AGILENT TECHNOLOGIES INC
Form 10-Q
September 06, 2017
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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 JULY 31, 2017
OR
¨ TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934.
FOR THE TRANSITION PERIOD FROM TO
COMMISSION FILE NUMBER: 001-15405
AGILENT TECHNOLOGIES, INC.
(EXACT NAME OF REGISTRANT AS SPECIFIED IN ITS CHARTER)

DELAWARE	77-0518772
(State or other jurisdiction of incorporation or organization)	(IRS employer Identification no.)

5301 STEVENS CREEK BLVD., SANTA CLARA, CALIFORNIA	95051
(Address of principal executive offices)	(Zip Code)

Registrant’s telephone number, including area code: (408) 345-8886
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 x 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 x No ¨
Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, smaller reporting company or an emerging growth company. See definitions of “large accelerated filer,” “accelerated filer,” “smaller reporting company” and "emerging growth company" in Rule 12b-2 of the Exchange Act.

Large accelerated filer x	Accelerated filer ¨
Non-accelerated filer ¨	Smaller reporting company ¨
(do not check if a smaller reporting company)	Emerging growth company ¨

If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the Exchange Act. ¨
Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes ¨ No x

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

CLASS	OUTSTANDING AT AUGUST 31, 2017
COMMON STOCK, $0.01 PAR VALUE	321,828,003

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PART I — FINANCIAL INFORMATION

ITEM 1. CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

AGILENT TECHNOLOGIES, INC.
CONDENSED CONSOLIDATED STATEMENT OF OPERATIONS
(in millions, except per share amounts)
(Unaudited)

	Three Months Ended July 31,		Nine Months Ended July 31,	
	2017	2016	2017	2016
Net revenue:				
Products	$842	$798	$2,502	$2,380
Services and other	272	246	781	711
Total net revenue	1,114	1,044	3,283	3,091
Costs and expenses:				
Cost of products	368	362	1,083	1,084
Cost of services and other	150	140	438	398
Total costs	518	502	1,521	1,482
Research and development	87	86	250	245
Selling, general and administrative	308	310	904	932
Total costs and expenses	913	898	2,675	2,659
Income from operations	201	146	608	432
Interest income	6	3	15	8
Interest expense	(19)	(17)	(59)	(53)
Other income (expense), net	5	2	13	6
Income before taxes	193	134	577	393
Provision for income taxes	18	10	70	57
Net income	$175	$124	$507	$336
Net income per share:				
Basic	$0.55	$0.38	$1.57	$1.03
Diluted	$0.54	$0.38	$1.56	$1.02
Weighted average shares used in computing net income per share:				
Basic	321	325	322	326
Diluted	326	328	325	329
Cash dividends declared per common share	$0.132	$0.115	$0.396	$0.345

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

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AGILENT TECHNOLOGIES, INC.
CONDENSED CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME (LOSS)
(in millions)
(Unaudited)

	Three Months Ended July 31,		Nine Months Ended July 31,	
	2017	2016	2017	2016
Net income	$175	$124	$507	$336
Other comprehensive income (loss):				
Unrealized loss on derivative instruments, net of tax benefit of $(1), $(4), $0 and $(7)	(3)	(5)	(3)	(11)
Amounts reclassified into earnings related to derivative instruments, net of tax expense (benefit) of $0, $1, $(1) and $0	(1)	1	(2)	—
Foreign currency translation, net of tax expense (benefit) of $6, $(3), $6 and $4	57	(48)	61	41
Net defined benefit pension cost and post retirement plan costs:				
Change in actuarial net loss, net of tax expense of $4, $2, $15 and $9	8	8	34	29
Change in net prior service benefit, net of tax benefit of $(1), $(1), $(3) and $(7)	(1)	(2)	(4)	(13)
Other comprehensive income (loss)	60	(46)	86	46
Total comprehensive income	$235	$78	$593	$382

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

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AGILENT TECHNOLOGIES, INC.
CONDENSED CONSOLIDATED BALANCE SHEET
(in millions, except par value and share amounts)
(Unaudited)

	July 31, 2017	October 31, 2016
ASSETS		
Current assets:		
Cash and cash equivalents	$2,563	$ 2,289
Accounts receivable, net	678	631
Inventory	566	533
Other current assets	189	182
Total current assets	3,996	3,635
Property, plant and equipment, net	716	639
Goodwill	2,612	2,517
Other intangible assets, net	375	408
Long-term investments	137	135
Other assets	425	460
Total assets	$8,261	$ 7,794
LIABILITIES AND EQUITY		
Current liabilities:		
Accounts payable	$289	$ 257
Employee compensation and benefits	230	235
Deferred revenue	301	269
Short-term debt	280	—
Other accrued liabilities	141	184
Total current liabilities	1,241	945
Long-term debt	1,801	1,904
Retirement and post-retirement benefits	323	360
Other long-term liabilities	285	339
Total liabilities	3,650	3,548
Commitments and contingencies (Note 11)		
Total equity:		
Stockholders’ equity:		
Preferred stock; $0.01 par value; 125 million shares authorized; none issued and outstanding	—	—
Common stock; $0.01 par value; 2 billion shares authorized; 322 million shares at July 31, 2017 and 614 million shares at October 31, 2016 issued	3	6
Treasury stock at cost; zero shares at July 31, 2017 and 290 million shares at October 31, 2016	—	(10,508)
Additional paid-in-capital	5,282	9,159
(Accumulated deficit) retained earnings	(260)	6,089
Accumulated other comprehensive loss	(417)	(503)
Total stockholders' equity	4,608	4,243
Non-controlling interest	3	3
Total equity	4,611	4,246
Total liabilities and equity	$8,261	$ 7,794

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

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AGILENT TECHNOLOGIES, INC.
CONDENSED CONSOLIDATED STATEMENT OF CASH FLOWS
(in millions)
(Unaudited)

	Nine Months Ended July 31,	
	2017	2016
Cash flows from operating activities:		
Net income	$507	$336
Adjustments to reconcile net income to net cash provided by (used in) operating activities:		
Depreciation and amortization	160	190
Share-based compensation	48	47
Deferred taxes	83	34
Excess and obsolete inventory related charges	19	16
Other non-cash expense, net	5	16
Changes in assets and liabilities:		
Accounts receivable	(29)	19
Inventory	(46)	(11)
Accounts payable	11	(27)
Employee compensation and benefits	(11)	(14)
Other assets and liabilities	(146)	(47)
Net cash provided by operating activities	601	559
Cash flows from investing activities:		
Investments in property, plant and equipment	(118)	(87)
Loan to equity method investment	—	(3)
Payment to acquire cost method investment	—	(80)
Payment in exchange for convertible note	(1)	(1)
Change in restricted cash and cash equivalents, net	—	245
Proceeds from sale of investment securities	—	1
Proceeds from divestitures	1	—
Acquisitions of businesses and intangible assets, net of cash acquired	(127)	(235)
Net cash used in investing activities	(245)	(160)
Cash flows from financing activities:		
Issuance of common stock under employee stock plans	58	59
Payment of taxes related to net share settlement of equity awards	(13)	(6)
Payment of dividends	(127)	(112)
Proceeds from revolving credit facility	343	255
Repayment of revolving credit facility	(163)	(20)
Treasury stock repurchases	(194)	(388)
Net cash used in financing activities	(96)	(212)
Effect of exchange rate movements	14	9
Net increase in cash and cash equivalents	274	196
Cash and cash equivalents at beginning of period	2,289	2,003

Cash and cash equivalents at end of period	$2,563	$2,199
Supplemental cash flow information:		
Income tax paid, net	$56	$54
Interest payments	$69	$66

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

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AGILENT TECHNOLOGIES, INC.
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(UNAUDITED)

1. OVERVIEW, BASIS OF PRESENTATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Overview. Agilent Technologies, Inc. ("we", "Agilent" or the "company"), incorporated in Delaware in May 1999, is a global leader in life sciences, diagnostics and applied chemical markets, providing application focused solutions that include instruments, software, services and consumables for the entire laboratory workflow.

Our fiscal year-end is October 31, and our fiscal quarters end on January 31, April 30 and July 31. Unless otherwise stated, these dates refer to our fiscal year and fiscal quarters.

Basis of Presentation. We have prepared the accompanying financial data for the three and nine months ended July 31, 2017 and 2016 pursuant to the rules and regulations of the Securities and Exchange Commission (“SEC”). Certain information and footnote disclosures normally included in financial statements prepared in accordance with generally accepted accounting principles (“GAAP”) in the U.S. have been condensed or omitted pursuant to such rules and regulations. The October 31, 2016 condensed balance sheet data was derived from audited financial statements but does not include all the disclosures required in audited financial statements by U.S. GAAP. The accompanying financial data and information should be read in conjunction with our Annual Report on Form 10-K for the fiscal year ended October 31, 2016.

In the opinion of management, the accompanying condensed consolidated financial statements contain all normal and recurring adjustments necessary for a fair statement of our condensed consolidated balance sheet as of July 31, 2017 and October 31, 2016, condensed consolidated statement of comprehensive income (loss) for the three and nine months ended July 31, 2017 and 2016, condensed consolidated statement of operations for the three and nine months ended July 31, 2017 and 2016, and condensed consolidated statement of cash flows for the nine months ended July 31, 2017 and 2016.

Use of Estimates. The preparation of condensed consolidated financial statements in accordance with GAAP in the U.S. requires management to make estimates and assumptions that affect the amounts reported in our condensed consolidated financial statements and accompanying notes. Management bases its estimates on historical experience and various other assumptions believed to be reasonable. Although these estimates are based on management’s best knowledge of current events and actions that may impact the company in the future, actual results may be different from the estimates. Our critical accounting policies are those that affect our financial statements materially and involve difficult, subjective or complex judgments by management. Those policies are revenue recognition, inventory valuation, share-based compensation, retirement and post-retirement benefit plan assumptions, goodwill and purchased intangible assets and accounting for income taxes.

Retirement of Treasury Shares. Upon the formal retirement of treasury shares, we deduct the par value of the retired treasury shares from common stock and allocate the excess of cost over par as a deduction to additional paid-in capital, based on the pro-rata portion of additional paid-in-capital, and the remaining excess as a deduction to retained earnings. All retired treasury shares revert to the status of authorized but unissued shares.

Variable Interest Entities. We make a determination upon entering into an arrangement whether an entity in which we have made an investment is considered a Variable Interest Entity (“VIE”). The company evaluates its investments in privately held companies on an ongoing basis. We have determined that as of July 31, 2017 there were no VIE’s required to be consolidated in the company’s consolidated financial statements because we do not have a controlling financial interest in any of the VIE’s that we have invested in nor are we the primary beneficiary. We account for these investments under either the equity or cost method, depending on the circumstances. We periodically reassess whether we are the primary beneficiary of a VIE. The reassessment process considers whether we have acquired the power to direct the most significant activities of the VIE through changes in governing documents or other circumstances. We also reconsider whether entities previously determined not to be VIEs have become VIEs, based on changes in facts and circumstances including changes in contractual arrangements and capital structure. As of July 31, 2017, the carrying value of our cost method investment in a VIE was $80 million with a maximum exposure of $80 million. The investments are included on the long-term investments line of the condensed consolidated balance sheet.

Fair Value of Financial Instruments. The carrying values of certain of our financial instruments including cash and cash equivalents, accounts receivable, accounts payable, accrued compensation and other accrued liabilities approximate fair value because of their short maturities. The fair value of long-term equity investments is determined using quoted market prices for those securities when available. For those long-term equity investments accounted for under the cost or equity method, their carrying value approximates their estimated fair value. Equity method investments are reported at the amount of the company's initial investment and adjusted each period for the company's share of the investee's income or loss and dividend paid. There are no equity method investments as of July 31, 2017. The fair value of our long-term debt, calculated from quoted prices which are primarily Level 1 inputs under the accounting guidance fair value hierarchy, exceeds the carrying value by approximately $169 million and $104 million as of July 31, 2017 and October 31, 2016, respectively. The change in the excess of fair value over carrying value in the nine months ended July 31, 2017 is due to fluctuations in market interest rates. The carrying value as of October 31, 2016 reflects the new accounting guidance related to the presentation of debt issuance costs which we adopted on November 1, 2016. The fair value of foreign currency contracts used for hedging purposes is estimated internally by using inputs tied to active markets. These inputs, for example, interest rate yield curves, foreign exchange rates, and forward and spot prices for currencies are observable in the market or can be corroborated by observable market data for substantially the full term of the assets or liabilities. See also Note 8, "Fair Value Measurements" for additional information on the fair value of financial instruments.

2. NEW ACCOUNTING PRONOUNCEMENTS

There were no changes to the new accounting pronouncements not yet adopted as described in our Annual Report on Form 10-K for the fiscal year ended October 31, 2016 except for the following:

In April 2015, the Financial Accounting Standards Board ("FASB") issued amendments to simplify the presentation of debt issuance costs. The amendments require that debt issuance costs related to a recognized debt liability to be presented in the balance sheet as a direct deduction from the carrying amount of that debt liability, consistent with debt discounts. The recognition and measurement guidance for debt issuance costs remain unchanged. The amendments were effective for us beginning November 1, 2016. The impact of adoption to our condensed consolidated balance sheet was a decrease of $8 million in other assets and long-term debt. The October 31, 2016 consolidated balance sheet has been revised to reflect the new disclosure requirement.

In May 2014, the FASB issued amendments to the accounting guidance related to revenue recognition, Topic 606, Revenue from contracts with customers. The objective of the amendments was to significantly enhance comparability and clarify principles of revenue recognition practices across entities, industries, jurisdictions and capital markets. The amendments are effective for us beginning fiscal 2019. The company expects to adopt this guidance on November 1, 2018 and will apply the modified retrospective method. We are currently evaluating the impact the adoption of this standard will have on our consolidated financial statements and disclosures.

In January 2017, the FASB issued guidance intended to clarify the definition of a business in connection with business combinations with the objective of adding guidance to assist entities with evaluating whether transactions should be accounted for as acquisitions (or disposals) of assets or businesses. This guidance is effective for us beginning November 1, 2018, and for interim periods within that year. Adjustments will be recorded in the period that they are determined rather than applied retrospectively via revision to the period of acquisition and each period thereafter. We do not expect this guidance to have a material impact on our consolidated financial statements and disclosures.

In January 2017, the FASB issued an amendment to modify the concept of impairment from the condition that exists when the carrying amount of goodwill exceeds its implied fair value to the condition that exists when the carrying amount of a reporting unit exceeds its fair value. The amendment also simplifies the subsequent measurement of goodwill by eliminating Step 2 from the goodwill impairment test. The amendments are effective for us beginning November 1, 2020. Early adoption is permitted for interim or annual goodwill impairment tests performed on testing dates after January 1, 2017. We do not expect this guidance to have a material impact on our consolidated financial statements and disclosures.

In March 2017, the FASB issued guidance on the presentation of the net periodic pension and postretirement benefit cost. This guidance also specifies that only the service cost component of net benefit cost is eligible for capitalization. The amendments are effective for us beginning November 1, 2018, including interim periods within those annual periods. We are evaluating the impact of adopting this guidance to our consolidated financial statements.

In May 2017, the FASB issued an update to clarify when to account for a change to the terms or conditions of a share-based payment award as a modification. Under the new guidance, modification accounting is required only if the fair value, the vesting conditions, or the classification of the award (as equity or liability) changes as a result of the change in terms or conditions. The amendments are effective for us beginning November 1, 2018. We do not expect this guidance to have a material impact on our consolidated financial statements and disclosures.

In August 2017, the FASB issued amendments to hedge accounting intended to better align a company's risk management strategies and financial reporting for hedging relationships through changes to both the designation and measurement guidance for qualifying hedging relationships and presentation of hedge results. The amendments expand and refine accounting for both nonfinancial and financial risk components and align the recognition and presentation of the effects of the hedging instrument and hedged item in the financial statements. The amendments are effective for us beginning November 1, 2019, including the interim periods within those annual periods. We are currently evaluating the impact the adoption of this guidance will have on our consolidated financial statements and disclosures.

Other amendments to GAAP in the U.S. that have been issued by the FASB or other standards-setting bodies that do not require adoption until a future date are not expected to have a material impact on our consolidated financial statements upon adoption.

3. SHARE-BASED COMPENSATION

Agilent accounts for share-based awards in accordance with the provisions of the authoritative accounting guidance which requires the measurement and recognition of compensation expense for all share-based payment awards made to our employees and directors including employee stock option awards, restricted stock units, employee stock purchases made under our employee stock purchase plan (“ESPP”) and performance share awards granted to selected members of our senior management under the long-term performance plan (“LTPP”) based on estimated fair values.

Participants in the LTPP are entitled to receive unrestricted shares of the company's stock after the end of a three-year period, if specified performance targets are met. Certain LTPP awards are generally designed to meet the criteria of a performance award with the performance metrics and peer group comparison based on the Total Stockholders’ Return (“TSR”) set at the beginning of the performance period. Effective November 1, 2015, the Compensation Committee of the Board of Directors approved another type of performance stock award, for the company's executive officers and other key employees. Participants in this program are also entitled to receive unrestricted shares of the company's stock after the end of a three-year period, if specified performance targets over the three-year period are met. The performance target for grants made in 2016 and 2017 were based on Operating Margin (“OM”) and Earnings Per Share ("EPS"), respectively. The performance targets for the LTPP-EPS grants for year 2 and year 3 of the performance period will be set in the first quarter of year 2 and year 3, respectively. All LTPP awards granted after November 1, 2015, are subject to a one-year post-vest holding period.

The final LTPP award may vary from zero to 200 percent of the target award. The maximum award value cannot exceed 300 percent of the grant date target value. We consider the dilutive impact of these programs in our diluted net income per share calculation only to the extent that the performance conditions are expected to be met. Restricted stock units generally vest, with some exceptions, at a rate of 25 percent per year over a period of four years from the date of grant.

The impact on our results for share-based compensation was as follows:

	Three Months Ended July 31,		Nine Months Ended July 31,	
	2017	2016	2017	2016
	(in millions)			
Cost of products and services	$3	$ 2	$12	$ 11
Research and development	1	1	4	4
Selling, general and administrative	8	8	32	33
Total share-based compensation expense	$12	$ 11	$48	$ 48

At July 31, 2017 and October 31, 2016, there was no share-based compensation capitalized within inventory.

The following assumptions were used to estimate the fair value of awards granted.

	Three Months Ended July 31,		Nine Months Ended July 31,	
	2017	2016	2017	2016
LTPP:				
Volatility of Agilent shares	23%	24%	23%	24%
Volatility of selected peer-company shares	15%-63%	14%-50%	15%-63%	14%-50%
Price-wise correlation with selected peers	36%	35%	36%	35%
Post-vest restriction discount for all executive awards	5.3%	5.5%	5.3%	5.5%

Shares granted under the LTPP (TSR) were valued using a Monte Carlo simulations model. The Monte Carlo simulation fair value model requires the use of highly subjective and complex assumptions, including the price volatility of the underlying stock.

For the volatility of our 2015 and 2016 LTPP (TSR) grants, we used the 3-year average historical stock price volatility of a group of our peer companies. We believed our historical volatility prior to the separation of Keysight in 2015 was no longer relevant to use. For the volatility of our 2017 LTPP (TSR) grants, we used our own historical stock price volatility.

The ESPP allows eligible employees to purchase shares of our common stock at 85 percent of the price at purchase and uses the purchase date to establish the fair market value.

The estimated fair value of restricted stock units, LTPP (OM) and LTPP (EPS) awards is determined based on the market price of Agilent’s common stock on the date of grant adjusted for expected dividend yield. The compensation cost for LTPP (OM) and LTPP (EPS) reflects the cost of awards that are probable to vest at the end of the performance period.

All awards granted in 2017 and 2016 to our senior management employees have a one-year post-vest holding restriction. The estimated discount associated with post-vest holding restrictions is calculated using the Finnerty model (see table above). The model calculates the potential lost value if the employee were able to sell the shares during the lack of marketability period, instead of being required to hold the shares. The model used the same historical stock price volatility and dividend yield assumption used for the Monte Carlo simulations model and an expected dividend yield to compute the discount.

4. INCOME TAXES

The company's income tax expense was $18 million and $70 million for the three and nine months ended July 31, 2017 with an effective tax rate of 9.3 percent and 12.1 percent, respectively. The income tax expense was $10 million and $57 million for the three and nine months ended July 31, 2016 with an effective tax rate of 7.5 percent and 14.5 percent, respectively.

The income tax provision for the three and nine months ended July 31, 2017 included net discrete tax benefits of $60 million and $63 million, respectively. The significant component of the net discrete tax benefit for the nine months ended July 31, 2017 included a $51 million tax benefit due to the settlement of an audit in Germany for the fiscal years 2005 to 2008.

The U.S. statute of limitations for audit of tax returns for the fiscal years 2012 and 2013 expired in July 2017. The statute expiration resulted in the recognition of previously unrecognized tax benefits of $40 million. This discrete tax benefit was offset by a deferred tax liability required for the tax expected upon repatriation of related unremitted foreign earnings that were not asserted as indefinitely invested outside the U.S.

During the current quarter, the company assessed its overall cash needs and funding sources for fiscal year 2017, which included evaluating its intent and ability regarding the indefinite reinvestment of foreign earnings from certain foreign subsidiaries and the use of cash tax attributes in anticipation of U.S. tax reform. Accordingly, the company determined that a portion of current year foreign earnings from its low tax jurisdictions would be repatriated in the near term. As such, a deferred tax liability for the expected repatriation of foreign earnings was accrued in the current quarter, which increased the annual estimated effective tax rate and the year to date tax expense of the company.

The income tax provision for the three and nine months ended July 31, 2016 included net discrete tax benefits of $6 million and $9 million, respectively. The significant component of the net discrete tax benefit for the nine months ended July 31, 2016 included an out of period correcting tax benefit of $11 million associated with a true-up of deferred tax liability for unremitted foreign earnings that should have been recorded in the third quarter of fiscal year 2015. The out-of-period correction was determined to be immaterial to the previously issued financial statements.

In the U.S., tax years remain open back to the year 2014 for federal income tax purposes and the year 2000 for significant states. Other than as mentioned above, there were no substantial changes from our 2016 Annual Report on Form 10-K to the status of these open tax years in the first nine months of fiscal year 2017.

In other major jurisdictions where the company conducts business, the tax years generally remain open back to the year 2001. During the first quarter of fiscal year 2017, the company settled its ongoing tax audit in Italy for the years 2011 to 2013 resulting in a net tax expense of $7 million. The settlement resulted in the recognition of previously unrecognized tax benefits of approximately $14 million. During the three months ended July 31, 2017, the company settled its ongoing tax audit in Germany for the years 2005 to 2008, which resulted in the recognition of previously unrecognized tax benefits of approximately $51 million.

AGILENT TECHNOLOGIES, INC.
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED) - (Continued)

With these jurisdictions and the U.S., it is reasonably possible that there could be significant changes to our unrecognized tax benefits in the next twelve months due to either the expiration of a statute of limitation or a tax audit settlement which could partially offset by an anticipated tax liability related to unremitted foreign earnings, where applicable. Given the number of years and numerous matters that remain subject to examination in various tax jurisdictions, management is unable to estimate the range of possible changes to the balance of our unrecognized tax benefits.

5. NET INCOME PER SHARE

The following is a reconciliation of the numerator and denominator of the basic and diluted net income per share computations for the periods presented below:

	Three Months Ended July 31,		Nine Months Ended July 31,	
	2017	2016	2017	2016
	(in millions)			
Numerator:				
Net income	$175	$124	$507	$336
Denominator:				
Basic weighted-average shares	321	325	322	326
Potential common shares— stock options and other employee stock plans	5	3	3	3
Diluted weighted-average shares	326	328	325	329

The dilutive effect of share-based awards is reflected in diluted net income per share by application of the treasury stock method, which includes consideration of unamortized share-based compensation expense and the dilutive effect of in-the-money options and non-vested restricted stock units. Under the treasury stock method, the amount the employee must pay for exercising stock options and unamortized share-based compensation expense collectively are assumed proceeds to be used to repurchase hypothetical shares. An increase in the fair market value of the company's common stock can result in a greater dilutive effect from potentially dilutive awards.

We exclude stock options with exercise prices greater than the average market price of our common stock from the calculation of diluted earnings per share because their effect would be anti-dilutive. For the three and nine months ended July 31, 2017, no options to purchase shares were excluded from the calculation of diluted earnings per share as compared to zero and 1.1 million options to purchase shares excluded for the three and nine months ended July 31, 2016. In addition, we exclude from the calculation of diluted earnings per share stock options, ESPP, LTPP and restricted stock awards whose combined exercise price and unamortized fair value were greater than the average market price of our common stock because their effect would also be anti-dilutive. For the three and nine months ended July 31, 2017, zero and 300 additional shares were excluded from the calculation of diluted earnings per share as compared to zero and 306,100 additional shares excluded for the three and nine months ended July 31, 2016.

6. INVENTORY

	July 31,	October 31,
	2017	2016
	(in millions)	

Finished goods	$ 358	$ 339
Purchased parts and fabricated assemblies	208	194
Inventory	$ 566	$ 533

AGILENT TECHNOLOGIES, INC.
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED) - (Continued)

7. GOODWILL AND OTHER INTANGIBLE ASSETS

The following table presents goodwill balances and the movements for each of our reportable segments during the nine months ended July 31, 2017:

	Life Sciences and Applied Markets	Diagnostics and Genomics	Agilent CrossLab	Total
	(in millions)			
Goodwill as of October 31, 2016	$790	$ 1,223	$ 504	$2,517
Foreign currency translation impact	5	11	3	19
Goodwill arising from acquisitions	25	51	—	76
Goodwill as of July 31, 2017	$820	$ 1,285	$ 507	$2,612

The components of other intangibles as of July 31, 2017 and October 31, 2016 are shown in the table below:

	Purchased Other Intangible Assets		
	Gross Carrying Amount	Accumulated Amortization	Net Book Value
	(in millions)		
As of October 31, 2016			
Purchased technology	$ 823	$ 572	$ 251
Backlog	1	1	—
Trademark/Tradename	149	61	88
Customer relationships	263	211	52
Total amortizable intangible assets	1,236	845	391
In-Process R&D	17	—	17
Total	$ 1,253	$ 845	$ 408
As of July 31, 2017			
Purchased technology	$ 856	$ 630	$ 226
Trademark/Tradename	149	70	79
Customer relationships	155	106	49
Total amortizable intangible assets	1,160	806	354
In-Process R&D	21	—	21
Total	$ 1,181	$ 806	$ 375

On July 7, 2017, we completed the acquisition of Cobalt Light Systems (“Cobalt”), an Oxfordshire, U.K. based provider of differentiated Raman spectroscopic instruments for the pharmaceutical industry, applied markets and public safety, for approximately $53 million in cash. Due to the timing of the close, the valuation of the tangible and intangible assets of this acquisition is preliminary and will be finalized in the fourth quarter.

On January 20, 2017, we acquired Multiplicom NV (“Multiplicom”), a leading European diagnostics company with state-of-the-art genetic testing technology and products, for approximately $72 million in cash.

During the nine months ended July 31, 2017, we recorded additions to goodwill of $76 million and additions to other intangible assets of $52 million related to these acquisitions. During the nine months ended July 31, 2017, other intangible assets, net increased $4 million due to the impact of foreign exchange translation.

During the nine months ended July 31, 2017, we wrote-off the gross carrying amount of $131 million and the related accumulated amortization of fully amortized intangible assets.

Each quarter we review the events and circumstances to determine if impairment of indefinite-lived intangible assets and goodwill is indicated. There were no indicators of impairments of indefinite-lived intangible assets during the three and nine months ended July 31, 2017. During the three and nine months ended July 31, 2016, we recorded an impairment of $4 million due to the cancellation of a specific IPR&D project. There were no indicators of impairment of goodwill during the nine months ended July 31, 2017.

Amortization expense of intangible assets was $27 million and $89 million for the three and nine months ended July 31, 2017, respectively. Amortization expense of intangible assets was $37 million and $120 million for the three and nine months ended July 31, 2016, respectively.

Future amortization expense related to existing finite-lived purchased intangible assets for the remainder of fiscal year 2017 and for each of the five succeeding fiscal years and thereafter is estimated below:

Estimated future amortization expense:	
(in millions)	
Remainder of 2017	$27
2018	$91
2019	$66
2020	$55
2021	$43
2022	$31
Thereafter	$41

8. FAIR VALUE MEASUREMENTS

The authoritative guidance defines fair value as the price that would be received from selling an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. When determining the fair value measurements for assets and liabilities required or permitted to be recorded at fair value, we consider the principal or most advantageous market and assumptions that market participants would use when pricing the asset or liability.

Fair Value Hierarchy

The guidance establishes a fair value hierarchy that prioritizes the use of inputs used in valuation techniques into three levels. A financial instrument's categorization within the fair value hierarchy is based upon the lowest level of input that is significant to the fair value measurement. There are three levels of inputs that may be used to measure fair value:

Level 1- applies to assets or liabilities for which there are quoted prices in active markets for identical assets or liabilities.

Level 2- applies to assets or liabilities for which there are inputs other than quoted prices included within level 1 that are observable, either directly or indirectly, for the asset or liability such as: quoted prices for similar assets or liabilities in active markets; quoted prices for identical or similar assets or liabilities in less active markets; or other inputs that can be derived principally from, or corroborated by, observable market data.

Level 3- applies to assets or liabilities for which there are unobservable inputs to the valuation methodology that are significant to the measurement of the fair value of the assets or liabilities.

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AGILENT TECHNOLOGIES, INC.
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED) - (Continued)

Financial Assets and Liabilities Measured at Fair Value on a Recurring Basis

Financial assets and liabilities measured at fair value on a recurring basis as of July 31, 2017 were as follows:

		Fair Value Measurement at July 31, 2017 Using		
	July 31, 2017	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
	(in millions)			
Assets:				
Short-term				
Cash equivalents (money market funds)	$1,549	$1,549	$ —	$ —
Derivative instruments (foreign exchange contracts)	7	—	7	—
Long-term				
Trading securities	31	31	—	—
Total assets measured at fair value	$1,587	$1,580	$ 7	$ —
Liabilities:				
Short-term				
Derivative instruments (foreign exchange contracts)	$8	$—	$ 8	$ —
Long-term				
Deferred compensation liability	31	—	31	—
Total liabilities measured at fair value	$39	$—	$ 39	$ —

Financial assets and liabilities measured at fair value on a recurring basis as of October 31, 2016 were as follows:

		Fair Value Measurement at October 31, 2016 Using		
	October 31, 2016	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
	(in millions)			
Assets:				