ORTHOFIX INTERNATIONAL N V
Form 10-Q/A
March 31, 2015
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UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, DC 20549

FORM 10-Q/A

(Amendment No. 1)

(Mark one)

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

For the quarterly period ended March 31, 2014

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 Number: 0-19961

ORTHOFIX INTERNATIONAL N.V.

(Exact name of registrant as specified in its charter)

Curaçao	**Not applicable**
(State or other jurisdiction of	**(I.R.S. Employer**
incorporation or organization)	**Identification No.)**
7 Abraham de Veerstraat	
Curaçao	**Not applicable**
(Address of principal executive offices)	**(Zip Code)**

599-9-4658525

(Registrant s telephone number, including area code)

Not applicable

(Former name, former address and former fiscal year, if changed since last report)

Indicate by check mark whether the registrant: (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. ¨ Yes x No

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). ¨ Yes x No

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or smaller reporting company. See definition of large accelerated filer, accelerated filer, non-accelerated filer and smaller reporting company in Rule 12b-2 of the Exchange Act.

Large Accelerated filer ¨	Accelerated filer x
Non-Accelerated filer ¨ (Do not check if a smaller reporting company)	Smaller Reporting Company ¨

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

As of March 27, 2015, 18,754,831 shares of common stock were issued and outstanding.

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EXPLANATORY NOTE

Orthofix International N.V. (together with its respective consolidated subsidiaries and affiliates, the Company, sometimes referred to as we , us or our) is filing this amendment (this Amendment or Form 10-Q/A) to its Quarte Report on Form 10-Q for the fiscal quarter ended March 31, 2014, which was originally filed on May 8, 2014 (the Original Form 10-Q).

In connection with the Company s preparation of its consolidated interim quarterly financial statements for the fiscal quarter ended June 30, 2014, the Company determined that certain manual journal entries with respect to the previously filed financial statements contained in the Original Form 10-Q and the Company s originally filed Annual Report on Form 10-K for the fiscal year ended December 31, 2013 (the Original 2013 Form 10-K) were not properly accounted for under U.S. generally accepted accounting principles (U.S. GAAP). As further described below, these additional errors affect the fiscal years ended December 31, 2013, 2012 and 2011, as well as the fiscal quarter ended March 31, 2014 and other prior periods. Due to these errors, the Company determined in August 2014 to restate its consolidated financial statements for the fiscal years ended December 31, 2013, 2012 and 2011 (including the interim quarterly periods contained within the fiscal years ended December 31, 2013 and 2012) and the fiscal quarter ended March 31, 2014, and that the previously filed financial statements for these periods (including those contained in the Original 2013 Form 10-K and the Original Form 10-Q) should no longer be relied upon. This Form 10-Q/A contains restated consolidated interim financial statements for the fiscal quarters ended March 31, 2014 and 2013.

Contemporaneously with the filing of this Form 10-Q/A, the Company is filing (i) an amendment to the 2013 Form 10-K (the 2013 Form 10-K/A), which amendment contains restated consolidated financial statements for the fiscal years ended December 31, 2013, 2012 and 2011, and (ii) its delayed Quarterly Reports on Form 10-Q for the fiscal quarters ended June 30, 2014 (the 2014 Second Quarter Form 10-Q) and September 30, 2014 (the 2014 Third Quarter Form 10-Q), which contain restated consolidated interim financial statements for the fiscal quarterly and year to date periods ended June 30, 2013 and September 30, 2013, respectively. The corrections of the additional errors in this Form 10-Q/A and the 2013 Form 10-K/A are referred to herein as the Further Restatement.

The Original 2013 Form 10-K reflected a prior restatement of the Company s consolidated financial statements for the fiscal years ended December 31, 2012 and 2011 and the fiscal quarter ended March 31, 2013, which we refer to herein as the Original Restatement.

Description of the Further Restatement

The errors corrected by the Further Restatement are as follows:

A majority of revenue from the Company s BioStim SBU is derived from third parties, which is subject to change due to contractual adjustments related to commercial insurance carriers, and may include certain patient co-pay amounts. The Company previously recorded certain co-pay and self-pay amounts as revenue with estimated uncollectible portions being recognized as bad debt expense. Given the collectability of co-pay and self-pay amounts was not reasonably assured, the conditions for revenue recognition had not been met and revenue for those amounts should not have been recognized until collected. Adjustments to correct the foregoing reduce equally both the Company s historical net sales and its sales and marketing expense by approximately $2.2 million, $9.0 million and $6.0 million for the fiscal years ended December 31, 2013, 2012 and 2011, respectively, and $1.4 million for the fiscal quarter ended March 31, 2014. Additionally, there was $1.4 million in the fiscal quarter ended March 31, 2014 related to contractual amounts from commercial insurance carriers which was incorrectly classified to bad debt expense rather than a reduction of revenue, for a total reduction to bad debt and revenue of $2.8 million for the fiscal quarter ended March 31, 2014. These adjustments have no effect on net income from continuing operations or net income in those periods.

Certain bad debt reserves originally recorded in fiscal years 2011 and 2012 were reversed in incorrect periods in the Original Restatement in connection with the change to sell-through accounting for certain distributors. As a result, sales and marketing expense was understated by approximately $1.5 million and $1.1 million for the fiscal years ended December 31, 2013 and 2012, respectively, and overstated by approximately $2.1 million for the fiscal year ended December 31, 2011.

As part of analyzing collections experience on accounts receivable, the Company identified that it had incorrectly considered certain deferred revenue amounts included in gross accounts receivable when calculating estimated reserves. Specifically, the computation of the contractual allowances and bad debt allowances, which serves to adjust accounts receivable to the estimated collectible amount, incorrectly assumed that some percentage of deferred amounts would be collected, rather than fully deferring these amounts. Adjustments to correct this error resulted in a net decrease in operating income of $0.7 million and $0.2 million for the fiscal years ended December 31, 2013 and 2011, respectively, and a net increase in operating income of $2.1 million for the fiscal year ended December 31, 2012, as well as a net decrease in operating loss of $1.5 million for the fiscal quarter ended March 31, 2014.

As part of the Original Restatement, the Company made certain corrections to prior period excess and obsolete inventory reserves. The effect of these corrections was not considered when determining the adjustments needed to eliminate intercompany profits from inventories in the Original Restatement. Adjustments to correct this error resulted in an increase to cost of sales of $1.1 million, $0.2 million and $0.3 million for the fiscal years ended December 31, 2013, 2012 and 2011, respectively, as well as an increase to cost of sales of $3.0 million for the fiscal quarter ended March 31, 2014.

As part of the remediation activities that followed the Original Restatement, the Company expanded its procedures in the second quarter of 2014 to validate the existence of field inventory held by independent sales representatives and noted that, in many cases, this inventory had higher rates of missing inventory (shrinkage) than previously estimated. To determine whether these higher error rates were pervasive across its field inventory, the Company counted approximately 90% of its field inventory during the third and fourth fiscal quarters of 2014. These counts resulted in the identification of errors relating to previous estimates of shrinkage. Adjustments in the Further Restatement to correct these errors, net of the related effect on previously recorded excess and obsolete inventory reserves, resulted in an increase to cost of sales of $0.4 million, $0.3 million and $0.2 million for the fiscal years ended December 31, 2013, 2012 and 2011, respectively, as well as an increase to cost of sales of $0.2 million for the fiscal quarter ended March 31, 2014.

In connection with its remediation efforts associated with the material weakness noted in the Original Restatement related to inventory reserves, including performing a hindsight analysis of previously established reserves, the Company concluded that it was not appropriately calculating inventory reserves, including its consideration of demand assumptions for kits , which contain a variety of piece part components to be used during surgery as well as inventory held by third parties under inventory purchase obligations. Adjustments to correct this error resulted in an increase to cost of sales of $3.2 million, $1.5 million and $0.1

million for the fiscal years ended December 31, 2013, 2012 and 2011, respectively, as well as an increase to cost of sales of $2.4 million for the fiscal quarter ended March 31, 2014.

In addition to the adjustments described above, the Company is correcting certain other items. The impact of correcting these items results in a decrease to income tax expense of $0.5 million and $1.1 million for the fiscal years ended December 31, 2013 and 2012, respectively, to correct an income tax payable error that was recorded during the Original Restatement; these adjustments are separate from the tax effect of the errors described above.

In the aggregate, the remaining additional adjustments resulted in a decrease to loss before income taxes of $1.1 million for the fiscal year ended December 31, 2013, a decrease to income before income taxes of $0.1 million for the fiscal year ended December 31, 2012 and a increase to loss before income taxes of $0.7 million for the fiscal year ended December 31, 2011, as well as a decrease to loss before income taxes of $1.6 million for the fiscal quarter ended March 31, 2014.

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Items Amended by this Form 10-Q/A

For the convenience of the reader, this Form 10-Q/A sets forth the Original Form 10-Q, as modified and superseded where necessary to reflect the Further Restatement. Specifically, the following items included in the Original Form 10-Q are amended by this Form 10-Q/A:

- Part I, Item 1, Financial Statements
- Part I, Item 2, Management s Discussion and Analysis of Financial Condition and Results of Operations
- Part I, Item 4, Controls and Procedures
- Part II, Item 1, Legal Proceedings
- Part II, Item 1A, Risk Factors
- Part II, Item 6, Exhibits

The correction of the errors described above is further discussed in Note 2 to the consolidated financial statements included in Part I, Item 1 herein and in Part I, Item 2, Management s Discussion and Analysis of Financial Condition and Results of Operations.

Other than this Form 10-Q/A and the 2013 Form 10-K/A, we do not intend to file any other amended reports in connection with the Further Restatement. All of our future Annual Reports on Form 10-K and Quarterly Reports on Form 10-Q will reflect the restated information included in this Form 10-Q/A and the 2013 Form 10-K/A, as applicable.

Other than with respect to matters related to the Further Restatement (including consequences of the Company s delay in filing the 2014 Second Quarter Form 10-Q and the 2014 Third Quarter Form 10-Q), this Form 10-Q/A generally does not reflect events that have occurred after May 8, 2014, the filing date of the Original Form 10-Q, or modify or update the disclosures presented in the Original Form 10-Q, except to reflect the effects of the restatement. Accordingly, this Form 10-Q/A should be read in conjunction with (i) the Company s Current Reports on Form 8-K filed with the Commission since May 8, 2014, (ii) the 2013 Form 10-K/A, (iii) the 2014 Second Quarter Form 10-Q and (iv) the 2014 Third Quarter Form 10-Q.

The Company s current Chief Executive Officer and Interim Chief Financial Officer have issued certifications required by Sections 302 and 906 of the Sarbanes-Oxley Act of 2002 in connection with this Form 10-Q/A. The certifications are included in this Form 10-Q/A and Exhibits 31.1, 31.2 and 32.1.

Internal Control Considerations

In connection with the Further Restatement, management has re-evaluated the effectiveness of our disclosure controls and procedures as of December 31, 2013 and the effectiveness of the Company s internal control over financial reporting as of December 31, 2013 based on the framework in Internal Control Integrated Framework (1992 framework) issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO). Based on such re-evaluation, management confirmed that the material weaknesses described in the Original Form 10-Q continue to be material weaknesses as of the time of the re-evaluation, and that some of these same material weaknesses contributed to the Further Restatement. In addition, the re-evaluation concluded that two additional material weaknesses existed related to (i) the calculation of our accounts receivable reserve, and (ii) the oversight of field inventory held by our independent sales representatives, which also contributed to the Further Restatement.

For a discussion of management s consideration of our disclosure controls and procedures and the material weaknesses identified, see Part I, Item 4 of this Form 10-Q/A, as well Part II, Item 9A, Controls and Procedures of the 2013 Form 10-K/A.

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Forward-Looking Statements

This report contains forward-looking statements within the meaning of Section 21E of the Securities Exchange Act of 1934, as amended, and Section 27A of the Securities Act of 1933, as amended, relating to our business and financial outlook, which are based on our current beliefs, assumptions, expectations, estimates, forecasts and projections. In some cases, you can identify forward-looking statements by terminology such as may, will, should, expects, plans anticipates, believes, estimates, projects, intends, predicts, potential or continue or other comparable te These forward-looking statements are not guarantees of our future performance and involve risks, uncertainties, estimates and assumptions that are difficult to predict. Therefore, our actual outcomes and results may differ materially from those expressed in these forward-looking statements. You should not place undue reliance on any of these forward-looking statements. Further, any forward-looking statement speaks only as of May 8, 2014, the date on which the Original Form 10-Q was filed, unless it is specifically otherwise stated to be made as of a different date, or refers to matters related to the Further Restatement (including consequences of the Company s delay in filing the 2014 Second Quarter Form 10-Q and the 2014 Third Quarter Form 10-Q). We undertake no obligation to further update any such statement to reflect new information, the occurrence of future events or circumstances or otherwise.

The forward-looking statements in this filing do not constitute guarantees or promises of future performance. Factors that could cause or contribute to such differences may include, but are not limited to, risks relating to our recent Audit Committee accounting matters review, the restatements of our financial statements for certain prior periods described herein and in the 2013 Form 10-K/A, and related legal proceedings (including potential action by the Division of Enforcement of the SEC and pending securities class action litigation), the Company s review of allegations of improper payments involving the Company s Brazil-based subsidiary, the Company s previous and current non-compliance with certain Nasdaq Stock Market LLC listing rules, and related pending hearings proceedings in connection therewith, the expected sales of our products, including recently launched products, unanticipated expenditures, changing relationships with customers, suppliers, strategic partners and lenders, changes to and the interpretation of governmental regulations, the resolution of pending litigation matters (including our indemnification obligations with respect to certain product liability claims against, and the government investigation of, our former sports medicine global business unit), our ongoing compliance obligations under a corporate integrity agreement with the Office of Inspector General of the Department of Health and Human Services (and related terms of probation), a deferred prosecution agreement with the U.S. Department of Justice and a consent decree with the SEC, risks relating to the protection of intellectual property, changes to the reimbursement policies of third parties, the impact of competitive products, changes to the competitive environment, the acceptance of new products in the market, conditions of the orthopedic industry, credit markets and the economy, corporate development and market development activities, including acquisitions or divestitures, unexpected costs or operating unit performance related to recent acquisitions, and other risks described in Part I, Item 1A under the heading *Risk Factors* in the 2013 Form 10-K/A, as well as in other reports that we will file in the future.

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PART I. FINANCIAL INFORMATION

Item 1. Condensed Consolidated Financial Statements

ORTHOFIX INTERNATIONAL N.V.

Condensed Consolidated Balance Sheets

(U.S. Dollars, in thousands, except share data)	March 31, 2014 (Restated) (unaudited)	December 31, 2013 (Restated)
Assets		
Current assets:		
Cash and cash equivalents	$ 25,117	$ 28,924
Restricted cash	19,270	23,761
Trade accounts receivable, less allowance for doubtful accounts of $8,841 and $9,111 at March 31, 2014 and December 31, 2013, respectively	73,447	70,811
Inventories	70,677	72,678
Deferred income taxes	40,007	39,999
Prepaid expenses and other current assets	31,050	28,933
Total current assets	259,568	265,106
Property, plant and equipment, net	52,656	54,372
Patents and other intangible assets, net	8,518	9,046
Goodwill	53,565	53,565
Deferred income taxes	22,816	22,394
Other long-term assets	6,850	7,492
Total assets	$ 403,973	$ 411,975
Liabilities and shareholders equity		
Current liabilities:		
Trade accounts payable	$ 14,022	$ 20,674
Other current liabilities	43,700	49,676
Total current liabilities	57,722	70,350
Long-term debt	20,000	20,000
Deferred income taxes	13,201	13,026
Other long-term liabilities	12,487	12,736
Total liabilities	103,410	116,112
Contingencies (Note 16)		
Shareholders equity:		
Common shares $0.10 par value; 50,000,000 shares authorized; 18,365,910 and 18,102,335 issued and outstanding as of March 31, 2014 and December 31, 2013,	1,836	1,810

respectively		
Additional paid-in capital	223,356	216,653
Retained earnings	71,389	73,897
Accumulated other comprehensive income	3,982	3,503
Total shareholders equity	300,563	295,863
Total liabilities and shareholders equity	$ 403,973	$ 411,975

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

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ORTHOFIX INTERNATIONAL N.V.

Condensed Consolidated Statements of Operations and Comprehensive Income (loss)

For the three months ended March 31, 2014 and 2013

(Unaudited, U.S. Dollars, in thousands, except share and per share data)	Three Months Ended March 31, 2014 (Restated)	2013 (Restated)
Product sales	$ 88,300	$ 90,241
Marketing service fees	11,714	12,038
Net sales	100,014	102,279
Cost of sales	26,773	25,841
Gross profit	73,241	76,438
Operating expenses		
Sales and marketing	41,171	45,844
General and administrative	17,276	18,241
Research and development	5,933	5,741
Amortization of intangible assets	584	544
Costs related to the accounting review and restatement	8,306	
	73,270	70,370
Operating (loss) income	(29)	6,068
Other income and expense		
Interest expense, net	(468)	(542)
Other (expense) income	(272)	4,764
	(740)	4,222
(Loss) income before income taxes	(769)	10,290
Income tax expense	(1,179)	(4,364)
Net (loss) income from continuing operations	(1,948)	5,926
Discontinued operations (Note 15)		
Loss from discontinued operations	(794)	(3,960)
Income tax benefit	234	1,481
Net loss from discontinued operations	(560)	(2,479)
Net (loss) income	$ (2,508)	$ 3,447

Net (loss) income per common share basic:				
Net (loss) income from continuing operations	$	(0.11)	$	0.30
Net loss from discontinued operations		(0.03)		(0.12)
Net (loss) income per common share basic	$	(0.14)	$	0.18
Net (loss) income per common share diluted:				
Net (loss) income from continuing operations	$	(0.11)	$	0.30
Net loss from discontinued operations		(0.03)		(0.12)
Net (loss) income per common share diluted	$	(0.14)	$	0.18
Weighted average number of common shares:				
Basic		18,197,363		19,431,093
Diluted		18,197,363		19,691,141
Other comprehensive (loss) income:				
Unrealized (loss) gain on cross-currency swap, net of tax		103		(318)
Foreign currency translation adjustment		376		(2,679)
Comprehensive (loss) income	$	(2,029)	$	450

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

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ORTHOFIX INTERNATIONAL N.V.

Condensed Consolidated Statements of Cash Flows

For the three months ended March 31, 2014 and 2013

	Three Months Ended March 31,	
(Unaudited, U.S. Dollars, in thousands)	**2014 (Restated)**	**2013 (Restated)**
Cash flows from operating activities:		
Net (loss) income	$ (2,508)	$ 3,447
Adjustments to reconcile net (loss) income to net cash (used in) provided by operating activities:		
Depreciation and amortization	5,746	5,067
Amortization of debt costs	180	180
Amortization of exclusivity agreements	346	311
Provision for doubtful accounts	108	1,368
Deferred income taxes	(246)	(6)
Share-based compensation	1,187	1,943
Excess income tax benefit on employee stock-based compensation	(29)	(78)
Other	14	421
Change in operating assets and liabilities:		
Trade accounts receivable	(2,607)	9,665
Inventories	2,487	(2,106)
Prepaid expenses and other current assets	(3,464)	4,843
Trade accounts payable	(6,670)	(7,247)
Other current liabilities	(4,606)	(162)
Long-term assets	130	(1,553)
Long-term liabilities	(280)	(1,039)
Net cash (used in) provided by operating activities	(10,212)	15,054
Cash flows from investing activities:		
Capital expenditures for property, plant and equipment	(3,691)	(6,029)
Capital expenditures for intangible assets	(46)	(44)
Sale of other investments	32	(506)
Net cash used in investing activities	(3,705)	(6,579)
Cash flows from financing activities:		
Net proceeds from issuance of common shares	5,542	2,143
Repayment of bank borrowings, net		(15)
Changes in restricted cash	4,502	(8,141)
Excess income tax benefit on employee stock-based awards	29	78
Net cash provided by (used in) financing activities	10,073	(5,935)
Effect of exchange rate changes on cash	37	(433)

Net (decrease) increase in cash and cash equivalents	(3,807)	2,107
Cash and cash equivalents at the beginning of the period	28,924	30,767
Cash and cash equivalents at the end of the period	$ 25,117	$ 32,874

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

ORTHFIX INTERNATIONAL N.V.

Notes to the Unaudited Condensed Consolidated Financial Statements

1. Summary of significant accounting policies

(a) Basis of presentation

The accompanying unaudited condensed consolidated financial statements have been prepared in accordance with generally accepted accounting principles in the United States (U.S. GAAP) for interim financial information and with the instructions to Form 10-Q and Rule 10-01 of Regulation S-X. Pursuant to these rules and regulations, certain information and note disclosures, normally included in financial statements prepared in accordance with U.S. GAAP, have been condensed or omitted. In the opinion of management, all adjustments (consisting of normal recurring items) considered necessary for a fair presentation have been included. Operating results for the three months ended March 31, 2014, are not necessarily indicative of the results that may be expected for the year ending December 31, 2014. The balance sheet at December 31, 2013, has been derived from the audited financial statements at that date, but does not include all of the information and footnotes required by accounting principles generally accepted in the U.S. for complete financial statements. For further information, refer to the consolidated financial statements and notes thereto contained in the 2013 Form 10-K/A. The notes to the unaudited condensed consolidated financial statements are presented on a continuing basis unless otherwise noted.

(b) Reclassifications

The Company has reclassified certain line items to conform to the current year presentation. The reclassifications have no effect on previously reported net earnings or shareholders equity.

(c) Use of estimates

The preparation of financial statements in conformity with U.S. GAAP requires management to make estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes. On an ongoing basis, the Company evaluates its estimates including those related to contractual allowances, doubtful accounts, inventories, potential goodwill and intangible asset impairment, income taxes, and shared-based compensation. Actual results could differ from these estimates.

(d) Foreign currency translation

The financial statements for operations outside the U.S. are generally maintained in their local currency. All foreign currency denominated balance sheet accounts, except shareholders equity, are translated to U.S. dollars at period end exchange rates and revenue and expense items are translated at weighted average rates of exchange prevailing during the year. Gains and losses resulting from the translation of foreign currency are recorded in the accumulated other comprehensive income component of shareholders equity.

(e) Collaborative agreement

The Company receives a marketing fee through our collaboration with Musculoskeletal Transplant Foundation (MTF) for Trinity Evolution® and Trinity ELITE®, for which, we have exclusive marketing rights and VersaShield for which we have non-exclusive marketing rights. Under our agreements with MTF, MTF processes the tissues, maintains inventory, and invoices hospitals and surgery centers and other points of care for service fees, which are submitted by customers via purchase orders. MTF is considered the primary obligor in these arrangements and therefore we recognize these marketing service fees on a net basis upon shipment of the product to the customer.

2. Original and Further Restatement of the Consolidated Financial Statements

In connection with the Company s preparation of its consolidated interim quarterly financial statements for the fiscal quarter ended June 30, 2014, the Company determined that certain entries with respect to the previously filed financial statements contained in the Original Form 10-Q and the Original 2013 Form 10-K were not properly accounted for under U.S. generally accepted accounting principles (U.S. GAAP). As further described below, these additional errors affect the fiscal years ended December 31, 2013, 2012 and 2011, as well as the fiscal quarter ended March 31, 2014. Due to these errors, the Company determined in August 2014 to restate its consolidated financial statements for the fiscal years ended December 31, 2013, 2012 and 2011 (including the interim quarterly

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periods contained within the fiscal years ended December 31, 2013 and 2012) and the fiscal quarter ended March 31, 2014, and that the previously filed financial statements for these periods (including those contained in the Original 2013 Form 10-K and the Original Form 10-Q) should no longer be relied upon. This Form 10-Q/A contains restated consolidated interim financial statements for the fiscal quarters ended March 31, 2014 and 2013.

Contemporaneously with the filing of this Form 10-Q/A, the Company is filing (i) an amendment to the Original 2013 Form 10-K (the 2013 Form 10-K/A), which amendment contains restated consolidated financial statements for the fiscal years ended December 31, 2013, 2012 and 2011, and the quarterly reporting periods contained within the fiscal years ended December 31, 2013 and 2012, and (ii) its delayed Quarterly Reports on Form 10-Q for the fiscal quarters ended June 30, 2014 (the 2014 Second Quarter Form 10-Q) and September 30, 2014 (the 2014 Third Quarter Form 10-Q), which contain restated consolidated interim financial statements for the fiscal quarterly and year-to-date periods ended June 30, 2013 and September 30, 2013, respectively. The corrections of the additional errors in this Form 10-Q/A and the 2013 Form 10-K/A are referred to herein as the Further Restatement.

The Original 2013 Form 10-K reflected a prior restatement of the Company s consolidated financial statements for the fiscal years ended December 31, 2012 and 2011 and the fiscal quarter ended March 31, 2013, which we refer to herein as the Original Restatement. For additional information regarding the Original Restatement, see the 2013 Form 10-K/A.

Background of Further Restatement

During the second quarter of 2014, the Company s management noted that the Company s bad debt expense for its BioStim strategic business unit (SBU) during the first quarter of 2014 was higher than internally budgeted. As a result, the Company s internal finance department reviewed bad debt expense entries in prior periods. In connection with this review, the Company also further considered its accounting methodology with respect to certain prior revenue adjustments related to uncollectible patient co-pay and self-pay amounts. As further described below, after performing this review, the Company determined that errors existed relating to the accounting for uncollectible patient co-pay and self-pay amounts, and that certain bad debt reserves originally recorded in fiscal years 2011 and 2012 were reversed in incorrect periods in the Original Restatement in connection with the change to sell-through accounting for certain distributors. After analyzing these errors, the Company determined to further restate its financial statements as described in the 2013 Form 10-K/A and herein. In addition to these matters, certain other adjustments identified by management, including revisions to inventory reserves, intercompany profit adjustments and accounts receivable reserves, were made to the consolidated financial statements in connection with the Further Restatement, as discussed below.

Co-Pay and Self-Pay Revenue Adjustments

A majority of revenue from the Company s BioStim SBU is derived from third parties, which is subject to change due to contractual adjustments related to commercial insurance carriers, and may include certain patient co-pay amounts. In addition, certain patient purchasers are without insurance, with revenue derived from self-pay arrangements. In previously issued financial statements, the Company recorded these co-pay and self-pay amounts as revenue with estimated uncollectible portions being recognized as bad debt expense. Upon further analysis, it was determined that because collectability of co-pay and self-pay amounts was not reasonably assured, the conditions for revenue recognition had not been met and revenue for those amounts should not have been recognized until collected. Additionally, in the quarter ended March 31, 2014, there were amounts related to contractual amounts from commercial insurance carriers that were incorrectly classified to bad debt expense rather than a reduction of revenue.

Adjustments to correct the foregoing reduce equally both the Company s historical net sales and its sales and marketing expense by approximately $1.4 million and $1.5 million for the fiscal quarters ended March 31, 2014 and 2013, respectively. Additionally, there was $1.4 million in the fiscal quarter ended March 31, 2014 which was inappropriately classified to bad debt expense rather than a reduction of revenue, for a total reduction to bad debt and revenue of $2.8 million for the fiscal quarter ended March 31, 2014. These adjustments have no effect on net income from continuing operations, net income or total assets in any period.

Bad Debt Timing Adjustments

In connection with the foregoing, the Company determined to review bad debt expense trends more broadly across all of its business units. As a result of this process, the Company determined that certain bad debt reserves originally recorded in fiscal years 2011 and 2012 were reversed in incorrect periods in the Original Restatement in connection with the change to sell-through accounting for certain distributors. Because the Original Restatement transferred these transactions to sell-through accounting (as opposed to sell-in accounting, which had been used when the original bad debt reserves were recorded), the bad debt reserve was reversed as part of the Original Restatement, as the receivable that was being reserved for was no longer recognized.

Adjustments to correct this error result in an increase of sales and marketing expense of $1.5 million for the fiscal quarter ended March 31, 2013. There were no adjustments to the fiscal quarter ended March 31, 2014. These adjustments resulted in no impact to the accounts receivable balance as of March 31, 2014 and December 31, 2013.

Accounts Receivable Reserve Adjustments

As part of analyzing collections experience on accounts receivable, the Company identified that it had incorrectly considered certain deferred revenue amounts included in gross accounts receivable when calculating estimated reserves. Specifically, the computation of the contractual allowances and bad debt allowances, which serves to adjust accounts receivable to the estimated collectible amount, incorrectly assumed that some percentage of the deferred amounts would be collected, rather than fully deferring these amounts.

Adjustments to correct this error resulted in a net decrease in operating loss of $1.5 million for the fiscal quarter ended March 31, 2014 and a net increase in operating income of $0.4 million for the fiscal quarter ended March 31 2013.

This adjustment resulted in a decrease in accounts receivable, net (due to an increase in reserves) as of March 31, 2014 and December 31, 2013, by $2.8 million and $4.2 million, respectively.

Intercompany Profit Adjustments

The Company has two manufacturing facilities which support the inventory needs of other subsidiaries through intercompany sales transactions. These intercompany sales include a profit margin for the selling subsidiary (intercompany profit) that is eliminated by the Company as part of its consolidated financial reporting process. The elimination of intercompany profit requires determining the affected net inventory amounts and their related intercompany profit margin to eliminate all intercompany profit, resulting in all inventories being carried at historical cost in the Company s consolidated financial statements.

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As part of the Original Restatement the Company made certain corrections to prior period excess and obsolete inventory reserves. The effect of these corrections was not properly considered when determining the adjustments needed to eliminate intercompany profits from inventories in the Original Restatement.

Adjustments to correct this error resulted in an increase to cost of sales of $3.0 million and a decrease to cost of sales of $0.1 million for the fiscal quarters ended March 31, 2014 and 2013, respectively.

This adjustment resulted in a decrease in inventory as of March 31, 2014 and December 31, 2013, by $5.5 million and $2.6 million, respectively.

Inventory

Inventory Existence

As part of the remediation activities that followed the Original Restatement, the Company expanded its procedures in the second quarter of 2014 to validate the existence of field inventory held by independent sales representatives and noted that, in many cases, this inventory had higher rates of missing inventory (shrinkage) than previously estimated. To determine whether these higher error rates were pervasive across its field inventory, the Company counted approximately 90% of its field inventory during the third and fourth fiscal quarters of 2014. These counts resulted in the identification of errors relating to previous estimates of shrinkage.

Adjustments in the Further Restatement to correct these errors, net of the related effect on previously recorded excess and obsolete inventory reserves, resulted in an increase to cost of sales of $0.2 million and $0.1 million for the fiscal quarters ended March 31, 2014 and 2013, respectively.

These adjustments resulted in a decrease in inventory as of March 31, 2014 and December 31, 2013, by $1.2 million and $1.0 million, respectively.

Inventory Reserves

In connection with its remediation efforts associated with the material weakness noted in the Original Restatement related to inventory reserves, the Company concluded that it was not appropriately calculating inventory reserves, including its consideration of demand assumptions for kits , which contain a variety of piece part components to be used during surgery that have various demand considerations, as well as inventory held by third parties under inventory purchase obligations.

Adjustments to correct these errors resulted in an increase to cost of sales of $2.4 million and $0.8 million for the fiscal quarters ended March 31, 2014 and 2013, respectively. These adjustments resulted in a decrease to inventory (due to an increase in reserves) as of March 31, 2014 and December 31, 2013, by $16.4 million and $14.4 million, respectively.

Other Adjustments

In addition to the adjustments described above, the Company is correcting certain other items. The impact of correcting these items results in a decrease to loss before income taxes of $1.6 million for the fiscal quarter ended March 31, 2014, and a decrease to income before income taxes of $0.3 million for the fiscal quarter ended March 31, 2013.

The tables below show the effects of the Original Restatement for the fiscal quarter ended March 31, 2013, as well as the effects of the Further Restatement for each of the fiscal quarters ended March 31, 2014 and 2013. In each case, the tax effect of the adjustments is estimated based on the Company s estimated tax rate.

		Three Months Ended March 31, 2014 Further Restatement Adjustments by Category							
(U.S. Dollars, in thousands)	Originally Reported in 2014 Form 10-Q	Co-Pay and Self-Pay Revenue	Bad Debt Timing	Accounts Receivable Reserve	Intercompany Profit	Inventory	Other	Total Further Restatement Adjustments	Restated
Net sales	$ 101,342	$ (2,800)	$	$ 1,651	$	$	$ (179)	$ (1,328)	$ 100,014
Cost of sales	22,632				2,966	2,564	(1,389)	4,141	26,773
Gross profit	78,710	(2,800)		1,651	(2,966)	(2,564)	1,210	(5,469)	73,241
Operating expenses									
Sales and marketing	43,871	(2,800)		201			(101)	(2,700)	41,171
General and administrative	17,545						(269)	(269)	17,276
Research and development	5,939						(6)	(6)	5,933
Amortization of intangible assets	584								584
Costs related to the accounting review and restatement	8,306								8,306
	76,245	(2,800)		201			(376)	(2,975)	73,270
Operating (loss) income	2,465			1,450	(2,966)	(2,564)	1,586	(2,494)	(29)
Other income and (expense)	(747)						7	7	(740)
Loss before income taxes	1,718			1,450	(2,966)	(2,564)	1,593	(2,487)	(769)
Income tax expense	(1,940)			(508)	1,039	898	(668)	761	(1,179)
Net loss from continuing operations	$ (222)	$	$	$ 942	$ (1,927)	$ (1,666)	$ 925	$ (1,726)	$ (1,948)

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(U.S. Dollars, in thousands)	As Reported in the 2013 Form 10-Q Prior to Original Restatement	Three Months Ended March 31, 2013 Original Restatement Adjustments by Category Distributor Revenue	Inventory Reserves	Royalties	Other	Total Original Restatement Adjustments	As Originally Restated in 2013 Form 10-Q/A
Net sales	$ 100,254	$ 2,963	$	$	$ 156	$ 3,119	$ 103,373
Cost of sales	22,699	471	86	2,030	331	2,918	25,617
Gross profit	77,555	2,492	(86)	(2,030)	(175)	201	77,756
Operating expenses							
Sales and marketing	48,839	(2,073)		(2,030)	318	(3,785)	45,054
General and administrative	18,788				(458)	(458)	18,330
Research and development	5,400				341	341	5,741
Amortization of intangible assets	504				40	40	544
Charges related to U.S. Government resolutions							
	73,531	(2,073)		(2,030)	241	(3,862)	69,669
Operating income	4,024	4,565	(86)		(416)	4,063	8,087
Other income and (expense)	4,204						4,204
Income before income taxes	8,228	4,565	(86)		(416)	4,063	12,291
Income tax expense	(3,320)	(1,529)	29		139	(1,361)	(4,681)
Net income from continuing operations	$ 4,908	$ 3,036	$ (57)	$	$ (277)	$ 2,702	$ 7,610

(U.S. Dollars, in thousands)	As Originally Restated in 2013 Form 10-Q/A	Three Months Ended March 31, 2013 Further Restatement Adjustments by Category Co-Pay and Self-Pay Revenue	Bad Debt Timing	Accounts Receivable Reserve	Intercompany Profit	Inventory	Other	Total Further Restatement Adjustments	Restated
Net sales	$ 103,373	$ (1,453)	$	$ 437	$	$	$ (78)	$ (1,094)	$ 102,279
Cost of sales	25,617				(120)	820	(476)	224	25,841
Gross profit	77,756	(1,453)		437	120	(820)	398	$ (1,318)	76,438
Operating expenses									
Sales and marketing	45,054	(1,453)	1,455	(8)			796	790	45,844

General and administrative	18,330						(89)	(89)	18,241
Research and development	5,741								5,741
Amortization of intangible assets	544								544
	69,669	(1,453)	1,455	(8)			707	701	70,370
Operating income	8,087		(1,455)	445	120	(820)	(309)	(2,019)	6,068
Other income and (expense)	4,204						18	18	4,222
Income before income taxes	12,291		(1,455)	445	120	(820)	(291)	(2,001)	10,290
Income tax expense	(4,681)		509	(156)	(42)	287	(281)	317	(4,364)
Net income from continuing operations	$ 7,610	$	$ (946)	$ 289	$ 78	$ (533)	$ (572)	$ (1,684)	$ 5,926

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The effects of the Further Restatement on our condensed consolidated balance sheet as of March 31, 2014 are as follows:

	As of March 31, 2014		
(Unaudited, U.S. Dollars, in thousands, except share data)	Originally Reported in 2014 Form 10-Q	Further Restatement Adjustments	Restated
Assets			
Current assets:			
Cash and cash equivalents	$ 26,747	$ (1,630)	$ 25,117
Restricted cash	19,270		19,270
Trade accounts receivable, less allowances of $8,841 at March 31, 2014	76,917	(3,470)	73,447
Inventories	92,753	(22,076)	70,677
Deferred income taxes	33,956	6,051	40,007
Prepaid expenses and other current assets	28,781	2,269	31,050
Total current assets	278,424	(18,856)	259,568
Property, plant and equipment, net	52,532	124	52,656
Patents and other intangible assets, net	8,518		8,518
Goodwill	53,565		53,565
Deferred income taxes	18,758	4,058	22,816
Other long-term assets	6,743	107	6,850
Total assets	$ 418,540	$ (14,567)	$ 403,973
Liabilities and shareholders equity			
Current liabilities:			
Trade accounts payable	$ 14,022	$	$ 14,022
Other current liabilities	41,467	2,233	43,700
Total current liabilities	55,489	2,233	57,722
Long-term debt	20,000		20,000
Deferred income taxes	13,307	(106)	13,201
Other long-term liabilities	12,487		12,487
Total liabilities	101,283	2,127	103,410
Contingencies (Note 16)			
Shareholders equity:			
Common shares $0.10 par value; 50,000,000 shares authorized; 18,365,910 issued and outstanding as of March 31, 2014	1,836		1,836
Additional paid-in capital	223,630	(274)	223,356
Retained earnings	88,550	(17,161)	71,389
Accumulated other comprehensive income	3,241	741	3,982

Total shareholders equity	317,257	(16,694)	300,563
Total liabilities and shareholders equity	$ 418,540	$ (14,567)	$ 403,973

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The effects of the Further Restatement on our condensed consolidated balance sheet as of December 31, 2013 are as follows:

	As of December 31, 2013		
(Unaudited, U.S. Dollars, in thousands, except share data)	Originally Reported in 2014 Form 10-Q	Further Restatement Adjustments	Restated
Assets			
Current assets:			
Cash and cash equivalents	$ 30,486	$ (1,562)	$ 28,924
Restricted cash	23,761		23,761
Trade accounts receivable, less allowances of $9,111 at December 31, 2013	75,567	(4,756)	70,811
Inventories	90,577	(17,899)	72,678
Deferred income taxes	33,947	6,052	39,999
Prepaid expenses and other current assets	25,906	3,027	28,933
Total current assets	280,244	(15,138)	265,106
Property, plant and equipment, net	54,606	(234)	54,372
Patents and other intangible assets, net	9,046		9,046
Goodwill	53,565		53,565
Deferred income taxes	18,336	4,058	22,394
Other long-term assets	7,385	107	7,492
Total assets	$ 423,182	$ (11,207)	$ 411,975
Liabilities and shareholders equity			
Current liabilities:			
Trade accounts payable	$ 20,674	$	$ 20,674
Other current liabilities	46,146	3,530	49,676
Total current liabilities	66,820	3,530	70,350
Long-term debt	20,000		20,000
Deferred income taxes	13,132	(106)	13,026
Other long-term liabilities	12,736		12,736
Total liabilities	112,688	3,424	116,112
Contingencies (Note 16)			
Shareholders equity:			
Common shares $0.10 par value; 50,000,000 shares authorized; 18,102,335 issued and outstanding as of December 31, 2013	1,810		1,810
Additional paid-in capital	216,653		216,653
Retained earnings	89,332	(15,435)	73,897
Accumulated other comprehensive income	2,699	804	3,503

Total shareholders equity	310,494	(14,631)	295,863
Total liabilities and shareholders equity	$ 423,182	$ (11,207)	$ 411,975

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The effects of the Further Restatement on our condensed consolidated statement of operations and comprehensive loss for the three months ended March 31, 2014 are as follows:

	Three Months Ended March 31, 2014		
(Unaudited, U.S. Dollars, in thousands, except share and per share data)	Originally Reported in 2014 Form 10-Q	Further Restatement Adjustments	Restated
Product sales	$ 89,684	$ (1,384)	$ 88,300
Marketing service fees	11,658	56	11,714
Net sales	101,342	(1,328)	100,014
Cost of sales	22,632	4,141	26,773
Gross profit	78,710	(5,469)	73,241
Operating expenses			
Sales and marketing	43,871	(2,700)	41,171
General and administrative	17,545	(269)	17,276
Research and development	5,939	(6)	5,933
Amortization of intangible assets	584		584
Costs related to the accounting review and restatement	8,306		8,306
	76,245	(2,975)	73,270
Operating income (loss)	2,465	(2,494)	(29)
Other income and expense			
Interest expense, net	(486)	18	(468)
Other (loss) income	(261)	(11)	(272)
	(747)	7	(740)
Income (loss) before income taxes	1,718	(2,487)	(769)
Income tax expense	(1,940)	761	(1,179)
Net loss from continuing operations	(222)	(1,726)	(1,948)
Discontinued operations (Note 15)			
Loss from discontinued operations	(794)		(794)
Income tax benefit	234		234
Net loss from discontinued operations	(560)		(560)
Net loss	$ (782)	$ (1,726)	$ (2,508)
Net loss per common share basic:			
Net loss from continuing operations	$ (0.01)	$ (0.10)	$ (0.11)
Net loss from discontinued operations	(0.03)		(0.03)

Net loss per common share basic	$ (0.04)	$ (0.10)	$ (0.14)
Net loss per common share diluted:			
Net loss from continuing operations	$ (0.01)	$ (0.10)	$ (0.11)
Net loss from discontinued operations	(0.03)		(0.03)
Net loss per common share diluted	$ (0.04)	$ (0.10)	$ (0.14)
Weighted average number of common shares:			
Basic	18,197,363		18,197,363
Diluted	18,197,363		18,197,363
Other comprehensive income:			
Unrealized gain (loss) on cross-currency swap, net of tax	103		103
Foreign currency translation adjustment	439	(63)	376
Comprehensive loss	$ (240)	$ (1,789)	$ (2,029)

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The effects of the Original Restatement and the Further Restatement on our condensed consolidated statement of operations and comprehensive income (loss) for the three months ended March 31, 2013 are as follows:

	Three Months Ended March 31, 2013				
(U.S. Dollars, in thousands, except share and per share data)	As Reported in the 2013 Form 10-Q Prior to Original Restatement	Original Restatement Adjustments	As Originally Restated in the 2013 Form 10-Q/A	Further Restatement Adjustments	Restated
Product sales	$ 88,358	$ 2,978	$ 91,336	(1,095)	$ 90,241
Marketing service fees	11,896	141	12,037	1	12,038
Net sales	100,254	3,119	103,373	(1,094)	102,279
Cost of sales	22,699	2,918	25,617	224	25,841
Gross profit	77,555	201	77,756	(1,318)	76,438
Operating expenses					
Sales and marketing	48,839	(3,785)	45,054	790	45,844
General and administrative	18,788	(458)	18,330	(89)	18,241
Research and development	5,400	341	5,741		5,741
Amortization of intangible assets	504	40	544		544
	73,531	(3,862)	69,669	701	70,370
Operating income	4,024	4,063	8,087	(2,019)	6,068
Other income and (expense)					
Interest expense, net	(560)		(560)	18	(542)
Other income	4,764		4,764		4,764
	4,204		4,204	18	4,222
Income before income taxes	8,228	4,063	12,291	(2,001)	10,290
Income tax expense	(3,320)	(1,361)	(4,681)	317	(4,364)
Net income from continuing operations	4,908	2,702	7,610	(1,684)	5,926
Discontinued operations (Note 15)					
Loss from discontinued operations	(4,432)	(2)	(4,434)	474	(3,960)
Income tax benefit (expense)	1,640	(316)	1,324	157	1,481
Net loss from discontinued operations	(2,792)	(318)	(3,110)	631	(2,479)
Net income	2,116	$ 2,384	$ 4,500	(1,053)	$ 3,447
Net income (loss) per common share basic:					

Net income from continuing operations	$	0.25	$	0.14	$	0.39	(0.09)	$	0.30
Net loss from discontinued operations		(0.14)		(0.02)		(0.16)	0.04		(0.12)
Net income per common share basic	$	0.11	$	0.12	$	0.23	(0.05)	$	0.18
Net income (loss) per common share diluted:									
Net income from continuing operations	$	0.25	$	0.14	$	0.39	(0.09)	$	0.30
Net loss from discontinued operations		(0.14)		(0.02)		(0.16)	0.04		(0.12)
Net income per common share diluted:	$	0.11	$	0.12	$	0.23	(0.05)	$	0.18
Weighted average number of common shares:									
Basic		19,431,093				19,431,093			19,431,093
Diluted		19,691,141				19,691,141			19,691,141
Other comprehensive (loss) income, before tax:									
Unrealized gain on derivative instrument		(318)				(318)			(318)
Translation adjustment		(2,814)		106		(2,708)	29		(2,679)
Comprehensive (loss) income	$	(1,016)	$	2,490	$	1,474	$ (1,024)	$	450

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The effects of the Further Restatement on our condensed consolidated statement of cash flows for the three months ended March 31, 2014 are as follows:

(Unaudited, U.S. Dollars, in thousands)	Three Months Ended March 31, 2014 Originally Reported in 2014 Form 10-Q	Further Restatement Adjustments	Restated
Cash flows from operating activities:			
Net loss	$ (782)	$ (1,726)	$ (2,508)
Adjustments to reconcile net loss to net cash used in operating activities:			
Depreciation and amortization	6,004	(258)	5,746
Amortization of debt costs	180		180
Amortization of exclusivity agreements	346		346
Provision for doubtful accounts	2,579	(2,471)	108
Deferred income taxes	(246)		(246)
Share-based compensation	1,461	(274)	1,187
Excess income tax benefit on employee stock-based awards	(29)		(29)
Other	166	(152)	14
Change in operating assets and liabilities:			
Trade accounts receivable	(3,780)	1,173	(2,607)
Inventories	(1,690)	4,177	2,487
Prepaid expenses and other current assets	(2,806)	(658)	(3,464)
Trade accounts payable	(6,670)		(6,670)
Other current liabilities	(4,761)	155	(4,606)
Long-term assets	130		130
Long-term liabilities	(280)		(280)
Net cash used in operating activities	(10,178)	(34)	(10,212)
Cash flows from investing activities:			
Capital expenditures for property, plant and equipment	(3,691)		(3,691)
Capital expenditures for intangible assets	(46)		(46)
Sale of other investments		32	32
Net cash used in investing activities	(3,737)	32	(3,705)
Cash flows from financing activities:			
Net proceeds from issuance of common shares	5,542		5,542
(Repayment of) proceeds from bank borrowings, net			
Changes in restricted cash	4,502		4,502
Excess income tax benefit on employee stock-based awards	29		29

Net cash provided by financing activities	10,073		10,073
Effect of exchange rate changes on cash	103	(66)	37
Net decrease in cash and cash equivalents	(3,739)	(68)	(3,807)
Cash and cash equivalents at the beginning of the period	30,486	(1,562)	28,924
Cash and cash equivalents at the end of the period	$ 26,747	$ (1,630)	$ 25,117

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The effects of the Original Restatement and the Further Restatement on our condensed consolidated statement of cash flows for the three months ended March 31, 2013 are as follows:

(Unaudited, U.S. Dollars, in thousands)	Three Months Ended March 31, 2013 As Reported in the 2013 Form 10-Q Prior to Original Restatement	Original Restatement Adjustments	As Originally Restated in the 2013 Form 10-Q/A	Further Restatement Adjustments	Restated
Cash flows from operating activities:					
Net income	$ 2,116	$ 2,384	$ 4,500	$ (1,053)	$ 3,447
Adjustments to reconcile net income to net cash provided by operating activities:					
Depreciation and amortization	4,995	34	5,029	38	5,067
Amortization of debt costs	180		180		180
Amortization of exclusivity agreements	311		311		311
Provision for doubtful accounts	3,227	(1,853)	1,374	(6)	1,368
Deferred income taxes	(744)	738	(6)		(6)
Share-based compensation	1,943		1,943		1,943
Excess income tax benefit on employee stock-based awards	(78)		(78)		(78)
Other	(345)	736	391	30	421
Change in operating assets and liabilities:					
Trade accounts receivable	13,779	(5,190)	8,589	1,076	9,665
Inventories	(4,230)	2,130	(2,100)	(6)	(2,106)
Prepaid expenses and other current assets	(179)	2,874	2,695	2,148	4,843
Trade accounts payable	(7,242)	(5)	(7,247)		(7,247)
Other current liabilities	4,478	(2,408)	2,070	(2,232)	(162)
Long-term assets	(2,014)	461	(1,553)		(1,553)
Long-term liabilities	(743)	(296)	(1,039)		(1,039)
Net cash provided by operating activities	15,454	(395)	15,059	(5)	15,054
Cash flows from investing activities:					
Capital expenditures for property, plant and equipment	(6,029)		(6,029)		(6,029)
Capital expenditures for intangible assets	(439)	395	(44)		(44)
Purchase of other investments				(506)	(506)
Net cash used in investing activities	(6,468)	395	(6,073)	(506)	(6,579)
Cash flows from financing activities:					
Net proceeds from issuance of common shares	2,143		2,143		2,143
(Repayment of) proceeds from bank borrowings, net	(15)		(15)		(15)

Changes in restricted cash	(8,141)		(8,141)		(8,141)
Excess income tax benefit on employee stock-based awards	78		78		78
Net cash used in financing activities	(5,935)		(5,935)		(5,935)
Effect of exchange rate changes on cash	(431)		(431)	(2)	(433)
Net increase in cash and cash equivalents	2,620		2,620	(513)	2,107
Cash and cash equivalents at the beginning of the period	31,055		31,055	(288)	30,767
Cash and cash equivalents at the end of the period	$ 33,675	$	$ 33,675	(801)	$ 32,874

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3. Inventories

The Company s inventories are primarily stated at standard cost, which approximates actual cost determined on a first-in, first-out basis. The Company adjusts the value of its inventory to the extent management determines that the cost cannot be recovered due to obsolescence or other factors. In order to make these determinations, management uses estimates of future demand and sales prices for each product to determine the appropriate inventory reserves and to make corresponding adjustments to the carrying value of these inventories to reflect the lower of cost or market value. In the event of a sudden significant decrease in demand for the Company s products, or a higher incidence of inventory obsolescence, the Company could be required to increase its inventory reserves, which would increase cost of sales and decrease gross profit.

Work-in-process and finished products, include material, labor and production overhead costs. Deferred cost of sales result from transactions where the Company has shipped product or performed services for which all revenue recognition criteria have not been met. Once the revenue recognition criteria have been met, both the deferred revenues and associated cost of sales are recognized.

Inventories were as follows:

(U.S. Dollars, in thousands)	March 31, 2014 (Restated)	December 31, 2013 (Restated)
Raw materials	$ 5,220	$ 6,515
Work-in-process	7,412	6,606
Finished products	51,190	51,991
Deferred cost of sales	6,855	7,566
Total Inventory	$ 70,677	$ 72,678

4. Patents and other intangible assets

(U.S. Dollars, in thousands)	March 31, 2014	December 31, 2013
Cost		
Patents	$ 34,815	$ 34,820
Trademarks definite lived	645	620
Licenses and other	7,748	7,748
	43,208	43,188
Accumulated amortization		
Patents	(32,170)	(31,739)
Trademarks definite lived	(484)	(454)
Licenses and other	(2,036)	(1,949)
	(34,690)	(34,142)

Patents and other intangible assets, net	$	8,518	$	9,046

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5. Goodwill

As a result of the Company s change in reporting structure in July of 2013, the Company allocated goodwill to each reporting unit, and subsequently evaluated all reporting units, including the Extremity Fixation and Spine Fixation reporting units, for the possible impairment of goodwill. The result of this evaluation was a full impairment of the goodwill allocated to our Extremity Fixation and our Spine Fixation reporting units, totaling $19.2 million. As of December 31, 2013 and March 31, 2014, accumulated impairment was $9.8 million for our Extremity Fixation reportable unit and $9.4 million for our Spine Fixation reporting unit. Our BioStim and Biologics reportable units have not been impaired. The following table presents the net carrying value of goodwill by reportable segment as of March 31, 2014 and December 31, 2013.

(U.S. Dollars, in thousands)	March 31, 2014	December 31, 2013
BioStim	$ 42,678	$ 42,678
Biologics	10,887	10,887
Total goodwill	$ 53,565	$ 53,565

6. Bank borrowings

The Company had no borrowings and an unused available line of credit of 5.8 million ($8.0 million) at both March 31, 2014 and December 31, 2013, on its Italian line of credit. This line of credit provides the Company the option to borrow amounts in Italy at rates which are determined at the time of borrowing. This line of credit is unsecured.

7. Long-term debt

On August 30, 2010, the Company s wholly-owned U.S. holding company, Orthofix Holdings, Inc. (Orthofix Holdings) entered into a Credit Agreement (the Credit Agreement) with certain domestic direct and indirect subsidiaries of the Company (the Guarantors), JPMorgan Chase Bank, N.A., as Administrative Agent, RBS Citizens, N.A., as Syndication Agent, and certain lender parties thereto.

The Credit Agreement provides for a five year, $200 million secured revolving credit facility (the Revolving Credit Facility), and a five year, $100 million secured term loan facility (the Term Loan Facility, and together with the Revolving Credit Facility, the Credit Facilities). On January 15, 2015, at the Company s request, the lenders agreed to reduce the available capacity under the Revolving Credit Facility to $100 million.

As of March 31, 2014, and December 31, 2013, there was $20 million outstanding under the Revolving Credit Facility. Borrowings under the Credit Facilities bear interest at a floating rate, which is, at Orthofix Holdings option, either the London Inter-Bank Offered Rate (LIBOR) plus an applicable margin or a base rate (as defined in the Credit Agreement) plus an applicable margin (in each case subject to adjustment based on financial ratios). Such applicable margin will be up to 3.25% for LIBOR borrowings and up to 2.25% for base rate borrowings depending upon a measurement of the consolidated leverage ratio with respect to the immediately preceding four fiscal quarters. As of March 31, 2014, and December 31, 2013, the entire Revolving Credit Facility was at the LIBOR rate plus a margin of 2.50%. The effective interest rate on the Credit Facilities as of March 31, 2014, and December 31, 2013, was 2.7%. Outstanding balances on the Revolving Credit Facility are due on August 30, 2015.

Borrowings under the Revolving Credit Facility, which may be made in the future, may used for working capital, capital expenditures and other general corporate purposes of Orthofix Holdings and its subsidiaries. The Guarantors have guaranteed repayment of Orthofix Holdings   obligations under the Credit Agreement. The obligations of Orthofix Holdings and each of the Guarantors with respect to the Credit Facilities are secured by a pledge of substantially all of the assets of Orthofix Holdings and each of the Guarantors.

The Credit Agreement, as amended, requires Orthofix Holdings and the Company to comply with coverage ratios on a consolidated basis and contains affirmative and negative covenants, including limitations on additional debt, liens, investments and acquisitions. The Credit Agreement, as amended, also includes events of default customary for facilities of this type. Upon the occurrence of an event of default, all outstanding loans may be accelerated and/or the lenders commitments terminated. On August 14, 2013, the Company entered into a Limited Waiver (the Original Limited Waiver) with the lenders under the Credit Agreement (the Lenders) which waived requirements under the Credit Agreement to deliver quarterly financial statements for the fiscal quarter ended on June 30, 2013, and related financial covenant certificates, until the earlier of (i) March 31, 2014 or (ii) the date that is one day after such financial statements are publicly filed or released. The Company was in compliance with the affirmative and negative covenants at March 31, 2014 and there were no events of default.

In connection with the Further Restatement and the Company s delay in filing the 2014 Second Quarter Form 10-Q, on August 14, 2014 the Company entered into a subsequent Limited Waiver with the Lenders which was extended on September 30, 2014, January 15, 2015 and February 26, 2015 (the Subsequent Limited Waivers). Under the Subsequent Limited Waivers, the Lenders collectively waived requirements under the Credit Agreement that the Company deliver quarterly financial statements with respect to the fiscal quarters ended June 30, 2014 and September 30, 2014, and related financial covenant certificates, until the earlier of (i) March 31, 2015 or (ii) the date that is one day after such financial statements are publicly filed or released. The Subsequent Limited Waivers also extend the date by which the Company is required to provide certain 2014 fiscal year financial statements until the earlier of (i) one business day following the date that the Company files its Annual Report on Form 10-K for the fiscal year ended December 31, 2014 or (ii) April 30, 2015. In addition, the Subsequent Limited Waivers provided that the Further Restatement would not constitute a default or event of default provided that within one business day after the public release or filing of such restated financial statements, the Company delivered corrected financial statements and compliance certificates with respect to such restated periods and immediately paid any additional interest and other fees that would have been owed had applicable interest and fees originally been calculated based on the restated financial statements. As of the date hereof, the Company has delivered the quarterly consolidated financial statements for the fiscal quarters ended June 30, 2014 and September 30, 2014, and the Company does not expect the Further Restatement to trigger any such additional interest or fees with respect to such prior periods. However, in the event that the Company does not satisfy these respective obligations under the Original Limited Waiver, the Subsequent Limited Waivers and/or the Credit Agreement, an event of default could be declared under the Credit Agreement, which could have a material adverse effect on the Company s financial position.

Certain subsidiaries of the Company have restrictions on their ability to pay dividends or make intercompany loan advances pursuant to the Company s Credit Facilities. The net assets of Orthofix Holdings and its subsidiaries are restricted for distributions to the parent company. Domestic subsidiaries of the Company, as parties to the credit agreement, have access to these net assets for operational purposes.

The amount of restricted net assets of Orthofix Holdings and its subsidiaries as of March 31, 2014, and December 31, 2013, is $171.1 million and $168.5 million, respectively. In addition, the Credit Agreement restricts the Company and subsidiaries that are not parties to the Credit Facilities from access to cash held by Orthofix Holdings, Inc. and its subsidiaries. All of the Company s subsidiaries that are parties to the Credit Agreement have access to this cash for operational and debt repayment purposes. The amount of restricted cash of the Company as of March 31, 2014, and December 31, 2013, was $19.3 million and $23.8 million, respectively.

In conjunction with obtaining the Credit Facilities and the Credit Agreement, as amended, the Company incurred debt issuance costs of $5 million. These costs are being amortized using the effective interest method over the life of the Credit Facilities. As of March 31, 2014, and December 31, 2013, debt issuance costs, net of accumulated amortization, related to the Credit Agreement were $0.9 million and $1.1 million, respectively.

8. Derivative instruments

The tables below disclose the types of derivative instruments the Company owns, the classifications and fair values of these instruments within the balance sheet, and the amount of gain (loss) recognized in other comprehensive income (loss) (OCI   ) or net income (loss).

(U.S. Dollars, in thousands)

As of March 31, 2014	**Fair value: favorable (unfavorable)**		**Balance sheet location**
Cross-currency swap	$	(1,035)	Other long-term liabilities
Warrants	$	107	Other long-term assets
As of December 31, 2013			
Cross-currency swap	$	(1,036)	Other long-term liabilities
Warrants	$	107	Other long-term assets

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(U.S. Dollars, in thousands)	Three Months Ended March 31, 2014	2013
Cross-currency swap unrealized gain (loss) recorded in other comprehensive income (loss), net of taxes	$ 103	$ (318)

Cross-currency swap

On September 30, 2010, the Company entered into a cross-currency swap agreement (the replacement swap agreement) with JPMorgan Chase Bank and Royal Bank of Scotland PLC (the counterparties) to manage its cash flows related to foreign currency exposure for a portion of the Company s intercompany receivable of a U.S. dollar functional currency subsidiary that is denominated in Euro.

Under the terms of the swap agreement, the Company pays Euros based on a 28.7 million notional value and a fixed rate of 5.00% and receives U.S. dollars based on a notional value of $39 million and a fixed rate of 4.635%. The expiration date is December 30, 2016, the date upon which the underlying intercompany debt, to which the swap agreement applies, matures. The swap agreement is designated as a cash flow hedge and therefore the Company recognized an unrealized gain (loss) on the change in fair value, net of tax, within other comprehensive income (loss).

Warrants

In 2013, the Company purchased notes receivable from Bone Biologics, Inc. (Bone Biologics) totaling $250 thousand, all of which were issued with detachable warrants to purchase common stock of Bone Biologics. As of March 31, 2014 and December 31, 2013 the Company held warrants for 125 thousand shares of Bone Biologics, at an exercise price of $1.00 per share.

Under the terms of the note and warrant purchase agreements, the warrants to purchase common stock in Bone Biologics are detachable from the note, exercisable over a seven year period, and transferable by the holder to other parties. There was no change in fair value of the warrants for the three months ended March 31, 2014 or 2013.

9. Fair value measurements

Fair value is defined as the price that would be received for an asset or paid to transfer a liability (an exit price) in the principal or most advantageous market for the asset or liability in an orderly transaction between market participants on the measurement date. Non-financial assets and liabilities of the Company measured at fair value include any long-lived assets or equity method investments that are impaired in a currently reported period. The authoritative guidance also describes three levels of inputs that may be used to measure fair value: