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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 MARCH 31, 2012**

Commission File Number 001-16407



**ZIMMER HOLDINGS, INC.**

*(Exact name of registrant as specified in its charter)*

**Delaware**  
*(State or other jurisdiction of  
incorporation or organization)*

**13-4151777**  
*(IRS Employer  
Identification No.)*

**345 East Main Street, Warsaw, IN 46580**  
*(Address of principal executive offices)*  
**Telephone: (574) 267-6131**

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 the registrant was required to submit and post such files). Yes ☒ No ☐

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

Large accelerated filer ☒ Accelerated filer ☐ Non-accelerated filer ☐ Smaller reporting company ☐  
(Do not check if a 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 April 24, 2012, 176,137,946 shares of the registrant's \$.01 par value common stock were outstanding.

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**ZIMMER HOLDINGS, INC.**

**INDEX TO FORM 10-Q**

**March 31, 2012**

	<u><b>Page</b></u>
<b>Part I — Financial Information</b>	
<b>Item 1.</b> Financial Statements	
Condensed Consolidated Statements of Earnings for the Three Months Ended March 31, 2012 and 2011 .....	3
Condensed Consolidated Statements of Comprehensive Income for the Three Months Ended March 31, 2012 and 2011 .....	4
Condensed Consolidated Balance Sheets as of March 31, 2012 and December 31, 2011 .....	5
Condensed Consolidated Statements of Cash Flows for the Three Months Ended March 31, 2012 and 2011 .....	6
Notes to Interim Condensed Consolidated Financial Statements .....	7
<b>Item 2.</b> Management's Discussion and Analysis of Financial Condition and Results of Operations ....	21
<b>Item 3.</b> Quantitative and Qualitative Disclosures About Market Risk .....	31
<b>Item 4.</b> Controls and Procedures .....	31
<b>Part II — Other Information</b>	
There is no information required to be reported under any items except those indicated below.	
<b>Item 1.</b> Legal Proceedings .....	32
<b>Item 1A.</b> Risk Factors .....	32
<b>Item 2.</b> Unregistered Sales of Equity Securities and Use of Proceeds .....	32
<b>Item 5.</b> Other Information .....	32
<b>Item 6.</b> Exhibits .....	33
<b>Signatures</b> .....	34

## Part I — Financial Information

### Item 1. *Financial Statements*

#### ZIMMER HOLDINGS, INC. AND SUBSIDIARIES CONDENSED CONSOLIDATED STATEMENTS OF EARNINGS (in millions, except per share amounts, unaudited)

	Three Months Ended March 31,	
	2012	2011
<b>Net Sales</b> .....	\$1,140.7	\$1,115.6
Cost of products sold .....	288.7	279.0
<b>Gross Profit</b> .....	852.0	836.6
Research and development .....	59.6	55.6
Selling, general and administrative .....	463.3	458.3
Special items (Note 2) .....	33.5	25.5
Operating expenses .....	556.4	539.4
<b>Operating Profit</b> .....	295.6	297.2
Interest income .....	3.1	2.0
Interest expense .....	(17.6)	(13.0)
Earnings before income taxes .....	281.1	286.2
Provision for income taxes .....	72.2	77.3
Net earnings .....	208.9	208.9
Less: Net loss attributable to noncontrolling interest .....	(0.7)	—
<b>Net Earnings of Zimmer Holdings, Inc.</b> .....	<u>\$ 209.6</u>	<u>\$ 208.9</u>
<b>Earnings Per Common Share</b>		
Basic .....	\$ 1.18	\$ 1.08
Diluted .....	\$ 1.17	\$ 1.08
<b>Weighted Average Common Shares Outstanding</b>		
Basic .....	177.4	192.6
Diluted .....	178.5	193.8

The accompanying notes are an integral part of these consolidated financial statements.

**ZIMMER HOLDINGS, INC. AND SUBSIDIARIES**  
**CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME**  
(in millions, unaudited)

	Three Months Ended March 31,	
	2012	2011
Net earnings .....	\$208.9	\$208.9
Other Comprehensive Income:		
Foreign currency cumulative translation adjustments .....	28.1	130.7
Unrealized cash flow hedge gains/(losses), net of tax .....	4.1	(47.3)
Reclassification adjustments on foreign currency hedges, net of tax .....	0.9	4.4
Unrealized gains on securities, net of tax .....	0.2	0.2
Adjustments to prior service cost and unrecognized actuarial assumptions, net of tax .....	22.9	0.7
Total Other Comprehensive Gain .....	56.2	88.7
Comprehensive Income .....	265.1	297.6
Comprehensive loss attributable to the noncontrolling interest .....	(0.7)	—
Comprehensive Income Attributable to Zimmer Holdings, Inc. ....	<u>\$265.8</u>	<u>\$297.6</u>

The accompanying notes are an integral part of these consolidated financial statements.

**ZIMMER HOLDINGS, INC. AND SUBSIDIARIES**  
**CONDENSED CONSOLIDATED BALANCE SHEETS**  
(in millions, unaudited)

	<u>March 31, 2012</u>	<u>December 31, 2011</u>
<b>ASSETS</b>		
<b>Current Assets:</b>		
Cash and cash equivalents .....	\$ 674.0	\$ 768.3
Short-term investments .....	555.1	455.5
Accounts receivable, less allowance for doubtful accounts .....	895.0	838.8
Inventories .....	937.0	929.8
Prepaid expenses and other current assets .....	64.7	73.7
Deferred income taxes .....	196.7	210.5
<b>Total Current Assets</b> .....	<b>3,322.5</b>	<b>3,276.6</b>
Property, plant and equipment, net .....	1,192.7	1,207.3
Goodwill .....	2,658.3	2,626.0
Intangible assets, net .....	784.3	798.5
Other assets .....	645.9	606.9
<b>Total Assets</b> .....	<b>\$ 8,603.7</b>	<b>\$ 8,515.3</b>
<b>LIABILITIES AND STOCKHOLDERS' EQUITY</b>		
<b>Current Liabilities:</b>		
Accounts payable .....	\$ 126.0	\$ 143.3
Income taxes .....	48.1	8.6
Short-term debt .....	144.6	143.3
Other current liabilities .....	543.1	571.9
<b>Total Current Liabilities</b> .....	<b>861.8</b>	<b>867.1</b>
Other long-term liabilities .....	507.5	557.4
Long-term debt .....	1,572.8	1,576.0
<b>Total Liabilities</b> .....	<b>2,942.1</b>	<b>3,000.5</b>
<b>Commitments and Contingencies (Note 14)</b>		
<b>Stockholders' Equity:</b>		
Zimmer Holdings, Inc. Stockholders' Equity:		
Common stock, \$0.01 par value, one billion shares authorized, 256.3 million shares issued in 2012 (255.9 million in 2011) .....	2.6	2.5
Paid-in capital .....	3,421.5	3,399.2
Retained earnings .....	6,636.3	6,426.8
Accumulated other comprehensive income .....	327.6	271.4
Treasury stock, 80.2 million shares (77.9 million shares in 2011) .....	(4,733.3)	(4,592.7)
<b>Total Zimmer Holdings, Inc. stockholders' equity</b> .....	<b>5,654.7</b>	<b>5,507.2</b>
Noncontrolling interest .....	6.9	7.6
<b>Total Stockholders' Equity</b> .....	<b>5,661.6</b>	<b>5,514.8</b>
<b>Total Liabilities and Stockholders' Equity</b> .....	<b>\$ 8,603.7</b>	<b>\$ 8,515.3</b>

The accompanying notes are an integral part of these consolidated financial statements.

**ZIMMER HOLDINGS, INC. AND SUBSIDIARIES**  
**CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS**  
(in millions, unaudited)

	For the Three Months Ended March 31,	
	2012	2011
<b>Cash flows provided by (used in) operating activities:</b>		
Net earnings	\$ 208.9	\$ 208.9
Adjustments to reconcile net earnings to cash provided by operating activities:		
Depreciation and amortization	96.8	86.1
Share-based compensation	12.8	14.3
Income tax benefit from stock option exercises	6.2	6.2
Excess income tax benefit from stock option exercises	(1.2)	(2.4)
Inventory step-up	1.0	4.4
Changes in operating assets and liabilities, net of effect of acquisitions:		
Income taxes	47.8	18.1
Receivables	(54.2)	(70.5)
Inventories	(6.0)	(13.8)
Accounts payable and accrued expenses	(29.9)	(23.0)
Other assets and liabilities	(74.8)	(46.1)
Net cash provided by operating activities	<u>207.4</u>	<u>182.2</u>
<b>Cash flows provided by (used in) investing activities:</b>		
Additions to instruments	(28.8)	(46.3)
Additions to other property, plant and equipment	(19.5)	(17.1)
Purchases of investments	(255.6)	(65.3)
Sales of investments	174.6	75.0
Investments in other assets	(34.9)	(13.2)
Net cash used in investing activities	<u>(164.2)</u>	<u>(66.9)</u>
<b>Cash flows provided by (used in) financing activities:</b>		
Net proceeds under revolving credit facilities	1.0	0.2
Proceeds from employee stock compensation plans	10.3	17.0
Excess income tax benefit from stock option exercises	1.2	2.4
Repurchase of common stock	(141.6)	(236.1)
Net cash used in financing activities	<u>(129.1)</u>	<u>(216.5)</u>
Effect of exchange rates on cash and cash equivalents	(8.4)	7.9
Increase (decrease) in cash and cash equivalents	(94.3)	(93.3)
Cash and cash equivalents, beginning of year	<u>768.3</u>	<u>668.9</u>
Cash and cash equivalents, end of period	<u>\$ 674.0</u>	<u>\$ 575.6</u>

The accompanying notes are an integral part of these consolidated financial statements.

## ZIMMER HOLDINGS, INC. AND SUBSIDIARIES

### NOTES TO INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

#### 1. Basis of Presentation

The financial data presented herein is unaudited and should be read in conjunction with the consolidated financial statements and accompanying notes included in the 2011 Annual Report on Form 10-K filed by Zimmer Holdings, Inc. The condensed consolidated financial statements for the majority of our international subsidiaries are for periods that ended on March 25, 2012 and 2011. For these international subsidiaries, the three month results included in these condensed consolidated financial statements are for the period of December 26 through March 25 or the period of January 1 to March 25.

In our opinion, the accompanying unaudited condensed consolidated financial statements include all adjustments necessary for a fair statement of the financial position, results of operations and cash flows for the interim periods presented. The December 31, 2011 condensed balance sheet data was derived from audited financial statements, but does not include all disclosures required by accounting principles generally accepted in the United States of America (GAAP). Results for interim periods should not be considered indicative of results for the full year. Certain amounts in the 2011 condensed consolidated financial statements have been reclassified to conform to the 2012 presentation.

The words “we,” “us,” “our” and similar words refer to Zimmer Holdings, Inc. and its subsidiaries. Zimmer Holdings refers to the parent company only.

#### 2. Significant Accounting Policies

*Special Items* — We recognize expenses resulting directly from our business combinations, employee termination benefits, certain contract terminations, consulting and professional fees and asset impairment charges connected with global restructuring, quality excellence and transformation initiatives, and other items as “Special items” in our condensed consolidated statement of earnings. “Special items” included (in millions):

	Three Months Ended March 31,	
	2012	2011
Impairment/loss on disposal of assets .....	\$ 0.4	\$ 2.5
Consulting and professional fees .....	18.3	3.5
Employee severance and retention .....	3.4	16.2
Dedicated project personnel .....	3.3	0.3
Distributor acquisitions .....	0.1	0.6
Certain litigation matters .....	6.4	0.1
Contract terminations .....	1.5	1.0
Contingent consideration adjustments .....	(0.8)	—
Other .....	0.9	1.3
Special items .....	<u>\$33.5</u>	<u>\$25.5</u>

In the first quarter of 2012, we announced our plans to outsource our Warsaw, Indiana distribution center to a third party service provider at a national transportation hub, among other organizational changes. Approximately 140 employees were or will be affected by these actions.

In the first quarter of 2011, we terminated employees as part of a reduction of management layers, expansion of management spans of control, and changes in our organizational structure. Approximately 450 employees from across the globe were affected by these actions.

As a result of these actions, we incurred expenses related to severance benefits, share-based compensation acceleration and other employee termination-related costs. The vast majority of these termination benefits were provided in accordance with our existing policies or local government regulations and are considered ongoing benefits. These costs were accrued when they became probable and estimable and were recorded as part of other current liabilities. The majority of these costs have been paid or will be paid in the year they were accrued.

*Recent Accounting Pronouncements* — In 2011 the Financial Accounting Standards Board issued an accounting standard update (ASU) requiring companies to present net income and other comprehensive income in either a single continuous statement or in two separate, but consecutive, statements of net income and other comprehensive income. The ASU also required that the reclassifications adjustments from accumulated other comprehensive income to net income be presented on the statement of earnings by line item, but this provision of the ASU has been delayed indefinitely. The requirement regarding presentation of net income and other comprehensive income in a single or two separate, but consecutive, statements became effective for us this quarter. The ASU changes the presentation requirements of other comprehensive income only and does not change any accounting for other comprehensive income and therefore had no effect on our financial position, results of operations or cash flows.

There are no other recently issued accounting pronouncements that we have not yet adopted that are expected to have a material effect on our financial position, results of operations or cash flows.

### 3. Inventories

	March 31, 2012	December 31, 2011
	(in millions)	
Finished goods .....	\$733.8	\$743.0
Work in progress .....	60.3	47.8
Raw materials .....	142.9	139.0
Inventories .....	<u>\$937.0</u>	<u>\$929.8</u>

### 4. Property, Plant and Equipment

	March 31, 2012	December 31, 2011
	(in millions)	
Land .....	\$ 22.1	\$ 22.3
Buildings and equipment .....	1,212.2	1,196.8
Capitalized software costs .....	209.8	208.4
Instruments .....	1,526.1	1,509.2
Construction in progress .....	81.0	76.4
	<u>3,051.2</u>	<u>3,013.1</u>
Accumulated depreciation .....	<u>(1,858.5)</u>	<u>(1,805.8)</u>
Property, plant and equipment, net .....	<u>\$ 1,192.7</u>	<u>\$ 1,207.3</u>



## 5. Investments

We invest in short and long-term investments classified as available-for-sale securities. Information regarding our investments is as follows (in millions):

	Amortized Cost	Gross Unrealized		Fair value
		Gains	Losses	
<b>As of March 31, 2012</b>				
Corporate debt securities .....	\$331.1	\$0.4	\$(0.1)	\$331.4
U.S. government and agency debt securities .....	200.5	—	(0.1)	200.4
Foreign government debt securities .....	2.8	—	—	2.8
Commercial paper .....	127.3	—	—	127.3
Certificates of deposit .....	90.1	—	—	90.1
Total short and long-term investments .....	<u>\$751.8</u>	<u>\$0.4</u>	<u>\$(0.2)</u>	<u>\$752.0</u>
<b>As of December 31, 2011</b>				
Corporate debt securities .....	\$324.8	\$0.2	\$(0.3)	\$324.7
U.S. government and agency debt securities .....	177.1	0.1	—	177.2
Municipal bonds .....	1.0	—	—	1.0
Foreign government debt securities .....	6.8	—	—	6.8
Commercial paper .....	74.5	—	—	74.5
Certificates of deposit .....	88.5	—	—	88.5
Total short and long-term investments .....	<u>\$672.7</u>	<u>\$0.3</u>	<u>\$(0.3)</u>	<u>\$672.7</u>

Unrealized gains and losses on these investments are recorded in accumulated other comprehensive income in our condensed consolidated balance sheet.

The following table shows the fair value and gross unrealized losses for all available-for-sale securities in an unrealized loss position deemed to be temporary (in millions):

	March 31, 2012		December 31, 2011	
	Fair Value	Unrealized Losses	Fair value	Unrealized Losses
Corporate debt securities .....	\$131.1	\$(0.1)	\$164.5	\$(0.3)
U.S. government and agency debt securities .....	173.0	(0.1)	—	—
Total .....	<u>\$304.1</u>	<u>\$(0.2)</u>	<u>\$164.5</u>	<u>\$(0.3)</u>

All securities in the table above have been in an unrealized loss position for less than twelve months. A total of 94 securities were in an unrealized loss position as of March 31, 2012.

The unrealized losses on our investments in corporate debt securities were caused by increases in interest yields resulting from adverse conditions in the global credit markets. We believe the unrealized losses associated with our available-for-sale securities as of March 31, 2012 are temporary because we do not intend to sell these investments, and we do not believe we will be required to sell them before recovery of their amortized cost basis.

The amortized cost and fair value of our available-for-sale fixed-maturity securities by contractual maturity are as follows (in millions):

	March 31, 2012	
	Amortized Cost	Fair Value
Due in one year or less .....	\$555.0	\$555.1
Due after one year through two years .....	196.8	196.9
Total .....	<u>\$751.8</u>	<u>\$752.0</u>

## 6. Other Current Liabilities

	March 31, 2012	December 31, 2011
	(in millions)	
Other current liabilities:		
Salaries, wages and benefits .....	\$ 74.4	\$116.5
Accrued liabilities .....	468.7	455.4
Total other current liabilities .....	<u>\$543.1</u>	<u>\$571.9</u>

## 7. Debt

Our debt consisted of the following (in millions):

	March 31, 2012	December 31, 2011
Short-term debt		
Senior Credit Facility .....	\$ 141.8	\$ 143.0
Other short-term debt .....	2.8	0.3
Total short-term debt .....	<u>\$ 144.6</u>	<u>\$ 143.3</u>
Long-term debt		
Senior Notes due 2014 .....	\$ 250.0	\$ 250.0
Senior Notes due 2019 .....	500.0	500.0
Senior Notes due 2021 .....	300.0	300.0
Senior Notes due 2039 .....	500.0	500.0
Debt discount .....	(1.8)	(1.8)
Adjustment related to interest rate swaps .....	24.6	27.8
Total long-term debt .....	<u>\$1,572.8</u>	<u>\$1,576.0</u>

The estimated fair value of our Senior Notes as of March 31, 2012, based on quoted prices for the specific securities from transactions in over-the-counter markets (Level 2), was \$1,674.1 million. The carrying value of the Senior Credit Facility approximates fair value, as the underlying instruments have variable interest rates at market value.

## 8. Fair Value Measurement of Assets and Liabilities

The following assets and liabilities are recorded at fair value on a recurring basis (in millions):

Description	As of March 31, 2012			
	Fair Value Measurements at Reporting Date Using:			
	Recorded Balance	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
<b>Assets</b>				
Available-for-sale securities				
Corporate debt securities . . . . .	\$331.4	\$—	\$331.4	\$—
U.S. government and agency debt securities . . . . .	200.4	—	200.4	—
Foreign government debt securities . . . . .	2.8	—	2.8	—
Commercial paper . . . . .	127.3	—	127.3	—
Certificates of deposit . . . . .	90.1	—	90.1	—
Total available-for-sale securities . . . . .	752.0	—	752.0	—
Derivatives, current and long-term				
Foreign currency forward contracts and options . . . . .	16.7	—	16.7	—
Interest rate swaps . . . . .	24.6	—	24.6	—
	<u>\$793.3</u>	<u>\$—</u>	<u>\$793.3</u>	<u>\$—</u>
<b>Liabilities</b>				
Derivatives, current and long-term				
Foreign currency forward contracts and options . . . . .	<u>\$ 10.3</u>	<u>\$—</u>	<u>\$ 10.3</u>	<u>\$—</u>

	As of December 31, 2011			
	Fair Value Measurements at Reporting Date Using:			
		Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Description	Recorded Balance			
Assets				
Available-for-sale securities				
Corporate debt securities . . . . .	\$324.7	\$—	\$324.7	\$—
U.S. government and agency debt securities . . . . .	177.2	—	177.2	—
Municipal bonds . . . . .	1.0	—	1.0	—
Foreign government debt securities . . . . .	6.8	—	6.8	—
Commercial paper . . . . .	74.5	—	74.5	—
Certificates of deposit . . . . .	88.5	—	88.5	—
Total available-for-sale securities . . . . .	672.7	—	672.7	—
Derivatives, current and long-term				
Foreign currency forward contracts and options . . . . .	18.3	—	18.3	—
Interest rate swaps . . . . .	27.8	—	27.8	—
	\$718.8	\$—	\$718.8	\$—
Liabilities				
Derivatives, current and long-term				
Foreign currency forward contracts and options . . . . .	\$ 25.2	\$—	\$ 25.2	\$—
Cross-currency interest rate swaps . . . . .	8.2	—	8.2	—
	\$ 33.4	\$—	\$ 33.4	\$—

We value our available-for-sale securities using a market approach based on broker prices for identical assets in over-the-counter markets and perform ongoing assessments of counterparty credit risk.

We value our foreign currency forward contracts and foreign currency options using a market approach based on foreign currency exchange rates obtained from active markets and we perform ongoing assessments of counterparty credit risk.

We value our interest rate swaps using a market approach based on publicly available market yield curves and the terms of our swaps and we perform ongoing assessments of counterparty credit risk.

We value our cross-currency interest rate swaps using a market approach based upon publicly available market yield curves, foreign currency exchange rates obtained from active markets and the terms of our swaps. We also perform ongoing assessments of counterparty credit risk.

## 9. Derivative Instruments and Hedging Activities

We are exposed to certain market risks relating to our ongoing business operations, including foreign currency exchange rate risk, commodity price risk, interest rate risk and credit risk. We manage our exposure to these and other market risks through regular operating and financing activities. Currently, the only risks that we manage through the use of derivative instruments are interest rate risk and foreign currency exchange rate risk.

## **Interest Rate Risk**

### ***Derivatives Designated as Fair Value Hedges***

We use interest rate derivative instruments to manage our exposure to interest rate movements by converting fixed-rate debt into variable-rate debt. Under these agreements, we agree to exchange, at specified intervals, the difference between fixed and variable interest amounts calculated by reference to an agreed-upon notional principal amount. The objective of the instruments is to more closely align interest expense with interest income received on cash and cash equivalents. These derivative instruments are designated as fair value hedges under GAAP. Changes in the fair value of the derivative instrument are recorded in current earnings and are offset by gains or losses on the underlying debt instrument.

We have multiple nine-year fixed-to-variable interest rate swap agreements with a total notional amount of \$250 million. These interest rate swap agreements were designated as fair value hedges of the fixed interest rate obligation of our 2019 Notes. We receive a fixed interest rate of 4.625 percent and pay variable interest equal to the three-month LIBOR plus an average of 133 basis points on these interest rate swap agreements.

## **Foreign Currency Exchange Rate Risk**

We operate on a global basis and are exposed to the risk that our financial condition, results of operations and cash flows could be adversely affected by changes in foreign currency exchange rates. To reduce the potential effects of foreign currency exchange rate movements on net earnings, we enter into derivative financial instruments in the form of foreign currency exchange forward contracts and options with major financial institutions. We are primarily exposed to foreign currency exchange rate risk with respect to transactions and net assets denominated in Euros, Swiss Francs, Japanese Yen, British Pounds, Canadian Dollars, Australian Dollars, Korean Won, Swedish Krona, Czech Koruna, Thai Baht, Taiwan Dollars, South African Rand, Russian Rubles and Indian Rupees. We do not use derivative financial instruments for trading or speculative purposes.

### ***Derivatives Designated as Cash Flow Hedges***

Our revenues are generated in various currencies throughout the world. However, a significant amount of our inventory is produced in U.S. Dollars. Therefore, movements in foreign currency exchange rates may have different proportional effects on our revenues compared to our cost of products sold. To minimize the effects of foreign currency exchange rate movements on cash flows, we hedge intercompany sales of inventory expected to occur within the next 30 months with foreign currency exchange forward contracts and options. We designate these derivative instruments as cash flow hedges.

We perform quarterly assessments of hedge effectiveness by verifying and documenting the critical terms of the hedge instrument and that forecasted transactions have not changed significantly. We also assess on a quarterly basis whether there have been adverse developments regarding the risk of a counterparty default. For derivatives which qualify as hedges of future cash flows, the effective portion of changes in fair value is temporarily recorded in other comprehensive income and then recognized in cost of products sold when the hedged item affects net earnings. The ineffective portion of a derivative's change in fair value, if any, is immediately reported in cost of products sold.

For forward contracts and options outstanding at March 31, 2012, we have obligations to purchase U.S. Dollars and sell Euros, Japanese Yen, British Pounds, Canadian Dollars, Australian Dollars, Korean Won, Swedish Krona, Czech Koruna, Thai Baht, Taiwan Dollars, South African Rand, Russian Rubles and Indian Rupees and purchase Swiss Francs and sell U.S. Dollars at set maturity dates ranging from April 2012 through September 2014. As of March 31, 2012, the notional amounts of outstanding forward contracts and options entered into with third parties to purchase U.S. Dollars were \$1.4 billion. As of March 31, 2012, the notional amounts of outstanding forward contracts and options entered into with third parties to purchase Swiss Francs were \$288.2 million.

### ***Derivatives Not Designated as Hedging Instruments***

We enter into foreign currency forward exchange contracts with terms of one month to manage currency exposures for monetary assets and liabilities denominated in a currency other than an entity's functional currency. As a result, any foreign currency remeasurement gains/losses recognized in earnings are generally offset with gains/losses on the foreign currency forward exchange contracts in the same reporting period. These offsetting gains/losses are recorded in cost of products sold as the underlying assets and liabilities exposed to remeasurement include inventory-related transactions. These contracts are settled on the last day of each reporting period. Therefore, there is no outstanding balance related to these contracts recorded on the balance sheet as of the end of the reporting period. The notional amounts of these contracts are typically in a range of \$1.2 billion to \$1.7 billion per quarter.

### **Foreign Currency Exchange and Interest Rate Risk**

#### ***Derivatives Designated as Cash Flow Hedges***

In 2011, our subsidiary in Japan, with a functional currency of Japanese Yen, borrowed variable-rate debt of \$143.0 million denominated in U.S. Dollars under our Senior Credit Facility. To manage the foreign currency exchange risk associated with remeasuring the debt to Japanese Yen and the interest rate risk associated with the variable-rate debt, we entered into multiple cross-currency interest rate swap agreements with a total notional amount of 11,798 million Japanese Yen. We designated these swaps as cash flow hedges of the foreign currency exchange and interest rate risks. The effective portion of changes in fair value of the cross-currency interest rate swaps was temporarily recorded in other comprehensive income and then recognized in interest expense when the hedged item affected net earnings. The cross-currency interest rate swap agreements matured in the first quarter of 2012 and we paid off the subsidiary's U.S. Dollar debt with Japanese Yen debt borrowed under the Senior Credit Facility.

### **Income Statement Presentation**

#### ***Derivatives Designated as Fair Value Hedges***

Derivative instruments designated as fair value hedges had the following effects on our condensed consolidated statements of earnings (in millions):

<u>Derivative Instrument</u>	<u>Location on Statement of Earnings</u>	<u>Loss on Instrument</u>		<u>Gain on Hedged Item</u>	
		<u>Three Months Ended March 31,</u>		<u>Three Months Ended March 31,</u>	
		<u>2012</u>	<u>2011</u>	<u>2012</u>	<u>2011</u>
Interest rate swaps . . . . .	Interest expense	\$(3.2)	\$(3.1)	\$3.2	\$3.1

We had no ineffective fair value hedging instruments during the three month periods ended March 31, 2012 and 2011.

### ***Derivatives Designated as Cash Flow Hedges***

Derivative instruments designated as cash flow hedges had the following effects, before taxes, on other comprehensive income (OCI) and net earnings on our condensed consolidated statements of earnings, condensed consolidated statements of comprehensive income and condensed consolidated balance sheets (in millions):

	<u>Amount of Gain / (Loss) Recognized in OCI</u>			<u>Amount of Gain / (Loss) Reclassified from OCI</u>	
	<u>Three Months Ended March 31,</u>			<u>Three Months Ended March 31,</u>	
<u>Derivative Instrument</u>	<u>2012</u>	<u>2011</u>	<u>Location on Statement of Earnings</u>	<u>2012</u>	<u>2011</u>
Foreign exchange forward contracts . . . . .	\$8.0	\$(58.1)	Cost of products sold	\$(4.1)	\$(5.2)
Foreign exchange options . . . . .	—	0.9	Cost of products sold	—	—
Cross-currency interest rate swaps . . . . .	—	1.0	Interest expense	0.2	(3.0)
	<u>\$8.0</u>	<u>\$(56.2)</u>		<u>\$(3.9)</u>	<u>\$(8.2)</u>

The net amount recognized in earnings during the three month periods ended March 31, 2012 and 2011 due to ineffectiveness and amounts excluded from the assessment of hedge effectiveness was not significant.

The fair value of outstanding derivative instruments designated as cash flow hedges and recorded on the balance sheet at March 31, 2012, together with settled derivatives where the hedged item has not yet affected earnings, was a net unrealized loss of \$10.8 million, or \$5.2 million after taxes, which is deferred in accumulated other comprehensive income. Of the net unrealized loss, \$22.9 million, or \$11.1 million after taxes, is expected to be reclassified to earnings over the next twelve months.

### ***Derivatives Not Designated as Hedging Instruments***

The following losses from these derivative instruments were recognized on our condensed consolidated statements of earnings (in millions):

<b>Derivative Instrument</b>	<b>Location on Statement of Earnings</b>	<b>Three Months Ended March 31,</b>	
		<b>2012</b>	<b>2011</b>
Foreign exchange forward contracts .....	Cost of products sold	\$(1.9)	\$(15.0)

This impact does not include any offsetting gains/losses recognized in earnings as a result of foreign currency remeasurement of monetary assets and liabilities denominated in a currency other than an entity's functional currency.

## Balance Sheet Presentation

As of March 31, 2012 and December 31, 2011, all derivative instruments designated as fair value hedges and cash flow hedges are recorded at fair value on the balance sheet. On our condensed consolidated balance sheets, we recognize individual forward contracts and options with the same counterparty on a net asset/liability basis if we have a master netting agreement with the counterparty. The fair value of derivative instruments on a gross basis is as follows (in millions):

		March 31, 2012		December 31, 2011	
		Balance Sheet Location	Fair Value	Balance Sheet Location	Fair Value
<b>Asset Derivatives</b>					
Foreign exchange forward contracts . . . .	Other current assets		\$21.3	Other current assets	\$24.9
Foreign exchange options . . . . .	Other current assets		1.5	Other current assets	1.4
Foreign exchange forward contracts . . . .	Other assets		15.5	Other assets	14.5
Foreign exchange options . . . . .	Other assets		0.4	Other assets	1.0
Interest rate swaps . . . . .	Other assets		24.6	Other assets	27.8
<b>Total asset derivatives . . . . .</b>			<u>\$63.3</u>		<u>\$69.6</u>
<b>Liability Derivatives</b>					
Foreign exchange forward contracts . . . .	Other current liabilities		\$26.1	Other current liabilities	\$35.6
Cross-currency interest rate swaps . . . .	Other current liabilities		—	Other current liabilities	8.2
Foreign exchange forward contracts . . . .	Other long-term liabilities		6.2	Other long-term liabilities	13.1
<b>Total liability derivatives . . . . .</b>			<u>\$32.3</u>		<u>\$56.9</u>

## 10. Income Taxes

We operate on a global basis and are subject to numerous and complex tax laws and regulations. Our income tax filings are regularly under audit in multiple federal, state and foreign jurisdictions. Income tax audits may require an extended period of time to reach resolution and may result in significant income tax adjustments when interpretation of tax laws or allocation of company profits is disputed. The net amount of tax liability for unrecognized tax benefits may change within the next twelve months due to changes in audit status, expiration of statutes of limitations and other events which could impact our determination of unrecognized tax benefits. Currently, we cannot reasonably estimate the amount by which our unrecognized tax benefits will change.

During the second quarter of 2011, the IRS concluded their examination of our U.S. federal returns for years 2005 through 2007 and issued income tax assessments reallocating profits between certain of our U.S. and foreign subsidiaries. We believe that we have followed applicable U.S. tax laws and are vigorously defending our income tax positions. The ultimate resolution of this matter is uncertain and could have a material impact on our income tax expense, results of operations, and cash flows for future periods. Our U.S. federal returns for years 2008 and 2009 are currently under IRS examination.

In the three month period ended March 31, 2012, our effective tax rate was 25.7 percent. Our effective tax rates were lower than the U.S. statutory income tax rate of 35 percent primarily due to income earned in foreign locations with lower tax rates.

## 11. Retirement Benefit Plans

We have defined benefit pension plans covering certain U.S. and Puerto Rico employees. The employees who are not participating in the defined benefit plans receive additional benefits under our defined contribution plans. Plan benefits are primarily based on years of credited service and the participant's compensation. In addition to the U.S. and Puerto Rico defined benefit pension plans, we sponsor various non-U.S. pension arrangements, including retirement and termination benefit plans required by local law or coordinated with government sponsored plans.



The components of net pension expense for our U.S. and non-U.S. defined benefit retirement plans are as follows (in millions):

	Three Months Ended March 31,	
	2012	2011
Service cost . . . . .	\$ 6.8	\$ 6.9
Interest cost . . . . .	5.0	5.0
Expected return on plan assets . . . . .	(8.3)	(7.8)
Amortization of prior service cost . . . . .	(0.2)	(0.2)
Amortization of unrecognized actuarial loss . . . . .	3.4	1.9
Net periodic benefit cost . . . . .	<u>\$ 6.7</u>	<u>\$ 5.8</u>

We contributed \$37.0 million during the three month period ended March 31, 2012 to our U.S. and Puerto Rico defined benefit plans and expect to contribute an additional \$15.5 million to these plans during the remainder of 2012. We contributed \$3.8 million to our foreign-based defined benefit plans in the three month period ended March 31, 2012 and expect to contribute \$11.5 million to these foreign-based plans during the remainder of 2012.

In March 2012, we amended our U.S. defined benefit pension plan which led us to remeasure our plan assets and obligations. Accordingly, the resulting remeasurement was reflected in our condensed consolidated statements of earnings, condensed consolidated statements of comprehensive income and condensed consolidated balance sheets.

## 12. Earnings Per Share

The following is a reconciliation of weighted average shares for the basic and diluted shares computations (in millions):

	Three Months Ended March 31,	
	2012	2011
Weighted average shares outstanding for basic net earnings per share . . . . .	177.4	192.6
Effect of dilutive stock options and other equity awards . . . . .	1.1	1.2
Weighted average shares outstanding for diluted net earnings per share . . . . .	<u>178.5</u>	<u>193.8</u>

During the three month period ended March 31, 2012, an average of 12.3 million options to purchase shares of common stock were not included in the computation of diluted earnings per share because the exercise prices of these options were greater than the average market price of the common stock. During the three month period ended March 31, 2011, an average of 12.7 million options were not included in the computation.

In the three month period ended March 31, 2012, we repurchased 2.3 million shares of our common stock at an average price of \$61.03 per share for a total cash outlay of \$141.6 million, including commissions. As of March 31, 2012, approximately \$1.4 billion remained authorized under a \$1.5 billion repurchase program, which will expire on December 31, 2014.

## 13. Segment Information

We design, develop, manufacture and market orthopaedic reconstructive implants, biologics, dental implants, spinal implants, trauma products and related surgical products which include surgical supplies and instruments designed to aid in surgical procedures and post-operation rehabilitation. We also provide other healthcare-related services. Revenue related to these services currently represents less than 1 percent of our total net sales. We manage operations through three major geographic segments — the Americas, which is comprised principally of the U.S. and includes other North, Central and South American markets; Europe, which is comprised principally of Europe and includes the Middle East and African markets; and Asia Pacific, which is

comprised primarily of Japan and includes other Asian and Pacific markets. This structure is the basis for our reportable segment information discussed below. Management evaluates reportable segment performance based upon segment operating profit exclusive of operating expenses pertaining to share-based payment expense, inventory step-up, "Certain claims," goodwill impairment, "Special items," and global operations and corporate functions. Global operations and corporate functions include research, development engineering, medical education, brand management, corporate legal, finance, and human resource functions, U.S., Puerto Rico and Ireland-based manufacturing operations and logistics and intangible asset amortization resulting from business combination accounting. Intercompany transactions have been eliminated from segment operating profit.

Net sales and segment operating profit are as follows (in millions):

	Net Sales		Operating Profit	
	Three Months Ended March 31,		Three Months Ended March 31,	
	2012	2011	2012	2011
Americas .....	\$ 634.4	\$ 629.7	\$ 320.8	\$ 311.4
Europe .....	300.8	299.2	94.7	110.0
Asia Pacific .....	205.5	186.7	77.7	73.9
Total .....	<u>\$1,140.7</u>	<u>\$1,115.6</u>		
Share-based compensation .....			(12.8)	(14.3)
Inventory step-up .....			(1.0)	(4.4)
Special items .....			(33.5)	(25.5)
Global operations and corporate functions .....			(150.3)	(153.9)
Operating profit .....			<u>\$ 295.6</u>	<u>\$ 297.2</u>

Net sales by product category are as follows (in millions):

	Three Months Ended March 31,	
	2012	2011
Reconstructive		
Knees .....	\$ 470.6	\$ 462.2
Hips .....	344.5	337.3
Extremities .....	44.8	42.9
	<u>859.9</u>	<u>842.4</u>
Dental .....	60.2	62.4
Trauma .....	75.5	70.1
Spine .....	53.2	56.9
Surgical and other .....	91.9	83.8
Total .....	<u>\$1,140.7</u>	<u>\$1,115.6</u>

#### 14. Commitments and Contingencies

Other than as described below, there have been no significant developments relating to the information previously reported in Note 19 to our Consolidated Financial Statements in our Annual Report on Form 10-K for the year ended December 31, 2011.

On a quarterly and annual basis, we review relevant information with respect to loss contingencies and update our accruals, disclosures and estimates of reasonably possible losses or ranges of loss based on such reviews. We establish liabilities for loss contingencies when it is probable that a loss has been incurred and the amount of the loss can be reasonably estimated. For matters where a loss is believed to be reasonably possible, but not probable, no accrual has been made.

## Litigation

**Durom® Cup-related claims:** On July 22, 2008, we temporarily suspended marketing and distribution of the *Durom* Acetabular Component (*Durom* Cup) in the U.S. Subsequently, a number of product liability lawsuits and other claims have been asserted against us. We have settled some of these claims and the others are still pending. Additional claims may be asserted in the future.

Since 2008, we have accrued estimated losses of \$388.2 million for *Durom* Cup-related claims. With respect to the periods covered by this report, our estimate of our total liability for these claims as of March 31, 2012 remains consistent with our prior estimate, and, accordingly, we did not record any expense during the three month period ended March 31, 2012. During the three month period ended March 31, 2011, we recognized \$1.1 million of expense in SG&A.

Our understanding of clinical outcomes with the *Durom* Cup continues to evolve. We rely on significant estimates in determining the provisions for *Durom* Cup-related claims, including the number of claims that we will receive and the average amount we will pay per claim. The actual number of claims that we receive and the amount we pay per claim may differ from our estimates. Among other factors, since our understanding of the clinical outcomes is still evolving, we cannot reasonably estimate the possible loss or range of loss that may result from *Durom* Cup-related claims in excess of the losses we have accrued.

**Margo and Daniel Polett v. Zimmer, Inc. et al.:** On August 20, 2008, the Poletts filed an action against us and an unrelated third party, Public Communications, Inc. (PCI), in the Court of Common Pleas, Philadelphia, Pennsylvania seeking an unspecified amount of damages for injuries and loss of consortium allegedly suffered by Mrs. Polett and her spouse, respectively. The complaint alleged that defendants were negligent in connection with Mrs. Polett's participation in a promotional video featuring one of our knee products. The case was tried in November 2010 and the jury returned a verdict in favor of plaintiffs. The jury awarded \$27.6 million in compensatory damages and apportioned fault 30 percent to plaintiffs, 34 percent to us and 36 percent to PCI. Under applicable law, we may be liable for any portion of the damages apportioned to PCI that it does not pay. On December 2, 2010, we and PCI filed a Motion for Post-Trial Relief seeking a judgment notwithstanding the verdict, a new trial or a remittitur. On June 10, 2011, the trial court entered an order denying our Motion for Post-Trial Relief and affirming the jury verdict in full and entered judgment for \$20.3 million against us and PCI. On June 29, 2011, we filed a Notice of Appeal to the Superior Court of Pennsylvania and posted a bond for the verdict amount plus interest. Oral argument before the appellate court in Philadelphia, Pennsylvania was held as scheduled on March 13, 2012. A ruling has not yet been issued. We have not accrued an estimated loss related to this matter. Although we believe we have strong grounds to reverse the jury's verdict, the ultimate resolution of this matter is uncertain. We could in the future be required to record a charge to our consolidated statement of earnings that could have a material adverse effect on our results of operations in any particular period.

**NexGen® Knee System claims:** Following a wide-spread advertising campaign conducted by certain law firms beginning in 2010, a number of product liability lawsuits have been filed against us in various jurisdictions. The majority of the cases are currently pending in a federal Multidistrict Litigation in the Northern District of Illinois. Other cases are pending in other state and federal courts, and additional lawsuits may be filed. As of March, 31, 2012, discovery in these lawsuits was underway and no trial dates had been set. We have not accrued an estimated loss relating to these lawsuits. Although we intend to vigorously defend these lawsuits, their ultimate resolution is uncertain.

## Intellectual Property-Related Claims

**Royalty arrangements:** We are involved in certain ongoing contractual and other disputes pertaining to certain royalty arrangements. We intend to defend ourselves vigorously against these claims. These matters are in varying stages of dispute resolution processes. In the three month period ended March 31, 2012, we accrued an estimated loss related to one of these matters. With respect to the other matters, we cannot reasonably estimate the possible loss, if any, we may incur or predict the likely outcome of the matters. An adverse result in any of these matters could have an adverse effect on our results of operations in any particular period.

## **Government Investigations**

FCPA investigation: In September 2007, the Staff of the U.S. Securities and Exchange Commission (SEC) informed us that it was conducting an investigation regarding potential violations of the Foreign Corrupt Practices Act (FCPA) in the sale of medical devices in a number of foreign countries by companies in the medical device industry. In November 2007, we received a letter from the U.S. Department of Justice (DOJ) requesting that any information provided to the SEC also be provided to the DOJ on a voluntary basis. In the course of continuing dialogues with the agencies, we have voluntarily disclosed information to the SEC and DOJ relating to sales of our products by independent distributors in two South American countries. In the first quarter of 2011, we received a subpoena from the SEC seeking documents and other records pertaining to our business activities in substantially all countries in the Asia Pacific region where we operate. We are in the process of responding to the subpoena. We cannot currently predict the outcome of this investigation. If the result of the investigation is that we are found to be in violation of the FCPA, we could face significant monetary penalties or be required to take other remedial actions.

## **Regulatory Matters**

In July 2011, the U.S. Food and Drug Administration (FDA) conducted an inspection of our Warsaw, Indiana manufacturing facility, following which it issued a Form FDA-483 (Form 483 notice). The Form 483 notice identified certain inspectional observations regarding the facility's quality systems. We responded in writing to the observations and met with representatives of the district office of the FDA to discuss our response and action plans. We have been executing our action plans and communicating on a regular basis with representatives of the district office of the FDA on the status of our execution of the action plans. As anticipated, in April 2012, the FDA commenced a re-inspection of our Warsaw, Indiana manufacturing facility and this matter is on-going. At this time, we do not know whether the FDA will take additional actions following the completion of the re-inspection and, therefore, we are unable to estimate the impact, if any, these matters may have on our financial position, results of operations and cash flows.

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

The following discussion and analysis should be read in conjunction with the condensed consolidated financial statements and corresponding notes included elsewhere in this Form 10-Q. Certain percentages presented in this discussion and analysis are calculated from the underlying whole-dollar amounts and therefore may not recalculate from the rounded numbers used for disclosure purposes. In addition, certain amounts in the 2011 condensed consolidated financial statements have been reclassified to conform to the 2012 presentation.

### **Overview**

We believe the following developments or trends are important in understanding our financial condition, results of operations and cash flows for the three month period ended March 31, 2012 and our expected results for the remainder of 2012.

#### **Demand (Volume and Mix) Trends**

Increased volume and changes in the mix of product sales contributed 5 percentage points of year-over-year sales growth during the three month period ended March 31, 2012, which is 1 percentage point better than the three month period ended March 31, 2011, as well as the three month period ended December 31, 2011.

Procedure volumes in the broader musculoskeletal market remained stable in the first quarter of 2012 relative to the fourth quarter of 2011, consistent with our expectations. We believe long-term indicators point toward sustained growth driven by an aging global population, growth in emerging markets, obesity, proven clinical benefits, new material technologies, advances in surgical techniques and more active lifestyles, among other factors. In addition, the ongoing shift in demand to premium products, such as *Prolong*® Highly Crosslinked Polyethylene, *Trabecular Metal*™ Technology products, hip stems with *Kinectiv*® Technology, high-flex knees, porous hip stems and the introduction of patient specific devices, is expected to continue to positively affect sales growth.

#### **Pricing Trends**

Global selling prices had a negative effect of 2 percent on year-over-year sales growth during the three month period ended March 31, 2012, which is 1 percentage point worse than the three month period ended March 31, 2011, and consistent with the three month period ended December 31, 2011. Selling prices in the Americas had a negative effect of 3 percent on sales growth in that operating segment during the three month period ended March 31, 2012. Europe and Asia Pacific selling prices had a negative effect of 1 percent on sales growth in those operating segments during the three month period ended March 31, 2012. We continue to see pricing pressure from governmental healthcare cost containment efforts and from local hospitals and health systems. In addition, effective April 1, 2012, a biennial price adjustment went into effect in Japan which is expected to further negatively affect pricing the remainder of the year. The Japan adjustment was greater than we anticipated coming into the year. Consequently, this adds modest incremental pressure to our full year pricing outlook of negative 2 percent. We are confident in our ability to offset this incremental pressure with positive revenue contributions from other sources.

#### **Foreign Currency Exchange Rates**

For the three month period ended March 31, 2012, foreign currency exchange rates resulted in a 1 percent decrease in sales. If foreign currency exchange rates remain consistent with March 31, 2012 rates, we estimate that a stronger dollar versus foreign currency exchange rates will have a negative effect in 2012 of approximately 1.5 to 2 percent on sales. We address currency risk through regular operating and financing activities and through the use of forward contracts and foreign currency options solely to manage foreign currency volatility and risk. Changes to foreign currency exchange rates affect sales growth, but due to offsetting gains/losses on hedge contracts and options, which are recorded in cost of products sold, the effect on net earnings in the near term is expected to be minimal.

## 2012 Outlook

We estimate our sales will grow between 0 and 2.5 percent in 2012. Such sales growth assumes knee and hip procedures will grow in low single digits with modest global economic growth and relatively stable employment. As discussed above, we expect the Japan biennial price adjustment to add modest incremental pressure to our previously disclosed pricing outlook of negative 2 percent, and we expect foreign currency exchange rates to have a negative effect on sales growth of approximately 1.5 to 2 percent based upon March 31, 2012 rates. Foreign currency translation is expected to decrease revenues by 2.5 percent in the second quarter.

Assuming currency rates remain at March 31, 2012 levels, we expect our gross margin to be approximately 75 percent of sales in 2012. This takes into account the cost pressures we have experienced from lower than planned manufacturing volumes, as well as anticipated losses from foreign currency hedges. However, if currency rates remain at March 31, 2012 levels, the hedge losses we recognize in 2012 will be less than the hedge losses recognized in 2011. We expect to continue making investments in research and development (R&D) in the range of 5 to 6 percent of sales. Selling, general and administrative expenses (SG&A) as a percent of sales is expected to be between 39.5 and 40.5 percent as we realize operational efficiencies from global restructuring and transformation initiatives and further leverage revenue growth. However, as we continue to fund strategic initiatives, our SG&A expense in the second quarter is expected to be at or near 40.5 percent of sales.

We expect to incur approximately \$110 million of expenses in 2012 related to certain restructuring and transformation initiatives. The specific programs related to these expenses are targeted at streamlining the organization and business processes. They are expected to be mostly completed in 2012. We also expect to incur approximately \$15 million for certain acquisition, integration and other costs. We expect to recognize the majority of these \$125 million of expenses in "Special items" on our statement of earnings. The gross margin and SG&A percentages discussed above do not include these expenses.

Assuming variable rates remain at March 31, 2012 levels, we expect interest expense, net of interest income, to be approximately \$60 million in 2012, which is higher than 2011 primarily due to the \$550 million offering of senior notes we completed in November 2011.

## **FIRST QUARTER RESULTS OF OPERATIONS**

### *Net Sales by Operating Segment*

The following table presents net sales by operating segment and the components of the percentage changes (dollars in millions):

	<b>Three Months Ended March 31,</b>		<b>% Inc</b>	<b>Volume/ Mix</b>	<b>Price</b>	<b>Foreign Exchange</b>
	<b>2012</b>	<b>2011</b>				
Americas .....	\$ 634.4	\$ 629.7	1%	4%	(3)%	—%
Europe .....	300.8	299.2	1	5	(1)	(3)
Asia Pacific .....	205.5	186.7	10	8	(1)	3
Total .....	<u>\$1,140.7</u>	<u>\$1,115.6</u>	2	5	(2)	(1)

"Foreign Exchange" as used in the tables in this report represents the effect of changes in foreign currency exchange rates on sales growth.

### Net Sales by Product Category

The following table presents net sales by product category and the components of the percentage changes (dollars in millions):

	Three Months Ended March 31,		% Inc (Dec)	Volume/ Mix	Price	Foreign Exchange
	2012	2011				
Reconstructive						
Knees . . . . .	\$ 470.6	\$ 462.2	2%	5%	(3)%	—%
Hips . . . . .	344.5	337.3	2	4	(2)	—
Extremities . . . . .	44.8	42.9	4	6	(1)	(1)
	859.9	842.4	2	5	(2)	(1)
Dental . . . . .	60.2	62.4	(3)	(3)	1	(1)
Trauma . . . . .	75.5	70.1	8	9	(1)	—
Spine . . . . .	53.2	56.9	(7)	(2)	(4)	(1)
Surgical and other . . . . .	91.9	83.8	10	9	—	1
Total . . . . .	<u>\$1,140.7</u>	<u>\$1,115.6</u>	2	5	(2)	(1)

The following table presents net sales by product category by region (dollars in millions):

	Three Months Ended March 31,		
	2012	2011	% Inc (Dec)
Reconstructive			
Knees			
Americas . . . . .	\$ 278.5	\$ 277.8	—%
Europe . . . . .	118.1	117.2	1
Asia Pacific . . . . .	74.0	67.2	10
Hips			
Americas . . . . .	153.9	154.6	—
Europe . . . . .	114.0	114.2	—
Asia Pacific . . . . .	76.6	68.5	12
Extremities			
Americas . . . . .	35.2	33.2	6
Europe . . . . .	7.0	6.8	2
Asia Pacific . . . . .	2.6	2.9	(9)
	859.9	842.4	2
Dental			
Americas . . . . .	35.3	34.7	2
Europe . . . . .	20.1	20.7	(3)
Asia Pacific . . . . .	4.8	7.0	(32)
Trauma			
Americas . . . . .	37.2	37.0	—
Europe . . . . .	16.0	14.1	13
Asia Pacific . . . . .	22.3	19.0	18
Spine			
Americas . . . . .	36.6	38.8	(6)
Europe . . . . .	12.4	13.8	(11)
Asia Pacific . . . . .	4.2	4.3	(3)
Surgical and other			
Americas . . . . .	57.7	53.6	8
Europe . . . . .	13.2	12.4	7
Asia Pacific . . . . .	21.0	17.8	18
Total . . . . .	<u>\$1,140.7</u>	<u>\$1,115.6</u>	2



## ***Knees***

Knee sales increased 2 percent in the three month period ended March 31, 2012 when compared to the same prior year period. The increase in sales was driven by positive procedure volume/mix for the period, which was better than any similar quarterly measure experienced in 2011. The increase was partially offset by higher pricing pressures in the 2012 period than we experienced in any of the 2011 quarterly periods. We are cautiously optimistic this quarter's uptick in the U.S. Knee market represents the beginnings of an improved environment. However, we are not assuming that this single data point is a trend just yet.

The *NexGen*® Complete Knee Solution product line, including *Gender Solutions*® Knee Femoral Implants, the *NexGen* LPS-Flex Knee and the *NexGen* CR-Flex Knee led knee sales. In addition, sales of the *Gender Solutions* Patello Femoral Joint and *Zimmer*® Patient Specific Instruments exhibited growth. In Europe, changes in foreign currency exchange rates negatively affected knee sales in the three month period ended March 31, 2012 by 4 percent. In Asia Pacific, changes in foreign currency exchange rates positively affected knee sales in the three month period ended March 31, 2012 by 3 percent.

## ***Hips***

Hip sales increased 2 percent in the three month period ended March 31, 2012 when compared to the same prior year period. The increase was driven primarily by higher sales of our primary stems, including the *Zimmer*® M/L Taper Stem and the *Zimmer* M/L Taper Stem with *Kinectiv* Technology, and our *Continuum*® Acetabular System, *Trilogy*® IT Acetabular System and *Allofit*® IT *Alloclassic*® Acetabular System.

Also leading hip stem sales were the *CLS*® *Spotorno*® Stem from the *CLS* Hip System and the *Alloclassic Zweymüller*® Hip Stem. In addition, sales of the *Trabecular Metal* Revision Shell and Augment Cups were strong when compared to the prior year period, as were sales of *BIOLOX*®<sup>1</sup> *delta* Heads and *Fitmore*® Hip Stems. In Europe, changes in foreign currency exchange rates negatively affected hip sales in the three month period ended March 31, 2012 by 3 percent. In Asia Pacific, changes in foreign currency exchange rates positively affected hip sales in the three month period ended March 31, 2012 by 4 percent.

## ***Extremities***

Extremities sales increased by 4 percent in the three month period ended March 31, 2012 when compared to the same prior year period. The *Zimmer Trabecular Metal* Reverse Shoulder System led extremities sales. Reverse shoulder procedures continue to gain popularity as a solution for patients with rotator cuff damage.

## ***Dental***

Dental sales declined by 3 percent in the three month period ended March 31, 2012 when compared to the same prior year period. The decrease was driven by lower sales of dental reconstructive implants and restorative products, partially offset by sales growth in regenerative products and digital solutions. Much of the decline in implants was attributable to our Asia Pacific segment, where we sell through stocking distributors. The timing of bulk orders from these distributors had a negative impact on quarterly sales results. Sales were led by the *Tapered Screw-Vent*® Implant System.

## ***Trauma***

Trauma sales increased 8 percent in the three month period ended March 31, 2012 when compared to the same prior year period. The *Zimmer Natural Nail*® System continued to increase sales significantly. In addition to the *Zimmer Natural Nail* System, the *Zimmer*® Periarticular Locking Plates System led trauma sales, while sales of the *Zimmer*® Universal Locking System also made a strong contribution.

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<sup>1</sup> Registered trademark of CeramTec GmbH



### *Spine*

Spine sales decreased 7 percent in the three month period ended March 31, 2012 when compared to the same prior year period. Each of our geographic segments experienced sales declines. This product category continues to face challenges related to pricing pressure and payor approvals. Solid sales of the *PathFinder NXT*<sup>®</sup> and *Sequoia*<sup>®</sup> Pedicle Screw Systems, the *InCompass*<sup>®</sup> Spinal Fixation System and *Trabecular Metal* Technology products partly offset a decline in sales of the *Dynesys*<sup>®</sup> Dynamic Stabilization System.

### *Surgical and other*

Surgical sales increased 10 percent in the three month period ended March 31, 2012 when compared to the same prior year period. Surgical and other sales were led by *PALACOS*<sup>®2</sup> Bone Cement and tourniquet products. Our wound debridement products, powered instruments and *DeNovo*<sup>®</sup> NT Natural Tissue Graft also made a strong contribution to sales results, as did our January 2012 acquisition of Synvasive Technology, Inc (Synvasive). The Synvasive acquisition enhances our product portfolio through the addition of their *STABLECUT*<sup>®</sup> surgical saw blades.

### *Expenses as a Percent of Net Sales*

	Three Months Ended March 31,		
	2012	2011	Inc (Dec)
Cost of products sold . . . . .	25.3%	25.0%	0.3
Research and development . . . . .	5.2	5.0	0.2
Selling, general and administrative . . . . .	40.6	41.1	(0.5)
Special items . . . . .	2.9	2.3	0.6
Operating profit . . . . .	25.9	26.6	(0.7)

### *Cost of Products Sold*

The increase in cost of products sold as a percentage of net sales for the three month period ended March 31, 2012 compared to the same prior year period is due to higher average costs per unit sold due to lower manufacturing volumes and lower average selling prices. This higher cost per unit in the 2012 period was partially offset by lower excess and obsolescence charges from some product specific matters, lower inventory step-up charges based upon timing of business combinations, and lower royalty charges from expiration of certain contracts.

### *Operating Expenses*

R&D expenses and R&D as a percent of sales increased when compared to the same prior year period. Higher spending reflects investments in new platform development projects across all product categories, including our next generation knee system. We continue to align R&D support functions with our product category leaders to continue to drive a faster pace of product innovation, which is a key feature of our growth strategy. We expect R&D spending in 2012 to be between 5 to 6 percent of sales for the full year.

SG&A increased in dollar terms but decreased as a percent of sales when compared to the same prior year period. The dollar increase is primarily from variable selling expenses resulting from higher net sales in the 2012 period compared to the 2011 period, increased legal costs, increased bad debt expenses, and higher employee recruiting and relocation expenses. This increase was partially offset by lower product liability costs and lower instrument costs. SG&A as a percent of sales has decreased 50 basis points relative to the same prior year period, reflecting disciplined discretionary spending and the effect of our transformation initiatives, which have lowered expenses such as salaries, wages and benefits.

<sup>2</sup> Registered trademark of Heraeus Kulzer GmbH

“Special items” for the three month period ended March 31, 2012 increased to \$33.5 million from \$25.5 million in the prior year period. We continue to implement our transformation programs and have incurred costs related to consulting and professional fees and dedicated personnel costs for those programs, as well as other costs. Additionally, severance costs were recognized as we announced our plans to outsource our Warsaw, Indiana distribution center to a third party service provider at a national transportation hub, among other organizational changes. We also recognized charges related to certain litigation matters.

“Special items” in 2011 was largely composed of employee severance and termination-related expenses resulting from a reduction in management layers, expansion of management spans of control, and changes in our organizational structure. “Special items” also included expenses relating to integration of business acquisitions and fixed asset impairments. See Note 2 to the condensed consolidated financial statements for more information regarding “Special items” charges.

#### ***Interest Income, Interest Expense, Income Taxes and Net Earnings***

Interest expense for the three month period ended March 31, 2012 increased primarily due to the \$550 million offering of senior notes we completed in November 2011. Interest income has increased due to higher balances of cash and cash equivalents and short-term and long-term investments upon which interest income is being earned.

The effective tax rate on earnings before income taxes for the three month period ended March 31, 2012 decreased to 25.7 percent, from 27.0 percent in the same prior year period. The decrease is primarily due to changes in the mix of earnings between taxing jurisdictions. We anticipate the outcome of various federal, state and foreign audits as well as expiration of certain statutes of limitations could potentially impact our 2012 effective tax rate in future quarters. Currently, we cannot reasonably estimate the impact of these items on our financial results.

Net earnings of Zimmer Holdings, Inc. of \$209.6 million for the three month period ended March 31, 2012 was similar to net earnings in the same prior year period of 208.9 million as a result of the changes in revenues and expenses discussed above. For the 2012 period, basic and diluted earnings per share increased 9 percent and 8 percent, respectively, from the same prior year period. The disproportional change in earnings per share as compared with net earnings is attributed to the effect of 2012 and 2011 share repurchases.

#### ***Non-GAAP operating performance measures***

We use non-GAAP financial measures to evaluate our operating performance that differ from financial measures determined in accordance with GAAP. Our non-GAAP financial measures exclude the impact of inventory step-up charges, “Special items,” and the taxes on those items. We use this information internally and believe it is helpful to investors because it allows more meaningful period-to-period comparisons of our ongoing operating results, it helps to perform trend analysis and to better identify operating trends that may otherwise be masked or distorted by these types of items, and it provides a higher degree of transparency of certain items. Certain of these non-GAAP financial measures are used as metrics for our incentive compensation programs.

Our non-GAAP adjusted net earnings used for internal management purposes for the three month periods ended March 31, 2012 and 2011 were \$231.3 million and \$230.9 million, respectively, and our non-GAAP adjusted diluted earnings per share were \$1.30 and \$1.19, respectively.

The following are reconciliations from our GAAP net earnings and diluted earnings per share to our non-GAAP adjusted net earnings and non-GAAP adjusted diluted earnings per share used for internal management purposes.

<u>(In millions)</u>	<b>Three Months Ended March 31,</b>	
	<b>2012</b>	<b>2011</b>
Net Earnings of Zimmer Holdings, Inc. ....	\$209.6	\$208.9
Inventory step-up .....	1.0	4.4
Special items .....	33.5	25.5
Taxes on inventory step-up and special items* .....	(12.8)	(7.9)
Adjusted Net Earnings .....	<u>\$231.3</u>	<u>\$230.9</u>

\* The tax effect is calculated based upon the statutory rates for the jurisdictions where the items were incurred.

	<b>Three Months Ended March 31,</b>	
	<b>2012</b>	<b>2011</b>
Diluted EPS .....	\$ 1.17	\$ 1.08
Inventory step-up .....	0.01	0.02
Special items .....	0.19	0.13
Taxes on inventory step-up and special items* .....	(0.07)	(0.04)
Adjusted Diluted EPS .....	<u>\$ 1.30</u>	<u>\$ 1.19</u>

\* The tax effect is calculated based upon the statutory rates for the jurisdictions where the items were incurred.

### ***Healthcare Reform in the U.S.***

We continue to assess the impact that federal healthcare reform will have on our business. Federal healthcare reform includes a 2.3 percent excise tax on a majority of our U.S. sales that is scheduled to be implemented in 2013. We do not expect to be able to offset the full impact of the tax on net earnings through higher pricing on our products or through higher sales volumes resulting from the expansion of health insurance coverage. However, we believe we will be able to fully offset the financial impact of the tax through savings generated from our various transformation programs and other cost savings initiatives.

### **Liquidity and Capital Resources**

Cash flows provided by operating activities were \$207.4 million for the three month period ended March 31, 2012, compared to \$182.2 million in the same prior year period. The principal source of cash from operating activities was net earnings. Non-cash items included in net earnings accounted for another \$110.6 million of operating cash. All other items of operating cash flows reflect a use of \$112.1 million of cash, compared to a use of \$131.5 million in the same 2011 period. The higher cash flows provided by operating activities in the 2012 period were primarily due to the timing of tax payments, which were partially offset by increased product liability payments.

At March 31, 2012, we had 70 days of sales outstanding in trade accounts receivable, which represents an increase of 6 days compared to December 31, 2011 and an increase of 4 days compared to March 31, 2011, reflecting the economic environment in our Europe operating segment. At March 31, 2012, we had 293 days of inventory on hand, which is an increase of 16 days compared to December 31, 2011 and a decrease of 19 days from March 31, 2011. This reflects relatively stable inventory balances despite an increase in sales.

Cash flows used in investing activities were \$164.2 million for the three month period ended March 31, 2012, compared to \$66.9 million in the same prior year period. Additions to instruments decreased in the 2012 period compared to the 2011 period as the 2011 period reflected purchases for some significant product launches, such as our *Continuum* Acetabular System. Spending on other property, plant and equipment was relatively

consistent between the 2012 period and the 2011 period, reflecting cash outlays necessary to complete new product-related investments and replace older machinery and equipment. We invest some of our cash and cash equivalents in highly-rated debt securities. The purchases and any sales or maturities of these investments are reflected as cash flows from investing activities. The timing of these investments can vary from quarter to quarter depending on the maturity of the debt securities and other cash and cash equivalent needs. Investments in other assets increased in the 2012 period compared to the 2011 period primarily related to the acquisition of Synvative.

Cash flows used in financing activities were \$129.1 million for the three month period ended March 31, 2012, compared to \$216.5 million in the same 2011 period. In the 2012 period, we repurchased 2.3 million common shares for a total of \$141.6 million, including commissions, under our share repurchase program authorized by our Board of Directors, compared to \$236.1 million in the same 2011 period.

In December 2011, our Board of Directors declared a dividend of \$0.18 per share, resulting in \$31.7 million to be paid in April 2012. We expect to continue paying cash dividends on a quarterly basis; however, future dividends are subject to approval of the Board of Directors and may be adjusted for reasons the Board deems appropriate, such as changes in market conditions or business needs.

We have four tranches of senior notes outstanding: \$250 million aggregate principal amount of 1.4 percent notes due November 30, 2014, \$500 million aggregate principal amount of 4.625 percent notes due November 30, 2019, \$300 million aggregate principal amount of 3.375 percent notes due November 30, 2021 and \$500 million aggregate principal amount of 5.75 percent notes due November 30, 2039. Interest on each series is payable on May 30 and November 30 of each year until maturity.

We may redeem the senior notes at our election in whole or in part at any time prior to maturity at a redemption price equal to the greater of 1) 100 percent of the principal amount of the notes being redeemed; or 2) the sum of the present values of the remaining scheduled payments of principal and interest (not including any portion of such payments of interest accrued as of the date of redemption), discounted to the date of redemption on a semi-annual basis at the Treasury Rate (as defined in the debt agreement), plus 15 basis points in the case of the 2014 notes, 20 basis points in the case of the 2019 and 2021 notes, and 25 basis points in the case of the 2039 notes. We will also pay the accrued and unpaid interest on the senior notes to the redemption date.

We have a five year \$1,350 million revolving, multi-currency, senior unsecured credit facility maturing November 30, 2012 (Senior Credit Facility). We had \$141.8 million outstanding under the Senior Credit Facility at March 31, 2012, and an availability of \$1,208.2 million. We expect to finalize and enter into another senior credit facility in the second quarter of 2012 before our current Senior Credit Facility matures.

We also have available uncommitted credit facilities totaling \$73.0 million.

We place our cash and cash equivalents in highly-rated financial institutions and limit the amount of credit exposure to any one entity. We invest only in high-quality financial instruments in accordance with our internal investment policy.

As of March 31, 2012, we had short-term and long-term investments in debt securities with a fair value of \$752.0 million. These investments are in debt securities of many different issuers and therefore we have no significant concentration of risk with a single issuer. All of these debt securities remain highly-rated and therefore we believe the risk of default by the issuers is low.

As of March 31, 2012, \$1,210.4 million of our cash and cash equivalents and short-term and long-term investments are held in jurisdictions outside of the U.S. and are expected to be indefinitely reinvested for continued use in foreign operations. Repatriation of these assets to the U.S. would have negative tax consequences. Approximately \$1,125.0 million of this amount is denominated in U.S. Dollars and therefore bears no foreign currency translation risk. The balance of these assets is denominated in currencies of the various countries where we operate.

Our concentrations of credit risks with respect to trade accounts receivable is limited due to the large number of customers and their dispersion across a number of geographic areas and by frequent monitoring of the creditworthiness of the customers to whom credit is granted in the normal course of business. Substantially all of our trade receivables are concentrated in the public and private hospital and healthcare industry in the U.S. and internationally or with distributors or dealers who operate in international markets and, accordingly, are exposed to their respective business, economic and country specific variables.

Our ability to collect accounts receivable in some countries depends in part upon the financial stability of these hospital and healthcare sectors and the respective countries' national economic and healthcare systems. Most notably, in Europe healthcare is typically sponsored by the government. Since we sell products to public hospitals in those countries, we are indirectly exposed to government budget constraints. The ongoing financial crisis in the Euro zone impacts the indirect credit exposure we have to those governments through their public hospitals. We have experienced an increasing number of days sales outstanding in some European countries. In Greece, Italy, Portugal and Spain, countries that have been widely recognized as presenting the highest risk, our short-term and long-term trade accounts receivable, net of allowances for doubtful accounts, as of March 31, 2012 totaled \$242.1 million, or 27% of our total short-term and long-term trade accounts receivable balance, net, with Italy and Spain accounting for \$229.8 million of that amount. We are actively monitoring the situations in these countries and, to the extent the respective governments' ability to fund their public hospital programs deteriorates, we may have to record significant bad debt expenses in the future.

We may use excess cash to repurchase additional common stock under our share repurchase program. As of March 31, 2012, approximately \$1.4 billion remained authorized under a \$1.5 billion repurchase program, which will expire on December 31, 2014.

Management believes that cash flows from operations and available borrowings under the Senior Credit Facility are sufficient to meet our working capital, capital expenditure, dividend and debt service needs. Should investment opportunities arise, we believe that our earnings, balance sheet and cash flows will allow us to obtain additional capital, if necessary.

### **Recent Accounting Pronouncements**

See Note 2 to our condensed consolidated financial statements included in Part I, Item 1 of this report to see how recent accounting pronouncements have affected or may affect our financial position, results of operations and cash flows.

### **Forward-Looking Statements**

This quarterly report contains certain statements that are forward-looking statements within the meaning of federal securities laws. Forward-looking statements can be identified by the fact that they do not relate strictly to historical or current facts. When used in this report, the words "may," "will," "should," "would," "could," "anticipate," "expect," "plan," "seek," "believe," "predict," "estimate," "potential," "project," "target," "forecast," "intend," "strategy," "future," "opportunity," "assume," "guide" and similar expressions are intended to identify forward-looking statements. Forward-looking statements are based on current expectations and assumptions that are subject to risks and uncertainties that could cause actual results to differ materially from such forward-looking statements. These risks and uncertainties include, but are not limited to:

- our compliance through September 2012 with the Corporate Integrity Agreement we entered into as part of the 2007 settlement with the U.S. government;
- the outcome of the investigation by the U.S. government into Foreign Corrupt Practices Act matters announced in October 2007;
- competition;
- pricing pressures;

- changes in customer demand for our products and services caused by demographic changes or other factors;
- dependence on new product development, technological advances and innovation;
- product liability claims;
- retention of our independent agents and distributors;
- our ability to protect proprietary technology and other intellectual property and claims for infringement of the intellectual property rights of third parties;
- the possible disruptive effect of additional strategic acquisitions and our ability to successfully integrate acquired companies;
- our ability to form and implement strategic alliances;
- our dependence on a limited number of suppliers for key raw materials and outsourced activities;
- the impact of the federal healthcare reform legislation, including the impact of the new excise tax on medical devices;
- reductions in reimbursement levels by third-party payors and cost containment efforts of healthcare purchasing organizations;
- the impact of the ongoing financial crisis on countries in the Euro zone on our ability to collect accounts receivable in affected countries;
- challenges relating to changes in and compliance with governmental laws and regulations affecting our U.S. and international businesses, including regulations of the U.S. Food and Drug Administration and foreign government regulators, such as more stringent requirements for regulatory clearance of our products;
- changes in tax obligations arising from tax reform measures or examinations by tax authorities;
- the success of our quality and operational improvement initiatives;
- changes in prices of raw materials and products and our ability to control costs and expenses;
- changes in general domestic and international economic conditions, including interest rate and currency exchange rate fluctuations;
- changes in general industry and market conditions, including domestic and international growth rates; and
- shifts in our product category sales mix or our regional sales mix away from products or geographic regions that generate higher operating margins.

Our Annual Report on Form 10-K for the year ended December 31, 2011 contains a detailed discussion of these and other important factors under the heading “Risk Factors” in Part I, Item 1A of that report. You should understand that it is not possible to predict or identify all factors that could cause actual results to differ materially from forward-looking statements. Consequently, you should not consider any list or discussion of such factors to be a complete set of all potential risks or uncertainties.

Readers of this report are cautioned not to place undue reliance on these forward-looking statements. While we believe the assumptions on which the forward-looking statements are based are reasonable, there can be no assurance that these forward-looking statements will prove to be accurate. This cautionary statement is applicable to all forward-looking statements contained in this report.

We expressly disclaim any obligation to update or revise any forward-looking statements, whether as a result of new information, future events or otherwise. You are advised, however, to consult any further disclosures we make on related subjects in our Form 10-Q, 8-K and 10-K reports and our other filings with the Securities and Exchange Commission.



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

There have been no material changes from the information provided in our Annual Report on Form 10-K for the year ended December 31, 2011.

**Item 4. *Controls and Procedures*****Evaluation of Disclosure Controls and Procedures**

We maintain disclosure controls and procedures (as defined in Rules 13a-15(e) under the Securities Exchange Act of 1934 (Exchange Act)) that are designed to provide reasonable assurance that information required to be disclosed in the reports that we file or submit under the Exchange Act is recorded, processed, summarized and reported within the time periods specified in the SEC's rules and forms, and that such information is accumulated and communicated to our management, including our Chief Executive Officer and Chief Financial Officer, as appropriate to allow timely decisions regarding required disclosures. Because of inherent limitations, disclosure controls and procedures, no matter how well designed and operated, can provide only reasonable, and not absolute, assurance that the objectives of disclosure controls and procedures are met.

Our management, with the participation of our Chief Executive Officer and Chief Financial Officer, evaluated the effectiveness of the design and operation of our disclosure controls and procedures. Based on that evaluation, our Chief Executive Officer and Chief Financial Officer concluded that, as of the end of the period covered by this report, our disclosure controls and procedures are effective at a reasonable assurance level.

**Changes in Internal Control Over Financial Reporting**

During the quarter ended March 31, 2012, we continued transitioning work to a third-party service provider to outsource certain finance functions that historically have been performed in multiple countries throughout Europe and in the U.S. We also continued centralizing other finance functions that historically have been performed in a decentralized manner. This outsourcing and centralization is part of our ongoing global business transformation initiatives, and we plan to continue transitioning work to the service provider and the centralized finance departments over the course of 2012.

Also in 2012, we intend to implement new software to consolidate our worldwide financial information. This software implementation is part of our transformation initiatives in order to improve the overall efficiency and effectiveness of our financial reporting process.

In connection with the outsourcing, centralization of finance functions, and software implementation and the resulting business process changes, we continue to enhance the design and documentation of our internal control processes to ensure suitable controls over our financial reporting. There were no other changes in our internal control over financial reporting (as defined in Rule 13a-15(f) of the Exchange Act) that occurred during the quarter ended March 31, 2012 that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

## Part II — Other Information

### Item 1. Legal Proceedings

Information pertaining to legal proceedings can be found in Note 14 to the interim condensed consolidated financial statements included in Part I, Item 1 of this report.

### Item 1A. Risk Factors

Except as set forth below, there have been no material changes from the risk factors disclosed in Part I, Item 1A of our Annual Report on Form 10-K for the year ended December 31, 2011.

The risk factor entitled **“In July 2011, we received Form FDA-483 Inspectional Observations from the FDA concerning quality systems at our Warsaw, Indiana manufacturing facility and we may not be able to timely and adequately address the quality system issues raised by the FDA”** is revised as follows:

Following a July 2011 routine inspection of our Warsaw, Indiana manufacturing facility, the FDA issued a Form 483 notice. The Form 483 notice identified certain inspectional observations regarding the facility’s quality systems. The facility manufactures reconstructive products that are sold globally. We responded in writing to the observations and met with representatives of the district office of the FDA to discuss our response and action plans. We have been executing our action plans and communicating on a regular basis with representatives of the district office of the FDA on the status of our execution of the action plans. As anticipated, in April 2012, the FDA commenced a re-inspection of our Warsaw, Indiana manufacturing facility and this matter is on-going. If the FDA is not satisfied with the results of the re-inspection, the FDA could take additional actions such as issuing a warning letter to us, which, among other things, could adversely affect our ability to receive approvals of regulatory applications until the issues are resolved. Any of these possible sanctions could have an adverse impact on our revenues, financial position, results of operations and cash flows, and otherwise harm our business and reputation.

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

The following table summarizes repurchases of common stock settled during the three month period ended March 31, 2012:

	Total Number of Shares Purchased	Average Price Paid per Share	Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs*	Approximate Dollar Value of Shares that May Yet Be Purchased Under Plans or Programs
January 2012 .....	—	\$ —	77,936,850	\$1,500,000,000
February 2012 .....	1,029,800	61.53	78,966,650	1,436,632,347
March 2012 .....	1,290,000	60.63	80,256,650	1,358,415,859
Total .....	<u>2,319,800</u>	<u>\$61.03</u>	<u>80,256,650</u>	<u>\$1,358,415,859</u>

\* Includes repurchases made under expired programs as well as the current program authorizing \$1.5 billion of repurchases through December 31, 2014.

### Item 5. Other Information

During the period covered by this report, the Audit Committee of our Board of Directors approved the engagement of PricewaterhouseCoopers LLP, our independent registered public accounting firm, to perform certain non-audit services related to certain accounting and tax matters. This disclosure is made pursuant to Section 10A(i)(2) of the Exchange Act, as added by Section 202 of the Sarbanes-Oxley Act of 2002.



**Item 6. Exhibits**

The following exhibits are filed or furnished as part of this report:

31.1	Certification pursuant to Rule 13a-14(a)/15d-14(a) of the Securities Exchange Act of 1934 of the Chief Executive Officer, as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
31.2	Certification pursuant to Rule 13a-14(a)/15d-14(a) of the Securities Exchange Act of 1934 of the Chief Financial Officer, as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
32	Certifications pursuant to 18 U.S.C. Section 1350, as adopted pursuant to 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.LAB	XBRL Taxonomy Extension Label Linkbase Document
101.PRE	XBRL Taxonomy Extension Presentation Linkbase Document
101.DEF	XBRL Taxonomy Extension Definition Linkbase Document

## 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.

ZIMMER HOLDINGS, INC.  
(Registrant)

Date: May 3, 2012

By: /s/ James T. Crines  
James T. Crines  
*Executive Vice President, Finance and  
Chief Financial Officer*

Date: May 3, 2012

By: /s/ Derek M. Davis  
Derek M. Davis  
*Vice President, Finance and Corporate  
Controller and Chief Accounting Officer*

**CERTIFICATION PURSUANT TO RULE 13a-14(a)/15d-14(a) OF THE SECURITIES EXCHANGE ACT OF 1934, AS ADOPTED PURSUANT TO SECTION 302 OF THE SARBANES-OXLEY ACT OF 2002**

I, David C. Dvorak, certify that:

1. I have reviewed this quarterly report on Form 10-Q of Zimmer Holdings, Inc.;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
  - (a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
  - (b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
  - (c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
  - (d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors:
  - (a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
  - (b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: May 3, 2012

/s/ David C. Dvorak

David C. Dvorak

*President and Chief Executive Officer*

**CERTIFICATION PURSUANT TO RULE 13a-14(a)/15d-14(a) OF THE SECURITIES EXCHANGE ACT OF 1934, AS ADOPTED PURSUANT TO SECTION 302 OF THE SARBANES-OXLEY ACT OF 2002**

I, James T. Crines, certify that:

1. I have reviewed this quarterly report on Form 10-Q of Zimmer Holdings, Inc.;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
  - (a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
  - (b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
  - (c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
  - (d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors:
  - (a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
  - (b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: May 3, 2012

/s/ James T. Crines

James T. Crines  
Executive Vice President, Finance  
and Chief Financial Officer

**CERTIFICATION PURSUANT TO  
18 U.S.C. SECTION 1350,  
AS ADOPTED PURSUANT TO  
SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002**

In connection with the Quarterly Report of Zimmer Holdings, Inc. (the “Company”) on Form 10-Q for the period ending March 31, 2012 as filed with the Securities and Exchange Commission on the date hereof (the “Report”), each of the undersigned certify, pursuant to 18 U.S.C. § 1350, as adopted pursuant to § 906 of the Sarbanes-Oxley Act of 2002, that:

(1) The Report fully complies with the requirements of section 13(a) or 15(d) of the Securities Exchange Act of 1934; and

(2) The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

/s/ David C. Dvorak

David C. Dvorak  
*President and Chief Executive Officer*

May 3, 2012

/s/ James T. Crines

James T. Crines  
*Executive Vice President, Finance  
and Chief Financial Officer*

May 3, 2012