

RTI Biologics, Inc.
Form 10-Q
November 04, 2011
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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

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

For the quarterly period ended September 30, 2011

OR

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

For the transition period from to

Commission file number 0-31271

RTI BIOLOGICS, INC.

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Delaware
(State or other jurisdiction of
incorporation or organization)

59-3466543
(I.R.S. Employer

Identification Number)

11621 Research Circle

Alachua, Florida 32615

(386) 418-8888

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

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that 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, or a non-accelerated filer. See definition of accelerated filer and large accelerated filer in Rule 12b-2 of the Exchange Act. (Check one):

Large Accelerated Filer

Accelerated Filer

Non-Accelerated Filer

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

Shares of common stock, \$0.001 par value, outstanding on October 26, 2011: 55,192,845

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RTI BIOLOGICS, INC.

FORM 10-Q For the Quarter Ended September 30, 2011

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Table of Contents**RTI BIOLOGICS, INC. AND SUBSIDIARIES****Condensed Consolidated Balance Sheets****(In thousands, except share data)****(Unaudited)**

	September 30, 2011	December 31, 2010
Assets		
Current Assets:		
Cash and cash equivalents	\$ 44,700	\$ 28,212
Accounts receivable - less allowances of \$325 at September 30, 2011 and \$490 at December 31, 2010	18,251	20,126
Inventories - net	78,538	87,278
Prepaid and other current assets	4,767	7,646
Deferred tax assets - net	15,844	15,810
Total current assets	162,100	159,072
Property, plant and equipment - net	42,670	43,346
Deferred tax assets - net	5,896	7,099
Other intangible assets - net	14,103	15,611
Other assets - net	464	630
Total assets	\$ 225,233	\$ 225,758
Liabilities and Stockholders Equity		
Current Liabilities:		
Accounts payable	\$ 11,205	\$ 12,570
Accrued expenses	14,510	14,340
Deferred tax liabilities	962	939
Current portion of deferred revenue	4,650	4,474
Current portion of long-term obligations	555	1,120
Total current liabilities	31,882	33,443
Long-term obligations - less current portion	201	1,877
Other long-term liabilities	1,624	3,135
Deferred tax liabilities	133	249
Deferred revenue	21,755	25,118
Total liabilities	55,595	63,822
Stockholders equity:		
Common stock, \$.001 par value: 150,000,000 shares authorized; 55,179,345 and 54,806,762 shares issued and outstanding, respectively	55	55
Additional paid-in capital	410,309	408,849
Accumulated other comprehensive loss	(1,204)	(1,438)
Accumulated deficit	(239,508)	(245,516)
Less treasury stock, 133,296 shares, at cost	(14)	(14)
Total stockholders equity	169,638	161,936

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Total liabilities and stockholders' equity	\$ 225,233	\$ 225,758
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See notes to condensed consolidated financial statements.

Table of Contents**RTI BIOLOGICS, INC. AND SUBSIDIARIES****Condensed Consolidated Statements of Operations****(In thousands, except share and per share data)****(Unaudited)**

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2011	2010	2011	2010
Revenues:				
Fees from tissue distribution	\$ 40,490	\$ 40,793	\$ 121,513	\$ 117,899
Other revenues	1,767	1,043	4,872	2,896
Total revenues	42,257	41,836	126,385	120,795
Costs of processing and distribution	22,934	21,950	69,006	64,994
Gross profit	19,323	19,886	57,379	55,801
Expenses:				
Marketing, general and administrative	13,664	15,630	41,759	44,935
Research and development	2,510	2,076	7,407	7,010
Goodwill impairment		134,681		134,681
Asset abandonments	1	3	58	18
Total operating expenses	16,175	152,390	49,224	186,644
Operating income (loss)	3,148	(132,504)	8,155	(130,843)
Other (expense) income:				
Interest expense	(37)	(129)	(149)	(436)
Interest income	47	22	132	85
Foreign exchange loss	(39)	(61)	(151)	(13)
Total other expense - net	(29)	(168)	(168)	(364)
Income (loss) before income tax provision	3,119	(132,672)	7,987	(131,207)
Income tax provision	(377)	(387)	(1,979)	(958)
Net income (loss)	\$ 2,742	\$ (133,059)	\$ 6,008	\$ (132,165)
Net income (loss) per common share - basic	\$ 0.05	\$ (2.43)	\$ 0.11	\$ (2.42)
Net income (loss) per common share - diluted	\$ 0.05	\$ (2.43)	\$ 0.11	\$ (2.42)
Weighted average shares outstanding - basic	55,167,178	54,806,262	55,071,761	54,703,890
Weighted average shares outstanding - diluted	55,397,794	54,806,262	55,205,997	54,703,890

See notes to condensed consolidated financial statements.

Table of Contents**RTI BIOLOGICS, INC. AND SUBSIDIARIES****Condensed Consolidated Statements of Cash Flows****(In thousands)****(Unaudited)**

	Three Months Ended		Nine Months Ended	
	September 30,		September 30,	
	2011	2010	2011	2010
Cash flows from operating activities:				
Net income (loss)	\$ 2,742	\$ (133,059)	\$ 6,008	\$ (132,165)
Adjustments to reconcile net income (loss) to net cash provided by (used in) operating activities:				
Depreciation and amortization expense	2,035	1,886	6,002	5,529
Amortization of deferred financing costs	5	21	16	59
Provision for bad debts and product returns	82	10	445	193
Provision for inventory write-downs	1,282	468	4,367	1,669
Amortization of deferred revenue	(1,165)	(569)	(3,187)	(1,372)
Deferred income tax provision (benefit)	310	(167)	759	(245)
Stock-based compensation	501	479	1,494	1,290
Goodwill impairment		134,681		134,681
Loss on asset abandonments	1	3	58	18
Change in assets and liabilities:				
Accounts receivable	(2,043)	(2,170)	1,501	403
Inventories	1,751	1,422	4,529	2,387
Prepaid and other current assets	(543)	665	2,870	(1,045)
Other long-term assets	24	1	149	55
Accounts payable	(503)	(4,560)	(2,255)	(7,535)
Accrued expenses	2,411	834	171	918
Other long-term liabilities	431	(776)	(513)	(1,895)
Net cash provided by (used in) operating activities	7,321	(831)	22,414	2,945
Cash flows from investing activities:				
Purchases of property, plant and equipment	(1,173)	(1,727)	(2,483)	(2,388)
Patent and acquired intangible asset costs	(56)	(1,060)	(1,129)	(1,283)
Net cash used in investing activities	(1,229)	(2,787)	(3,612)	(3,671)
Cash flows from financing activities:				
Proceeds from exercise of common stock options	61	19	246	764
Net proceeds (payments) on short-term obligations		163		(886)
Proceeds from long-term obligations		5,500		9,750
Payments on long-term obligations	(222)	(4,274)	(2,473)	(10,713)
Net cash (used in) provided by financing activities	(161)	1,408	(2,227)	(1,085)
Effect of exchange rate changes on cash and cash equivalents	(280)	29	(87)	(23)
Net increase (decrease) in cash and cash equivalents	5,651	(2,181)	16,488	(1,834)
Cash and cash equivalents, beginning of period	39,049	17,729	28,212	17,382

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Cash and cash equivalents, end of period	\$ 44,700	\$ 15,548	\$ 44,700	\$ 15,548
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See notes to condensed consolidated financial statements.

Table of Contents**RTI BIOLOGICS, INC. AND SUBSIDIARIES****Condensed Consolidated Statement of Stockholders' Equity****For the Nine Months Ended September 30, 2011****(In thousands)****(Unaudited)**

	Common Stock	Additional Paid-In Capital	Accumulated Other Comprehensive Income (Loss)	Accumulated Deficit	Treasury Stock	Total
Balance, December 31, 2010	\$ 55	\$ 408,849	\$ (1,438)	\$ (245,516)	\$ (14)	\$ 161,936
Net income				6,008		6,008
Foreign currency translation adjustment			234			234
Comprehensive income for the nine months ended September 30, 2011			234	6,008		6,242
Exercise of common stock options		246				246
Stock-based compensation		1,494				1,494
Change in tax benefit from stock-based compensation		(280)				(280)
Balance, September 30, 2011	\$ 55	\$ 410,309	\$ (1,204)	\$ (239,508)	\$ (14)	\$ 169,638

See notes to condensed consolidated financial statements.

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RTI BIOLOGICS, INC. AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited)

(In thousands, except share and per share data)

1. Operations and Organization

We are a leader in the use of natural tissues and innovative technologies to produce orthopedic and other surgical implants that repair and promote the natural healing of human bone and other human tissues and improve surgical outcomes. We process donated human musculoskeletal and other tissue, including bone, cartilage, tendon, ligament, fascia lata, pericardium, sclera and dermal tissue, and bovine animal tissue in producing allograft and xenograft implants utilizing our proprietary BIOCLEANSE® and TUTOPLAST® sterilization processes, for distribution to hospitals and surgeons. We process at two facilities in Alachua, Florida and one facility in Neunkirchen, Germany and distribute our products and services in all 50 states and in over 30 countries worldwide.

2. Basis of Presentation

The accompanying unaudited condensed consolidated financial statements include all adjustments, consisting of normal recurring accruals, which the Company considers necessary for a fair presentation of the results of operations for the periods shown. The condensed consolidated financial statements have been prepared in accordance with the instructions to Form 10-Q and, therefore, do not include all information and footnotes necessary for a fair presentation of consolidated financial position, results of operations and cash flows in conformity with accounting principles generally accepted in the United States of America. All intercompany balances and transactions have been eliminated in consolidation. The results of operations for any interim period are not necessarily indicative of the results to be expected for the full year. For further information, refer to the consolidated financial statements and notes thereto included in the Company's Annual Report on Form 10-K for the year ended December 31, 2010.

The condensed consolidated financial statements include the accounts of RTI Biologics, Inc. (RTI) and its wholly owned subsidiaries, Tutogen Medical, Inc. (TMI), RTI Biologics, Inc. Cardiovascular (inactive), Biological Recovery Group (inactive), and RTI Services, Inc. The condensed consolidated financial statements also include the accounts of RTI Donor Services, Inc. (RTIDS), which is a controlled entity. The condensed consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America.

3. Summary of Significant Accounting Policies

Long-Lived Assets The Company periodically evaluates the period of depreciation or amortization for long-lived assets to determine whether current circumstances warrant revised estimates of useful lives. The Company reviews its property, plant and equipment for impairment whenever events or changes in circumstances indicate that the carrying value of an asset may not be recoverable. Recoverability is measured by a comparison of the carrying amount to the net undiscounted cash flows expected to be generated by the asset. An impairment loss would be recorded for the excess of net carrying value over the fair value of the asset impaired. The fair value is estimated based on expected discounted future cash flows. The results of impairment tests are subject to management's estimates and assumptions of projected cash flows and operating results. Changes in assumptions or market conditions could result in a change in estimated future cash flows and the likelihood of materially different reported results. Past estimates by management of the fair values and useful lives of long-lived assets and investments have been accurate but have periodically been impacted by one-time events.

Other Intangible Assets Financial Accounting Standards Board (FASB) Accounting Standards Codification (ASC) 350 requires that definite lived intangible assets subject to amortization be tested for recoverability at the asset group level in accordance with ASC 360. The Company had one asset group for the year ended December 31, 2010 and the quarterly period ended September 30, 2011. The recoverability test is described in the Company's accounting policy for long-lived assets set forth above.

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Other intangible assets generally consist of patents, trademarks, procurement contracts, customer lists, non-compete agreements, selling and marketing relationships, licensing rights, and acquired exclusivity rights. Patents and trademarks are amortized on the straight-line method over the shorter of the remaining protection period or estimated useful lives of between 8 and 16 years. Procurement contracts, customer lists, non-compete agreements, selling and marketing relationships, and licensing rights are amortized over estimated useful lives of between 5 to 25 years. The acquired exclusivity rights are being amortized over eight years, the remaining term at the amendment date of the related amended distribution agreement.

Subsequent Events The Company evaluated subsequent events as of the issuance date of the financial statements, November 4, 2011, and determined that there were no applicable recognized events or transactions required to be recorded or disclosed in the financial statements.

4. Other Intangible Assets

Other intangible assets are as follows:

	September 30, 2011		December 31, 2010	
	Gross Carrying Amount	Accumulated Amortization	Gross Carrying Amount	Accumulated Amortization
Patents	\$ 4,369	\$ 1,203	\$ 4,392	\$ 1,032
Acquired exclusivity rights	2,941	1,950	2,941	1,671
Acquired licensing rights	10,850	2,601	10,850	1,692
Marketing and procurement intangible assets	2,973	1,276	2,964	1,141
Total	\$ 21,133	\$ 7,030	\$ 21,147	\$ 5,536

Marketing and procurement intangible assets include the following: procurement contracts, trademarks, selling and marketing relationships, customer lists, and non-compete agreements.

Amortization expense of other intangible assets for the three months ended September 30, 2011 and 2010 was \$495 and \$427, respectively, and for the nine months ended September 30, 2011 and 2010 was \$1,485 and \$1,207, respectively. At September 30, 2011, management's estimates of future amortization expense were as follows:

	Amortization Expense
2011	\$ 493
2012	2,100
2013	2,100
2014	1,800
2015	1,500
	\$ 7,993

5. Stock-Based Compensation

The Company has five stock-based compensation plans under which employees, consultants and outside directors have received stock options and restricted stock awards. Stock options are granted with an exercise price equal to 100% of the market value of a share of common stock on the date of the grant, generally have ten-year contractual

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terms, and vest over a one to five year period from the date of grant. Restricted stock awards are granted with a fair value equal to 100% of the market value of a share of common stock on the date of the grant, and vest over one to three year periods.

2010 Equity Incentive Plan On April 20, 2010, the Company's stockholders approved and adopted the 2010 Equity Incentive Plan, (the 2010 Plan). The 2010 Plan provides for the grant of incentive and nonqualified stock options and restricted stock to key employees, including officers and directors of the Company and consultants and advisors. The option price per share may not be less than 100% of the fair market value of such shares on the date granted. The 2010 Plan allows for up to 5,000,000 shares of common stock to be issued with respect to awards granted.

1998 Stock Option Plan and 2004 Equity Incentive Plan The Company adopted equity incentive plans in 1998 (the 1998 Plan) and 2004 (the 2004 Plan), which provide for the grant of incentive and nonqualified stock options and restricted stock to key employees, including officers and directors of the Company and consultants and advisors. The option price per share may not be less than 100% of the fair market value of such shares on the date granted. The 1998 and 2004 Plans allow for up to 4,406,400 and 2,000,000 shares, respectively, of common stock to be issued with respect to awards granted. New stock options may no longer be awarded under the 1998 Plan.

TMI 1996 Stock Option Plan and TMI 2006 Incentive and Non-Statutory Stock Option Plan In connection with the merger with TMI, the Company assumed the TMI 1996 Stock Option Plan and the TMI 2006 Incentive and Non-Statutory Stock Option Plan (TMI Plans). The TMI Plans allow for 4,880,000 and 1,830,000 shares of common stock, respectively, which may be issued with respect to stock options granted to former TMI employees or employees of the Company hired subsequent to the TMI acquisition. New stock options may no longer be awarded under the TMI 1996 Stock Option Plan.

Stock options outstanding, exercisable and available for grant at September 30, 2011 are summarized as follows:

	Number of Shares	Weighted Average Exercise Price	Weighted Average Remaining Contractual Life (Years)	Aggregate Intrinsic Value
Outstanding at January 1, 2011	6,308,182	\$ 5.79		
Granted	641,000	2.69		
Exercised	(100,300)	2.46		
Forfeited or expired	(168,760)	8.41		
Outstanding at September 30, 2011	6,680,122	\$ 5.47	4.66	\$ 1,218
Vested or expected to vest at September 30, 2011	6,492,759	\$ 5.53	4.54	\$ 1,154
Exercisable at September 30, 2011	4,883,722	\$ 6.13	3.28	\$ 722
Available for grant at September 30, 2011	4,438,478			

Outstanding options under all option plans vest over a one to five year period. Options expire ten years from the date of grant. The weighted-average grant date fair value of options granted for the nine months ended September 30, 2011 and 2010 was \$1.71 and \$2.56, respectively. The total intrinsic value of options exercised for the nine months ended September 30, 2011 and 2010 was \$38 and \$242, respectively. The intrinsic value of a stock option at the end of the quarter is the difference between the Company's closing stock price on the last trading day of the quarter and the exercise price, multiplied by the number of in-the-money options that would have been received by the option holders had all option holders exercised their options at quarter end. Cash received from option exercises for the nine months ended September 30, 2011 and 2010 were \$246 and \$764, respectively.

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As of September 30, 2011, there was \$3,087 of total unrecognized stock-based compensation related to nonvested stock options. That expense is expected to be recognized over a weighted-average period of 3.42 years.

During the first quarter of 2011, the Company granted 272,283 shares of restricted stock, at no cost to the recipients, with a weighted-average grant date fair value of \$2.69 which vest over one and three year periods. No shares of restricted stock were granted in the second or third quarters of 2011. As of September 30, 2011, there was \$388 of total unrecognized stock-based compensation related to time-based, nonvested restricted stock. That expense is expected to be recognized over a weighted-average period of 1.18 years.

For the three and nine months ended September 30, 2011 and 2010, the Company recognized stock-based compensation as follows:

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2011	2010	2011	2010
Stock-based compensation:				
Costs of processing and distribution	\$ 51	\$ 38	\$ 156	\$ 115
Marketing, general and administrative	435	411	1,292	1,085
Research and development	15	30	46	90
Total	\$ 501	\$ 479	\$ 1,494	\$ 1,290

6. Earnings Per Share

A reconciliation of the number of shares of common stock used in the calculation of basic and diluted earnings per share (EPS) is presented below:

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2011	2010	2011	2010
Basic shares	55,167,178	54,806,262	55,071,761	54,703,890
Effect of dilutive securities:				
Stock options	230,616		134,236	
Diluted shares	55,397,794	54,806,262	55,205,997	54,703,890

For the three months ended September 30, 2011 and 2010, approximately 4,696,000 and 5,924,000, respectively, and for the nine months ended September 30, 2011 and 2010, approximately 5,585,000 and 5,490,000, respectively, of issued stock options were not included in the computation of diluted EPS because they were anti-dilutive since their exercise price exceeded their market price. For the three and nine months ended September 30, 2010, options to purchase 80,770 and 262,610 shares of common stock, respectively, were not included in the computation of diluted EPS because dilutive shares are not factored into the calculation of EPS when a loss from continuing operations is reported.

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Inventories by stage of completion are as follows:

	September 30, 2011	December 31, 2010
Unprocessed donor tissue	\$ 24,378	\$ 27,774
Tissue in process	27,570	30,688
Implantable donor tissue	25,020	27,092
Supplies	1,570	1,724
	\$ 78,538	\$ 87,278

For the three months ended September 30, 2011 and 2010, the Company had inventory write-downs of \$1,282 and \$468, respectively, and for the nine months ended September 30, 2011 and 2010, the Company had inventory write-downs of \$4,367 and \$1,669, respectively, relating primarily to product obsolescence.

8. Property, Plant and Equipment

Property, plant and equipment are as follows:

	September 30, 2011	December 31, 2010
Land	\$ 1,847	\$ 1,816
Buildings and improvements	43,488	42,992
Processing equipment	29,182	27,376
Office equipment, furniture and fixtures	2,215	2,025
Computer equipment and software	4,602	3,881
Construction in process	572	258
Equipment under capital leases:		
Processing equipment	416	285
Computer equipment	744	744
	83,066	79,377
Less accumulated depreciation	(40,396)	(36,031)
	\$ 42,670	\$ 43,346

Depreciation expense of property, plant and equipment was \$1,540 and \$1,459 for the three months ended September 30, 2011 and 2010, respectively, and \$4,517 and \$4,322 for the nine months ended September 30, 2011 and 2010, respectively.

Table of Contents**9. Accrued Expenses**

Accrued expenses are as follows:

	September 30, 2011	December 31, 2010
Accrued compensation	\$ 4,340	\$ 3,372
Accrued donor recovery fees	712	1,535
Accrued distributor fees and marketing commissions	267	429
Accrued severance		40
Accrued licensing fees	2,151	3,354
Accrued taxes	2,117	161
Accrued professional service fees	833	544
Other	4,090	4,905
	\$ 14,510	\$ 14,340

The Company accrues for the estimated donor recovery fees due to third party recovery agencies as tissue is received.

10. Short and Long-Term Obligations

Short and long-term obligations are as follows:

	September 30, 2011	December 31, 2010
Term loans	\$ 241	\$ 2,307
Capital leases	515	690
	756	2,997
Less current portion	(555)	(1,120)
Long-term portion	\$ 201	\$ 1,877

The Company has two outstanding term loans with German banks. The first term loan of 125 Euro, or \$170, maturing March 31, 2012 has an outstanding interest rate swap agreement. Under this agreement, the Company pays a fixed interest rate of 5.15% and payments or receipts on the agreement are recorded as adjustments to interest expense. Such adjustments have not been significant. The second term loan of 52 Euro, or \$71, maturing September 30, 2012 has a fixed interest rate of 5.75%.

The Company has capital leases with interest rates ranging from 5.00% to 8.46% and maturity dates from May 2013 through December 2013.

The Company has four credit facilities, one credit facility with a U.S. bank and three credit facilities with German banks. As of September 30, 2011, there were no amounts outstanding on any of the four credit facilities.

On July 21, 2010, the Company entered into a second amendment to its credit agreement with Mercantile Bank, a division of Toronto-Dominion Bank. Under the second amendment to the credit agreement, 1) the revolving U.S. credit facility was increased from \$10,000 to \$15,000, available based on levels of accounts receivable and inventories, 2) the revolving credit facility's maturity date was extended from February 3, 2011 to July 21, 2012, and 3) a \$5,000 compensating balance requirement was eliminated. The revolving credit facility contains various restrictive covenants which limit, among other things, indebtedness and liens. Under the agreement, the credit facility was secured by the Company's domestic accounts receivable, inventory and certain processing equipment. The Company has \$13,096 available credit on the revolving credit facility at September 30, 2011. The current interest rate for this line of credit is 2.76%.

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Under the terms of the revolving credit facilities with three German banks, the Company may borrow up to 1,700 Euro, or approximately \$2,311, for working capital needs. The 1,000 Euro revolving credit facility is secured by a mortgage on the Company's German facility and a 4,000 Euro guarantee by the Company. The 500 Euro revolving credit facility is secured by accounts receivable of the Company's German subsidiary. The 200 Euro revolving credit facility is unsecured. The current interest rates for these lines of credit vary from 3.30% to 6.18%.

The Company was in compliance with all covenants related to its term loans and credit facilities as of September 30, 2011.

As of September 30, 2011, contractual maturities of long-term obligations are as follows:

	Term Loans	Capital Leases	Total
2011	\$ 44	\$ 28	\$ 72
2012	197	316	513
2013		163	163
2014		8	8
	\$ 241	\$ 515	\$ 756

The \$515 representing future maturities of capital leases includes interest in the amount of \$27. The present value of net minimum lease payments as of September 30, 2011 is \$488.

11. Income Taxes

The Company expects the domestic net deferred tax assets of approximately \$21,740, net of a valuation allowance at September 30, 2011 of \$469, to be realized through the generation of future taxable income and the reversal of existing taxable temporary differences. Valuation allowances have been recorded for certain state tax loss carryforwards as the Company does not believe that it will have future income in the state to utilize these loss carryforwards.

Valuation allowances are established when necessary to reduce deferred tax assets to amounts which are more likely than not to be realized. As such, valuation allowances of \$469 and \$1,137 as of September 30, 2011 and 2010, respectively, have been established against a portion of the deferred tax assets based on the nature of the credits claimed for certain state net operating loss carryforwards.

As of September 30, 2011, the Company has federal net operating loss carryforwards of \$11,027 that will expire in years 2025 to 2028, as well as state net operating loss carryforwards of \$18,600 that will expire in the years 2016 to 2018 and 2020 to 2027.

As of September 30, 2011, the Company has research tax credit carryforwards of \$5,153 that will expire in years 2018 through 2030, as well as alternative minimum tax credit carryforwards of \$544 that can be carried forward indefinitely.

United States income taxes have not been provided on the undistributed earnings of the Company's German subsidiary. It is not practicable to estimate the amount of tax that might be payable. The Company's intention is to permanently reinvest earnings in its German subsidiary.

During the third quarter of 2011, the Internal Revenue Service provided safe harbor guidance to its Large Business & International examiners regarding the deductibility of transaction fees incurred as part of the Company's merger with TMI in 2008, and as a result the Company de-recognized an uncertain tax liability which reduced income tax expense by \$800 in the quarter.

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Selected cash payments, receipts, and noncash activities are as follows:

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2011	2010	2011	2010
Cash paid for interest	\$ 24	\$ 121	\$ 113	\$ 381
Income taxes paid	142	128	317	300
Purchases of property, plant and equipment financed through capital leases			116	744
Payable for acquired licensing rights	1,000	4,000	1,000	4,000
Change in accrual for purchases of property, plant and equipment	1,187	562	1,147	562

13. Segment Data

The Company processes human and bovine animal tissue and distributes the tissue through various distribution channels. The Company's one line of business is comprised primarily of five product categories: sports medicine, spine, dental, surgical specialties, and bone graft substitutes (BGS) and general orthopedic. The following table presents revenues from tissue distribution and other revenues:

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2011	2010	2011	2010
Fees from tissue distribution:				
Sports medicine	\$ 11,072	\$ 10,887	\$ 34,881	\$ 32,751
Spine	10,322	9,743	31,060	24,474
Dental	4,551	7,714	13,615	22,061
Surgical specialties	7,519	6,800	22,583	18,885
BGS and general orthopedic	7,026	5,649	19,374	19,728
Other revenues	1,767	1,043	4,872	2,896
Total revenues	\$ 42,257	\$ 41,836	\$ 126,385	\$ 120,795
Domestic revenues	37,282	37,632	110,507	106,830
International revenues	4,975	4,204	15,878	13,965
Total revenues	\$ 42,257	\$ 41,836	\$ 126,385	\$ 120,795

For the three months ended September 30, 2011 and 2010, the Company derived approximately 18% and 22%, respectively, and for the nine months ended September 30, 2011 and 2010, the Company derived approximately 19% and 18%, respectively, of its total revenues from Medtronic, Inc.

For the three months ended September 30, 2011 and 2010, the Company derived approximately 16% and 19%, respectively, and for the nine months ended September 30, 2011 and 2010, the Company derived approximately 15% and 21%, respectively, of its total revenues from Zimmer, Inc.

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For the three months ended September 30, 2011 and 2010, the Company derived approximately 12% and 10%, respectively, and for the nine months ended September 30, 2011 and 2010, the Company derived approximately 13% and 12%, respectively, of its total revenues from foreign distribution.

As of September 30, 2011, the Company had \$31,292 of property, plant and equipment located domestically, and \$11,378 of property, plant and equipment located at its processing facility in Germany.

14. Commitments and Contingencies

On September 3, 2010, the Company and Zimmer Dental Inc. (Zimmer), a subsidiary of Zimmer, Inc., entered into a new exclusive distribution agreement (the Agreement), with an effective date of September 30, 2010. The Agreement has an initial term of ten years. Under the terms of the Agreement, the Company will supply sterilized allograft and xenograft implants at an agreed upon transfer price, and Zimmer will be the exclusive distributor of the implants for dental and oral applications worldwide (except the Ukraine), subject to certain Company obligations under an existing distribution agreement with a third party with respect to certain implants for the dental market. In consideration for Zimmer s exclusive distribution rights, Zimmer agreed to the following: 1) payment to the Company of \$13,000 within ten days of the effective date (the Upfront Payment), 2) annual exclusivity fees (Annual Exclusivity Fee) paid annually for the term of the contract to be paid at the beginning of each calendar year, the first of which was paid on January 18, 2011 in the amount of \$4,000, and 3) escalating annual purchase minimums to maintain exclusivity. Upon occurrence of an event that materially and adversely affects Zimmer s ability to distribute the Implants, Zimmer may be entitled to certain refund rights with respect to the Upfront Payment and the then current Annual Exclusivity Fee, where such refund would be in an amount limited by a formula specified in the Agreement that is based substantially on the number of days from the occurrence of such event to the date that it is cured by the Company to the satisfaction of Zimmer. Both the Upfront Payment and the initial Annual Exclusivity Fee have been deferred and will be recognized as other revenues over the term of the Agreement based on the expected contractual escalating annual purchase minimums relative to the total contractual minimum purchase requirements in the Agreement. Future annual exclusivity fees received will be deferred as received and will be recognized as other revenues in the same manner. Additionally, the Company has considered the potential impact of the Agreement s contractual refund provisions and does not expect these provisions to impact future expected revenue related to the Agreement.

On July 13, 2009, the Company and Davol amended their previous distribution agreement with TMI for human dermis implants. Under the amended agreement, 1) Davol paid the Company \$8,000 in non-refundable fees for exclusive distribution rights for the distribution to the breast reconstruction market until July 13, 2019, 2) the exclusive worldwide distribution agreement related to the hernia market was extended to July 13, 2019, and 3) Davol agreed to pay the Company certain additional exclusive distribution rights fees contingent upon the achievement of certain revenue milestones by Davol during the duration of the contract. In the fourth quarter of 2010, Davol paid the first revenue milestone payment of \$3,500. The \$8,000 and \$3,500 exclusivity payments have been deferred and are being recognized as other revenues on a straight-line basis over ten years, the initial term of the contract, and the remaining term of the contract, respectively. The straight-line method approximates the expected pattern of product distribution based on the distribution agreement s contractual annual minimum purchase requirements.

The Company s aforementioned revenue recognition methods related to the Zimmer and Davol distribution agreements result in the deferral of revenue more than amounts that would be refundable in the event the agreements were to be terminated in future periods. Additionally, the Company evaluates the appropriateness of the aforementioned revenue recognition methods on an ongoing basis.

On September 10, 2010, the Company entered into an Exclusive License Agreement with Athersys, Inc. (Athersys), pursuant to which Athersys will provide RTI access to its Multipotent Adult Progenitor Cell (MAPC) technologies to develop and commercialize MAPC technology-based biologic implants for certain orthopedic applications. In consideration for the Exclusive License, the Company agreed to pay Athersys the following: 1) a non-refundable \$3,000 license fee, payable in three time-based \$1,000 installments, the last of which was paid in the first quarter of 2011, 2) payment of \$2,000 contingent upon successful achievement of certain development milestones which the Company has recorded in accrued expenses, and 3) up to \$32,500 contingent upon achievement of certain cumulative revenue milestones in future years. In addition, the Company will pay Athersys royalties from the distribution of

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implants under a tiered royalty structure based on achievement of certain cumulative revenue milestones. The term of the Exclusive License Agreement is the longer of five years, or the remaining life of any patent or trade secret. These acquired licensing rights are being amortized to expense on a straight-line basis over the expected life of the asset.

In 2008, the Company was audited by the German value added tax (VAT) authorities and received an assessment for 600 Euro for the year ended December 31, 2008. The Company also received an assessment for the year ended December 31, 2009, in the third quarter of 2010 for 1,069 Euro. The Company estimates additional potential assessments of 1,095 Euro for the year ended December 31, 2010, and 966 Euro for the nine months ended September, 30, 2011. The potential cumulative assessments were 3,730 Euro, or \$5,073 as of September 30, 2011. The Company has not accrued a liability for this contingency. The Company does not believe that it is probable that it will ultimately be required to pay the assessment to the German VAT authorities.

The Company leases certain facilities, items of office equipment, and vehicles under non-cancelable operating lease arrangements expiring on various dates through 2016. The facility leases generally contain renewal options and escalation clauses based upon increases in the lessors operating expenses and other charges. The Company anticipates that most of these leases will be renewed or replaced upon expiration. At September 30, 2011, the aggregate future minimum lease payments under all non-cancelable lease agreements were as follows:

	Operating Leases
2011	\$ 440
2012	1,260
2013	676
2014	119
2015 and beyond	124
	\$ 2,619

The Company is, from time to time, involved in litigation relating to claims arising out of its operations in the ordinary course of business. The Company believes that none of these claims that were outstanding as of September 30, 2011 will have a material adverse impact on its financial position or results of operations.

The Company and Medtronic Sofamor Danek, USA, Inc. (MSD), a subsidiary of Medtronic, Inc., (Medtronic), have filed claims against each other with the American Arbitration Association related to events stemming from the actions of Biomedical Tissue Services, Ltd. (BTS), an unaffiliated company recovery agency, and the subsequent voluntary recall of allografts processed by the Company from tissue originating from BTS (the Allografts). MSD seeks indemnification from the Company for its legal fees, costs and expenses allegedly incurred during the defense of cases brought by recipients of Allografts. The Company denies that it is obligated to indemnify MSD in respect of the Allografts. In the same proceeding, the Company is seeking damages from MSD due to actions taken by MSD during the recall process. Among other allegations, the Company alleges that MSD s actions were negligent and in breach of the contractual agreements between the Company and MSD. As of the filing date, hearings have concluded on the matter and post-hearing briefs are being prepared for submission to the arbitrator. Final resolution of the matter is anticipated to occur late in the fourth quarter of 2011 or in the first quarter of 2012. The probability of a favorable or unfavorable outcome to the Company is unknown and a range of loss, if any, cannot be estimated at this time. However, while the Company believes its defenses and counterclaims are meritorious, the ultimate resolution of the matters could adversely impact the Company s business, financial condition or results of operations.

The Company s accounting policy is to accrue for legal costs as they are incurred.

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**Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations
Cautionary Statement Relating to Forward Looking Statements**

Information contained in this filing contains forward-looking statements which can be identified by the use of forward-looking terminology such as believes, expects, may, will, should, anticipates or comparable terminology, or by discussions of strategy. There can be no assurance that future results covered by these forward-looking statements will be achieved. Some of the matters described in the Risk Factors section of our Form 10-K constitute cautionary statements which identify factors regarding these forward-looking statements, including certain risks and uncertainties, that could cause actual results to vary materially from the future results indicated in these forward-looking statements. Other factors could also cause actual results to vary materially from the future results indicated in such forward-looking statements.

Management Overview

Due to the challenging economic environment, and the predominantly elective nature of the surgeries our products support, we are seeing lower than historical growth rates in most of our markets, which is impacting the performance in several of our product categories.

Our principal goals are to build on our competitive strengths in the marketplace to increase revenues, profitability and cash flow as we focus on improved operational efficiency, productivity and asset management. In addition, we are making investments in new product development and our U.S. direct distribution network to fuel growth in 2011 and beyond.

We continue to maintain our commitment to research and development and the introduction of new strategically targeted allograft and xenograft implants as well as focused clinical efforts to support their market acceptance.

Table of Contents**Three and Nine Months Ended September 30, 2011 Compared With Three and Nine Months Ended September 30, 2010**

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2011	2010	2011	2010
	(In Thousands)			
Fees from tissue distribution:				
Sports medicine	\$ 11,072	\$ 10,887	\$ 34,881	\$ 32,751
Spine	10,322	9,743	31,060	24,474
Dental	4,551	7,714	13,615	22,061
Surgical specialties	7,519	6,800	22,583	18,885
BGS and general orthopedic	7,026	5,649	19,374	19,728
Other revenues	1,767	1,043	4,872	2,896
 Total revenues	 \$ 42,257	 \$ 41,836	 \$ 126,385	 \$ 120,795
 Domestic revenues	 37,282	 37,632	 110,507	 106,830
International revenues	4,975	4,204	15,878	13,965
 Total revenues	 \$ 42,257	 \$ 41,836	 \$ 126,385	 \$ 120,795

Three Months Ended September 30, 2011 Compared With Three Months Ended September 30, 2010

Revenues. Our total revenues increased \$421,000, or 1.0%, to \$42.3 million for the three months ended September 30, 2011 compared to \$41.8 million for the three months ended September 30, 2010.

Sports Medicine - Revenues from sports medicine allografts increased \$185,000, or 1.7%, to \$11.1 million for the three months ended September 30, 2011 compared to \$10.9 million for the three months ended September 30, 2010. Sports medicine revenues increased primarily as a result of higher unit volumes of 3.2%, partially offset by lower average revenues per unit of 1.5%.

Spine - Revenues from spinal allografts increased \$579,000, or 5.9%, to \$10.3 million for the three months ended September 30, 2011 compared to \$9.7 million for the three months ended September 30, 2010. Spine revenues increased primarily as a result of higher unit volumes of 5.6%.

Dental - Revenues from dental allografts decreased \$3.2 million, or 41.0%, to \$4.6 million for the three months ended September 30, 2011 compared to \$7.7 million for the three months ended September 30, 2010. Dental revenues for the third quarter of 2011 compared to the third quarter of 2010 decreased primarily as a result of our entering into a new exclusive distribution agreement with our dental distributor effective September 30, 2010 where all orders are distributed in consideration for transfer fees, which resulted in lower average revenues per unit of 27.3% rather than end of market costs for which we then paid a distribution fee. Unit volumes decreased 18.5% for the third quarter of 2011 compared to the third quarter of 2010, primarily as a result of a significant initial stocking order in the third quarter of 2010.

Surgical Specialties - Revenues from surgical specialty allografts increased \$719,000, or 10.6%, to \$7.5 million for the three months ended September 30, 2011 compared to \$6.8 million for the three months ended September 30, 2010. Surgical specialties revenues increased primarily as a result of higher unit volumes of 12.5%, partially offset by lower revenues per unit of 1.5% due primarily to changes in product mix.

Bone Graft Substitutes (BGS) and General Orthopedic - Revenues from BGS and general orthopedic allografts increased \$1.4 million, or 24.4%, to \$7.0 million for the three months ended September 30, 2011 compared to \$5.6 million for the three months ended September 30, 2010. BGS and general orthopedic revenue increases were primarily the result of higher unit volumes of 25.5%.

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Other Revenues - Revenues from other sources consisting of tissue recovery fees, biomedical laboratory fees, recognition of previously deferred revenues, shipping fees and distribution of reproductions of our allografts to distributors for demonstration purposes and restocking fees increased by \$724,000 to \$1.8 million for the three months ended September 30, 2011 compared to \$1.0 million for the three months ended September 30, 2010. The increase was due to higher deferred revenue amortization resulting from exclusivity payments received from our dental and surgical specialty distributors.

Foreign Currency Fluctuations - For the three months ended September 30, 2011, foreign currency exchange fluctuations resulted in an increase in total revenues of \$394,000 due to a 9.7% decrease in the value of the U.S. dollar versus the Euro, as compared to the prior year period.

Costs of Processing and Distribution. Costs of processing and distribution increased \$984,000, or 4.5%, to \$22.9 million for the three months ended September 30, 2011 compared to \$22.0 million for the three months ended September 30, 2010 due primarily to volume increases and changes in product mix.

Costs of processing and distribution increased as a percentage of revenues from 52.5% for the three months ended September 30, 2010 to 54.3% for the three months ended September 30, 2011. The increase was primarily due to the new distribution agreement with our dental distributor effective September 30, 2010 where all orders are distributed in consideration for transfer fees rather than end of market costs for which we then paid a distribution fee, resulting in lower average revenues per unit, partially offset by higher production levels and operating efficiencies for the third quarter of 2011 compared to the third quarter of 2010.

Marketing, General and Administrative Expenses. Marketing, general and administrative expenses decreased by \$2.0 million, or 12.6%, to \$13.7 million for the three months ended September 30, 2011 from \$15.6 million for the three months ended September 30, 2010. Marketing, general and administrative expenses decreased as a percentage of revenues from 37.4% for the three months ended September 30, 2010 to 32.3% for the three months ended September 30, 2011. The decrease was primarily due to a decrease in distributor commissions of \$2.1 million attributable to the new distribution agreement with our dental distributor effective September 30, 2010.

Research and Development Expenses. Research and development expenses increased by \$434,000, or 20.9%, to \$2.5 million for the three months ended September 30, 2011 from \$2.1 million for the three months ended September 30, 2010. As a percentage of revenues, research and development expenses increased from 5.0% for the three months ended September 30, 2010 to 5.9% for the three months ended September 30, 2011. The increase was primarily due to higher research supplies and materials expenses of \$420,000.

Asset Impairments and Abandonments. Asset abandonments were negligible for the three months ended September 30, 2011 and 2010, respectively. We recognized a \$134.7 million loss on asset impairment and abandonments during the three months ended September 30, 2010. The other than temporary asset impairment charge of \$134.7 million was charged against our goodwill.

Net Other Expense. Net other expense was \$29,000 for the three months ended September 30, 2011 compared to \$168,000 for the three months ended September 30, 2010. Interest expense decreased for the three months ended September 30, 2011 to \$37,000 from \$129,000 for the three months ended September 30, 2010 due to a reduction of interest bearing long-term obligations. Interest income for the three months ended September 30, 2011 increased to \$47,000 compared to \$22,000 for the three months ended September 30, 2010 due to higher average balances of cash and cash equivalents. Foreign exchange loss was \$39,000 for the three months ended September 30, 2011 compared to a foreign exchange loss of \$61,000 for the three months ended September 30, 2010 due to changes in the value of the U.S. dollar versus the Euro and the timing of payments on foreign currency liabilities.

Income Tax Provision. Income tax provision for the three months ended September 30, 2011 was \$377,000 compared to \$387,000 for the three months ended September 30, 2010. Our effective tax rate for the three months ended September 30, 2011 and 2010 was 12.1% and (0.3)%, respectively. The effective tax rate was favorably impacted during the third quarter of 2011 by the de-recognition of an uncertain tax liability of \$800,000 resulting from new safe harbor guidance issued by the Internal Revenue Service regarding the deductibility of transaction fees

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incurred as part of our merger with Tutogen Medical, Inc (TMI) in 2008. The effective tax rate was negatively impacted during the third quarter of 2010 by the non-deductible goodwill impairment in the three months ended September 30, 2010.

Nine Months Ended September 30, 2011 Compared With Nine Months Ended September 30, 2010

Revenues. Our total revenues increased \$5.6 million, or 4.6%, to \$126.4 million for the nine months ended September 30, 2011 compared to \$120.8 million for the nine months ended September 30, 2010.

Sports Medicine - Revenues from sports medicine allografts increased \$2.1 million, or 6.5%, to \$34.9 million for the nine months ended September 30, 2011 compared to \$32.8 million for the nine months ended September 30, 2010. Sports medicine revenues increased primarily as a result of higher unit volumes of 7.6%, partially offset by lower average revenues per unit of 1.1%.

Spine - Revenues from spinal allografts increased \$6.6 million, or 26.9%, to \$31.1 million for the nine months ended September 30, 2011 compared to \$24.5 million for the nine months ended September 30, 2010. Spine revenues increased primarily as a result of higher unit volumes of 25.8% due primarily to inventory reductions initiated by our distributors in the first half of 2010.

Dental - Revenues from dental allografts decreased \$8.5 million, or 38.3%, to \$13.6 million for the nine months ended September 30, 2011 compared to \$22.1 million for the nine months ended September 30, 2010. Dental revenues for the first nine months of 2011 compared to the first nine months of 2010 decreased primarily as a result of our entering into a new exclusive distribution agreement with our dental distributor effective September 30, 2010 where all orders are distributed in consideration for transfer fees, which resulted in lower average revenues per unit of 36.5% rather than end of market costs for which we then paid a distribution fee. Additionally, unit volumes decreased 2.6% for the nine months ended September 30, 2011 compared to the nine months ended September 30, 2010, primarily as a result of a significant initial stocking order in the third quarter of 2010.

Surgical Specialties - Revenues from surgical specialty allografts increased \$3.7 million, or 19.6%, to \$22.6 million for the nine months ended September 30, 2011 compared to \$18.9 million for the nine months ended September 30, 2010. Surgical specialties revenues increased primarily as a result of higher unit volumes of 3.1% and higher average revenues per unit of 16.2%, due primarily to changes in product mix.

Bone Graft Substitutes (BGS) and General Orthopedic - Revenues from BGS and general orthopedic allografts decreased \$354,000, or 1.8%, to \$19.4 million for the nine months ended September 30, 2011 compared to \$19.7 million for the nine months ended September 30, 2010. BGS and general orthopedic revenue decreases were due primarily to changes in product mix and lower unit volumes of 3.8%, partially offset by higher average revenues per unit of 2.1%.

Other Revenues - Revenues from other sources consisting of tissue recovery fees, biomedical laboratory fees, recognition of previously deferred revenues, shipping fees and distribution of reproductions of our allografts to distributors for demonstration purposes and restocking fees increased by \$2.0 million to \$4.9 million for the nine months ended September 30, 2011 compared to \$2.9 million for the nine months ended September 30, 2010. The increase was due to higher deferred revenue amortization resulting from exclusivity payments received from our dental and surgical specialty distributors.

Foreign Currency Fluctuations - For the nine months ended September 30, 2011, foreign currency exchange fluctuations resulted in an increase in total revenues of \$910,000 due to a 6.9% decrease in the value of the U.S. dollar versus the Euro, as compared to the prior year period.

Costs of Processing and Distribution. Costs of processing and distribution increased \$4.0 million, or 6.2%, to \$69.0 million for the nine months ended September 30, 2011 compared to \$65.0 million for the nine months ended September 30, 2010 due to volume increases and changes in product mix.

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Costs of processing and distribution increased as a percentage of revenues from 53.8% for the nine months ended September 30, 2010 to 54.6% for the nine months ended September 30, 2011. The increase was primarily due to the new distribution agreement with our dental distributor effective September 30, 2010 where all orders are distributed in consideration for transfer fees rather than end of market costs for which we then paid a distribution fee, resulting in lower average revenues per unit, partially offset by higher production levels and operating efficiencies for the nine months ended September 30, 2011 compared to the nine months ended September 30, 2010.

Marketing, General and Administrative Expenses. Marketing, general and administrative expenses decreased by \$3.2 million, or 7.1%, to \$41.8 million for the nine months ended September 30, 2011 from \$44.9 million for the nine months ended September 30, 2010. Marketing, general and administrative expenses decreased as a percentage of revenues from 37.2% for the nine months ended September 30, 2010 to 33.0% for the nine months ended September 30, 2011. The decrease was due primarily to a decrease in distributor commissions of \$6.9 million attributable to the new distribution agreement with our dental distributor effective September 30, 2010, partially offset by an increase in compensation of \$1.6 million, marketing programs and demonstration products of \$1.0 million, amortization expense of \$295,000 relating to license agreements, and legal expenses of \$344,000. In addition, expenses related to our foreign operations increased \$511,000 for the nine months ended September 30, 2011 compared to the prior period, of which \$475,000 is due to a 6.9% decrease in the value of the U.S. dollar versus the Euro, as compared to the prior year period.

Research and Development Expenses. Research and development expenses increased by \$397,000, or 5.7%, to \$7.4 million for the nine months ended September 30, 2011 from \$7.0 million for the nine months ended September 30, 2010. As a percentage of revenues, research and development expenses increased from 5.8% for the nine months ended September 30, 2010 to 5.9% for the nine months ended September 30, 2011. The increase was primarily due to higher research supplies and studies expenses of \$300,000 and \$204,000, respectively, partially offset by lower payroll and benefits expense of \$167,000.

Asset Impairments and Abandonments. Asset abandonments were \$58,000 for the nine months ended September 30, 2011. We recognized a \$134.7 million loss on asset impairment and abandonments during the nine months ended September 30, 2010. The other than temporary asset impairment charge of \$134.7 million was charged against our goodwill.

Net Other Expense. Net other expense was \$168,000 for the nine months ended September 30, 2011 compared to \$364,000 for the nine months ended September 30, 2010. Interest expense decreased for the nine months ended September 30, 2011 to \$149,000 from \$436,000 for the nine months ended September 30, 2010 due to a reduction on interest bearing long-term obligations. Interest income for the nine months ended September 30, 2011 increased to \$132,000 compared to \$85,000 for the nine months ended September 30, 2010 due to higher average balances of cash and cash equivalents. Foreign exchange loss was \$151,000 for the nine months ended September 30, 2011 compared to a foreign exchange loss of \$13,000 for the nine months ended September 30, 2010 due to changes in the value of the U.S. dollar versus the Euro and the timing of payments on foreign currency liabilities.

Income Tax Provision. Income tax provision for the nine months ended September 30, 2011 was \$2.0 million compared to \$1.0 million for the nine months ended September 30, 2010. Our effective tax rate for the nine months ended September 30, 2011 and 2010 was 24.8% and (0.7)%, respectively. Our effective tax rate for the nine months ended September 30, 2011 was positively impacted by the de-recognition of an uncertain tax liability of \$800,000 resulting from new safe harbor guidance issued by the Internal Revenue Service regarding the deductibility of transaction fees incurred as part of our merger with TMI in 2008, and research tax credit carryforwards applied in the first nine months of 2011 with no comparable credits being recognized in the prior period. The effective tax rate was negatively impacted during the third quarter of 2010 by the non-deductible goodwill impairment in the three months ended September 30, 2010.

Table of Contents**Liquidity and Capital Resources**

Our working capital at September 30, 2011 increased \$4.6 million to \$130.2 million from \$125.6 million at December 31, 2010. The increase in working capital was primarily due to the increase in cash and cash equivalents on hand. At September 30, 2011, we had 39 days of revenues outstanding in trade accounts receivable, a decrease of 5 days compared to December 31, 2010. The decrease was due to higher cash receipts from customers than shipments and corresponding billings to customers in the first nine months of 2011. At September 30, 2011 we had 312 days of inventory on hand, a decrease of 28 days compared to December 31, 2010. We had \$44.7 million of cash and cash equivalents at September 30, 2011.

Our long term obligations at September 30, 2011 decreased \$2.2 million to \$756,000 from \$3.0 million at December 31, 2010. The decrease in long term obligations was primarily due to our paying down \$2.1 million of our term loans. At September 30, 2011, we have \$15.4 million of borrowing capacity available under our revolving credit facilities.

As of September 30, 2011, we believe that our working capital, together with our borrowing ability under our revolving credit facilities, will be adequate to fund our on-going operations for the next twelve months.

Certain Commitments.

The Company's short-term and long-term obligations and availability of credit as of September 30, 2011 are as follows:

	Outstanding Balance	Available Credit
	(In thousands)	
<u>Short-term obligations:</u>		
Credit facilities	\$	\$ 2,311
Total short-term obligations		2,311
<u>Long-term obligations:</u>		
Credit facility		13,096
Long-term obligations	241	
Capital leases	515	
Total long-term obligations	756	13,096
Total obligations	\$ 756	\$ 15,407

The following table provides a summary of our debt obligations, operating lease obligations, and other significant obligations as of September 30, 2011.

	Total	Contractual Obligations Due by Period				After 2014
		2011	2012	2013	2014	
	(In thousands)					
Debt obligations	\$ 756	\$ 72	\$ 513	\$ 163	\$ 8	\$
Operating leases	2,619	440	1,260	676	119	124
Other significant obligations (1)	5,812	3,209	2,271	202	130	
Total	\$ 9,187	\$ 3,721	\$ 4,044	\$ 1,041	\$ 257	\$ 124

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(1) *These amounts consist of contractual obligations for tissue recovery, development grants and licensing fees.*

The Company was in compliance with all covenants related to its credit facilities and term loans as of September 30, 2011.

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Item 3. Quantitative and Qualitative Disclosures About Market Risk

We are subject to market risk from exposure to changes in interest rates based upon our financing, investing and cash management activities. We do not expect changes in interest rates to have a material adverse effect on our income or our cash flows in 2011. However, we cannot assure that interest rates will not significantly change in the future.

In the United States and in Germany, we are exposed to interest rate risk. Changes in interest rates affect interest income earned on cash and cash equivalents and interest expense on revolving credit arrangements. Except for an interest rate swap associated with 125,000 Euro, or \$170,000, of long-term debt over six years that was started March 31, 2006, we do not enter into derivative transactions related to cash and cash equivalents or debt. Accordingly, we are subject to changes in interest rates. Based on September 30, 2011 outstanding obligations, a 1% change in interest rates would have had a de-minimis impact on our results of operations.

The value of the U.S. dollar compared to the Euro affects our financial results. Changes in exchange rates may positively or negatively affect revenues, gross margins, operating expenses and net income. Our international operation currently transacts business primarily in the Euro. Assets and liabilities of foreign subsidiaries are translated at the period end exchange rate while revenues and expenses are translated at the average exchange rate for the period. Intercompany transactions are translated from the Euro to the U.S. dollar. Based on September 30, 2011 outstanding intercompany balances, a 1% change in currency rates would have had a de-minimis impact on our results of operations.

Item 4. Controls and Procedures

As of the end of the period covered by this report, an evaluation was performed on the effectiveness of the design and operation of our disclosure controls and procedures under the supervision and with the participation of our management, including our Chief Executive Officer and Chief Financial Officer. Disclosure controls and procedures include controls and other procedures that are designed to ensure that information required to be disclosed by the Company in the reports that it files or submits under the Exchange Act is recorded, processed, summarized and reported, within the time periods specified in the Commission's rules and forms, and accumulated and communicated to the Company's management, including its principal executive and principal financial officers, or persons performing similar functions, as appropriate to allow timely decisions regarding required disclosure. Based upon that evaluation, our Chief Executive Officer and Chief Financial Officer concluded that the design and operation of our disclosure controls and procedures were effective as of the end of the period covered by this report.

There have been no changes in the Company's internal control over financial reporting during the Company's last fiscal quarter that materially affected, or are reasonably likely to materially affect, the Company's internal control over financial reporting.

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PART II. OTHER INFORMATION

Item 1. Legal Proceedings

We refer you to Part I, Item 1, Note 14 entitled "Commitments and Contingencies" to the condensed consolidated financial statements included in this Quarterly Report on Form 10-Q for a description of current legal proceedings.

Item 1A. Risk Factors

There has been no material change in our risk factors as previously disclosed in Part I, Item 1.A., *Risk Factors*, of our Annual Report on Form 10-K for the year ended December 31, 2010, as filed with the SEC on February 22, 2011.

Item 2. Unregistered Sales of Equity Securities and Use of Proceeds

None.

Item 3. Defaults Upon Senior Securities

Not applicable.

Item 6. Exhibits

- 31.1 Certification of the Chief Executive Officer Under Section 302 of the Sarbanes-Oxley Act of 2002.
- 31.2 Certification of the Executive Vice President and Chief Financial Officer Under Section 302 of the Sarbanes-Oxley Act of 2002.
- 32.1 Certification of Periodic Financial Report by Chief Executive Officer Under Section 906 of the Sarbanes-Oxley Act of 2002.
- 32.2 Certification of Periodic Financial Report by Executive Vice President and Chief Financial Officer Under Section 906 of the Sarbanes-Oxley Act of 2002.
- 101.INS** XBRL Instance Document
- 101.SCH** XBRL Taxonomy Extension Schema Document
- 101.CAL** XBRL Taxonomy Extension Calculation Linkbase Document
- 101.DEF** XBRL Taxonomy Extension Definition Linkbase Document
- 101.LAB** XBRL Taxonomy Extension Label Linkbase Document
- 101.PRE** XBRL Taxonomy Extension Presentation Linkbase Document

** XBRL (Extensible Business Reporting Language) information is furnished and not filed or a part of a registration statement or prospectus for purposes of Sections 11 or 12 of the Securities Act of 1933, is deemed not filed for purposes of Section 18 of the Securities Exchange Act of 1934, and otherwise is not subject to liability under these sections.

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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.

RTI BIOLOGICS, INC. (Registrant)

By: /s/ Brian K. Hutchison
Brian K. Hutchison

Chief Executive Officer

By: /s/ Robert P. Jordheim
Robert P. Jordheim

**Executive Vice President and Chief Financial
Officer**

Date: November 4, 2011

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EXHIBIT INDEX

Exhibit No.	Description
31.1	Certification of the Chief Executive Officer Under Section 302 of the Sarbanes-Oxley Act of 2002.
31.2	Certification of the Executive Vice President and Chief Financial Officer Under Section 302 of the Sarbanes-Oxley Act of 2002.
32.1	Certification of Periodic Financial Report by Chief Executive Officer Under Section 906 of the Sarbanes-Oxley Act of 2002.
32.2	Certification of Periodic Financial Report by Executive Vice President and Chief Financial Officer Under Section 906 of the Sarbanes-Oxley Act of 2002.
101.INS**	XBRL Instance Document
101.SCH**	XBRL Taxonomy Extension Schema Document
101.CAL**	XBRL Taxonomy Extension Calculation Linkbase Document
101.DEF**	XBRL Taxonomy Extension Definition Linkbase Document
101.LAB**	XBRL Taxonomy Extension Label Linkbase Document
101.PRE**	XBRL Taxonomy Extension Presentation Linkbase Document

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