

INTEGRA LIFESCIENCES HOLDINGS CORP  
Form 10-Q  
July 26, 2018  
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 June 30, 2018

or

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  
(STATE OR OTHER JURISDICTION OF  
INCORPORATION OR ORGANIZATION)

51-0317849  
(I.R.S. EMPLOYER  
IDENTIFICATION NO.)

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

08536

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 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, a smaller reporting company, or an emerging growth company. See the definitions of "large accelerated filer," "accelerated filer," "smaller reporting company," and "emerging growth company" in Rule 12b-2 of the Exchange Act.

Large accelerated filer  Accelerated filer

Non-accelerated filer  Smaller reporting company

Emerging growth company

If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the

Exchange Act.

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

Indicate by check mark whether the registrant has filed all documents and reports required to be filed by Section 12, 13 or 15(d) of the Securities Exchange Act of 1934 subsequent to the distribution of securities under a plan confirmed by a court. Yes  No

---

The number of shares of the registrant's Common Stock, \$0.01 par value, outstanding as of July 24, 2018 was 85,131,560.

INTEGRA LIFESCIENCES HOLDINGS CORPORATION  
INDEX

	Page Number
<u>PART I. FINANCIAL INFORMATION</u>	
<u>Item 1. Financial Statements</u>	<u>3</u>
Condensed Consolidated Statements of Operations and Comprehensive Income for the three and six months ended June 30, 2018 and 2017 (Unaudited)	<u>3</u>
Condensed Consolidated Balance Sheets as of June 30, 2018 and December 31, 2017 (Unaudited)	<u>4</u>
Condensed Consolidated Statements of Cash Flows for the six months ended June 30, 2018 and 2017 (Unaudited)	<u>5</u>
<u>Notes to Unaudited Condensed Consolidated Financial Statements</u>	<u>6</u>
<u>Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations</u>	<u>30</u>
<u>Item 3. Quantitative and Qualitative Disclosures About Market Risk</u>	<u>42</u>
<u>Item 4. Controls and Procedures</u>	<u>43</u>
<u>PART II. OTHER INFORMATION</u>	
<u>Item 1. Legal Proceedings</u>	<u>43</u>
<u>Item 1A. Risk Factors</u>	<u>44</u>
<u>Item 2. Unregistered Sales of Equity Securities and Use of Proceeds</u>	<u>45</u>
<u>Item 4. Mine Safety Disclosures</u>	<u>45</u>
Item 5. Other Information	<u>45</u>
<u>Item 6. Exhibits</u>	<u>46</u>
<u>SIGNATURES</u>	<u>47</u>
<u>Exhibit 31.1</u>	
<u>Exhibit 31.2</u>	
<u>Exhibit 32.1</u>	
<u>Exhibit 32.2</u>	

EX-101 INSTANCE DOCUMENT

EX-101 SCHEMA DOCUMENT

EX-101 CALCULATION LINKBASE DOCUMENT

EX-101 DEFINITION LINKBASE DOCUMENT

EX-101 LABELS LINKBASE DOCUMENT

EX-101 PRESENTATION LINKBASE DOCUMENT

---

Table of Contents

## 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		Six Months Ended	
	June 30,		June 30,	
	2018	2017	2018	2017
Total revenue, net	\$366,190	\$282,164	\$723,272	\$540,801
Costs and expenses:				
Cost of goods sold	137,565	98,998	281,787	185,583
Research and development	19,108	15,747	37,433	31,241
Selling, general and administrative	176,597	145,015	340,163	287,512
Intangible asset amortization	5,286	5,419	10,676	9,520
Total costs and expenses	338,556	265,179	670,059	513,856
Operating income	27,634	16,985	53,213	26,945
Interest income	174	64	250	71
Interest expense	(17,504 )	(6,181 )	(36,272 )	(11,312 )
Other income (expense), net	2,427	(2,866 )	4,672	(2,956 )
Income before income taxes	12,731	8,002	21,863	12,748
Income tax expense (benefit)	1,355	(2,833 )	(505 )	(4,482 )
Net income	\$11,376	\$10,835	\$22,368	\$17,230
Net income per share				
Basic	\$0.14	\$0.14	\$0.28	\$0.23
Diluted	\$0.14	\$0.14	\$0.27	\$0.22
Weighted average common shares outstanding (See Note 12):				
Basic	82,423	76,213	80,491	75,487
Diluted	83,513	78,963	81,702	78,703
Comprehensive income (See Note 13)	\$(12,269 )	\$28,131	\$21,401	\$40,226

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

Table of Contents

INTEGRA LIFESCIENCES HOLDINGS CORPORATION  
 CONDENSED CONSOLIDATED BALANCE SHEETS  
 (UNAUDITED)

(In thousands, except per share amount)

	June 30, 2018	December 31, 2017
<b>ASSETS</b>		
Current assets:		
Cash and cash equivalents	\$ 183,771	\$ 174,935
Trade accounts receivable, net of allowances of \$3,464 and \$8,882	258,380	251,799
Inventories, net	290,517	296,332
Prepaid expenses and other current assets	88,654	99,080
Total current assets	821,322	822,146
Property, plant and equipment, net	277,025	269,251
Intangible assets, net	1,121,845	1,159,627
Goodwill	927,148	937,905
Deferred tax assets, net	7,677	6,250
Other assets	30,756	16,078
Total assets	\$3,185,773	\$3,211,257
<b>LIABILITIES AND STOCKHOLDERS' EQUITY</b>		
Current liabilities:		
Short-term portion of borrowings under senior credit facility	\$—	\$ 60,000
Accounts payable, trade	84,037	93,967
Accrued compensation	63,211	73,392
Short-term portion of contingent consideration	4,900	22,793
Accrued expenses and other current liabilities	81,194	98,759
Total current liabilities	233,342	348,911
Long-term borrowings under senior credit facility	1,476,488	1,781,142
Deferred tax liabilities	73,311	65,130
Other liabilities	60,727	53,768
Total liabilities	1,843,868	2,248,951
Commitments and contingencies		
Stockholders' equity:		
Preferred stock; no par value; 15,000 authorized shares; none outstanding	—	—
Common stock; \$0.01 par value; 240,000 authorized shares; 87,771 and 81,306 issued at June 30, 2018 and December 31, 2017, respectively	877	813
Additional paid-in capital	1,177,125	821,758
Treasury stock, at cost; 2,890 shares and 2,912 shares at June 30, 2018 and December 31, 2017, respectively	(120,732 )	(121,644 )
Accumulated other comprehensive loss	(25,306 )	(23,807 )
Retained earnings	309,941	285,186
Total stockholders' equity	1,341,905	962,306
Total liabilities and stockholders' equity	\$3,185,773	\$3,211,257

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

Table of Contents

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

	Six Months Ended June 30,	
	2018	2017
<b>OPERATING ACTIVITIES:</b>		
Net income	\$22,368	\$17,230
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	54,002	41,312
Deferred income tax	(423)	(1,138)
Amortization of debt issuance costs	3,657	784
Realized loss on sale of short-term investment	—	2,287
Loss on disposal of property and equipment	127	452
Change in fair value of contingent consideration and other	914	(1,995)
Share-based compensation	10,214	11,050
Changes in assets and liabilities, net of business acquisitions:		
Accounts receivable	(8,420)	(11,303)
Inventories	(3,596)	(5,464)
Prepaid expenses and other current assets	(1,959)	(9,236)
Other non-current assets	(436)	(1,811)
Accounts payable, accrued expenses and other current liabilities	(3,405)	20,287
Deferred revenue	(91)	2,083
Other non-current liabilities	4,792	(6,785)
Net cash provided by operating activities	77,744	57,753
<b>INVESTING ACTIVITIES:</b>		
Purchases of property and equipment	(35,387)	(22,010)
Proceeds from sale of short-term investments	—	16,951
Proceeds from note receivable	446	—
Proceeds from sale of property and equipment	205	143
Cash provided by (used in) business acquisitions	26,704	(225,744)
Net cash used in investing activities	(8,032)	(230,660)
<b>FINANCING ACTIVITIES:</b>		
Borrowings under senior credit facility	50,000	245,000
Repayments under senior credit facility	(415,000)	(30,000)
Payment of debt issuance costs	(4,221)	—
Proceeds from the issuance of common stock, net of issuance costs	349,599	—
Net cash paid for financing liabilities from business acquisitions	(33,843)	87
Proceeds from exercised stock options	3,727	9,774
Cash taxes paid in net equity settlement	(7,240)	(6,498)
Net cash (used in) provided by financing activities	(56,978)	218,363
Effect of exchange rate changes on cash and cash equivalents	(3,898)	7,089
Net increase in cash and cash equivalents	8,836	52,545
Cash and cash equivalents at beginning of period	174,935	102,055
Cash and cash equivalents at end of period	\$183,771	\$154,600

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





Table of Contents

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

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 June 30, 2018 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, 2017 included in the Company’s Annual Report on Form 10-K. The December 31, 2017 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- and six-month periods ended June 30, 2018 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 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 derivative instruments, valuation of pension assets and liabilities, 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.

Equity Offering

In May 2018, the Company commenced and closed on a public offering of common stock. The Company issued 6.0 million shares of common stock and received total proceeds, net of underwriting fees and offering expenses of approximately \$349.6 million. The net proceeds from the offering were used to reduce outstanding borrowings under the revolving credit portion of the Company's Senior Credit Facility.

Recently Issued Accounting Standards

In May 2014, the FASB issued Update No. 2014-09, Revenue from Contracts with Customers (Topic 606). The core principle of the guidance is that an entity should recognize revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. To achieve that core principle, an entity should 1) identify the contract(s) with a customer, 2) identify the performance obligations in the contract, 3) determine the transaction price, 4) allocate the transaction price to the performance obligations in the contract, and 5) recognize revenue when (or as) the entity satisfies a performance obligation. This update became effective for all annual periods and interim reporting periods beginning after December 15, 2017. The Company adopted Topic 606 as of January 1, 2018 using the modified retrospective method. See Note 3, Revenues, for further details.

In February 2016, the FASB issued Update No. 2016-02, Leases (Topic 842). Under current accounting guidance, an entity is not required to report operating leases on the balance sheet. The amendment requires that lessees recognize virtually all of its leases on the balance sheet by recording a right-of-use asset and lease liability (other than leases that meet the definition of a "short-term lease"). This update will become effective for all annual periods and interim

reporting periods beginning after December 15, 2018. The new standard must be adopted using a modified retrospective transition. Early adoption is permitted. While the Company has not yet completed its assessment, the adoption of this guidance may have a material impact on the Company's financial position.

In August 2016, the FASB issued Update No. 2016-15, Classification of Certain Cash Receipts and Cash Payments. The guidance addresses the classification of cash flows related to debt repayment or extinguishment costs, settlement of zero-coupon debt instruments or debt instruments with coupon rates that are insignificant in relation to the effective interest rate of the borrowing, contingent consideration payments made after business combinations, proceeds from the settlement of insurance claims and

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

corporate-owned life insurance, distributions received from equity method investees and beneficial interests in securitization transaction. This update became effective for all annual periods and interim reporting periods beginning after December 15, 2017. The Company adopted ASU 2016-15 effective January 1, 2018 on a retrospective basis. The adoption of this guidance had no significant impact on the Company's consolidated financial statements.

In October 2016, the FASB issued Update No. 2016-16, Intra-Entity Transfers of Assets Other Than Inventory. The guidance requires that the income tax consequences of intra-entity transfers of assets other than inventory be recognized as a current-period income tax expense or benefit and removes the requirement to defer and amortize the consolidated tax consequences of intra-entity transfers. The new standard became effective for all annual periods beginning after December 15, 2017. The Company adopted ASU 2016-16 effective January 1, 2018, and this guidance had no significant impact on its consolidated financial statements.

In March 2017, the FASB issued Update No. 2017-07, Compensation - Retirement Benefits (Topic 715): Improving the Presentation of Net Periodic Pension Cost and Net Periodic Postretirement Benefit Cost. The guidance requires that an employer report the service cost component in the same line item or items as other compensation costs arising from services rendered by the pertinent employees during the period. The other components of net benefit cost are required to be presented in the income statement separately from the service cost component and outside a subtotal of income from operations, if one is presented. If a separate line item or items were to be used to present the other components of net benefit cost, that line item or items must be appropriately described. If a separate line item or items is/are not used, the line item or items used in the income statement to present the other components of net benefit cost must be disclosed. In addition, the amendments also allow only the service cost component to be eligible for capitalization when applicable. The new standard became effective for annual periods beginning after December 15, 2017. The Company adopted ASU 2017-07 effective January 1, 2018. The Company recognized the components of net periodic benefit cost other than the service cost component in other (expense) income, net in the consolidated statements of operations. The adoption of this guidance had no significant impact on the Company's prior-year consolidated financial statements.

In May 2017, the FASB issued ASU 2017-09, Stock Compensation (Topic 718): Scope of Modification Accounting. The update serves to provide clarity and reduce both (1) diversity in practice and (2) cost and complexity when applying the guidance in Topic 718, Compensation-Stock Compensation, to a change to the terms or conditions of a share-based payment award. The new standard became effective for all annual periods beginning after December 15, 2017. The Company adopted ASU 2017-09 effective January 1, 2018, and there was no significant impact of this guidance on its consolidated financial statements.

In August 2017, the FASB issued ASU 2017-12, Derivatives and Hedging (Topic 815): Targeted Improvements to Accounting for Hedging Activities. This update amends the hedge accounting rules to simplify the application of hedge accounting guidance and better portray the economic results of risk management activities in the financial statements. The guidance expands the ability to hedge nonfinancial and financial risk components, reduces complexity in fair value hedges of interest rate risk, eliminates the requirement to separately measure and report hedge ineffectiveness, as well as eases certain hedge effectiveness assessment requirements. This update will become effective for all annual periods and interim reporting periods beginning after December 15, 2018. Early adoption is permitted. The Company elected to early adopt ASU 2017-12 effective January 1, 2017 using the modified retrospective method. The implementation of the amended guidance did not have a significant impact on the Company's consolidated financial statements.

In February 2018, the FASB issued ASU 2018-02, Reclassification of Certain Tax Effects From Accumulated Other Comprehensive Income. This amendment allows a reclassification from accumulated other comprehensive income to retained earnings for stranded tax effects resulting from the 2017 Tax Act (as defined in Note 11, Income Taxes). This

guidance is effective for annual and interim periods beginning after December 15, 2018. Early adoption is permitted. The Company elected to early adopt the ASU 2018-02 effective January 1, 2018, which resulted in the reclassification of \$0.5 million from accumulated other comprehensive loss to retained earnings related to net unrealized loss on cash flow hedges.

There are no other recently issued accounting pronouncements that are expected to have any significant effect on the Company's financial position, results of operations or cash flows.

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

## 2. BUSINESS ACQUISITIONS AND DIVESTITURE

### Johnson & Johnson's Codman Neurosurgery Business

On October 2, 2017, upon the terms and subject to the conditions set forth in the asset purchase agreement entered into by the Company with DePuy Synthes, Inc., a Delaware corporation ("DePuy Synthes"), a wholly owned subsidiary of Johnson & Johnson (the "Purchase Agreement"), the Company completed the acquisition of certain assets, and assumed certain liabilities, of Johnson & Johnson's Codman neurosurgery business (the "Codman Acquisition"). Under the terms of the Purchase Agreement, the Company paid an aggregate purchase price of \$1.014 billion, subject to adjustments set forth in the Purchase Agreement relating to the book value of inventory transferred to the Company at the closing of the Codman Acquisition. The book value of certain inventory retained by DePuy Synthes will be transferred to the Company in the future along with certain prepaid taxes.

The Codman Acquisition was accounted for using the acquisition method of business combination under ASC 805, Business Combinations.

The Company recorded revenue for Codman Neurosurgery of approximately \$79.2 million and \$157.1 million, in the condensed consolidated statements of operations and comprehensive income for the three and six months ended June 30, 2018. The net income or loss attributable to this acquisition cannot be identified on a stand-alone basis because it is in the process of being integrated into the Company's operations.

The following summarizes the preliminary allocation of the purchase price based on the fair value of the assets acquired and liabilities assumed:

	Preliminary Purchase Price Allocation (Dollars in thousands)	Weighted Average Life
Inventory	\$ 74,962	
Assets held for sale	30,813	
Other current assets	8,202	
Property, plant and equipment	35,949	
Intangible assets:		
Codman corporate trade name	162,900	Indefinite
Completed technology	379,900	22 years
Goodwill	343,012	
Total assets acquired	1,035,738	
Accrued expenses	1,730	
Pension liabilities	19,917	
Net assets acquired	\$ 1,014,091	

During the first six months of 2018, the Company adjusted its preliminary purchase price allocation of goodwill by \$3.2 million because of working capital adjustments of \$6.2 million that were offset by inventory adjustments of \$3.0 million when the Company obtained additional information about the acquired assets.

During the first quarter of 2018, the Company received cash of \$5.7 million from DePuy Synthes related to working capital adjustments, which was recorded within investing activities on the consolidated statements of cash flows.

During the second quarter of 2018, the Company received an additional \$21.0 million related to working capital adjustments.

During the first half of 2018, the Company paid \$15.9 million for inventory that was included in the initial purchase price allocation. The payment was included within financing activities on the consolidated statements of cash flows.

The Company recorded \$3.0 million and \$14.5 million in cost of goods sold related to fair value inventory purchase accounting adjustments for the three and six months ended June 30, 2018.

As of June 30, 2018, certain amounts relating to the valuation of property, plant and equipment have not been finalized. The finalization of these matters may result in changes to goodwill.

Goodwill related to the Codman Acquisition was allocated to the Codman Specialty Surgical segment. Goodwill is the excess of the consideration transferred over the net assets recognized and represents the expected revenue and cost synergies of the combined company and assembled workforce. Goodwill recognized as a result of the acquisition is generally deductible for income tax purposes.

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

In the fourth quarter of 2017, the Company wrote-off construction in progress of \$6.3 million related to a project acquired as part of the Codman Acquisition that the Company decided to discontinue after the acquisition.

Divestiture to Natus

On September 8, 2017, to facilitate the acquisition of the Codman Neurosurgery Business and to comply with legal requirements, the Company and certain of its subsidiaries entered into an asset purchase agreement (the "Divestiture Agreement") with Natus Medical Incorporated ("Natus"), pursuant to which the Company agreed to divest its global Camino® Intracranial Pressure monitoring product lines and the U.S. rights to its fixed pressure shunts business within its Codman Specialty Surgical segment together with certain neurosurgery assets acquired as part of the Codman Acquisition, which includes Codman U.S. dural graft implant, external ventricular drainage catheter and cerebrospinal fluid collection systems businesses (the "Divestiture"). The Divestiture Agreement was entered into in connection with the review of the Codman Acquisition by the Federal Trade Commission and the antitrust authority of Spain.

On October 6, 2017, upon the terms and subject to the conditions of the Divestiture Agreement, the Divestiture was completed and Natus paid an aggregate purchase price of \$46.4 million.

Assets and liabilities divested consisted of the following as of October 6, 2017 (amounts in thousands):

Inventories	\$8,348
Prepaid expenses and other current assets	36
Assets held for sale	30,813
Property, plant and equipment, net	1,122
Goodwill	2,861
Total assets divested	\$43,180

Deferred revenue	\$1,082
Accrued compensation	209
Total liabilities divested	\$1,291

Assets held for sale includes assets and liabilities related to the U.S. dural graft implant, external ventricular drainage catheters and cerebrospinal fluid collection systems businesses acquired as part of the Codman Acquisition.

The transitional supply agreement with Natus requires the Company to provide to Natus certain assets defined in the transitional supply agreement upon termination. The Company recognized a liability of \$1.3 million, included in other liabilities in the consolidated balance sheet, related to estimated cost of assets to be provided to Natus upon termination of the transitional supply agreement.

The Divestiture does not represent a strategic shift that will have a major effect on the Company's operations and financial statements. Goodwill was allocated to the assets and liabilities divested using the relative fair value method. The Company recognized a pretax gain on sale of business of \$2.6 million included in other income, net in its consolidated statement of operations for the year ended December 31, 2017.

Derma Sciences

On February 24, 2017, the Company executed the Agreement and Plan of Merger (the "Merger Agreement") under which the Company acquired all of the outstanding shares of Derma Sciences, Inc., a Delaware corporation ("Derma Sciences") for an aggregate purchase price of approximately \$210.8 million, including payment of certain of Derma Sciences' closing expenses and settlement of stock-based compensation plans of \$4.8 million and \$4.3 million, respectively. The purchase price consisted of a cash payment to the former stockholders of Derma Sciences of approximately \$201.7 million upon the closing of the transaction.

Derma Sciences is a tissue regeneration company focused on advanced wound and burn care that offers products to help manage chronic and hard-to-heal wounds, especially those resulting from diabetes and poor vascular functioning. The revenue and the net income or loss attributable to this acquisition cannot be identified on a stand-alone basis because it has been integrated into the Company's operations.

The following summarizes the allocation of the purchase price based on the fair value of the assets acquired and liabilities assumed:

9

---



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

	Purchase Price Allocation (Dollars in thousands)	
Cash and cash equivalents	\$ 16,512	
Short-term investments	19,238	
Accounts receivable	8,949	
Inventory	17,977	
Prepaid expenses and other current assets	4,369	
Property, plant and equipment	4,311	
Intangible assets:		Wtd. Avg. Life:
Customer relationship	78,300	14 years
Trademarks/brand names	13,500	15 years
Completed technology	11,600	14 years
Non-compete agreement	280	1 year
Goodwill	73,765	
Deferred tax assets	14,524	
Other assets	101	
Total assets acquired	263,426	
Accounts payable	4,560	
Accrued expenses and other current liabilities	7,409	
Contingent liability	37,174	
Other liabilities	3,805	
Net assets acquired	\$ 210,478	

Goodwill related to the Derma Sciences acquisition was allocated to the Orthopedics and Tissue Technologies segment. Goodwill is the excess of the consideration transferred over the net assets recognized and represents the expected revenue and cost synergies of the combined company and assembled workforce. Goodwill recognized as a result of the acquisition is not deductible for income tax purposes.

#### Short-term Investments

Short-term investments recognized at the acquisition date of Derma Sciences are investments in equity and debt securities including certificates of deposit purchased with an original maturity greater than three months which are deposited in various U.S. financial institutions and are fully insured by the Federal Deposit Insurance Corporation. The Company considers securities with original maturities of greater than 90 days to be available for sale securities. Securities under this classification are recorded at fair value and unrealized gains and losses are recorded within accumulated other comprehensive income. The estimated fair value of the available for sale securities is determined based on quoted market prices. The Company evaluates securities with unrealized losses to determine whether such losses, if any, are other than temporary. Short-term investments are classified as Level 1 in fair value hierarchy. Fair values of short-term investments are determined using the unadjusted quoted prices in active markets for identical assets or liabilities that the Company has the ability to access at the balance sheet date.

In the second quarter of 2017, the Company sold the acquired short-term investments and recognized a loss of \$2.3 million included in other income (expense), net in the consolidated statement of operations.

#### Deferred Taxes

The acquired deferred taxes of \$14.5 million include a deferred tax asset of \$39.7 million related to a federal net operating loss which the Company expects to utilize against income in future periods and a deferred tax asset of \$16.4 million related to intangibles acquired by Derma Sciences in previous periods, offset by a deferred tax liability of \$41.1 million for new intangibles for which the Company will not receive a tax benefit and a deferred tax liability of

\$0.5 million related to various deferred items. In the second quarter of 2017, the Company decreased the preliminary estimated value of this deferred tax liability by \$1.5 million to reflect the adjustments to preliminary estimated fair values of assets and liabilities acquired. In the fourth quarter of 2017, the Company decreased the preliminary value of the deferred tax asset by \$3.3 million to reflect returns filed for periods prior to the acquisition date and adjustments for expected effective state tax rates.

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

United States Food and Drug Administration ("FDA") Untitled Letter

On June 22, 2015, the FDA issued an Untitled Letter (the "Untitled Letter") alleging that BioD morselized amniotic membrane- based products do not meet the criteria for regulation as human cellular tissue-based products ("HCT/Ps") solely under Section 361 of the Public Health Service Act and that, as a result, BioD would need a biologics license to lawfully market those morselized products. Since the issuance of the Untitled Letter, BioD and more recently, the Company, have been in discussions with the FDA to communicate their disagreement with the FDA's assertion that certain products do not fall within the HCT/Ps. The FDA has not changed its position that certain of the BioD acquired products are not eligible for marketing solely under Section 361.

In November 2017, the FDA issued its final guidance document related to human tissue titled, "Regulatory Considerations for Human Cells, Tissues, and Cellular and Tissue-Based Products: Minimal Manipulation and Homologous Use" (the "HCT/P Final Guidance"). The HCT/P Final Guidance maintains the FDA's position that products such as the Company's morselized amniotic membrane tissue based products do not meet the criteria for regulation solely as HCT/Ps. In addition, the FDA articulated a risk-based approach to enforcement and, while some uses for amniotic membrane tissue-based products would enjoy as much as thirty-six months of enforcement discretion, other high risk uses could be subject to immediate enforcement action. The Company does not believe the uses for its amniotic membrane tissue based products fall into the high-risk category. Nonetheless, the Company can make no assurances that the FDA will continue to exercise its enforcement discretion with respect to the Company's amniotic membrane tissue based products, and any potential action of the FDA could have a financial impact regarding the sales of such products. Although the Company continues to disagree with the FDA's position, the Company has been considering and continues to consider regulatory approval pathways for its amniotic membrane tissue-based products. Revenues from BioD morselized amniotic material based products for the three and six months ended June 30, 2018 and 2017 were less than 1.0% of consolidated revenues.

Contingent Consideration

The Company assumed contingent consideration incurred by Derma Sciences related to its acquisitions of BioD and the intellectual property related to the Medihoney product. The Company accounted for the contingent liabilities by recording their fair value on the date of the acquisition based on a discounted cash-flow model. The contingent liabilities recognized as part of the Derma Sciences acquisition relate to the following:

- i. contractual incentive payments that could be made to former equity owners of BioD if net sales of BioD products exceed a certain amount for the twelve-month periods ending June 30, 2017 and 2018 ("BioD Earnout Payments");
- ii. a contractual incentive payment that could be made to the former equity owners if there has been no specific enforcement action or notice by the FDA against the specific BioD products as a result of the Untitled Letter for a certain period after closing as defined by the agreement ("Product Payment"); and
- iii. contractual incentive payments that could be made to the former owner of the intellectual property relating to the Medihoney product line, if net sales of Medihoney products exceed certain amounts defined in the agreement between Derma Sciences and the former owner of the intellectual property of Medihoney for any twelve-month period ("Medihoney Earnout Payments").

At the date of the acquisition, net sales used in estimating the BioD Earnout Payments is based on the weighted average of different possible scenarios using a revenue volatility of 13.5%. The BioD Earnout Payments were valued using a discount rate of 3.0%. The maximum payout related to the BioD Earnout Payments is \$26.5 million. The estimated fair value as of February 24, 2017 was \$9.1 million. In August 2017, the Company paid \$4.8 million for the twelve-month period ending June 30, 2017 component of the BioD Earnout Payments. As of June 30, 2018 and December 31, 2017, the estimated fair value of the remaining portion of the BioD Earnout Payments were zero and \$0.3 million.

At the date of acquisition, the Company estimated that the probability of the Product Payment was 98.0% and valued it at a discount rate of 2.5%. The maximum payout related to the Product Payment is \$29.7 million. The estimated fair value as of February 24, 2017 was \$26.8 million. In the second quarter of 2017, the Company adjusted the preliminary estimated fair value to increase the Product Payment by \$0.9 million related to additional products that should have been included in the preliminary estimate based on the Merger Agreement. On May 25, 2017, the Company made full payment for the Product Payment of \$26.6 million. The payment was included in cash used in business acquisition, net of cash acquired within investing activities in the condensed consolidated statements of cash flows since the payment was made shortly after the acquisition.

At the date of the acquisition, the net sales used in estimating the Medihoney Earnout Payments were based on the weighted average of different possible scenarios using revenue volatility of 27.5%. The Medihoney Earnout Payments were valued using a discount rate of 4.5%. The maximum payout related to the Medihoney Earnout Payments is \$5.0 million. During the second

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

quarter of 2018, the Company paid \$2.0 million for the Medihoney Earnout Payment. The estimated fair value as of June 30, 2018 was \$0.2 million. The estimated fair value as of February 24, 2017 and December 31, 2017 was \$1.4 million.

These fair value measurements were based on significant inputs not observed in the market and thus represented a Level 3 measurement. The contingent considerations are re-measured to fair value at each reporting date until the contingency is resolved, and those changes in fair value are recognized in earnings. Depending on the expected timing of the estimated payments, the acquisition date fair values and subsequent remeasurement could change.

#### Pro Forma Results

The following unaudited pro forma financial information summarizes the results of operations for the three and six months ended June 30, 2017 as if the acquisitions of Codman Neurosurgery and Derma Sciences and the divestiture to Natus, which were completed by the Company during 2017, had been completed as of the beginning of 2016. The pro forma results are based upon certain assumptions and estimates, and they give effect to actual operating results prior to the acquisitions and adjustments to reflect (i) the change in interest expense, depreciation expenses, intangible asset amortization and inventory step-up, (ii) timing of recognition for certain expenses that will not be recurring in a post-acquisition period, which includes \$2.9 million incurred by Derma Sciences prior to the acquisition and \$3.1 million and \$12.0 million incurred by Integra, for the three and six months ended June 30, 2018, and (iii) income taxes at a rate consistent with the Company's statutory rate at the date of the acquisitions. 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 acquisition had taken place on the basis assumed above, nor are they indicative of the results of future combined operations.

	Three Months Ended June 30, 2017	Six Months Ended June 30, 2017
	(In thousands, except per share amounts)	
Total revenue	\$360,879	\$707,539
Net income	\$14,274	\$22,850
Basic income per share	\$0.19	\$0.30

### 3. REVENUES FROM CONTRACTS WITH CUSTOMERS

#### Summary of Accounting Policies on Revenue Recognition

Revenue is recognized upon the transfer of control of promised products or services to the customers in an amount that reflects the consideration the Company expects to receive in exchange for those products and services.

Total revenue, net, includes product sales, product royalties and other revenues, such as fees received from services. For products shipped with FOB shipping point terms, the control of the product passes to the customer at the time of shipment. For shipments in which the control of the product is transferred when the customer receives the product, the Company recognizes revenue upon receipt by the customer. Certain products that the Company produces for private label customers have no alternative use and the Company has a right of payment for performance to date. Revenues from those products are recognized over the period that the Company manufactures these products, which is typically one to three months. The Company uses the input method to measure the manufacturing activities completed to date, which depicts the progress of the Company's performance obligation of transferring control of goods being manufactured for private label customers.

A portion of the Company's product revenue is generated from consigned inventory maintained at hospitals and distributors, and also from inventory physically held by field sales representatives. For these types of products sales,

the Company retains control until the product has been used or implanted, at which time revenue is recognized. Revenues from sale of products and services are evidenced by either a contract with the customer or a valid purchase order and an invoice which includes all relevant terms of sale. For product sales, invoices are generally issued upon the transfer of control (or upon the completion of the manufacturing in the case of the private label transactions recognized over time) and are typically payable 30 days after the invoice date. The Company performs a review of each specific customer's credit worthiness and ability to pay prior to acceptance as a customer. Further, the Company performs periodic reviews of its customers' creditworthiness prospectively.

#### Performance Obligations

The Company's performance obligations consist mainly of transferring control of goods and services identified in the contracts, purchase orders, or invoices. The Company has no significant multi-element contracts with customers.

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

### Significant Judgments

Usage-based royalties and licenses are estimated based on the provisions of contracts with customers and recognized in the same period that the royalty-based products are sold by the Company's strategic partners. The Company estimates and recognizes royalty revenue based upon communication with licensees, historical information, and expected sales trends. Differences between actual reported licensee sales and those that were estimated are adjusted in the period in which they become known, which is typically the following quarter. Historically, such adjustments have not been significant.

The Company estimates returns, price concessions, and discount allowances using the expected value method based on historical trends and other known factors. Rebate allowances are estimated using the most likely method based on each customer contract.

The Company's return policy, as set forth in its product catalogs and sales invoices, requires the Company to review and authorize the return of a product in advance. Upon the authorization, a credit will be issued for the goods returned within a set amount of days from the shipment, which is generally ninety days.

The Company disregards the effects of a financing component if the Company expects, at contract inception, that the period between the transfer and customer payment for the good or services will be one year or less. The Company has no significant revenues recognized on payments expected to be received more than one year after the transfer of control of products or services to customers.

### Contract Asset and Liability

Revenues recognized from the Company's private label business that are not invoiced to the customers as a result of recognizing revenue over time are recorded as a contract asset included in the prepaid expenses and other current assets account in the consolidated balance sheet.

Other operating revenues may include fees received under service agreements. Non-refundable fees received under multiple-period service agreements are recognized as revenue as the Company satisfies the performance obligations to the other party. A portion of the transaction price allocated to the performance obligations to be satisfied in the future periods is recognized as contract liability.

The following table summarized the changes in the contract asset and liability balances for the six months ended June 30, 2018:

#### Contract Asset

Contract asset, January 1, 2018	\$3,552
Transferred to trade receivable of contract asset included in beginning of the year contract asset	(3,552 )
Contract asset, net of transferred to trade receivables on contracts during the period	4,856
Contract asset, June 30, 2018	\$4,856

#### Contract Liability

Contract liability, January 1, 2018	\$11,059
Recognition of revenue included in beginning of year contract liability	(2,687 )
Contract liability, net of revenue recognized on contracts during the period	2,603
Foreign currency translation	(9 )
Contract liability, June 30, 2018	\$10,966

At June 30, 2018, the short-term portion of the contract liability of \$3.5 million and the long-term portion of \$7.5 million were included in accrued expenses and other current liabilities and other liabilities in the consolidated balance sheet.

As of June 30, 2018, the Company is expected to recognize revenue of approximately \$2.3 million for the remainder of 2018, \$2.6 million in 2019, \$1.9 million in 2020, \$1.0 million in 2021, \$0.7 million in 2022, and \$2.5 million thereafter.

### Shipping and Handling Fees

The Company elected to account for shipping and handling activities as a fulfillment cost rather than a separate performance obligation. Amounts billed to customers for shipping and handling are included as part of the transaction price and recognized as revenue when control of underlying products is transferred to the customer. The related shipping and freight charges incurred by the Company are included in the cost of goods sold.



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

Product Warranties

Certain of the Company's medical devices, including monitoring systems and neurosurgical systems, are designed to operate over long periods of time. These products are sold with warranties which may extend for up to two years from the date of purchase. The warranties are not considered a separate performance obligation. The Company estimates its product warranties using the expected value method based on historical trends and other known factors. The Company includes them in accrued expenses and other current liabilities in the consolidated balance sheet.

Taxes Collected from Customers

The Company elected to exclude from the measurement of the transaction price all taxes assessed by a governmental authority that are both imposed on and concurrent with a specific revenue-producing transaction and collected by the entity from a customer.

Disaggregated Revenue

The following table presents revenues disaggregated by the major sources of revenues for the three and six months ended June 30, 2018 (amounts in thousands):

	Three Months Ended June 30, 2018	Three Months Ended June 30, 2017	Six Months Ended June 30, 2018	Six Months Ended June 30, 2017
	(amounts in thousands)			
Neurosurgery	\$170,588	\$91,218	\$337,487	\$180,687
Precision Tools and Instruments	68,916	\$68,639	138,132	\$135,460
Total Codman Specialty Surgical	239,504	159,857	475,619	316,147
Wound Reconstruction and Care	76,601	69,746	146,713	124,510
Extremity Orthopedics	23,727	24,322	48,537	48,283
Private Label	26,358	28,239	52,403	51,861
Total Orthopedics and Tissue Technologies	126,686	122,307	247,653	224,654
Total revenue	\$366,190	\$282,164	\$723,272	\$540,801

See Note 14, Segment and Geographical Information, for details of revenues based on the location of the customer.

Effect of Adoption of ASC Topic 606

On January 1, 2018, the Company adopted Topic 606 using the modified retrospective method applied to all contracts which were not completed as of January 1, 2018. Result of operations for the reporting periods after January 1, 2018 are presented under Topic 606, while prior period amounts are not adjusted and continue to be reported in accordance with Topic 605, Revenue Recognition.

The adoption of Topic 606 resulted in an increase to the opening retained earnings of \$1.9 million, which was recorded net of taxes as of January 1, 2018 to reflect the change in timing of the recognition of revenue related to the Company's private label business from point in time to over time during the manufacturing process and goods in transit for which control was transferred to customers at the time of shipment. The total assets and liabilities increased by \$7.1 million and \$5.2 million, respectively, as of January 1, 2018.

The impact of adoption of Topic 606 to the Company's consolidated statement of operations for the three and six months ended June 30, 2018 was as follows:

	Three Months Ended June 30, 2018	Six Months Ended June 30, 2018
As Reported	Excluding Impact of	Excluding Impact of

	Topic 606		Topic 606	
	(Amounts in thousands)			
Statement of Operations				
Total revenue, net	\$366,190	\$363,381	\$723,272	\$719,420
Cost of goods sold	137,565	137,032	281,787	281,051
Income tax benefit	1,355	853	(505)	(1,135)
Net income	11,376	9,603	22,368	19,882

14

---

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

The adoption of Topic 606 had no significant impact on the Company's consolidated balance sheet as of June 30, 2018.

#### 4. INVENTORIES

Inventories, net consisted of the following:

	June 30, 2018	December 31, 2017
	(In thousands)	
Finished goods	\$ 181,831	\$ 190,100
Work in process	61,045	58,637
Raw materials	47,641	47,595
	\$ 290,517	\$ 296,332

#### 5. GOODWILL AND OTHER INTANGIBLE ASSETS

Changes in the carrying amount of goodwill for the six-month period ended June 30, 2018 were as follows:

	Codman Specialty Surgical	Orthopedics and Tissue Technologies	Total
	(In thousands)		
Goodwill at December 31, 2017	\$ 634,767	\$ 303,138	\$ 937,905
Codman acquisition purchase price allocation adjustments	(3,207 )	—	(3,207 )
Foreign currency translation	(5,101 )	(2,449 )	(7,550 )
Balance, June 30, 2018	\$ 626,459	\$ 300,689	\$ 927,148

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

	June 30, 2018			
	Weighted Average Life	Cost	Accumulated Amortization	Net
	(Dollars in thousands)			
Completed technology	19 years	\$ 865,467	\$ (146,727 )	\$ 718,740
Customer relationships	13 years	232,312	(98,919 )	133,393
Trademarks/brand names	28 years	104,398	(23,956 )	80,442
Codman trade name	Indefinite	162,900	—	162,900
Supplier relationships	27 years	34,721	(15,805 )	18,916
All other	4 years	11,055	(3,601 )	7,454
		\$ 1,410,853	\$ (289,008 )	\$ 1,121,845

	December 31, 2017			
	Weighted Average Life	Cost	Accumulated Amortization	Net
	(Dollars in thousands)			
Completed technology	19 years	\$ 869,174	\$ (124,096 )	\$ 745,078

Edgar Filing: INTEGRA LIFESCIENCES HOLDINGS CORP - Form 10-Q

Customer relationships	13 years	233,430	(91,961	)	141,469
Trademarks/brand names	28 years	104,879	(22,293	)	82,586
Codman trade name	Indefinite	162,900	—		162,900
Supplier relationships	27 years	34,721	(15,092	)	19,629
All other	4 years	11,511	(3,546	)	7,965
		\$1,416,615	\$ (256,988	)	\$1,159,627

15

---

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

During the third quarter of 2017, the Company recorded an impairment charge of \$3.3 million in cost of goods sold related to completed technology assets acquired from Tarsus Medical, Inc. ("Tarsus Technology"), since the underlying product will no longer be sold. Tarsus Technology was included in the Orthopedic and Tissue Technology segment.

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 be approximately \$67.0 million in 2018, \$66.7 million in 2019, \$66.6 million in 2020, \$65.6 million in 2021, \$62.1 million in 2022, \$61.2 million in 2023 and \$602.6 million thereafter. Identifiable intangible assets are initially recorded at fair market value at the time of acquisition using an income or cost approach.

## 6. DEBT

### Amended and Restated Senior Credit Agreement

On May 3, 2018, the Company entered into the fifth amendment and restatement (the "May 2018 Amendment") of its Senior Credit Facility (the "Senior Credit Facility") with a syndicate of lending banks with Bank of America, N.A., as Administrative Agent. The May 2018 Amendment extended the maturity date to May 3, 2023 and decreased the applicable rate, as described below. The Company continues to have the aggregate principal amount of \$2.2 billion available to it through the following facilities:

- i. a \$900.0 million Term Loan facility; and
- ii. a \$1.3 billion revolving credit facility, which includes a \$60.0 million sublimit for the issuance of standby letters of credit and a \$60.0 million sublimit for swingline loans.

In connection with the May 2018 Amendment, the Company's maximum consolidated total leverage ratio in the financial covenants (as defined in the Senior Credit Facility) was modified to the following:

Fiscal Quarter	Maximum Consolidated Total Leverage Ratio
Execution of May 2018 Amendment through March 31, 2019	5.50 : 1.00
June 30, 2019 through March 31, 2020	5.00 : 1.00
June 30, 2020 through March 31, 2021	4.50 : 1.00
June 30, 2021 and thereafter	4.00 : 1.00

Borrowings under the Senior Credit Facility bear interest, at the Company's option, at a rate equal to the following:

- i. the Eurodollar Rate (as defined in the Senior Credit Facility) in effect from time to time plus the applicable rate (ranging from 1.00% to 1.75%), or
  - ii. the highest of:
    1. the weighted average overnight Federal funds rate, as published by the Federal Reserve Bank of New York, plus 0.50%, plus the applicable rate (ranging from 0% to 0.75%),
    2. the prime lending rate of Bank of America, N.A. plus the applicable rate (ranging from 0% to 0.75%), and
    3. the one-month Eurodollar Rate plus 1.00% plus the applicable rate (ranging from 0% to 0.75%).
- The applicable rates are based on the Company's consolidated total leverage ratio (defined as the ratio of (a) consolidated funded indebtedness less cash that is not subject to any restriction on the use or investment thereof to (b) consolidated EBITDA at the time of the applicable borrowing).

The Company will pay an annual commitment fee ranging from 0.15% to 0.30%, based on the Company's consolidated total leverage ratio, on the amount available for borrowing under the revolving 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 June 30, 2018, the Company was

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

in compliance with all such covenants. The Company capitalized \$0.5 million of incremental financing costs in 2017 in connection with modifications to the Senior Credit Facility. In connection with the May 2018 Amendment, the Company capitalized \$4.2 million of financing costs and wrote off \$0.8 million of previously capitalized financing costs during the second quarter of 2018.

In October 2017, the Company capitalized \$19.1 million of incremental financing costs related to the drawing of the Term Loan A-1 component of the Senior Credit Facility.

At June 30, 2018 and December 31, 2017, there were \$590.0 million and \$655.0 million outstanding, respectively, under the revolving credit component of the Senior Credit Facility at weighted average interest rates of 3.8% and 3.7%, respectively. At June 30, 2018 and December 31, 2017, there were \$900.0 million and \$1.2 billion outstanding, respectively, under the Term Loan component of the Senior Credit Facility at weighted average interest rates of 3.7% and 3.6%, respectively. At June 30, 2018, there was approximately \$709.4 million available for borrowing under the Senior Credit Facility.

The fair value of outstanding borrowings of the Senior Credit Facility's revolving credit and Term Loan components at June 30, 2018 was approximately \$562.7 million and, \$868.6 million, respectively. These fair values were 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.

Letters of credit outstanding as of June 30, 2018 and December 31, 2017 totaled \$0.6 million. There were no amounts drawn as of June 30, 2018.

Contractual repayments of the Term Loan component of the Senior Credit Facility are due as follows:

Year Ended December 31,	Principal Repayment (In thousands)
Remainder of 2018	—
2019	22,500
2020	45,000
2021	56,250
2022	\$ 67,500
2023	\$ 708,750
	\$ 900,000

The outstanding balance of the revolving credit component of the Senior Credit Facility is due on May 3, 2023.

## 7. DERIVATIVE INSTRUMENTS

### Interest Rate Hedging

The Company's interest rate risk relates to U.S. dollar denominated variable interest rate borrowings. The Company uses interest rate swap derivative instruments to manage earnings and cash flow exposure resulting from changes in interest rates. These interest rate swaps apply a fixed interest rate on a portion of our expected LIBOR-indexed floating-rate borrowings. The Company held the following interest rate swaps as of June 30, 2018 (amounts in thousands):

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

Hedged Item	Current Notional Amount	Designation Date	Effective Date	Termination Date	Fixed Interest Rate	Floating Rate	Estimated Fair Value Assets (Liabilities)
3-month USD LIBOR Loan	\$50,000	June 22, 2016	December 31, 2016	June 30, 2019	1.062 %	3-month USD LIBOR	\$ 735
3-month USD LIBOR Loan	50,000	June 22, 2016	December 31, 2016	June 30, 2019	1.062 %	3-month USD LIBOR	892
1-month USD LIBOR Loan	50,000	July 12, 2016	December 31, 2016	June 30, 2019	0.825 %	1-month USD LIBOR	777
3-month USD LIBOR Loan	50,000	February 6, 2017	June 30, 2017	June 30, 2020	1.834 %	3-month USD LIBOR	742
1-month USD LIBOR Loan	100,000	February 6, 2017	June 30, 2017	June 30, 2020	1.652 %	1-month USD LIBOR	1,855
1-month USD LIBOR Loan	100,000	March 27, 2017	December 31, 2017	June 30, 2021	1.971 %	1-month USD LIBOR	2,033
1-month USD LIBOR Loan	150,000	December 13, 2017	January 1, 2018	December 31, 2022	2.201 %	1-month USD LIBOR	3,431
1-month USD LIBOR Loan	150,000	December 13, 2017	January 1, 2018	December 31, 2022	2.201 %	1-month USD LIBOR	3,400
1-month USD LIBOR Loan	100,000	December 13, 2017	July 1, 2019	June 30, 2024	2.423 %	1-month USD LIBOR	2,093
1-month USD LIBOR Loan	50,000	December 13, 2017	July 1, 2019	June 30, 2024	2.423 %	1-month USD LIBOR	973
1-month USD LIBOR Loan	200,000	December 13, 2017	January 1, 2018	December 31, 2024	2.313 %	1-month USD LIBOR	5,413
Total interest rate derivatives designated as cash flow hedge	\$1,050,000						\$ 22,344

The Company has designated these derivative instruments as cash flow hedges. The Company assesses the effectiveness of these derivative instruments and has recorded the changes in the fair value of the 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 affected earnings, at which point any gain or loss was 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 remaining amount of any gain or loss on the related cash flow hedge recorded in AOCI to interest



expense at that time.

#### 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 assesses the effectiveness of the contracts that are designated as hedging instruments. The changes in fair value of foreign currency cash flow hedges are recorded in AOCI, net of tax, until the hedged item affects earnings. Once the related hedged item affects earnings, the Company reclassifies amounts recorded in AOCI 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. For contracts not designated as hedging instruments, the changes in fair value of the contracts are recognized in other income (expense), net in the consolidated statements of operation, along with the offsetting foreign currency gain or loss on the underlying assets or liabilities.

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

On November 28, 2017, the Company entered into a foreign currency forward contract, with a notional amount of \$8.9 million, to mitigate the foreign currency exchange risk related to a certain intercompany loan denominated in Swiss Francs ("CHF"). The contract is not designated as a hedging instrument. For the three and six months ended June 30, 2018, the Company recognized a \$0.2 million loss from the change in fair value of the contract, which was included in other income (expense), net in the consolidated statement of operations. The fair value of the foreign currency forward contract was an asset of \$0.2 million as of June 30, 2018, that is included in prepaid expenses and other current assets in the consolidated balance sheet.

#### Cross-Currency Rate Swap

On October 2, 2017, the Company entered into cross-currency swap agreements to convert a notional amount of \$300.0 million equivalent to 291.2 million of CHF denominated intercompany loans into U.S. dollars. The CHF-denominated intercompany loans were the result of the purchase of intellectual property by a subsidiary in Switzerland as part of the Codman Acquisition. The objective of these cross-currency swaps is to reduce volatility of earnings and cash flows associated with changes in the foreign currency exchange rate. Under the terms of these contracts, which have been designated as cash flow hedges, the Company will make interest payments in Swiss Francs and receive interest in U.S. dollars. Upon the maturity of these contracts, the Company will pay the principal amount of the loans in Swiss Francs and receive U.S. dollars from the counterparties.

The Company held the following cross-currency rate swaps as of June 30, 2018 (dollar amounts in thousands):

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

	Effective Date	Termination Date	Fixed Rate	Aggregate Notional Amount	Fair Value Liability
Pay CHF Receive U.S.\$	October 2, 2017	October 2, 2020	1.75% 4.38%	CHF 97,065 \$ 100,000	\$ 73
Pay CHF Receive U.S.\$	October 2, 2017	October 2, 2021	1.85% 4.46%	CHF 48,533 \$ 50,000	(256 )
Pay CHF Receive U.S.\$	October 2, 2017	October 2, 2022	1.95% 4.52%	CHF 145,598 \$ 150,000	(1,671 )
Total					\$ (1,854 )

The cross-currency swaps were carried on the consolidated balance sheet at fair value, and changes in the fair values were recorded as unrealized gains or losses in AOCI. For the three and six months ended June 30, 2018, the Company recorded a gain of \$11.3 million and \$4.9 million in other income (expense), net for the foreign currency rate translation to offset the gains or losses recognized on the intercompany loans. For the three and six months ended June 30, 2018, the Company recorded gains of \$13.0 million and \$6.1 million in AOCI related to the change in fair value of the cross-currency swap and gains of \$2.0 million and \$3.9 million in other income, net included in the consolidated statements of operations related to the interest rate differential of the cross-currency swap. As of June 30, 2018, an estimated gain of \$7.7 million is expected to be reclassified within the next twelve months to other income, net from AOCI. As of June 30, 2018, the Company does not expect any gains or losses will be reclassified into earnings as a result of the discontinuance of these cash flow hedges because the original forecasted transaction will not occur.

#### 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 is subject to collateral or other security arrangements, and none contain provisions that depend upon the Company's credit ratings from any credit rating agency.

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

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 terms of the derivative instruments. The fair value of the interest rate swaps and the cross-currency 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 June 30, 2018 and December 31, 2017:

Location on Balance Sheet <sup>(1)</sup> :	Fair Value as of June 30, 2018    December 31, 2017 (In thousands)	
Derivatives designated as hedges — Assets:		
Prepaid expenses and other current assets		
Interest rate swap <sup>(2)</sup>	\$4,817	\$ 1,521
Cross-currency swap	7,691	7,757
Other assets		
Interest rate swap <sup>(2)</sup>	17,527	2,491
Cross-currency swap	—	—
Total derivatives designated as hedges — Assets	\$30,035	\$ 11,769
Derivatives designated as hedges — Liabilities:		
Accrued expenses and other current liabilities		
Interest rate swap <sup>(2)</sup>	\$—	\$ 1,845
Cross-currency swap	—	—
Other liabilities		
Interest rate swap <sup>(2)</sup>	—	1,575
Cross-currency swap	9,545	11,714
Total derivatives designated as hedges — Liabilities	\$9,545	\$ 15,134

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

(2) At June 30, 2018 and December 31, 2017, the notional amount related to the Company's interest rate swaps was \$1.05 billion. The notional amount will be reduced by \$150.0 million in June 2019.

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

The following presents the effect of derivative instruments designated as cash flow hedges on the accompanying condensed consolidated statement of operations during the three and six months ended June 30, 2018 and 2017:

	Balance in AOCI Beginning of Quarter	Amount of Gain (Loss) Recognized in AOCI	Amount of Gain (Loss) Reclassified from AOCI into Earnings	Balance in AOCI End of Quarter	Location in Statements of Operations
(In thousands)					
Three Months Ended June 30, 2018					
Interest rate swap	\$ 16,188	\$ 6,306	\$ 150	\$ 22,344	Interest (expense)
Cross-currency swap	(7,677 )	13,029	13,244	(7,892 )	Other income (expense)
	\$ 8,511	\$ 19,335	\$ 13,394	\$ 14,452	
Three Months Ended June 30, 2017					
Interest rate swap	\$ 2,479	\$ (1,500 )	\$ 44	\$ 935	Interest (expense)
	\$ 2,479	\$ (1,500 )	\$ 44	\$ 935	
	Balance in AOCI Beginning of Year	Amount of Gain (Loss) Recognized in AOCI- Effective Portion	Amount of Gain (Loss) Reclassified from AOCI into Earnings-Effective Portion	Balance in AOCI End of Quarter	Location in Statements of Operations
(In thousands)					
Six Months Ended June 30, 2018					
Interest rate swap	592	21,247	(505 )	22,344	Interest (expense)
Cross-currency swap	(5,104 )	6,067	8,856	(7,892 )	Other income (expense)
	\$(4,512 )	\$ 27,314	\$ 8,351	\$ 14,452	
Six Months Ended June 30, 2017					
Interest rate swap	1,871	(914 )	(22 )	935	Interest (expense)
	\$ 1,871	\$ (914 )	\$ (22 )	\$ 935	

At June 30, 2018, the Company expects \$12.5 million of pre-tax income recorded in AOCI related to cash flow hedges to be reclassified to earnings in the next twelve months.

#### 8. STOCK-BASED COMPENSATION

As of June 30, 2018, the Company had stock options, restricted stock awards, performance stock units, contract stock awards and restricted stock unit awards outstanding under two plans, 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 three to four years from the date of grant for officers and employees, and within a year from date of grant for directors and generally

expire eight years from the grant date for employees, and from eight 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 June 30, 2018, there were approximately \$5.5 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 three years. There were 139,938 stock options granted during the six months ended June 30, 2018.

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

#### Awards of Restricted Stock and Performance Stock

Performance stock and restricted stock awards generally have requisite service periods of three years. Performance stock units 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 awards on a straight-line basis over the requisite service period. As of June 30, 2018, there were approximately \$29.9 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 263,637 restricted stock awards and 119,459 performance stock during the six months ended June 30, 2018.

The Company has no formal policy related to the repurchase of stock 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.

#### 9. DEFINED BENEFIT PLANS

The Company maintains defined benefit pension plans that cover certain employees in Austria, France, Japan, Germany and Switzerland.

Net periodic benefit costs for the Company's defined benefit pension plans for the three and six months ended June 30, 2018 were \$0.6 million and \$1.1 million, respectively. The components of the net periodic benefit costs other than the service cost component of \$0.7 million and \$1.4 million for the three and six months ended June 30, 2018, respectively, are included in other income (expense), net in consolidated statements of operation.

The Company previously disclosed in its consolidated financial statements for the year ended December 31, 2017 that it expected to contribute \$1.8 million to its defined benefit pension plans in 2018. For the six months ended June 30, 2018, the Company contributed \$1.0 million, to the defined benefit plans. As of June 30, 2018, the Company anticipates contributing an additional \$1.0 million to its defined benefit plans in 2018, for a total of \$2.0 million. The estimated fair values of plan assets were \$29.2 million and \$26.9 million as of June 30, 2018 and December 31, 2017, respectively. The net plan assets of the pension plans are invested in common trusts as of June 30, 2018 and December 31, 2017. Common trusts are classified as Level 2 in the fair value hierarchy. The fair value of common trusts is valued at the net asset value based on the fair values of the underlying investments of the trusts as determined by the sponsor of the trusts. The investment strategy of the Company's defined benefit plans is both to meet the liabilities of the plans as they fall due and to maximize the return on invested assets within an appropriate risk profile.

#### 10. TREASURY STOCK

On October 25, 2016, the Board of Directors terminated its October 2014 authorization for the repurchase of its outstanding common stock and authorized management to repurchase up to \$150.0 million of its outstanding common stock through December 31, 2018. Shares may be repurchased either in the open market or in privately negotiated transactions. As of June 30, 2018, there remained \$150.0 million available for repurchase under this authorization.

As of June 30, 2018 and December 31, 2017, there were 2.9 million shares of treasury stock outstanding with a cost of \$120.7 million and \$121.6 million, respectively, at a weighted average of \$41.77 per share.

There were no cash treasury stock repurchases during the six months ended June 30, 2018 or in 2017.

11. INCOME TAXES

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

	Three Months		Six Months	
	Ended June 30,	Ended June 30,	Ended June 30,	Ended June 30,
	2018	2017	2018	2017
Reported tax rate	10.6%	(35.4)%	(2.3)%	(35.2)%

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

The Company's effective income tax rates for the three months ended June 30, 2018 and 2017 were 10.6% and (35.4)%, respectively. For the three months ended June 30, 2018, the primary drivers of the change in rate are higher income before income taxes compared to the same period in 2017 and the inclusion of the new GILTI (as defined below) provisions of \$1.5 million and other tax reform-related changes; offset by the reduction in the federal statutory rate from 35% to 21%. The three months ended June 30, 2017 included an additional excess tax benefit of \$4.1 million from share-based compensation compared to the three months ended June 30, 2018.

The Company's effective income tax rates for the six months ended June 30, 2018 and 2017 were (2.3)% and (35.2)%, respectively. For the six months ended June 30, 2018, the primary drivers of the higher tax rate were higher income before income taxes compared to the same period in 2017, and the inclusion of the new GILTI (as defined below) provisions and other tax reform-related changes; offset by the reduction in the federal statutory rate from 35% to 21%. The six months ended June 30, 2017 included an additional tax benefit of \$4.0 million related to share-based compensation, when compared to the same period in 2018.

The Tax Cuts and Jobs Act (the "2017 Tax Act"), enacted in December 2017, made significant changes to the previous tax laws. Included among the numerous changes were a reduction of the federal statutory rate from 35% to 21%, limitations on the deductibility of interest expense and executive compensation, and the elimination of certain domestic tax deductions such as the domestic production activities deduction. Additionally, the 2017 Tax Act provided for a one-time repatriation tax on accumulated foreign subsidiaries' untaxed foreign earnings (the "Toll Tax").

The 2017 Tax Act implemented a territorial tax system and includes base erosion provisions on non-U.S. earnings, which subjects certain foreign earnings to additional taxation as global intangible low-taxed income ("GILTI"). These provisions became effective on January 1, 2018. As of June 30, 2018, the Company included GILTI related to current-year operations in its estimated annual effective tax rate but has not yet included additional GILTI on deferred tax items.

The 2017 Tax Act eliminated the deferral of U.S. income tax on unrepatriated earnings from foreign subsidiaries through the imposition of the Toll Tax, a one-time tax in 2017 on deemed repatriated foreign earnings, which is paid over an eight-year period. The tax is assessed on the foreign subsidiary accumulated foreign earnings that were not previously taxed. Foreign earnings in cash and cash equivalents are taxed at 15.5% and all other earnings are taxed at 8.0%. The calculation of the Toll Tax allows for the ability to offset positive foreign earnings with existing foreign deficits and use of foreign tax credits. The Company prepared a reasonable estimate of this tax and expects to continue to refine the estimate as it finalizes its 2017 tax returns. As of December 31, 2017, we recorded an estimated income tax expense of \$5.5 million related to the Toll Tax, of which, \$0.4 million is expected to be paid within one year. The Company continued to analyze its foreign earnings and profits ("E&P") during the six months ended June 30, 2018 and has not made any adjustments to the provisional amounts recognized during 2017. The Company will continue to refine its E&P analysis, which may affect the measurement of the Toll Tax liability.

As a result of the 2017 Tax Act's reduction of the federal statutory rate from 35% to 21%, the Company remeasured deferred tax assets and liability and recorded a tax benefit of \$43.4 million as of December 31, 2017. The Company did not record any adjustments to this provisional amount during the six months ended June 30, 2018 and will continue to analyze and refine its calculations related to the remeasurement as the impact of the 2017 Tax Act is finalized.

On December 22, 2017, the SEC staff issued Staff Accounting Bulletin No. 118 to address the application of U.S. GAAP in situations when a registrant does not have the necessary information available, prepared, or analyzed (including computations) in reasonable detail to complete the accounting for certain income tax effects of the 2017



Tax Act. The Company made reasonable estimates of the impact of the 2017 Tax Act on its consolidated financial statements as of December 31, 2017 and recognized the provisional tax impacts related to the deemed repatriated earnings and the revaluation of deferred tax assets and liabilities and included these amounts in its consolidated financial statements for the twelve months ended December 31, 2017. The ultimate impact may differ from these provisional amounts, possibly materially, due to, among other things, additional analysis, changes in interpretations and assumptions the Company has made, additional regulatory guidance that may be issued, and actions the Company may take as a result of the 2017 Tax Act.

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

## 12. NET INCOME PER SHARE

Basic and diluted net income per share was as follows:

	Three Months Ended June 30, 2018		Six Months Ended June 30, 2017	
	2018	2017	2018	2017
	(In thousands, except per share amounts)			
Basic net income per share:				
Net income	\$11,376	\$10,835	\$22,368	\$17,230
Weighted average common shares outstanding	82,423	76,213	80,491	75,487
Basic net income per common share	\$0.14	\$0.14	\$0.28	\$0.23
Diluted net income per share:				
Net income	\$11,376	\$10,835	\$22,368	\$17,230
Weighted average common shares outstanding — Basic	82,423	76,213	80,491	75,487
Effect of dilutive securities:				
Warrants	—	1,589	—	1,864
Stock options and restricted stock	1,090	1,161	1,211	1,352
Weighted average common shares for diluted earnings per share	83,513	78,963	81,702	78,703
Diluted net income per common share	\$0.14	\$0.14	\$0.27	\$0.22

Shares of common stock of approximately 0.2 million and 0.2 million at June 30, 2018 and 2017, respectively, that are issuable through the exercise of dilutive securities were not included in the computation of diluted net income per share because their effect would have been antidilutive.

In connection with the issuance of the 1.625% Convertible Senior Notes due in 2016, which the Company extinguished on December 15, 2016, the Company entered into call transactions and warrant transactions with the affiliates of the initial purchasers of such notes. The warrants expired on a series of expiration dates from March 2017 to August 2017. For the year ended December 31, 2017, the hedge participants exercised 8,707,202 warrants. As a result, the Company issued 2,839,743 shares of common stock for the year ended December 31, 2017. The company has no outstanding warrants as of June 30, 2018.

For the three and six months ended June 30, 2017, the potential excess conversion value on warrants was included in the Company's dilutive share calculation because the average stock price for the three and six months ended June 30, 2017 exceeded the conversion price.

Restricted and performance units that entitle the holders to approximately 0.5 million shares of common stock are included in the basic and diluted weighted average shares outstanding calculation because no further consideration is due related to the issuance of the underlying common shares.

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

COMPREHENSIVE INCOME

Comprehensive income was as follows:

	Three Months Ended June 30,		Six Months Ended June 30,	
	2018	2017	2018	2017
	(In thousands)			
Net income	\$11,376	\$10,835	\$22,368	\$17,230
Foreign currency translation adjustment	(27,785 )	19,484	(14,005 )	23,548
Change in unrealized (loss) gain on derivatives, net of tax	4,128	(884 )	13,032	(537 )
Unrealized (loss) on short-term investments	—	(1,291 )	—	—
Pension liability adjustment, net of tax	12	(13 )	6	(15 )
Comprehensive income, net	\$(12,269)	\$28,131	\$21,401	\$40,226

Changes in Accumulated Other Comprehensive Income by component between December 31, 2017 and June 30, 2018 are presented in the table below, net of tax:

	Cash Flow Hedges	Defined Benefit Pension Items	Foreign Currency Items	Total
	(In thousands)			
Balance at December 31, 2017	\$(2,979)	\$ (93 )	\$(20,735)	\$(23,807)
Reclassification of stranded tax effect	(532 )	—	—	(532 )
Balance at January 1, 2018	(3,511 )	(93 )	(20,735 )	(24,339 )
Other comprehensive income (loss)	19,488	6	(14,005 )	5,489
Amounts reclassified from accumulated other comprehensive income	6,456	—	—	6,456
Net current-period other comprehensive income (loss)	13,032	6	(14,005 )	(967 )
Balance at June 30, 2018	\$9,521	\$ (87 )	\$(34,740)	\$(25,306)

For the six months ended June 30, 2018, the Company reclassified \$0.4 million loss and \$6.8 million gain of loss from AOCI to interest expense and other income (expenses), net, respectively.

14. SEGMENT AND GEOGRAPHIC INFORMATION

In October 2017, as part of our branding strategy, the Company leveraged the globally recognized Codman name by rebranding the Specialty Surgical Solutions segment as Codman Specialty Surgical.

The Company internally manages two global reportable segments and reports the results of its businesses to its chief operating decision maker. The two reportable segments and their activities are described below.

The Codman Specialty Surgical segment includes (i) the Neurosurgery business, which sells a full line of products for neurosurgery and neuro critical care such as tissue ablation equipment, dural repair products, cerebral spinal fluid management devices, intracranial monitoring equipment, and cranial stabilization equipment and (ii) the precision tools and instruments business, which sells more than 60,000 instrument patterns and surgical and lighting products to hospitals, surgery centers, dental, podiatry, and veterinary offices.

The Orthopedics and Tissue Technologies segment 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 products.

The Corporate and other category includes (i) various executive, finance, human resource, information systems and legal functions, (ii) brand management, and (iii) share-based compensation costs.

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

25

---

INTEGRA LIFESCIENCES HOLDINGS CORPORATION  
 NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)  
 (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 and six months ended June 30, 2018 and 2017 are as follows:

	Three Months Ended		Six Months Ended	
	June 30, 2018	2017	June 30, 2018	2017
	(In thousands)			
Segment Net Sales				
Codman Specialty Surgical	\$239,504	\$159,857	\$475,619	\$316,147
Orthopedics and Tissue Technologies	126,686	122,307	247,653	224,654
Total revenues	\$366,190	\$282,164	\$723,272	\$540,801
Segment Profit				
Codman Specialty Surgical	\$91,118	\$67,250	\$180,609	\$129,953
Orthopedics and Tissue Technologies	37,141	31,010	69,579	58,089
Segment profit	128,259	98,260	250,188	188,042
Amortization	(5,286 )	(5,419)	(10,676)	(9,520)
Corporate and other	(95,339 )	(75,856 )	(186,299)	(151,577 )
Operating income	\$27,634	\$16,985	\$53,213	\$26,945

The Company does not allocate any assets to the reportable segments. No asset information is reported to the chief operating decision maker and disclosed in the financial information for each segment.

The Company attributes revenues to geographic areas based on the location of the customer. Total revenue by major geographic area consisted of the following:

	Three Months		Six Months Ended	
	Ended June 30, 2018	2017	June 30, 2018	2017
	(In thousands)			
United States	\$259,711	\$219,266	\$508,639	\$420,363
Europe	51,405	32,499	103,178	61,315
Asia Pacific	35,497	15,565	71,282	31,653
Rest of World	19,577	14,834	40,173	27,470
Total Revenues	\$366,190	\$282,164	\$723,272	\$540,801

#### 15. 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 it sells. 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 the Company's 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.

TEI, acquired by Integra on July 17, 2015, manufactures a bovine-derived surgical mesh product for Boston Scientific Corporation ("BSC") and has been named as a defendant in lawsuits under a broad range of products liability theories, many of which have not been served on TEI. As of June 30, 2018, only ten active cases remained against TEI.

Pursuant to an indemnification agreement with BSC (i) BSC is managing the litigation; and (ii) TEI has in place a product liability insurance policy, of which it must exhaust \$3.0 million before BSC's indemnity begins to cover relevant claims (and of which only a small portion has been utilized to date and against which the insurer has reserved the entire \$3.0 million). Because the thrust of products liability litigation focuses on synthetic surgical mesh products, counsel is filing motions to dismiss on behalf of TEI in many cases. In addition, Integra has certain protections in the merger agreements with TEI which would indemnify it for approximately \$30.0 million for the first

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

fifteen months after closing and between \$20.0 and \$30.0 million for the remainder of the three-year period after closing for losses relating to a variety of matters, including half of certain products liability claims (including those related to the product it manufactures for BSC) not covered by insurance. As of July 26, 2018, no indemnification payments were received nor owed in relation to the lawsuits.

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.

#### Contingent Consideration

The Company determined the fair value of contingent consideration during the three and six-month period ended June 30, 2018 and 2017 to reflect the change in estimate, additions, payments, transfers and the time value of money during the period.

A reconciliation of the opening balances to the closing balances of these Level 3 measurements for the six months ended June 30, 2018 and 2017 is as follows (in thousands):

	Contingent Considerations Liabilities Related to Acquisition of Derma Sciences (See Note 2) Short-term	Contingent Consideration Liability Related to Acquisition of Confluent Surgical, Inc. Short-term	Contingent Consideration Liability Related to Acquisition of Confluent Surgical, Inc. Short-term	Location in Financial Statements
Six Months Ended June 30, 2018				
Balance as of January 1, 2018	\$315	\$ 1,387	\$ 22,478	
Transfers from long-term to current portion	1,387	(1,387 )		
Payments	(2,000)		(19,000 )	
Loss from change in fair value of contingent consideration liabilities	298	230	1,422	Selling, general and administrative
Balance as of June 30, 2018	\$—	\$ 230	\$ 4,900	
Six Months Ended June 30, 2017				
Balance as of January 1, 2017	\$—	\$ —	\$—	\$ 22,036
Additions from acquisition of Derma Sciences	33,707	3,467	—	—
Transfers from long-term to current portion	—	—	4,662	(4,662 )
Payments	(26,598)	—	—	—
(Gain)/Loss from change in fair value of contingent consideration liabilities	(2,359 )	82	—	148
Balance as of June 30, 2017	\$4,750	\$ 3,549	\$4,662	\$ 17,522

On January 15, 2014, the Company acquired all outstanding shares of Confluent Surgical, Inc., ("Confluent Surgical"). The purchase price includes contingent consideration. The potential maximum undiscounted contingent consideration of \$30.0 million consists of \$25.0 million upon obtaining certain U.S. governmental approvals (the "U.S. Contingent Consideration") and \$5.0 million upon obtaining certain European governmental approvals, both

related to the completion of the transition of the Confluent Surgical business. The U.S. Contingent Consideration is subject to adjustment to reduce the amount of maximum payment based on the timing of obtaining the U.S. governmental approval up to the minimum of \$19.0 million. The fair values of contingent consideration related to the acquisition of Confluent Surgical were estimated using a discounted cash flow model using discount rate of 2.2%. In March 2018, the Company received the U.S. governmental approvals and adjusted the related contingent consideration liability to \$19.0 million, which the Company paid in April 2018. The Company expects to receive the European governmental approvals and pay the related contingent consideration liability within the next twelve months.

The Company assesses these assumptions on an ongoing basis as additional information affecting the assumptions is obtained. The contingent consideration balance was included in accrued expenses and other current liabilities and other liabilities at June 30, 2018 and June 30, 2017.



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

28

---

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

Supply Agreement Liability and Above Market Supply Agreement Liability

On January 15, 2014, the Company entered into a transitional supply agreement with Covidien Group S.a.r.l ("Covidien"). This agreement contains financial incentives to Covidien for the timely supply of products each fiscal quarter through the third anniversary of the agreement. The prices paid under the supply agreement were essentially flat through the third anniversary of the agreement, and then increase significantly in each of the following three years. The Company determined the fair value of its supply agreement liability and above market supply agreement liability with Covidien during the six-month periods ended June 30, 2018 and 2017 to reflect the payments, change in estimate and the time value of money during the period.

A reconciliation of the opening balances to the closing balances of these Level 3 measurements is as follows (amounts in thousands):

	Above Market Supply Agreement Liability - Short-term	Location in Financial Statements		
Six Months Ended June 30, 2018				
Balance as of January 1, 2018	\$ 2,641			
Payments	(1,110 )			
Gain from change in fair value	(980 )	Selling, general and administrative		
Transfer to accounts payable	(248 )			
Balance as of June 30, 2018	\$ 303			
	Supply Agreement Liability - Short-term	Above Market Supply Agreement Liability - Short- Term	Above Market Supply Agreement Liability - Long-term	Location in Financial Statements
Six Months Ended June 30, 2017				
Balance as of January 1, 2017	\$ 166	\$ —	\$ 2,648	
Payments	(166 )	—	(155 )	
Transfer from long-term to current portion	—	1,752	(1,752 )	
Loss from increase in fair value	—	—	59	Selling, general and administrative
Balance as of June 30, 2017	\$ —	\$ 1,752	\$ 800	

The fair values of supply agreement liability and above market supply agreement liability were estimated using a discounted cash flow model using a discount rate of 12.0%. The Company assesses these assumptions on an ongoing basis as additional information impacting the assumptions is obtained. The above market supply agreement liability - short-term was included in accrued expenses and other current liabilities at June 30, 2018 and December 31, 2017.

There are no transfers between level 1, 2 or 3 during the six months ended June 30, 2018 and 2017. If the Company's estimate regarding the fair value of its contingent consideration liabilities, supply agreement liability and above market supply agreement liability are inaccurate, a future adjustment to these estimated fair values may be required which could change significantly.

BioD

On April 7, 2017, the Company's indirect wholly-owned subsidiary, BioD filed an action in the Superior Court of New Jersey, Chancery Division, Middlesex County seeking a declaration that the resignation of Russell Olsen, the former

CEO of BioD, was “for Good Reason” (as defined in Olsen’s employment agreement); a finding that Olsen breached the implied covenant of good faith and fair dealing, committed legal fraud, equitable fraud and negligent misrepresentation; and an award of damages for such actions, including a return of severance fees paid to Olsen. BioD was acquired in August 2016 by Derma Sciences, which Integra subsequently acquired in February 2017. After receiving a job offer from Integra that Olsen believed materially diminished his title and authority, on February 24, 2017 Olsen indicated his intention to terminate his position with BioD for Good Reason, as otherwise permitted by his employment agreement with BioD. Shortly thereafter, Cynthia Weatherly (as representative of the former equity owners of BioD) claimed in a letter to Derma Sciences that Olsen’s resignation was a “termination Without Cause” (as also defined in Olsen’s employment agreement), which would arguably trigger an acceleration of the earn out under a merger agreement between Derma Sciences, BioD and other parties (the "BioD Merger Agreement"), which was entered into in July 2016,

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

and require as a result of the acceleration the payment of \$26.5 million by BioD. As previously disclosed and described in Note 2 - Business Acquisitions and Divestiture, Integra assumed this contingent liability in connection with its acquisition of Derma Sciences. The action for a declaratory judgment was filed to clarify that Olsen's termination was for Good Reason and not Without Cause. If the employment agreement was terminated for Good Reason, then the Company believes that the earn out provision under the BioD Merger Agreement should not be accelerated and the likelihood of loss is remote.

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, 2017 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 and other matters. Our actual results could 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, 2017, and under the heading "Risk Factor" 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," "might," "could," "will," "estimate," "continue," "anticipate," "intend," "seek," "plan," "expect," "should," "would" and similar expressions in this report.

GENERAL

Integra is a worldwide leader in medical technology focused on limiting uncertainty for surgeons so that they can concentrate on providing the best patient care. Integra provides customers with clinically relevant, innovative and cost-effective products that improve the quality of life for patients. We focus on cranial procedures, small bone and joint reconstruction, the repair and reconstruction of soft tissue, and instruments for surgery.

We manufacture and sell our products in two reportable business segments: Codman Specialty Surgical and Orthopedics and Tissue Technologies. Our Codman Specialty Surgical products offer specialty surgical implants and instrumentation for a broad range of specialties. This product category includes products and solutions for dural access and repair, precision tools and instruments, advanced energy, cerebral spinal fluid (CSF) management and neuro monitoring including market-leading product portfolios used in neurosurgery operation suites and critical care units. Our Orthopedics and Tissue Technologies products portfolios consists of differentiated regenerative technology products for soft tissue repair and tissue regeneration products, and small bone fixation and joint replacement hardware products for both upper extremities and lower extremities. This business also includes private-label sales of a broad set of our regenerative and wound care medicine technologies.

We manufacture many of our products in plants located in the United States (the "U.S."), France, Germany, Ireland, Mexico, Puerto Rico and Switzerland. We also source most of our handheld surgical instruments, specialty metal and pyrocarbon implants, and dural sealant products through specialized third-party vendors.

Codman Specialty Surgical products are sold through a combination of directly employed sales representatives, distributors and wholesalers, depending on the customer call point. During the first half of 2018, we integrated the commercial teams from the acquired global Codman Neurosurgery and legacy Integra businesses.

Orthopedics and Tissue Technologies products are sold through directly employed sales representatives, distributors focused on their respective surgical specialties and strategic partners. During the first half of 2018, we completed the expansion of our sales channels by establishing dedicated teams for the extremity orthopedics, acute wound

reconstruction, outpatient wound care and surgical reconstruction markets. We added 60 sales positions across these channels which will improve our focus and competitiveness and better align our product portfolio with our clinical customers.

Our objective is to become 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 becoming a company recognized as a leader by our customers worldwide in specialty surgical applications, regenerative technologies and extremities orthopedics. Our strategy is built around four pillars: 1) building an execution-focused culture, 2) achieving relevant scale, 3) improving agility and innovations, and 4) leading in customer excellence. These four pillars support our strategic initiatives to deliver on our commitments through improved planning and communication, optimizing our infrastructure, and strategically aligned tuck-in acquisitions.

Table of Contents

We aim to achieve growth in our revenues while maintaining strong financial results. While we pay attention to any meaningful trend in our financial results, we pay particular attention to measurements that are indicative of long-term profitable growth. These measurements include (1) revenue growth (including organic growth and acquisitions), (2) gross margins on total revenues, (3) earnings before interest, taxes, depreciation, and amortization, (4) earnings per diluted share of common stock, and (5) operating cash flows.

We believe that we are particularly effective in the following aspects of our business:

**Regenerative Technology Platform.** We have developed numerous product lines through our proprietary collagen, amniotic tissue, and polyethylene glycol technologies that are sold through all our sales channels.

**Diversification and Platform Synergies.** The selling platforms of Codman Specialty Surgical and Orthopedics and Tissue Technologies each contribute a different strength to our core business. Codman Specialty Surgical provides us with a strong presence in the hospital, with market-leading products and comprehensive solutions for surgical specialties, such as neurosurgery, as well as a strong capacity to generate cash flows. Orthopedics and Tissue Technologies enables us to grow our top line by continuing to introduce new, differentiated products in fast-growing markets, such as small joint replacement and advanced wound care, as well as to increase gross margins. We generate synergies between these platforms, such as our regenerative technology, instrument sourcing capabilities, and enterprise contract management.

**Specialized Sales Footprint**