MOHAWK INDUSTRIES INC
Form 10-Q
November 02, 2012
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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10-Q

[Mark One]

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

For the quarterly period ended September 29, 2012

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 01-13697

MOHAWK INDUSTRIES, INC.
(Exact name of registrant as specified in its charter)

| Delaware<br>(State or other jurisdiction of<br>incorporation or organization) | 52-1604305<br>(I.R.S. Employer<br>Identification No.) |
|---|---|
| 160 S. Industrial Blvd., Calhoun, Georgia<br>(Address of principal executive offices) | 30701<br>(Zip Code) |

Registrant’s telephone number, including area code: (706) 629-7721

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 a smaller reporting company. See the definitions of “large accelerated filer”, “accelerated filer” and “smaller reporting company” in Rule 12b-2 of the Exchange Act.

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

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

The number of shares outstanding of the issuer's classes of common stock as of October 29, 2012, the latest practicable date, is as follows: 69,060,413 shares of Common Stock, $.01 par value.

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PART I. FINANCIAL INFORMATION

ITEM I. FINANCIAL STATEMENTS

MOHAWK INDUSTRIES, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED BALANCE SHEETS
ASSETS
(In thousands)
(Unaudited)

| | September 29, 2012 | December 31, 2011 |
|---|---|---|
| ASSETS | | |
| Current assets: | | |
| Cash and cash equivalents | $380,842 | 311,945 |
| Receivables, net | 817,214 | 686,165 |
| Inventories | 1,139,403 | 1,113,630 |
| Prepaid expenses | 128,497 | 112,779 |
| Deferred income taxes | 112,995 | 150,910 |
| Other current assets | 17,778 | 22,735 |
| Total current assets | 2,596,729 | 2,398,164 |
| Property, plant and equipment, net | 1,657,226 | 1,712,154 |
| Goodwill | 1,371,494 | 1,375,175 |
| Tradenames | 448,425 | 450,432 |
| Other intangible assets, net | 105,832 | 154,668 |
| Deferred income taxes and other non-current assets | 122,906 | 115,635 |
| | $6,302,612 | 6,206,228 |

See accompanying notes to condensed consolidated financial statements.

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MOHAWK INDUSTRIES, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED BALANCE SHEETS
LIABILITIES AND STOCKHOLDERS' EQUITY
(In thousands, except per share data)
(Unaudited)

| | September 29, 2012 | December 31, 2011 |
|---|---|---|
| LIABILITIES AND STOCKHOLDERS' EQUITY | | |
| Current liabilities: | | |
| Current portion of long-term debt | $57,673 | 386,255 |
| Accounts payable and accrued expenses | 761,186 | 715,091 |
| Total current liabilities | 818,859 | 1,101,346 |
| Deferred income taxes | 329,190 | 355,653 |
| Long-term debt, less current portion | 1,467,269 | 1,200,184 |
| Other long-term liabilities | 92,359 | 99,537 |
| Total liabilities | 2,707,677 | 2,756,720 |
| Commitments and contingencies (Notes 6 and 11) | | |
| Redeemable noncontrolling interest | — | 33,723 |
| Stockholders' equity: | | |
| Preferred stock, $.01 par value; 60 shares authorized; no shares issued | — | — |
| Common stock, $.01 par value; 150,000 shares authorized; 80,087 and 79,815 shares issued in 2012 and 2011, respectively | 801 | 798 |
| Additional paid-in capital | 1,266,108 | 1,248,131 |
| Retained earnings | 2,538,634 | 2,354,765 |
| Accumulated other comprehensive income, net | 112,854 | 135,639 |
| | 3,918,397 | 3,739,333 |
| Less treasury stock at cost; 11,032 and 11,034 shares in 2012 and 2011, respectively | 323,462 | 323,548 |
| Total stockholders' equity | 3,594,935 | 3,415,785 |
| | $6,302,612 | 6,206,228 |

See accompanying notes to condensed consolidated financial statements.

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MOHAWK INDUSTRIES, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS
(In thousands, except per share data)
(Unaudited)

| | Three Months Ended | |
|---|---|---|
| | September 29, 2012 | October 1, 2011 |
| Net sales | $1,473,493 | 1,442,512 |
| Cost of sales | 1,100,656 | 1,084,889 |
| Gross profit | 372,837 | 357,623 |
| Selling, general and administrative expenses | 268,883 | 266,159 |
| Operating income | 103,954 | 91,464 |
| Interest expense | 17,969 | 25,132 |
| Other expense | 322 | 13,413 |
| Earnings before income taxes | 85,663 | 52,919 |
| Income tax expense | 15,359 | 5,223 |
| Net earnings | 70,304 | 47,696 |
| Less: Net earnings attributable to noncontrolling interest | — | 1,050 |
| Net earnings attributable to Mohawk Industries, Inc. | $70,304 | 46,646 |
| Basic earnings per share attributable to Mohawk Industries, Inc. | $1.02 | 0.68 |
| Weighted-average common shares outstanding—basic | 69,010 | 68,759 |
| Diluted earnings per share attributable to Mohawk Industries, Inc. | $1.01 | 0.68 |
| Weighted-average common shares outstanding—diluted | 69,337 | 68,954 |

See accompanying notes to condensed consolidated financial statements.

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MOHAWK INDUSTRIES, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS
(In thousands, except per share data)
(Unaudited)

| | Nine Months Ended | |
|---|---|---|
| | September 29, 2012 | October 1, 2011 |
| Net sales | $4,352,321 | 4,263,961 |
| Cost of sales | 3,231,594 | 3,182,499 |
| Gross profit | 1,120,727 | 1,081,462 |
| Selling, general and administrative expenses | 837,079 | 832,214 |
| Operating income | 283,648 | 249,248 |
| Interest expense | 59,311 | 77,487 |
| Other (income) expense | (1,063) | 13,794 |
| Earnings before income taxes | 225,400 | 157,967 |
| Income tax expense | 40,896 | 23,639 |
| Net earnings | 184,504 | 134,328 |
| Less: Net earnings attributable to noncontrolling interest | 635 | 3,337 |
| Net earnings attributable to Mohawk Industries, Inc. | $183,869 | 130,991 |
| Basic earnings per share attributable to Mohawk Industries, Inc. | $2.67 | 1.91 |
| Weighted-average common shares outstanding—basic | 68,952 | 68,725 |
| Diluted earnings per share attributable to Mohawk Industries, Inc. | $2.66 | 1.90 |
| Weighted-average common shares outstanding—diluted | 69,247 | 68,946 |

See accompanying notes to condensed consolidated financial statements.

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MOHAWK INDUSTRIES, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME (LOSS)
(In thousands)
(Unaudited)

| | Three Months Ended | | Nine Months Ended | |
|---|---|---|---|---|
| | September 29, 2012 | October 1, 2011 | September 29, 2012 | October 1, 2011 |
| Net earnings | $70,304 | 47,696 | 184,504 | 134,328 |
| Other comprehensive income (loss): | | | | |
| Foreign currency translation adjustments | 42,382 | (146,826) | (22,773) | 6,544 |
| Pension prior service cost and actuarial gain (loss) | 8 | (101) | (12) | (10) |
| Other comprehensive income (loss) | 42,390 | (146,927) | (22,785) | 6,534 |
| Comprehensive income (loss) | 112,694 | (99,231) | 161,719 | 140,862 |
| Less: comprehensive income attributable to the noncontrolling interest | — | 1,050 | 635 | 3,337 |
| Comprehensive income (loss) attributable to Mohawk Industries, Inc. | $112,694 | (100,281) | 161,084 | 137,525 |

See accompanying notes to condensed consolidated financial statements.

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MOHAWK INDUSTRIES, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
(In thousands)
(Unaudited)

| | Nine Months Ended | |
|---|---|---|
| | September 29, 2012 | October 1, 2011 |
| Cash flows from operating activities: | | |
| Net earnings | $184,504 | 134,328 |
| Adjustments to reconcile net earnings to net cash provided by operating activities: | | |
| Restructuring | 12,455 | 15,513 |
| Depreciation and amortization | 216,415 | 222,804 |
| Deferred income taxes | 7,335 | (732) |
| Loss on extinguishment of debt | — | 1,116 |
| Loss on disposal of property, plant and equipment | 1,773 | 956 |
| Stock-based compensation expense | 11,210 | 8,129 |
| Other | — | (1,257) |
| Changes in operating assets and liabilities, net of effects of acquisitions: | | |
| Receivables, net | (97,280) | (161,398) |
| Tax deposits | (31,820) | — |
| Inventories | (24,723) | (114,682) |
| Accounts payable and accrued expenses | 39,632 | 37,764 |
| Other assets and prepaid expenses | (12,463) | (6,293) |
| Other liabilities | (8,491) | 1,940 |
| Net cash provided by operating activities | 298,547 | 138,188 |
| Cash flows from investing activities: | | |
| Additions to property, plant and equipment | (134,998) | (182,260) |
| Acquisitions, net of cash acquired | — | (24,097) |
| Investment in joint venture | (7,007) | — |
| Net cash used in investing activities | (142,005) | (206,357) |
| Cash flows from financing activities: | | |
| Payments on Senior Credit Facility | (1,059,650) | (1,158,354) |
| Proceeds from Senior Credit Facility | 1,334,500 | 1,428,849 |
| Repayment of senior notes | (336,270) | (15,000) |
| Payments on term loan and other debt | (216) | (298,295) |
| Debt issuance costs | (1,018) | (8,218) |
| Purchase of non-controlling interest | (35,000) | — |
| Distribution to non-controlling interest | (423) | (4,763) |
| Change in restricted cash | — | 27,954 |
| Change in outstanding checks in excess of cash | 1,029 | 17,155 |
| Proceeds from stock transactions | 9,356 | 2,703 |
| Net cash used in financing activities | (87,692) | (7,969) |
| Effect of exchange rate changes on cash and cash equivalents | 47 | (1,923) |
| Net change in cash and cash equivalents | 68,897 | (78,061) |
| Cash and cash equivalents, beginning of period | 311,945 | 354,217 |
| Cash and cash equivalents, end of period | $380,842 | 276,156 |

See accompanying notes to condensed consolidated financial statements.

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MOHAWK INDUSTRIES, INC. AND SUBSIDIARIES
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(In thousands, except per share amounts)
(Unaudited)

1. Interim reporting

The accompanying unaudited condensed consolidated financial statements have been prepared in accordance with instructions to Form 10-Q and do not include all of the information and footnotes required by U.S. generally accepted accounting principles for complete financial statements. In the opinion of management, all adjustments (consisting of normal recurring accruals) considered necessary for a fair presentation have been included. These statements should be read in conjunction with the consolidated financial statements and notes thereto, and the Company's description of critical accounting policies, included in the Company's 2011 Annual Report on Form 10-K, as filed with the Securities and Exchange Commission.

On March 19, 2012, the Company purchased the non-controlling interest within the Dal-Tile segment for $35,000.

Accounting Standards Update ("ASU") No. 2011-05, "Comprehensive Income (Topic 220)—Presentation of Comprehensive Income" ("ASU 2011-05") requires comprehensive income to be presented as a single continuous financial statement or in two separate but consecutive statements. The option of presenting other comprehensive income in the statement of stockholders' equity was eliminated. The Company adopted ASU 2011-05 in the first quarter of 2012 and chose to present comprehensive income (loss) as two separate but consecutive statements.

Foreign Currency Translation: Prior to the second quarter of 2012, operations carried out in Mexico used the U.S. dollar as the functional currency. Effective April 1, 2012, the Company changed the functional currency of its Mexico operations to the Mexican peso. The Company believes that the completion of a second plant in Mexico and growth in sales to the local Mexican market indicated a significant change in the economic facts and circumstances that justified the change in the functional currency. Consistent with the Company's policy on foreign currency translation disclosed in the Company's 2011 Annual Report filed on Form 10-K, the new functional currency will be translated into U.S. dollars for balance sheet accounts using the month end rates in effect as of the balance sheet date and average exchange rate for revenue and expense accounts for each respective period. The translation adjustments are deferred as a separate component of stockholders' equity, within other comprehensive income. The effects of the change in functional currency were not significant to the Company's condensed consolidated financial statements.

2. Receivables, net

Receivables, net are as follows:

| | September 29, 2012 | December 31, 2011 |
|---|---|---|
| Customers, trade | $802,605 | 696,856 |
| Income tax receivable | 613 | 1,703 |
| Other | 54,835 | 31,311 |
| | 858,053 | 729,870 |
| Less allowance for discounts, returns, claims and doubtful accounts | 40,839 | 43,705 |
| Receivables, net | $817,214 | 686,165 |

3. Inventories

The components of inventories are as follows:

| | September 29, 2012 | December 31, 2011 |
|---|---|---|
| Finished goods | $707,742 | 670,877 |
| Work in process | 107,679 | 113,311 |
| Raw materials | 323,982 | 329,442 |
| Total inventories | $1,139,403 | 1,113,630 |

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NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (continued)

4. Goodwill and intangible assets

The components of goodwill and other intangible assets are as follows:

Goodwill:

| | Mohawk | Dal-Tile | Unilin | Total |
|---|---|---|---|---|
| Balances as of December 31, 2011 | | | | |
| Goodwill | $199,132 | 1,186,913 | 1,316,555 | 2,702,600 |
| Accumulated impairment losses | (199,132) | (531,930) | (596,363) | (1,327,425) |
| | $— | 654,983 | 720,192 | 1,375,175 |
| Currency translation during the period | $— | — | (3,681) | (3,681) |
| Balances as of September 29, 2012 | | | | |
| Goodwill | $199,132 | 1,186,913 | 1,312,874 | 2,698,919 |
| Accumulated impairment losses | (199,132) | (531,930) | (596,363) | (1,327,425) |
| | $— | 654,983 | 716,511 | 1,371,494 |

Intangible assets:

| Indefinite life assets not subject to amortization: | Tradenames |
|---|---|
| Balance as of December 31, 2011 | $450,432 |
| Currency translation during the period | (2,007) |
| Balance as of September 29, 2012 | $448,425 |

| Intangible assets subject to amortization: | Customer relationships | Patents | Other | Total |
|---|---|---|---|---|
| Balances as of December 31, 2011 | $64,958 | 88,544 | 1,166 | 154,668 |
| Amortization during the period | (33,908) | (13,943) | (91) | (47,942) |
| Currency translation during the period | (171) | (733) | 10 | (894) |
| Balances as of September 29, 2012 | $30,879 | 73,868 | 1,085 | 105,832 |

| | Three Months Ended | | Nine Months Ended | |
|---|---|---|---|---|
| | September 29, 2012 | October 1, 2011 | September 29, 2012 | October 1, 2011 |
| Amortization expense | $15,683 | 17,746 | 47,942 | 53,120 |

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (continued)

5. Accounts payable and accrued expenses

Accounts payable and accrued expenses are as follows:

| | September 29, 2012 | December 31, 2011 |
|---|---|---|
| Outstanding checks in excess of cash | $18,619 | 17,590 |
| Accounts payable, trade | 397,865 | 372,616 |
| Accrued expenses | 184,455 | 154,560 |
| Product warranties | 34,449 | 30,144 |
| Accrued interest | 12,431 | 34,235 |
| Deferred tax liability | 6,184 | 8,760 |
| Accrued compensation and benefits | 107,183 | 97,186 |
| Total accounts payable and accrued expenses | $761,186 | 715,091 |

6. Product warranties

The Company warrants certain qualitative attributes of its products for up to 50 years. The Company records a provision for estimated warranty and related costs in accrued expenses, based on historical experience, and periodically adjusts these provisions to reflect actual experience.

The activity related to warranty obligations is as follows:

| | Three Months Ended | | Nine Months Ended | |
|---|---|---|---|---|
| | September 29, 2012 | October 1, 2011 | September 29, 2012 | October 1, 2011 |
| Balance at beginning of period | $34,867 | 32,052 | 30,144 | 37,265 |
| Warranty claims paid during the period | (15,166) | (13,247) | (43,952) | (43,994) |
| Pre-existing warranty accrual adjustment during the period | — | 300 | — | 3,784 |
| Warranty expense during the period | 14,748 | 10,140 | 48,257 | 32,190 |
| Balance at end of period | $34,449 | 29,245 | 34,449 | 29,245 |

7. Stock-based compensation

The Company recognizes compensation expense for all share-based payments granted based on the grant-date fair value estimated in accordance with the provisions of the Financial Accounting Standards Board Accounting Standards Codification topic ("ASC") 718-10. Compensation expense is recognized on a straight-line basis over the options' or other awards' estimated lives for fixed awards with ratable vesting provisions.

Under the Company's 2007 Incentive Plan ("2007 Plan"), the Company's principal stock compensation plan prior to May 9, 2012, the Company reserved up to a maximum of 3,200 shares of common stock for issuance upon the grant or exercise of stock options, restricted stock, restricted stock units ("RSUs") and other types of awards, to directors and key employees through 2017. Option awards are granted with an exercise price equal to the market price of the Company's common stock on the date of the grant and generally vest between three and five years with a 10-year contractual term. Restricted stock and RSUs are granted with a price equal to the market price of the Company's common stock on the date of the grant and generally vest between three and five years. On May 9, 2012, the Company's stockholders approved the 2012 Long-Term Incentive Plan ("2012 Plan"), which allows the Company to reserve up to a maximum of 3,200 shares of common stock for issuance upon the grant or exercise of awards under the 2012 Plan. No additional awards may be granted under the 2007 Plan after May 9, 2012. As of September 29, 2012, there have been no awards

granted under the 2012 Plan.

Under the 2007 Plan, the Company granted 83 and 76 options to employees at a weighted-average grant-date fair value of $28.71 and $25.39 per share for the nine months ended September 29, 2012 and October 1, 2011, respectively. There were no options granted during the three months ended September 29, 2012 and October 1, 2011. The Company recognized stock-based compensation costs related to stock options of $516 ($327 net of taxes) and $443 ($281 net of taxes) for the three months ended September 29, 2012 and October 1, 2011, respectively, and $1,648 ($1,044 net of taxes) and $1,452 ($920 net of taxes) for the nine months ended September 29, 2012 and October 1, 2011, respectively, which has been allocated to selling, general and administrative expenses. Pre-tax unrecognized compensation expense for stock options granted to employees and outside

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NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (continued)

directors, net of estimated forfeitures, was $2,624 as of September 29, 2012, and will be recognized as expense over a weighted-average period of approximately 1.7 years.

The fair value of the option award is estimated on the date of grant using the Black-Scholes-Merton valuation model. Expected volatility is based on the historical volatility of the Company's common stock. The Company uses historical data to estimate option exercise and forfeiture rates within the valuation model.

Under the 2007 Plan, the Company granted 261 and 196 RSUs at a weighted-average grant-date fair value of $65.98 and $57.35 per unit for the nine months ended September 29, 2012 and October 1, 2011, respectively. There were no RSUs granted during the three months ended September 29, 2012 and October 1, 2011. The Company recognized stock-based compensation costs related to the issuance of RSUs of $2,294 ($1,453 net of taxes) and $1,628 ($1,032 net of taxes) for the three months ended September 29, 2012 and October 1, 2011, respectively, and $9,542 ($6,045 net of taxes) and $6,608 ($4,186 net of taxes) for the nine months ended September 29, 2012 and October 1, 2011, respectively, which has been allocated to selling, general and administrative expenses. Pre-tax unrecognized compensation expense for unvested RSUs granted to employees, net of estimated forfeitures, was $17,778 as of September 29, 2012, and will be recognized as expense over a weighted-average period of approximately 3.1 years.

The Company did not grant any restricted stock awards for the nine months ended September 29, 2012 and October 1, 2011. Compensation expense for restricted stock awards for the three months and nine months ended September 29, 2012 and October 1, 2011, respectively, was not significant.

8. Other (income) expense

Other (income) expense is as follows:

| | Three Months Ended | | Nine Months Ended | |
|---|---|---|---|---|
| | September 29, 2012 | October 1, 2011 | September 29, 2012 | October 1, 2011 |
| Foreign currency (gains) losses, net | $(219) | 12,500 | (6,921) | 10,717 |
| All other, net | 541 | 913 | 5,858 | 3,077 |
| Total other expense (income) | $322 | 13,413 | (1,063) | 13,794 |

9. Earnings per share

Basic net earnings per share ("EPS") is calculated using net earnings available to common stockholders divided by the weighted-average number of shares of common stock outstanding for the period. Diluted EPS is similar to basic EPS except that the weighted-average number of shares is increased to include the number of additional common shares that would have been outstanding if the potentially dilutive common shares had been issued.

Dilutive common stock options are included in the diluted EPS calculation using the treasury stock method. Common stock options and unvested restricted shares (units) that were not included in the diluted EPS computation because the price was greater than the average market price of the common shares for the three months ended September 29, 2012 and October 1, 2011 were 902 and 1,200, respectively. Common stock options and unvested restricted shares (units) that were not included in the diluted EPS computation because the price was greater than the average market price of the common shares for the nine months ended September 29, 2012 and October 1, 2011 were 948 and 1,183, respectively.

| Three Months Ended | Nine Months Ended |
|---|---|

| | September 29, 2012 | October 1, 2011 | September 29, 2012 | October 1, 2011 |
|---|---|---|---|---|
| Net earnings available to common stockholders | $70,304 | 46,646 | 183,869 | 130,991 |
| Weighted-average common shares outstanding-basic and diluted: | | | | |
| Weighted-average common shares outstanding—basic | 69,010 | 68,759 | 68,952 | 68,725 |
| Add weighted-average dilutive potential common shares—options and RSUs to purchase common shares, net | 327 | 195 | 295 | 221 |
| Weighted-average common shares outstanding-diluted | 69,337 | 68,954 | 69,247 | 68,946 |
| Basic earnings per share attributable to Mohawk Industries, Inc. | $1.02 | 0.68 | 2.67 | 1.91 |
| Diluted earnings per share attributable to Mohawk Industries, Inc. | $1.01 | 0.68 | 2.66 | 1.90 |

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10. Segment reporting

The Company has three reporting segments: the Mohawk segment, the Dal-Tile segment and the Unilin segment. The Mohawk segment designs, manufactures, sources, distributes and markets its floor covering product lines, which include carpets, ceramic tile, laminate, rugs, carpet pad, hardwood and resilient, primarily in North America through its network of regional distribution centers and satellite warehouses using Company-operated trucks, common carriers or rail transportation. The segment's product lines are sold through various selling channels, which include independent floor covering retailers, home centers, mass merchandisers, department stores, commercial dealers and commercial end users. The Dal-Tile segment designs, manufactures, sources, distributes and markets a broad line of ceramic tile, porcelain tile, natural stone and other products, primarily in North America and Mexico through its network of regional distribution centers and Company-operated service centers using Company-operated trucks, common carriers or rail transportation. The segment's product lines are sold through independent distributors, home center retailers, tile and flooring retailers and contractors. The Unilin segment designs, manufactures, sources, licenses, distributes and markets laminate and hardwood flooring, roofing systems, insulation panels and other wood products, primarily in North America and Europe through various selling channels, which include retailers, independent distributors and home centers.

The accounting policies for each operating segment are consistent with the Company's policies for the consolidated financial statements. Amounts disclosed for each segment are prior to any elimination or consolidation entries. Corporate general and administrative expenses attributable to each segment are estimated and allocated accordingly. Segment performance is evaluated based on operating income.

Segment information is as follows:

| | Three Months Ended | | Nine Months Ended | |
|---|---|---|---|---|
| | September 29, 2012 | October 1, 2011 | September 29, 2012 | October 1, 2011 |
| Net sales: | | | | |
| Mohawk | $751,787 | 754,470 | 2,186,160 | 2,203,699 |
| Dal-Tile | 417,533 | 381,891 | 1,214,746 | 1,105,775 |
| Unilin | 328,582 | 329,514 | 1,020,380 | 1,018,443 |
| Intersegment sales | (24,409) | (23,363) | (68,965) | (63,956) |
| | $1,473,493 | 1,442,512 | 4,352,321 | 4,263,961 |
| Operating income (loss): | | | | |
| Mohawk | $43,810 | 30,946 | 106,228 | 79,187 |
| Dal-Tile | 37,452 | 33,073 | 99,912 | 82,911 |
| Unilin | 28,892 | 33,048 | 96,613 | 105,507 |
| Corporate and intersegment eliminations | (6,200) | (5,603) | (19,105) | (18,357) |
| | $103,954 | 91,464 | 283,648 | 249,248 |

| | September 29, 2012 | December 31, 2011 |
|---|---|---|
| Assets: | | |
| Mohawk | $1,760,828 | 1,769,065 |
| Dal-Tile | 1,783,147 | 1,732,818 |
| Unilin | 2,586,084 | 2,533,070 |
| Corporate and intersegment eliminations | 172,553 | 171,275 |

| | | |
|---|---|---|
| | $6,302,612 | 6,206,228 |

11. Commitments, contingencies and other

The Company is involved in litigation from time to time in the regular course of its business. Except as noted below, there are no material legal proceedings pending or known by the Company to be contemplated to which the Company is a party or to which any of its property is subject.

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Beginning in August 2010, a series of civil lawsuits were initiated in several U.S. federal courts alleging that certain manufacturers of polyurethane foam products and competitors of the Company’s carpet underlay division had engaged in price fixing in violation of U.S. antitrust laws. Mohawk has been named as a defendant in a number of the individual cases (the first filed on August 26, 2010), as well as in two consolidated amended class action complaints, the first filed on February 28, 2011, on behalf of a class of all direct purchasers of polyurethane foam products, and the second filed on March 21, 2011, on behalf of a class of indirect purchasers. All pending cases in which the Company has been named as a defendant have been filed in or transferred to the U.S. District Court for the Northern District of Ohio for consolidated pre-trial proceedings under the name In re: Polyurethane Foam Antitrust Litigation, Case No. 1:10-MDL-02196.

In these actions, the plaintiffs, on behalf of themselves and/or a class of purchasers, seek three times the amount of unspecified damages allegedly suffered as a result of alleged overcharges in the price of polyurethane foam products from at least 1999 to the present. Each plaintiff also seeks attorney fees, pre-judgment and post-judgment interest, court costs, and injunctive relief against future violations. In April 2011, the Company filed a motion to dismiss the class action claims brought by the direct purchasers, and in May 2011, the Company moved to dismiss the claims brought by the indirect purchasers. On July 19, 2011, the Court issued a written opinion denying all defendants’ motions to dismiss. In December 2011, the Company was named as a defendant in a Canadian Class action, Hi ! Neighbor Floor Covering Co. Limited v. Hickory Springs Manufacturing Company, et al., filed in the Superior Court of Justice of Ontario, Canada and Options Consommateures v. Vitafoam, Inc. et.al., filed in the Superior Court of Justice of Quebec, Montreal, Canada, both of which allege similar claims against the Company as raised in the U.S. actions and seek unspecified damages and punitive damages. The Company denies all of the allegations in these actions and will vigorously defend itself.

The Company believes that adequate provisions for resolution of all contingencies, claims and pending litigation have been made for probable losses that are reasonably estimable. These contingencies are subject to significant uncertainties and we are unable to estimate the amount or range of loss, if any, in excess of amounts accrued. The Company does not believe that the ultimate outcome of these actions will have a material adverse effect on its financial condition but could have a material adverse effect on its results of operations, cash flows or liquidity in a given quarter or year.
In January 2012, the Company received a €24,000 assessment from the Belgian tax authority related to its year ended December 31, 2008, asserting that the Company had understated its Belgian taxable income for that year. The Company filed a formal protest in the first quarter of 2012 refuting the Belgian tax authority's position and in order to eliminate the accrual of additional interest on the assessed amount, the Company remitted payment of the tax assessment, plus applicable interest of €2,912 (collectively, the “Deposit”). In July 2012, the Company received notification of the Belgian tax authority's intention to extend the statute of limitations back to and including the tax year 2005. On September 10, 2012, the Company received notice from the Belgian tax authority setting aside the 2008 assessment and refunding the Deposit to the Company. Accordingly, the prepayment that the Company recorded in the first quarter of 2012 in the amount of the Deposit has been reclassified as a current other receivable as of September 29, 2012.

Subsequent to the quarter ended September 29, 2012, the Company received notifications from the Belgian taxing authority of its intent to assess the Company under a revised theory for certain years in the extended statute of limitations period. The Company disagrees with the views of the Belgian tax authority on this matter and will continue to vigorously defend itself. Although there can be no assurances, the Company believes the ultimate outcome of these actions will not have a material adverse effect on its financial condition but could have a material adverse effect on its results of operations, liquidity or cash flows in a given quarter or year.

For the three and nine months ended September 29, 2012, the Company recorded pre-tax business restructuring charges of $4,229 and $12,455 of which $2,984 and $9,620 was recorded as cost of sales and $1,245 and $2,835 was recorded as selling, general and administrative expenses for the same periods, respectively. For the three and nine months ended October 1, 2011, the Company recorded pre-tax business restructuring charges of $2,186 and $15,513 respectively, of which $1,185 and $13,064 was recorded as cost of sales and $1,001 and $2,449 was recorded as selling, general and administrative expenses for the same periods, respectively. The charges for 2012 and 2011 primarily relate to the Company's actions taken to lower its cost structure and improve the efficiency of its manufacturing and distribution operations as the Company adjusts to current economic conditions.

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NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (continued)

The restructuring activity for the nine months ended September 29, 2012 is as follows:

| | Lease impairments | Asset write-downs | Severance | Other restructuring costs | Total |
|---|---|---|---|---|---|
| Balance as of December 31, 2011 | $ 10,956 | — | 2,378 | 1,511 | 14,845 |
| Provision - Unilin Segment | — | 138 | 1,775 | 38 | 1,951 |
| Provision - Mohawk Segment | — | 6,687 | 4,069 | (252) | 10,504 |
| Cash payments | (2,795) | — | (4,996) | (773) | (8,564) |
| Non-cash items | — | (6,825) | — | — | (6,825) |
| Balance as of September 29, 2012 | $ 8,161 | — | 3,226 | 524 | 11,911 |

The Company expects the remaining severance costs, lease impairments and other restructuring costs to be paid over the next four years.

Subsequent to the balance sheet date, the Company announced plans to consolidate mosaic tile production in the Dal-Tile segment in order to streamline manufacturing capabilities. The Company is finalizing its estimates and expects to record a restructuring charge in the fourth quarter of 2012.

12. Debt

Senior Credit Facility

On July 8, 2011, the Company entered into a five-year, senior, secured revolving credit facility (the “Senior Credit Facility”). The Senior Credit Facility provides for a maximum of $900,000 of revolving credit, including limited amounts of credit in the form of letters of credit and swingline loans. The Company paid financing costs of $8,218 in connection with its Senior Credit Facility. These costs were deferred and, along with unamortized costs of $12,277 related to the Company’s prior senior, secured revolving credit facility, are being amortized over the term of the Senior Credit Facility.

On January 20, 2012, the Company entered into an amendment to the Senior Credit Facility that provides for an incremental term loan facility in the aggregate principal amount of $150,000. The Company paid financing costs of $1,018 in connection with the amendment to its Senior Credit Facility. These costs were deferred and are being amortized over the remaining term of the Senior Credit Facility. The incremental term loan facility provides for eight scheduled quarterly principal payments of $1,875, with the first such payment due on June 30, 2012, followed by four scheduled quarterly principal payments of $3,750, with remaining quarterly principal payments of $5,625 prior to maturity.

The Senior Credit Facility is scheduled to mature on July 8, 2016. The Company can terminate and prepay the Senior Credit Facility at any time without payment of any termination or prepayment penalty (other than customary breakage costs in respect of loans bearing interest at a rate based on LIBOR).

At the Company’s election, revolving loans under the Senior Credit Facility bear interest at annual rates equal to either (a) LIBOR for 1-, 2-, 3- or 6- month periods, as selected by the Company, plus an applicable margin ranging between 1.25% and 2.0%, or (b) the higher of the Bank of America, N.A. prime rate, the Federal Funds rate plus 0.5%, and a monthly LIBOR rate plus 1.0%, plus an applicable margin ranging between 0.25% and 1.0%. The Company also pays a commitment fee to the lenders under the Senior Credit Facility on the average amount by which the aggregate commitments of the lenders exceed utilization of the Senior Credit Facility ranging from 0.25% to 0.4% per annum.

The applicable margin and the commitment fee are determined based on the Company's Consolidated Net Leverage Ratio (with applicable margins and the commitment fee increasing as the ratio increases).

All obligations of the Company and the other borrowers under the Senior Credit Facility are required to be guaranteed by all of the Company's material domestic subsidiaries, and all obligations of borrowers that are foreign subsidiaries are guaranteed by those foreign subsidiaries of the Company which the Company designates as guarantors.

Due to the rating agency upgrade announced on March 14, 2012 by Standard & Poor's Financial Services, LLC ("S&P"), the security interests in domestic accounts receivable and inventories, certain shares of capital stock (or equivalent ownership interests) of the domestic borrowers' and domestic guarantors' subsidiaries, and proceeds of any of the foregoing securing obligations under the Senior Credit Facility were released. The Company will be required to reinstate such security interests if there is a ratings downgrade such that: (a) both (i) the Moody's Investors Service, Inc. ("Moody's") rating is Ba2 and (ii) the

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NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (continued)

S&P rating is BB, (b) (i) the Moody's rating is Ba3 or lower and (ii) the S&P rating is below BBB- (with a stable outlook or better) or (c) (i) the Moody's rating is below Baa3 (with a stable outlook or better) and (ii) the S&P rating is BB- or lower.

The Senior Credit Facility includes certain affirmative and negative covenants that impose restrictions on the Company's financial and business operations, including limitations on liens, indebtedness, investments, fundamental changes, asset dispositions, dividends and other similar restricted payments, transactions with affiliates, payments and modifications of certain existing debt, future negative pledges, and changes in the nature of the Company's business. Many of these limitations are subject to numerous exceptions. The Company is also required to maintain a Consolidated Interest Coverage Ratio of at least 3.0 to 1.0 and a Consolidated Net Leverage Ratio of no more than 3.75 to 1.0, each as of the last day of any fiscal quarter, as defined in the Senior Credit Facility. The Senior Credit Facility also contains customary representations and warranties and events of default, subject to customary grace periods.

As of September 29, 2012, the amount utilized under the Senior Credit Facility including the term loan was $670,213 resulting in a total of $376,037 available under the Senior Credit Facility. The amount utilized included $572,850 of borrowings, $46,823 of standby letters of credit guaranteeing the Company's industrial revenue bonds and $50,540 of standby letters of credit related to various insurance contracts and foreign vendor commitments.

Senior Notes

On January 17, 2006, the Company issued $900,000 aggregate principal amount of 6.125% notes due January 15, 2016. Interest payable on these notes is subject to adjustment if either Moody's or S&P, or both, upgrades or downgrades the rating assigned to the notes. Each rating agency downgrade results in a 0.25% increase in the interest rate, subject to a maximum increase of 1% per rating agency. If later the rating of these notes improves, then the interest rates would be reduced accordingly. Each 0.25% increase in the interest rate of these notes would increase the Company's interest expense by approximately $63 per quarter per $100,000 of outstanding notes. In 2009, interest rates increased by an aggregate amount of 75 basis points as a result of downgrades by Moody's and S&P. In the first quarter of 2012, interest rates decreased by 50 basis points as a result of the upgrades from S&P and Moody's. Any future downgrades in the Company's credit ratings could increase the cost of its existing credit and adversely affect the cost of and ability to obtain additional credit in the future.

In 2002, the Company issued

9,165

$

11,296

For the nine month period ended September 30:

| **(In US$ thousands)** | **External Sales** | | **Intersegment Sales** | |
|---|---|---|---|---|
| | **2007** | **2006** | **2007** | **2006** |
| Domestic | $ 122,718 | $ 113,185 | $ 3,137 | $ 2,476 |
| Blackstone | 85,859 | - | 2,449 | - |
| Breg | 61,522 | 55,901 | 2,561 | 1,027 |
| International | 91,389 | 80,133 | 22,108 | 44,218 |
| Total | $ 361,488 | $ 249,219 | $ 30,255 | $ 47,721 |

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The following table presents operating income (loss) by segment for the three and nine month periods ended September 30:

| **Operating Income (Loss)**<br>**(In US$ thousands)** | **Three Months Ended September 30,** 2007 | 2006 | **Nine Months Ended September 30,** 2007 | 2006 |
|---|---|---|---|---|
| Domestic | $ 14,050 | $ 7,391 | $ 42,124 | $ 26,430 |
| Blackstone | (816) | (40,271) | (2,164) | (40,271) |
| Breg | 2,686 | 1,392 | 6,013 | 4,926 |
| International | 4,230 | 4,594 | 14,824 | 16,509 |
| Group Activities | (3,735) | (3,258) | (11,644) | (8,546) |
| Eliminations | (624) | (305) | (2,802) | (1,681) |
| Total | $ 15,791 | $ (30,457) | $ 46,351 | $ (2,633) |

The following tables present sales by market sector for the three and nine month periods ended September 30, 2007 and 2006:

**Sales by Market Sector**
**for the three month period ended September 30, 2007**

| **(In US$ thousands)** | **Orthofix Domestic** | **Blackstone** | **Breg** | **Orthofix International** | **Total** |
|---|---|---|---|---|---|
| Spine | $ 31,693 | $ 29,448 | $ - | $ 168 | $ 61,309 |
| Orthopedics | 10,278 | - | - | 16,026 | 26,304 |
| Sports Medicine | - | - | 21,206 | 869 | 22,075 |
| Vascular | - | - | - | 4,718 | 4,718 |
| Other | - | - | - | 6,714 | 6,714 |
| Total | $ 41,971 | $ 29,448 | $ 21,206 | $ 28,495 | $ 121,120 |

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**Sales by Market Sector**
**for the three month period ended September 30, 2006**

| (In US$ thousands) | Orthofix Domestic | Blackstone | Breg | Orthofix International | Total |
|---|---|---|---|---|---|
| Spine | $ 29,216 | $ - | $ - | $ 66 | $ 29,282 |
| Orthopedics | 8,736 | - | - | 14,749 | 23,485 |
| Sports Medicine | - | - | 18,667 | 739 | 19,406 |
| Vascular | - | - | - | 5,084 | 5,084 |
| Other | - | - | - | 6,111 | 6,111 |
| Total | $ 37,952 | $ - | $ 18,667 | $ 26,749 | $ 83,368 |

**Sales by Market Sector**
**for the nine month period ended September 30, 2007**

| (In US$ thousands) | Orthofix Domestic | Blackstone | Breg | Orthofix International | Total |
|---|---|---|---|---|---|
| Spine | $ 92,650 | $ 85,859 | $ - | $ 421 | $ 178,930 |
| Orthopedics | 30,068 | - | - | 51,865 | 81,933 |
| Sports Medicine | - | - | 61,522 | 3,033 | 64,555 |
| Vascular | - | - | - | 15,217 | 15,217 |
| Other | - | - | - | 20,853 | 20,853 |
| Total | $ 122,718 | $ 85,859 | $ 61,522 | $ 91,389 | $ 361,488 |

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| | Sales by Market Sector for the nine month period ended September 30, 2006 | | | | |
|---|---|---|---|---|---|
| **(In US$ thousands)** | **Orthofix Domestic** | **Blackstone** | **Breg** | **Orthofix International** | **Total** |
| Spine | $ 86,595 | $ - | $ - | $ 186 | $ 86,781 |
| Orthopedics | 26,590 | - | - | 44,552 | 71,142 |
| Sports Medicine | - | - | 55,901 | 2,018 | 57,919 |
| Vascular | - | - | - | 15,417 | 15,417 |
| Other | - | - | - | 17,960 | 17,960 |
| Total | $ 113,185 | $ - | $ 55,901 | $ 80,133 | $ 249,219 |

NOTE 14: INCOME TAXES

The difference between the reported provision for income taxes and a provision computed by applying the statutory rates applicable to each subsidiary of the Company is primarily attributable to a discrete tax benefit resulting from tax credits associated with research and development expense. Further, the effective tax rate has been positively affected by the Company's European restructuring in 2006 and a similar transaction in 2002, whereby certain intangible assets were sold between subsidiaries in order to optimize the Company's supply chain. Such assets were sold at estimates of fair value based upon valuations which remain subject to review by the local taxing authorities. Further the effective tax rate has been affected by non-deductible foreign losses, the generation of unutilizable net operating losses in various jurisdictions, tax planning associated with the acquisition of Breg and the Section 199 deduction related to income attributable to production activities occurring in the United States.

NOTE 15: EARNINGS PER SHARE

For the three and nine month periods ended September 30, 2007 and 2006, there were no adjustments to net income (loss) (the numerators) for purposes of calculating basic and diluted net income (loss) per common share. The following table sets forth a reconciliation of the share numbers (the denominators) in computing earnings per share in accordance with SFAS No. 128, "Earnings Per Share":

| | Three Months Ended September 30, | | Nine Months Ended September 30, | |
|---|---|---|---|---|
| | **2007** | **2006** | **2007** | **2006** |
| Weighted average common shares - basic | 16,639,019 | 16,193,086 | 16,546,385 | 16,084,388 |
| Effect of dilutive securities | 250,284 | - | 378,699 | - |
| Weighted average common shares – diluted | 16,889,303 | 16,193,086 | 16,925,084 | 16,084,388 |

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The Company did not include 172,218 and 145,218 options in the diluted shares outstanding calculation for the three and nine month periods ended September 30, 2007, because their inclusion would have been antidilutive or because their exercise price exceeded the average market price of the Company's common stock during the period. For both the three and nine month periods ended September 30, 2006, the Company did not include 680,300 options in the diluted shares outstanding calculation because their inclusion would have been antidilutive or because their exercise price exceeded the average market price of the Company's common stock during the period.

NOTE 16: DERIVATIVE INSTRUMENT

In 2006, the Company entered into a cross-currency swap agreement to manage its foreign currency exposure related to a portion of the Company's intercompany receivable of a U.S. dollar functional currency subsidiary that is denominated in Euro. The derivative instrument, a ten-year fully amortizable agreement with a notional amount of $63.0 million, is scheduled to expire on December 30, 2016. The instrument is designated as a cash flow hedge. The amount outstanding under the agreement as of September 30, 2007 is $63.0 million. Under the agreement, the Company pays Euro and receives U.S. dollars based on scheduled cash flows in the agreement. The Company recognized the unrealized loss on the change in fair value of this swap arrangement of $0.4 million and $0.6 million, net of tax, within other comprehensive income for the three and nine month periods ended September 30, 2007.

NOTE 17: CONTINGENCIES

*Litigation*

Effective October 29, 2007, the Company's subsidiary, Blackstone, entered into a settlement agreement with respect to a patent infringement lawsuit captioned Medtronic Sofamor Danek USA Inc., Warsaw Orthopedic, Inc., Medtronic Puerto Rico Operations Co., and Medtronic Sofamor Danek Deggendorf, GmbH v. Blackstone Medical, Inc., Civil Action No. 06-30165-MAP, filed on September 22, 2006 in the United States District Court for the District of Massachusetts. In that lawsuit, the plaintiffs had alleged that (i) they were the exclusive licensees of United States Patent Nos. 6,926,718 B1, 6,936,050 B2, 6,936,051 B2, 6,398,783 B1 and 7,066,961 B2 (the "Patents"), and (ii) Blackstone's making, selling, offering for sale, and using within the United States of its Blackstone Anterior Cervical Plate, 3º Anterior Cervical Plate, Hallmark Anterior Cervical Plate and Construx Mini PEEK VBR System products infringed the Patents, and that such infringement was willful. The Complaint requested both damages and an injunction against further alleged infringement of the Patents. The Complaint did not specifically state an amount of damages. Blackstone denied infringement and asserted that the Patents were invalid. On July 20, 2007, the Company submitted a claim for indemnification from the escrow fund established in connection with the agreement and plan of merger between the Company, New Era Medical Corp. and Blackstone, dated as of August 4, 2006 (the "Merger Agreement"), for any losses to the Company or Blackstone resulting from this matter. The Company was subsequently notified by legal counsel for the former shareholders that the representative of the former shareholders of Blackstone has objected to the indemnification claim and intends to contest it in accordance with the terms of the Merger Agreement. The Company is unable to predict the outcome of the escrow claim or to estimate the amount, if any, that may ultimately be returned to the Company from the escrow fund. The settlement agreement is not expected to have a material impact on the Company's consolidated financial position, results of operations or cash flows.

On or about July 23, 2007, Blackstone received a subpoena issued by the Department of Health and Human Services, Office of Inspector General, under the authority of the federal healthcare anti-kickback and false claims statutes. The subpoena seeks documents for the period January 1, 2000 through July 31, 2006 which is prior to Blackstone's acquisition by the Company. The Company believes that the subpoena concerns the compensation of physician consultants and related matters. Blackstone is cooperating with the government's request and is in the process of responding to the subpoena. The Company is unable to predict what action, if any, might be taken in the future by the Department of Health and Human Services, Office of Inspector General or other governmental authorities as a result

of this investigation or what impact, if any, the outcome of this matter might have on its consolidated financial position, results of operations, or cash flows. On September 17, 2007, the Company submitted a claim for indemnification from the escrow fund established in connection with the Merger Agreement for any losses to the Company or Blackstone resulting from this matter. The Company was subsequently notified by legal counsel for the former shareholders that the representative of the former shareholders of Blackstone has objected to the indemnification claim and intends to contest it in accordance with the terms of the Merger Agreement. The Company is unable to predict the outcome of the escrow claim or to estimate the amount, if any, that may ultimately be returned to the Company from the escrow fund.

On or about September 27, 2007, Blackstone received a federal grand jury subpoena issued by the United States' Attorney's Office for the District of Nevada ("USAO-Nevada"). The subpoena seeks documents for the period from January 1999 to the present. The Company believes that the subpoena concerns payments or gifts made by Blackstone to certain physicians. Blackstone is cooperating with the government's request and is in the process of responding to the subpoena. The Company is unable to predict what action, if any, might be taken in the future by the USAO-Nevada or other governmental authorities as a result of this investigation or what impact, if any, the outcome of this matter might have on its consolidated financial position, results of operations, or cash flows. It is the Company's intention to submit a claim for indemnification from the escrow fund established in connection with the Merger Agreement for any losses to the Company or Blackstone resulting from this matter.

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By order entered on January 4, 2007, the United States District Court for the Eastern District of Arkansas unsealed a qui tam complaint captioned Thomas v. Chan, et al., 4:06-cv-00465-JLH, filed against Dr. Chan, Blackstone and other defendants including another device manufacturer. A qui tam action is a civil lawsuit brought by an individual for an alleged violation of a federal statute, in which the U.S. Department of Justice has the right to intervene and take over the prosecution of the lawsuit at its option. The complaint alleges causes of action under the False Claims Act for alleged inappropriate payments and other items of value conferred on Dr. Chan. On December 29, 2006, the U.S. Department of Justice filed a notice of non-intervention in the case. Plaintiff subsequently amended the complaint to add the Company as a defendant. The Company believes Blackstone and the Company have meritorious defenses to the claims alleged and the Company intends to defend vigorously against this lawsuit. On September 17, 2007, the Company submitted a claim for indemnification from the escrow fund established in connection with the Merger Agreement for any losses to the Company or Blackstone resulting from this matter. The Company was subsequently notified by legal counsel for the former shareholders that the representative of the former shareholders of Blackstone has objected to the indemnification claim and intends to contest it in accordance with the terms of the Merger Agreement. The Company is unable to predict the outcome of the escrow claim or to estimate the amount, if any, that may ultimately be returned to the Company from the escrow fund.

Between January 2007 and May 2007, Orthofix, Inc. and/or Blackstone were named defendants, along with other medical device manufacturers, in three civil lawsuits alleging that Dr. Chan had performed unnecessary surgeries in three different instances. All three civil lawsuits have recently been served and are pending in the Circuit Court of White County, Arkansas. The Company believes Blackstone and Orthofix, Inc. have meritorious defenses to the claims alleged and we intend to defend vigorously against these lawsuits. On September 17, 2007, the Company submitted a claim for indemnification from the escrow fund established in connection with the Merger Agreement for any losses to the Company or Blackstone resulting from one of these three civil lawsuits. The Company was subsequently notified by legal counsel for the former shareholders that the representative of the former shareholders of Blackstone has objected to the indemnification claim and intends to contest it in accordance with the terms of the Merger Agreement. The Company is unable to predict the outcome of the escrow claim or to estimate the amount, if any, that may ultimately be returned to the Company from the escrow fund.

In addition to the foregoing, the Company has submitted claims for indemnification from the escrow fund established in connection with the Merger Agreement for losses that have or may result from certain claims against Blackstone alleging that plaintiffs and/or claimants were entitled to payments for Blackstone stock options not reflected in Blackstone's corporate ledger at the time of Blackstone's acquisition by the Company. To date, the representative of the former shareholders of Blackstone and the Company has not objected to approximately $1.5 million in claims from the escrow fund, with certain claims remaining pending.

The Company cannot predict the outcome of any proceedings or claims made against the Company or its subsidiaries and there can be no assurance that the ultimate resolution of any claim will not have a material adverse impact on its consolidated financial position, results of operations, or cash flows.

In addition to the foregoing, in the normal course of our business, the Company is involved in various lawsuits from time to time and may be subject to certain other contingencies.

*Concentrations of credit risk*

There have been no material changes from the information provided in the Company’s Annual Report on Form 10-K for the fiscal year ended December 31, 2006.

**Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations**

The following discussion and analysis addresses our liquidity, financial condition, and the results of our operations for the three and nine months ended September 30, 2007 compared to our results of operations for the three and nine months ended September 30, 2006. These discussions should be read in conjunction with our historical consolidated financial statements and related notes thereto and the other financial information included in this Form 10-Q and in our Annual Report on Form 10-K for the fiscal year ended December 31, 2006.

**General**

We are a diversified orthopedic products company offering a broad line of surgical and non-surgical products for the Spine, Orthopedics, Sports Medicine and Vascular market sectors. Our products are designed to address the lifelong bone-and-joint health needs of patients of all ages, helping them achieve a more active and mobile lifestyle. We design, develop, manufacture, market and distribute medical equipment used principally by musculoskeletal medical specialists for orthopedic applications. Our main products are invasive and minimally invasive spinal implant products and related biologics; non-invasive bone growth stimulation products used to enhance the success rate of spinal fusions and to treat non-union fractures; external and internal fixation devices used in fracture treatment, limb lengthening and bone reconstruction; and bracing products used for ligament injury prevention, pain management and protection of surgical repair to promote faster healing. Our products also include a device for enhancing venous circulation, cold therapy, other pain management products, bone cement and devices for removal of bone cement used to fix artificial implants and airway management products used in anesthesia applications.

We have administrative and training facilities in the United States and Italy and manufacturing facilities in the United States, the United Kingdom, Italy and Mexico. We directly distribute our products in the United States, the United Kingdom, Italy, Germany, Switzerland, Austria, France, Belgium, Mexico, Brazil, and Puerto Rico. In several of these and other markets, we also distribute our products through independent distributors.

Our consolidated financial statements include the financial results of the Company and its wholly-owned and majority-owned subsidiaries and entities over which we have control. All intercompany accounts and transactions are eliminated in consolidation.

Our reporting currency is the United States Dollar. All balance sheet accounts, except shareholders' equity, are translated at period-end exchange rates, and revenue and expense items are translated at weighted average rates of exchange prevailing during the period. Gains and losses resulting from foreign currency transactions are included in other income (expense). Gains and losses resulting from the translation of foreign currency financial statements are recorded in the accumulated other comprehensive income component of shareholders' equity.

Our financial condition, results of operations and cash flows are not significantly impacted by seasonal trends. In addition, we do not believe our operations will be significantly affected by inflation. However, in the ordinary course of business, we are exposed to the impact of changes in interest rates and foreign currency fluctuations. Our objective is to limit the impact of such movements on earnings and cash flows. In order to achieve this objective, we seek to balance non-dollar income and expenditures. During the first nine months of 2007, we have used derivative instruments to hedge certain foreign currency fluctuation exposures. See Item 3 – "Quantitative and Qualitative Disclosures About Market Risk."

On September 22, 2006, we completed the acquisition of Blackstone Medical, Inc. ("Blackstone"), a privately held company specializing in the design, development and marketing of spinal implant and related biologics products. The purchase price for the acquisition was $333.0 million, subject to certain closing adjustments, plus transaction costs and other accruals totaling approximately $12.1 million as of September 30, 2007. The acquisition and related costs were

financed with $330.0 million of senior secured term debt and cash on hand. Debt issuance costs were approximately $6.2 million.

Effective with the acquisition of Blackstone, we manage our operations as four business segments: Domestic, Blackstone, Breg, and International. Orthofix Domestic (“Domestic”) consists of operations of our subsidiary Orthofix Inc. Blackstone consists of Blackstone’s domestic and international operations. Breg consists of Breg Inc.’s (“Breg”) domestic operations and international distributors. Orthofix International (“International”) consists of operations which are located in the rest of the world (excluding Blackstone’s international operations), as well as independent export distribution operations. Group Activities are comprised of the operating expenses and identifiable assets of Orthofix International N.V. and its U.S. holding company, Orthofix Holdings, Inc.

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**Segment and Market Sector Revenues**

The following tables display net sales by business segment and net sales by market sector. We provide net sales by market sector for information purposes only. We keep our books and records and account for net sales, costs of sales and expenses by business segment. In 2006, concurrent with the acquisition of Blackstone, we redefined our business segments and market sectors. All prior period information has been restated to conform to the new business segments and market sectors.

**Business Segment:**

| | Three Months Ended September 30, | | | |
|---|---|---|---|---|
| **(In US$ thousands)** | **2007** | | **2006** | |
| | **Net Sales** | **Percent of Total Net Sales** | **Net Sales** | **Percent of Total Net Sales** |
| Domestic | $ 41,971 | 35% | $ 37,952 | 46% |
| Blackstone | 29,448 | 24% | - | -% |
| Breg | 21,206 | 17% | 18,667 | 22% |
| International | 28,495 | 24% | 26,749 | 32% |
| Total | $ 121,120 | 100% | $ 83,368 | 100% |

| | Nine Months Ended September 30, | | | |
|---|---|---|---|---|
| **(In US$ thousands)** | **2007** | | **2006** | |
| | **Net Sales** | **Percent of Total Net Sales** | **Net Sales** | **Percent of Total Net Sales** |
| Domestic | $ 122,718 | 34% | $ 113,185 | 46% |
| Blackstone | 85,859 | 24% | - | -% |
| Breg | 61,522 | 17% | 55,901 | 22% |
| International | 91,389 | 25% | 80,133 | 32% |
| Total | $ 361,488 | 100% | $ 249,219 | 100% |

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**Market Sector:**

| (In US$ thousands) | Three Months Ended September 30, 2007 | | 2006 | |
|---|---|---|---|---|
| | Net Sales | Percent of Total Net Sales | Net Sales | Percent of Total Net Sales |
| Spine | $ 61,309 | 51% | $ 29,282 | 35% |
| Orthopedics | 26,304 | 22% | 23,485 | 29% |
| Sports Medicine | 22,075 | 18% | 19,406 | 23% |
| Vascular | 4,718 | 4% | 5,084 | 6% |
| Other | 6,714 | 5% | 6,111 | 7% |
| Total | $ 121,120 | 100% | $ 83,368 | 100% |

| (In US$ thousands) | Nine Months Ended September 30, 2007 | | 2006 | |
|---|---|---|---|---|
| | Net Sales | Percent of Total Net Sales | Net Sales | Percent of Total Net Sales |
| Spine | $ 178,930 | 49% | $ 86,781 | 35% |
| Orthopedics | 81,933 | 23% | 71,142 | 29% |
| Sports Medicine | 64,555 | 18% | 57,919 | 23% |
| Vascular | 15,217 | 4% | 15,417 | 6% |
| Other | 20,853 | 6% | 17,960 | 7% |
| Total | $ 361,488 | 100% | $ 249,219 | 100% |

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The following table presents certain items from our Condensed Consolidated Statements of Operations as a percentage of net sales for the periods indicated:

| | **Three Months Ended September 30,** | | **Nine Months Ended September 30,** | |
|---|---|---|---|---|
| | **2007** (%) | **2006** (%) | **2007** (%) | **2006** (%) |
| Net sales | 100 | 100 | 100 | 100 |
| Cost of sales | 25 | 25 | 26 | 26 |
| Gross profit | 75 | 75 | 74 | 74 |
| Operating expenses (income) | | | | |
| Sales and marketing | 39 | 44 | 38 | 40 |
| General and administrative | 14 | 15 | 14 | 15 |
| Research and development | 5 | 51* | 5 | 20* |
| Amortization of intangible assets | 4 | 2 | 4 | 2 |
| KCI settlement, net of litigation costs | - | - | - | (1) |
| Total operating income (loss) | 13 | (37) | 13 | (1) |
| Net income (loss) | 7 | (43) | 6 | (6) |

* - Includes $40.0 million related to the write-off of acquired in-process research and development of Blackstone.

**Three Months Ended September 30, 2007 Compared to Three Months Ended September 30, 2006**

Net sales increased 45% to $121.1 million for the third quarter of 2007 compared to $83.4 million for the third quarter of 2006. The impact of foreign currency increased sales by $1.5 million during the third quarter of 2007 as compared to the third quarter of 2006.

*Sales by Business Segment:*

Net sales in Domestic increased to $42.0 million in the third quarter of 2007 compared to $38.0 million in the third quarter of 2006, an increase of 11%. Domestic represented 35% of total net sales during the third quarter of 2007 and 46% of total net sales for the third quarter of 2006. The increase in Domestic sales was partially the result of a 8% increase in sales in the Spine market sector. This increase continues to be driven by our Spinal-Stim® and Cervical-Stim® products. The Cervical-Stim® continues to be the only FDA-approved stimulation device for the enhancement of fusion in the cervical spine. The Orthopedic market sector sales increased 18% due to increased sales of internal fixation products and a 26% increase in sales of the Physio-Stim® compared to the third quarter of 2006. These increases were partially offset by a 15% decrease in sales of external fixation products when compared to the third quarter of 2006.

**Domestic Sales by Market Sector:**

| | **Net Sales for the Three Months Ended September 30,** | | |
|---|---|---|---|
| **(In US$ thousands)** | **2007** | **2006** | **Growth** |
| Spine | $ 31,693 | $ 29,216 | 8% |

| | | | | |
|---|---|---|---|---|
| Orthopedics | | 10,278 | 8,736 | 18% |
| Total | $ | 41,971 | $ 37,952 | 11% |

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Net sales in Blackstone were $29.4 million in the third quarter of 2007, which represented 24% of total net sales for the third quarter of 2007. There are no sales for Blackstone for the comparable period of the prior year. All of Blackstone's sales are recorded in our Spine market sector. On a pro forma basis Blackstone sales increased 41% when compared to the third quarter of 2006 and would have represented 20% of pro forma total net sales in third quarter 2006.

Net sales in Breg increased $2.5 million to $21.2 million for the third quarter of 2007 compared to $18.7 million for the third quarter of 2006, an increase of 14%. The increase in sales was primarily due to sales of Breg bracing products which increased 18% from the third quarter of 2006. Our Fusion XT™ products contributed to this increase. Sales of cold therapy products increased 15% compared to third quarter of 2006. These increases were partially offset by a 5% decrease in sales for pain therapy products. All of Breg's sales are recorded in our Sports Medicine market sector.

Net sales in International increased 7% to $28.5 million in the third quarter of 2007 compared to $26.7 million in the third quarter of 2006. International net sales represented 24% and 32% of our total net sales in the third quarter of 2007 and the third quarter of 2006, respectively. The impact of foreign currency increased International sales by 6% or $1.5 million, during the third quarter of 2007 as compared to the third quarter of 2006. International sales in the third quarter of 2007 were also positively impacted by a 9% increase in Orthopedic products due to increased sales of our internal fixation products, including the eight-Plate Guided Growth System®, as well as increased sales of Physio-Stim® and other products used in orthopedic applications. Sales of Breg products within International, included in the Sports Medicine market sector, increased $0.1 million or 18% when compared to third quarter 2006. International sales in the Vascular market sector, which consist of the A-V Impulse product, decreased $0.4 million or 7%. Sales of our Other products increased $0.6 million or 10% when compared to third quarter 2006. These increases were slightly offset by sales of external fixation products which decreased 14% compared to the prior period.

**International Sales by Market Sector:**

| | Net Sales for the Three Months Ended September 30, | | |
|---|---|---|---|
| **(In US$ thousands)** | **2007** | **2006** | **Growth** |
| Spine | $ 168 | $ 66 | 155% |
| Orthopedics | 16,026 | 14,749 | 9% |
| Sports Medicine | 869 | 739 | 18% |
| Vascular | 4,718 | 5,084 | (7)% |
| Other | 6,714 | 6,111 | 10% |
| Total | $ 28,495 | $ 26,749 | 7% |

*Sales by Market Sector:*

Sales of Spine products increased 109% to $61.3 million in the third quarter of 2007 compared to $29.3 million in the third quarter of 2006. The increase is primarily due to the addition of Blackstone product sales and sales growth of spinal stimulation products in the United States. The Cervical-Stim® continues to be the only FDA-approved device for the enhancement of fusion in the cervical spine.

Sales of our Orthopedic products increased 12% to $26.3 million in the third quarter of 2007 compared to $23.5 million in the third quarter of 2006. The increase of $2.8 million was attributable to sales of internal fixation devices including the eight-Plate Guided Growth System® which increased 74%, Physio-Stim® which increased 28% and sales of other products used in orthopedic applications which increased 142%. These increases were partially offset by sales of external fixation products which decreased 14% compared to the prior period.

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Sales of our Sports Medicine products increased 14% to $22.1 million in the third quarter of 2007 compared to $19.4 million in the third quarter of 2006. As discussed above, the increase in sales is primarily due to sales of our Breg bracing products and cold therapy, particularly the Fusion™ XT knee brace as well as increased sales of Breg products in International.

Sales of our Vascular products decreased 7% to $4.7 million in the third quarter of 2007 compared to $5.1 million in the third quarter of 2006. The $0.4 million decrease in A-V Impulse sales was due to weaker sales in the US market.

Sales of Other products grew 10% to $6.7 million in the third quarter of 2007 compared to $6.1 million in the third quarter of 2006. The increase was primarily due to an increase in sales of distributed products and airway management products.

*Gross Profit* - Our gross profit increased 45% to $90.4 million in the third quarter of 2007, from $62.4 million in the third quarter of 2006. The increase was primarily due to the increase of 45% in net sales. Gross profit as a percent of net sales in the third quarter 2007 was 74.6% compared to 74.8% in the third quarter of 2006. During the third quarter, we experienced negative impacts from the amortization of the step-up in inventory associated with the Blackstone acquisition and from negative foreign currency impacts which were slightly offset by a reversal of a previously recorded accrual made in connection with one of our distributors. Excluding the favorable benefit to gross margins in the third quarter of 2007, gross margins would have been 73.9%. The step-up in the Blackstone inventory from purchase accounting is now fully amortized.

*Sales and Marketing Expenses* - Sales and marketing expenses, which includes commissions, royalties and bad debt provision, generally increase and decrease in relation to sales. Sales and marketing expense increased $10.8 million to $47.1 million in the third quarter of 2007 compared to $36.3 million in the third quarter of 2006. As a percent of sales, sales and marketing expenses were 38.8% in the third quarter of 2007 compared to 43.5% for the prior year. Sales and marketing expense in the third quarter of 2006 included the impact of approximately $4.7 million of monthly fees associated with the termination of the Medtronic Sofamor Danek ("Danek") marketing agreement. Excluding these fees, the sales and marketing as a percent of sales in the third quarter of 2006 was 37.9%. The year-over-year increase in sales and marketing as a percent of sales, excluding the impact of the termination of the Danek agreement is primarily attributable to the inclusion of Blackstone sales and marketing expense.

*General and Administrative Expense*– General and administrative expense increased $5.2 million in the third quarter of 2007 to $16.9 million compared to $11.7 million in the third quarter of 2006. The increase was primarily attributable to the inclusion of Blackstone general and administrative expense of $4.1 million for which there was no comparable cost in the third quarter of 2006. General and administrative expense as a percent of sales slightly decreased to 14.0% for the third quarter 2007 compared to 14.1% in the prior year.

*Research and Development Expense* - Research and development expense decreased $36.9 million in the third quarter of 2007 to $6.0 million compared to $42.9 million in the third quarter of 2006. Research and development expense in the third quarter of 2006 included a charge of $40.0 million related to the write-off of in-process research and development resulting from the Blackstone acquisition. Approximately $3.2 million is related to Blackstone, for which there was no comparable cost in the prior year.

*Amortization of Intangible Assets*– Amortization of intangible assets increased $2.8 million in the third quarter of 2007 to $4.7 million compared to $1.9 million in the third quarter of 2006. Amortization expense included $2.8 million related to amortization of intangible assets acquired in the Blackstone acquisition.

*Interest Income (Expense), net* – Interest expense, net was $5.7 million in the third quarter of 2007 compared to $0.5 million in the third quarter of 2006. Interest expense for the third quarter of 2007 included interest expense of $5.6

million related to the senior secured term loan used to finance the Blackstone acquisition.

*Other Income (Expense), net* – Other income, net was $0.5 million for the third quarter of 2007 compared to other expense of $0.5 million in the third quarter 2006. The other income in the third quarter of 2007 was due to foreign exchange gains resulting from the weakening during the quarter of the U.S. Dollar as contrasted to the opposite effect in the third quarter 2006.



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*Income Tax Expense*– Our estimated worldwide effective tax rate was 24.6% and 12.6% during the third quarter of 2007 and 2006, respectively. The effective tax rates for the third quarter of 2007 included a tax credit for research and development expense relating to 2003. Without this discrete item our estimated worldwide effective tax rate for the third quarter of 2007 was 26.7% due to the positive effects of our European restructuring, research and development tax credits, tax planning associated with the acquisition of Breg, and an increase in the domestic production deduction, which were partially offset by non-deductible foreign losses and the generation of unutilizable net operating losses in various jurisdictions which negatively affected our tax rate. The effective tax rate for the third quarter 2006 reflects the non-deductibility, for tax purposes, of the $40.0 million purchased in-process research and development charge associated with the Blackstone acquisition. Excluding the charge for in-process research and development, our effective tax rate was 46% due to negative effects of our European restructuring, tax adjustments in foreign jurisdictions and a higher percentage of income being earned in the United States, a higher tax jurisdiction.

*Net Income (Loss)*– Net income for the third quarter of 2007 was $8.0 million, or $0.48 per basic share and $0.48 per diluted share, compared to net loss of $35.4 million, or $2.19 per basic share and $2.19 per diluted share, for the third quarter of 2006. The weighted average number of basic common shares outstanding was 16,639,019 and 16,193,086 during the third quarter of 2007 and 2006, respectively. The weighted average number of diluted common shares outstanding was 16,889,303 and 16,193,086 during the third quarter of 2007 and 2006, respectively.

**Nine Months Ended September 30, 2007 Compared to Nine Months Ended September 30, 2006**

Net sales increased 45% to $361.5 million for the first nine months of 2007 compared to $249.2 million for the first nine months of 2006. The impact of foreign currency increased sales by $5.5 million during the first nine months of 2007 as compared to the first nine months of 2006.

*Sales by Business Segment:*

Net sales in Domestic increased to $122.7 million in the first nine months of 2007 compared to $113.2 million in the first nine months of 2006, an increase of 8%. Domestic represented 34% of total net sales during the first nine months of 2007 and 46% of total net sales for the first nine months of 2006. The increase in Domestic sales was partially the result of a 7% increase in sales in the Spine market sector. This increase continues to be driven by the only FDA-approved stimulator for the cervical spine, the Cervical-Stim®. The Orthopedic market sector sales increased 13% due to sales of internal fixation products and a 17% increase in sales of the Physio-Stim® compared to the first nine months of 2006. These increases were partially offset by a 9% decrease in sales of external fixation products when compared to the first nine months of 2006.

**Domestic Sales by Market Sector:**

| | **Net Sales for the Nine Months Ended September 30,** | | |
|---|---|---|---|
| **(In US$ thousands)** | **2007** | **2006** | **Growth** |
| Spine | $ 92,650 | $ 86,595 | 7% |
| Orthopedics | 30,068 | 26,590 | 13% |
| Total | $ 122,718 | $ 113,185 | 8% |

Net sales in Blackstone were $85.9 million in the first nine months of 2007, which represented 24% of total net sales for the first nine months of 2007. There are no sales for Blackstone for the comparable period of the prior year. All of Blackstone's sales are recorded in our Spine market sector. On a pro forma basis Blackstone sales increased 40% when compared to the first nine months of 2006 and would have represented 20% of pro forma total net sales in first nine months 2006.

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Net sales in Breg increased $5.6 million to $61.5 million for the first nine months of 2007 compared to $55.9 million for the first nine months of 2006, an increase of 10%. The increase in sales was primarily due to sales of Breg bracing products which increased 12% from the first nine months of 2006. Our Fusion XT™ products contributed to this increase. Sales of cold therapy products increased 13% compared to the first nine months of 2006. These increases were partially offset by a 11% decrease in sales for pain therapy products. All of Breg's sales are recorded in our Sports Medicine market sector.

Net sales in International increased 14% to $91.4 million in the first nine months of 2007 compared to $80.1 million in the first nine months of 2006. International net sales represented 25% and 32% of our total net sales in the first nine months of 2007 and the first nine months of 2006, respectively. The impact of foreign currency increased International sales by 6%, or $5.3 million, during the first nine months of 2007 as compared to the first nine months of 2006. Sales in the first nine months of 2007 were also positively affected by a $1.9 million sale to a distributor in Latin America. International sales in the first nine months of 2007 were also positively impacted by a 16% increase in sales of Orthopedic products due to increased sales of our internal fixation products, including the eight-Plate Guided Growth System®, as well as increased sales of Physio-Stim® and other products used in orthopedic applications. Sales of Breg products internationally which are included in the Sports Medicine market sector, increased $1.0 million or 50% when compared to the first nine months of 2006. International sales in the Vascular market sector, which consist of the A-V Impulse product, decreased $0.2 million. Sales of our Other products increased $2.9 million when compared to the first nine months of 2006.

**International Sales by Market Sector:**

| | **Net Sales for the Nine Months Ended September 30,** | | |
|---|---|---|---|
| **(In US$ thousands)** | **2007** | **2006** | **Growth** |
| Spine | $ 421 | $ 186 | 126% |
| Orthopedics | 51,865 | 44,552 | 16% |
| Sports Medicine | 3,033 | 2,018 | 50% |
| Vascular | 15,217 | 15,417 | (1)% |
| Other | 20,853 | 17,960 | 16% |
| Total | $ 91,389 | $ 80,133 | 14% |

*Sales by Market Sector:*

Sales of Spine products increased 106% to $179.0 million in the first nine months of 2007 compared to $86.8 million in the first nine months of 2006. The increase is primarily due to the addition of Blackstone product sales and sales growth of spine stimulation products in the United States. Spine stimulation sales increased 7% compared to the first nine months of 2006. The Cervical-Stim® continues to be the only FDA-approved stimulation device for the enhancement of fusion in the cervical spine.

Sales of our Orthopedic products increased 15% to $81.9 million in the first nine months of 2007 compared to $71.1 million in the first nine months of 2006. The increase of $10.8 million was attributable to sales of internal fixation devices including the eight-Plate Guided Growth System® which increased 95% and sales of other products used in orthopedic applications which increased 108%. These increases were partially offset by sales of external fixation products which decreased 6% compared to the prior period.

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Sales of our Sports Medicine products increased 11% to $64.6 million in the first nine months of 2007 compared to $57.9 million in the first nine months of 2006. As discussed above, the increase in sales is primarily due to sales of our Breg bracing products and cold therapy, particularly the Fusion™ XT knee brace as well as increased sales of Breg products in International.

Sales of our Vascular products decreased 1% to $15.2 million in the first nine months of 2007 compared to $15.4 million in the first nine months of 2006. This decrease was due to a $0.2 million decrease in A-V Impulse sales due to weaker sales in the US market.

Sales of Other products grew 16% to $20.9 million in the first nine months of 2007 compared to $18.0 million in the first nine months of 2006. The increase was primarily due to an increase in sales of distributed products and airway management products.

*Gross Profit* - Our gross profit increased 44% to $266.9 million in the first nine months of 2007, from $185.6 million in the first nine months of 2006. The increase was primarily due to the increase of 45% in net sales. Gross profit as a percent of net sales in the first nine months of 2007 was 73.8% compared to 74.5% in the first nine months of 2006. During the first nine months of 2007, we experienced negative impacts from the amortization of the step-up in inventory associated with the Blackstone acquisition and from negative foreign currency impacts which were slightly offset by a reversal of a previously recorded accrual made in connection with one of our distributors. Excluding the favorable benefit to, gross margins in the first nine months of 2007, gross margins would have been 73.6%. The step-up in the Blackstone inventory from purchase accounting is now fully amortized.

*Sales and Marketing Expenses* - Sales and marketing expenses, which include commissions, royalties and bad debt provision, generally increase and decrease in relation to sales. Sales and marketing expense increased $39.9 million to $138.9 million in the first nine months of 2007 compared to $99.0 million in the first nine months of 2006. As a percent of sales, sales and marketing expenses were 38.4% in the first nine months of 2007 compared to 39.7% for the prior year. Sales and marketing expense in the first nine months of 2006 included the impact of approximately $4.7 million of monthly fees associated with the termination of a marketing services agreement formerly in place between the Company’s subsidiary Orthofix Inc. and Medtronic Sofamor Danek. Excluding these fees, sales and marketing as a percent of sales for the first nine months of 2006 was 37.8%. The year-over-year increase in sales and marketing as a percent of sales, excluding the impact of the termination of the Danek agreement is primarily attributable to the inclusion of Blackstone sales and marketing expense.

*General and Administrative Expense*– General and administrative expense increased $13.3 million in the first nine months of 2007 to $49.6 million compared to $36.3 million in the first nine months of 2006. The increase is primarily attributable to the inclusion of Blackstone general and administrative expense of $11.5 million for which there was no comparable cost in the first nine months of 2006. General and administrative expense as a percent of sales decreased to 13.7% for the third quarter 2007 compared to 14.6% in the prior year reflecting leverage obtained from spreading general and administrative costs over a larger revenue base after the Blackstone acquisition.

*Research and Development Expense* - Research and development expense decreased $30.3 million in the first nine months of 2007 to $18.3 million compared to $48.6 million in the first nine months of 2006. Research and development expense in the first nine months of 2006 included a charge of $40.0 million related to the write-off of in-process research and development resulting from the Blackstone acquisition. Approximately $9.4 million is related to Blackstone, for which there was no comparable cost in the prior year.

*Amortization of Intangible Assets*– Amortization of intangible assets increased $8.3 million in the first nine months of 2007 to $13.7 million compared to $5.4 million in the first nine months of 2006. Amortization expense included $8.3 million related to amortization of intangible assets acquired in the Blackstone acquisition.

*KCI Settlement, Net of Litigation Costs*– The gain, net of litigation costs, on the settlement of the KCI litigation in the first nine months of 2006 was $1.1 million for which there was no comparable gain in the first nine months of 2007.

*Interest Income (Expense), net* – Interest expense, net was $17.2 million in the first nine months of 2007 compared to $0.2 million of interest income in the first nine months of 2006.  Interest expense for the first nine months of 2007 included interest expense of $16.8 million related to the senior secured term loan used to finance the Blackstone acquisition.

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*Other Income (Expense), net* – Other income, net was $0.3 million for the first nine months of 2007 compared to other expense of $0.8 million in the first nine months of 2006. The other income in the first nine months of 2007 was due to foreign exchange gains resulting from the weakening during the first nine months of the U.S. Dollar as contrasted to the opposite effect in the first nine months of 2006.

*Income Tax Expense*– Our estimated worldwide effective tax rate was 26.9% and (348.3)% during the first nine months of 2007 and 2006, respectively. The effective tax rate for the nine months of 2007 included a tax credit for research and development expense relating to 2003. Without this discrete item our estimated worldwide effective tax rate for the nine months of 2007 was 27.5% due to the positive effects of our European restructuring, research and development tax credits, tax planning associated with the acquisition of Breg, non-deductible foreign losses, and an increase in the domestic production deduction which were partially offset by the generation of unutilizable net operating losses in various jurisdictions. The effective tax rate for the first nine months of 2006 reflects the non-deductibility, for tax purposes, of the $40.0 million purchased in-process research and development charged associated with the Blackstone acquisition. Excluding the charge for in-process research and development, our effective tax rate was 31%. Our effective tax rate in the first nine months of 2006 benefited from a one-time tax benefit of $2.9 million resulting from our election to adopt a new tax provision in Italy. Without this discrete item, our estimated worldwide effective tax rate for the first nine months of 2006 was 38% as result of higher production of pre-tax income being earned in the United States, a higher tax jurisdiction.

*Net Income (Loss)* – Net income for the first nine months of 2007 was $21.5 million, or $1.30 per basic share and $1.27 per diluted share, compared to net loss of $14.4 million, or $0.90 per basic share and $0.90 per diluted share, for the first nine months of 2006. The weighted average number of basic common shares outstanding was 16,546,385 and 16,084,388 during the first nine months of 2007 and 2006, respectively. The weighted average number of diluted common shares outstanding was 16,925,084 and 16,084,388 during the first nine months of 2007 and 2006, respectively.

**Liquidity and Capital Resources**

Cash and cash equivalents at September 30, 2007 were $23.6 million. This compares to $25.9 million at December 31, 2006. In addition, we had $11.6 million of restricted cash at September 30, 2007 available for use in our U.S. operations as compared to $7.3 million at December 31, 2006.

Net cash provided by operating activities was $13.8 million for the first nine months of 2007 compared to net cash used in operating activities of $9.0 million in the first nine months of 2006. Net cash provided by (used in) operating activities is comprised of net income (loss), non-cash items (including stock-based compensation) and changes in working capital. Net income increased $35.9 million to $21.5 million in the first nine months of 2007 from a net loss of $14.4 million in the comparable 2006 period. Non-cash items decreased $22.6 million in the first nine months of 2007 compared to the same period in 2006 primarily as a result of the non-cash effect of increased depreciation and amortization related to the Blackstone acquisition and lower deferred tax assets which were offset by decreased in-process research and development costs due the write off of in-process research and development costs associated with the Blackstone acquisition. Working capital accounts consumed $38.6 million of cash in the first nine months of 2007 compared to $48.0 million in the same period in 2006. The principal uses of cash for working capital were attributable to increases in accounts receivable and inventory to support additional sales and certain operational initiatives which were partially offset by an increase in other current liabilities. Overall performance indicators for our two primary working capital accounts, accounts receivable and inventory, reflect days sales in receivables of 90 days at September 30, 2007 compared to 95 days at September 30, 2006 and inventory turns of 1.4 times at September 30, 2007 compared to 2.0 times at September 30, 2006. The lower inventory turns and resultant higher inventory reflect inventory investment to support Blackstone sales, to open an international distribution center and support for new internal fixation products.

Net cash used in investing activities was $25.9 million during the first nine months of 2007 compared to $343.6 million during the first nine months of 2006. During the first nine months of 2007, we invested $23.8 million in capital expenditures of which $6.2 million were related to the investment in instrumentation and the acquisition of InSWing™ interspinous process spacer patents at Blackstone. In the first nine months of 2007, we also invested $2.1 million in investment in subsidiaries and affiliates which was a result of adjustments in purchase accounting related to Blackstone and a purchase of a minority interest in our subsidiary in Brazil. On September 22, 2006, we purchased Blackstone for $333.0 million plus various transaction costs. In addition, during the first nine months of 2006, we invested $6.8 million in capital expenditures and we paid $1.1 million to purchase 52% of International Medical Supplies Distribution GmbH, a distributor of Breg products in Germany.

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Net cash provided by financing activities was $9.3 million in the first nine months of 2007 compared to $325.1 million in the first nine months of 2006. In the first nine months of 2007, we repaid approximately $6.5 million of principal of the senior secured term loan and borrowed $7.9 million to support working capital in our Italian subsidiary. In addition, we received net proceeds of $6.8 million from the issuance of 230,894 shares of our common stock upon the exercise of stock options and shares issued pursuant to our employee stock purchase plan. Commencing in June 2007, we offered restricted shares in addition to stock options as a form of stock-based compensation. In the first nine months of 2006, we prepaid the remaining $14.8 million of the principal of the senior secured term loan, which was obtained to help finance the Breg acquisition. On September 22, 2006, we borrowed $330.0 million in the form of a new senior secured credit agreement, which along with cash balances were used to finance the acquisition of Blackstone and pay debt issuance and other costs. In addition, we received net proceeds of $10.7 million from the issuance of 376,376 shares of our common stock upon the exercise of stock options and shares issued pursuant to our employee stock purchase plan and $2.0 million of related tax benefit in the first nine months of 2006.

On September 22, 2006 our wholly-owned U.S. holding company subsidiary, Orthofix Holdings, Inc. ("Orthofix Holdings"), entered into a senior secured credit facility with a syndicate of financial institutions to finance the acquisition of Blackstone. The senior secured credit facility provides for (1) a seven-year amortizing term loan facility of $330.0 million, the proceeds of which, together with cash balances were used for payment of the purchase price of Blackstone; and (2) a six-year revolving credit facility of $45.0 million. As of September 30, 2007 we had no amounts outstanding under the revolving credit facility and $308.7 million outstanding under the term loan facility. Obligations under the senior secured credit facility have a floating interest rate of London Inter-Bank Offered Rate ("LIBOR"), or prime rate plus a margin, currently LIBOR plus 1.75%, which is adjusted quarterly based upon the leverage ratio of the Company and its subsidiaries. Our effective interest rate as of September 30, 2007 on our senior secured debt is 6.95%. The Company, certain foreign subsidiaries of the Company, including Colgate Medical Limited (Orthofix Holdings's immediate parent) and certain of Orthofix Holdings's direct and indirect subsidiaries, including Orthofix Inc., Breg and Blackstone, have guaranteed the obligations of Orthofix Holdings under the senior secured credit facility. The obligations of Orthofix Holdings under the senior secured credit facility and the guarantors under their guarantees are secured by the pledge of their respective assets located in the United States.

At September 30, 2007, we had outstanding borrowings of $8.4 million and unused available lines of credit of approximately 0.3 million Euro ($0.2 million) under a line of credit established in Italy to finance the working capital of our Italian operations. The terms of the line of credit give us the option to borrow amounts in Italy at rates determined at the time of borrowing.

We will continue to search for viable acquisition candidates that would expand our global presence as well as add additional products appropriate for current distribution channels. An acquisition of another company or product line by us could result in our incurrence of additional debt and contingent liabilities.

We believe that current cash balances together with projected cash flows from operating activities, the available revolving credit facility, the exercise of stock options, and our debt capacity are sufficient to cover anticipated working capital and capital expenditure needs including research and development costs over the near term.

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**Item 3. Quantitative and Qualitative Disclosures About Market Risk**

We are exposed to certain market risks as part of our ongoing business operations. Primary exposures include changes in interest rates and foreign currency fluctuations. These exposures can vary sales, cost of sales, costs of operations, and the cost of financing and yields on cash and short-term investments. We use derivative financial instruments, where appropriate, to manage these risks. However, our risk management policy does not allow us to hedge positions we do not hold nor do we enter into derivative or other financial investments for trading or speculative purposes. As of September 30, 2007, we had a currency swap in place to minimize foreign currency exchange risk related to a 46.2 million Euro intercompany note foreign currency exposure.

We are exposed to interest rate risk in connection with our senior secured term loan and borrowings under our revolving credit facility, which bear interest at floating rates based on LIBOR or the prime rate plus an applicable borrowing margin. Therefore, interest rate changes generally do not affect the fair market value of the debt, but do impact future earnings and cash flows, assuming other factors are held constant.

As of September 30, 2007, Orthofix Holdings had $308.7 million of variable rate term debt represented by borrowings under its senior secured term loan at a floating interest rate of LIBOR or prime rate plus a margin, currently LIBOR plus 1.75%, which is adjusted quarterly based upon the leverage ratio of the Company and its subsidiaries. The effective interest rate as of September 30, 2007 on the senior secured debt is 6.95%. Based on the balance outstanding under the credit facility as of December 31, 2006 an immediate change of one percentage point in the applicable interest rate on the variable rate debt would cause an increase or decrease in interest expense of approximately $3.1 million on an annual basis.

Our foreign currency exposure results from fluctuating currency exchange rates, primarily the U.S. Dollar against the Euro, Great Britain Pound, Mexican Peso and Brazilian Real. We face cost of goods currency exposure when we produce products in foreign currencies such as the Euro or Great Britain Pound and sell those products in U.S. Dollars. We face transactional currency exposures when foreign subsidiaries (or the Company itself) enter into transactions, generally on an intercompany basis, denominated in currencies other than their functional currency. As of September 30, 2007, we had an uncovered intercompany receivable denominated in Euro for approximately 6.4 million. We are currently evaluating our options to limit the foreign currency exposure on this receivable.

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**Item 4. Controls and Procedures**

*Disclosure Controls and Procedures*

Under the supervision and with the participation of our management, including our Chief Executive Officer and our Chief Financial Officer, we performed an evaluation of the effectiveness of the design and operation of our disclosure controls and procedures (as defined in Exchange Act Rule 13a - 15(e) or 15d – 15 (e)) as of the end of the period covered by this report. Based upon that evaluation, our Chief Executive Officer and Chief Financial Officer concluded that, as of the end of the period covered by this report, our disclosure controls and procedures were effective.

*Changes in Internal Control over Financial Reporting*

In July 2007, we implemented an Enterprise Resource Planning ("ERP") system at Blackstone, a wholly-owned subsidiary which we acquired on September 22, 2006. The ERP system, developed by Epicor, is expected to improve and enhance internal controls over financial reporting. This ERP system materially changes how transactions are processed at Blackstone.

As a result of the recent acquisition of Blackstone, we are continuing to integrate the processes, systems and controls relating to the acquired subsidiary into our existing system of internal control over financial reporting.

We identified certain business process and control issues at our Brazilian subsidiary which has September 2007 year to date revenues of approximately $6.5 million and net income of approximately $0.9 million. We have commenced implementing certain internal controls to address the business process and control issues. We expect these certain internal controls to be in place by December 31, 2007. We have implemented certain additional corporate oversight controls during the third quarter to help minimize the risk of the noted control issues.

Except for the processes, systems, and controls relating to the integration of Blackstone and conversion to the ERP system and certain business process and control issues at our Brazilian subsidiary, there have not been any changes in our internal control over financial reporting during the fiscal quarter ended September 30, 2007 that have materially affected or are reasonably likely to materially affect, our internal control over financial reporting.

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**PART II OTHER INFORMATION**

**Item 1. Legal Proceedings**

Effective October 29, 2007, our subsidiary, Blackstone, entered into a settlement agreement with respect to a patent infringement lawsuit captioned Medtronic Sofamor Danek USA Inc., Warsaw Orthopedic, Inc., Medtronic Puerto Rico Operations Co., and Medtronic Sofamor Danek Deggendorf, GmbH v. Blackstone Medical, Inc., Civil Action No. 06-30165-MAP, filed on September 22, 2006 in the United States District Court for the District of Massachusetts. In that lawsuit, the plaintiffs had alleged that (i) they were the exclusive licensees of United States Patent Nos. 6,926,718 B1, 6,936,050 B2, 6,936,051 B2, 6,398,783 B1 and 7,066,961 B2 (the “Patents”), and (ii) Blackstone's making, selling, offering for sale, and using within the United States of its Blackstone Anterior Cervical Plate, 3º Anterior Cervical Plate, Hallmark Anterior Cervical Plate and Construx Mini PEEK VBR System products infringed the Patents, and that such infringement was willful. The Complaint requested both damages and an injunction against further alleged infringement of the Patents. The Complaint did not specifically state an amount of damages. Blackstone denied infringement and asserted that the Patents were invalid. On July 20, 2007, we submitted a claim for indemnification from the escrow fund established in connection with the agreement and plan of merger between us, New Era Medical Corp. and Blackstone, dated as of August 4, 2006 (the “Merger Agreement”), for any losses to us or Blackstone resulting from this matter. We were subsequently notified by legal counsel for the former shareholders that the representative of the former shareholders of Blackstone has objected to the indemnification claim and intends to contest it in accordance with the terms of the Merger Agreement. We are unable to predict the outcome of the escrow claim or to estimate the amount, if any, that may ultimately be returned to us from the escrow fund. The settlement agreement is not expected to have a material impact on our consolidated financial position, results of operations or cash flows.

On or about July 23, 2007, Blackstone received a subpoena issued by the Department of Health and Human Services, Office of Inspector General, under the authority of the federal healthcare anti-kickback and false claims statutes. The subpoena seeks documents for the period January 1, 2000 through July 31, 2006 which is prior to Blackstone’s acquisition by us. We believe that the subpoena concerns the compensation of physician consultants and related matters. Blackstone is cooperating with the government’s request and is in the process of responding to the subpoena. We are unable to predict what action, if any, might be taken in the future by the Department of Health and Human Services, Office of Inspector General or other governmental authorities as a result of this investigation or what impact, if any, the outcome of this matter might have on its consolidated financial position, results of operations, or cash flows. On September 17, 2007, we submitted a claim for indemnification from the escrow fund established in connection with the Merger Agreement for any losses to us or Blackstone resulting from this matter. We were subsequently notified by legal counsel for the former shareholders that the representative of the former shareholders of Blackstone has objected to the indemnification claim and intends to contest it in accordance with the terms of the Merger Agreement. We are unable to predict the outcome of the escrow claim or to estimate the amount, if any, that may ultimately be returned to us from the escrow fund.

On or about September 27, 2007, Blackstone received a federal grand jury subpoena issued by the United States’ Attorney’s Office for the District of Nevada (“USAO-Nevada”). The subpoena seeks documents for the period from January 1999 to the present. We believe that the subpoena concerns payments or gifts made by Blackstone to certain physicians. Blackstone is cooperating with the government’s request and is in the process of responding to the subpoena. We are unable to predict what action, if any, might be taken in the future by the USAO-Nevada or other governmental authorities as a result of this investigation or what impact, if any, the outcome of this matter might have on its consolidated financial position, results of operations, or cash flows. It is our intention to submit a claim for indemnification from the escrow fund established in connection with the Merger Agreement for any losses to us or Blackstone resulting from this matter.

By order entered on January 4, 2007, the United States District Court for the Eastern District of Arkansas unsealed a qui tam complaint captioned Thomas v. Chan, et al., 4:06-cv-00465-JLH, filed against Dr. Chan, Blackstone and other defendants including another device manufacturer. A qui tam action is a civil lawsuit brought by an individual for an alleged violation of a federal statute, in which the U.S. Department of Justice has the right to intervene and take over the prosecution of the lawsuit at its option. The complaint alleges causes of action under the False Claims Act for alleged inappropriate payments and other items of value conferred on Dr. Chan. On December 29, 2006, the U.S. Department of Justice filed a notice of non-intervention in the case. Plaintiff subsequently amended the complaint to add the Company as a defendant. We believe Blackstone and the Company have meritorious defenses to the claims alleged and we intend to defend vigorously against this lawsuit. On September 17, 2007, we submitted a claim for indemnification from the escrow fund established in connection with the Merger Agreement for any losses to the us or Blackstone resulting from this matter. We were subsequently notified by legal counsel for the former shareholders that the representative of the former shareholders of Blackstone has objected to the indemnification claim and intends to contest it in accordance with the terms of the Merger Agreement. We are unable to predict the outcome of the escrow claim or to estimate the amount, if any, that may ultimately be returned to us from the escrow fund.

Between January 2007 and May 2007, Orthofix, Inc. and/or Blackstone were named defendants, along with other medical device manufacturers, in three civil lawsuits alleging that Dr. Chan had performed unnecessary surgeries in three different instances. All three civil lawsuits have recently been served and are pending in the Circuit Court of White County, Arkansas. We believe Blackstone and Orthofix, Inc. have meritorious defenses to the claims alleged and we intend to defend vigorously against these lawsuits. On September 17, 2007, we submitted a claim for indemnification from the escrow fund established in connection with the Merger Agreement for any losses to us or Blackstone resulting from one of these three civil lawsuits. We were subsequently notified by legal counsel for the former shareholders that the representative of the former shareholders of Blackstone has objected to the indemnification claim and intends to contest it in accordance with the terms of the Merger Agreement. We are unable to predict the outcome of the escrow claim or to estimate the amount, if any, that may ultimately be returned to us from the escrow fund.

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In addition to the foregoing, we have submitted claims for indemnification from the escrow fund established in connection with the Merger Agreement for losses that have or may result from certain claims against Blackstone alleging that plaintiffs and/or claimants were entitled to payments for Blackstone stock options not reflected in Blackstone's corporate ledger at the time of Blackstone's acquisition by us.  To date, the representative of the former shareholders of Blackstone and the Company has not objected to approximately $1.5 million in claims from the escrow fund, with certain claims remaining pending.

We cannot predict the outcome of any proceedings or claims made against us or our subsidiaries and there can be no assurance that the ultimate resolution of any claim will not have a material adverse impact on our consolidated financial position, results of operations, or cash flows.

In addition to the foregoing, in the normal course of our business, we are involved in various lawsuits from time to time and may be subject to certain other contingencies.

## Item 1A.  Risk Factors

There have been no material changes to our risk factors from the factors discussed in Part I, “Item 1A. Risk Factors” in our Annual Report on Form 10-K for the fiscal year ended December 31, 2006.

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**Item 6. Exhibits**

**(a) Exhibits**

| Exhibit Number | Description |
| --- | --- |
| 3.1 | Certificate of Incorporation of the Company (filed as an exhibit to the Company's annual report on Form 20-F dated June 29, 2001 and incorporated herein by reference). |
| 3.2 | Articles of Association of the Company as amended (filed as an exhibit to the Company's quarterly report on Form 10-Q for the quarter ended June 30, 2007 and incorporated herein by reference). |
| 10.1 | Orthofix Inc. Employee Stock Purchase Plan (filed as an exhibit to the Company's annual report on Form 10-K for the fiscal year ended December 31, 2002 and incorporated herein by reference). |
| 10.2 | Orthofix International N.V. Staff Share Option Plan (filed as an exhibit to the Company's annual report on Form 10-K for the fiscal year ended December 31, 2002 and incorporated herein by reference). |
| 10.3 | Form of Performance Accelerated Stock Option under the Staff Share Option Plan (filed as an exhibit to the Company's annual report on Form 10-K for the fiscal year ended December 31, 2002 and incorporated herein by reference). |
| 10.4 | Form of Performance Accelerated Stock Option Inducement Agreement (filed as an exhibit to the Company's annual report on Form 10-K for the fiscal year ended December 31, 2003 and incorporated here in by reference). |
| 10.5 | Orthofix International N.V. 2004 Long Term Incentive Plan, as amended and restated (filed as an exhibit to the Company's current report on Form 8-K filed June 26, 2007 and incorporated herein by reference). |
| 10.6 | Form of Nonqualified Stock Option Agreement Under the Orthofix International N.V. 2004 Long Term Incentive Plan (filed as an exhibit to the Company's current report on Form S-8 filed August 23, 2007 and incorporated herein by reference). |
| 10.7 | Form of Restricted Stock Grant Agreement under the Orthofix International N.V. Amended and Restated 2004 Long-Term Incentive Plan (filed as an exhibit to the Company's quarterly report on Form 10-Q for the quarter ended June 30, 2007 and incorporated herein by reference). |
| 10.8 | Orthofix Deferred Compensation Plan (filed as an exhibit to the Company's annual report on Form 10-K for the fiscal year ended December 31, 2006, as amended, and incorporated herein by reference). |
| 10.9 | Employment Agreement, dated as of April 15, 2005, between the Company and Charles W. Federico (filed as an exhibit to the Company's current report on Form 8-K filed April 18, 2005 and incorporated herein by reference). |
| 10.10 | Employment Agreement, dated as of July 13, 2006, between the Company and Thomas Hein (filed as an exhibit to the Company's annual report on Form 8-K filed July 18, 2006 and incorporated herein by reference). |
| 10.11 | Employment Agreement, dated as of November 20, 2003, between Orthofix International N.V. and Bradley R. Mason (filed as an exhibit to the Company's annual report on Form 10-K for the fiscal year ended December 31, 2003 and incorporated herein by reference). |

10.12 Acquisition Agreement dated as of November 20, 2003, among Orthofix International N.V., Trevor Acquisition, Inc., Breg, Inc. and Bradley R. Mason, as shareholders' representative (filed as an exhibit to the Company's current report on Form 8-K filed January 8, 2004 and incorporated herein by reference).

10.13 Amended and Restated Voting and Subscription Agreement dated as of December 22, 2003, among Orthofix International N.V. and the significant shareholders of Breg, Inc. identified on the signature pages thereto (filed as an exhibit to the Company's current report on Form 8-K filed on January 8, 2004 and incorporated herein by reference).

10.14 Employment Agreement amendment, dated December 29, 2005 between Orthofix International N.V. and Charles W. Federico (filed as an exhibit to the Company's current report on Form 8-K filed December 30, 2005 and incorporated herein by reference).

10.15 Form of Indemnity Agreement (filed as an exhibit to the Company's annual report on Form 10-K filed December 31, 2005 and incorporated herein by reference).

10.16 Settlement Agreement dated February 23, 2006, between Intavent Orthfix Limited, a wholly-owed subsidiary of Orthofix International N.V. and Galvin Mould (filed as an exhibit to the Company's annual report on Form 8-K filed on April 17, 2006 and incorporated herein by reference).

10.17 Employment Agreement, dated July 13, 2006, between Orthofix Inc. and Alan W. Milinazzo (filed as an exhibit to the Company's current report on Form 8-K filed July 18, 2006 and incorporated herein by reference).

10.18 Employment Agreement, dated July 13, 2006, between Orthofix Inc. and Raymond C. Kolls (filed as an exhibit to the Company's current report on Form 8-K filed July 18, 2006 and incorporated herein by reference).

10.19 Employment Agreement, dated July 13, 2006, between Orthofix Inc. and Michael M. Finegan (filed as an exhibit to the Company's current report on Form 8-K filed July 18, 2006 and incorporated herein by reference).

10.20 Credit Agreement, dated as of September 22, 2006, among Orthofix Holdings, Inc., Orthofix International N.V., certain domestic subsidiaries of Orthofix International N.V., Colgate Medical Limited, Victory Medical Limited, Swiftsure Medical Limited, Orthofix UK Ltd, the several banks and other financial institutions as may from time to time become parties thereunder, and Wachovia Bank, National Association (filed as an exhibit to the Company's current report on Form 8-K filed September 27, 2006 and incorporated herein by reference).

10.21 Agreement and Plan of Merger, dated as of August 4, 2006, among Orthofix International N.V., Orthofix Holdings, Inc., New Era Medical Limited, Blackstone Medical, Inc. and William G. Lyons, III, as Equityholders' Representative (filed as an exhibit to the Company's current report on Form 8-K filed August 7, 2006 and incorporated herein by reference).

10.22 Employment Agreement, dated as of September 22, 2006, between Blackstone Medical, Inc. and Matthew V. Lyons (filed as an exhibit to the Company's annual report on Form 10-K for the fiscal year ended December 31, 2006, as amended, and incorporated herein by reference).

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10.23 Description of Orthofix International N.V.'s Annual Incentive Plan including the Form of Participation Letter (filed as an exhibit to the Company's annual report on Form 10-K for the fiscal year ended December 31, 2006, as amended, and incorporated herein by reference).

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|---|---|
| 31.1* | Rule 13a-14(a)/15d-14(a) Certification of Chief Executive Officer. |
| 31.2* | Rule 13a-14(a)/15d-14(a) Certification of Chief Financial Officer. |
| 32.1* | Section 1350 Certification of Chief Executive Officer. |
| 32.2* | Section 1350 Certification of Chief Financial Officer. |

* Filed herewith.

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**SIGNATURES**

Pursuant to the requirements of the Securities Exchange Act of 1934, the Registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

ORTHOFIX INTERNATIONAL N.V.

| | | |
|---|---|---|
| Date: November 7, 2007 | By: | /s/ Alan W. Milinazzo<br>Name: Alan W. Milinazzo<br>Title: Chief Executive Officer and President |
| Date: November 7, 2007 | By: | /s/ Thomas Hein<br>Name: Thomas Hein<br>Title: Chief Financial Officer |