

INVACARE CORP
Form 10-Q
November 05, 2010

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549

FORM 10-Q

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

For the quarterly period ended September 30, 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 001-15103

INVACARE CORPORATION
(Exact name of registrant as specified in its charter)

Ohio
(State or other jurisdiction of
incorporation or organization)

95-2680965
(IRS Employer Identification No)

One Invacare Way, P.O. Box 4028, Elyria, Ohio
(Address of principal executive offices)

44036
(Zip Code)

(440) 329-6000
(Registrant's telephone number, including area code)

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

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15 (d) of the Securities Exchange Act of 1934 (the "Exchange Act") 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 the registrant was required to submit and post such files) Yes No

Edgar Filing: INVACARE CORP - Form 10-Q

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 "small reporting company" in Rule 12b-2 of the Exchange Act (Check One). Large accelerated filer Accelerated filer Non-accelerated filer (Do not check if a smaller reporting company) Smaller reporting company

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

As of November 2, 2010, the registrant had 31,317,518 Common Shares and 1,085,347 Class B Common Shares outstanding.

INVACARE CORPORATION

INDEX

	Page No.
<u>Part I. FINANCIAL INFORMATION:</u>	
<u>Item 1. Financial Statements (Unaudited)</u>	
<u>Condensed Consolidated Balance Sheets – September 30, 2010 and December 31, 2009</u>	3
<u>Condensed Consolidated Statement of Operations – Three and Nine Months Ended</u> <u>September 30, 2010 and 2009</u>	4
<u>Condensed Consolidated Statement of Cash Flows – Nine Months Ended September 30,</u> <u>2010 and 2009</u>	5
<u>Notes to Condensed Consolidated Financial Statements – September 30, 2010</u>	6
<u>Item 2. Management's Discussion and Analysis of Financial Condition and Results of</u> <u>Operations</u>	25
<u>Item 3. Quantitative and Qualitative Disclosures About Market Risk</u>	36
<u>Item 4. Controls and Procedures</u>	36
<u>Part II. OTHER INFORMATION:</u>	
<u>Item 1A. Risk Factors</u>	36
<u>Item 2. Unregistered Sales of Equity Securities and Use of Proceeds</u>	37
<u>Item 6. Exhibits</u>	37
<u>SIGNATURES</u>	37

Index

Part I. FINANCIAL INFORMATION
 Item 1. Financial Statements.

INVACARE CORPORATION AND SUBSIDIARIES
 Condensed Consolidated Balance Sheets (unaudited)

	September 30, 2010	December 31, 2009
(In thousands)		
ASSETS		
CURRENT ASSETS		
Cash and cash equivalents	\$ 32,089	\$ 37,501
Trade receivables, net	254,657	263,014
Installment receivables, net	3,338	3,565
Inventories, net	182,597	172,222
Deferred income taxes	1,327	390
Other current assets	48,308	51,772
TOTAL CURRENT ASSETS	522,316	528,464
OTHER ASSETS	42,925	48,006
OTHER INTANGIBLES	72,075	85,305
PROPERTY AND EQUIPMENT, NET	130,037	141,633
GOODWILL	495,184	556,093
TOTAL ASSETS	\$ 1,262,537	\$ 1,359,501
LIABILITIES AND SHAREHOLDERS' EQUITY		
CURRENT LIABILITIES		
Accounts payable	\$ 144,910	\$ 141,059
Accrued expenses	136,576	142,293
Accrued income taxes	4,121	5,884
Short-term debt and current maturities of long-term obligations	1,016	1,091
TOTAL CURRENT LIABILITIES	286,623	290,327
LONG-TERM DEBT	246,368	272,234
OTHER LONG-TERM OBLIGATIONS	94,994	95,703
SHAREHOLDERS' EQUITY		
Preferred shares	-	-
Common shares	8,372	8,273
Class B common shares	275	278
Additional paid-in-capital	229,917	229,272
Retained earnings	363,104	346,272
Accumulated other comprehensive earnings	96,403	174,204
Treasury shares	(63,519)	(57,062)
TOTAL SHAREHOLDERS' EQUITY	634,552	701,237
	\$ 1,262,537	\$ 1,359,501

TOTAL LIABILITIES AND SHAREHOLDERS'
EQUITY

See notes to condensed consolidated financial statements.

Index

INVACARE CORPORATION AND SUBSIDIARIES
Condensed Consolidated Statement of Operations - (unaudited)

(In thousands except per share data)	Three Months Ended September 30,		Nine Months Ended September 30,	
	2010	2009	2010	2009
Net sales	\$ 437,476	\$ 434,031	\$ 1,270,544	\$ 1,244,567
Cost of products sold	305,909	302,577	894,774	886,590
Gross profit	131,567	131,454	375,770	357,977
Selling, general and administrative expense	101,946	104,344	308,143	296,416
Loss on debt extinguishment including debt finance charges and associated fees	3,711	-	22,145	-
Charge related to restructuring activities	-	1,857	-	3,757
Interest expense	5,172	7,760	17,334	26,096
Interest income	(185)	(283)	(495)	(1,076)
Earnings before income taxes	20,923	17,776	28,643	32,784
Income taxes	5,325	4,300	10,550	9,250
NET EARNINGS	\$ 15,598	\$ 13,476	\$ 18,093	\$ 23,534
DIVIDENDS DECLARED PER COMMON SHARE	.0125	.0125	.0375	.0375
Net earnings per share – basic	\$ 0.48	\$ 0.42	\$ 0.56	\$ 0.74
Weighted average shares outstanding - basic	32,431	31,970	32,389	31,945
Net earnings per share – assuming dilution	\$ 0.48	\$ 0.42	\$ 0.56	\$ 0.74
Weighted average shares outstanding - assuming dilution	32,524	32,004	32,529	31,952

See notes to condensed consolidated financial statements.

Index

INVACARE CORPORATION AND SUBSIDIARIES
Condensed Consolidated Statement of Cash Flows - (unaudited)

	Nine Months Ended September 30,	
	2010	2009
	(In thousands)	
OPERATING ACTIVITIES		
Net earnings	\$ 18,093	\$ 23,534
Adjustments to reconcile net earnings to net cash provided by operating activities:		
Amortization of convertible debt discount	2,487	3,062
Loss on debt extinguishment including debt finance charges and associated fees	22,145	-
Depreciation and amortization	27,212	29,852
Provision for losses on trade and installment receivables	12,472	14,157
Provision for other deferred liabilities	2,106	1,976
Provision (benefit) for deferred income taxes	(214)	460
Provision for stock-based compensation	5,293	3,310
Gain on disposals of property and equipment	20	379
Changes in operating assets and liabilities:		
Trade receivables	(7,221)	9,782
Installment sales contracts, net	(1,730)	(2,821)
Inventories	(17,344)	6,131
Other current assets	1,799	9,257
Accounts payable	7,591	9,613
Accrued expenses	(387)	(22,585)
Other deferred liabilities	2,158	(100)
NET CASH PROVIDED BY OPERATING ACTIVITIES	74,480	86,007
INVESTING ACTIVITIES		
Purchases of property and equipment	(11,325)	(10,516)
Proceeds from sale of property and equipment	26	1,111
Other long term assets	1,058	(461)
Business acquisitions, net of cash acquired	(13,725)	-
Other	(629)	(270)
NET CASH USED FOR INVESTING ACTIVITIES	(24,595)	(10,136)
FINANCING ACTIVITIES		
Proceeds from revolving lines of credit and long-term borrowings	341,602	274,420
Payments on revolving lines of credit and long-term debt and capital lease obligations	(393,635)	(373,335)
Proceeds from exercise of stock options	1,137	1,001
Payment of dividends	(1,212)	(1,201)
NET CASH USED BY FINANCING ACTIVITIES	(52,108)	(99,115)

Edgar Filing: INVACARE CORP - Form 10-Q

Effect of exchange rate changes on cash	(3,189)	3,549
Decrease in cash and cash equivalents	(5,412)	(19,695)
Cash and cash equivalents at beginning of period	37,501	47,516
Cash and cash equivalents at end of period	\$ 32,089	\$ 27,821

See notes to condensed consolidated financial statements.

Index

INVACARE CORPORATION AND SUBSIDIARIES
Notes to Condensed Consolidated
Financial Statements
(Unaudited)
September 30, 2010

Nature of Operations - Invacare Corporation is the world's leading manufacturer and distributor in the estimated \$8.0 billion worldwide market for medical equipment and supplies used in the home based upon the Company's distribution channels, breadth of product line and net sales. The Company designs, manufactures and distributes an extensive line of health care products for the non-acute care environment, including the home health care, retail and extended care markets.

Principles of Consolidation - The consolidated financial statements include the accounts of the Company and its wholly owned subsidiaries and include all adjustments, which were of a normal recurring nature, necessary to present fairly the financial position of the Company as of September 30, 2010, the results of its operations for the three and nine months ended September 30, 2010 and changes in its cash flow for the nine months ended September 30, 2010 and 2009 respectively. Certain foreign subsidiaries, represented by the European segment, are consolidated using an August 31 quarter end in order to meet filing deadlines. No material subsequent events have occurred related to the European segment, which would require disclosure or adjustment to the Company's financial statements. All significant intercompany transactions are eliminated. The results of operations for the three and nine months ended September 30, 2010 are not necessarily indicative of the results to be expected for the full year.

Recent Accounting Pronouncements - On January 21, 2010, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update No. 2010-06, Improving Disclosures about Fair Value Measurements (ASU 2010-06). The ASU 2010-06 amends ASC 820 to require a number of additional disclosures regarding fair value measurements. The amended guidance requires entities to disclose additional information regarding assets and liabilities that are transferred between levels of the fair value hierarchy. Entities are also required to disclose information in the Level 3 roll forward about purchases, sales, issuances and settlements on a gross basis. In addition to these new disclosure requirements, ASU 2010-06 also amends Topic 820 to further clarify existing guidance pertaining to the level of disaggregation at which fair value disclosures should be made and the requirements to disclose information about the valuation techniques and inputs used in estimating Level 2 and Level 3 fair value measurements. The Company adopted ASU 2010-06 effective January 1, 2010 and it was utilized in preparing the fair value measurement disclosures.

On July 21, 2010, the FASB issued Accounting Standards Update No. 2010-20, Disclosures about the Credit Quality of Financing Receivables and the Allowance for Credit Losses (ASU 2010-20). ASU 2010-20 requires entities to provide additional disclosures regarding credit-risk exposures, including how credit risk is analyzed and assessed, and allowances for credit losses, including reasons for changes each period. The Company is analyzing the impact of ASU 2010-20, which is currently expected to impact the Company's installment receivable disclosures in the Company's 2010 Form 10-K. The Company does not believe ASU 2010-20 will have any material impact on the Company's financial position, results of operations or cash flows.

Use of Estimates - The consolidated financial statements are prepared in conformity with accounting principles generally accepted in the United States, which require management to make estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes. Actual results may differ from these estimates.

Business Segments - The Company operates in five primary business segments: North America/Home Medical Equipment (NA/HME), Invacare Supply Group (ISG), Institutional Products Group (IPG), Europe and Asia/Pacific.

The NA/HME segment sells each of three primary product lines, which includes: standard, rehab and respiratory products. Invacare Supply Group sells distributed product and the Institutional Products Group sells health care furnishings and accessory products. Europe and Asia/Pacific sell the same product lines as NA/HME and the Institutional Products Group. Each business segment sells to the home health care, retail and extended care markets.

The Company evaluates performance and allocates resources based on profit or loss from operations before income taxes for each reportable segment. The accounting policies of each segment are the same as those described in the summary of significant accounting policies for the Company's consolidated financial statements. Intersegment sales and transfers are based on the costs to manufacture plus a reasonable profit element. Therefore, intercompany profit or loss on intersegment sales and transfers is not considered in evaluating segment performance, except for Asia/Pacific due to its significant intercompany sales volume.

Index

The information by segment is as follows (in thousands):

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2010	2009	2010	2009
Revenues from external customers				
North America / HME	\$ 190,925	\$ 185,072	\$ 556,000	\$ 559,851
Invacare Supply Group	75,201	70,825	217,745	204,688
Institutional Products Group	19,777	23,462	64,755	67,469
Europe	128,613	134,604	369,446	360,209
Asia/Pacific	22,960	20,068	62,598	52,350
Consolidated	\$ 437,476	\$ 434,031	\$ 1,270,544	\$ 1,244,567
Intersegment Revenues				
North America / HME	\$ 20,717	\$ 21,775	\$ 64,060	\$ 50,549
Invacare Supply Group	29	16	61	214
Institutional Products Group	1,335	561	4,332	1,711
Europe	2,036	2,868	7,369	6,719
Asia/Pacific	8,821	7,331	24,605	22,724
Consolidated	\$ 32,938	\$ 32,551	\$ 100,427	\$ 81,827
Charge related to restructuring before income taxes				
North America / HME	\$ -	\$ (80)	\$ -	\$ 255
Invacare Supply Group	-	60	-	60
Institutional Products Group	-	-	-	171
Europe	-	1,810	-	2,434
Asia/Pacific	-	365	-	1,135
Consolidated	\$ -	\$ 2,155	\$ -	\$ 4,055
Earnings (loss) before income taxes				
North America / HME	\$ 15,091	\$ 9,679	\$ 37,117	\$ 24,986
Invacare Supply Group	2,249	1,567	4,448	3,442
Institutional Products Group	1,864	3,629	7,002	6,721
Europe	12,769	12,372	26,596	23,393
Asia/Pacific	2,893	468	6,244	131
All Other *	(13,943)	(9,939)	(52,764)	(25,889)
Consolidated	\$ 20,923	\$ 17,776	\$ 28,643	\$ 32,784

* "All Other" consists of un-allocated corporate selling, general and administrative costs, which do not meet the quantitative criteria for determining reportable segments. In addition, "All Other" loss before income taxes includes loss on debt extinguishment including finance charges and associated fees.

Index

Net Earnings Per Common Share - The following table sets forth the computation of basic and diluted net earnings per common share for the periods indicated (amounts in thousands, except per share amounts).

	Three Months Ended		Nine Months Ended	
	September 30,		September 30,	
	2010	2009	2010	2009
	(In thousands, except per share data)			
Basic				
Average common shares outstanding	32,431	31,970	32,389	31,945
Net earnings	\$ 15,598	\$ 13,476	\$ 18,093	\$ 23,534
Net earnings per common share	\$ 0.48	\$ 0.42	\$ 0.56	\$ 0.74
Diluted				
Average common shares outstanding	32,431	31,970	32,389	31,945
Stock options and awards	93	34	99	7
Shares related to convertible debt	-	-	41	-
Average common shares assuming dilution	32,524	32,004	32,529	31,952
Net earnings	\$ 15,598	\$ 13,476	\$ 18,093	\$ 23,534
Net earnings per common share	\$ 0.48	\$ 0.42	\$ 0.56	\$ 0.74

At September 30, 2010, 3,877,362 and 3,425,015 shares were excluded from the average common shares assuming dilution for the three and nine months ended September 30, 2010, respectively, as they were anti-dilutive. At September 30, 2009, 4,436,375 and 4,778,393 shares were excluded from the average common shares assuming dilution for the three and nine months ended September 30, 2009, respectively, as they were anti-dilutive. For the three and nine months ended September 30, 2010, the majority of the anti-dilutive shares were granted at an exercise price of \$25.24 which was higher than the average fair market value prices of \$23.28 and \$24.99, respectively. For the three and nine months ended September 30, 2009, the majority of the anti-dilutive shares were granted at an exercise price of \$41.87 which was higher than the average fair market value prices of \$20.41 and \$17.87, respectively. For the nine months ended September 30, 2010, the Company included the impact of 41,000 shares necessary to settle the conversion spread related to the Company's 4.125% Senior Subordinated Convertible Debentures due 2027. This is attributable to the Company's average stock price during the first nine months being greater than the conversion price of \$24.79, established under the indenture governing the convertible debentures.

Concentration of Credit Risk - The Company manufactures and distributes durable medical equipment and supplies to the home health care, retail and extended care markets. The Company performs credit evaluations of its customers' financial condition. In December 2000, Invacare entered into an agreement with De Lage Landen, Inc. ("DLL"), a third party financing company, to provide the majority of future lease financing to Invacare's North America customers. The DLL agreement provides for direct leasing between DLL and the Invacare customer. The Company retains a recourse obligation to DLL, which was \$26,439,000 at September 30, 2010, for events of default under the contracts, which total \$70,347,000 at September 30, 2010. Guarantees, ASC 460, requires the Company to record a guarantee liability

as it relates to the limited recourse obligation. As such, the Company has recorded a liability of \$670,000 for this guarantee obligation within accrued expenses. The Company monitors the collections status of these contracts and has provided amounts for estimated losses in its allowances for doubtful accounts in accordance with Receivables, ASC 310-10-05-4. Credit losses are provided for in the financial statements.

Substantially all of the Company's receivables are due from health care, medical equipment providers and long term care facilities located throughout the United States, Australia, Canada, New Zealand and Europe. A significant portion of products sold to dealers, both foreign and domestic, is ultimately funded through government reimbursement programs such as Medicare and Medicaid and the Company has seen a significant shift in reimbursement to customers from managed care entities. Government reimbursement program changes such as the Competitive Bidding Program in the U.S., announced in the second quarter of 2010 (which is scheduled to start January 1, 2011 in nine metropolitan statistical areas (MSAs)), can have a significant impact on the collectability of accounts receivable for those customers which are in the MSA locations impacted and which have a portion of their revenues tied to Medicare reimbursement. Changes in reimbursement programs can have an adverse impact on dealer liquidity and profitability. In addition, reimbursement guidelines in the home health care industry have a substantial impact on the nature and type of equipment an end user can obtain as well as the timing of reimbursement and, thus, affect the product mix, pricing and payment patterns of the Company's customers.

Index

Goodwill and Other Intangibles - The decrease in goodwill reflected on the balance sheet from December 31, 2009 to September 30, 2010 was the result of foreign currency translation offset by an increase of \$6,290,000 as the result of an acquisition included in the Institutional Products Group segment for which the entire amount is deductible for tax purposes.

All of the Company's other intangible assets have been assigned definite lives and continue to be amortized over their useful lives, except for \$30,517,000 related to trademarks, which have indefinite lives. The changes in intangible balances reflected on the balance sheet from December 31, 2009 to September 30, 2010 were the result of foreign currency translation and amortization except for \$2,430,000 recorded for customer lists as the result of an acquisition made during the second quarter of 2010 which is included in the Institutional Products Group segment.

As of September 30, 2010 and December 31, 2009, other intangibles consisted of the following (in thousands):

	September 30, 2010		December 31, 2009	
	Historical Cost	Accumulated Amortization	Historical Cost	Accumulated Amortization
Customer lists	\$ 71,677	\$ 37,360	\$ 78,780	\$ 36,359
Trademarks	30,517	—	34,953	—
License agreements	3,126	2,909	4,326	4,051
Developed technology	8,377	3,770	7,409	2,434
Patents	7,321	5,603	7,020	5,246
Other	6,009	5,310	5,905	4,998
	\$ 127,027	\$ 54,952	\$ 138,393	\$ 53,088

Amortization expense related to other intangibles was \$6,035,000 in the first nine months of 2010 and is estimated to be \$8,093,000 in 2010, \$8,116,000 in 2011, \$7,929,000 in 2012, \$6,651,000 in 2013, \$6,387,000 in 2014 and \$5,273,000 in 2015. Definite lived intangibles are being amortized on a straight-line basis for periods from 3 to 20 years with the majority of the intangibles being amortized over a life of between 10 and 13 years.

Accounting for Stock-Based Compensation - The Company accounts for share based compensation under the provisions of Compensation—Stock Compensation, ASC 718. The Company has not made any modifications to the terms of any previously granted options and no significant changes have been made regarding the valuation methodologies used to determine the fair value of options granted since 2005 and the Company continues to use a Black-Scholes valuation model.

The substantial majority of the options awarded have been granted at exercise prices equal to the market value of the underlying stock on the date of grant. Restricted stock awards granted without cost to the recipients are expensed on a straight-line basis over the vesting periods based on the market value at the date of grant.

The amounts of stock-based compensation expense recognized were as follows (in thousands):

	Three Months Ended		Nine Months Ended	
	September 30, 2010	September 30, 2009	September 30, 2010	September 30, 2009
Stock-based compensation expense recognized as part of selling, general and administrative expense	\$ 2,453	\$ 1,528	\$ 5,293	\$ 3,310

The amounts above reflect compensation expense related to restricted stock awards and nonqualified stock options awarded under the 2003 Performance Plan (the "2003 Plan"). Stock-based compensation is not allocated to the business segments, but is reported as part of All Other as shown in the Company's Business Segment Note to the Consolidated Financial Statements.

Stock Incentive Plans - The 2003 Plan allows the Compensation and Management Development Committee of the Board of Directors (the "Committee") to grant up to 6,800,000 Common Shares in connection with incentive stock options, non-qualified stock options, stock appreciation rights and stock awards (including the use of restricted stock). The Committee has the authority to determine which employees and directors will receive awards, the amount of the awards and the other terms and conditions of the awards. During the first nine months of 2010, the Committee granted 613,207 non-qualified stock options with a term of ten years at the fair market value of the Company's Common Shares on the date of grant under the 2003 Plan, which vest ratably in annual installments over the four years following the grant date.

Under the terms of the Company's outstanding restricted stock awards, all of the shares granted vest ratably over the four years after the grant date. Compensation expense of \$1,478,000 was recognized related to restricted stock awards in the first nine months of 2010 and as of September 30, 2010, outstanding restricted stock awards totaling 331,220 were not yet vested.

Index

As of September 30, 2010, there was \$16,864,000 of total unrecognized compensation cost from stock-based compensation arrangements granted under the 2003 Plan, which is related to non-vested options and shares, and includes \$5,692,000 related to restricted stock awards. The Company expects the compensation expense to be recognized over a four-year period for a weighted-average period of approximately two years.

Stock option activity during the nine months ended September 30, 2010 was as follows:

	2010	Weighted Average Exercise Price
Options outstanding at January 1	4,619,528	\$ 29.28
Granted	613,207	25.24
Exercised	(298,338)	23.31
Canceled	(358,576)	24.92
Options outstanding at September 30	4,575,821	\$ 29.47
Options price range at September 30	\$ 10.70 to	
	\$ 47.80	
Options exercisable at September 30	3,011,917	
Options available for grant at September 30*	2,478,035	

* Options available for grant as of September 30, 2010 reduced by net restricted stock award activity of 491,578.

The following table summarizes information about stock options outstanding at September 30, 2010:

Exercise Prices	Options Outstanding			Options Exercisable	
	Number Outstanding At 9/30/10	Weighted Average Remaining Contractual Life	Weighted Average Exercise Price	Number Exercisable At 9/30/10	Weighted Average Exercise Price
10.70 - \$ 14.89	23,892	1.8 years	\$ 10.83	23,142	\$ 10.70
16.55 - \$ 24.43	1,505,963	7.5	\$ 21.66	830,844	\$ 22.31
24.90 - \$ 36.40	1,888,075	6.2	\$ 28.53	1,000,040	\$ 31.29
37.70 - \$ 47.80	1,157,891	3.9	\$ 41.53	1,157,891	\$ 41.53
Total	4,575,821	6.0	\$ 29.47	3,011,917	\$ 32.59

When stock options are awarded, they generally become exercisable over a four-year vesting period whereby options vest in equal installments each year. Options granted with graded vesting are accounted for as single options. The fair value of each option grant is estimated on the date of grant using the Black-Scholes option-pricing model with assumptions for expected dividend yield, expected stock price volatility, risk-free interest rate and expected life. The assumed expected life is based on the Company's historical analysis of option history. The expected stock price volatility is also based on actual historical volatility, and expected dividend yield is based on historical dividends as the Company has no current intention of changing its dividend policy.

The 2003 Plan provides that shares granted come from the Company's authorized but unissued Common Shares or treasury shares. In addition, the Company's stock-based compensation plans allow employee participants to exchange shares for minimum withholding taxes, which results in the Company acquiring treasury shares.

Warranty Costs - Generally, the Company's products are covered from the date of sale to the customer by warranties against defects in material and workmanship for various periods depending on the product. Certain components carry a lifetime warranty. A provision for estimated warranty cost is recorded at the time of sale based upon actual experience. The Company continuously assesses the adequacy of its product warranty accrual and makes adjustments as needed. Historical analysis is primarily used to determine the Company's warranty reserves. Claims history is reviewed and provisions are adjusted as needed. However, the Company does consider other events, such as a product recall, which could warrant additional warranty reserve provision. No material adjustments to warranty reserves were necessary in the first nine months of 2010.

The following is a reconciliation of the changes in accrued warranty costs for the reporting period (in thousands):

Balance as of January 1, 2010	\$	21,506
Warranties provided during the period		4,431
Settlements made during the period		(7,366)
Changes in liability for pre-existing warranties during the period, including expirations		318
Balance as of September 30, 2010	\$	18,889

Index

Long-Term Debt - On May 9, 2008, Staff Position APB 14-1, Accounting for Convertible Debt Instruments That May Be Settled in Cash upon Conversion (Including Partial Cash Settlement) (FSP APB 14-1) as codified in Debt with Conversion and Other Options, ASC 470-20, was issued to provide clarification of the accounting for convertible debt that can be settled in cash upon conversion. The FASB believed this clarification was needed because the accounting that was being applied for convertible debt prior to FSP APB 14-1 did not fully reflect the true economic impact on the issuer since the conversion option was not captured as a borrowing cost and its full dilutive effect was not included in earnings per share. ASC 470-20 required separate accounting for the liability and equity components of the convertible debt in a manner that would reflect Invacare's nonconvertible debt borrowing rate. Accordingly, the Company initially split the total debt amount of \$135,000,000 attributable to its 4.125% Convertible Senior Subordinated Debentures due 2027 into a convertible debt amount of \$75,988,000 and a stockholders' equity (debt discount) amount of \$59,012,000 as of the retrospective adoption date of February 12, 2007 and is accreting the resulting debt discount as interest expense over a ten year life. The Consolidated Balance Sheet as of September 30, 2010 reflects a decrease in long-term debt of \$27,073,000 and a deferred tax liability of \$9,476,000 offset by a valuation reserve of the same amount compared to comparable amounts of \$48,272,000 and \$16,895,000, respectively, as of December 31, 2009.

During the three and nine months ended September 30, 2010, the Company paid down \$8,158,000 and \$83,061,000 par value of senior and convertible debt, respectively. Debt pay down for the three and nine months ended September 30, 2010 was \$8,158,000 (\$4,631,000 reduction of debt and \$3,527,000 reduction of equity) and \$54,061,000 (\$32,862,000 reduction of debt and \$21,199,000 reduction of equity), respectively, related to its 4.125% Convertible Senior Subordinated Debentures due 2027. Debt pay down for the nine months ended September 30, 2010 was \$29,000,000 related to its 9 3/4% Senior Notes due 2015. The Company retired the debt at a premium above par. In accordance with Convertible Debt, ASC 470-20, the Company utilized the inducement method of accounting to calculate the loss associated with the early retirement of the convertible debt. For the three and nine months ended September 30, 2010, the Company recorded pre-tax expense of \$3,711,000 and \$22,145,000, respectively, related to the loss on the debt extinguishment including the write-off of \$209,000 and \$2,094,000, respectively, of pre-tax of deferred financing fees, which were previously capitalized.

The Company utilized primarily its cash and cash flows from operations as well as its revolving line of credit to pay down the debt noted above. At September 30, 2010, the Company had outstanding \$39,500,000 on its revolving line of credit compared to \$1,725,000 as of December 31, 2009.

Charges Related to Restructuring Activities - On July 28, 2005, the Company announced multi-year cost reductions and profit improvement actions, which included: reducing global headcount, outsourcing improvements utilizing the Company's China manufacturing capability and third parties, shifting substantial resources from product development to manufacturing cost reduction activities and product rationalization, reducing freight exposure through freight auctions and changing the freight policy, general expense reductions and exiting four facilities. The restructuring was necessitated by the continued decline in reimbursement by the U.S. government as well as similar reimbursement pressures abroad and continued pricing pressures faced by the Company as a result of outsourcing by competitors to lower cost locations.

The Company's previous restructuring activities concluded in the fourth quarter of 2009 thus no additional charges were incurred in the first nine months of 2010. There are no material accrual balances related to the charge remaining as of September 30, 2010.

Index

A progression of the accruals by segment recorded as a result of the restructuring is as follows (in thousands):

	Severance	Product Line Discontinuance	Contract Terminations	Other	Total
December 31, 2009					
Balance					
NA/HME	46	1	23	—	70
IPG	5	—	—	—	5
Europe	816	—	—	343	1,159
Asia/Pacific	42	—	—	—	42
Total	\$ 909	\$ 1	\$ 23	\$ 343	\$ 1,276
Payments					
NA/HME	(46)	(1)	(23)	—	(70)
IPG	(5)	—	—	—	(5)
Europe	(816)	—	—	(343)	(1,159)
Asia/Pacific	(42)	—	—	—	(42)
Total	\$ (909)	\$ (1)	\$ (23)	\$ (343)	\$ (1,276)
September 30, 2010					
Balance					
NA/HME	—	—	—	—	—
IPG	—	—	—	—	—
Europe	—	—	—	—	—
Asia/Pacific	—	—	—	—	—
Total	\$ —	\$ —	\$ —	\$ —	\$ —

Comprehensive Earnings (loss) - Total comprehensive earnings (loss) were as follows (in thousands):

	Three Months Ended		Nine Months Ended	
	September 30,		September 30,	
	2010	2009	2010	2009
Net earnings	\$ 15,598	\$ 13,476	\$ 18,093	\$ 23,534
Foreign currency translation gain (loss)	31,438	22,544	(79,449)	94,494
Unrealized gain on available for sale securities	-	115	-	162
SERP/DBO amortization of prior service costs and unrecognized losses	29	249	337	440
Current period unrealized gain (loss) on cash flow hedges, net of tax	(1,056)	1,124	1,311	3,061
Total comprehensive earnings (loss)	\$ 46,009	\$ 37,508	\$ (59,708)	\$ 121,691

Inventories - Inventories determined under the first in, first out method consist of the following components (in thousands):

	September 30, 2010	December 31, 2009
Finished goods	\$ 107,764	\$ 99,701

Edgar Filing: INVACARE CORP - Form 10-Q

Raw Materials	63,218	59,451
Work in Process	11,615	13,070
	\$ 182,597	\$ 172,222

Property and Equipment - Property and equipment consist of the following (in thousands):

	September 30, 2010	December 31, 2009
Machinery and equipment	\$ 327,550	\$ 329,181
Land, buildings and improvements	89,811	98,160
Furniture and fixtures	26,383	26,635
Leasehold improvements	16,285	14,744
	460,029	468,720
Less allowance for depreciation	(329,992)	(327,087)
	\$ 130,037	\$ 141,633

Index

Acquisitions- In June 2010, Invacare Corporation acquired an equipment rental Company focused on skilled nursing and long-term care providers for \$13,725,000, which was paid in cash. Pursuant to the purchase agreement, the Company agreed to pay contingent consideration of up to \$1,000,000 if certain revenue growth and earnings projections are met for which the Company has estimated a de minimis fair value based on the Company's assessment of the probability of payout. In October 2008, Invacare Corporation purchased a billing Company operating as Homecare Collection Services (HCS) for \$6,268,000. Pursuant to the HCS purchase agreement, the Company agreed to pay contingent consideration based upon earnings before interest, taxes and depreciation over the three years subsequent to the acquisition up to a maximum of \$3,000,000. When the contingency related to the acquisition is determinable, any additional consideration paid will increase the respective purchase price and reported goodwill. No contingent consideration was payable based on the results of HCS in the first year.

Derivatives -Derivatives and Hedging, ASC 815, requires companies to recognize all derivative instruments in the consolidated balance sheet as either assets or liabilities at fair value. The accounting for changes in fair value of a derivative is dependent upon whether or not the derivative has been designated and qualifies for hedge accounting treatment and the type of hedging relationship. For derivatives designated and qualifying as hedging instruments, the Company must designate the hedging instrument, based upon the exposure being hedged, as a fair value hedge, cash flow hedge, or a hedge of a net investment in a foreign operation.

Cash Flow Hedging Strategy

The Company uses derivative instruments in an attempt to manage its exposure to commodity price risk, foreign currency exchange risk and interest rate risk. Foreign exchange contracts are used to manage the price risk associated with forecasted sales denominated in foreign currencies and the price risk associated with forecasted purchases of inventory over the next twelve months. Interest rate swaps are, at times, utilized to manage interest rate risk associated with the Company's fixed and floating-rate borrowings.

The Company recognizes its derivative instruments as assets or liabilities in the consolidated balance sheet measured at fair value. A majority of the Company's derivative instruments are designated and qualify as cash flow hedges. Accordingly, the effective portion of the gain or loss on the derivative instrument is reported as a component of other comprehensive income and reclassified into earnings in the same period or periods during which the hedged transaction affects earnings. The remaining gain or loss on the derivative instrument in excess of the cumulative change in the fair value of the hedged item, if any, is recognized in current earnings during the period of change.

The Company was not a party to any interest rate swap agreements during 2010. During 2009, the Company was a party to interest rate swap agreements that qualified as cash flow hedges and effectively converted floating-rate debt to fixed-rate debt, so the Company could avoid the risk of changes in market interest rates. The gains and or losses on interest rate swaps are reflected in interest expense on the consolidated statement of operations.

To protect against increases/decreases in forecasted foreign currency cash flows resulting from inventory purchases/sales over the next year, the Company utilizes foreign currency forward contracts to hedge portions of its forecasted purchases/sales denominated in foreign currencies. The gains and losses are included in cost of products sold and selling, general and administrative expenses on the consolidated statement of operations. If it is later determined that a hedged forecasted transaction is unlikely to occur, any gains or losses on the forward contracts associated with the forecasted transactions that are no longer probable of occurring would be reclassified from other comprehensive income into earnings. The Company does not expect any material amount of hedge ineffectiveness related to forward contract cash flow hedges during the next twelve months.

The Company has historically not recognized any material amount of ineffectiveness related to forward contract cash flow hedges because the Company generally limits its hedges to between 60% and 90% of total forecasted transactions for a given entity's exposure to currency rate changes and the transactions hedged are recurring in nature. Furthermore, the majority of the hedged transactions are related to intercompany sales and purchases for which settlement occurs on a specific day each month. Forward contracts with a total notional amount in USD of \$42,210,000 and \$124,292,000 matured during the three and nine months ended September 30, 2010, respectively.

Index

Foreign exchange forward contracts qualifying and designated for hedge accounting treatment were as follows (in thousands USD):

	September 30, 2010		December 31, 2009	
	Notional Amount	Unrealized Gain (Loss)	Notional Amount	Unrealized Gain (Loss)
USD / AUD	\$ 2,529	\$ (103)	\$ 3,294	\$ (41)
USD / CAD	46,011	100	49,345	202
USD / EUR	7,806	894	22,119	(526)
USD / GBP	1,134	54	3,640	(72)
USD / NZD	2,354	116	8,286	130
USD / SEK	2,681	67	8,965	(100)
USD / MXN	3,210	288	2,520	217
EUR / CHF	2,850	(127)	2,755	(9)
EUR / GBP	4,767	(336)	22,258	27
EUR / SEK	1,217	35	3,800	15
EUR / NZD	3,040	193	8,029	359
GBP / CHF	114	8	501	14
GBP / SEK	526	9	2,169	37
GBP / DKK	44	(3)	765	17
DKK / CHF	124	(15)	-	-
DKK / SEK	1,824	(57)	7,439	52
DKK / NOK	509	(29)	2,236	19
NOK / EUR	-	-	342	6
NOK / CHF	386	38	592	(9)
NOK / SEK	286	6	1,190	(21)
	\$ 81,412	\$ 1,138	\$ 150,245	\$ 317

Fair Value Hedging Strategy

In 2010 and 2009, the Company did not utilize any derivatives designated as fair value hedges. However, the Company has in the past utilized fair value hedges in the form of forward contracts to manage the foreign exchange risk associated with certain firm commitments and has entered into interest rate swaps to effectively convert fixed-rate debt to floating-rate debt in an attempt to avoid paying higher than market interest rates. For derivative instruments designated and qualifying as fair value hedges, the gain or loss on the derivative instrument as well as the offsetting gain or loss on the hedged item associated with the hedged risk are recognized in the same line item associated with the hedged item in earnings.

Derivatives Not Qualifying or Designated for Hedge Accounting Treatment

The Company also utilizes foreign currency forward contracts that are not designated as hedges in accordance with ASC 815 although they could qualify for hedge accounting treatment. These contracts are entered into to eliminate the risk associated with the settlement of short-term intercompany trading receivables and payables between Invacare Corporation and its foreign subsidiaries. The currency forward contracts are entered into at the same time as the intercompany receivables or payables are created so that upon settlement, the gain/loss on the settlement is offset by the gain/loss on the foreign currency forward contract. No material net gain or loss was realized by the Company for the quarter or nine month period ended September 30, 2010 related to these forward contracts and the associated short-term intercompany trading receivables and payables.

Index

Foreign exchange forward contracts not qualifying or designated for hedge accounting treatment entered into in and outstanding as of September 30, 2010 and 2009 were as follows (in thousands USD):

	September 30, 2010		September 30, 2009	
	Notional Amount	Gain (Loss)	Notional Amount	Gain (Loss)
CAD / USD	\$ 10,414	\$ 281	\$ 16,052	\$ 289
NZD / USD	13,403	18	6,161	(37)
NOK / USD	1,327	35	-	-
SEK / USD	13,380	426	24,799	25
DKK / USD	4,233	161	-	-
EUR / USD	16,948	789	12,022	202
EUR / GBP	839	(59)	-	-
EUR / SEK	72	(5)	-	-
	\$ 60,616	\$ 1,646	\$ 59,034	\$ 479

The fair values of the Company's derivative instruments were as follows (in thousands):

	September 30, 2010		December 31, 2009	
	Assets	Liabilities	Assets	Liabilities
Derivatives designated as hedging instruments under ASC 815				
Foreign currency forward contracts	\$ 2,345	\$ 1,207	\$ 1,815	\$ 1,498
Derivatives not designated as hedging instruments under ASC 815				
Foreign currency forward contracts	1,725	79	92	675
Total derivatives	\$ 4,070	\$ 1,286	\$ 1,907	\$ 2,173

The fair values of the Company's foreign currency forward assets and liabilities are included in Other Current Assets and Accrued Expenses, respectively in the Consolidated Balance Sheets.

The effect of derivative instruments on the Statement of Operations and Other Comprehensive Income (OCI) for the quarter and nine months ended September 30, 2010 was as follows (in thousands):

	Amount of Gain (Loss) Recognized in OCI on Derivatives (Effective Portion)	Amount of Gain (Loss) Reclassified from Accumulated OCI into Income (Effective Portion)	Amount of Gain (Loss) Recognized in Income on Derivatives (Ineffective Portion and Amount Excluded from Effectiveness Testing)
	Derivatives in ASC 815 cash flow hedge relationships		
Quarter ended September 30, 2010:			
Foreign currency forward contracts	\$ (2,429)	\$ 1,065	\$ (29)

Nine months ended September
30, 2010:

Foreign currency forward contracts	\$	(1,091))	\$	1,844	\$	(68)
------------------------------------	----	---------	---	----	-------	----	------

Quarter ended September 30,
2009:

Foreign currency forward contracts	\$	954	\$	(345)	\$	-
Interest rate swap contracts		857		(426)		-
	\$	1,811	\$	(771)	\$	-

Nine months ended September
30, 2009:

Foreign currency forward contracts	\$	587	\$	(277)	\$	-
Interest rate swap contracts		5,556		(2,819)		-
	\$	6,143	\$	(3,096)	\$	-

Index

Derivatives not designated as hedging instruments under ASC 815	Amount of Gain (Loss) Recognized in Income on Derivatives	
Quarter ended September 30, 2010:		
Foreign currency forward contracts	\$	1,901
Nine months ended September 30, 2010:		
Foreign currency forward contracts	\$	1,389
Quarter ended September 30, 2009:		
Foreign currency forward contracts	\$	(78)
Nine months ended September 30, 2009:		
Foreign currency forward contracts	\$	2,425

The gains or losses recognized as the result of the settlement of cash flow hedge foreign currency forward contracts are recognized in net sales for hedges of inventory sales or cost of product sold for hedges of inventory purchases. For the quarter and nine months ended September 30, 2010, net sales were increased by \$187,000 and \$734,000, respectively, and cost of product sold was decreased by \$878,000 and \$1,110,000 for net realized gains of \$1,065,000 and \$1,844,000, respectively. For the quarter and nine months ended September 30, 2009, net sales were increased by \$1,583,000 and \$2,413,000, respectively, and cost of product sold was increased by \$1,927,000 and \$2,690,000, respectively, for net realized losses of \$345,000 and \$277,000, respectively. No swap agreements were outstanding in 2010 while swaps were outstanding in 2009 which resulted in losses of \$426,000 and \$2,819,000 for the quarter and nine months ended September 30, 2009 which were recorded in interest expense for those periods.

Gains of \$1,901,000 and \$1,389,000 were recognized in selling, general and administrative (SG&A) expenses in the quarter and nine months ended September 30, 2010, respectively, compared to a loss of \$78,000 and a gain of \$2,425,000 in the quarter and nine months ended September 30, 2009, respectively, on foreign currency forward contracts not designated as hedging instruments, which were substantially offset by foreign currency gains/losses also recorded in SG&A expenses on the intercompany trade payables for which the derivatives were entered into to offset. In addition, losses of \$29,000 and \$68,000 were recognized in the quarter and nine months ended September 30, 2010, respectively, related to derivatives no longer qualifying for hedge accounting treatment as the forecasted transactions hedged by those derivatives are no longer probable of occurring and as a result, the hedging relationship is ineffective. No comparable gain or loss was recognized in the quarter or nine months ended September 30, 2009.

Fair Value Measurements - Pursuant to ASC 820, the inputs used to derive the fair value of assets and liabilities are analyzed and assigned a level of I, II or III, with level I being the highest and level III being the lowest in the hierarchy. Level I inputs are quoted prices in active markets for identical assets or liabilities. Level II inputs are quoted prices for similar assets or liabilities in active markets: quoted prices for identical or similar instruments in markets that are not active; and model-derived valuations in which all significant inputs are observable in active markets. Level III inputs are based on valuations derived from valuation techniques in which one or more significant inputs are unobservable.

The following table provides a summary of the Company's assets and liabilities that are measured on a recurring basis (in thousands):

Basis for Fair Value Measurements at Reporting Date

Edgar Filing: INVACARE CORP - Form 10-Q

	September 30, 2010	Quoted Prices in Active Markets for Identical Assets / (Liabilities) Level I	Significant Other Observable Inputs Level II	Significant Other Unobservable Inputs Level III
Forward Exchange Contracts	\$ 2,784	\$ -	\$ 2,784	\$ -

Forward Contracts: The Company operates internationally and as a result is exposed to foreign currency fluctuations. Specifically, the exposure includes intercompany trade receivables/payables and loans as well as third party sales or purchases. In an attempt to reduce this exposure, foreign currency forward contracts are utilized and accounted for as hedging instruments. The forward contracts are used to hedge various currencies. The Company does not use derivative financial instruments for speculative purposes. Fair values for the Company's foreign exchange forward contracts are based on quoted market prices for contracts with similar maturities.

Index

The carrying amounts and fair values of the Company's financial instruments at September 30, 2010 and December 31, 2009 are as follows (in thousands):

	September 30, 2010		December 31, 2009	
	Carrying Value	Fair Value	Carrying Value	Fair Value
Cash and cash equivalents	\$ 32,089	\$ 32,089	\$ 37,501	\$ 37,501
Other investments	1,547	1,547	1,521	1,521
Installment receivables, net	5,406	5,406	7,106	7,106
Long-term debt (including current maturities of long-term debt) *	(247,384)	(271,868)	(273,325)	(299,288)
Forward contracts in other current assets	4,070	4,070	1,907	1,907
Forward contracts in accrued expenses	(1,286)	(1,286)	(2,173)	(2,173)

* The carrying amounts and fair values exclude convertible debt classified as equity in accordance with FSP APB 14-1 (\$27,073,000 and \$48,272,000 as of September 30, 2010 and December 31, 2009, respectively).

Income Taxes - The Company had an effective tax rate of 25.4% and 36.8% on earnings before tax for the three and nine month periods ended September 30, 2010, respectively, compared to an expected rate at the US statutory rate of 35%. For the three and nine month periods ended September 30, 2009, the Company had an effective rate of 24.2% and 28.2%, respectively, compared to an expected rate at the U.S. statutory rate of 35%. The Company's effective tax rate for the three months ended September 30, 2010 was lower than the U.S. federal statutory rate as a result of foreign earnings taxed at an effective rate lower than the US statutory rate, and a net profit for the quarter related to countries with tax valuation allowances. The Company's effective tax rate for the nine month period ended September 30, 2010 was higher than the US statutory rate due to the negative impact of the Company not being able to record tax benefits related to losses in countries which had tax valuation allowances for the year, more than offsetting the benefit of foreign taxes at rates below the US statutory rate. The Company continued to be in a loss position in the U.S. principally as a result of recording pre-tax expense of \$3,711,000 and \$22,145,000 for the three and nine months ended September 30, 2010, respectively, related to the extinguishment of convertible and senior debt at a premium.

For the three and nine month periods ended September 30, 2009, the effective tax rate was lower than the U.S. federal statutory rate as a result of the negative impact of the Company not being able to record tax benefits related to losses in countries which had tax valuation allowances, which was more than offset by normal tax expense recognized in countries without tax allowances. The Company's foreign subsidiaries, as a group excluding those with tax valuation allowances, recognized an effective tax rate lower than the U.S. statutory rate.

During the third quarter of 2010 the Company settled an outstanding contested audit resulting in a reduction of its unrecognized tax benefits related to positions taken during a prior year of \$1,825,000. Also during the third quarter, the Company agreed with the IRS to reduce a federal refund claim which generated a corresponding increase in tax credit carryforwards of \$1,675,000 for which a full valuation allowance has been recorded.

Subsequent Events - On October 28, 2010, the Company entered into a new credit agreement (the "New Credit Agreement") which provides for a \$400,000,000 senior secured revolving credit facility maturing in October 2015. Pursuant to the terms of the New Credit Agreement, the Company, certain of its foreign subsidiaries and certain additional foreign subsidiaries that may become parties to the New Credit Agreement may from time to time borrow,

repay and re-borrow up to an aggregate outstanding at any one time of \$400,000,000 under the new senior secured revolving credit facility, subject to customary conditions. The New Credit Agreement also provides for the issuance of swing line loans and letters of credit.

A portion of the proceeds from the New Credit Agreement were used to: (a) repay in full all amounts outstanding under the Credit Agreement, dated as of February 12, 2007, among the Company, the guarantors party thereto, and the lenders party thereto and related agreements and documents (as amended, the "Prior Credit Agreement"); (b) finance the Company's repurchase, on November 1, 2020, of \$142,945,000 in outstanding principal amount of the Company's 9 ¾% Senior Notes due 2015 (the "Senior Notes"), in the tender offer for the Senior Notes conducted by the Company and (c) pay related fees and expenses. The proceeds of the borrowings under the New Credit Agreement may otherwise be used to provide working capital and for other general corporate purposes. The prior Credit Agreement was terminated on October 28, 2010.

Borrowings under the new senior secured revolving credit facility will bear interest, at the Company's election, at (i) the London Inter-Bank Offer Rate ("LIBOR") plus a margin; or (ii) a Base Rate Option plus a margin. The applicable margin is based on the Company's leverage ratio and at the time of entry into the New Credit Agreement, the applicable margin was 2.50% per annum for LIBOR loans and 1.50% for the Base Rate Option loans. In addition to interest, the Company is required to pay commitment fees on the unused portion of the senior secured revolving credit facility. The commitment fee rate is initially 0.40% per annum and, like the interest rate spreads, is subject to adjustment thereafter based on the Company's leverage ratio. The obligations of the borrowers under the New Credit Agreement are secured by substantially all of the Company's U.S. assets and are guaranteed by substantially all of the Company's material domestic and foreign subsidiaries.

Index

The New Credit Agreement contains certain covenants that are customary for similar credit arrangements, including covenants relating to, among other things, financial reporting and notification, compliance with laws, preservation of existence, maintenance of books and records, use of proceeds, maintenance of properties and insurance, and limitations on liens, dispositions, issuance of debt, investments, payment of dividends, repurchases of capital stock, acquisitions, transactions with affiliates, and capital expenditures. There also are financial covenants that require the Company to maintain a maximum leverage ratio (consolidated funded indebtedness to consolidated EBITDA, each as defined in the New Credit Agreement) of no greater than 3.50 to 1, and a minimum interest coverage ratio (consolidated EBITDA to consolidated interest charges, each as defined in the New Credit Agreement) of no less than 3.50 to 1. The New Credit Agreement also requires the Company to redeem, purchase or repurchase no less than \$100,000,000 in principal amount of the Senior Notes and/or the Company's 4.125% Convertible Senior Subordinated Debentures due 2027 (the "Convertible Notes") by February 28, 2011, which requirement the Company has satisfied through the repurchase of Senior Notes in the tender offer completed on November 1, 2010. After that date, the Company may redeem, purchase or repurchase the Senior Notes and/or the Convertible Notes so long as no event of default is then occurring or would be caused thereby and the Company's leverage ratio after such redemption, purchase or repurchase is not more than 3.00 to 1.

The New Credit Agreement provides for customary events of default with corresponding grace periods, including, among other things, failure to pay any principal or interest when due, failure to perform or observe covenants, bankruptcy or insolvency events and change of control.

On November 1, 2010, the Company purchased an aggregate of 142,945,000 in principal amount of the Senior Notes in a tender offer conducted by the Company. The Company paid \$1,075.00 for each \$1,000 principal amount of the Senior Notes validly tendered in the tender offer, which included a consent payment of \$30.00 per \$1,000 principal amount of the Senior Notes. The Company also paid accrued and unpaid interest on the purchased Senior Notes up to, but not including, November 1, 2010. After giving effect to the Senior Notes purchased in the tender offer, an aggregate of approximately \$3,055,000 principal amount of the Senior Notes remain outstanding. In connection with tender offer, the Company received a sufficient number of consents to adopt, on November 1, 2010, amendments to the indenture governing the Senior Notes pursuant to a supplemental indenture entered into with the trustee for the Senior Notes. The amendments have eliminated substantially all of the restrictive covenants and reduced the list of potential events that would constitute events of default in the indenture governing the Senior Notes.

Supplemental Guarantor Information - Effective February 12, 2007, substantially all of the domestic subsidiaries (the "Guarantor Subsidiaries") of the Company became guarantors of the indebtedness of Invacare Corporation under its Senior Notes with an initial aggregate principal amount of \$175,000,000 and under its Convertible Notes with an initial aggregate principal amount of \$135,000,000. The majority of the Company's subsidiaries, which are primarily foreign subsidiaries of the Company, are not guaranteeing the indebtedness of the Senior Notes or Convertible Notes (the "Non-Guarantor Subsidiaries"). Each of the Guarantor Subsidiaries has fully and unconditionally guaranteed, on a joint and several basis, to pay principal, premium, and interest related to the Senior Notes and to the Convertible Notes and each of the Guarantor Subsidiaries are directly or indirectly wholly-owned subsidiaries of the Company.

Presented below are the consolidating condensed financial statements of Invacare Corporation (Parent), its combined Guarantor Subsidiaries and combined Non-Guarantor Subsidiaries with their investments in subsidiaries accounted for using the equity method. The Company does not believe that separate financial statements of the Guarantor Subsidiaries are material to investors and accordingly, separate financial statements and other disclosures related to the Guarantor Subsidiaries are not presented.

Index

CONSOLIDATING CONDENSED STATEMENTS OF OPERATIONS

(in thousands)

Three month period ended September 30, 2010	The Company (Parent)	Combined Guarantor Subsidiaries	Combined Non-Guarantor Subsidiaries	Eliminations	Total
Net sales	\$ 105,143	\$ 180,297	\$ 176,793	\$ (24,757)	\$ 437,476
Cost of products sold	73,400	139,855	117,485	(24,831)	305,909
Gross Profit	31,743	40,442	59,308	74	131,567
Selling, general and administrative expenses	32,911	28,784	40,251	-	101,946
Loss on debt extinguishment including debt finance charges and associated fees	3,711	-	-	-	3,711
Income (loss) from equity investee	25,227	8,973	6	(34,206)	-
Interest expense - net	4,170	227	590	-	4,987
Earnings (loss) before Income Taxes	16,178	20,404	18,473	(34,132)	20,923
Income taxes	580	109	4,636	-	5,325
Net Earnings (loss)	\$ 15,598	\$ 20,295	\$ 13,837	\$ (34,132)	\$ 15,598
Three month period ended September 30, 2009					
Net sales	\$ 104,511	\$ 171,241	\$ 181,938	\$ (23,659)	\$ 434,031
Cost of products sold	74,084	133,629	118,540	(23,676)	302,577
Gross Profit	30,427	37,612	63,398	17	131,454
Selling, general and administrative expenses	43,607	21,650	39,087	-	104,344
Charge related to restructuring activities	(80)	60	1,877	-	1,857
Income (loss) from equity investee	33,209	9,365	(3,615)	(38,959)	-
Interest expense - net	6,277	(849)	2,049	-	7,477
Earnings (loss) before Income Taxes	13,832	26,116	16,770	(38,942)	17,776
Income taxes	356	100	3,844	-	4,300
Net Earnings (loss)	\$ 13,476	\$ 26,016	\$ 12,926	\$ (38,942)	\$ 13,476

Index

CONSOLIDATING CONDENSED STATEMENTS OF OPERATIONS

(in thousands)

Nine month period ended September 30, 2010	The Company (Parent)	Combined Guarantor Subsidiaries	Combined Non-Guarantor Subsidiaries	Eliminations	Total
Net sales	\$ 300,383	\$ 535,735	\$ 509,575	\$ (75,149)	\$ 1,270,544
Cost of products sold	212,173	418,825	339,008	(75,232)	894,774
Gross Profit	88,210	116,910	170,567	83	375,770
Selling, general and administrative expenses	100,124	81,987	126,032	-	308,143
Loss on debt extinguishment including debt finance charges and associated fees	22,145	-	-	-	22,145
Income (loss) from equity investee	67,674	17,807	(377)	(85,104)	-
Interest expense - net	13,950	536	2,353	-	16,839
Earnings (loss) before Income Taxes	19,665	52,194	41,805	(85,021)	28,643
Income taxes	1,572	662	8,316	-	10,550
Net Earnings (loss)	\$ 18,093	\$ 51,532	\$ 33,489	\$ (85,021)	\$ 18,093
Nine month period ended September 30, 2009					
Net sales	\$ 288,590	\$ 522,818	\$ 491,486	\$ (58,327)	\$ 1,244,567
Cost of products sold	205,662	411,488	327,891	(58,451)	886,590
Gross Profit	82,928	111,330	163,595	124	357,977
Selling, general and administrative expenses	103,802	80,907	111,707	-	296,416
Charge related to restructuring activities	255	60	3,442	-	3,757
Income (loss) from equity investee	67,216	15,661	(9,848)	(73,029)	-
Interest expense - net	21,467	(2,085)	5,638	-	25,020
Earnings (loss) before Income Taxes	24,620	48,109	32,960	(72,905)	32,784
Income taxes	1,086	300	7,864	-	9,250
Net Earnings (loss)	\$ 23,534	\$ 47,809	\$ 25,096	\$ (72,905)	\$ 23,534

Index

CONSOLIDATING CONDENSED BALANCE SHEETS

(in thousands)	The Company (Parent)	Combined Guarantor Subsidiaries	Combined Non-Guarantor Subsidiaries	Eliminations	Total
September 30, 2010					
Assets					
Current Assets					
Cash and cash equivalents	\$ 4,004	\$ 2,140	\$ 25,945	\$ -	\$ 32,089
Trade receivables, net	94,705	69,864	90,088	-	254,657
Installment receivables, net	-	840	2,498	-	3,338
Inventories, net	44,205	41,611	98,016	(1,235)	182,597
Deferred income taxes	-	-	1,327	-	1,327
Other current assets	16,033	5,948	33,578	(7,251)	48,308
Total Current Assets	158,947	120,403	251,452	(8,486)	522,316
Investment in subsidiaries	1,438,089	613,052	-	(2,051,141)	-
Intercompany advances, net	77,591	705,670	228,478	(1,011,739)	-
Other Assets	39,887	2,239	799	-	42,925
Other Intangibles	1,279	9,105	61,691	-	72,075
Property and Equipment, net	47,005	12,102	70,930	-	130,037
Goodwill	5,022	34,388	455,774	-	495,184
Total Assets	\$ 1,767,820	\$ 1,496,959	\$ 1,069,124	\$ (3,071,366)	\$ 1,262,537
Liabilities and Shareholders' Equity					
Current Liabilities					
Accounts payable	\$ 78,257	\$ 16,608	\$ 50,045	\$ -	\$ 144,910
Accrued expenses	39,475	22,429	81,922	(7,250)	136,576
Accrued income taxes	-	-	4,121	-	4,121
Short-term debt and current maturities of long-term obligations	173	122	721	-	1,016
Total Current Liabilities	117,905	39,159	136,809	(7,250)	286,623
Long-Term Debt	238,418	5	7,945	-	246,368
Other Long-Term Obligations	48,205	23	46,766	-	94,994
Intercompany advances, net	728,740	191,416	91,583	(1,011,739)	-
Total Shareholders' Equity	634,552	1,266,356	786,021	(2,052,377)	634,552
Total Liabilities and Shareholders' Equity	\$ 1,767,820	\$ 1,496,959	\$ 1,069,124	\$ (3,071,366)	\$ 1,262,537

Index

CONSOLIDATING CONDENSED BALANCE SHEETS

(in thousands)	The Company (Parent)	Combined Guarantor Subsidiaries	Combined Non-Guarantor Subsidiaries	Eliminations	Total
December 31, 2009					
Assets					
Current Assets					
Cash and cash equivalents	\$ 6,569	\$ 2,526	\$ 28,406	\$ -	\$ 37,501
Trade receivables, net	101,416	64,451	101,312	(4,165)	263,014
Installment receivables, net	-	954	2,611	-	3,565
Inventories, net	42,512	39,114	91,916	(1,320)	172,222
Deferred income taxes	-	-	390	-	390
Other current assets	15,608	6,307	31,245	(1,388)	51,772
Total Current Assets	166,105	113,352	255,880	(6,873)	528,464
Investment in subsidiaries	1,447,759	594,024			