

CONMED CORP  
Form 10-Q  
November 05, 2007

**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  
September 30, 2007

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 is a large accelerated filer, an accelerated filer, or a non-accelerated filer. See definition of "accelerated filer and large accelerated filer" in Rule 12b-2 of the Exchange Act (Check one).

Large accelerated filer

Accelerated filer

Non-accelerated filer

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 November 1, 2007 is 28,611,431 shares.

**CONMED CORPORATION**

**QUARTERLY REPORT ON FORM 10-Q  
FOR THE QUARTER ENDED SEPTEMBER 30, 2007**

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**PART I FINANCIAL INFORMATION**  
**Item 1.**

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

	<u>Three Months Ended</u>		<u>Nine Months Ended</u>	
	<u>September 30,</u>		<u>September 30,</u>	
	<u>2006</u>	<u>2007</u>	<u>2006</u>	<u>2007</u>
Net sales	\$ 154,981	\$ 164,448	\$ 476,920	\$ 504,720
Cost of sales	80,250	82,090	246,515	251,277
Gross profit	74,731	82,358	230,405	253,443
Selling and administrative expense	56,219	57,506	172,716	175,518
Research and development expense	7,262	7,936	22,585	22,983
Other expense (income)	2,066	-	4,220	(4,102)
	65,547	65,442	199,521	194,399
Income from operations	9,184	16,916	30,884	59,044
Loss on early extinguishment of debt	-	-	678	-
Interest expense	4,962	3,861	14,503	12,706
Income before income taxes	4,222	13,055	15,703	46,338
Provision for income taxes	890	4,700	4,617	16,716
Net income	\$ 3,332	\$ 8,355	\$ 11,086	\$ 29,622
<b>Per share data:</b>				
Net income				
Basic	\$ .12	\$ .29	\$ .40	\$ 1.06
Diluted	.12	.29	.39	1.04
Weighted average common shares				
Basic	27,888	28,572	27,999	27,990
Diluted	28,134	29,101	28,241	28,580

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

	December 31, <u>2006</u>	September 30, <u>2007</u>
<b>ASSETS</b>		
Current assets:		
Cash and cash equivalents	\$ 3,831	\$ 5,411
Accounts receivable, net	75,120	81,765
Inventories	151,687	166,712
Income taxes receivable	747	2,919
Deferred income taxes	15,212	15,432
Prepaid expenses and other current assets	3,286	3,284
Total current assets	249,883	275,523
Property, plant and equipment, net	116,480	121,653
Goodwill	290,512	294,659
Other intangible assets, net	191,135	189,470
Other assets	13,561	10,767
Total assets	\$ 861,571	\$ 892,072
<b>LIABILITIES AND SHAREHOLDERS' EQUITY</b>		
Current liabilities:		
Current portion of long-term debt	\$ 3,148	\$ 3,247
Accounts payable	41,823	34,769
Accrued compensation and benefits	17,712	18,452
Accrued interest	727	1,901
Other current liabilities	11,795	13,108
Total current liabilities	75,205	71,477
Long-term debt	264,676	239,647
Deferred income taxes	51,004	66,399
Other long-term liabilities	30,332	25,817
Total liabilities	421,217	403,340
Commitments and contingencies		
Shareholders' equity:		
Preferred stock, par value \$.01 per share; authorized 500,000 shares; none outstanding	-	-
Common stock, par value \$.01 per share; 100,000,000 shares authorized; 31,304,203 and 31,299,203 shares issued in 2006 and 2007, respectively	313	313
Paid-in capital	284,858	287,180
Retained earnings	247,425	273,049
Accumulated other comprehensive income (loss)	(8,612)	(3,869)

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Less: 3,321,545 and 2,698,421 shares of common stock in treasury, at cost in 2006 and 2007, respectively	(83,630)	(67,941)
Total shareholders' equity	440,354	488,732
Total liabilities and shareholders' equity	\$ 861,571	\$ 892,072

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

	<u>Nine months ended</u>	
	<u>September 30,</u>	
	<u>2006</u>	<u>2007</u>
Cash flows from operating activities:		
Net income	\$ 11,086	\$ 29,622
Adjustments to reconcile net income, to net cash provided by operating activities:		
Depreciation	8,591	9,498
Amortization	13,704	14,015
Stock-based compensation	2,599	2,932
Deferred income taxes	4,670	14,869
Loss on extinguishment of debt	203	-
Increase (decrease) in cash flows from changes in assets and liabilities:		
Sale of accounts receivable	(3,000)	(4,000)
Accounts receivable	3,320	(2,424)
Inventories	(9,975)	(21,826)
Accounts payable	4,065	(5,284)
Income taxes receivable	(1,979)	(1,904)
Accrued compensation and benefits	2,148	740
Accrued interest	844	1,174
Other assets	(1,083)	(298)
Other liabilities	5,604	(1,651)
	29,711	5,841
Net cash provided by operating activities	40,797	35,463
Cash flows from investing activities:		
Purchases of property, plant, and equipment	(16,738)	(15,964)
Proceeds from sale of equity investment	1,205	-
Payments related to business acquisitions	(2,463)	(5,837)
Net cash used in investing activities	(17,996)	(21,801)
Cash flows from financing activities:		
Net proceeds from common stock issued under employee plans	2,103	11,119
Excess tax benefits from stock-based compensation	102	-
Repurchase of common stock	(7,848)	-
Payments on senior credit agreement	(141,822)	(24,664)
Proceeds of senior credit agreement	135,000	-
Payments on mortgage notes	(223)	(266)
Payments related to issuance of long-term debt	(1,260)	-
Net change in cash overdrafts	(604)	(1,770)
Net cash used in financing activities	(14,552)	(15,581)
Effect of exchange rate changes on cash and cash equivalents	1,789	3,499

Net increase in cash and cash equivalents	10,038	1,580
Cash and cash equivalents at beginning of period	3,454	3,831
Cash and cash equivalents at end of period	\$ 13,492	\$ 5,411

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

**Note 1 – Operations and Significant Accounting Policies****Organization and operations**

The accompanying consolidated condensed financial statements include the accounts of CONMED Corporation and its controlled subsidiaries (“CONMED”, the “Company”, “we” or “us”). All intercompany accounts and transactions have been eliminated. CONMED 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 disposables, 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. In the opinion of management, all adjustments (consisting of normal recurring accruals) considered necessary for a fair presentation have been included. Results for the period ended September 30, 2007 are not necessarily indicative of the results that may be expected for the year ending December 31, 2007.

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, 2006 included in our Annual Report on Form 10-K.

**Note 3 – Other comprehensive income**

Comprehensive income consists of the following:

	<b><u>Three months ended</u></b>		<b><u>Nine months ended</u></b>	
	<b><u>September 30,</u></b>		<b><u>September 30,</u></b>	
	<b><u>2006</u></b>	<b><u>2007</u></b>	<b><u>2006</u></b>	<b><u>2007</u></b>
Net income	\$ 3,332	\$ 8,355	\$ 11,086	\$ 29,622
Other comprehensive income:				
Adjustment to net amortization and deferral of pension cost	-	145	-	434
Foreign currency translation adjustment	860	2,368	2,182	4,309
Comprehensive income	\$ 4,192	\$ 10,868	\$ 13,268	\$ 34,365





Accumulated other comprehensive income consists of the following:

	<b>Minimum Pension Liability</b>	<b>Cumulative Translation Adjustments</b>	<b>Accumulated Other Comprehensive Income (loss)</b>
Balance, December 31, 2006	\$ (12,386)	\$ 3,774	\$ (8,612)
Adjustment to net amortization and deferral of pension cost	434	-	434
Foreign currency translation adjustments	-	4,309	4,309
Balance, September 30, 2007	\$ (11,952)	\$ 8,083	\$ (3,869)

#### **Note 4 – Income Taxes**

The Company adopted Financial Accounting Standards Board (“FASB”) Interpretation No. 48, “Accounting for Uncertainty in Income Taxes” (“FIN 48”) on January 1, 2007. The impact of this pronouncement was not material to the Company’s consolidated financial statements. As of the date of adoption the Company’s unrecognized tax benefits totaled approximately \$1.4 million; \$1.3 million in taxes and \$0.1 million in interest. If recognized, the entire amount of unrecognized tax benefits would decrease the effective income tax rate.

The Internal Revenue Service (“IRS”) has completed examinations of our United States federal income tax returns through 2004. Tax years subsequent to 2004 are subject to future examination. Substantially all material state jurisdictions are closed for examination for tax years through 2002.

It is reasonably possible that the amount of unrecognized tax benefits could change in the next 12 months as a result of the anticipated completion of the 2005, 2006 and 2007 IRS examinations and expiration of statutes of limitations on prior tax returns. Unrecognized tax benefits for these years relate to permanent deductions and tax credits. A reasonable estimate of the range of change in unrecognized tax benefits cannot be made at this time.

The Company’s policy is to classify interest and penalties related to income tax matters as income tax expense.

#### **Note 5 - Inventories**

Inventories consist of the following:

	<b>December 31, 2006</b>	<b>September 30, 2007</b>
Raw materials	\$ 50,225	\$ 59,094
Work-in-process	17,815	22,488
Finished goods	83,647	85,130
Total	\$ 151,687	\$ 166,712



**Note 6 – Earnings per share**

Basic earnings per share (“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 share-based awards during the period. The following table sets forth the computation of basic and diluted earnings per share for the three and nine month periods ended September 30, 2006 and 2007.

	<b>Three months ended</b>		<b>Nine months ended</b>	
	<b>September 30,</b>		<b>September 30,</b>	
	<b>2006</b>	<b>2007</b>	<b>2006</b>	<b>2007</b>
Net income	\$ 3,332	\$ 8,355	\$ 11,086	\$ 29,622
Basic – weighted average shares outstanding	27,888	28,572	27,999	27,990
Effect of dilutive potential securities	246	529	242	590
Diluted – weighted average shares outstanding	28,134	29,101	28,241	28,580
Basic EPS	\$ .12	\$ .29	\$ .40	\$ 1.06
Diluted EPS	.12	.29	.39	1.04

Stock based awards for both the three and nine months ended September 30, 2006 of approximately 1.7 million and for the three and nine months ended September 30, 2007 of 0.7 million and 0.6 million, respectively, were excluded from the computation of diluted earnings per share as the effect of exercise would be anti-dilutive. Upon conversion of our 2.50% convertible senior subordinated notes (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 September 30, 2007, 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. Under the net share settlement method and in accordance with Emerging Issues Task Force (“EITF”) Issue 04-8, “The Effect of Contingently Convertible Debt on Diluted Earnings per Share”, 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 nine months ended September 30, 2007 are as follows:

Balance as of January 1, 2007	\$ 290,512
Goodwill acquired	3,253
Adjustments to goodwill resulting from business acquisitions finalized	492

Foreign currency translation	402
Balance as of September 30, 2007	\$ 294,659

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

	<b>December 31, <u>2006</u></b>	<b>September 30, <u>2007</u></b>
CONMED Electrosurgery	\$ 16,645	\$ 16,645
CONMED Endosurgery	42,419	42,430
CONMED Linvatec	173,007	173,409
CONMED Patient Care	58,441	62,175
	<b>\$ 290,512</b>	<b>\$ 294,659</b>

During the third quarter of 2007, we acquired a business in the amount of \$4.6 million of which \$3.3 million related to goodwill.

During our fourth quarter 2006 goodwill impairment testing, we determined that the goodwill of our Endoscopic Technologies operating unit was impaired and consequently we recorded a goodwill impairment charge of \$46.7 million in the year ended December 31, 2006.

Other intangible assets consist of the following:

	<b><u>December 31, 2006</u></b>		<b><u>September 30, 2007</u></b>	
	<b>Gross Carrying Amount</b>	<b>Accumulated Amortization</b>	<b>Gross Carrying Amount</b>	<b>Accumulated Amortization</b>
<b>Amortized intangible assets:</b>				
Customer relationships	\$ 113,376	\$ (24,498)	\$ 114,708	\$ (27,107)
Patents and other intangible assets	39,609	(24,696)	39,597	