

INTEGRA LIFESCIENCES HOLDINGS CORP  
Form 10-Q  
May 01, 2014  
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UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION  
WASHINGTON, DC 20549

FORM 10-Q

(Mark One)

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

For the quarterly period ended March 31, 2014

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

For the transition period from \_\_\_\_\_ to \_\_\_\_\_  
COMMISSION FILE NO. 0-26224

INTEGRA LIFESCIENCES HOLDINGS CORPORATION  
(EXACT NAME OF REGISTRANT AS SPECIFIED IN ITS CHARTER)

DELAWARE 51-0317849  
(STATE OR OTHER JURISDICTION OF (I.R.S. EMPLOYER  
INCORPORATION OR ORGANIZATION) IDENTIFICATION NO.)

311 ENTERPRISE DRIVE 08536  
PLAINSBORO, NEW JERSEY  
(ADDRESS OF PRINCIPAL EXECUTIVE OFFICES) (ZIP CODE)

REGISTRANT'S TELEPHONE NUMBER, INCLUDING AREA CODE: (609) 275-0500

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 such shorter period that the registrant was required to submit and post such files). Yes  No

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer or a smaller reporting company. See the definitions of "large accelerated filer", "accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer  Accelerated filer

Non-accelerated filer  (Do not check if a smaller reporting company) 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 of the registrant's Common Stock, \$0.01 par value, outstanding as of April 28, 2014 was 32,567,024.

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## PART I. FINANCIAL INFORMATION

## Item 1. Financial Statements

INTEGRA LIFESCIENCES HOLDINGS CORPORATION  
 CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS  
 AND COMPREHENSIVE INCOME  
 (UNAUDITED)  
 (In thousands, except per share amounts)

|   | Three Months Ended March 31, |                       |
|---|------------------------------|-----------------------|
|   | 2014                         | 2013<br>(As adjusted) |
| Total revenue, net  | \$215,059                    | \$196,652             |
| Costs and Expenses:                                       |                              |                       |
| Cost of goods sold  | 82,383                       | 79,612                |
| Research and development                                  | 12,567                       | 12,716                |
| Selling, general and administrative                       | 108,338                      | 102,963               |
| Intangible asset amortization                             | 3,033                        | 3,551                 |
| Total costs and expenses                                  | 206,321                      | 198,842               |
| Operating income (loss)                                   | 8,738                        | (2,190 )              |
| Interest income   | 62                           | 63                    |
| Interest expense  | (5,142 )                     | (4,800 )              |
| Other income (expense), net                               | 317                          | (974 )                |
| Income (loss) before income taxes                         | 3,975                        | (7,901 )              |
| Income tax expense (benefit)                              | 1,769                        | (1,873 )              |
| Net income (loss)   | \$2,206                      | \$(6,028 )            |
| Basic net income (loss) per common share                  | \$0.07                       | \$(0.22 )             |
| Diluted net income (loss) per common share                | \$0.07                       | \$(0.22 )             |
| Weighted average common shares outstanding (See Note 11): |                              |                       |
| Basic   | 32,275                       | 27,796                |
| Diluted   | 32,768                       | 27,796                |
| Comprehensive income (loss) (See Note 12)                 | \$3,206                      | \$(12,512 )           |

The accompanying notes are an integral part of these condensed consolidated financial statements.

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INTEGRA LIFESCIENCES HOLDINGS CORPORATION  
 CONDENSED CONSOLIDATED BALANCE SHEETS  
 (UNAUDITED)  
 (In thousands)

|  | March 31, 2014 | December 31,<br>2013<br>(As adjusted) |
|--|----------------|---------------------------------------|
| <b>ASSETS</b>  |                |                                       |
| Current Assets:  |                |                                       |
| Cash and cash equivalents  | \$ 129,038     | \$ 120,614                            |
| Trade accounts receivable, net of allowances of \$6,287 and \$6,194  | 112,521        | 118,145                               |
| Inventories, net   | 215,232        | 206,919                               |
| Deferred tax assets  | 48,459         | 48,616                                |
| Prepaid expenses and other current assets  | 34,496         | 26,858                                |
| Total current assets   | 539,746        | 521,152                               |
| Property, plant and equipment, net   | 205,667        | 200,310                               |
| Intangible assets, net   | 429,446        | 197,163                               |
| Goodwill   | 367,649        | 249,764                               |
| Deferred tax assets  | 5,645          | 15,412                                |
| Other assets   | 7,770          | 8,338                                 |
| Total assets   | \$ 1,555,923   | \$ 1,192,139                          |
| <b>LIABILITIES AND STOCKHOLDERS' EQUITY</b>  |                |                                       |
| Current Liabilities:   |                |                                       |
| Accounts payable, trade  | \$ 46,428      | \$ 50,752                             |
| Deferred revenue   | 4,220          | 4,197                                 |
| Accrued compensation   | 28,487         | 28,079                                |
| Accrued expenses and other current liabilities   | 37,696         | 36,354                                |
| Total current liabilities  | 116,831        | 119,382                               |
| Long-term borrowings under senior credit facility  | 421,875        | 186,875                               |
| Long-term convertible securities   | 207,125        | 205,182                               |
| Deferred tax liabilities   | 94,612         | 2,083                                 |
| Other liabilities  | 36,280         | 12,527                                |
| Total liabilities  | 876,723        | 526,049                               |
| Commitments and contingencies  |                |                                       |
| Stockholders' Equity:  |                |                                       |
| Preferred Stock; no par value; 15,000 authorized shares; none outstanding  | —              | —                                     |
| Common stock; \$0.01 par value; 60,000 authorized shares; 41,449 and 41,042 issued at March 31, 2014 and December 31, 2013, respectively | 415            | 410                                   |
| Additional paid-in capital   | 760,817        | 750,918                               |
| Treasury stock, at cost; 8,903 shares at March 31, 2014 and December 31, 2013  | (367,121)      | (367,121)                             |
| Accumulated other comprehensive income (loss)  | 1,927          | 927                                   |
| Retained earnings  | 283,162        | 280,956                               |
| Total stockholders' equity   | 679,200        | 666,090                               |
| Total liabilities and stockholders' equity   | \$ 1,555,923   | \$ 1,192,139                          |

The accompanying notes are an integral part of these condensed financial statements.



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INTEGRA LIFESCIENCES HOLDINGS CORPORATION  
 CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS  
 (UNAUDITED)  
 (In thousands)

|   | Three Months Ended March 31, |                       |
|---|------------------------------|-----------------------|
|   | 2014                         | 2013<br>(As adjusted) |
| <b>OPERATING ACTIVITIES:</b>  |                              |                       |
| Net income (loss)   | \$2,206                      | \$(6,028)             |
| Adjustments to reconcile net income (loss) to net cash provided by operating activities:          |                              |                       |
| Depreciation and amortization   | 13,961                       | 11,389                |
| Non-cash impairment charges   | 600                          | —                     |
| Deferred income tax provision (benefit)   | 1,563                        | (1,055)               |
| Amortization of debt issuance costs   | 608                          | 545                   |
| Non-cash interest expense   | 1,666                        | 1,610                 |
| Loss on disposal of property and equipment  | —                            | 1,865                 |
| Share-based compensation  | 2,471                        | 2,072                 |
| Excess tax benefits from stock-based compensation arrangements                                    | (541)                        | (23)                  |
| Changes in assets and liabilities, net of business acquisitions:                                  |                              |                       |
| Accounts receivable   | 5,671                        | 2,109                 |
| Inventories   | (8,516)                      | (6,739)               |
| Prepaid expenses and other current assets   | (1,582)                      | 2,704                 |
| Other non-current assets  | (127)                        | (115)                 |
| Accounts payable, accrued expenses and other current liabilities                                  | (4,438)                      | (515)                 |
| Deferred revenue  | 21                           | 391                   |
| Other non-current liabilities   | (2,309)                      | (364)                 |
| Net cash provided by operating activities   | 11,254                       | 7,846                 |
| <b>INVESTING ACTIVITIES:</b>  |                              |                       |
| Purchases of property and equipment   | (11,335)                     | (10,853)              |
| Sales of property and equipment   | —                            | 532                   |
| Cash used in business acquisition, net of cash acquired   | (235,000)                    | (2,766)               |
| Net cash used in investing activities   | (246,335)                    | (13,087)              |
| <b>FINANCING ACTIVITIES:</b>  |                              |                       |
| Borrowings under senior credit facility   | 235,000                      | —                     |
| Principal payments under capital lease obligations  | (122)                        | —                     |
| Proceeds from exercised stock options   | 7,755                        | 234                   |
| Excess tax benefits from stock-based compensation arrangements                                    | 541                          | 23                    |
| Net cash provided by financing activities   | 243,174                      | 257                   |
| Effect of exchange rate changes on cash and cash equivalents                                      | 331                          | (2,263)               |
| Net change in cash and cash equivalents   | 8,424                        | (7,247)               |
| Cash and cash equivalents at beginning of period  | 120,614                      | 96,938                |
| Cash and cash equivalents at end of period  | \$129,038                    | \$89,691              |
| The accompanying notes are an integral part of these condensed consolidated financial statements. |                              |                       |



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INTEGRA LIFESCIENCES HOLDINGS CORPORATION  
NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

1. BASIS OF PRESENTATION

General

The terms “we,” “our,” “us,” “Company” and “Integra” refer to Integra LifeSciences Holdings Corporation, a Delaware corporation, and its subsidiaries unless the context suggests otherwise.

In the opinion of management, the March 31, 2014 unaudited condensed consolidated financial statements contain all adjustments (consisting only of normal recurring adjustments) necessary for a fair statement of the financial position, results of operations and cash flows of the Company. Certain information and footnote disclosures normally included in financial statements prepared in accordance with generally accepted accounting principles have been condensed or omitted in accordance with the instructions to Form 10-Q and Rule 10-01 of Regulation S-X. These unaudited condensed consolidated financial statements should be read in conjunction with the Company’s consolidated financial statements for the year ended December 31, 2013 included in the Company’s Annual Report on Form 10-K. The December 31, 2013 consolidated balance sheet was derived from audited financial statements, but does not include all disclosures required by accounting principles generally accepted in the United States. Operating results for the three-month period ended March 31, 2014 are not necessarily indicative of the results to be expected for the entire year.

The preparation of consolidated financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amount of assets and liabilities, the disclosure of contingent liabilities, and the reported amounts of revenues and expenses. Significant estimates affecting amounts reported or disclosed in the consolidated financial statements include allowances for doubtful accounts receivable and sales returns and allowances, net realizable value of inventories, valuation of intangible assets including in-process research and development, amortization periods for acquired intangible assets, discount rates and estimated projected cash flows used to value and test impairments of long-lived assets and goodwill, estimates of projected cash flows and depreciation and amortization periods for long-lived assets, computation of taxes, valuation allowances recorded against deferred tax assets, the valuation of stock-based compensation, valuation of pension assets and liabilities, valuation of derivative instruments, valuation of the equity component of convertible debt instruments, valuation of contingent liabilities, the fair value of debt instruments and loss contingencies. These estimates are based on historical experience and on various other assumptions that are believed to be reasonable under the current circumstances. Actual results could differ from these estimates.

Certain amounts from the prior year’s financial statements have been reclassified in order to conform to the current year’s presentation.

Change in accounting principle

In the first quarter of 2014, the Company changed its method of accounting for the medical device excise tax (“MDET”). Prior to the change the Company recorded the MDET in inventory at the time of the first sale and then recognized the tax in cost of goods sold when the medical device was sold to the ultimate customer. Under the new method, the MDET will be recorded in selling, general and administrative expenses in the period the first sale occurs, which could be an intercompany sale.

The Company believes that this change in accounting principle is preferable as the new method provides a better comparison with the Company’s industry peers, the majority of which expense the MDET at the time of the first sale.

The medical device excise tax applies to sales beginning January 1, 2013; therefore, only 2013 financial results were affected by this change. The cumulative effect of the change in the prior years is included in retained earnings as of December 31, 2013 and the comparative period for the three months ended March 31, 2013 has been revised to reflect the retrospective application of the change in accounting principle had the new method been in effect for all periods,

as follows:

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INTEGRA LIFESCIENCES HOLDINGS CORPORATION  
 NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (continued)

## Condensed Consolidated Statements of Operations and Comprehensive Income:

|  | Three Months Ended March 31, 2013        |             |                |
|--|--|-------------|----------------|
|  | Originally<br>Reported                   | Adjustments | As<br>Adjusted |
|  | (In thousands, except per share amounts) |             |                |
| Cost of goods sold                         | \$80,268                                 | \$(656 )    | \$79,612       |
| Selling, general and administrative        | 100,161                                  | 2,802       | 102,963        |
| Income tax expense (benefit)               | (1,705 )                                 | (168 )      | (1,873 )       |
| Net income (loss)                          | (4,050 )                                 | (1,978 )    | (6,028 )       |
| Basic net income (loss) per common share   | \$(0.15 )                                |             | \$(0.22 )      |
| Diluted net income (loss) per common share | (0.15 )                                  |             | (0.22 )        |
| Comprehensive income (loss)                | \$(10,534 )                              | \$(1,978 )  | \$(12,512 )    |

## Condensed Consolidated Balance Sheets:

|   | December 31, 2013      |             |                |
|---|------------------------|-------------|----------------|
|   | Originally<br>Reported | Adjustments | As<br>Adjusted |
|   | (In thousands)         |             |                |
| Inventories                               | \$213,431              | \$(6,512 )  | \$206,919      |
| Deferred tax assets - current             | 46,300                 | 2,316       | 48,616         |
| Prepaid expenses and other current assets | 26,752                 | 106         | 26,858         |
| Retained earnings                         | 285,046                | (4,090 )    | 280,956        |

## Condensed Consolidated Statements of Cash Flows:

|                                  | Three Months Ended March 31, 2013 |             |                |
|----------------------------------|-----------------------------------|-------------|----------------|
|                                  | Originally<br>Reported            | Adjustments | As<br>Adjusted |
|                                  | (In thousands)                    |             |                |
| Net income (loss)                | \$(4,050 )                        | \$(1,978 )  | \$(6,028 )     |
| Inventories                      | (8,885 )                          | 2,146       | (6,739 )       |
| Prepaid and other current assets | 2,872                             | (168 )      | 2,704          |

## Recently Issued Accounting Standards

On July 18, 2013, the FASB issued ASU No. 2013-11, Presentation of an Unrecognized Tax Benefit When a Net Operating Loss Carryforward, a Similar Tax Loss, or a Tax Credit Carryforward Exists. This updated guidance requires an unrecognized tax benefit to be presented in the financial statements as a reduction to a deferred tax asset for a net operating loss carryforward, similar tax loss, or a tax credit carryforward. To the extent the tax benefit is not available at the reporting date under the governing tax law or if the entity does not intend to use the deferred tax asset for such purpose, the unrecognized tax benefit should be presented as a liability and not combined with deferred tax assets. This ASU is effective for fiscal years and interim periods within those years beginning after December 15, 2013 for public entities. Early adoption is permitted. The amendments are to be applied to all unrecognized tax benefits that exist as of the effective date and may be applied retrospectively to each prior reporting period presented. The standard adoption does not have a material impact on the Company's financial statements.

In April 2014, the FASB issued amendments to guidance for reporting discontinued operations and disposals of components of an entity. The amended guidance requires that a disposal representing a strategic shift that has (or will

have) a major effect on an entity's financial results or a business activity classified as held for sale should be reported as discontinued operations. The amendments also expand the disclosure requirements for discontinued operations and add new disclosures for individually significant dispositions that do not qualify as discontinued operations. The amendments are effective prospectively for fiscal years,

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INTEGRA LIFESCIENCES HOLDINGS CORPORATION  
 NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (continued)

and interim reporting periods within those years, beginning after December 15, 2014 (early adoption is permitted only for disposals that have not been previously reported). The implementation of the amended guidance is not expected to have a material impact on our consolidated financial position or results of operations.

## 2. BUSINESS ACQUISITIONS

### Confluent Surgical, Inc.

On January 15, 2014, the Company acquired all outstanding shares of Confluent Surgical, Inc., ("Confluent Surgical") - including its surgical sealant and adhesion barrier product lines - from Covidien Group S.a.r.l, ("Covidien") for an aggregate purchase price of \$255.9 million. The purchase price is comprised of an initial cash payment to Covidien of \$231.0 million upon the closing of the transaction, a separate prepayment of \$4.0 million made under a transitional supply agreement with an affiliate of Covidien, and contingent consideration with an acquisition date fair value of \$20.9 million. The potential maximum undiscounted contingent consideration of \$30.0 million consists of: \$25.0 million upon obtaining certain U.S. governmental approvals and \$5.0 million upon obtaining certain European governmental approvals, both related to the completion of the transition of the Confluent Surgical business.

The transitional supply agreement secures the supply of the acquired products from an affiliate of Covidien until the earlier of (i) the time that the transition of the Confluent Surgical business as discussed above is complete, or (ii) the fifth anniversary of the effective date of the agreement; the agreement also contains an option to extend for another two years by providing written notice at least 180 days prior to the end of the initial five-year period. This agreement contains financial incentives to the affiliate of Covidien for the timely supply of products each fiscal quarter through the third anniversary of the agreement. The prices paid under the supply agreement are essentially flat through the third anniversary of the agreement, and then increase significantly each of the following three years. The Company also entered into a transition services agreement with an affiliate of Covidien at the closing for services such as: customer service, accounting and information technology management; clinical and regulatory affairs; manufacturing transition services; and other functions.

This acquisition complements the Company's global neurosurgery growth strategy aimed at providing a broader set of solutions for surgical procedures in the head.

The following summarizes the preliminary allocation of the purchase price based on the fair value of the assets acquired and liabilities assumed, the allocation of goodwill to the Company's reporting units has not yet been completed:

|                                    | Preliminary<br>Purchase Price<br>Allocation<br>(Dollars in thousands) |                  |
|------------------------------------|---|------------------|
| Inventory deposit                  | \$4,000   |                  |
| Fixed assets                       | 438   |                  |
| Intangible assets:                 |   | Wtd. Avg. Life   |
| Technology product rights          | 239,800   | 20 years         |
| Other                              | 400   | Less than 1 year |
| Deferred tax asset - long term     | 14  |                  |
| Goodwill                           | 117,715   |                  |
| Total assets acquired              | 362,367   |                  |
| Contingent supply liability        | 5,891   |                  |
| Other                              | 731   |                  |
| Deferred tax liability - long term | 99,850  |                  |
| Net assets acquired                | \$255,895   |                  |

Subsequent to the acquisition date, a regulatory event occurred that resulted in the full-impairment of one of the acquired technology product rights for \$0.6 million. This event was not known, or knowable, at the time of the acquisition and therefore the impairment has been included in the Company's March 31, 2014 cost of sales.

The Company accounted for the contingent supply liability by recording its fair value as a liability on the date of the acquisition based on a discounted cash-flow model. This contingent supply liability relates to contractual quarterly incentive payments that will be made to an affiliate of Covidien if certain supply minimums under the transitional supply agreement are met.

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INTEGRA LIFESCIENCES HOLDINGS CORPORATION  
 NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (continued)

The Company accounted for the contingent consideration by recording its fair value as a liability on the date of the acquisition. The contingent consideration relates to the Company obtaining certain U.S. and European regulatory approvals. At the date of the acquisition, both of these milestones were valued using a discount rate of 2.2%, which is equivalent to the cost of debt for the estimated time horizon, and an overall probability of occurring of 95%. Accordingly, on January 15, 2014 the Company recorded a \$20.9 million liability representing the initial fair value estimate of the probability weighted contingent consideration that management believes will be paid between early 2017 and late 2018. Depending on the expected timing of the estimated payments, the acquisition date fair value of the probability adjusted payments could have been \$0.3 million higher or \$0.4 million lower. These fair value measurements were based on significant inputs not observed in the market and thus represented a Level 3 measurement. The contingent consideration is re-measured to fair value at each reporting date until the contingency is resolved, and those changes in fair value are recognized in earnings.

The goodwill recorded in connection with this acquisition is based on (i) expected cost savings, operating synergies and other benefits expected to result from the combined operations, (ii) the value of the going-concern element of Confluent Surgical's existing business (that is, the higher rate of return on the assembled net assets versus if the Company had acquired all of the net assets separately), and (iii) intangible assets that do not qualify for separate recognition such as Confluent Surgical's assembled workforce. The goodwill acquired will not be deductible for tax purposes.

#### Contingent consideration

The carrying value of contingent consideration was increased during the three-months ended March 31, 2014 to reflect current period acquisitions and the change in the time value of money during the period. A reconciliation of the opening balances to the closing balances of these Level 3 measurements are as follows (dollars in thousands):

|  |          | Location in Statement of Operations |
|--|----------|-------------------------------------|
| Balance as of January 1, 2014  | \$1,227  |                                     |
| Contingent consideration from Confluent Surgical acquisition           | 20,895   |                                     |
| Loss from increase in fair value of contingent consideration liability | 128      | Selling, general and administrative |
| Fair value at March 31, 2014   | \$22,250 |                                     |

#### Pro Forma Results

The following unaudited pro forma financial information summarizes the results of operations for the three months ended March 31, 2013 as if the Confluent Surgical acquisition completed by the Company during 2014 had been completed as of January 1, 2013. The pro forma results are based upon certain assumptions and estimates, and they give effect to actual operating results prior to the acquisition and adjustments to reflect (i) the change in interest expense, depreciation expense, and intangible asset amortization, (ii) certain external expenses related to the acquisition as if they were incurred on January 1, 2013 that will not be recurring in the post-acquisition periods, (iii) income taxes on the aforementioned adjustments at the Company's statutory rate, and (iv) the earnings per share impact of the increase in the number of weighted average shares outstanding from the sale of registered common shares during November 2013 in anticipation of the Confluent Surgical acquisition. No effect has been given to other cost reductions or operating synergies. As a result, these pro forma results do not necessarily represent results that would have occurred if the acquisitions had taken place on the basis assumed above, nor are they indicative of the results of future combined operations.

The pro forma impact of the Confluent Surgical acquisition was not material to the 2014 consolidated operating results of the Company; therefore the pro forma impact on that period has not been included below. The pro forma results below also incorporate the impact of the change in accounting for the MDET on the 2013 results which is discussed in Note 1.

Three Months Ended  
 March 31, 2013  
 (Dollars in thousands)

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|                              |            |   |
|------------------------------|------------|---|
| Total revenue                | \$ 213,051 |   |
| Net income (loss)            | \$ (5,469  | ) |
| Net income (loss) per share: |            |   |
| Basic                        | \$ (0.17   | ) |
| Diluted                      | \$ (0.17   | ) |

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INTEGRA LIFESCIENCES HOLDINGS CORPORATION  
 NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (continued)

## 3. INVENTORIES

Inventories, net consisted of the following:

|                 | March 31, 2014 | December 31,<br>2013 |
|-----------------|----------------|----------------------|
|                 | (In thousands) | (As adjusted)        |
| Finished goods  | \$ 131,791     | \$ 123,786           |
| Work in process | 47,836         | 47,403               |
| Raw materials   | 35,605         | 35,730               |
|                 | \$ 215,232     | \$ 206,919           |

The December 31, 2013 amounts above have been revised to correct an immaterial reclassification of certain items between work in process and raw materials.

## 4. GOODWILL AND OTHER INTANGIBLE ASSETS

The Company reviews goodwill for impairment annually during its third quarter and whenever events or changes in circumstances indicate the carrying value of goodwill may not be recoverable. The Company performed its most recent annual assessment on July 31, 2013 which resulted in a non-cash goodwill impairment charge of \$46.7 million for its U.S. Spine reporting unit, which is a part of the U.S. Spine and Other reportable segment.

Changes in the carrying amount of goodwill for the three months ended March 31, 2014 were as follows:

|   | U.S.<br>Neurosurgery | U.S.<br>Instruments | U.S.<br>Extremities | U.S.<br>Spine<br>and<br>Other | International | Total      |
|---|----------------------|---------------------|---------------------|-------------------------------|---------------|------------|
|   | (In thousands)       |                     |                     |                               |               |            |
| Goodwill, gross   | \$95,165             | \$58,033            | \$61,079            | \$56,325                      | \$25,900      | \$296,502  |
| Accumulated impairment losses                           |                      |                     |                     | (46,738 )                     |               | (46,738 )  |
| Goodwill at December 31, 2013                           | 95,165               | 58,033              | 61,079              | 9,587                         | 25,900        | 249,764    |
| Confluent Surgical acquisition - preliminary allocation | 94,315               | —                   | —                   | —                             | 23,400        | 117,715    |
| Foreign currency translation                            | 88                   | 27                  | 28                  | 4                             | 23            | 170        |
| Goodwill at March 31, 2014                              | \$ 189,568           | \$ 58,060           | \$ 61,107           | \$ 9,591                      | \$ 49,323     | \$ 367,649 |

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 NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (continued)

The components of the Company's identifiable intangible assets were as follows:

|                          | March 31, 2014         |           |              |           |
|--------------------------|------------------------|-----------|--------------|-----------|
|                          | Weighted               | Cost      | Accumulated  | Net       |
|                          | Average                |           | Amortization |           |
|                          | Life                   |           |              |           |
|                          | (Dollars in thousands) |           |              |           |
| Completed technology     | 18 years               | \$320,460 | \$(49,607 )  | \$270,853 |
| Customer relationships   | 12 years               | 146,701   | (81,926 )    | 64,775    |
| Trademarks/brand names   | 31 years               | 33,601    | (15,726 )    | 17,875    |
| Trademarks/brand names   | Indefinite             | 48,484    | —            | 48,484    |
| Supplier relationships   | 27 years               | 34,721    | (9,677 )     | 25,044    |
| All other <sup>(1)</sup> | 4 years                | 4,652     | (2,237 )     | 2,415     |
|                          |                        | \$588,619 | \$(159,173 ) | \$429,446 |

  

|                          | December 31, 2013      |           |              |           |
|--------------------------|------------------------|-----------|--------------|-----------|
|                          | Weighted               | Cost      | Accumulated  | Net       |
|                          | Average                |           | Amortization |           |
|                          | Life                   |           |              |           |
|                          | (Dollars in thousands) |           |              |           |
| Completed technology     | 12 years               | \$81,238  | \$(45,343 )  | \$35,895  |
| Customer relationships   | 12 years               | 146,627   | (79,624 )    | 67,003    |
| Trademarks/brand names   | 31 years               | 33,703    | (15,648 )    | 18,055    |
| Trademarks/brand names   | Indefinite             | 48,484    | —            | 48,484    |
| Supplier relationships   | 27 years               | 34,721    | (9,305 )     | 25,416    |
| All other <sup>(1)</sup> | 5 years                | 4,251     | (1,941 )     | 2,310     |
|                          |                        | \$349,024 | \$(151,861 ) | \$197,163 |

(1) At March 31, 2014 and December 31, 2013, all other included in-process research and development ("IPR&D") of \$1.4 million in both periods, which was indefinite-lived.

During the three months ended March 31, 2014, the Company recorded an impairment charge of \$0.6 million in cost of goods sold related to technology assets acquired from Confluent Surgical that will no longer be sold due to a regulatory event that occurred after the acquisition date.

Based on quarter-end exchange rates, annual amortization expense (including amounts reported in cost of product revenues, but excluding any possible future amortization associated with acquired IPR&D) is expected to approximate \$30.9 million in 2014, \$28.8 million in 2015, \$26.5 million in 2016, \$24.4 million in 2017 and \$24.1 million in 2018. Identifiable intangible assets are initially recorded at fair market value at the time of acquisition using an income or cost approach.

## 5. DEBT

### Amended and Restated Senior Credit Agreement

On August 10, 2010, the Company entered into an amended and restated credit agreement with a syndicate of lending banks (the "Senior Credit Facility"). The Company amended the Senior Credit Facility on June 8, 2011, May 11, 2012 and June 21, 2013.

The June 8, 2011 amendment:

i.

increased the revolving credit component from \$450 million to \$600 million and eliminated the \$150 million term loan component that existed under the original amended and restated credit agreement;

- ii. allows the Company to further increase the size of the revolving credit component by an aggregate of \$200 million with additional commitments;

INTEGRA LIFESCIENCES HOLDINGS CORPORATION

NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (continued)

... provides the Company with decreased borrowing rates and annual commitment fees, and provides more favorable  
iii. financial covenants; and

iv. extended the maturity date from August 10, 2015 to June 8, 2016.

On May 11, 2012, the Company entered into an amendment to the Senior Credit Facility (the "2012 Amendment"). The 2012 Amendment modified certain financial and negative covenants. The 2012 Amendment provides that the Company's Maximum Consolidated Total Leverage Ratio (a measure of net debt to consolidated EBITDA, in each case as defined in the Senior Credit Facility, as amended) during any consecutive four quarter period should not be greater than 3.75 to 1.00 during any such period ending on December 31, 2013 (instead of March 31, 2012). In addition, when calculating consolidated EBITDA for any period, the 2012 Amendment permits the addition of certain costs and expenses in the calculation of consolidated net income for such period, to the extent deducted in the calculation of consolidated net income.

On June 21, 2013, the Company entered into an amendment to the Senior Credit Facility (the "2013 Amendment"). The 2013 Amendment modified certain financial and negative covenants and increased the Company's Maximum Consolidated Total Leverage Ratio (a measure of net debt to consolidated EBITDA, in each case as defined in the Senior Credit Facility, as amended) to 4.25 through June 30, 2014, with a step-down to 4.00 through March 31, 2015, and then with another step-down to 3.75 thereafter. In addition, when calculating consolidated EBITDA for any period, the 2013 Amendment permits the addition of certain costs and expenses in the calculation of consolidated net income for such period, to the extent deducted in the calculation of consolidated net income. The effect of the 2013 Amendment is to increase the ability of the Company to borrow under the Senior Credit Facility during the affected periods. The Company capitalized \$1.1 million of incremental financing costs in connection with the 2013 Amendment, which will be amortized through the maturity date of the Senior Credit Facility.

The Senior Credit Facility is collateralized by substantially all of the assets of the Company's U.S. subsidiaries, excluding intangible assets. The Senior Credit Facility is subject to various financial and negative covenants and at March 31, 2014, the Company was in compliance with all such covenants.

Borrowings under the Senior Credit Facility currently bear interest, at the Company's option, at a rate equal to (i) the Eurodollar Rate (as defined in the Senior Credit Facility, which definition has not changed) in effect from time to time plus the applicable rate (ranging from 1.00% to 1.75%) or (ii) the highest of (x) the weighted average overnight Federal funds rate, as published by the Federal Reserve Bank of New York, plus 0.5%, (y) the prime lending rate of Bank of America, N.A. or (z) the one-month Eurodollar Rate plus 1.0%. The applicable rates are based on the Company's consolidated total leverage ratio (defined as the ratio of (a) consolidated funded indebtedness less cash in excess of \$40 million that is not subject to any restriction of the use or investment thereof to (b) consolidated EBITDA) at the time of the applicable borrowing.

The Company also pays an annual commitment fee (ranging from 0.15% to 0.30%, based on the Company's consolidated total leverage ratio) on the daily amount by which the revolving credit facility exceeds the outstanding loans and letters of credit under the credit facility.

At March 31, 2014 and December 31, 2013, there was \$421.9 million and \$186.9 million outstanding under the Senior Credit Facility at a weighted average interest rate of 1.7% and 2.0%, respectively. At March 31, 2014, there was approximately \$178.1 million available for borrowing under the Senior Credit Facility. The fair value of outstanding borrowings under the Senior Credit Facility at March 31, 2014 was approximately \$425.7 million. The fair value of the Senior Credit Facility was determined by using a discounted cash flow model based on current market interest rates available to the Company. These inputs are corroborated by observable market data for similar liabilities and therefore classified within Level 2 of the fair value hierarchy. Level 2 inputs represent inputs that are observable for the asset or liability, either directly or indirectly and are other than active market observable inputs that reflect unadjusted quoted prices for identical assets or liabilities. The Company considers the balance to be long-term in nature based on its current intent and ability to repay the borrowing outside of the next twelve-month period.

#### 2016 Convertible Senior Notes

On June 15, 2011, the Company issued \$230.0 million aggregate principal amount of its 1.625% Convertible Senior Notes due in 2016 (the "2016 Notes"). The 2016 Notes mature on December 15, 2016, and bear interest at a rate of

1.625% per annum payable semi-annually in arrears on December 15 and June 15 of each year. The portion of the debt proceeds that was classified as equity at the time of the offering was \$43.2 million, an equivalent of that amount is being amortized to interest expense using the effective interest method through December 2016. The effective interest rate implicit in the liability component is 5.6%.

At March 31, 2014, the carrying amount of the liability component was \$207.1 million, the remaining unamortized discount was \$22.9 million, and the principal amount outstanding was \$230.0 million. The fair value of the 2016 Notes at March 31, 2014 was approximately \$248.6 million. At December 31, 2013, the carrying amount of the liability component was \$205.2 million, the remaining unamortized discount was \$24.8 million and the principal amount outstanding was \$230.0 million. The fair value of

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 NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (continued)

the liability of the 2016 Notes was determined using a discounted cash flow model based on current market interest rates available to the Company. These inputs are corroborated by observable market data for similar liabilities and therefore classified within Level 2.

The 2016 Notes are senior, unsecured obligations of the Company, and are convertible into cash and, if applicable, shares of its common stock based on an initial conversion rate, subject to adjustment of 17.4092 shares per \$1,000 principal amount of 2016 Notes (which represents an initial conversion price of approximately \$57.44 per share). The Company will satisfy any conversion of the 2016 Notes with cash up to the principal amount of the 2016 Notes pursuant to the net share settlement mechanism set forth in the indenture and, with respect to any excess conversion value, with shares of the Company's common stock. The 2016 Notes are convertible only in the following circumstances: (1) if the closing sale price of the Company's common stock exceeds 150% of the conversion price during a period as defined in the indenture; (2) if the average trading price per \$1,000 principal amount of the 2016 Notes is less than or equal to 98% of the average conversion value of the 2016 Notes during a period as defined in the indenture; (3) at any time on or after June 15, 2016; or (4) if specified corporate transactions occur. The issue price of the 2016 Notes was equal to their face amount, which is also the amount holders are entitled to receive at maturity if the 2016 Notes are not converted. As of March 31, 2014, none of these conditions existed with respect to the 2016 Notes and as a result, the 2016 Notes are classified as long term.

In connection with the issuance of the 2016 Notes, the Company entered into call transactions and warrant transactions, primarily with affiliates of the initial purchasers of such notes (the "hedge participants"). The initial strike price of the call transaction is approximately \$57.44 per share, subject to customary anti-dilution adjustments. The initial strike price of the warrant transaction is approximately \$70.05 per share, subject to customary anti-dilution adjustments.

#### Convertible Note Interest

The interest expense components of the Company's convertible notes are as follows (net of capitalized interest amounts):

|  | Three Months Ended March 31, |         |
|--|------------------------------|---------|
|  | 2014                         | 2013    |
|  | (In thousands)               |         |
| 2016 Notes:  |                              |         |
| Amortization of the discount on the liability component  | \$1,666                      | \$1,610 |
| Cash interest related to the contractual interest coupon | 801                          | 818     |
| Total  | \$2,467                      | \$2,428 |

## 6. DERIVATIVE INSTRUMENTS

### Interest Rate Hedging

The Company's interest rate risk relates to U.S. dollar denominated variable LIBOR interest rate borrowings. The Company uses an interest rate swap derivative instrument entered into on August 10, 2010 with an effective date of December 31, 2010 to manage its earnings and cash flow exposure to changes in interest rates by converting a portion of its floating-rate debt into fixed-rate debt beginning on December 31, 2010. This interest rate swap expires on August 10, 2015.

The Company designates this derivative instrument as a cash flow hedge. The Company records the effective portion of any change in the fair value of a derivative instrument designated as a cash flow hedge as unrealized gains or losses in accumulated other comprehensive income ("AOCI"), net of tax, until the hedged item affects earnings, at which point the effective portion of any gain or loss will be reclassified to earnings. If the hedged cash flow does not occur, or if it becomes probable that it will not occur, the Company will reclassify the amount of any gain or loss on the related cash flow hedge to interest expense at that time.

The Company expects that approximately \$1.7 million of pre-tax losses recorded as net in AOCI related to the interest rate hedge could be reclassified to earnings within the next twelve months.

#### Foreign Currency Hedging

From time to time the Company enters into foreign currency hedge contracts intended to protect the U.S. dollar value of certain forecasted foreign currency denominated transactions. The Company records the effective portion of any change in the fair value of foreign currency cash flow hedges in AOCI, net of tax, until the hedged item affects earnings. Once the related hedged item affects earnings, the Company reclassifies the effective portion of any related unrealized gain or loss on the foreign currency cash flow hedge to earnings. If the hedged forecasted transaction does not occur, or if it becomes probable that it will not occur, the Company will reclassify the amount of any gain or loss on the related cash flow hedge to earnings at that time.

INTEGRA LIFESCIENCES HOLDINGS CORPORATION  
 NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (continued)

The success of the Company's hedging program depends, in part, on forecasts of certain activity denominated in euros. The Company may experience unanticipated currency exchange gains or losses to the extent that there are differences between forecasted and actual activity during periods of currency volatility. In addition, changes in currency exchange rates related to any unhedged transactions may affect its earnings and cash flows.

#### Counterparty Credit Risk

The Company manages its concentration of counterparty credit risk on its derivative instruments by limiting acceptable counterparties to a group of major financial institutions with investment grade credit ratings, and by actively monitoring their credit ratings and outstanding positions on an ongoing basis. Therefore, the Company considers the credit risk of the counterparties to be low. Furthermore, none of the Company's derivative transactions are subject to collateral or other security arrangements, and none contain provisions that depend upon the Company's credit ratings from any credit rating agency.

#### Fair Value of Derivative Instruments

The Company has classified all of its derivative instruments within Level 2 of the fair value hierarchy because observable inputs are available for substantially the full term of the derivative instruments. The fair value of the foreign currency forward exchange contracts related to inventory purchases is determined by comparing the forward rate as of the period end and the settlement rate specified in each contract. The fair value of the interest rate swaps was developed using a market approach based on publicly available market yield curves and the terms of the related swap. The Company performs ongoing assessments of counterparty credit risk.

The following table summarizes the fair value and presentation for derivatives designated as hedging instruments in the condensed consolidated balance sheets as of March 31, 2014 and December 31, 2013:

| Location on Balance Sheet <sup>(1)</sup> :   | Fair Value as of |                   |
|--|------------------|-------------------|
|  | March 31, 2014   | December 31, 2013 |
|  | (In thousands)   |                   |
| Derivatives designated as hedges — Liabilities:                                    |                  |                   |
| Interest rate swap — Accrued expenses and other current liabilities <sup>(2)</sup> | \$1,653          | \$1,676           |
| Interest rate swap — Other liabilities <sup>(2)</sup>                              | 444              | 763               |
| Total Derivatives designated as hedges — Liabilities                               | \$2,097          | \$2,439           |

<sup>(1)</sup> The Company classifies derivative assets and liabilities as current based on the cash flows expected to be incurred within the following 12 months.

At March 31, 2014 and December 31, 2013, the notional amount related to the Company's sole interest rate swap <sup>(2)</sup> was \$108.8 million and \$112.5 million, respectively. In the next twelve months, the Company expects to reduce the notional amount by \$15.0 million.



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 NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (continued)

The following presents the effect of derivative instruments designated as cash flow hedges on the accompanying condensed consolidated statements of operations during the three months ended March 31, 2014 and 2013:

|                                       | Balance in AOCI<br>Beginning of<br>Quarter | Amount of<br>Gain (Loss)<br>Recognized in<br>AOCI-<br>Effective Portion | Amount of Gain (Loss)<br>Reclassified from<br>AOCI into<br>Earnings-Effective<br>Portion | Balance in AOCI<br>End of Quarter | Location in<br>Statements of<br>Operations |
|---------------------------------------|--|---|--|-----------------------------------|--|
| (In thousands)                        |  |   |  |                                   |  |
| Three Months Ended March 31,<br>2014  |  |   |  |                                   |  |
| Interest rate swap                    | \$(2,439 )                                 | \$(109 )  | \$ (451 )  | \$ (2,097 )                       | Interest<br>(expense)                      |
|                                       | \$(2,439 )                                 | \$(109 )  | \$ (451 )  | \$ (2,097 )                       |  |
| Three Months Ended March 31,<br>2013  |  |   |  |                                   |  |
| Forward currency forward<br>contracts | \$(34 )                                    | \$—   | \$ (34 )   | \$ —                              | Cost of goods<br>sold                      |
| Interest rate swap                    | (4,125 )                                   | (9 )  | (490 )   | (3,644 )                          | Interest<br>(expense)                      |
|                                       | \$(4,159 )                                 | \$(9 )  | \$ (524 )  | \$ (3,644 )                       |  |

The Company recognized no gains or losses resulting from ineffectiveness of cash flow hedges during the three months ended March 31, 2014 and 2013.

## 7. STOCK-BASED COMPENSATION

As of March 31, 2014, the Company had stock options, restricted stock awards, performance stock awards, contract stock awards and restricted stock unit awards outstanding under three plans, the 2000 Equity Incentive Plan (the "2000 Plan"), the 2001 Equity Incentive Plan (the "2001 Plan"), and the 2003 Equity Incentive Plan (the "2003 Plan," and collectively, the "Plans").

Stock options issued under the Plans become exercisable over specified periods, generally within four years from the date of grant for officers, directors, and employees, and generally expire six years from the grant date for employees, and from six to ten years for directors and certain executive officers. Restricted stock issued under the Plans vests over specified periods, generally three years after the date of grant. The vesting of performance stock, issued under the Plans, is subject to service and performance conditions.

### Stock Options

As of March 31, 2014, there were approximately \$2.0 million of total unrecognized compensation costs related to unvested stock options. These costs are expected to be recognized over a weighted-average period of approximately two years. There were 56,727 stock options granted during the three months ended March 31, 2014.

### Awards of Restricted Stock, Performance Stock and Contract Stock

Performance stock, restricted stock and contract stock awards generally have requisite service periods of three years. Performance stock awards are subject to graded vesting conditions and the Company expenses their fair value over the requisite service period. The Company expenses the fair value of restricted stock and contract stock awards on a straight-line basis over the vesting period or requisite service period, whichever is shorter. As of March 31, 2014,

there were approximately \$21.5 million of total unrecognized compensation costs related to these unvested awards. The Company expects to recognize these costs over a weighted-average period of approximately two years. The Company granted 204,397 restricted stock awards/stock units and 74,424 performance shares during the three months ended March 31, 2014.

The Company has no formal policy related to the repurchase of shares for the purpose of satisfying stock-based compensation obligations.

The Company also maintains an Employee Stock Purchase Plan (the "ESPP"), which provides eligible employees with the opportunity to acquire shares of common stock at periodic intervals by means of accumulated payroll deductions. The ESPP is a non-compensatory plan based on its terms.

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 NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (continued)

## 8. TREASURY STOCK

On October 23, 2012, the Company's Board of Directors authorized a repurchase of up to \$75.0 million of its outstanding common stock through December 2014. The Company has not repurchased any of its outstanding shares of common stock during the three month periods ended March 31, 2014 and 2013.

As of March 31, 2014, there remained \$75.0 million available for repurchases under this authorization.

## 9. RETIREMENT BENEFIT PLANS

The Company maintains defined benefit pension plans that cover employees in its manufacturing plants located in Andover, United Kingdom (the "UK Plan") and Tuttlingen, Germany (the "Germany Plan"). The Company closed the Tuttlingen, Germany plant in December 2005. The Company did not terminate the Germany Plan, and the Company remains obligated for the accrued pension benefits related to this plan. Effective March 31, 2011, the Company froze the benefits due to the participants of the UK Plan in their entirety; this curtailment resulted in a \$0.3 million reduction in the projected benefit obligations which the Company recorded on that date. The plans cover certain current and former employees.

Net periodic benefit costs for the Company's defined benefit pension plans included the following amounts:

|                         | Three Months Ended March 31, |        |
|-------------------------|------------------------------|--------|
|                         | 2014                         | 2013   |
|                         | (In thousands)               |        |
| Interest cost           | \$ 163                       | \$ 137 |
| Return on plan assets   | (134                         | ) (100 |
| Net period benefit cost | \$ 29                        | \$ 37  |

The Company made \$0.3 million and \$0.2 million of contributions to its defined benefit pension plans during the three months ended March 31, 2014 and 2013, respectively.

## 10. INCOME TAXES

The following table provides a summary of the Company's effective tax rate:

|                   | Three Months Ended March 31, |          |
|-------------------|------------------------------|----------|
|                   | 2014                         | 2013     |
|                   | (As adjusted)                |          |
| Reported tax rate | 44.5                         | % 23.7 % |

The Company's effective income tax rates for the three months ended March 31, 2014 and 2013 were 44.5% and 23.7%, respectively.

For the three months ended March 31, 2014, the increase in the income tax rate compared to the same period in 2013 was primarily the result of discrete state income tax audit settlements of \$0.6 million, as well as higher income within U.S.-based operations relative to foreign operations, which created an unfavorable effect on the effective tax rate. Additionally, the effective rate for the three months ended March 31, 2013 included an income tax benefit in France which is no longer available in 2014 because of a change in French tax law change that occurred on December 30, 2013.

For the three months ended March 31, 2013, the reduction in the income tax rate compared to the same period in 2012 was primarily the result of a change in the jurisdictional mix of year-to-date worldwide pretax income and a reinstatement of the Federal research and development credit. The Company recorded a benefit of \$0.9 million in the

first quarter of 2013 due to the extension of the Federal research credit by the American Taxpayer Relief Act which was signed into law at that time. The Company recorded a benefit of \$0.4 million in the first quarter of 2013 for the release of tax contingency reserves. This amount is offset by an expense of \$0.4 million due to a change in the German local tax rate, which was also effective that quarter.

The Company expects its effective income tax rate for the full year to be approximately 23% to 24%, resulting largely from the jurisdictional mix of pretax income in U.S.-based operations relative to foreign operations. The Company may revise this estimate in the future as additional information becomes available.

INTEGRA LIFESCIENCES HOLDINGS CORPORATION  
 NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (continued)

## 11. NET INCOME (LOSS) PER SHARE

Basic and diluted net income (loss) per share was as follows:

|   | Three Months Ended March 31,             |               |
|---|--|---------------|
|   | 2014                                     | 2013          |
|   | (In thousands, except per share amounts) |               |
|   |  | (as adjusted) |
| Basic net income (loss) per share:                            |  |               |
| Net income (loss)   | \$2,206                                  | \$(6,028 )    |
| Weighted average common shares outstanding                    | 32,275                                   | 27,796        |
| Basic net income (loss) per common share                      | \$0.07                                   | \$(0.22 )     |
| Diluted net income (loss) per share:                          |  |               |
| Net income (loss)   | \$2,206                                  | \$(6,028 )    |
| Weighted average common shares outstanding — Basic            | 32,275                                   | 27,796        |
| Effect of dilutive securities:                                |  |               |
| Stock options and restricted stock                            | 493                                      | —             |
| Weighted average common shares for diluted earnings per share | 32,768                                   | 27,796        |
| Diluted net income (loss) per common share                    | \$0.07                                   | \$(0.22 )     |

At March 31, 2014 and 2013, the Company had 1.4 million and 1.7 million of outstanding stock options, respectively. The Company also has warrants outstanding relating to its 2016 Notes at March 31, 2014 and 2013. Stock options, restricted stock and warrants are included in the diluted earnings per share calculation using the treasury stock method, unless the effect of including the stock options would be anti-dilutive. For the three months ended March 31, 2014, 0.2 million of anti-dilutive stock options were excluded from the diluted earnings per share calculation. For the three months ended March 31, 2013 all stock options, restricted stock and warrants were excluded from the diluted earnings per share calculation using the treasury stock method because of their anti-dilutive effect.

## 12. COMPREHENSIVE INCOME (LOSS)

Comprehensive income (loss) was as follows:

|  | Three Months Ended March 31, |               |
|--|------------------------------|---------------|
|  | 2014                         | 2013          |
|  | (In thousands)               |               |
|  |                              | (as adjusted) |
| Net income (loss)                                    | \$2,206                      | \$(6,028 )    |
| Foreign currency translation adjustment              | 819                          | (6,780 )      |
| Change in unrealized gain on derivatives, net of tax | 195                          | 296           |
| Pension liability adjustment, net of tax             | (14 )                        | —             |
| Comprehensive income (loss)                          | \$3,206                      | \$(12,512 )   |

INTEGRA LIFESCIENCES HOLDINGS CORPORATION  
 NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (continued)

Changes in Accumulated Other Comprehensive Income (Loss) by component between December 31, 2013 and March 31, 2014 are presented in the table below, net of tax:

|  | Gains and<br>(Losses) on<br>Cash Flow<br>Hedges<br>(In thousands) | Defined<br>Benefit<br>Pension<br>Items | Foreign<br>Currency<br>Items | Total    |
|--|---|--|------------------------------|----------|
| Beginning balance  | \$ (1,390 )   | \$ (2,287 )                            | \$ 4,604                     | \$ 927   |
| Other comprehensive income (loss) before reclassifications       | (62 )   | (14 )                                  | 819                          | 743      |
| Amounts reclassified from accumulated other comprehensive income | 257   | —                                      | —                            | 257      |
| Net current-period other comprehensive income (loss)             | 195   | (14 )                                  | 819                          | 1,000    |
| Ending balance   | \$ (1,195 )   | \$ (2,301 )                            | \$ 5,423                     | \$ 1,927 |

The reclassification adjustments out of Accumulated Other Comprehensive Income (Loss) during the three months ended March 31, 2014 were as follows:

| Details about Accumulated Other Comprehensive Income (Loss) Components | Amount Reclassified from Accumulated Other Comprehensive Income (Loss)<br>(In thousands) | Affected Line Item in the Statement where Net Income (Loss) is Presented |
|--|--|--|
| Gains and losses on cash flow hedges                                   |  |  |
| Interest rate swap   | \$ (451 )  | ) Interest (expense)   |
|  | (451 )   | ) Total before tax   |
|  | 194  | ) Tax (expense) or benefit   |
|  | \$ (257 )  | ) Net of tax   |

### 13. SEGMENT AND GEOGRAPHIC INFORMATION

The Company internally manages and reports the results of its businesses to its chief operating decision maker through five reportable segments. The five reportable segments and a description of their activities are described below:

The U.S. Neurosurgery segment sells a full line of products specifically for neurosurgery and critical care such as tissue ablation equipment, dural repair products, cerebral spinal fluid management devices, intracranial monitoring equipment, and cranial stabilization equipment.

The U.S. Instruments business sells more than 60,000 instrument patterns and surgical and lighting products to hospitals, surgery centers, and dental, podiatry, and veterinary offices.

The U.S. Extremities segment includes the U.S. Extremity reconstruction business, which includes such offerings as skin and wound repair, bone and joint fixation, implants in the upper and lower extremities, bone grafts and nerve and tendon repair.

The U.S. Spine and Other segment includes (i) the U.S. Spine business, which focuses on spinal fusion, spinal implants, and deformity correction, together with bone graft substitutes and other related medical devices that are used to enhance the repair and regeneration of bone in various types of orthopedic surgical procedures, and (ii) the Private Label business, which sells the Company's regenerative medicine and other products to strategic partners.

The International segment sells similar products to those discussed above, but are managed through the following geographies: (i) Europe, Middle East and Africa, and (ii) Central/South America, Asia-Pacific and Canada.

The Corporate and other category includes (i) various legal, finance, information systems, executive, and human resource functions, (ii) brand management, (iii) share-based compensation costs, and (iv) costs related to procurement, manufacturing operations and logistics for the Company's entire organization.

The operating results of the various reportable segments as presented are not comparable to one another because (i) certain operating segments are more dependent than others on corporate functions for unallocated general and administrative and/or operational

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INTEGRA LIFESCIENCES HOLDINGS CORPORATION  
 NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (continued)

manufacturing functions, and (ii) the Company does not allocate certain manufacturing costs and general and administrative costs to the operating segment results.

Net sales and profit by reportable segment for the three months ended March 31, 2014 and 2013 are as follows:

|                         | Three Months Ended March 31, |               |
|-------------------------|------------------------------|---------------|
|                         | 2014                         | 2013          |
|                         | (In thousands)               |               |
|                         |                              | (as adjusted) |
| Segment Net Sales       |                              |               |
| U.S. Neurosurgery       | \$54,383                     | \$38,996      |
| U.S. Instruments        | 36,720                       | 36,948        |
| U.S. Extremities        | 31,912                       | 31,361        |
| U.S. Spine and Other    | 41,067                       | 43,548        |
| International           | 50,977                       | 45,799        |
| Total revenues          | \$215,059                    | \$196,652     |
| Segment Profit          |                              |               |
| U.S. Neurosurgery       | \$27,788                     | \$17,768      |
| U.S. Instruments        | 10,481                       | 10,084        |
| U.S. Extremities        | 11,753                       | 10,791        |
| U.S. Spine and Other    | 11,977                       | 13,213        |
| International           | 17,212                       | 12,878        |
| Segment profit          | 79,211                       | 64,734        |
| Amortization            | (3,033                       | ) (3,551)     |
| Corporate and other     | (67,440                      | ) (63,373     |
| Operating income (loss) | \$8,738                      | \$(2,190)     |

Revenue by major product category consisted of the following:

|                | Three Months Ended March 31, |           |
|----------------|------------------------------|-----------|
|                | 2014                         | 2013      |
|                | (In thousands)               |           |
| Orthopedics    | \$87,239                     | \$90,260  |
| Neurosurgery   | 84,370                       | 63,185    |
| Instruments    | 43,450                       | 43,207    |
| Total Revenues | \$215,059                    | \$196,652 |

The Company attributes revenues to geographic areas based on the location of the customer. There are certain revenues managed by the various U.S. segments that are generated from non-U.S. customers and therefore are included in Europe and the Rest of World revenues below. Total revenue by major geographic area consisted of the following:

|                | Three Months Ended March 31, |           |
|----------------|------------------------------|-----------|
|                | 2014                         | 2013      |
|                | (In thousands)               |           |
| United States  | \$163,382                    | \$150,019 |
| Europe         | 25,324                       | 23,617    |
| Rest of World  | 26,353                       | 23,016    |
| Total Revenues | \$215,059                    | \$196,652 |





INTEGRA LIFESCIENCES HOLDINGS CORPORATION

NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (continued)

14. COMMITMENTS AND CONTINGENCIES

In consideration for certain technology, manufacturing, distribution, and selling rights and licenses granted to the Company, the Company has agreed to pay royalties on sales of certain products that we sell. The royalty payments that the Company made under these agreements were not significant for any of the periods presented.

The Company is subject to various claims, lawsuits and proceedings in the ordinary course of the Company's business, including claims by current or former employees, distributors and competitors and with respect to its products and product liability claims, lawsuits and proceedings, some of which have been settled by the Company. In the opinion of management, such claims are either adequately covered by insurance or otherwise indemnified, or are not expected, individually or in the aggregate, to result in a material adverse effect on our financial condition. However, it is possible that the Company's results of operations, financial position and cash flows in a particular period could be materially affected by these contingencies.

On June 6, 2012, the Company was contacted by the United States Attorney's Office for the District of New Jersey regarding the activities of sales representatives in a single region within our Extremities Reconstruction division. The U.S. Attorney's Office is investigating the activities of three sales representatives, one of whom was a supervisor until terminated by the Company for failure to cooperate with this investigation. The activities at issue pertain to alleged improper billing of products for extremities indications. The Company has been cooperating with the U.S. Attorney's Office on a voluntary basis and is not a subject or target of an investigation at this time. In cooperating with the U.S. Attorney's Office, the Company has responded to multiple government requests for documents and information; and in the fall of 2013 it responded to what the government currently indicated is its final request. Representatives of the Company met with the Assistant United States Attorney in charge of the matter and an agent from the Federal Bureau of Investigation on April 11, 2014, to discuss the matter, the behavior of the sales representatives in question, and the disposition of the matter as to the Company. The Company awaits word from the U.S. Attorney's Office as to the disposition of the matter as to the Company.

The Company accrues for loss contingencies when it is deemed probable that a loss has been incurred and that loss is estimable. The amounts accrued are based on the full amount of the estimated loss before considering insurance proceeds, and do not include an estimate for legal fees expected to be incurred in connection with the loss contingency. The Company consistently accrues legal fees expected to be incurred in connection with loss contingencies as those fees are incurred by outside counsel as a period cost.

15. SUBSEQUENT EVENT

On April 29, 2014, the Board of Directors (the "Board") of the Company appointed Glenn G. Coleman as Corporate Vice President of the Company effective as of May 2, 2014. In addition, on April 29, 2014, the Board of the Company appointed Mr. Coleman as Corporate Vice President, Chief Financial Officer and Principal Accounting Officer effective one business day after the Company files its Form 10-Q for the quarter ended March 31, 2014 with the Securities and Exchange Commission (the "SEC"), as early as May 2, 2014 and no later than May 13, 2014. At such time that Mr. Coleman commences as Chief Financial Officer, John B. Henneman, III will cease to serve as the Company's Chief Financial Officer and will then serve as Corporate Vice President, Chief Administrative Officer. At such time that Mr. Coleman commences as Principal Accounting Officer, Jerry Corbin will cease to serve as the Company's Principal Accounting Officer, but Mr. Corbin will still serve as Corporate Vice President, Corporate Controller. The Company expects to incur severance obligations pursuant to Mr. Henneman's employment agreement.

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

The following discussion and analysis of our financial condition and results of operations should be read in conjunction with our condensed consolidated financial statements and the related notes thereto appearing elsewhere in

this report and our consolidated financial statements for the year ended December 31, 2013 included in our Annual Report on Form 10-K.

We have made statements in this report which constitute forward-looking statements within the meaning of Section 27A of the Securities Act of 1933 and Section 21E of the Securities Exchange Act of 1934 (the "Exchange Act"). These forward-looking statements are subject to a number of risks, uncertainties and assumptions about the Company. Our actual results may differ materially from those anticipated in these forward-looking statements as a result of many factors, including but not limited to those set forth under the heading "Risk Factors" in our Annual Report on Form 10-K for the year ended December 31, 2013 and under the heading "Risk Factors" in this report. We undertake no obligation to publicly update or revise any forward-looking statements, whether as a result of new information, future events or otherwise.

You can identify these forward-looking statements by forward-looking words such as "believe," "may," "could," "will," "estimate," "continue," "anticipate," "intend," "seek," "plan," "expect," "should," "would" and similar expressions in this report.

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GENERAL

Integra is a world leader in medical technology focused on limiting uncertainty for surgeons so they can concentrate on providing the best patient care. Integra offers innovative solutions in orthopedic extremity surgery, neurosurgery, spine surgery, and reconstructive and general surgery.

We manage our business through a combination of product groups and geography, and accordingly, we report our financial results under five reportable segments - U.S. Instruments, U.S. Neurosurgery, U.S. Extremities, U.S. Spine and Other (which consists of our U.S. Spine and Private Label businesses) and International.

We present revenues in the following three product categories: Orthopedics, Neurosurgery and Instruments. Our orthopedics product group includes specialty metal implants for surgery of the extremities, shoulder and spine, orthobiologics products for repair and grafting of bone, dermal regeneration products and tissue-engineered wound dressings and nerve and tendon repair products. Our neurosurgery product group includes, among other things, dural grafts and dural sealants which are indicated for the repair of the dura mater, ultrasonic surgery systems for tissue ablation, cranial stabilization and brain retraction systems, systems for measurement of various brain parameters and devices used to gain access to the cranial cavity and to drain excess cerebrospinal fluid from the ventricles of the brain. Our instruments product group includes a wide range of specialty and general surgical and dental instruments and surgical lighting for sale to hospitals, outpatient surgery centers, and physician, veterinarian and dental practices. We manufacture many of our products in plants located in the United States, Puerto Rico, France, Germany, Ireland, the United Kingdom and Mexico. We also source most of our handheld surgical instruments and specialty metal and pyrocarbon implants through specialized third-party vendors.

In the United States, we have several sales channels. We sell orthopedics products through a large direct sales organization and through specialty distributors focused on their respective surgical specialties. Neurosurgery products are sold through directly employed sales representatives. Instruments products are sold through two sales channels, both directly and through distributors and wholesalers, depending on the customer call point. We sell in the international markets through a combination of a direct sales organization and distributors.

We also market certain products through strategic partners in the United States.

We aspire to be a multi-billion dollar diversified global medical technology company that helps patients by limiting uncertainty for medical professionals, and is a high quality investment for shareholders. We will achieve these goals by delivering on our Brand Promises to our customers worldwide and by becoming a top player in all markets in which we compete.

Our strategy is built around three pillars - optimize, execute and accelerate growth. These three pillars support our strategic initiatives to optimize our infrastructure, to deliver on our commitments through improved planning and communication, and to grow by introducing new products to the market through internal development, expanding geographically, and strategic acquisitions.

Acquisition of Confluent Surgical, Inc.

On January 15, 2014, we acquired all outstanding shares of Confluent Surgical, Inc., ("Confluent Surgical") - including its surgical sealant and adhesion barrier product lines - from Covidien Group S.a.r.l, ("Covidien") for an aggregate purchase price of \$255.9 million. The purchase price is comprised of an initial cash payment to Covidien of \$231.0 million upon the closing of the transaction, a separate prepayment of \$4.0 million made under a transitional supply agreement with an affiliate of Covidien, and contingent consideration with an acquisition date fair value of \$20.9 million. The purchase agreement includes a potential maximum undiscounted contingent consideration of \$30.0 million which consists of: \$25.0 million upon obtaining certain U.S. governmental approvals and \$5.0 million upon obtaining certain European governmental approvals, both related to the completion of the transition of the Confluent Surgical business.

The transitional supply agreement secures the supply of the acquired products from an affiliate of Covidien until the earlier of (i) the time that the transition of the Confluent Surgical business as discussed above is complete, or (ii) the fifth anniversary of the effective date of the agreement; the agreement also contains an option to extend for another two years by providing written notice at least 180 days prior to the end of the initial five-year period. This agreement contains financial incentives to the affiliate of Covidien for the timely supply of products each fiscal quarter through the third anniversary of the agreement. The prices paid under the supply agreement are essentially flat through the

third anniversary of the agreement, and then increase significantly each of the following three years. We also entered into a transition services agreement with an affiliate of Covidien at the closing for services such as: customer service, accounting and information technology management; clinical and regulatory affairs; manufacturing transition services; and other functions.

This acquisition complements our global neurosurgery growth strategy aimed at providing a broader set of solutions for surgical procedures in the head.

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### Change in Accounting Treatment for the Medical Device Excise Tax

In the first quarter of 2014, the Company changed its method of accounting for the medical device excise tax ("MDET"). Prior to the change the Company recorded the MDET in inventory at the time of the first sale and then recognized the tax in cost of goods sold when the medical device was sold to the ultimate customer. Under the new method, the MDET will be recorded in selling, general and administrative expenses in the period the first sale occurs, which could be an intercompany sale.

The Company believes that this change in accounting principle is preferable as the new method provides a better comparison with the Company's industry peers, the majority of which expense the MDET at the time of the first sale.

The medical device excise tax applies to sales beginning January 1, 2013; therefore, only 2013 financial results were affected by this change. The cumulative effect of the change in the prior years is included in retained earnings as of December 31, 2013 and the comparative period for the three months ended March 31, 2013. The financial impact of this change on 2013 has been incorporated into the amounts presented throughout this Form 10-Q and the impact on the first quarter of 2013 is discussed in detail in Note 1 to the condensed consolidated financial statements. For a full reconciliation of the impact on the 2013 historical quarterly financial results, see the investor presentations on the Investor Relations homepage of Integra's website at [investor.integralife.com](http://investor.integralife.com).

### Management Changes

On April 29, 2014, the Board of Directors (the "Board") of the Company appointed Glenn G. Coleman as Corporate Vice President of the Company effective as of May 2, 2014. In addition, on April 29, 2014, the Board of the Company appointed Mr. Coleman as Corporate Vice President, Chief Financial Officer and Principal Accounting Officer effective one business day after the Company files its Form 10-Q for the quarter ended March 31, 2014 with the Securities and Exchange Commission (the "SEC"), as early as May 2, 2014 and no later than May 13, 2014. At such time that Mr. Coleman commences as Chief Financial Officer, John B. Henneman, III will cease to serve as the Company's Chief Financial Officer and will then serve as Corporate Vice President, Chief Administrative Officer. At such time that Mr. Coleman commences as Principal Accounting Officer, Jerry Corbin will cease to serve as the Company's Principal Accounting Officer, but Mr. Corbin will still serve as Corporate Vice President, Corporate Controller. The Company expects to incur severance obligations pursuant to Mr. Henneman's employment agreement.

## RESULTS OF OPERATIONS

### Executive Summary

Net income for the three months ended March 31, 2014, was \$2.2 million, or \$0.07 per diluted share as compared with a net loss of \$6.0 million or \$0.22 per diluted share for the three months ended March 31, 2013.

The results of operations for the three months ended March 31, 2013 were adversely affected by a voluntary recall of certain collagen-based products manufactured in our Añasco, Puerto Rico facility. This recall resulted in lost revenues, increased sales reserves, inventory scrap, and costs of remediation at the facility which continued throughout 2013. We resolved the issues relating to the recall by the beginning of the first quarter of 2014, and saw improved margins from DuraSeal revenues; however, the costs associated with closing the Confluent Surgical acquisition and the related integration effort impacted our 2014 financial results.

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Income before taxes includes the following special charges:

|  | Three Months Ended March 31, |          |
|--|------------------------------|----------|
|  | 2014                         | 2013     |
|  | (In thousands)               |          |
| Global ERP implementation charges                | \$6,100                      | \$6,149  |
| Structural optimization charges                  | 2,960                        | 3,408    |
| Manufacturing facility remediation costs         | 143                          | 2,125    |
| Certain expenses associated with product recalls | —                            | 1,279    |
| Certain employee termination charges             | 681                          | —        |
| Acquisition-related charges                      | 3,753                        | 388      |
| Impairment charges                               | 600                          | —        |
| Convertible debt non-cash interest               | 1,667                        | 1,610    |
| Total  | \$15,904                     | \$14,959 |

The items reported above are reflected in the condensed consolidated statements of operations as follows:

|                                     | Three Months Ended March 31, |          |
|-------------------------------------|------------------------------|----------|
|                                     | 2014                         | 2013     |
|                                     | (In thousands)               |          |
| Cost of goods sold                  | \$2,877                      | \$4,501  |
| Selling, general and administrative | 11,360                       | 8,848    |
| Interest expense                    | 1,667                        | 1,610    |
| Total                               | \$15,904                     | \$14,959 |

We typically define special charges as items for which the amounts and/or timing of such expenses may vary significantly from period to period, depending upon our acquisition, integration and restructuring activities, and for which the amounts are non-cash in nature, or for which the amounts are not expected to recur at the same magnitude as we implement certain tax planning strategies. We believe that given our ongoing strategy of seeking acquisitions, our continuing focus on rationalizing our existing manufacturing and distribution infrastructure and our continuing review of various product lines in relation to our current business strategy, certain of the special charges discussed above could recur with similar materiality in the future. In 2010 we began investing significant resources in the global implementation of a single enterprise resource planning system. We began capitalizing certain costs for the project starting in 2011 and will continue to do so during 2014.

We believe that the separate identification of these special charges provides important supplemental information to investors regarding financial and business trends relating to our financial condition and results of operations. Investors may find this information useful in assessing comparability of our operating performance from period to period, the business model objectives that management has established, and other companies in our industry. We provide this information to investors so that they can analyze our operating results in the same way that management does and to use this information in their assessment of our core business and valuation of Integra.

#### Update on Remediation Activities

The FDA inspected our neurosurgery manufacturing facility in Andover, England in June 2012. On November 5, 2012, we received a warning letter dated November 1, 2012 related to quality systems issues at that facility. The warning letter identified violations related to corrective and preventative actions, process validations, internal quality audits, and internal review of the suitability and effectiveness of the quality system at defined intervals. Since the conclusion of the FDA inspection in June 2012, we have undertaken significant efforts to remediate the observations that the FDA has made and continue to do so. We have provided the FDA with monthly status reports and are working cooperatively with the FDA to resolve any outstanding issues.

On February 14, 2013, we received a warning letter from the FDA relating to quality systems issues at our manufacturing facility located in Añasco, Puerto Rico. The letter resulted from an inspection conducted at that facility

during October and November 2012. On February 15, 2013 we stopped distribution of our collagen products manufactured in the Añasco facility in order to confirm that we had successfully validated all such products and engaged a third-party consultant having appropriate quality system regulations expertise to confirm such validations. On February 22, 2013 the third-party consultant certified the completeness of such validations and we resumed distribution of collagen products from the Añasco, Puerto Rico facility.



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We met with the Office of Compliance at the Center for Devices and Radiological Health on March 26, 2013. We presented our plans for both immediate remediation and our corporate plan for the development and implementation of a single Quality System for the entire Company. We have engaged former FDA professionals as third party consultants to work with us on our remediation plans. We also met with the Office of Compliance at the FDA San Juan, Puerto Rico office to discuss the remediation plans at the Añasco, Puerto Rico facility. We have prioritized senior level quality and regulatory staff to address the quality system improvement plans at all of our facilities. On October 24, 2013, the United States Food and Drug Administration began an inspection of the Añasco facility. At the end of the inspection on November 26, 2013, the FDA issued a new Form 483 with six additional observations relating to Corrective and Preventative Action (“CAPA”), quality system procedures and instructions, procedures pertaining to complaints, procedures pertaining to checking and maintaining equipment, procedures for finished device acceptance and procedures to prevent contamination of equipment or products. These observations did not impact our ability to manufacture and sell product. On March 4, 2014 we met with the FDA Office of Compliance, San Juan, Puerto Rico District to discuss the Corrective Action and remediation plan at the Añasco, Puerto Rico facility. We had committed to several corporate-wide corrections and additional site corrections and will continue to complete these within the timeframes provided to the FDA in order to remediate the observations that the FDA has made.

Over the past several years we have undertaken significant efforts to remediate the observations that the FDA has made and have been working on improving and revising our quality systems. During the three months ended March 31, 2014 and 2013, we incurred \$0.1 million and \$2.1 million in remediation activities expenses, respectively, consisting of consulting expenses and other work activities required to complete our remediation activities, and we expect to incur similar types of expenses during 2014, albeit at lower spending levels compared to 2013. We will provide periodic status reports to the FDA and work cooperatively with the agency to resolve any outstanding issues.

Revenues and Gross Margin on Product Revenues

Our revenues and gross margin on product revenues were as follows:

|  | Three Months Ended March 31, |           |   |
|--|------------------------------|-----------|---|
|  | 2014                         | 2013      |   |
| Segment Net Sales                              | (In thousands)               |           |   |
| U.S. Neurosurgery                              | \$54,383                     | \$38,996  |   |
| U.S. Instruments                               | 36,720                       | 36,948    |   |
| U.S. Extremities                               | 31,912                       | 31,361    |   |
| U.S. Spine and Other                           | 41,067                       | 43,548    |   |
| International *                                | 50,977                       | 45,799    |   |
| Total revenue                                  | 215,059                      | 196,652   |   |
| Cost of goods sold                             | 82,383                       | 79,612    |   |
| Gross margin on total revenues                 | \$132,676                    | \$117,040 |   |
| Gross margin as a percentage of total revenues | 61.7                         | % 59.5    | % |

\* The Company attributes revenue to geographic areas based on the location of the customer. There are certain revenues managed by the various U.S. segments above that are generated from non-U.S. customers and therefore included in Europe and the Rest of World revenues.

### Three Months Ended March 31, 2014 as Compared to Three Months Ended March 31, 2013

#### Revenues and Gross Margin

For the three months ended March 31, 2014 total revenues increased by \$18.4 million to \$215.1 million from \$196.7 million for the same period in 2013.

U.S. Neurosurgery revenues were \$54.4 million, an increase of 39% from the prior-year period. The increase largely resulted from the impact of the DuraSeal product sales arising out of the Confluent Surgical acquisition, which were \$10.6 million during the quarter. We also saw increases from our dural repair franchise, which was up against a soft comparable as a result of the recall in 2013, and neuro critical care and tissue ablation, both of which benefited from

strong sales of capital equipment in the quarter.

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U.S. Instruments revenues were \$36.7 million, a decrease of 1% from the prior-year period. The decrease resulted primarily from product discontinuances. The decline was offset in part by increases in alternate site, acute care, and lighting revenues.

U.S. Extremities revenues were \$31.9 million, an increase of 2% from the prior-year period. This increase resulted primarily from dermal and wound care products, and from our shoulder business due to the launch of new shoulder lines in the latter-half of 2013. We saw some softness in our lower extremity and nerve franchises during the quarter.

U.S. Spine and Other revenues, which include our spine hardware, orthobiologics and private label products, were \$41.1 million, a 6% decrease from the prior-year period. Our spine hardware product sales continued to decline compared to the prior year, but we expect positive comparisons in this category for the remainder of the year. Orthobiologics sales were up low-single digits for the quarter. Sales of our private label products were down from the prior-year period primarily due to the loss of business to certain customers because of the prolonged recall-related supply disruptions last year.

International segment revenues were \$51.0 million, an increase of 11% from the prior-year period. These increases primarily resulted from the incremental impact of DuraSeal product sales of \$3.6 million during the quarter, Duragen sales as we recover from the recall in 2013, and skin and wound sales in both regions. Foreign currency had a negligible impact on our sales in the current quarter.

Gross margin increased to \$132.7 million for the three-month period ended March 31, 2014 from \$117.0 million for the same period last year. Gross margin as a percentage of total revenue increased to 61.7% for the first quarter of 2014 from 59.5% for the same period last year. The increase in gross margin percentage resulted primarily from decreased remediation costs at our manufacturing facilities. Throughout 2013 we invested in improvements to quality systems across our organization as a result of prior FDA findings. In 2014, we are seeing our spending return to a more normal level since those initial remediation efforts are largely complete. Our 2014 gross margin also saw improvement from product recall expenses in 2013 that did not recur, improved margins from the sales of Duragen products no longer subject to the recall, and margins on the sales of DuraSeal products.

We expect our consolidated gross margin percentage for the full year 2014 to be between 61% and 62%, up compared to 2013. We expect our gross margin will see increases from improved product mix - with more sales in the orthopedics and DuraSeal lines - and improvements in yield as we resolve FDA inspection issues.

Operating Expenses

The following is a summary of operating expenses as a percent of total revenues:

|                                     | Three Months Ended March 31, |        |   |
|-------------------------------------|------------------------------|--------|---|
|                                     | 2014                         | 2013   |   |
| Research and development            | 5.8                          | % 6.5  | % |
| Selling, general and administrative | 50.4                         | % 52.4 | % |
| Intangible asset amortization       | 1.4                          | % 1.8  | % |
| Total operating expenses            | 57.6                         | % 60.7 | % |

Total operating expenses, which consist of research and development expenses, selling, general and administrative expenses, and amortization expense, increased \$4.7 million, or 4%, to \$123.9 million in the three months ended March 31, 2014, compared to \$119.2 million in the same period last year.

Research and development expenses in the first quarter of 2014 decreased \$0.1 million compared to the same period last year, resulting from lower product development spending, which, in turn, was driven by headcount reductions, and lower overall project costs. We target full-year 2014 spending on research and development to be approximately 6% of total revenues.

Selling, general and administrative expenses in the first quarter of 2014 increased by \$5.4 million to \$108.3 million compared to \$103.0 million in the same period last year. Selling and marketing expenses increased by \$1.1 million, primarily resulting from higher commissions related to the DuraSeal sales, and overall sales increases in general.

General and administrative costs were up \$4.2 million as a result of bank fees paid in connection with the Confluent Surgical acquisition, fees for the related transitional services agreement, and higher licensing fees related to our ERP implementation.

Amortization expense in the first quarter of 2014 was \$3.0 million compared to \$3.6 million in the same period last year. The decrease resulted primarily from certain non-technology intangible assets becoming fully amortized in 2013.

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## Non-Operating Income and Expenses

The following is a summary of non-operating income and expenses:

|                        | Three Months Ended March 31, |          |
|------------------------|------------------------------|----------|
|                        | 2014                         | 2013     |
|                        | (In thousands)               |          |
| Interest income        | \$62                         | \$63     |
| Interest expense       | (5,142                       | ) (4,800 |
| Other income (expense) | 317                          | (974     |

## Interest Income and Interest Expense

Interest expense in the three months ended March 31, 2014 increased by \$0.3 million primarily as a result of additional borrowings under our credit facility to fund the Confluent Surgical acquisition, partially offset by capitalization of interest expense in connection with our construction-in-progress. Our reported interest expense for the three-month periods ended March 31, 2014 and 2013 includes non-cash interest related to the accounting for convertible securities of \$1.7 million and \$1.6 million, respectively. Interest income was negligible for the three months ended March 31, 2014.

## Other Income (Expense)

Other income for the first quarter of 2014 was primarily attributable to an employment assistance grant received from Ireland. Other expense for the first quarter of 2013 was primarily attributable to a write off of \$1.5 million for a capital expenditure project not placed into service offset by foreign exchange gains on intercompany balances.

## Income Taxes

|                                   | Three Months Ended March 31, |          |
|-----------------------------------|------------------------------|----------|
|                                   | 2014                         | 2013     |
|                                   | (In thousands)               |          |
| Income (loss) before income taxes | \$3,975                      | \$(7,901 |
| Income tax expense (benefit)      | 1,769                        | (1,873   |
| Effective tax rate                | 44.5                         | % 23.7   |

Our effective income tax rates for the three months ended March 31, 2014 and 2013 were 44.5% and 23.7%, respectively. For the three months ended March 31, 2014, the increase in the income tax rate compared to the same period in 2013 resulted from discrete state income tax audit settlements of \$0.6 million, as well as higher income within U.S.-based operations relative to foreign operations, which created an unfavorable effect on the effective tax rate. Additionally, the effective rate for the three months ended March 31, 2013 included an income tax benefit in France which is no longer available in 2014 because of a change in French tax law that occurred on December 30, 2013.

For the three months ended March 31, 2013, the reduction in the income tax rate compared to the same period in 2012 was primarily the result of a change in the jurisdictional mix of year-to-date worldwide pretax income and a reinstatement of the Federal research and development credit. The Company recorded a benefit of \$0.9 million in the first quarter of 2013 due to the extension of the Federal research credit by the American Taxpayer Relief Act which was signed into law at that time. The Company recorded a benefit of \$0.4 million in the first quarter of 2013 for the release of tax contingency reserves. This amount is offset by an expense of \$0.4 million due to a change in the German local tax rate, which was also effective that quarter.

We expect that our effective income tax rate for the full year to be approximately 23% to 24% resulting largely from the jurisdictional mix of pretax income in U.S.-based operations relative to foreign operations. We may revise this estimate in the future as additional information becomes available.

The effective tax rate may vary from period to period depending on, among other factors, the geographic and business mix of taxable earnings and losses, tax planning and settlements with various taxing authorities. We consider these factors and others, including our history of generating taxable earnings, in assessing our ability to realize deferred tax assets on a quarterly basis.

While it is often difficult to predict the final outcome or the timing of resolution of any particular matter with the various Federal, state and foreign tax authorities, we believe that our reserves reflect the most probable outcome of known tax contingencies.

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Settlement of any particular issue would usually require the use of cash. Favorable resolution would be recognized as a reduction to our annual effective tax rate in the year of resolution. The tax reserves are presented in the balance sheet within other liabilities, except for amounts relating to items we expect to pay in the coming year which would be classified as current income taxes payable.

**GEOGRAPHIC PRODUCT REVENUES AND OPERATIONS**

We attribute revenues to geographic areas based on the location of the customer. There are certain revenues managed by the various U.S. segments that are generated from non-U.S. customers and therefore included in Europe and the Rest of World revenues below. Total revenue by major geographic area consisted of the following:

|                | Three Months Ended March 31, |           |
|----------------|------------------------------|-----------|
|                | 2014                         | 2013      |
|                | (In thousands)               |           |
| United States  | \$163,382                    | \$150,019 |
| Europe         | 25,324                       | 23,617    |
| Rest of World  | 26,353                       | 23,016    |
| Total Revenues | \$215,059                    | \$196,652 |

Domestic revenues increased to \$163.4 million, or 76% of total revenues, for the three months ended March 31, 2014 from \$150.0 million, or 76% of total revenues, for the three months ended March 31, 2013. International revenues increased to \$51.7 million from \$46.6 million in the prior-year period, an increase of 11%. Foreign exchange rate fluctuations had a negligible impact on our sales in the current quarter.

We generate significant revenues outside the United States, a portion of which are U.S. dollar-denominated transactions conducted with customers who generate revenue in currencies other than the U.S. dollar. As a result, currency fluctuations between the U.S. dollar and the currencies in which those customers do business could have an impact on the demand for our products in foreign countries.

Local economic conditions, regulatory compliance or political considerations, the effectiveness of our sales representatives and distributors, local competition and changes in local medical practice all may combine to affect our sales into markets outside the United States.

**LIQUIDITY AND CAPITAL RESOURCES****Cash and Marketable Securities**

We had cash and cash equivalents totaling approximately \$129.0 million and \$120.6 million at March 31, 2014 and December 31, 2013, respectively. At March 31, 2014, our non-U.S. subsidiaries held approximately \$102.3 million of cash and cash equivalents that are available for use by our operations outside of the United States. If these funds were repatriated to the United States, or used for United States operations, certain amounts could be subject to tax in the United States for the incremental amount in excess of the foreign tax paid.

**Cash Flows**

|  | Three Months Ended March 31, |           |
|--|------------------------------|-----------|
|  | 2014                         | 2013      |
|  | (In thousands)               |           |
| Net cash provided by operating activities            | \$11,254                     | \$7,846   |
| Net cash used in investing activities                | (246,335                     | ) (13,087 |
| Net cash provided by financing activities            | 243,174                      | 257       |
| Effect of exchange rate fluctuations on cash         | 331                          | (2,263    |
| Net increase (decrease) in cash and cash equivalents | \$8,424                      | \$(7,247  |





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In 2014, we anticipate that our principal uses of cash will include between \$45.0 million and \$55.0 million on capital expenditures primarily for our continued expansion of regenerative medicine manufacturing capacity, support and maintenance in our existing plants, our enterprise resource planning system implementation, and additions to our instrument kits used in sales of orthopedic products. Additionally, we will continue to build inventories in preparation for our facilities consolidations expected to occur in the latter half of 2014.

### Cash Flows Provided by Operating Activities

We generated operating cash flows of \$11.3 million and \$7.8 million for the three months ended March 31, 2014 and 2013, respectively.

Operating cash flows for the three months ended March 31, 2014 benefited from an increase in net income of \$8.2 million compared to the same period in 2013. Changes in working capital decreased cash flows for the three months ended March 31, 2014 by approximately \$8.8 million. Among the changes in working capital, accounts receivable provided \$5.7 million of cash, inventory used \$8.5 million of cash, prepaid expenses and other current assets used \$1.6 million of cash, and accounts payable, accrued expenses and other current liabilities used \$4.4 million of cash. Operating cash flow for the three months ended March 31, 2013 was negatively impacted by the net income decrease of \$12.7 million compared to the same period in 2012. Changes in working capital decreased cash flows by approximately \$2.1 million. Among the changes in working capital, accounts receivable provided \$2.1 million of cash, inventory used \$6.7 million of cash, prepaid expenses and other current assets provided \$2.7 million of cash, and accounts payable, accrued expenses and other current liabilities used \$0.4 million of cash.

### Cash Flows Used in Investing Activities

During the three months ended March 31, 2014, we paid \$235.0 million for the acquisition of Confluent Surgical, and \$11.3 million for capital expenditures, most of which was directed to the expansion of our regenerative medicine production capacity and global enterprise system implementation.

During the three months ended March 31, 2013, we paid \$10.9 million for capital expenditures, most of which was directed to the expansion of our regenerative medicine production capacity and global enterprise system implementation, and \$2.8 million for the acquisition of Tarsus Medical, Inc.

### Cash Flows Provided by Financing Activities

Our principal sources of cash for financing activities in the three months ended March 31, 2014 were \$235.0 million of borrowings under our Senior Credit Facility to fund the Confluent Surgical acquisition, and stock option exercises of \$7.8 million.

Our principal sources of cash for financing activities in the three months ended March 31, 2013 were \$0.2 million from stock option exercises.

### Working Capital

At March 31, 2014 and December 31, 2013, working capital was \$422.9 million and \$401.8 million, respectively.

### Amended and Restated Senior Credit Agreement

On August 10, 2010, the Company entered into an amended and restated credit agreement (the "Senior Credit Facility") with a syndicate of lending banks and further amended the Senior Credit Facility on June 8, 2011 (the "2011 Amendment"). The 2011 Amendment increased the revolving credit component from \$450.0 million to \$600.0 million and eliminated the \$150.0 million term loan component that previously existed under the Senior Credit Facility, allows the Company to further increase the size of the revolving credit component by an aggregate of \$200.0 million with additional commitments, provides the Company with decreased borrowing rates and annual commitment fees, and provides more favorable financial covenants. The 2011 Amendment extended the Senior Credit Facility's maturity date from August 10, 2015 to June 8, 2016.

The Senior Credit Facility is collateralized by substantially all of the assets of the Company's U.S. subsidiaries, excluding intangible assets. The Senior Credit Facility is subject to various financial and negative covenants and at March 31, 2014, the Company was in compliance with all such covenants.

On May 11, 2012, the Company entered into an amendment to the Senior Credit Facility. The amendment modified certain financial and negative covenants as disclosed in Note 5 to the Financial Statements, the effect of which was to increase the Company's capacity to borrow.



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On June 21, 2013, the Company entered into an amendment to the Senior Credit Facility. The amendment provides for an increase to the Company's Maximum Consolidated Total Leverage Ratio and permits the addition of certain costs and expenses in the calculation of the consolidated EBIDTA as disclosed in Note 5 to the Financial Statements. There were no other changes as a result of the second amendment. In connection with the June 21, 2013 amendment, the Company capitalized \$1.1 million in incremental financing costs.

Borrowings under the Senior Credit Facility currently bear interest, at the Company's option, at a rate equal to (i) the Eurodollar Rate (as defined in the Senior Credit Facility, which definition has not changed) in effect from time to time plus the applicable rate (ranging from 1.00% to 1.75%) or (ii) the highest of (x) the weighted average overnight Federal funds rate, as published by the Federal Reserve Bank of New York, plus 0.5%, (y) the prime lending rate of Bank of America, N.A. or (z) the one-month Eurodollar Rate plus 1.0%. The applicable rates are based on the Company's Consolidated Total Leverage Ratio (defined as the ratio of (a) consolidated funded indebtedness less cash in excess of \$40 million that is not subject to any restriction of the use or investment thereof ("net debt") to (b) consolidated EBITDA) at the time of the applicable borrowing. The Company will also pay an annual commitment fee (ranging from 0.15% to 0.30%, based on the Company's consolidated total leverage ratio) on the daily amount by which the revolving credit facility exceeds the outstanding loans and letters of credit under the credit facility.

We plan to utilize the Senior Credit Facility for working capital, capital expenditures, share repurchases, acquisitions, debt repayments and other general corporate purposes. At March 31, 2014 and December 31, 2013, there was \$421.9 million and \$186.9 million, respectively, outstanding under the Senior Credit Facility at a weighted average interest rate of 1.7% and 2.0%, respectively. The Company considers the balance to be long-term in nature based on its current intent and ability to repay the borrowing outside of the next twelve-month period.

At March 31, 2014, there was approximately \$178.1 million available, subject to certain limitations, for borrowing under the Senior Credit Facility.

#### Convertible Debt and Related Hedging Activities

We pay interest each June 15 and December 15 on our \$230.0 million senior convertible notes due December 2016 ("2016 Notes") at an annual interest rate of 1.625%.

The 2016 Notes are senior, unsecured obligations of Integra, and are convertible into cash and, if applicable, shares of our common stock based on an initial conversion rate, subject to adjustment, of 17.4092 shares per \$1,000 principal amount of 2016 Notes (which represents an initial conversion price of approximately \$57.44 per share). We expect to satisfy any conversion of the 2016 Notes with cash up to the principal amount pursuant to the net share settlement mechanism set forth in the respective indenture and, with respect to any excess conversion value, with shares of our common stock. The 2016 Notes are convertible only in the following circumstances: (1) if the closing sale price of our common stock exceeds 150% of the conversion price during a period as defined in the applicable indenture; (2) if the average trading price per \$1,000 principal amount of the 2016 Notes is less than or equal to 98% of the average conversion value of the 2016 Notes during a period as defined in the applicable indenture; (3) at any time on or after June 15, 2016; or (4) if specified corporate transactions occur. The issue price of the 2016 Notes was equal to their face amounts, which is also the amount holders are entitled to receive at maturity if the 2016 Notes are not converted. None of these conditions existed with respect to the 2016 Notes; therefore the 2016 Notes are classified as long-term. In connection with the issuance of the 2016 Notes, we entered into call transactions and warrant transactions, primarily with affiliates of the initial purchasers of the 2016 Notes (the "hedge participants"). The cost of the call transactions to us was approximately \$42.9 million for the 2016 Notes. We received approximately \$28.5 million of proceeds from the warrant transactions for the 2016 Notes. The call transactions involved our purchasing call options from the hedge participants, and the warrant transactions involved us selling call options to the hedge participants with a higher strike price than the purchased call options. The initial strike price of the call transactions is approximately \$57.44 for the 2016 Notes, subject to anti-dilution adjustments. The initial strike price of the warrant transactions is approximately \$70.05 for the 2016 Notes, in each case subject to customary anti-dilution adjustments.

We may from time to time seek to retire or purchase a portion of our outstanding 2016 Notes through cash purchases and/or exchanges for equity securities, in open market purchases, privately negotiated transactions or otherwise. Such repurchases or exchanges, if any, will depend on prevailing market conditions, our liquidity requirements, contractual restrictions and other factors. Under certain circumstances, the call options associated with any repurchased 2016

Notes may terminate early, but only with respect to the number of 2016 Notes that cease to be outstanding. The amounts involved may be material.

Share Repurchase Plan

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On October 23, 2012, our Board of Directors authorized a repurchase of up to \$75.0 million of outstanding common stock through December 2014. Shares may be repurchased either in the open market or in privately negotiated transactions. We repurchased no shares under this program during the first three months of 2014 and \$75.0 million remains available under the authorization.

**Dividend Policy**

We have not paid any cash dividends on our common stock since our formation. Our Senior Credit Facility limits the amount of dividends that we may pay. Any future determinations to pay cash dividends on our common stock will be at the discretion of our Board of Directors and will depend upon our financial condition, results of operations, cash flows and other factors deemed relevant by the Board of Directors.

**Capital Resources**

We believe that our cash and available borrowings under the Senior Credit Facility are sufficient to finance our operations and capital expenditures. The Company considers all such outstanding amounts to be long-term in nature based on its current intent and ability to repay the borrowings outside of the next twelve month period.

**Contractual Obligations and Commitments**

As of March 31, 2014, we were obligated to pay the following amounts under various agreements:

|                               | Total    | Less than 1<br>Year | 1-3 Years | 3-5 Years | More than 5<br>Years |
|-------------------------------|----------|---------------------|-----------|-----------|----------------------|
| Convertible Securities (1)    | \$ 230.0 | \$—                 | \$ 230.0  | \$—       | \$—                  |
| Revolving Credit Facility (2) | 421.9    | —                   | 421.9     | —         | —                    |
| Interest (3)                  | 11.2     | 3.7                 | 7.5       | —         | —                    |
| Employment Agreements (4)     | 1.0      | 1.0                 | —         | —         | —                    |
| Operating Leases              | 65.8     | 11.5                | 17.1      | 9.6       | 27.6                 |
| Purchase Obligations          | 18.7     | 6.8                 | 5.6       | 6.3       | —                    |
| Other                         | 8.4      | 3.1                 | 3.1       | 1.0       | 1.2                  |
| Total                         | \$ 757.0 | \$ 26.1             | \$ 685.2  | \$ 16.9   | \$ 28.8              |

(1) The estimated debt service obligation of the senior convertible securities includes interest expense representing the amortization of the discount on the liability component of the senior convertible notes in accordance with the authoritative guidance. See Note 5 "Debt" of our condensed consolidated financial statements for additional information.

(2) The Company may borrow and make payments against the credit facility from time to time and considers all of the outstanding amounts to be long term based on its current intent and ability to repay the borrowing outside of the next twelve-month period.

(3) Interest is calculated on the convertible securities based on current interest rates paid by the Company. As the revolving credit facility can be repaid at any time, no interest has been included in the calculation.

(4) Amounts shown under Employment Agreements do not include compensation resulting from a change in control.

Excluded from the contractual obligations table is the liability for uncertain tax benefits, including interest and penalties, totaling \$3.0 million. This liability for uncertain tax benefits has been excluded because we cannot make a reliable estimate of the period in which the uncertain tax benefits may be realized.

**Off-Balance Sheet Arrangements**

There were no off-balance sheet arrangements during the three months ended March 31, 2014 that have or are reasonably likely to have, a current or future effect on our financial condition, changes in financial condition, revenues or expenses, results of operations, liquidity, capital expenditures or capital resources that is material to our interests.



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**OTHER MATTERS**

**Critical Accounting Estimates**

The critical accounting estimates included in our Annual Report on Form 10-K for the fiscal year ended December 31, 2013 have not materially changed, except as noted below.

**Inventory**

In the first quarter of 2014, the Company changed its method of accounting for the medical device excise tax (“MDET”). Prior to the change the Company recorded the MDET in inventory at the time of the first sale and then recognized the tax in cost of goods sold when the medical device was sold to the ultimate customer. Under the new method, the MDET will be recorded in selling, general and administrative expenses in the period the first sale occurs, which could be an intercompany sale.

The Company believes that this change in accounting principle is preferable as the new method provides a better comparison with the Company's industry peers, the majority of which expense the MDET at the time of the first sale.

The medical device excise tax applies to sales beginning January 1, 2013; therefore, only 2013 financial results were affected by this change. The cumulative effect of the change in the prior years is included in retained earnings as of December 31, 2013 and the comparative period for the three months ended March 31, 2013. The financial impact of this change on 2013 has been incorporated into the amounts presented throughout this Form 10-Q and the impact on the first quarter of 2013 is discussed in detail in Note 1 to the condensed consolidated financial statements. For a full reconciliation of the impact on the 2013 historical quarterly financial results, see the investor presentations on the Investor Relations homepage of Integra's website at [investor.integralife.com](http://investor.integralife.com).

**Recently Issued Accounting Standards**

On July 18, 2013, the FASB issued ASU No. 2013-11, Presentation of an Unrecognized Tax Benefit When a Net Operating Loss Carryforward, a Similar Tax Loss, or a Tax Credit Carryforward Exists. This updated guidance requires an unrecognized tax benefit to be presented in the financial statements as a reduction to a deferred tax asset for a net operating loss carryforward, similar tax loss, or a tax credit carryforward. To the extent the tax benefit is not available at the reporting date under the governing tax law or if the entity does not intend to use the deferred tax asset for such purpose, the unrecognized tax benefit should be presented as a liability and not combined with deferred tax assets. This ASU is effective for fiscal years and interim periods within those years beginning after December 15, 2013 for public entities. Early adoption is permitted. The amendments are to be applied to all unrecognized tax benefits that exist as of the effective date and may be applied retrospectively to each prior reporting period presented. The standard adoption does not have a material impact on the Company's financial statements.

In April 2014, the FASB issued amendments to guidance for reporting discontinued operations and disposals of components of an entity. The amended guidance requires that a disposal representing a strategic shift that has (or will have) a major effect on an entity's financial results or a business activity classified as held for sale should be reported as discontinued operations. The amendments also expand the disclosure requirements for discontinued operations and add new disclosures for individually significant dispositions that do not qualify as discontinued operations. The amendments are effective prospectively for fiscal years, and interim reporting periods within those years, beginning after December 15, 2014 (early adoption is permitted only for disposals that have not been previously reported). The implementation of the amended guidance is not expected to have a material impact on our consolidated financial position or results of operations.

**ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK**

We are exposed to various market risks, including changes in foreign currency exchange rates and interest rates that could adversely affect our results of operations and financial condition. To manage the volatility relating to these typical business exposures, we may enter into various derivative transactions when appropriate. We do not hold or issue derivative instruments for trading or other speculative purposes.

Foreign Currency Exchange and Other Rate Risks

We operate on a global basis and are exposed to the risk that changes in foreign currency exchange rates could adversely affect our financial condition, results of operations and cash flows. We are primarily exposed to foreign currency exchange rate risk with



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respect to transactions and net assets denominated in euros, Swiss francs, British pounds, Canadian dollars, Australian dollars and Japanese yen. We manage the foreign currency exposure centrally, on a combined basis, which allows us to net exposures and to take advantage of any natural offsets. To mitigate the impact of currency fluctuations on transactions denominated in nonfunctional currencies, we periodically enter into derivative financial instruments in the form of foreign currency exchange forward contracts with major financial institutions. We temporarily record realized and unrealized gains and losses on these contracts that qualify as cash flow hedges in other comprehensive income, and then recognize them in other income or expense when the hedged item affects net earnings.

From time to time, we enter into foreign currency forward exchange contracts with terms of up to 12 months to manage currency exposures for transactions denominated in a currency other than an entity's functional currency. As a result, the impact of foreign currency gains/losses recognized in earnings are partially offset by gains/losses on the related foreign currency forward exchange contracts in the same reporting period.

We maintain written policies and procedures governing our risk management activities. With respect to cash flow hedges, changes in cash flows attributable to hedged transactions are generally expected to be completely offset by changes in the fair value of hedge instruments. Consequently, foreign currency exchange contracts would not subject us to material risk due to exchange rate movements, because gains and losses on these contracts offset gains and losses on the assets, liabilities or transactions being hedged.

The results of operations discussed herein have not been materially affected by inflation.

### Interest Rate Risk

**Cash and Cash Equivalents** - We are exposed to the risk of interest rate fluctuations on the interest income earned on our cash and cash equivalents. A hypothetical 100 basis point movement in interest rates applicable to our cash and cash equivalents outstanding at March 31, 2014 would increase interest income by approximately \$1.3 million on an annual basis. No significant decrease in interest income would be expected as our cash balances are earning interest at rates of approximately 24 basis points. We are subject to foreign currency exchange risk with respect to cash balances maintained in foreign currencies.

**Senior Credit Facility** - Our interest rate risk relates primarily to U.S. dollar LIBOR-indexed borrowings. We have used an interest rate derivative instrument to manage our earnings and cash flow exposure to changes in interest rates by utilizing a forward-starting interest rate swap that began to offset a portion of our interest payments in the first quarter of 2011. This interest rate derivative instrument fixed the interest rate on a portion of our expected LIBOR-indexed floating-rate borrowings beginning on December 31, 2010. The interest rate swap had a notional amount of \$108.8 million outstanding as of March 31, 2014. We recognized \$0.5 million of additional interest expense related to this derivative during the three months ended March 31, 2014. The fair value of our interest rate derivative instrument was a net liability of \$2.1 million at March 31, 2014.

Based on our outstanding borrowings at March 31, 2014, a one-percentage point change in interest rates would have impacted interest expense on the unhedged portion of the debt by \$3.1 million on an annualized basis.

## ITEM 4. CONTROLS AND PROCEDURES

### Evaluation of Disclosure Controls and Procedures

We maintain disclosure controls and procedures that are designed to provide reasonable assurance that information required to be disclosed in our Exchange Act report is recorded, processed, summarized and reported within the time periods specified in the Securities and Exchange Commission's rules and forms and that such information is accumulated and communicated to our management, including our principal executive officer and principal financial officer, as appropriate, to allow timely decisions regarding required disclosure. Disclosure controls and procedures, no matter how well designed and operated, can provide only reasonable assurance of achieving the desired control objectives, and management is required to apply its judgment in evaluating the cost-benefit relationship of possible controls and procedures. Management has designed our disclosure controls and procedures to provide reasonable assurance of achieving the desired control objectives.

As required by Exchange Act Rule 13a-15(b), we have carried out an evaluation, under the supervision and with the participation of our management, including our principal executive officer and principal financial officer, of the effectiveness of the design and operation of our disclosure controls and procedures as of March 31, 2014. Based upon

this evaluation, our principal executive officer and principal financial officer concluded that our disclosure controls and procedures were effective as of March 31, 2014 to provide such reasonable assurance.

As previously disclosed, the Company is in the process of a multi-year implementation of a global enterprise resource planning (“ERP”) system. In addition, in response to business integration activities, the Company has and will continue to further align and streamline the design and operation of the financial control environment to be responsive to the changing business model.

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Changes in Internal Control Over Financial Reporting

There were no changes in our internal control over financial reporting (as defined in Rule 13a-15(f) under the Exchange Act) that occurred during the quarter ended March 31, 2014 that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

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PART II. OTHER INFORMATION

ITEM 1. LEGAL PROCEEDINGS

Various lawsuits, claims and proceedings are pending or have been settled by us; the most significant of which are described below.

The Company is subject to various claims, lawsuits and proceedings in the ordinary course of the Company's business, including claims by current or former employees, distributors and competitors and with respect to its products and product liability claims, lawsuits and proceedings, some of which have been settled by the Company. In the opinion of management, such claims are either adequately covered by insurance or otherwise indemnified, or are not expected, individually or in the aggregate, to result in a material adverse effect on our financial condition. However, it is possible that the Company's results of operations, financial position and cash flows in a particular period could be materially affected by these contingencies.

On June 6, 2012, the Company was contacted by the United States Attorney's Office for the District of New Jersey regarding the activities of sales representatives in a single region within our Extremities Reconstruction division. The U.S. Attorney's Office is investigating the activities of three sales representatives, one of whom was a supervisor until terminated by the Company for failure to cooperate with this investigation. The activities at issue pertain to alleged improper billing of products for extremities indications. The Company has been cooperating with the U.S. Attorney's Office on a voluntary basis and is not a subject or target of an investigation at this time. In cooperating with the U.S. Attorney's Office, the Company has responded to multiple government requests for documents and information; and in the fall of 2013 it responded to what the government currently indicated is its final request. Representatives of the Company met with the Assistant United States Attorney in charge of the matter and an agent from the Federal Bureau of Investigation on April 11, 2014, to discuss the matter, the behavior of the sales representatives in question, and the disposition of the matter as to the Company. The Company awaits word from the U.S. Attorney's Office as to the disposition of the matter as to the Company.

The Company manufactures and sells certain extremities products internationally pursuant to a license agreement that the licensor has indicated it will terminate effective October 20, 2014 after the parties were unable to resolve disagreements under the license agreement. Revenues for products sold under that license agreement approximated \$5.5 million in 2013. Subject to certain conditions described in the license agreement, Integra may sell the remaining inventory of covered products after the expiration of the license agreement. In the first quarter of 2014, the parties resumed their discussions to resolve their disagreements under the license agreement. At this time, we cannot predict whether the licensor will bring any claims against the Company or whether those claims, if successful, would have a material, adverse effect on the financial results of the Company. Should the licensor bring any claims against the Company, the Company might assert counterclaims against the licensor.

The Company accrues for loss contingencies when it is deemed probable that a loss has been incurred and that loss is estimable. The amounts accrued are based on the full amount of the estimated loss before considering insurance proceeds, and do not include an estimate for legal fees expected to be incurred in connection with the loss contingency. The Company consistently accrues legal fees expected to be incurred in connection with loss contingencies as those fees are incurred by outside counsel as a period cost.

ITEM 1A. RISK FACTORS

The Risk Factors included in our Annual Report on Form 10-K for the fiscal year ended December 31, 2013 have not materially changed.

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

On October 23, 2012, our Board of Directors authorized a repurchase of up to \$75.0 million of outstanding common stock through December 2014. Shares may be repurchased either in the open market or in privately negotiated transactions.

There were no repurchases of our common stock during the three months ended March 31, 2014 under this program.

ITEM 4. MINE SAFETY DISCLOSURES

Not applicable.

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ITEM 6. EXHIBITS

|           |   |
|-----------|---|
| 2.1       | Stock Purchase Agreement, dated as of October 25, 2013, by and between Covidien Group S.A.R.L. and Integra LifeSciences Corporation (Incorporated by Reference to Exhibit 10.1 to the Company's Current Report on Form 8-K filed on January 15, 2014) |
| *18       | Preferability letter of Independent Public Accounting Firm dated May 1, 2014  |
| *31.1     | Certification of Principal Executive Officer Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002  |
| *31.2     | Certification of Principal Financial Officer Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002  |
| *32.1     | Certification of Principal Executive Officer Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002  |
| *32.2     | Certification of Principal Financial Officer Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002  |
| *†101.INS | XBRL Instance Document  |
| *†101.SCH | XBRL Taxonomy Extension Schema Document   |
| *†101.CAL | XBRL Taxonomy Extension Calculation Linkbase Document   |
| *†101.DEF | XBRL Definition Linkbase Document   |
| *†101.LAB | XBRL Taxonomy Extension Labels Linkbase Document  |
| *†101.PRE | XBRL Taxonomy Extension Presentation Linkbase Document  |

\* Filed herewith

† The financial information of Integra LifeSciences Holdings Corporation Quarterly Report on Form 10-Q for the quarter ended March 31, 2014 filed on May 1, 2014 formatted in XBRL (Extensible Business Reporting Language): (i) the Condensed Consolidated Statements of Operations and Comprehensive Income, (ii) the Condensed Consolidated Balance Sheets, (iii) Parenthetical Data to the Condensed Consolidated Balance Sheets, (iv) the Condensed Consolidated Statements of Cash Flows, and (v) Notes to Condensed Consolidated Financial Statements, is furnished electronically herewith.

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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.

INTEGRA LIFESCIENCES HOLDINGS  
CORPORATION

Date: May 1, 2014

/s/ Peter J. Arduini  
Peter J. Arduini  
President and Chief Executive Officer

Date: May 1, 2014

/s/ John B. Henneman, III  
John B. Henneman, III  
Corporate Vice President, Finance and  
Administration,  
and Chief Financial Officer

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Exhibits

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