BIOMET INC
Form 10-Q
October 15, 2010
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UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

(Mark One)

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

For the quarterly period ended August 31, 2010.

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 001-15601

BIOMET, INC.

(Exact name of registrant as specified in its charter)

Indiana	**35-1418342**
(State or other jurisdiction of	***(I.R.S. Employer***
incorporation or organization)	***Identification No.)***
56 East Bell Drive, Warsaw, Indiana	**46582**
(Address of principal executive offices)	***(Zip Code)***

(574) 267-6639

(Registrant s telephone number, including area code)

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

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

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

Large accelerated filer	¨	Accelerated filer	¨
Non-accelerated filer	þ (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 þ

As of August 31, 2010, there was no established public trading market for any of the common stock of the registrant. As of August 31, 2010, there were 1,000 shares of common stock of the registrant outstanding, 100.0% of which were owned by LVB Acquisition, Inc.

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PART I. FINANCIAL INFORMATION

Item 1. Financial Statements.
Biomet, Inc. and Subsidiaries Condensed Consolidated Balance Sheets.

(in millions)

	(Unaudited) August 31, 2010	May 31, 2010
Assets		
Current assets:		
Cash and cash equivalents	$ 274.0	$ 189.1
Accounts receivable, net	429.0	452.5
Income tax receivable	14.4	19.2
Inventories	534.9	507.3
Deferred income taxes	57.4	64.3
Prepaid expenses and other	86.8	72.6
Total current assets	1,396.5	1,305.0
Property, plant and equipment, net	626.2	622.0
Investments	19.3	23.3
Intangible assets, net	5,169.0	5,190.3
Goodwill	4,755.6	4,707.5
Other assets	114.1	120.9
Total assets	$ 12,080.7	$ 11,969.0
Liabilities & Shareholder s Equity		
Current liabilities:		
Current portion long-term debt	$ 36.0	$ 35.6
Accounts payable	87.6	86.3
Accrued interest	137.9	70.2
Accrued wages and commissions	81.1	111.3
Other accrued expenses	221.6	215.1
Total current liabilities	564.2	518.5
Long-term liabilities:		
Long-term debt, net of current portion	5,887.8	5,860.9
Deferred income taxes	1,636.8	1,674.9
Other long-term liabilities	202.8	181.2
Total liabilities	8,291.6	8,235.5
Shareholder s equity:		
Contributed and additional paid-in capital	5,610.0	5,605.1
Accumulated deficit	(1,778.8)	(1,761.0)
Accumulated other comprehensive loss	(42.1)	(110.6)
Total shareholder s equity	3,789.1	3,733.5
Total liabilities and shareholder s equity	$ 12,080.7	$ 11,969.0

The accompanying notes are a part of the condensed consolidated financial statements.

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Biomet, Inc. and Subsidiaries Condensed Consolidated Statements of Operations.

(in millions)

	(Unaudited) Three Months Ended August 31,	
	2010	2009
Net sales	$ 640.7	$ 630.1
Cost of sales	194.0	185.3
Gross profit	446.7	444.8
Selling, general and administrative expense	251.9	246.0
Research and development expense	29.9	24.9
Amortization	95.2	94.8
Operating income	69.7	79.1
Interest expense	126.8	131.5
Other (income) expense	(1.8)	(4.3)
Other (income) expense, net	125.0	127.2
Loss before income taxes	(55.3)	(48.1)
Benefit from income taxes	(37.5)	(25.3)
Net loss	$ (17.8)	$ (22.8)

The accompanying notes are a part of the condensed consolidated financial statements.

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Biomet, Inc. and Subsidiaries Condensed Consolidated Statements of Cash Flows.

(in millions)

	(Unaudited) Three Months Ended August 31, 2010	2009
Cash flows provided by operating activities:		
Net loss	$ (17.8)	$ (22.8)
Adjustments to reconcile net loss to net cash from operating activities:		
Depreciation and amortization	136.7	136.6
Amortization of deferred financing costs	2.8	2.8
Stock-based compensation expense	5.1	5.2
Recovery of doubtful accounts receivable	(1.3)	(5.2)
Gain on investments, net		(0.8)
Property, plant and equipment impairment charge	0.6	
Provision for inventory obsolescence	1.7	6.5
Deferred income taxes	(43.8)	(47.1)
Other	(0.1)	(1.1)
Changes in operating assets and liabilities:		
Accounts receivable	27.1	19.8
Inventories	(18.3)	(22.5)
Prepaid expenses	(12.2)	(4.4)
Accounts payable	(0.6)	(3.0)
Income tax receivable	4.3	14.6
Accrued interest	67.7	70.0
Accrued expenses and other	(20.6)	(93.1)
Net cash provided by operating activities	131.3	55.5
Cash flows used in investing activities:		
Proceeds from sales/maturities of investments	3.8	
Net proceeds from sale of property and equipment		1.6
Capital expenditures	(36.5)	(53.9)
Acquisitions, net of cash acquired	(9.6)	(2.4)
Net cash used in investing activities	(42.3)	(54.7)
Cash flows provided by (used in) financing activities:		
Debt:		
Proceeds under revolving credit agreements	0.1	20.1
Payments under revolving credit agreements	(0.6)	(1.3)
Payments under senior secured credit facility	(8.5)	(8.9)
Equity:		
Repurchase of LVB Acquisition, Inc. shares	(0.2)	(0.6)
Net cash provided by (used in) financing activities	(9.2)	9.3
Effect of exchange rate changes on cash	5.1	0.7
Increase in cash and cash equivalents	84.9	10.8
Cash and cash equivalents, beginning of period	189.1	215.6
Cash and cash equivalents, end of period	$ 274.0	$ 226.4

Supplemental disclosures of cash flow information:		
Cash paid during the period for:		
Interest	$ 56.3	$ 58.9
Income taxes	$ 6.5	$ 0.8

The accompanying notes are a part of the condensed consolidated financial statements.

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Biomet, Inc. and Subsidiaries Notes to Condensed Consolidated Financial Statements (Unaudited)

Note 1 Basis of Presentation.

The accompanying unaudited condensed consolidated financial statements include the accounts of Biomet, Inc. and its subsidiaries (individually and collectively referred to as Biomet , the Company , we , us , or our). Intercompany accounts and transactions have been eliminated in consolidation.

The unaudited condensed consolidated financial statements have been prepared in accordance with U.S. generally accepted accounting principles (GAAP) for condensed financial information and with instructions to Form 10-Q and Article 10 of Regulation S-X. As a result, they do not include all of the information and footnotes required by U.S. GAAP for complete financial statements. In the opinion of management, all adjustments (consisting of normal recurring accruals) considered necessary for a fair presentation of the financial condition, results of operations and cash flows for the periods presented have been included. Operating results for the period ended August 31, 2010 are not necessarily indicative of the results that may be expected for the fiscal year ending May 31, 2011. For further information, including the Company s significant accounting policies, refer to the audited consolidated financial statements and notes thereto included in the Company s Form 10-K for the fiscal year ended May 31, 2010.

Recent Accounting Pronouncements There are no recently issued accounting pronouncements that the Company has yet to adopt that are expected to have a material effect on the Company s financial position, results of operations or cash flows.

Note 2 Inventories.

Inventories are stated at the lower of cost or market, with cost determined under the first-in, first-out method. The Company reviews inventory on hand and writes down excess and slow-moving inventory based on an assessment of future demand and historical experience. Inventories consisted of the following:

(in millions)	**August 31, 2010**	**May 31, 2010**
Raw materials	$ 83.9	$ 69.1
Work-in-process	47.5	43.6
Finished goods	403.5	394.6
Inventories	$ 534.9	$ 507.3

Note 3 Property, Plant and Equipment.

Property, plant and equipment are carried at cost less accumulated depreciation. Depreciation is computed by the straight-line method over the estimated useful lives of 3 to 30 years. Depreciation on instruments is included within cost of sales. Related maintenance and repairs are expensed as incurred.

Property, plant and equipment consisted of the following:

(in millions)	**August 31, 2010**	**May 31, 2010**
Land and land improvements	$ 46.3	$ 45.7
Buildings and leasehold improvements	127.4	124.1
Machinery and equipment	305.6	283.3
Instruments	454.6	420.6
Construction in progress	23.8	29.4
Total property, plant and equipment	957.7	903.1
Accumulated depreciation	(331.5)	(281.1)

Total property, plant and equipment, net	$	626.2	$	622.0

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Biomet, Inc. and Subsidiaries Notes to Condensed Consolidated Financial Statements (Unaudited) (continued)

Note 4 Investments.

At August 31, 2010, the Company s investment securities were classified as follows:

(in millions)	Amortized Cost	Unrealized Gains	Unrealized Losses	Fair Value
Available-for-sale:				
Debt securities	$ 5.2	$ 2.4	$	$ 7.6
Equity securities	0.5		(0.1)	0.4
Mortgage-backed securities	0.7		(0.2)	0.5
Total available-for-sale	6.4	2.4	(0.3)	8.5
Money market funds	9.5			9.5
Other	1.3			1.3
Total	$ 17.2	$ 2.4	$ (0.3)	$ 19.3

At May 31, 2010, the Company s investment securities were classified as follows:

(in millions)	Amortized Cost	Unrealized Gains	Unrealized Losses	Fair Value
Available-for-sale:				
Debt securities	$ 5.2	$ 2.4	$	$ 7.6
Equity securities	0.5		(0.1)	0.4
Mortgage-backed securities	0.7			0.7
Total available-for-sale	6.4	2.4	(0.1)	8.7
Money market funds	9.5			9.5
Other	5.1			5.1
Total	$ 21.0	$ 2.4	$ (0.1)	$ 23.3

There were no sales of available-for-sale securities for the three months ended August 31, 2010. The proceeds from maturities of held-to-maturity securities was $3.8 million for the three months ended August 31, 2010. The proceeds from sales of available-for-sale securities was $1.6 million for the three months ended August 31, 2009. There were no maturities of held-to-maturity securities for the three months ended August 31, 2009. The cost of marketable securities sold is determined by the specific identification method. The Company recorded in other (income) expense a net realized gain on sales of available-for-sale securities of $0.8 million for the three months ended August 31, 2009. The Company s debt securities at August 31, 2010 all have maturities greater than 1 year.

The Company reviews impairments to investment securities quarterly to determine if the impairment is temporary or other-than-temporary. The Company reviews several factors to determine whether losses are other-than-temporary, including but not limited to (1) the length of time each security was in an unrealized loss position, (2) the extent to which fair value was less than cost, (3) the financial condition and near-term prospects of the issuer, and (4) the Company s intent and ability to hold each security for a period of time sufficient to allow for any anticipated recovery in fair value.

As of August 31, 2010, the Company held auction-rate securities with a fair value of $5.5 million. These securities are AAA-rated with long-term nominal maturities secured by student loans, which are guaranteed by the U.S. Government. Each of these securities was subject to auction processes for which there were insufficient bidders on the scheduled rollover dates. These auction-rate securities were classified as long-term available-for-sale securities as of August 31, 2010 because of the inability to predict when the market would recover. The securities continued to earn and pay interest at the maximum contractual rate. During September 2010, the balance of the Company s auction-rate securities was redeemed at their fair value, resulting in a realized gain of $2.6 million.

Biomet, Inc. and Subsidiaries Notes to Condensed Consolidated Financial Statements (Unaudited) (continued)

Note 5 Goodwill and Other Intangible Assets.

The balance of goodwill as of August 31, 2010 and May 31, 2010 was $4,755.6 million and $4,707.5 million, respectively. The change in goodwill reflects foreign currency fluctuations, primarily the weakening of the euro against the U.S. dollar.

The Company uses an accelerated method for amortizing customer relationship intangibles as the value for those relationships is greater at the beginning of their life. The change in intangible assets reflects foreign currency fluctuations, primarily the weakening of the euro against the U.S. dollar, as well as amortization.

Intangible assets consisted of the following at August 31, 2010 and May 31, 2010:

	August 31, 2010			May 31, 2010		
(in millions)	Gross Carrying Amount	Accumulated Amortization	Net Carrying Amount	Gross Carrying Amount	Accumulated Amortization	Net Carrying Amount
Core technology	$ 2,092.6	$ (336.2)	$ 1,756.4	$ 2,087.4	$ (308.9)	$ 1,778.5
Completed technology	664.9	(147.7)	517.2	664.9	(135.3)	529.6
Product trade names	183.6	(32.5)	151.1	183.6	(29.6)	154.0
Customer relationships	2,939.6	(635.4)	2,304.2	2,935.4	(583.7)	2,351.7
Non-compete contracts	4.6	(1.5)	3.1	4.6	(1.2)	3.4
Sub-total	5,885.3	(1,153.3)	4,732.0	5,875.9	(1,058.7)	4,817.2
Corporate trade names	397.6		397.6	397.6		397.6
In-process research & development	2.2		2.2			
Currency translation	39.8	(2.6)	37.2	(33.7)	9.2	(24.5)
Total	$ 6,324.9	$ (1,155.9)	$ 5,169.0	$ 6,239.8	$ (1,049.5)	$ 5,190.3

The weighted average useful life of the intangible assets at August 31, 2010 was as follows:

	Weighted Average Useful Life
Core technology	18 Years
Completed technology	12 Years
Product trade names	16 Years
Customer relationships	17 Years
Non-compete contracts	4 Years
Corporate trade names	Indefinite life

Expected amortization expense, for the intangible assets stated above, for the years ending May 31, 2011 through 2015 is $367.3 million, $359.7 million, $351.1 million, $341.4 million, and $327.9 million, respectively.

Cytosol Acquisition

On June 30, 2010, the Company completed the acquisition of substantially all the assets of Cytosol Laboratories, Inc. (Cytosol), located in Braintree, Massachusetts, a market leader in production of small volume anticoagulants. Cytosol was founded in 1968 to develop anticoagulants and other products to aid in the processing of blood components. The acquired business has three proprietary products with new drug application approvals: TriCitrasol®, noClot-50® and Rejuvesol® products. TriCitrasol® is used for anticoagulation during granulocytapheresis, noClot-50® is used as an anticoagulant in extracorporeal blood processing in the preparation of platelet rich plasma, and Rejuvesol® is used for the rejuvenation of stored, frozen red blood cells prior to transfusion. The purchase price of $8.7 million was paid on June 30, 2010. The acquisition did not have a material effect on the Company s net sales or operating income for the three months ended August 31, 2010. The purchase price was primarily allocated to identifiable intangible assets based on their estimated fair values at the acquisition date. The fair value assigned to the identifiable intangibles was determined using the income approach. The purchase price allocation was based upon a preliminary valuation and is subject to change during the measurement period as the valuation is finalized.

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Biomet, Inc. and Subsidiaries Notes to Condensed Consolidated Financial Statements (Unaudited) (continued)

Note 6 Debt.

The terms and carrying value of each debt instrument at August 31, 2010 and May 31, 2010 are set forth below:

(U.S. dollars and euros in millions)	Maturity Date	Interest Rate	Currency	August 31, 2010	May 31, 2010
Debt Instruments					
European facilities	No Maturity Date	Primarily	EUR	4.7	5.1
		Euribor + 1.90%		$ 6.0	$ 6.3
Term loan facility	March 25, 2015	Libor + 3.00%	USD	$ 2,275.7	$ 2,281.5
Term loan facility	March 25, 2015	Libor + 3.00%	EUR	850.9	853.1
				$ 1,080.9	$ 1,047.3
Cash flow revolving credit facility	September 25, 2013	Libor + 2.25%	USD	$	$
Cash flow revolving credit facility	September 25, 2013	Libor + 2.25%	EUR/USD	$/	$/
Asset-based revolving credit facility	September 25, 2013	Libor + 1.25%	USD	$	$
Senior cash pay notes	October 15, 2017	10%	USD	$ 771.0	$ 771.0
Senior toggle notes		10 3/ 8% /11			
	October 15, 2017	1/8%	USD	$ 771.0	$ 771.0
Senior subordinated notes	October 15, 2017	11 5/8%	USD	$ 1,015.0	$ 1,015.0
Premium on notes				$ 4.2	$ 4.4
			Total	$ 5,923.8	$ 5,896.5

The Company currently elects to use 3-month LIBOR for setting the interest rates on the majority of its U.S. dollar and euro term loans. The 3-month LIBOR rate for the U.S. dollar term loan as of August 31, 2010 was 0.54%. The euro term loan had a 3-month LIBOR rate of 0.67% as of August 31, 2010. The term loan facilities require quarterly principal payments equal to one quarter percent (0.25%) of the original principal balance (equal payments each quarter). Such payments commenced on the last business day of December 2007, and will continue on the last business day of each calendar year quarter with the remaining outstanding principal due on the maturity date. The Company made required payments of $5.8 million on June 30, 2010 for the U.S. dollar-denominated term loan facility, and made required payments of $2.7 million on June 30, 2010 for the euro-denominated term loan facility. There were no borrowings under the asset-based revolving credit facility as of August 31, 2010. The cash flow and asset-based revolving credit facilities and the notes do not have terms for mandatory principal pay downs. To calculate the U.S. dollar equivalent on outstanding balances for disclosure purposes, the Company used a currency conversion rate of 1 euro to $1.2703 and $1.2276, which represents the currency exchange rate from euros to U.S. dollars on August 31, 2010 and May 31, 2010, respectively.

The Company s revolving borrowing base available under all debt facilities at August 31, 2010 was $826.3 million, which is net of the borrowing base limitations relating to the senior secured asset-based revolving facility.

As of August 31, 2010, $54.0 million of financing fees related to the Company s credit agreement remained in long-term assets and continue to be amortized through interest expense over the remaining life of the credit agreement.

Note 7 Fair Value Measurements.

Under guidance issued by the FASB for fair value measurements, fair value is defined as the exit price, or the amount that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants as of the measurement date. This guidance also establishes a hierarchy for inputs used in measuring fair value that maximizes the use of observable inputs and minimizes the use of unobservable inputs by requiring that the most observable inputs be used when available. Observable inputs are inputs market participants would use in valuing the asset or liability developed based on market data obtained from sources independent of the Company. Unobservable inputs are inputs that reflect the Company s assumptions about the factors market participants would use in valuing the asset or liability developed based upon the best information available in the circumstances. The categorization of financial assets and financial liabilities within the valuation hierarchy is based upon the lowest level of input that is significant to the fair value measurement. The hierarchy is broken down into three levels defined as follows:

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Biomet, Inc. and Subsidiaries Notes to Condensed Consolidated Financial Statements (Unaudited) (continued)

Note 7 Fair Value Measurements, Continued.

Level 1 Inputs are quoted prices in active markets for identical assets or liabilities. The Company s Level 1 assets include money market investments and marketable equity securities.

Level 2 Inputs include quoted prices for similar assets or liabilities in active markets, quoted prices for identical or similar assets or liabilities in markets that are not active, and inputs (other than quoted prices) that are observable for the asset or liability, either directly or indirectly. The Company s Level 2 assets and liabilities primarily include agency bonds, corporate debt securities, asset-backed securities, certain mortgage-backed securities, and interest rate swaps whose value is determined using a pricing model with inputs that are observable in the market or can be derived principally from or corroborated by observable market data.

Level 3 Inputs are unobservable for the asset or liability. The Company s Level 3 assets include auction-rate securities and other equity investments. See the section below titled *Level 3 Valuation Techniques* for further discussion of how the Company determines fair value for investments classified as Level 3.

Assets and Liabilities that are Measured at Fair Value on a Recurring Basis

Guidance issued by the FASB for fair value measurements is principally applied to financial assets and liabilities such as marketable equity securities and debt securities that are classified and accounted for as available-for-sale, investments in equity and other securities, and derivative instruments consisting of interest rate swaps. These items are marked-to-market at each reporting period and measured at fair value as defined by this guidance. The information in the following paragraphs and tables primarily addresses matters relative to these financial assets and liabilities. Separately, there were no material fair value measurements with respect to nonfinancial assets or liabilities that were recognized or disclosed at fair value in the Company s financial statements on a recurring basis subsequent to the effective date of this guidance.

The following table provides information by level for assets and liabilities that are measured at fair value on a recurring basis at August 31, 2010 and May 31, 2010:

		Fair Value Measurements Using Inputs Considered as		
(in millions)	**Fair Value at August 31, 2010**	**Level 1**	**Level 2**	**Level 3**
Assets:				
Corporate debt securities	$ 2.6	$	$ 2.6	$
Auction-rate securities	5.5			5.5
Money market funds	109.6	109.6		
Foreign currency exchange contracts				
Other	1.7	1.0	0.5	0.2
Total assets	$ 119.4	$ 110.6	$ 3.1	$ 5.7
Liabilities:				
Interest rate swaps	$ 144.9	$	$ 144.9	$
Total liabilities	$ 144.9	$	$ 144.9	$

(in millions)	Fair Value at May 31, 2010	Fair Value Measurements Using Inputs Considered as Level 1	Level 2	Level 3
Assets:				
Corporate debt securities	$ 2.6	$	$ 2.6	$
Auction-rate securities	5.5			5.5
Money market funds	64.5	64.5		
Other	5.7	4.7	0.8	0.2
Total assets	$ 78.3	$ 69.2	$ 3.4	$ 5.7
Liabilities:				
Interest rate swaps	$ 129.9	$	$ 129.9	$
Total liabilities	$ 129.9	$	$ 129.9	$

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Biomet, Inc. and Subsidiaries Notes to Condensed Consolidated Financial Statements (Unaudited) (continued)

Note 7 Fair Value Measurements, Continued.

Level 3 Valuation Techniques

Financial assets are considered Level 3 when their fair values are determined using pricing models, discounted cash flow methodologies or similar techniques and at least one significant model assumption or input is unobservable. Level 3 financial assets also include certain investment securities for which there is limited market activity where the determination of fair value requires significant judgment or estimation. Level 3 investment securities primarily include certain auction-rate securities and other equity investments for which there was a decrease in the observation of market pricing. As of August 31, 2010 and May 31, 2010, these securities were valued primarily using internal cash flow valuation that incorporates transaction details such as contractual terms, maturity, timing and amount of future cash flows, as well as assumptions about liquidity and credit valuation adjustments of marketplace participants.

The following table provides a reconciliation of the beginning and ending balances of items measured at fair value on a recurring basis in the tables above that used significant unobservable inputs (Level 3) as of August 31, 2010 and May 31, 2010.

(in millions)	
Balance at June 1, 2009	22.7
Total net gains included in earnings	4.3
Total unrealized gains included in other comprehensive income	2.6
Total proceeds from sale of available-for-sale securities	(23.9)
Balance at May 31, 2010	5.7
Total net gains included in earnings	
Total unrealized gains included in other comprehensive income	
Total proceeds from sale of available-for-sale securities	
Balance at August 31, 2010	$ 5.7

The estimated fair value of the Company s long-term debt, including the current portion, at August 31, 2010 was $6,161.0 million compared to a carrying value of $5,923.8 million, and was $6,060.8 million compared to a carrying value of $5,896.5 million at May 31, 2010. Fair value of our traded debt was estimated using quoted market prices for the same or similar instruments. Fair value of our variable rate term debt was estimated using the carrying value as this debt has rates which approximate market interest rates. The fair values and carrying values consider the terms of the related debt and exclude the impacts of debt discounts and interest rate swaps.

The carrying value of the Company s other financial assets and liabilities on the balance sheet approximate fair value at August 31, 2010 and May 31, 2010.

Assets and Liabilities that are Measured at Fair Value on a Nonrecurring Basis

During the three months ended August 31, 2010, the Company had no significant measurements of financial assets or liabilities at fair value on a nonrecurring basis subsequent to their initial recognition.

Note 8 Derivative Instruments and Hedging Activities.

The Company is exposed to certain market risks relating to its ongoing business operations, including foreign currency risk, interest rate risk and commodity price risk. The Company currently manages foreign currency risk and interest rate risk through the use of derivatives.

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Biomet, Inc. and Subsidiaries Notes to Condensed Consolidated Financial Statements (Unaudited) (continued)

Note 8 Derivative Instruments and Hedging Activities, Continued.

Derivatives Designated as Hedging Instruments

Foreign Currency Instruments Certain assets, liabilities and forecasted transactions are exposed to foreign currency risk, primarily the fluctuation of the U.S. dollar against the euro. The Company faces transactional currency exposures that arise when it or its foreign subsidiaries enter into transactions, primarily on an intercompany basis, denominated in currencies other than their functional currency. The Company also faces currency exposure that arises from translating the results of its global operations to the U.S. dollar at exchange rates that have fluctuated from the beginning of the period. In order to mitigate the currency exposure related to debt service under the Company s debt facilities, the Company has hedged a portion of its net investment in its European subsidiaries with the issuance of a 875.0 million (approximately $1,207.4 million at September 25, 2007) principal amount euro term loan on September 25, 2007. The Company s net investment in its European subsidiaries at the hedging date of September 25, 2007 was 1,238.0 million ($1,690.0 million at September 25, 2007). As of August 31, 2010, the Company s net investment in European subsidiaries totaled 2,076.2 million ($2,637.4 million) and the outstanding principal balance of the euro term loan was 850.9 million ($1,080.9 million). The difference of 1,225.3 million ($1,556.5 million) remained unhedged as of August 31, 2010. Hedge effectiveness is tested quarterly to determine whether hedge treatment is still appropriate. The Company tests effectiveness on this net investment hedge by determining if the net investment in its European subsidiaries is greater than the outstanding euro-denominated debt balance. Any amount under hedges determined to be ineffective is recorded as other (income) expense in the statement of operations.

Interest Rate Instruments The Company uses interest rate swap agreements (cash flow hedges) in both U.S. dollars and euros as a means of fixing the interest rate on portions of its floating-rate debt instruments. As of August 31, 2010, the Company had a swap liability of $144.9 million, which consisted of $74.1 million short term, and $75.3 million long term, partially offset by a $4.5 million credit valuation adjustment. See the table below for existing contracts:

(U.S. dollars and euros in millions)

Structure	Currency	Notional Amount	Effective Date	Termination Date	Fair Value at August 31, 2010 Asset (Liability)	Fair Value at May 31, 2010 Asset (Liability)
3 year	EUR	75.0	September 25, 2007	September 25, 2010	$ (0.9)	$ (1.8)
3 year	EUR	50.0	March 25, 2008	March 25, 2011	(1.5)	(1.9)
4 year	EUR	75.0	September 25, 2007	September 25, 2011	(4.3)	(4.9)
4 year	EUR	40.0	March 25, 2008	March 25, 2012	(2.7)	(2.9)
5 year	EUR	230.0	September 25, 2007	September 25, 2012	(22.8)	(23.4)
5 year	EUR	40.0	March 25, 2008	March 25, 2013	(4.1)	(4.0)
3 year	USD	$ 195.0	September 25, 2007	September 25, 2010	(0.6)	(2.8)
3 year	USD	110.0	March 25, 2008	March 25, 2011	(1.4)	(1.7)
4 year	USD	195.0	September 25, 2007	September 25, 2011	(9.9)	(10.9)
4 year	USD	140.0	March 25, 2008	March 25, 2012	(5.3)	(4.7)
5 year	USD	585.0	September 25, 2007	September 25, 2012	(55.2)	(52.6)
5 year	USD	190.0	March 25, 2008	March 25, 2013	(11.9)	(9.1)
5 year	USD	325.0	December 26, 2008	December 25, 2013	(14.8)	(6.3)
5 year	USD	195.0	September 25, 2009	September 25, 2014	(14.0)	(7.3)
Credit Valuation Adjustment					4.5	4.4
Total					$ (144.9)	$ (129.9)

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Biomet, Inc. and Subsidiaries Notes to Condensed Consolidated Financial Statements (Unaudited) (continued)

Note 8 Derivative Instruments and Hedging Activities, Continued.

The interest rate swaps are recorded in other accrued expenses and other long term liabilities. As a result of cash flow hedge treatment being applied, all unrealized gains and losses related to the derivative instruments are recorded in accumulated other comprehensive income (loss) and are reclassified into operations in the same period in which the hedged transaction affects earnings. Hedge effectiveness is tested quarterly to determine if hedge treatment is still appropriate. The amount of ineffectiveness was not material for any period presented. The following represents applicable disclosure related to the interest rate swaps:

(in millions)

Derivatives in Cash Flow Hedging Relationships	Amount of Gain or (Loss) Recognized in OCI on Derivative for the Three Months Ended August 31, 2010 (Effective Portion)	Location of Loss Reclassified from Accumulated OCI into Income (Effective Portion)	Amount of Loss Reclassified from Accumulated OCI into Income (Effective Portion)	Location of Loss Recognized in Income on Derivative (Ineffective Portion and Amount Excluded From Effectiveness Testing)	Income on Derivative (Ineffective Portion and Amount Excluded from Effectiveness Testing) for the Three Months Ended August 31, 2010
Interest rate swaps, net of tax	$ 9.2	Interest expense	$	Other (income) expense	$

As of August 31, 2010, the effective interest rate, including the applicable lending margin, on 85.0% ($1,935.0 million) of the outstanding principal of the Company s U.S. dollar term loan was fixed at 6.94% through the use of interest rate swaps. The effective interest rate on 59.9% (510.0 million) of the outstanding principal of the Company s euro term loan was fixed at 7.30% through the use of interest rate swaps. The remaining unhedged balances of the U.S. dollar and euro term loans and senior secured asset-based revolving credit facility had effective interest rates of 3.26% and 3.58%, respectively. As stated in Note 6 to the condensed consolidated financial statements, the remaining debt instruments have a fixed interest rate. As of August 31, 2010, the Company s effective weighted average interest rate on all outstanding debt was 8.07%.

Derivatives Not Designated as Hedging Instruments

Foreign Currency Instruments The Company faces transactional currency exposures that arise when it or its foreign subsidiaries enter into transactions, primarily on an intercompany basis, denominated in currencies other than their functional currency. Beginning in fiscal 2011, the Company entered into short-term forward currency exchange contracts in order to mitigate the currency exposure related to these intercompany payables and receivables arising from intercompany purchases of finished goods inventory. The Company does not designate these contracts as hedges; therefore, all forward currency exchange contracts are recorded at their fair value each period, with the resulting gains and losses recorded in other income (expense). Any foreign currency remeasurement gains or losses recognized in a period are generally offset with gains or losses on the forward currency exchange contracts. The notional amount of these contracts at August 31, 2010 was $13.1 million. The fair value of these contracts was not material at August 31, 2010. There was no material gain or loss on the forward currency exchange contracts during the three months ended August 31, 2010.

Note 9 Other Comprehensive Income (Loss).

Other comprehensive income (loss) includes net income (loss), currency translation adjustments, certain derivative-related activity, changes in the value of available-for-sale investments, and changes in prior service cost from pension plans. The Company generally deems its foreign investments to be essentially permanent in nature and does not provide for taxes on currency translation adjustments arising from translating the investment in a foreign currency to U.S. dollars. When the Company determines that a foreign investment is no longer permanent in nature, estimated taxes are provided for the related deferred tax liability (asset), if any, resulting from currency translation adjustments. As of August 31, 2010, foreign investments were all permanent in nature.

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Biomet, Inc. and Subsidiaries Notes to Condensed Consolidated Financial Statements (Unaudited) (continued)

Note 9 Other Comprehensive Income (Loss), Continued.

Other comprehensive income (loss) and the related components are included in the table below:

(in millions)	Three Months Ended August 31, 2010	Three Months Ended August 31, 2009
Net loss	$ (17.8)	$ (22.8)
Other comprehensive income (loss), net of tax:		
Unrecognized actuarial gain (loss) on pension assets	(10.9)	(0.7)
Foreign currency translation adjustments	88.7	45.8
Unrealized gain (loss) on interest rate swaps	(9.2)	5.2
Unrealized gain (loss) on available-for-sale securities	(0.1)	0.2
Total other comprehensive income (loss), net of tax	68.5	50.5
Total other comprehensive income (loss)	$ 50.7	$ 27.7

Note 10 Share-based Compensation and Stock Plans.

The Company follows guidance issued by the FASB for share-based compensation to record share-based payment expense. This guidance requires the fair value of all share-based payments to employees, including stock options, to be expensed based on their fair value over the required award service period. The Company s share-based payments consist of stock options. For the Company s non-employee distributors, share-based expense is recorded in accordance with guidance issued by the FASB for equity instruments issued to other than employees in conjunction with selling goods or services.

Share-based compensation expense recognized was $5.1 million and $5.2 million for the three months ended August 31, 2010 and 2009, respectively.

Note 11 Income Taxes.

The Company applies guidance issued by the FASB for uncertainty in income taxes. This guidance prescribes a recognition threshold and measurement attribute for the financial statement recognition and measurement of tax contingencies and the tax position taken, or expected to be taken, in a tax return. The Company records the liability for unrecognized tax benefits as a long-term liability.

The Company conducts business globally and, as a result, certain of its subsidiaries file income tax returns in the U.S. federal jurisdiction, and various state and foreign jurisdictions. In the normal course of business, the Company is subject to examinations by taxing authorities throughout the world, including major jurisdictions such as Australia, Canada, France, Germany, Japan, Netherlands, Spain, the United Kingdom and the United States. In addition, certain state and foreign tax returns are under examination by various regulatory authorities.

The Internal Revenue Service is currently examining the Company s U.S. federal income tax returns for the years ended May 31, 2007 and 2008. The remainder of this examination is expected to be completed in 2011. The Company is no longer subject to U.S. federal income tax examinations for the fiscal years prior to and including the year ended May 31, 2002.

The Company regularly reviews issues that are raised from ongoing examinations and open tax years to evaluate the adequacy of its liabilities. As the various taxing authorities continue with their audit/examination programs, the Company will adjust its reserves accordingly to reflect these settlements. Substantially all of the Company s unrecognized tax benefits as of August 31, 2010, if recognized, would affect its effective tax rate. As of August 31, 2010, the Company believes that it is reasonably possible that its gross liabilities for unrecognized tax benefits may decrease by up to $6.0 million within the succeeding twelve months due to potential tax settlements.

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Biomet, Inc. and Subsidiaries Notes to Condensed Consolidated Financial Statements (Unaudited) (continued)

Note 12 Segment Reporting.

The Company operates in one reportable segment, musculoskeletal products, which includes the designing, manufacturing and marketing of reconstructive products, fixation devices, spinal products and other products. Other products consist primarily of softgoods and bracing products, sports medicine products, general instruments and operating room supplies. The Company manages its business segment primarily on a geographic basis. These geographic markets are comprised of the United States, Europe and International. Major markets included in the International geographic market are Canada, South America, Mexico and the Pacific Rim.

Net sales by product category in the periods presented were as follows:

(in millions)	Three Months Ended August 31, 2010	Three Months Ended August 31, 2009 [1]
Net sales by product:		
Reconstructive	$ 478.4	$ 468.6
Fixation	59.4	61.1
Spinal	57.9	58.0
Other	45.0	42.4
Total	$ 640.7	$ 630.1

(1) Certain amounts have been adjusted to conform to the current presentation. Specifically, reconstructive product net sales increased, and other product net sales decreased, $5.8 million and fixation product net sales increased, and spine product net sales decreased, $1.3 million. The current presentation aligns with how the Company presently manages and markets its products.

Net sales by geographic segment in the periods presented were as follows:

(in millions)	Three Months Ended August 31, 2010	Three Months Ended August 31, 2009 [1]
Net sales by geographic segment:		
United States	$ 419.1	$ 400.2
Europe	137.2	153.8
International	84.4	76.1
Total	$ 640.7	$ 630.1

(1) Certain amounts have been adjusted to conform to the current presentation. Specifically, International net sales increased, and Europe net sales decreased, $1.0 million. The current presentation aligns with how the Company presently manages and markets its products.

Long-term assets by geographic segment as of the period presented were as follows:

(in millions)	August 31, 2010	May 31, 2010
Long-term assets [1] by geographic segment:		
United States	$ 7,440.8	$ 7,508.0
Europe	1,990.0	1,939.6
International	1,120.0	1,072.2
Total	$ 10,550.8	$ 10,519.8

[1] Defined as property, plant and equipment, intangibles and goodwill.

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Biomet, Inc. and Subsidiaries Notes to Condensed Consolidated Financial Statements (Unaudited) (continued)

Note 13 Guarantor and Non-guarantor Financial Statements.

Each of the Company s existing wholly-owned domestic subsidiaries are fully, unconditionally, jointly, and severally guaranteeing the senior cash pay and PIK toggle notes on a senior unsecured basis and the senior subordinated notes on a senior subordinated unsecured basis, in each case to the extent such subsidiaries guarantee the Company s senior secured cash flow facilities.

The following financial information illustrates the composition of the combined guarantor subsidiaries:

Condensed Consolidating Balance Sheets

			August 31, 2010		
(in millions)	Biomet, Inc.	Guarantors	Non-Guarantors	Eliminations	Total
Assets					
Current assets:					
Cash and cash equivalents	$	$ 197.8	$ 76.2	$	$ 274.0
Accounts receivable, net		228.2	200.8		429.0
Income tax receivable		13.8	0.6		14.4
Inventories		293.7	353.1	(111.9)	534.9
Deferred income taxes		42.3	15.1		57.4
Prepaid expenses and other		43.3	43.5		86.8
Total current assets		819.1	689.3	(111.9)	1,396.5
Property, plant and equipment, net		364.0	268.6	(6.4)	626.2
Investments		19.3			19.3
Investment in subsidiaries	9,844.9			(9,844.9)	
Intangible assets, net		3,621.4	1,547.6		5,169.0
Goodwill		3,461.4	1,294.2		4,755.6
Other assets		66.5	47.6		114.1
Total assets	$ 9,844.9	$ 8,351.7	$ 3,847.3	$ (9,963.2)	$ 12,080.7
Liabilities & Shareholder s Equity					
Current liabilities:					
Current portion of long-term debt	$ 34.6	$	$ 1.4	$	$ 36.0
Accounts payable		50.7	36.9		87.6
Accrued interest	137.9				137.9
Accrued wages and commissions		48.7	32.4		81.1
Other accrued expenses		161.9	59.7		221.6
Total current liabilities	172.5	261.3	130.4		564.2
Long-term debt	5,883.3		4.5		5,887.8