Hill-Rom Holdings, Inc.
Form 10-Q
February 01, 2016

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

FORM 10-Q

(Mark One)

x Quarterly Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934
For the quarterly period ended December 31, 2015

OR

o Transition Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934
For the transition period from ____ to ____

Commission File No. 1-6651

HILL-ROM HOLDINGS, INC.
(Exact name of registrant as specified in its charter)

Indiana	35-1160484
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)

Two Prudential Plaza, Suite 4100

Chicago, IL	60601
(Address of principal executive offices)	(Zip Code)

(312) 819-7200
(Registrant's telephone number, including area code)

Not Applicable
(Former name, former address and former fiscal year, if changed since last report)

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.

Yes þ No o

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 þ No o

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company (as defined in Rule 12b-2 of the Exchange Act).

Large accelerated filer R Accelerated filer £ Non-accelerated filer £ 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 o No þ

Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date.

Common Stock, without par value – 65,316,490 shares as of January 25, 2016.

HILL-ROM HOLDINGS, INC.

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PART I – FINANCIAL INFORMATION

Item 1. FINANCIAL STATEMENTS

Hill-Rom Holdings, Inc. and Subsidiaries
Condensed Consolidated Statements of Income (Unaudited)
(In millions, except per share data)

	Quarter Ended December 31	
	2015	2014
Net Revenue		
Capital sales	$ 565.1	$ 373.4
Rental revenue	96.1	91.6
Total revenue	661.2	465.0
Cost of Revenue		
Cost of goods sold	323.1	220.5
Rental expenses	47.4	44.6
Total cost of revenue	370.5	265.1
Gross Profit	290.7	199.9
Research and development expenses	33.6	21.8
Selling and administrative expenses	221.2	155.1
Special charges (Note 8)	7.1	3.7
Operating Profit	28.8	19.3
Interest expense	(22.5)	(3.2)
Investment income and other, net	(0.5)	0.9
Income Before Income Taxes	5.8	17.0
Income tax expense (Note 9)	1.5	4.9
Net Income	4.3	12.1
Less: Net loss attributable to noncontrolling interests	(0.5)	-
Net Income Attributable to Common Shareholders	$ 4.8	$ 12.1
Net Income Attributable to Common Shareholders per Common Share - Basic	$ 0.07	$ 0.21
Net Income Attributable to Common Shareholders per Common Share - Diluted	$ 0.07	$ 0.21
Dividends per Common Share	$ 0.1600	$ 0.1525

Average Common Shares Outstanding - Basic (thousands) (Note 10)	65,217	57,137
Average Common Shares Outstanding - Diluted (thousands) (Note 10)	66,274	58,154

See Notes to Condensed Consolidated Financial Statements

Hill-Rom Holdings, Inc. and Subsidiaries
Condensed Consolidated Statements of Comprehensive Income (Loss)
(Unaudited)
(In millions)

	Quarter Ended December 31	
	2015	2014
Net Income	$ 4.3	$ 12.1
Other Comprehensive Income (Loss), net of tax (Note 7):		
Available-for-sale securities and currency hedges	0.1	(0.4)
Foreign currency translation adjustment	(10.2)	(22.6)
Change in pension and postretirement defined benefit plans	0.7	0.9
Total Other Comprehensive Income (Loss), net of tax	(9.4)	(22.1)
Total Comprehensive Income (Loss)	(5.1)	(10.0)
Less: Comprehensive loss attributable to noncontrolling interests	(0.5)	-
Total Comprehensive Income (Loss) Attributable to Common Shareholders	$ (4.6)	$ (10.0)

See Notes to Condensed Consolidated Financial Statements

Hill-Rom Holdings, Inc. and Subsidiaries
Condensed Consolidated Balance Sheets (Unaudited)
(In millions)

	December 31, 2015	September 30, 2015
ASSETS		
Current Assets		
Cash and cash equivalents	$ 174.4	$ 192.8
Trade accounts receivable, net of allowances (Note 2)	460.6	494.7
Inventories (Note 2)	248.9	267.4
Deferred income taxes (Notes 1 and 9)	-	77.0
Other current assets	105.4	109.1
Total current assets	989.3	1,141.0
Property, plant and equipment, net (Note 2)	375.3	378.4
Goodwill (Note 4)	1,607.8	1,610.5
Software and other intangible assets, net (Note 2)	1,221.6	1,247.7
Deferred income taxes (Notes 1 and 9)	26.1	21.6
Other assets	51.5	58.4
Total Assets	$ 4,271.6	$ 4,457.6
LIABILITIES		
Current Liabilities		
Trade accounts payable	$ 114.7	$ 136.3
Short-term borrowings (Note 5)	64.4	58.0
Accrued compensation	99.5	171.8
Accrued product warranties (Note 12)	32.7	32.1
Accrued rebates	39.6	33.7
Other current liabilities	142.5	146.9
Total current liabilities	493.4	578.8
Long-term debt (Note 5)	2,136.2	2,175.2
Accrued pension and postretirement benefits (Note 6)	118.6	118.8
Deferred income taxes (Notes 1 and 9)	332.6	380.6
Other long-term liabilities	44.6	47.3
Total Liabilities	3,125.4	3,300.7
Commitments and Contingencies (Note 14)		
SHAREHOLDERS' EQUITY		
Common Stock (Note 2)	4.4	4.4
Additional paid-in-capital	563.3	562.0
Retained earnings	1,504.2	1,509.9
Accumulated other comprehensive loss (Note 7)	(150.2)	(140.8)
Treasury stock, at cost (Note 2)	(785.0)	(788.6)
Total Shareholders' Equity Attributable to Common Shareholders	1,136.7	1,146.9
Noncontrolling interests	9.5	10.0
Total Shareholders' Equity	1,146.2	1,156.9
Total Liabilities and Shareholders' Equity	$ 4,271.6	$ 4,457.6

See Notes to Condensed Consolidated Financial Statements

Hill-Rom Holdings, Inc. and Subsidiaries
Condensed Consolidated Statements of Cash Flows (Unaudited)
(In millions)

	Quarter Ended December 31	
	2015	2014
Operating Activities		
Net income	$ 4.3	$ 12.1
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation	23.6	17.3
Amortization	4.3	2.9
Acquisition-related intangible asset amortization	24.2	8.1
Provision for deferred income taxes	22.3	0.3
Loss (gain) on disposal of property, equipment leased to others, intangible assets, and impairments	0.7	(0.3)
Stock compensation	5.0	4.7
Excess tax benefits from employee stock plans	(1.0)	(1.0)
Change in working capital excluding cash, current debt, acquisitions and dispositions:		
Trade accounts receivable	31.6	36.1
Inventories	17.4	4.3
Other current assets	3.5	(3.2)
Trade accounts payable	(23.8)	(16.0)
Accrued expenses and other liabilities	(66.1)	(30.6)
Other, net	0.2	(3.7)
Net cash provided by operating activities	46.2	31.0
Investing Activities		
Capital expenditures and purchases of intangible assets	(17.7)	(44.9)
Proceeds on sale of property and equipment leased to others	0.3	0.5
Net cash used in investing activities	(17.4)	(44.4)
Financing Activities		
Net change in short-term debt	-	(0.7)
Borrowings on revolving credit facility	-	95.0
Payment of long-term debt	(34.5)	(3.8)
Purchase of noncontrolling interest of former joint venture	(0.4)	(1.0)
Payment of cash dividends	(10.4)	(8.6)
Proceeds on exercise of stock options	0.7	4.7
Proceeds from stock issuance	0.8	0.7
Excess tax benefits from employee stock plans	1.0	1.0
Treasury stock acquired	(2.8)	(56.9)
Net cash provided by (used in) financing activities	(45.6)	30.4
Effect of exchange rate changes on cash	(1.6)	(2.6)
Net Cash Flows	(18.4)	14.4

Cash and Cash Equivalents:		
At beginning of period	192.8	99.3
At end of period	$ 174.4	$ 113.7

See Notes to Condensed Consolidated Financial Statements

Hill-Rom Holdings, Inc. and Subsidiaries
Notes to Condensed Consolidated Financial Statements (Unaudited)
(Dollars in millions except per share data)

1. Summary of Significant Accounting Policies

Basis of Presentation and Principles of Consolidation

Unless the context otherwise requires, the terms “Hill-Rom,” “the Company,” “we,” “our,” and “us” refer to Hill-Rom Holdin Inc. and its wholly-owned subsidiaries. The unaudited Condensed Consolidated Financial Statements appearing in this Quarterly Report on Form 10-Q should be read in conjunction with the audited Consolidated Financial Statements and notes thereto included in Hill-Rom’s latest Annual Report on Form 10-K for the fiscal year ended September 30, 2015 (“2015 Form 10-K”) as filed with the United States (“U.S.”) Securities and Exchange Commission. The September 30, 2015 Condensed Consolidated Balance Sheet was derived from audited Consolidated Financial Statements, but does not include all disclosures required by accounting principles generally accepted in the U.S. In the opinion of management, the Condensed Consolidated Financial Statements herein include all adjustments, consisting only of normal recurring adjustments, necessary to state fairly the financial position, results of operations and cash flows for the interim periods presented. Quarterly results are not necessarily indicative of annual results.

The Condensed Consolidated Financial Statements include the accounts of Hill-Rom and its wholly-owned subsidiaries. In addition, we also consolidate variable interest entities (VIEs) where Hill-Rom is deemed to have a controlling financial interest. Intercompany accounts and transactions have been eliminated in consolidation, including the intercompany transactions with consolidated VIEs. Where our ownership interest is less than 100 percent, the noncontrolling interests are reported in our Condensed Consolidated Financial Statements.

Use of Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the U.S. requires the Company’s management to make estimates and assumptions that affect the reported amounts of certain assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenue and expense during the period. Actual results could differ from those estimates. Examples of such estimates include income taxes (Notes 1 and 9), accounts receivable reserves (Note 2), accrued warranties (Note 12), the impairment of intangibles and goodwill (Note 4), use of the spot yield curve approach for pension expense (Note 6), and commitments and contingencies (Note 14), among others.

Fair Value Measurements

Fair value measurements are classified and disclosed in one of the following three categories:

- Level 1: Financial instruments with unadjusted quoted prices in active markets that are accessible at the measurement date for identical, unrestricted assets and liabilities.

- Level 2: Financial instruments with observable inputs other than those included in Level 1 such as quoted prices for similar assets or liabilities; quoted prices in markets that are not active; or other inputs that are observable or can be corroborated by observable market data for substantially the full term of the assets or liabilities.

- Level 3: Financial instruments with unobservable inputs that are supported by little or no market activity and that are significant to the fair value of the assets or liabilities. Unobservable inputs reflect our own assumptions that market participants would use in pricing the asset or liability (including assumptions about risk). Unobservable inputs shall be developed based on the best information available in the circumstances, which might include our own data.

We record cash and cash equivalents, as disclosed on our Condensed Consolidated Balance Sheets, as Level 1 instruments and certain other insignificant derivatives and investments as either Level 2 or 3 instruments. Refer to Note 5 for disclosure of our debt instrument fair values.

Taxes Collected from Customers and Remitted to Governmental Units

Taxes assessed by a governmental authority that are directly imposed on a revenue producing transaction between us and our customers, including but not limited to sales taxes, use taxes and value added taxes, are accounted for on a net (excluded from revenue and costs) basis.

Income Taxes

Hill-Rom and its eligible domestic subsidiaries file a consolidated U.S. income tax return. Foreign operations file income tax returns in a number of jurisdictions. Deferred income taxes are computed using an asset and liability approach to reflect the net tax effects of temporary differences between the financial reporting carrying amounts of assets and liabilities and the corresponding income tax amounts. We have a variety of deferred tax assets in numerous tax jurisdictions. These deferred tax assets are subject to periodic assessment as to recoverability. If it is determined that it is more likely than not that the benefits will not be realized, valuation allowances are recognized. In evaluating whether it is more likely than not that we would recover these deferred tax assets, future taxable income, the reversal of existing temporary differences and tax planning strategies are considered.

As of December 31, 2015, we had $40.3 million of valuation allowances on deferred tax assets, on a tax-effected basis, primarily related to foreign operating loss carryforwards and other tax attributes. We believe that our estimates for the valuation allowances recorded against deferred tax assets are appropriate based on current facts and circumstances.

We account for uncertain income tax positions using a threshold and measurement attribute for the financial statement recognition and measurement of a tax position taken or expected to be taken in a tax return. The difference between the tax benefit recognized in the financial statements for an uncertain income tax position and the tax benefit claimed in the tax return is referred to as an unrecognized tax benefit.

Recently Issued Accounting Standards

In May 2014, the FASB issued Accounting Standards Update ("ASU") 2014-09, "Revenue from Contracts with Customers," which provides guidance for revenue recognition. The standard's core principle is that a company will recognize revenue when it transfers promised goods or services to customers in an amount that reflects the consideration to which the company expects to be entitled in exchange for those goods or services. In August 2015, the FASB issued ASU 2015-14 which delayed the effective date of the new revenue guidance by one year. As a result, the provisions of ASU 2014-09 will be effective for us in the first quarter of fiscal 2019, ending December 31, 2018. Early adoption is permitted as of the original effective date, but not earlier. We are currently in the process of evaluating the impact of adoption of this ASU on our Consolidated Financial Statements.

In November 2015, the FASB issued ASU 2015-17, Income Taxes (Topic 740), "Balance Sheet Classification of Deferred Taxes." The amendments in this update simplify the presentation of deferred income taxes by requiring deferred tax assets and liabilities to be classified as noncurrent in a classified balance sheet. As permitted, the Company elected to early-adopt this standard in the first quarter of fiscal 2016 on a prospective basis. Prior period amounts were not retrospectively adjusted for the impacts of this ASU.

Except as noted above, there have been no significant changes to our assessment of the impact of recently issued accounting standards included in Note 1 of Notes to Consolidated Financial Statements in our Fiscal 2015 Form 10-K.

2. Supplementary Balance Sheet Information

	December 31, 2015	September 30, 2015
Allowance for possible losses and discounts on trade receivables	$ 26.5	$ 26.0
Inventories:		
Finished products	$ 119.9	$ 133.2
Raw materials and work in process	129.0	134.2
Total inventory	$ 248.9	$ 267.4
Accumulated depreciation of property, plant and equipment	$ 610.9	$ 598.0
Accumulated amortization of software and other intangible assets	$ 324.3	$ 304.4
Preferred stock, without par value:		
Shares authorized	1,000,000	1,000,000
Shares issued	None	None
Common stock, without par value:		
Shares authorized	199,000,000	199,000,000
Shares issued	88,457,634	88,457,634
Shares outstanding	65,299,252	65,165,896
Treasury shares	23,158,382	23,291,738

3. Acquisitions

Welch Allyn

On September 8, 2015, we completed the acquisition of Welch Allyn Holdings, Inc. and its subsidiaries (collectively, “Welch Allyn”) for a consideration of $1,687.3 million in cash ($1,633.6 million, net of cash acquired) and 8,133,722 shares of Hill-Rom common stock for a total combined purchase price of approximately $2.1 billion. Welch Allyn is a leading manufacturer of medical diagnostic equipment and offers a diversified portfolio of devices that assess, diagnose, treat, and manage a wide variety of illnesses and diseases.

The cash portion of the consideration is preliminary and subject to adjustment for various true-up provisions as described in the terms of the merger agreement. The transaction was funded with new borrowings, including $1.8 billion in term loans and $425.0 million of senior notes issued in a private placement debt offering. Funds from this new financing were also used to retire pre-existing debt. Refer to Note 5 for additional information regarding our debt obligations.

The following summarizes the fair value of assets acquired and liabilities assumed at the date of the acquisition. During the first quarter of 2016, we made certain adjustments to the opening balance sheet as of the acquisition date which were insignificant. These results are preliminary and subject to normal true-up provisions in the purchase agreement and other fair value adjustments.

		Amount	
Trade receivables	$	63.2	
Inventory		110.5	
Other current assets		52.7	
Current deferred income taxes		27.3	
Property, plant, and equipment		93.2	
Goodwill		1,203.5	
Trade name (indefinite life)		434.0	
Customer relationships (12-year useful life)		516.8	
Developed technology (7-year weighted average useful life)		54.0	
Other intangibles		19.9	
Other noncurrent assets		30.3	
Current liabilities		(161.5	)
Noncurrent deferred income taxes		(368.9	)
Other noncurrent liabilities		(25.1	)
Total purchase price, net of cash acquired	$	2,049.9	
Fair value of common stock issued	$	416.3	
Cash payment, net of cash acquired		1,633.6	
Total consideration	$	2,049.9	

Goodwill from the Welch Allyn acquisition, which is not deductible for tax purposes, is primarily due to enhanced customer relevance and a stronger competitive position resulting from the business combination, including a complementary commercial position, product portfolio, and enhanced synergies. Welch Allyn is reported as its own reportable segment for the quarter ended December 31, 2015.

Our total revenue on an unaudited pro forma basis, as if the Welch Allyn acquisition had been consummated at the beginning of our 2014 fiscal year, would have been higher by approximately $190 million for the quarter ended December 31, 2014. On the same unaudited pro forma basis, our net income would have been lower by approximately $8 million for the quarter ended December 31, 2014. Pro forma net income is adversely impacted by significant costs related to the transaction including financing costs and purchase price accounting, including the effects of amortization of acquisition-related intangibles. These results are not indicative of expected future performance.

The unaudited pro forma results are based on the Company’s historical financial statements and those of the Welch Allyn business and do not necessarily indicate the results of operations that would have resulted had the acquisition been completed at the beginning of the comparable period presented and are not indicative of the results of operations in future periods.

4. Goodwill and Indefinite-Lived Intangible Assets

The following summarizes goodwill activity by reportable segment:

	North America	Surgical and Respiratory Care	International	Welch Allyn	Total
Balances at September 30, 2015:					
Goodwill	$ 390.6	$ 343.8	$ 145.4	$ 1,203.5	$ 2,083.3
Accumulated impairment losses	(358.1)	-	(114.7)	-	(472.8)
Goodwill, net at September 30, 2015	32.5	343.8	30.7	1,203.5	1,610.5
Changes in Goodwill during the period:					
Goodwill related to acquisitions	-	-	-	-	-
Currency translation effect	-	(2.1)	(0.6)	-	(2.7)
Balances at December 31, 2015:					
Goodwill	390.6	341.7	144.8	1,203.5	2,080.6
Accumulated impairment losses	(358.1)	-	(114.7)	-	(472.8)
Goodwill, net at December 31, 2015	$ 32.5	$ 341.7	$ 30.1	$ 1,203.5	$ 1,607.8

5. Financing Agreements

Total debt consists of the following:

	December 31, 2015	September 30, 2015
Current portion of long-term debt	$ 64.4	$ 58.0
Senior secured Term Loan A, long-term portion	914.1	931.7
Senior secured Term Loan B, long-term portion	756.8	778.3
Senior unsecured 5.75% notes due on September 1, 2023	418.4	418.2
Unsecured 7.00% debentures due on February 15, 2024	13.7	13.8
Unsecured 6.75% debentures due on December 15, 2027	29.6	29.6
Other	3.6	3.6
Total debt	2,200.6	2,233.2
Less current portion of debt	64.4	58.0
Total long-term debt	$ 2,136.2	$ 2,175.2

In September 2015, the Company entered into four new credit facilities for purposes of financing the Welch Allyn acquisition as well as refinancing our previously outstanding revolving credit facility. These new facilities consisted of the following:

- $1.0 billion senior secured Term Loan A facility (“TLA Facility”), maturing in September 2020
- $800.0 million senior secured Term Loan B facility (“TLB Facility”), maturing in September 2022
- Senior secured revolving credit facility (“Revolving Credit Facility”), providing borrowing capacity of up to $500.0 million, maturing in September 2020
- $425.0 million of senior unsecured notes (“Senior Notes”), maturing in September 2023

The TLA Facility, TLB Facility, and Revolving Credit Facility (collectively, the “Senior Secured Credit Facilities”) all bear interest at variable rates which are currently less than 4.0 percent. These interest rates are based primarily on the

London Interbank Offered Rate (LIBOR), but under certain conditions could also be based on the U.S. Federal Funds Rate or the U.S. Prime Rate, at the Company's option. The TLA Facility and TLB Facility have required principal payments. The TLA Facility requires minimum principal payments of $50.0 million in fiscal 2016, $75.0 million in fiscal 2017, and $100.0 million annually thereafter, with the remaining unpaid principal balance due at maturity. The TLB Facility requires annual principal payments of $8.0 million with the remaining unpaid principal balance due at maturity. We will be able to voluntarily prepay outstanding loans under the TLA Facility and the TLB Facility at any time. During the quarter ended December 31, 2015, we made a voluntary prepayment of $20.0 million on the TLB Facility.

At December 31, 2015, there were no borrowings on the Revolving Credit Facility, but available borrowing capacity was $492.1 million after giving effect to $7.9 million of outstanding standby letters of credit. The availability of borrowings under our Revolving Credit Facility is subject to our ability at the time of borrowing to meet certain specified conditions, including compliance with covenants contained in the governing credit agreement.

The Senior Secured Credit Facilities are held with a syndicate of banks, which includes over 20 institutions. The general corporate assets of the Company and its subsidiaries collateralize these obligations. The credit agreement governing these facilities contains financial covenants which specify a maximum secured net leverage ratio and a minimum interest coverage ratio, as such terms are defined in the credit agreement. These financial covenants are measured at the end of each fiscal quarter, with the first measurement date on December 31, 2015. The required ratios vary through December 31, 2019 providing a gradually decreasing maximum secured net leverage ratio and a gradually increasing minimum interest coverage ratio, as set forth in the table below:

Fiscal Quarter Ended	Maximum Secured Net Leverage Ratio	Minimum Interest Coverage Ratio
December 31, 2015	4.75x	3.25x
December 31, 2016	4.50x	3.25x
December 31, 2017	4.00x	3.50x
December 31, 2018	3.50x	3.75x
December 31, 2019 and thereafter	3.00x	4.00x

The Senior Notes bear interest at a fixed rate of 5.75 percent annually. These notes were issued at par in a private placement offering and are not registered securities on any public market. All of the Senior Notes are outstanding as of December 31, 2015. We are not required to make any mandatory redemption or sinking fund payments with respect to the Notes, other than in certain circumstances such as a change in control or material sale of assets. We may redeem the notes prior to maturity, but doing so prior to September 1, 2021 would require payment of a premium on any amounts redeemed, the amount of which varies based on the timing of the redemption. The indenture governing the Senior Notes contains certain covenants which impose limitations on the amount of dividends we may pay and the amount of common shares we may repurchase in the open market, but we do not expect these covenants to affect our current dividend policy or open share repurchase program. The terms of this indenture also impose certain restrictions on the amount and type of additional indebtedness we may obtain in the future, as well as the types of liens and guarantees we may provide.

We are in compliance with all financial covenants as of December 31, 2015.

As of December 31, 2015, unamortized debt issuance costs of $37.2 million have been recorded as a reduction of the carrying value of the related debt, compared to $39.1 million at September 30, 2015. In addition, $8.9 million of costs attributable to the Revolving Credit Facility are recorded as a component of other long-term assets on the Condensed Consolidated Balance Sheets as of December 31, 2015, compared with $9.4 million as of September 30, 2015. These costs will amortize into interest expense over the terms of the related credit facilities.

Unsecured debentures outstanding at December 31, 2015 and September 30, 2015 have fixed rates of interest. We have deferred gains included in the amounts above from the termination of previous interest rate swap agreements, and those deferred gains amounted to less than $1.0 million at both December 31, 2015 and September 30, 2015. The deferred gains on the termination of the swaps are being amortized and recognized as a reduction of interest expense over the remaining term of the related debt, and as a result, the effective interest rates on that debt have been and will continue to be lower than the stated interest rates on the debt.

From August 2012 through April 2015, we had a credit facility that provided for revolving loans of up to $500.0 million, plus a term loan in the aggregate amount of $200.0 million. A portion of the proceeds from the issuance of the Senior Secured Credit Facility and the Senior Notes in September 2015 was used to fully repay the previously outstanding credit facility, which is now terminated.

The fair value of our debt is estimated based on the quoted market prices for the same or similar issues or on the current rates offered to us for debt of the same remaining maturities. The book values of our short-term debt instruments approximate fair value. The estimated fair values of our long-term debt instruments are described in the table below:

	December 31, 2015	September 30, 2015
Senior secured Term Loan A	$ 955.1	$ 990.7
Senior secured Term Loan B	725.5	780.7
Senior unsecured 5.75% notes due on September 1, 2023	433.5	428.4
Unsecured debentures	44.1	43.4
Total debt	$ 2,158.2	$ 2,243.2

The estimated fair values of our long-term unsecured debentures were based on observable inputs such as quoted prices in markets that are not active. The estimated fair values of our term loans and the Senior Notes were based on quoted prices for similar liabilities. These fair value measurements were classified as Level 2, as described in Note 1.

6. Retirement and Postretirement Plans

We sponsor five defined benefit retirement plans. Those plans include: a master defined benefit retirement plan, a nonqualified supplemental executive defined benefit retirement plan, and three defined benefit retirement plans covering employees in Germany and France. Benefits for such plans are based primarily on years of service and the employee’s level of compensation during specific periods of employment. We contribute funds to trusts as necessary to provide for current service and for any unfunded projected future benefit obligation over a reasonable period of time. All of our plans have a September 30 measurement date. The following table details the components of net pension expense for our defined benefit retirement plans.

	Quarter Ended December 31	
	2015	2014
Service cost	$ 1.3	$ 1.4
Interest cost	2.7	3.7
Expected return on plan assets	(3.3)	(4.3)
Amortization of unrecognized prior service cost, net	0.1	0.1
Amortization of net loss	1.1	1.4
Net pension expense	$ 1.9	$ 2.3

Beginning in fiscal 2016, we elected to change the method we use to estimate the service and interest cost components of net periodic benefit cost for our defined benefit pension plans to a spot yield curve approach. Previously, we estimated the service and interest cost components of pension expense using a single weighted-average discount rate derived from the yield curve used to measure the benefit obligation at the beginning of the period. Under the new approach, we will apply discounting using individual spot rates from a yield curve composed of the rates of return on several hundred high-quality, fixed income corporate bonds available at the measurement date. These spot rates align to each of the projected benefit obligations and service cost cash flows. The service cost component relates to the active participants in the plan, so the relevant cash flows on which to apply the yield curve are considerably longer in duration on average than the total projected benefit obligation cash flows, which also include benefit payments to retirees. Interest cost is computed by multiplying each spot rate by the corresponding discounted projected benefit obligation cash flows. The spot yield curve approach reduces any actuarial gains and losses based upon interest rate expectations (e.g., built-in gains in interest cost in an upward sloping yield curve scenario), or gains and losses merely resulting from the timing and magnitude of cash outflows associated with our benefit obligations. The change does not affect the measurement of the total benefit obligations as the change in service and interest costs offsets in the actuarial gains and losses recorded in other comprehensive income.

We are making this change to improve the correlation between projected benefit cash flows and the corresponding yield curve spot rates and to provide a better measurement of service and interest costs. This change is considered a change in estimate and is accounted for on a prospective basis starting in fiscal year 2016.

In addition to defined benefit retirement plans, we also offer two domestic postretirement health care plans, one of which was assumed in the acquisition of Welch Allyn, that provide health care benefits to qualified retirees and their dependents. The plans are closed to new participants and include retiree cost sharing provisions. Annual costs related to these plans are not significant.

We have defined contribution savings plans that cover substantially all U.S. employees and certain non-U.S. employees. The general purpose of these plans is to provide additional financial security during retirement by providing employees with an incentive to make regular savings. Company contributions to the plans are based on eligibility and employee contributions. Expense under these plans was $6.1 million and $4.2 million in each of the quarterly periods ended December 31, 2015 and 2014.

7. Other Comprehensive Income

The following table represents the changes in accumulated other comprehensive loss by component:

	Quarter Ended December 31, 2015							
	Other comprehensive income (loss)					Accumulated other comprehensive loss		
	Prior to reclassification	Reclassification from	Pre-tax	Tax effect	Net of tax	Beginning balance	Net activity	Ending balance
Available-for-sale securities and currency hedges	$0.2	$ -	$0.2	$(0.1)	$0.1	$ -	$0.1	$0.1
Foreign currency translation adjustment	(10.2)	-	(10.2)	-	(10.2)	(92.8)	(10.2)	(103.0)
Change in pension and postretirement defined benefit plans	-	1.1	1.1	(0.4)	0.7	(48.0)	0.7	(47.3)
Total	$(10.0)	$ 1.1	$(8.9)	$(0.5)	$(9.4)	$(140.8)	$(9.4)	$(150.2)

	Quarter Ended December 31, 2014							
	Other comprehensive income					Accumulated other comprehensive loss		
	Prior to reclassification	Reclassification from	Pre-tax	Tax effect	Net of tax	Beginning balance	Net activity	Ending balance
Available-for-sale securities and currency hedges	$(0.6)	$ -	$(0.6)	$0.2	$(0.4)	$ -	$(0.4)	$(0.4)
Foreign currency translation adjustment	(22.6)	-	(22.6)	-	(22.6)	(34.2)	(22.6)	(56.8)
Change in pension and postretirement defined benefit plans	0.1	1.3	1.4	(0.5)	0.9	(39.9)	0.9	(39.0)
Total	$(23.1)	$ 1.3	$(21.8)	$(0.3)	$(22.1)	$(74.1)	$(22.1)	$(96.2)

The following table represents the items reclassified out of accumulated other comprehensive loss and the related tax effects:

	Quarter Ended December 31					
	2015			2014		
	Amount reclassified	Tax effect	Net of tax	Amount reclassified	Tax effect	Net of tax
Change in pension and postretirement defined benefit plans (a)	$1.1	$(0.4)	$0.7	$1.3	$(0.5)	$0.8

(a) Reclassified from accumulated other comprehensive loss into cost of goods sold and selling and administrative expenses. These components are included in the computation of net periodic pension expense.

8. Special Charges

We recognized special charges of $7.1 million and $3.7 million for the quarters ended December 31, 2015 and December 31, 2014, respectively, related to various organizational changes implemented to improve our business alignment and cost structure. These charges are summarized below.

Welch Allyn Integration

In conjunction with the acquisition of Welch Allyn in September 2015, we initiated plans to realign our business structure to facilitate the integration, take full advantage of available synergies, and position our existing businesses to capitalize on opportunities for growth. Immediately after the acquisition was completed, we eliminated approximately 100 positions in Welch Allyn's corporate support and administrative functions. We recorded special charges of $14.4 million in the fourth quarter of fiscal 2015 related to this action and as many of the affected employees were required to continue service for a specified period of time, additional amounts were expected to be incurred through the second quarter of fiscal 2016. During the first quarter of fiscal 2016, we incurred additional charges of approximately $3.5 million related to this action, along with an additional $1.0 million of severance and benefit costs related to other integration activities. We expect additional severance costs of up to $2 million to be recorded in the second quarter of fiscal 2016 related to the Welch Allyn redundancies, at which time all service obligations are expected to be fulfilled. We are continuing to evaluate additional actions related to integration and business realignment and expect additional special charges to be incurred, however, it is not practical at this time to estimate the amount of these future expected costs.

Site Consolidation

In the third quarter of fiscal 2015, we initiated a plan to streamline our operations and simplify our supply chain by consolidating certain manufacturing and distribution operations. As part of this action, we announced the closure of sites in Redditch, England and Charleston, South Carolina. Upon closure, each site's operations will either be relocated to other existing Company facilities or outsourced to third-party suppliers. During fiscal 2015, we recorded severance and benefit charges of $2.7 million for approximately 160 employees to be displaced by the closures, as well as $1.8 million of other related costs. During the first quarter of fiscal 2016, we recorded a net reversal of previously recorded severance and benefit charges of $0.2 million and recognized other related costs of $1.7 million related to these actions. We expect to incur approximately $1 million to $2 million of additional charges in fiscal 2016 for personnel costs and site closure expenses related to these actions, at which time such actions will be complete. The Company is continuing to evaluate its facilities footprint and additional costs are likely to be incurred with respect to other actions in the future, however, it is not practical to estimate the amount of these future expected costs until such time as the evaluations are complete.

Global Transformation

During the second quarter of fiscal 2014, we announced a global restructuring program focused on improving our cost structure. The domestic portion of this action is now complete. Part of this program included reducing our European manufacturing capacity and streamlining our global operations by, among other things, executing a back office process transformation program in Europe. The restructuring in Europe is in process and, for the first quarter of fiscal 2016, resulted in charges of $1.1 million for legal and professional fees, temporary labor, project management, and other administrative functions. These amounts compare to charges of $3.7 million in the prior year's first quarter. Since the inception of the global restructuring program through December 31, 2015, we have recognized aggregate special charges of $38.7 million. We expect to incur $4 million to $8 million of additional European restructuring costs through the completion of the program.

For all accrued severance and other benefit charges described above, we record restructuring reserves within other current liabilities. The reserve activity for severance and other benefits during fiscal 2016 was as follows:

Balance at September 30, 2015	$24.3
Expenses	4.6
Cash Payments	(11.8)
Reversals	(0.3)
Balance at December 31, 2015	$16.8

9. Income Taxes

On December 18, 2015, the President signed into law a combined tax and government funding bill (H.R. 2029). The tax portion of the bill, the Protecting Americans from Tax Hikes Act (the PATH Act), extended and made permanent several lapsed business incentives that impact the Company including the extension of bonus depreciation as well as the retroactive and permanent extension of the research tax credit. The research credit had previously expired effective December 31, 2014.

The effective tax rate for the three-month period ended December 31, 2015 was 25.9 percent compared to 28.8 percent for the comparable period in the prior year. The lower tax rate in the current period is primarily due to the difference in period tax benefits recognized for each period, both of which included the retroactive reinstatement of the research tax credit. Absent the discrete tax benefits, the current year rate would have been higher as a result of the geographic mix of income, along with losses incurred in select foreign jurisdictions for which no tax benefit could be recognized.

We expect the tax incentives extended as part of the PATH Act, primarily the reinstatement of the research tax credit, to favorably impact income tax expense for fiscal 2016 by approximately $4.0 million through a combination of a one-time catch-up adjustment from the reinstatement of the credit recorded in our first quarter of fiscal 2016 and the inclusion of the full-year research credit into the fiscal 2016 effective tax rate.

10. Earnings per Common Share

Basic earnings per share is calculated based upon the weighted average number of outstanding common shares for the period, plus the effect of deferred vested shares. Diluted earnings per share is calculated consistent with the basic earnings per share calculation plus the effect of dilutive unissued common shares related to stock-based employee compensation programs. For all periods presented, anti-dilutive stock options were excluded from the calculation of diluted earnings per share. Cumulative treasury stock acquired, less cumulative shares reissued, have been excluded in determining the average number of shares outstanding.

Earnings per share are calculated as follows (share information in thousands):

	Quarter Ended December 31	
	2015	2014
Net income attributable to common shareholders	$ 4.8	$ 12.1
Average shares outstanding - Basic	65,217	57,137
Add potential effect of exercise of stock options and other unvested equity awards	1,057	1,017
Average shares outstanding - Diluted	66,274	58,154
Net income attributable to common shareholders per common share - Basic	$ 0.07	$ 0.21
Net income attributable to common shareholders per common share - Diluted	$ 0.07	$ 0.21
Shares with anti-dilutive effect excluded from the computation of Diluted EPS	453	461

11. Common Stock

The stock-based compensation cost that was charged against income, net of tax, for all plans was $3.2 million for the quarterly period ended December 31, 2015 and $3.0 million for the comparable prior year period.

12. Guarantees

We routinely grant limited warranties on our products with respect to defects in material and workmanship. The terms of these warranties are generally one year, however, certain components and products have substantially longer warranty periods. We recognize a reserve with respect to these obligations at the time of product sale, with subsequent warranty claims recorded directly against the reserve. The amount of the warranty reserve is determined based on historical trend experience for the covered products. For more significant warranty-related matters which might require a broad-based correction, separate reserves are established when such events are identified and the cost of correction can be reasonably estimated.

A reconciliation of changes in the warranty reserve for the periods covered in this report is as follows:

	Quarter Ended December 31	
	2015	2014
Balance at beginning of period	$ 32.1	$ 28.4
Provision for warranties during the period	6.0	2.9
Warranty reserves acquired	-	1.1
Warranty claims during the period	(5.4)	(4.4)
Balance at end of period	$ 32.7	$ 28.0

In the normal course of business we enter into various other guarantees and indemnities in our relationships with suppliers, service providers, customers, business partners and others. Examples of these arrangements would include guarantees of product performance, indemnifications to service providers and indemnifications of our actions to business partners. These guarantees and indemnifications have not historically had, nor do we expect them to have, a material impact on our financial condition or results of operations, although indemnifications associated with our actions generally have no dollar limitations.

In conjunction with our acquisition and divestiture activities, we have entered into select guarantees and indemnifications of performance with respect to the fulfillment of commitments under applicable purchase and sale agreements. The arrangements generally indemnify the buyer or seller for damages associated with breach of contract, inaccuracies in representations and warranties surviving the closing date and satisfaction of liabilities and commitments retained under the applicable contract. With respect to sale transactions, we also routinely enter into non-competition agreements for varying periods of time. Guarantees and indemnifications with respect to acquisition and divestiture activities, if triggered, could have a materially adverse impact on our financial condition and results of operations.

13. Segment Reporting

We disclose segment information that is consistent with the way in which management operated and viewed the business. Our operating structure consisted of the following reporting segments:

- North America – sells and rents our patient support and near-patient technologies and services, as well as our clinical workflow solutions, in the U.S. and Canada.

- Surgical and Respiratory Care – sells and rents our surgical and respiratory care products globally.

- International – sells and rents similar products as our North America segment in regions outside of the U.S. and Canada.

- Welch Allyn – globally sells medical diagnostic equipment and a diversified portfolio of devices that assess, diagnose, treat, and manage a wide variety of illnesses and diseases.

Our performance under each reportable segment is measured on a divisional income basis before non-allocated operating and administrative costs, impairment of other intangibles, litigation, special charges, acquisition and integration costs, acquisition-related intangible asset amortization, and other unusual events. Divisional income generally represents the division's gross profit less its direct operating costs along with an allocation of manufacturing and distribution costs, research and development and certain corporate functional expenses.

Non-allocated operating and administrative costs include functional expenses that support the entire organization such as administration, finance, legal and human resources, expenses associated with strategic developments, acquisition-related intangible asset amortization, and other events that are not indicative of operating trends. We exclude such amounts from divisional income to allow management to evaluate and understand divisional operating trends without the effects of such items.

	Quarter Ended December 31	
	2015	2014
Revenue:		
North America	$ 248.9	$ 225.2
Surgical and Respiratory Care	120.6	126.3
International	93.7	113.5
Welch Allyn	198.0	-
Total revenue	$ 661.2	$ 465.0
Divisional income (loss):		
North America	$ 50.7	