revenues associated with each, are as follows:

|                              | Three months ended<br>June 30, |         | Six months ended<br>June 30, |         |
|------------------------------|--------------------------------|---------|------------------------------|---------|
|                              | 2010                           | 2011    | 2010                         | 2011    |
| Arthroscopy                  | 41.3                           | % 38.6  | % 41.1                       | % 39.8  |
| Powered Surgical Instruments | 19.8                           | 20.9    | 19.8                         | 20.8    |
| Electrosurgery               | 13.2                           | 14.2    | 13.2                         | 13.5    |
| Endosurgery                  | 9.5                            | 10.4    | 9.6                          | 10.1    |
| Patient Care                 | 9.6                            | 9.1     | 9.7                          | 9.1     |
| Endoscopic Technologies      | 6.6                            | 6.8     | 6.6                          | 6.7     |
| Consolidated Net Sales       | 100.0                          | % 100.0 | % 100.0                      | % 100.0 |

A significant amount of our products are used in surgical procedures with the majority of our revenues derived from the sale of single-use products. We manufacture substantially all of our products in facilities located in the United States, Mexico, and Finland. We market our products both domestically and internationally directly to customers and through distributors. International sales represent a significant portion of our business. During the three and six months ended June 30, 2011, sales to purchasers outside of the United States approximated 51% and 50%, respectively, of total net sales.

## Business Environment and Opportunities

The aging of the worldwide population along with lifestyle changes, continued cost containment pressures on healthcare systems and the desire of clinicians and administrators to use less invasive (or noninvasive) procedures are important trends which are driving the long-term growth in our industry. We believe that with our broad product offering of high quality surgical and patient care products, we can capitalize on this growth for the benefit of the Company and our shareholders.

In order to further our growth prospects, we have historically used strategic business acquisitions and exclusive distribution relationships to continue to diversify our product offerings, increase our market share and realize economies of scale.

We have a variety of research and development initiatives focused in each of our principal product lines as continued innovation and commercialization of new proprietary products and processes are essential elements of our long-term growth strategy. Our reputation as an innovator is exemplified by recent new product introductions such as the 2.8 and 3.3mm PopLock® Knotless Suture Anchors, for repair of unstable shoulders and for use in the emerging Endoscopic hip market; the Concept® Suture Passer, for use in rotator cuff repair; the Sequent™ Meniscal Repair System, which offers suture-locking implant cleats that will provide a knotless repair and allow the surgeon to complete an entire meniscal repair with one device without leaving the joint; CrossFT BC™ biocomposite suture anchor for rotator cuff repair; PRO6140 & PRO6240 pin drivers, to allow the use of one device during procedures such as total joint arthroplasty, trauma, sports medicine surgeries as well as small bone orthopedics; and the Altrus® Thermal Tissue Fusion System, which utilizes thermal energy to seal, cut, grasp, and dissect vessels up to 7mm in size utilizing

a closed feedback loop between the energy source and the single-use handpiece to precisely control the desired effect on tissue.



## Table of Contents

### Business Challenges

Significant volatility in the financial markets and foreign currency exchange rates and depressed economic conditions in both domestic and international markets have recently presented significant business challenges. While we are cautiously optimistic that the overall global economic environment is improving and experienced a return to revenue growth in 2010 and the first half of 2011, there can be no assurance that the improvement in the economic environment will be sustained. We will continue to monitor and manage the impact of the overall economic environment on the Company.

Over the past few years we successfully completed certain of our operational restructuring plans whereby we consolidated manufacturing and distribution centers as well as restructured certain of our administrative functions. We continue to restructure both operations and administrative functions as necessary throughout the organization. However, we cannot be certain such activities will be completed in the estimated time period or that planned cost savings will be achieved.

Our facilities are subject to periodic inspection by the United States Food and Drug Administration (“FDA”) and foreign regulatory agencies or notified bodies for, among other things, conformance to Quality System Regulation and Current Good Manufacturing Practice (“CGMP”) requirements and foreign or international standards. We are committed to the principles and strategies of systems-based quality management for improved CGMP compliance, operational performance and efficiencies through our Company-wide quality systems initiatives. However, there can be no assurance that our actions will ensure that we will not receive a warning letter or other regulatory action, which may include consent decrees or fines, that we will not make product recalls or that we will not experience temporary or extended periods during which we may not be able to sell products in foreign countries.

### Critical Accounting Policies

Preparation of our financial statements requires us to make estimates and assumptions which affect the reported amounts of assets, liabilities, revenues and expenses. Note 1 to the consolidated financial statements in our Annual Report on Form 10-K for the year-ended December 31, 2010 describes significant accounting policies used in preparation of the consolidated financial statements. The most significant areas involving management judgments and estimates are described below and are considered by management to be critical to understanding the financial condition and results of operations of CONMED Corporation. There have been no significant changes in our critical accounting estimates during the quarter ended June 30, 2011.

## Table of Contents

### Revenue Recognition

Revenue is recognized when title has been transferred to the customer which is at the time of shipment. The following policies apply to our major categories of revenue transactions:

- Sales to customers are evidenced by firm purchase orders. Title and the risks and rewards of ownership are transferred to the customer when product is shipped under our stated shipping terms. Payment by the customer is due under fixed payment terms.
- We place certain of our capital equipment with customers on a loaned basis in return for commitments to purchase related single-use products over time periods generally ranging from one to three years. In these circumstances, no revenue is recognized upon capital equipment shipment as the equipment is loaned and subject to return if certain minimum single-use purchases are not met. Revenue is recognized upon the sale and shipment of the related single-use products. The cost of the equipment is amortized over its estimated useful life.
- Product returns are only accepted at the discretion of the Company and in accordance with our “Returned Goods Policy”. Historically the level of product returns has not been significant. We accrue for sales returns, rebates and allowances based upon an analysis of historical customer returns and credits, rebates, discounts and current market conditions.
- Our terms of sale to customers generally do not include any obligations to perform future services. Limited warranties are provided for capital equipment sales and provisions for warranty are provided at the time of product sale based upon an analysis of historical data.
- Amounts billed to customers related to shipping and handling have been included in net sales. Shipping and handling costs are included in selling and administrative expense.
- We sell to a diversified base of customers around the world and, therefore, believe there is no material concentration of credit risk.
- We assess the risk of loss on accounts receivable and adjust the allowance for doubtful accounts based on this risk assessment. Historically, losses on accounts receivable have not been material. Management believes that the allowance for doubtful accounts of \$1.0 million at June 30, 2011 is adequate to provide for probable losses resulting from accounts receivable.

### Inventory Reserves

We maintain reserves for excess and obsolete inventory resulting from the inability to sell our products at prices in excess of current carrying costs. The markets in which we operate are highly competitive, with new products and surgical procedures introduced on an on-going basis. Such marketplace changes may result in our products becoming obsolete. We make estimates regarding the future recoverability of the costs of our products and record a provision for excess and obsolete inventories based on historical experience, expiration of sterilization dates and expected future trends. If actual product life cycles, product demand or acceptance of new product introductions are less favorable than projected by management, additional inventory write-downs may be required. We believe that our current inventory reserves are adequate.



## Table of Contents

### Goodwill and Intangible Assets

We have a history of growth through acquisitions. Assets and liabilities of acquired businesses are recorded at their estimated fair values as of the date of acquisition. Goodwill represents costs in excess of fair values assigned to the underlying net assets of acquired businesses. Other intangible assets primarily represent allocations of purchase price to identifiable intangible assets of acquired businesses. We have accumulated goodwill of \$294.9 million and other intangible assets of \$186.9 million as of June 30, 2011.

In accordance with Financial Accounting Standards Board (“FASB”) guidance, goodwill and intangible assets deemed to have indefinite lives are not amortized, but are subject to at least annual impairment testing. It is our policy to perform our annual impairment testing in the fourth quarter. The identification and measurement of goodwill impairment involves the estimation of the fair value of our reporting units. Estimates of fair value are based on the best information available as of the date of the assessment, which primarily incorporate management assumptions about expected future cash flows and other valuation techniques. Future cash flows may be affected by changes in industry or market conditions or the rate and extent to which anticipated synergies or cost savings are realized with newly acquired entities. We completed our goodwill impairment testing as of October 1, 2010 and determined that no impairment existed at that date. For our CONMED Electrosurgery, CONMED Endosurgery and CONMED Linvatec operating units, our impairment testing utilized CONMED Corporation’s EBIT multiple adjusted for a market-based control premium with the resultant fair values exceeding carrying values by 76% to 121%. Our CONMED Patient Care operating unit has the least excess of fair value over carrying value of our reporting units; we therefore utilized both a market-based approach and an income approach when performing impairment testing with the resultant fair value exceeding carrying value by 15%. The income approach contained certain key assumptions including that revenue would resume historical growth patterns in 2011 while including certain cost savings associated with the operational restructuring plan completed during 2010. We continue to monitor events and circumstances for triggering events which would more likely than not reduce the fair value of any of our reporting units and require us to perform impairment testing.

Intangible assets with a finite life are amortized over the estimated useful life of the asset and are evaluated each reporting period to determine whether events and circumstances warrant a revision to the remaining period of amortization. Intangible assets subject to amortization are reviewed for impairment whenever events or changes in circumstances indicate that its carrying amount may not be recoverable. The carrying amount of an intangible asset subject to amortization is not recoverable if it exceeds the sum of the undiscounted cash flows expected to result from the use of the asset. An impairment loss is recognized by reducing the carrying amount of the intangible asset to its current fair value.

Customer relationship assets arose principally as a result of the 1997 acquisition of Linvatec Corporation. These assets represent the acquisition date fair value of existing customer relationships based on the after-tax income expected to be derived during their estimated remaining useful life. The useful lives of these customer relationships were not and are not limited by contract or any economic, regulatory or other known factors. The estimated useful life of the Linvatec customer relationship assets was determined as of the date of acquisition as a result of a study of the observed pattern of historical revenue attrition during the 5 years immediately preceding the acquisition of Linvatec Corporation. This observed attrition pattern was then applied to the existing customer relationships to derive the future expected retirement of the customer relationships. This analysis indicated an annual attrition rate of 2.6%. Assuming an exponential attrition pattern, this equated to an average remaining useful life of approximately 38 years for the Linvatec customer relationship assets. Customer relationship intangible assets arising as a result of other business acquisitions are being amortized over a weighted average life of 17 years. The weighted average life for customer relationship assets in aggregate is 34 years.



Table of Contents

We evaluate the remaining useful life of our customer relationship intangible assets each reporting period in order to determine whether events and circumstances warrant a revision to the remaining period of amortization. In order to further evaluate the remaining useful life of our customer relationship intangible assets, we perform an analysis and assessment of actual customer attrition and activity as events and circumstances warrant. This assessment includes a comparison of customer activity since the acquisition date and review of customer attrition rates. In the event that our analysis of actual customer attrition rates indicates a level of attrition that is in excess of that which was originally contemplated, we would change the estimated useful life of the related customer relationship asset with the remaining carrying amount amortized prospectively over the revised remaining useful life.

We test our customer relationship assets for recoverability whenever events or changes in circumstances indicate that the carrying amount may not be recoverable. Factors specific to our customer relationship assets which might lead to an impairment charge include a significant increase in the annual customer attrition rate or otherwise significant loss of customers, significant decreases in sales or current-period operating income or cash flow losses or a projection or forecast of losses. We do not believe that there have been events or changes in circumstances which would indicate the carrying amount of our customer relationship assets might not be recoverable.

Pension Plan

We sponsor a defined benefit pension plan (“the plan”) covering substantially all our United States-based employees. The plan was frozen effective May 14, 2009. Major assumptions used in accounting for the plan include the discount rate, expected return on plan assets, rate of increase in employee compensation levels and expected mortality. Assumptions are determined based on Company data and appropriate market indicators, and are evaluated annually as of the plan’s measurement date. A change in any of these assumptions would have an effect on net periodic pension costs reported in the consolidated financial statements.

The weighted-average discount rate used to measure pension liabilities and costs is set by reference to the Citigroup Pension Liability Index. However, this index gives only an indication of the appropriate discount rate because the cash flows of the bonds comprising the index do not precisely match the projected benefit payment stream of the plan. For this reason, we also consider the individual characteristics of the plan, such as projected cash flow patterns and payment durations, when setting the discount rate. The rates used in determining 2010 and 2011 pension expense are 5.86% and 5.41%, respectively.

Table of Contents

We have used an expected rate of return on pension plan assets of 8.0% for purposes of determining the net periodic pension benefit cost. In determining the expected return on pension plan assets, we consider the relative weighting of plan assets, the historical performance of total plan assets and individual asset classes and economic and other indicators of future performance. In addition, we consult with financial and investment management professionals in developing appropriate targeted rates of return.

For the three and six months ending June 30, 2011 we recorded pension expense of \$0.0 million and \$0.5 million, respectively. Pension expense in 2011 is expected to be \$1.0 million compared to expense of \$0.9 million in 2010. In addition, we will be required to contribute approximately \$2.1 million to the pension plan for the 2011 plan year.

See Note 9 to the Consolidated Condensed Financial Statements for further discussion.

### Stock Based Compensation

All share-based payments to employees, including grants of employee stock options, restricted stock units, performance share units and stock appreciation rights are recognized in the financial statements based at their fair values. Compensation expense is generally recognized using a straight-line method over the vesting period. Compensation expense for performance share units is recognized using the graded vesting method.

### Income Taxes

The recorded future tax benefit arising from deductible temporary differences and tax carryforwards is approximately \$38.3 million at June 30, 2011. Management believes that earnings during the periods when the temporary differences become deductible will be sufficient to realize the related future income tax benefits.

We operate in multiple taxing jurisdictions, both within and outside the United States. We face audits from these various tax authorities regarding the amount of taxes due. Such audits can involve complex issues and may require an extended period of time to resolve. The Internal Revenue Service ("IRS") has completed examinations of our United States federal income tax returns through 2009. Tax years subsequent to 2009 are subject to future examination.

### Results of Operations

The following table presents, as a percentage of net sales, certain categories included in our consolidated statements of income for the periods indicated:

|                                      | Three months ended<br>June 30, |         | Six months ended<br>June 30, |         |
|--------------------------------------|--------------------------------|---------|------------------------------|---------|
|                                      | 2010                           | 2011    | 2010                         | 2011    |
| Net sales                            | 100.0                          | % 100.0 | % 100.0                      | % 100.0 |
| Cost of sales                        | 48.3                           | 50.1    | 48.1                         | 49.0    |
| Gross profit                         | 51.7                           | 49.9    | 51.9                         | 51.0    |
| Selling and administrative expense   | 39.5                           | 37.0    | 39.7                         | 37.6    |
| Research and development expense     | 3.6                            | 3.7     | 4.0                          | 4.0     |
| Other expense                        | 0.5                            | 0.1     | 0.3                          | 0.2     |
| Income from operations               | 8.1                            | 9.1     | 7.9                          | 9.2     |
| Loss on early extinguishment of debt | 0.0                            | 0.0     | 0.0                          | 0.0     |

Edgar Filing: CONMED CORP - Form 10-Q

|                               |     |       |       |       |
|-------------------------------|-----|-------|-------|-------|
| Amortization of bond discount | 0.6 | 0.6   | 0.6   | 0.6   |
| Interest expense              | 1.0 | 0.9   | 1.0   | 1.0   |
| Income before income taxes    | 6.5 | 7.6   | 6.3   | 7.6   |
| Provision for income taxes    | 2.5 | 2.8   | 2.2   | 2.9   |
| Net income                    | 4.0 | % 4.8 | % 4.1 | % 4.7 |



Table of Contents

Three months ended June 30, 2011 compared to three months ended June 30, 2010

Sales for the quarterly period ended June 30, 2011 were \$183.2 million, an increase of \$2.1 million (1.2%) compared to sales of \$181.1 million in the comparable 2010 period with increases across all product lines except Arthroscopy and Patient Care. In local currency, excluding the effects of the hedging program, sales decreased 0.3%. Sales of capital equipment decreased \$2.8 million (-6.5%) to \$40.1 million in the second quarter of 2011 from \$42.9 million in the same period a year ago; sales of single-use products increased \$4.9 million (3.5%) to \$143.1 million in the second quarter of 2011 from \$138.2 million in the same period a year ago. On a local currency basis, excluding the effects of our hedging program, sales of capital equipment decreased 8.0% while single-use products increased 2.0%. We believe the overall decline in capital sales is driven by capital purchasing constraints in hospitals due to the depressed economic conditions.

Cost of sales increased to \$91.8 million in the quarterly period ended June 30, 2011 as compared to \$87.4 million in the same period a year ago on overall increases in sales volumes as described above. Gross profit margins decreased 1.8 percentage points to 49.9% in the quarterly period ended June 30, 2011 as compared to 51.7% in the same period a year ago. The decrease in gross profit margins of 1.8 percentage points is primarily a result of unfavorable manufacturing production variances related to absorbing fixed costs into inventory that arose in the fourth quarter of 2010 when manufacturing production was conducted at lower levels in order to reduce inventory. In periods where we reduce our inventory levels to manage inventory carrying costs, the inventory we produce is carried at a higher unit cost due to absorbing those fixed costs over lower production levels. As a result, when that inventory is sold in subsequent periods, the gross profit margin on those sales is lower. We experienced this reduced gross profit margin in the second quarter of 2011.

Selling and administrative expense decreased to \$67.9 million in the quarterly period ended June 30, 2011 as compared to \$71.5 million in the same period a year ago as our restructuring and cost control efforts more than offset the approximately \$2.6 million unfavorable impact on expenses of foreign currency exchange rates (when compared to the foreign currency exchange rates in the same period a year ago). Selling and administrative expense as a percentage of net sales decreased to 37.0% in the quarterly period ended June 30, 2011 as compared to 39.5% in the same period a year ago as selling and administrative expense declined 5.1% while sales increased 1.2%.

Table of Contents

Research and development expense totaled \$6.8 million in the quarterly period ended June 30, 2011 as compared to \$6.4 million in the same period a year ago. As a percentage of net sales, research and development expense remained relatively flat at 3.7% in the quarterly period ending June 30, 2011 compared to 3.6% in the same period a year ago.

As discussed in Note 10 to the Consolidated Condensed Financial Statements, other expense in the quarterly period ended June 30, 2011 consisted of a \$0.1 million charge related to the consolidation of administrative functions in our Utica, NY facility. Other expense in the quarterly period ended June 30, 2010 consisted of a \$1.0 million charge related to the consolidation of administrative functions in our CONMED Linvatec division.

During the quarterly period ended June 30, 2010, we repurchased and retired \$3.0 million of our 2.50% convertible senior subordinated notes (the "Notes") for \$2.9 million and recorded a loss on the early extinguishment of debt of \$0.1 million. See additional discussion under Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations—Liquidity and Capital Resources and Note 4 to the Consolidated Condensed Financial Statements.

Amortization of debt discount was \$1.1 million in the quarterly period ended June 30, 2011 and in the same period a year ago.

Interest expense in the quarterly period ended June 30, 2011 was \$1.7 million compared to \$1.8 million in the same period a year ago. The interest expense decreased due to lower weighted average borrowings outstanding in the quarterly period ended June 30, 2011 as compared to the same period a year ago offset by higher weighted average interest rates. The weighted average interest rates on our borrowings (inclusive of the finance charge on our accounts receivable sale facility for the quarterly period ended June 30, 2010) increased to 3.74% in the quarterly period ended June 30, 2011 as compared to 3.17% in the same period a year ago.

A provision for income taxes has been recorded at an effective tax rate of 37.5% for the quarterly period ended June 30, 2011 compared to the 38.5% effective tax rate recorded in the same period a year ago. The effective tax rate for the quarterly period ended June 30, 2011 is lower than that recorded in the same period a year ago as a result of the 2011 tax rate including the benefit of the research and development tax credit which was not included in 2010. A reconciliation of the United States statutory income tax rate to our effective tax rate is included in our Annual Report on Form 10-K for the year-ended December 31, 2010, Note 6 to the Consolidated Financial Statements.

Six months ended June 30, 2011 compared to six months ended June 30, 2010

Sales for the six months ended June 30, 2011 were \$366.7 million, an increase of \$9.2 million (2.6%) compared to sales of \$357.5 million in the comparable 2010 period with increases across all product lines except Arthroscopy and Patient Care. In local currency, excluding the effects of the hedging program, sales increased 1.9%. Sales of capital equipment increased \$1.0 million (1.2%) to \$82.0 million in the six months ended June 30, 2011 from \$81.0 million in the same period a year ago; sales of single-use products increased \$8.2 million (3.0%) to \$284.7 million in the six months ended June 30, 2011 from \$276.5 million in the same period a year ago. On a local currency basis, excluding the effects of our hedging program, sales of capital equipment increased 0.5% and single-use products increased 2.3%.

## Table of Contents

Cost of sales increased to \$179.5 million in the six months ended June 30, 2011 as compared to \$172.0 million in the same period a year ago on overall increases in sales volumes as described above. Gross profit margins decreased 0.9 percentage points to 51.0% in the six months ended June 30, 2011 as compared to 51.9% in the same period a year ago. The decrease in gross profit margins of 0.9 percentage points is primarily a result of unfavorable manufacturing production variances related to absorbing fixed costs into inventory that arose in the fourth quarter of 2010 as further described above.

Selling and administrative expense decreased to \$137.9 million in the six months ended June 30, 2011 as compared to \$142.0 million in the same period a year ago as our restructuring and cost control efforts more than offset the approximately \$3.3 million unfavorable impact on expenses of foreign currency exchange rates (when compared to the foreign currency exchange rates in the same period a year ago). Selling and administrative expense as a percentage of net sales decreased to 37.6% in the six months ended June 30, 2011 as compared to 39.7% in the same period a year ago as selling and administrative expense declined 2.9% while sales increased 2.6%.

Research and development expense totaled \$14.5 million in the six months ended June 30, 2011 as compared to \$14.1 million in the same period a year ago. As a percentage of net sales, research and development expense remained flat at 4.0% for the six months ended June 30, 2011 compared to the same period a year ago.

As discussed in Note 10 to the Consolidated Condensed Financial Statements, other expense in the six months ended June 30, 2011 consisted of a \$0.8 million charge related to the consolidation of administrative functions in our Utica, NY facility. Other expense in the six months ended June 30, 2010 consisted of a \$1.0 million charge related to the consolidation of administrative functions in our CONMED Linvatec division.

During the quarter ended June 30, 2010, we repurchased and retired \$3.0 million of our 2.50% convertible senior subordinated notes (the “Notes”) for \$2.9 million and recorded a loss on the early extinguishment of debt of \$0.1 million. See additional discussion under Item 2. Management’s Discussion and Analysis of Financial Condition and Results of Operations—Liquidity and Capital Resources and Note 4 to the Consolidated Condensed Financial Statements.

Amortization of debt discount was \$2.2 million in the six months ended June 30, 2011 compared to \$2.1 million in the same period a year ago.

Interest expense remained flat at \$3.5 million in the six months ended June 30, 2011 and in the same period a year ago. Interest expense remained flat due to lower weighted average borrowings outstanding in the six month period ended June 30, 2011 as compared to the same period a year ago offset by higher weighted average interest rates. The weighted average interest rate on our borrowings (inclusive of the finance charge on our accounts receivable sale facility for the six month period ended June 30, 2010) increased to 3.67% in the six months ended June 30, 2011 as compared to 3.14% in the same period a year ago.

A provision for income taxes has been recorded at an effective tax rate of 37.4% for the six months ended June 30, 2011 compared to the 35.4% effective tax rate recorded in the same period a year ago. The effective tax rate for the six months ended June 30, 2011 is higher than that recorded in the same period a year ago as 2010 included the settlement of our 2008 IRS examination, and a resulting decrease to our reserves and income tax expense. A reconciliation of the United States statutory income tax rate to our effective tax rate is included in our Annual Report on Form 10-K for the year-ended December 31, 2010, Note 6 to the Consolidated Financial Statements.



Table of Contents

## Operating Segment Results:

Segment information is prepared on the same basis that we review financial information for operational decision-making purposes. CONMED conducts its business through five principal operating segments, CONMED Endoscopic Technologies, CONMED Endosurgery, CONMED Electrosurgery, CONMED Linvatec and CONMED Patient Care. We believe each of our segments are similar in the nature of their products, production processes, customer base, distribution methods and regulatory environment. Our CONMED Endosurgery, CONMED Electrosurgery and CONMED Linvatec operating segments also have similar economic characteristics and therefore qualify for aggregation. Our CONMED Patient Care and CONMED Endoscopic Technologies operating units do not qualify for aggregation since their economic characteristics do not meet the criteria for aggregation as a result of the lower overall operating margin in these segments.

The following tables summarize the Company's results of operations by segment for the three and six month periods ended June 30, 2010 and 2011.

## CONMED Linvatec, CONMED Electrosurgery and CONMED Endosurgery

|                           | Three months ended<br>June 30, |            | Six months ended<br>June 30, |            |
|---------------------------|--------------------------------|------------|------------------------------|------------|
|                           | 2010                           | 2011       | 2010                         | 2011       |
| Net sales                 | \$ 151,698                     | \$ 154,087 | \$ 299,104                   | \$ 309,012 |
| Income from<br>operations | 21,271                         | 20,529     | 38,527                       | 44,804     |
| Operating Margin          | 14.0                           | % 13.3     | % 12.9                       | % 14.5     |

Product offerings include capital equipment such as electrosurgical generators, video systems, small bone, large bone and specialty hand pieces, and arthroscopic instrumentation for use in orthopedic surgery. Single-use product offerings include a complete line of endo-mechanical instrumentation for minimally invasive laparoscopic procedures, electrosurgical single-use products including pencils and ground pads and orthopedic single-use products such as burs, blades, and implants.

- Arthroscopy sales decreased \$4.3 million (-5.7%) in the quarter ended June 30, 2011 to \$70.6 million from \$74.9 million in the same period a year ago mainly due to lower sales of our video imaging products for arthroscopy and general surgery. In local currency, excluding the effects of the hedging program, sales decreased 7.5%. Sales of capital equipment decreased \$6.9 million (-33.7%) to \$13.6 million in the second quarter of 2011 from \$20.5 million in the same period a year ago; sales of single-use products increased \$2.6 million (4.8%) to \$57.0 million in the second quarter of 2011 from \$54.4 million in the same period a year ago. On a local currency basis, excluding the effects of the hedging program, sales of capital equipment decreased 34.3% while single-use products increased 2.6%. Arthroscopy sales decreased \$1.1 million (-0.7%) in the six months ended June 30, 2011 to \$146.0 million from \$147.1 million in the same period a year ago mainly due to lower sales of our video imaging products for arthroscopy and general surgery. In local currency, excluding the effects of the hedging program, sales decreased 1.6%. Sales of capital equipment decreased \$6.9 million (-18.3%) to \$30.9 million in the six months ended June 30, 2011 from \$37.8 million in the same period a year ago; sales of single-use products increased \$5.8 million (5.3%) to \$115.1 million in the six months ended June 30, 2011 from \$109.3 million in the same period a year ago. On a

local currency basis, excluding the effects of our hedging program, sales of capital equipment decreased 18.4% while single-use products increased 4.2%. We believe the overall decline in capital sales is driven by capital purchasing constraints in hospitals due to the depressed economic conditions.

Table of Contents

- Powered surgical instrument sales increased \$2.6 million (7.3%) in the quarterly period ended June 30, 2011 to \$38.3 million from \$35.7 million in the comparable 2010 period mainly due to increases in large bone handpiece products and our burs and blades. In local currency, excluding the effects of the hedging program, sales increased 4.8%. Sales of capital equipment increased \$1.9 million (11.4%) to \$18.5 million in the second quarter of 2011 from \$16.6 million in the same period a year ago; sales of single-use products increased \$0.7 million (3.7%) in the second quarter of 2011 to \$19.8 million from \$19.1 million in the same period a year ago. On a local currency basis, excluding the effects of the hedging program, sales of capital equipment increased 9.1% while single-use products increased 1.1%. Powered surgical instrument sales increased \$5.7 million (8.1%) in the six months ended June 30, 2011 to \$76.4 million from \$70.7 million in the comparable 2010 period mainly due to increases in our large bone handpiece products and burs and blades. In local currency, excluding the effects of the hedging program, sales increased 6.9%. Sales of capital equipment increased \$4.8 million (15.3%) to \$36.2 million in the six months ended June 30, 2011 from \$31.4 million in the same period a year ago; sales of single-use products increased \$0.9 million (2.3%) to \$40.2 million in the six months ended June 30, 2011 from \$39.3 million in the same period a year ago. On a local currency basis, excluding the effects of the hedging program, sales of capital equipment increased 14.1% while single-use products increased 1.0%.
- Electrosurgery sales increased \$2.1 million (8.8%) in the quarterly period ended June 30, 2011 to \$26.1 million from \$24.0 million in the comparable 2010 period mainly due to increased sales of generators and our new smoke evacuation accessories. In local currency, excluding the effects of the hedging program, sales increased 7.9%. Sales of capital equipment increased \$2.2 million (37.9%) to \$8.0 million in the second quarter of 2011 from \$5.8 million in the same period a year ago; sales of single-use products decreased \$0.1 million (-0.5%) to \$18.1 million in the second quarter of 2011 from \$18.2 million in the same period a year ago. On a local currency basis, excluding the effects of our hedging program, sales of capital equipment increased 36.2% while single-use products decreased 1.1%. Electrosurgery sales increased \$2.6 million (5.5%) in the six months ended June 30, 2011 to \$49.7 million from \$47.1 million in the comparable 2010 period mainly due to increased sales of generators and our new smoke evacuation accessories. In local currency, excluding the effects of the hedging program, sales increased 4.9%. Sales of capital equipment increased \$3.1 million (26.3%) to \$14.9 million in the six months ended June 30, 2011 from \$11.8 million in the same period a year ago; sales of single-use products decreased \$0.5 million (-1.4%) to \$34.8 million in the six months ended June 30, 2011 from \$35.3 million in the same period a year ago. On a local currency basis, excluding the effects of the hedging program, sales of capital equipment increased 24.6% while single-use products decreased 1.7%.

Table of Contents

- Endosurgery sales increased \$2.0 million (11.7%) in the quarterly period ended June 30, 2011 to \$19.1 million compared to \$17.1 million in the same period a year ago mainly due to increased sales of our VCARE and suction/irrigation products. In local currency, excluding the effects of the hedging program, sales increased 10.6%. Endosurgery sales increased \$2.8 million (8.2%) in the six months ended June 30, 2011 to \$37.0 million from \$34.2 million in the comparable 2010 period mainly due to increased sales of our VCARE and suction/irrigation products. In local currency, excluding the effects of the hedging program, sales increased 7.9%.
- Operating margins as a percentage of net sales decreased 0.7 percentage points to 13.3% in the quarterly period ended June 30, 2011 compared to 14.0% in 2010 principally as a result of lower gross margins (1.0 percentage points) is primarily a result of unfavorable manufacturing production variances related to absorbing fixed costs into inventory that arose in the fourth quarter of 2010 as further described above offset by 2010 including charges related to the restructuring of administrative functions in our CONMED Linvatec division (0.6 percentage points).
- Operating margins as a percentage of net sales increased 1.6 percentage points to 14.5% in the six months ended June 30, 2011 compared to 12.9% in 2010 principally as a result of lower spending on selling and administrative expenses (1.5 percentage points) and 2010 including charges related to the restructuring of administrative functions in our CONMED Linvatec division (0.3 percentage points).

## CONMED Patient Care

|                                  | Three months ended<br>June 30, |          | Six months ended<br>June 30, |          |
|----------------------------------|--------------------------------|----------|------------------------------|----------|
|                                  | 2010                           | 2011     | 2010                         | 2011     |
| Net sales                        | \$17,461                       | \$16,636 | \$34,620                     | \$33,260 |
| Income (loss) from<br>operations | 1,200                          | (999 )   | 1,546                        | (1,735 ) |
| Operating Margin                 | 6.9 %                          | (6.0 %)  | 4.5 %                        | (5.2 %)  |

Product offerings include a line of vital signs and cardiac monitoring products including pulse oximetry equipment and sensors, ECG electrodes and cables, cardiac defibrillation and pacing pads and blood pressure cuffs. We also offer a complete line of single-use suction instruments and tubing for use in the operating room, as well as a line of IV products.

- Patient Care sales decreased \$0.9 million (-5.1%) in the quarter ended June 30, 2011 to \$16.6 million from \$17.5 million in the same period a year ago mainly due to decreased sales of I.V. devices and ECG electrodes. In local currency, excluding the effects of the hedging program, sales decreased 4.6%. Patient Care sales decreased \$1.5 million (-4.3%) in the six months ended June 30, 2011 to \$33.2 million from \$34.7 million in the same period a year ago as a result of decreased sales of I.V. devices and ECG electrodes. In local currency, excluding the effects of the hedging program, sales decreased 3.8%.



Table of Contents

- Operating margins as a percentage of net sales decreased 12.9 percentage points to (-6.0%) for the quarter ended June 30, 2011 compared to 6.9% in 2010 while operating margins decreased 9.7 percentage points to (-5.2%) for the six months ended June 30, 2011 compared to 4.5% in the same period a year ago. The decrease in operating margins of 12.9 percentage points and 9.7 percentage points, in the quarter and six months ended June 30, 2011, respectively was driven by \$0.1 million \$0.6 million, respectively, in administrative restructuring charges (0.6 and 1.8 percentage points, respectively) and lower gross margins as a result of lower sales volumes (13.9 and 8.8 percentage points, respectively), offset by lower administrative expenses (1.6 and 0.9 percentage points, respectively).

## CONMED Endoscopic Technologies

|                                  | Three months ended<br>June 30, |          | Six months ended<br>June 30, |          |
|----------------------------------|--------------------------------|----------|------------------------------|----------|
|                                  | 2010                           | 2011     | 2010                         | 2011     |
| Net sales                        | \$11,927                       | \$12,513 | \$23,727                     | \$24,414 |
| Income (loss) from<br>operations | (237 )                         | 355      | (38 )                        | 165      |
| Operating Margin                 | (2.0 %)                        | 2.8 %    | (0.2 %)                      | 0.7 %    |

Product offerings include a comprehensive line of single-use minimally invasive endoscopic diagnostic and therapeutic instruments used in procedures which require examination of the digestive tract.

- Endoscopic Technologies sales increased \$0.6 million (5.0%) in the quarter ended June 30, 2011 to \$12.5 million compared to \$11.9 million in the same period a year ago due to increased sales of our bite blocks and cleaning brushes. In local currency, excluding the effects of the hedging program, sales increased 3.4%. Endoscopic Technologies sales increased \$0.7 million (3.0%) in the six months ended June 30, 2011 to \$24.4 million from \$23.7 million in the same period a year ago due to increased sales of our bite blocks, cleaning brushes and polypectomy products. In local currency, excluding the effects of the hedging program, sales increased 1.7%.
- Operating margins as a percentage of net sales increased 4.8 percentage points to 2.8% in the quarterly period ending June 30, 2011 compared to -2.0% in 2010. The increase in operating margins in the quarter ending June 30, 2011 is principally due to overall lower selling and administrative expenses (5.9 percentage points) offset by increased spending in research and development (0.8 percentage points) and lower gross margins (0.3 percentage points) due to product mix. Operating margins increased 0.9 percentage points to 0.7% in the six months ended June 30, 2011 compared to -0.2% in the same period a year ago. The increase in operating margins in the six months ending June 30, 2011 is principally due to overall lower selling and administrative expenses (4.6 percentage points) offset by increased spending in research and development (1.2 percentage points), \$0.2 million in administrative restructuring charges during the first quarter of 2011 (0.8 percentage points) and lower gross margins (1.7 percentage points) primarily a result of unfavorable manufacturing production variances related to absorbing fixed costs into inventory that arose in the fourth quarter of 2010 as further described above.

Table of Contents

Liquidity and Capital Resources

Our liquidity needs arise primarily from capital investments, working capital requirements and payments on indebtedness under the senior credit agreement. We have historically met these liquidity requirements with funds generated from operations, including sales of accounts receivable and borrowings under our revolving credit facility. In addition, we have historically used term borrowings, including borrowings under the senior credit agreement and borrowings under separate loan facilities, in the case of real property purchases, to finance our acquisitions. We also have the ability to raise funds through the sale of stock or we may issue debt through a private placement or public offering.

Cash provided by operations

Our net working capital position was \$157.8 million at June 30, 2011. Net cash provided by operating activities was \$40.2 million in the six months ended June 30, 2011 and \$5.5 million in the same period a year ago.

The increase in cash provided by operating activities is primarily the result of a new accounting pronouncement effective January 1, 2010, which required accounts receivable sold under our accounts receivable sale agreement to be recorded as additional borrowings rather than as a reduction in accounts receivable. Accordingly, in the six months ended June 30, 2010, \$29.0 million in cash collections related to accounts receivable sold prior to January 1, 2010 have been presented as a reduction in cash from operations while net sales of additional accounts receivable generated subsequent to January 1, 2010 have been reflected as an increase in cash flows from financing activities. We terminated this agreement on November 4, 2010 at which time we repaid the outstanding balance in full.

Investing cash flows

Net cash used in investing activities in the quarterly period ended June 30, 2011 consisted primarily of capital expenditures. Capital expenditures were \$7.2 million and \$8.6 million for the six month periods ended June 30, 2010 and 2011, respectively and are expected to approximate \$20.0 million in 2011.

Financing cash flows

Net cash used in financing activities during 2011 consisted of the following: \$5.5 million in proceeds from the issuance of common stock under our equity compensation plans and employee stock purchase plan, \$22.0 million in repayments on our revolver under our senior credit agreement, \$0.7 million in repayments of term borrowings under our senior credit agreement, and \$0.4 million in repayments of our mortgage notes.

## Table of Contents

On November 30, 2010, we entered into the First Amendment to our Amended and Restated Credit Agreement (the "senior credit agreement") providing for an expanded revolving credit facility expiring on November 30, 2015. The senior credit agreement continues to consist of a \$135.0 million term loan of which \$54.3 million was outstanding as of June 30, 2011. There were no borrowings outstanding on the \$250.0 million revolving credit facility as of June 30, 2011. Our available borrowings on the revolving credit facility at June 30, 2011 were \$240.2 million with approximately \$9.8 million of the facility set aside for outstanding letters of credit.

Borrowings outstanding on the revolving credit facility are due and payable on November 30, 2015. The scheduled principal payments on the term loan portion of the senior credit agreement are \$0.7 million for the remainder of 2011, \$0.3 million due on March 31, 2012, \$31.7 million due June 30, 2012 and the remaining \$21.5 million due on September 30, 2012. We may also be required, under certain circumstances, to make additional principal payments based on excess cash flow as defined in the senior credit agreement. Interest rates on the term loan portion of the senior credit agreement are at LIBOR plus 1.50% (1.69% at June 30, 2011) or an alternative base rate; interest rates on the revolving credit facility portion of the senior credit agreement are at LIBOR plus 1.75% or an alternative base rate. For those borrowings where the Company elects to use the alternative base rate, the base rate will be the greater of the Prime Rate or the Federal Funds Rate in effect on such date plus 0.50%, plus a margin of 0.50% for term loan borrowings or 0.25% for borrowings under the revolving credit facility.

The senior credit agreement is collateralized by substantially all of our property and assets. The senior credit agreement contains covenants and restrictions which, among other things, require the maintenance of certain financial ratios, and restrict dividend payments and the incurrence of certain indebtedness and other activities, including acquisitions and dispositions. We were in full compliance with these covenants and restrictions as of June 30, 2011. We are also required, under certain circumstances, to make mandatory prepayments from net cash proceeds from any issuance of equity and asset sales.

We have a mortgage note outstanding in connection with the property and facilities utilized by our CONMED Linvatec subsidiary bearing interest at 8.25% per annum with semiannual payments of principal and interest through June 2019. The principal balance outstanding on the mortgage note aggregated \$10.0 million at June 30, 2011. The mortgage note is collateralized by the CONMED Linvatec property and facilities.

We have outstanding \$112.1 million in 2.50% convertible senior subordinated notes due 2024 ("the Notes"). During the quarterly period ended June 30, 2010, we repurchased and retired \$3.0 million of our 2.50% convertible senior subordinated notes (the "Notes") for \$2.9 million and recorded a loss on the early extinguishment of debt of \$0.1 million. The Notes represent subordinated unsecured obligations and are convertible under certain circumstances, as defined in the bond indenture, into a combination of cash and CONMED common stock. Upon conversion, the holder of each Note will receive the conversion value of the Note payable in cash up to the principal amount of the Note and CONMED common stock for the Note's conversion value in excess of such principal amount. Amounts in excess of the principal amount are at an initial conversion rate, subject to adjustment, of 26.1849 shares per \$1,000 principal amount of the Note (which represents an initial conversion price of \$38.19 per share). As of June 30, 2011, there was no value assigned to the conversion feature because the Company's share price was below the conversion price. The Notes mature on November 15, 2024 and are not redeemable by us prior to November 15, 2011. Holders of the Notes have the right to put to us some or all of the Notes for repurchase on November 15, 2011, 2014 and 2019 and, provided the terms of the indenture are satisfied, we will be required to repurchase those Notes, and therefore we have classified the Notes as a current liability. If the Notes are put to us on November 15, 2011, we plan to utilize our \$250.0 million revolving credit facility for payment of the Notes.



Table of Contents

The Notes contain two embedded derivatives. The embedded derivatives are recorded at fair value in other long-term liabilities and changes in their value are recorded through the consolidated statements of operations. The embedded derivatives have a nominal value, and it is our belief that any change in their fair value would not have a material adverse effect on our business, financial condition, results of operations, or cash flows.

Our Board of Directors has authorized a share repurchase program under which we may repurchase up to \$100.0 million of our common stock, although no more than \$50.0 million in any calendar year. We did not repurchase any shares during the first six months of 2011. The remaining availability under the Board of Directors' authorization for stock repurchases is \$23.8 million. In the past, we have financed the repurchases and may finance additional repurchases through operating cash flow and from available borrowings under our revolving credit facility.

Management believes that cash flow from operations, including cash and cash equivalents on hand and available borrowing capacity under our senior credit agreement will be adequate to meet our anticipated operating working capital requirements, debt service, funding of capital expenditures and common stock repurchases in the foreseeable future. See "Item 1. Business – Forward Looking Statements."

#### Restructuring

During 2010 and 2011, we continued our operational restructuring plan which includes the transfer of additional production lines from Utica, New York, Largo, Florida and Goleta, California to our manufacturing facility in Chihuahua, Mexico. We incurred \$1.0 million and \$1.7 million, respectively, in costs associated with the restructuring during the three and six months ended June 30, 2011. These costs were charged to cost of goods sold and include severance and other charges associated with the transfer of production to Mexico.

During 2011, we consolidated certain administrative functions in our Utica, New York facility and incurred \$0.1 million and \$0.8 million, respectively, in related costs consisting principally of severance charges in the three and six months ended June 30, 2011.

We will continue to restructure both our operations and administrative functions as necessary throughout the organization. As the restructuring plan progresses, we will incur additional charges, including employee termination costs and other exit costs. Based on criteria included in FASB guidance, no material accruals have been recorded at this time. We estimate restructuring costs will approximate \$4.0 million to \$5.0 million in 2011 and will be recorded to cost of goods sold and other expense.

See Note 14 to the Consolidated Condensed Financial Statements for further discussions regarding restructuring.

Table of Contents

New accounting pronouncements

See Note 13 to the Consolidated Condensed Financial Statements for a discussion of new accounting pronouncements.

Item 3. Quantitative and Qualitative Disclosures About Market Risk

There have been no significant changes in our primary market risk exposures or in how these exposures are managed during the three and six month periods ended June 30, 2011. Reference is made to Item 7A. of our Annual Report on Form 10-K for the year-ended December 31, 2010 for a description of Qualitative and Quantitative Disclosures About Market Risk.

Item 4. Controls and Procedures

An evaluation of the effectiveness of the design and operation of the Company's disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934, as amended ("Exchange Act")) was carried out under the supervision and with the participation of the Company's management, including the President and Chief Executive Officer and the Vice President-Finance and Chief Financial Officer ("the Certifying Officers") as of June 30, 2011. Based on that evaluation, the Certifying Officers concluded that the Company's disclosure controls and procedures are effective. There have been no changes in the Company's internal control over financial reporting (as such term is defined in Rules 13a-15(f) and 15d-15(f) under the Exchange Act) during the quarter ended June 30, 2011 that have materially affected, or are reasonably likely to materially affect, the Company's internal control over financial reporting.

PART II OTHER INFORMATION

Item 1. Legal Proceedings

Reference is made to Item 3 of the Company's Annual Report on Form 10-K for the year-ended December 31, 2010 and to Note 12 of the Notes to Consolidated Condensed Financial Statements included in Part I of this Report for a description of certain legal matters.

Table of Contents

Exhibit No. Description of Exhibit

- |      |   |
|------|---|
| 31.1 | Certification of Joseph J. Corasanti pursuant to Rule 13a-14(a) or Rule 15d-14(a), of the Securities Exchange Act, as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.  |
| 31.2 | Certification of Robert D. Shallish, Jr. pursuant to Rule 13a-14(a) or Rule 15d-14(a), of the Securities Exchange Act, as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.  |
| 32.1 | Certification of Joseph J. Corasanti and Robert D. Shallish, Jr. pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.  |
| 101  | The following materials from CONMED Corporation's Quarterly Report on Form 10-Q for the quarter ended June 30, 2011 formatted in XBRL (Extensible Business Reporting Language): (i) Consolidated Condensed Statements of Operations for the quarters and six months ended June 30, 2011 and 2010, (ii) the Consolidated Condensed Balance Sheets at June 30, 2011 and December 31, 2010, (iii) Consolidated Condensed Statements of Cash Flows for the six months ended June 30, 2011 and 2010, and (iv) Notes to Consolidated Condensed Financial Statements for the six months ended June 30, 2011. In accordance with Rule 406T of Regulation S-T, the XBRL related information in Exhibit 101 to this Quarterly Report on Form 10-Q shall not be deemed to be "filed" for purposes of Section 18 of the Exchange Act, or otherwise subject to the liability of that section, and shall not be part of any registration statement or other document filed under the Securities Act or the Exchange Act, except as shall be expressly set forth by specific reference in such filing. |

Table of Contents

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.

CONMED CORPORATION  
(Registrant)

Date: July 29, 2011

/s/ Robert D. Shallish, Jr.  
Robert D. Shallish, Jr.  
Vice President – Finance and  
Chief Financial Officer



Table of Contents

## Exhibit Index

| Exhibit |   | Sequential Page<br>Number |
|---------|---|---------------------------|
| 31.1    | Certification of Joseph J. Corasanti pursuant to Rule 13a-14(a) or Rule 15d-14(a) of the Securities Exchange Act, as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.   | E-1                       |
| 31.2    | Certification of Robert D. Shallish, Jr. pursuant to Rule 13a-14(a) or Rule 15d-14(a) of the Securities Exchange Act, as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.   | E-2                       |
| 32.1    | Certification of Joseph J. Corasanti and Robert D. Shallish, Jr. pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.  | E-3                       |
| 101     | The following materials from CONMED Corporation's Quarterly Report on Form 10-Q for the quarter ended June 30, 2011 formatted in XBRL (Extensible Business Reporting Language): (i) Consolidated Condensed Statements of Operations for the quarters and six months ended June 30, 2011 and 2010, (ii) Consolidated Condensed Balance Sheets at June 30, 2011 and December 31, 2010, (iii) Consolidated Condensed Statements of Cash Flows for the six months ended June 30, 2011 and 2010, and (iv) Notes to the Consolidated Condensed Financial Statements for the six months ended June 30, 2011. In accordance with Rule 406T of Regulation S-T, the XBRL related information in Exhibit 101 to this Quarterly Report on Form 10-Q shall not be deemed to be "filed" for purposes of Section 18 of the Exchange Act, or otherwise subject to the liability of that section, and shall not be part of any registration statement or other document filed under the Securities Act or the Exchange Act, except as shall be expressly set forth by specific reference in such filing. |                           |

