

HARMAN INTERNATIONAL INDUSTRIES INC /DE/  
Form 10-Q  
October 30, 2014  
Table of Contents

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

**FORM 10-Q**

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

**For the quarterly period ended September 30, 2014**

**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: 001-9764**

**Harman International Industries, Incorporated**  
**(Exact name of registrant as specified in its charter)**

**Delaware**  
**(State or other jurisdiction of**  
**incorporation or organization)**  
  
**400 Atlantic Street, Suite 1500**

**11-2534306**  
**(I.R.S. Employer**  
**Identification No.)**

**Stamford, CT**  
**(Address of principal executive offices)**  
  
**(203) 328-3500**

**06901**  
**(Zip code)**

**(Registrant's telephone number, including area code)**

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, a non-accelerated filer or a smaller reporting company. See the definitions of "large accelerated filer", "accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer  Accelerated filer   
Non-accelerated filer  (Do not check if a smaller reporting company) Smaller reporting company   
Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).  Yes  No

As of October 23, 2014 68,515,693 shares of common stock, par value \$.01, were outstanding.

**Table of Contents**

**HARMAN INTERNATIONAL INDUSTRIES, INCORPORATED AND SUBSIDIARIES**

**Form 10-Q**

**September 30, 2014**

**Table of Contents**

|   | <b>Page</b> |
|---|-------------|
| <u>Forward-Looking Statements</u>   | i           |
| <b><u>Part I</u></b> <b><u>FINANCIAL INFORMATION</u></b>  |             |
| Item 1. <u>Financial Statements</u>   | 1           |
| <u>Condensed Consolidated Financial Statements</u>  | 1           |
| <u>Condensed Consolidated Balance Sheets (Unaudited) September 30, 2014 and June 30, 2014</u>                               | 1           |
| <u>Condensed Consolidated Statements of Income (Unaudited) Three months ended September 30, 2014 and 2013</u>               | 2           |
| <u>Condensed Consolidated Statements of Comprehensive Income (Unaudited) Three months ended September 30, 2014 and 2013</u> | 3           |
| <u>Condensed Consolidated Statements of Cash Flows (Unaudited) Three months ended September 30, 2014 and 2013</u>           | 4           |
| <u>Notes to the Condensed Consolidated Financial Statements (Unaudited)</u>   | 5           |
| Item 2. <u>Management's Discussion and Analysis of Financial Condition and Results of Operations</u>                        | 29          |
| Item 3. <u>Quantitative and Qualitative Disclosures About Market Risk</u>   | 37          |
| Item 4. <u>Controls and Procedures</u>  | 38          |
| <b><u>Part II</u></b> <b><u>OTHER INFORMATION</u></b>   |             |
| Item 6. <u>Exhibits</u>   | 39          |
| <u>Signatures</u>   | 40          |

The page numbers in this Table of Contents reflect actual page numbers, not EDGAR page tag numbers.

References to Harman, the Company, we, us, and our in this Form 10-Q refer to Harman International Industries Incorporated and its subsidiaries unless the context requires otherwise.

Harman, the Harman logo, and the Harman products and brand names referred to herein are either the trademarks or the registered trademarks of Harman. All other trademarks are the property of their respective owners.

**Table of Contents**

**Forward-Looking Statements**

This report contains forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities Exchange Act of 1934, as amended. You should not place undue reliance on these statements. Forward-looking statements include information concerning possible or assumed future results of operations, cash flows, capital expenditures, the outcome of pending legal proceedings and claims, goals and objectives for future operations, including descriptions of our business strategies and purchase commitments from customers. These statements are typically identified by words such as believe, anticipate, expect, plan, intend, estimate, should, will and similar expressions. We base these statements on particular assumptions that we have made in light of our industry experience, as well as our perception of historical trends, current conditions, expected future developments and other factors that we believe are appropriate under the circumstances. As you read and consider the information in this report, you should understand that these statements are not guarantees of performance or results. They involve risks, uncertainties and assumptions. In light of these risks, uncertainties and assumptions, we cannot assure you that the results and events contemplated by the forward-looking statements contained in, or incorporated by reference into, this report will in fact transpire.

You should carefully consider the risks described below and the other information in this report because they identify important factors that could cause actual results to differ materially from those predicted in any such forward-looking statements. Our operating results may fluctuate significantly and may not meet our expectations or those of securities analysts or investors. The price of our stock would likely decline if this occurs. Factors that may cause fluctuations in our operating results include, but are not limited to, the following:

our ability to maintain profitability in our infotainment segment if there are delays in our product launches which may give rise to significant penalties and increased engineering expense;

the loss of one or more significant customers, or the loss of a significant platform with an automotive customer;

fluctuations in currency exchange rates, particularly with respect to the value of the U.S. Dollar and the Euro;

our ability to successfully implement our global footprint initiative, including achieving cost reductions and other benefits in connection with the restructuring of our manufacturing, engineering, procurement and administrative organizations;

fluctuations in the price and supply of raw materials including, without limitation, petroleum, copper, steel, aluminum, synthetic resins, rare metals and rare-earth minerals, or shortages of materials, parts and components;

the inability of our suppliers to deliver products at the scheduled rate and disruptions arising in connection therewith;

our ability to maintain a competitive technological advantage through innovation and leading product designs; and

our failure to maintain the value of our brands and implementing a sufficient brand protection program. Although we believe that these forward-looking statements are based on reasonable assumptions, you should be aware that many factors could affect our actual results of operations and could cause actual results to differ materially from those expressed in the forward-looking statements. As a result, the foregoing factors should not be construed as exhaustive and should be read together with the other cautionary statements included in this and other reports we file with the Securities and Exchange Commission. For additional information regarding certain factors that may cause our actual results to differ from those expected or anticipated see the information under the caption Risk Factors which is located in Item 1A of Part I of our Annual Report on Form 10-K for the fiscal year ended June 30, 2014. We undertake no obligation to publicly update or revise any forward-looking statement (except as required by law). This report also makes reference to our awarded business, which represents the estimated future lifetime net sales for all customers. Our future awarded business does not represent firm customer orders. We report our awarded business primarily based on written award letters from our customers. To validate these awards, we use various assumptions including global vehicle production forecasts, customer take rates for our products, revisions to product life cycle estimates and the impact of annual price reductions and exchange rates, among other factors. These assumptions are updated and reported externally on an annual basis. We update our estimated awarded business quarterly by adding the value of new awards received and subtracting sales recorded during the quarter. These quarterly updates do not include any assumptions for increased take rates, revisions to product life cycle, or any other factors.

**Table of Contents****PART I. FINANCIAL INFORMATION****Item 1. Financial Statements****HARMAN INTERNATIONAL INDUSTRIES, INCORPORATED AND SUBSIDIARIES****CONDENSED CONSOLIDATED BALANCE SHEETS****(Unaudited)**

| <b>(In thousands)</b>                      | <b>September 30, 2014</b> | <b>June 30, 2014</b> |
|--|---------------------------|----------------------|
| <b>Assets</b>                              |                           |                      |
| <b>Current assets</b>                      |                           |                      |
| Cash and cash equivalents                  | \$ 397,762                | \$ 581,312           |
| Receivables, net                           | 907,037                   | 894,579              |
| Inventories                                | 745,683                   | 662,128              |
| Other current assets                       | 371,861                   | 320,852              |
| <b>Total current assets</b>                | <b>2,422,343</b>          | <b>2,458,871</b>     |
| Property, plant and equipment, net         | 491,077                   | 509,856              |
| Goodwill                                   | 526,040                   | 540,952              |
| Deferred tax assets, long-term, net        | 141,695                   | 170,558              |
| Other assets                               | 478,159                   | 445,353              |
| <b>Total assets</b>                        | <b>\$ 4,059,314</b>       | <b>\$ 4,125,590</b>  |
| <b>Liabilities and Equity</b>              |                           |                      |
| <b>Current liabilities</b>                 |                           |                      |
| Current portion of long-term debt          | \$ 37,500                 | \$ 35,625            |
| Short-term debt                            | 2,893                     | 3,736                |
| Accounts payable                           | 746,452                   | 697,553              |
| Accrued liabilities                        | 546,893                   | 566,722              |
| Accrued warranties                         | 160,027                   | 155,472              |
| Income taxes payable                       | 25,003                    | 26,544               |
| <b>Total current liabilities</b>           | <b>1,518,768</b>          | <b>1,485,652</b>     |
| Borrowings under revolving credit facility | 200,000                   | 300,000              |
| Long-term debt                             | 210,030                   | 219,407              |
| Pension liability                          | 180,088                   | 186,352              |
| Other non-current liabilities              | 97,783                    | 141,158              |
| <b>Total liabilities</b>                   | <b>2,206,669</b>          | <b>2,332,569</b>     |
| <b>Commitments and contingencies</b>       |                           |                      |
| Preferred stock                            | 0                         | 0                    |

Edgar Filing: HARMAN INTERNATIONAL INDUSTRIES INC /DE/ - Form 10-Q

|   |              |              |
|---|--------------|--------------|
| Common stock  | 988          | 984          |
| Additional paid-in capital  | 1,038,210    | 1,040,254    |
| Accumulated other comprehensive income                                  | 41,260       | 39,799       |
| Retained earnings   | 2,039,472    | 1,979,234    |
| Less: Common stock held in treasury                                     | (1,267,693)  | (1,267,693)  |
| Total Harman International Industries, Incorporated shareholders equity | 1,852,237    | 1,792,578    |
| Noncontrolling interest   | 408          | 443          |
| Total equity  | 1,852,645    | 1,793,021    |
| Total liabilities and equity  | \$ 4,059,314 | \$ 4,125,590 |

See accompanying Notes to the Condensed Consolidated Financial Statements.

Table of Contents**HARMAN INTERNATIONAL INDUSTRIES, INCORPORATED AND SUBSIDIARIES****CONDENSED CONSOLIDATED STATEMENTS OF INCOME****(Unaudited)**

| <b>(In thousands, except earnings per share data)</b>                           | <b>Three Months Ended</b> |              |
|---|---------------------------|--------------|
|   | <b>September 30,</b>      |              |
|   | <b>2014</b>               | <b>2013</b>  |
| <b>Net sales</b>  | \$ 1,428,922              | \$ 1,171,805 |
| Cost of sales   | 1,014,290                 | 850,156      |
| <b>Gross profit</b>   | 414,632                   | 321,649      |
| Selling, general and administrative expenses                                    | 298,849                   | 252,267      |
| <b>Operating income</b>   | 115,783                   | 69,382       |
| Other expenses:   |                           |              |
| Interest expense, net   | 2,677                     | 1,970        |
| Foreign exchange losses, net  | 60                        | 861          |
| Miscellaneous, net  | 2,340                     | 1,329        |
| Income before income taxes  | 110,706                   | 65,222       |
| Income tax expense, net   | 27,772                    | 18,676       |
| Equity in loss of unconsolidated subsidiaries                                   | 0                         | 94           |
| <b>Net income</b>   | 82,934                    | 46,452       |
| Net loss attributable to noncontrolling interest                                | (39)                      | 0            |
| <b>Net income attributable to Harman International Industries, Incorporated</b> | \$ 82,973                 | \$ 46,452    |
| <b>Earnings per share:</b>  |                           |              |
| Basic   | \$ 1.20                   | \$ 0.67      |
| Diluted   | \$ 1.18                   | \$ 0.66      |
| <b>Weighted average shares outstanding:</b>                                     |                           |              |
| Basic   | 69,301                    | 69,547       |
| Diluted   | 70,194                    | 70,371       |

See accompanying Notes to the Condensed Consolidated Financial Statements.



**Table of Contents****HARMAN INTERNATIONAL INDUSTRIES, INCORPORATED AND SUBSIDIARIES****CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME****(Unaudited)**

| <b>(In thousands)</b>  | <b>Three Months Ended</b> |             |
|--|---------------------------|-------------|
|  | <b>September 30,</b>      | <b>2013</b> |
|  | <b>2014</b>               | <b>2013</b> |
| Net income   | \$ 82,934                 | \$ 46,452   |
| Net loss attributable to noncontrolling interest   | (39)                      | 0           |
| Net income attributable to Harman International Industries, Incorporated                               | \$ 82,973                 | \$ 46,452   |
| Other comprehensive income (loss), net of taxes <sup>(1)</sup> :                                       |                           |             |
| Foreign currency translation   | \$ (81,415)               | \$ 34,085   |
| Unrealized gains (losses) on hedging derivatives, net of taxes   | 81,864                    | (15,336)    |
| Pension liability adjustment, net of taxes   | 977                       | (62)        |
| Unrealized gains on available for sale securities  | 39                        | 7           |
| Other comprehensive income, net of taxes   | 1,465                     | 18,694      |
| Other comprehensive income, net of taxes attributable to noncontrolling interest                       | 4                         | 0           |
| Other comprehensive income, net of taxes attributable to Harman International Industries, Incorporated | \$ 1,461                  | \$ 18,694   |
| Comprehensive income, net of taxes   | \$ 84,399                 | \$ 65,146   |
| Comprehensive loss, net of taxes attributable to noncontrolling interest                               | (35)                      | 0           |
| Comprehensive income, net of taxes attributable to Harman International Industries, Incorporated       | \$ 84,434                 | \$ 65,146   |

<sup>(1)</sup> Refer to Note 15 *Other Comprehensive Income (Loss)* for more information.

See accompanying Notes to the Condensed Consolidated Financial Statements.

**Table of Contents****HARMAN INTERNATIONAL INDUSTRIES, INCORPORATED AND SUBSIDIARIES****CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS****(Unaudited)**

| <b>(In thousands)</b>   | <b>Three Months Ended</b> |             |
|---|---------------------------|-------------|
|   | <b>2014</b>               | <b>2013</b> |
| <b>Cash flows from operating activities:</b>                                      |                           |             |
| Net income  | \$ 82,934                 | \$ 46,452   |
| Adjustments to reconcile net income to net cash provided by operating activities: |                           |             |
| Depreciation and amortization   | 37,427                    | 31,713      |
| Deferred income taxes   | 22,944                    | 15,359      |
| (Gain) loss on disposition of assets  | (1,041)                   | 786         |
| Share-based compensation  | 10,818                    | 6,623       |
| Excess tax benefit from share-based compensation                                  | (2,803)                   | (878)       |
| Non-cash interest expense   | 545                       | 545         |
| Changes in operating assets and liabilities:                                      |                           |             |
| (Increase) decrease in:   |                           |             |
| Receivables, net  | (45,043)                  | (60,230)    |
| Inventories   | (110,201)                 | (55,703)    |
| Other current assets  | (42,188)                  | (1,795)     |
| Pre-production and development costs  | (1,680)                   | (4,149)     |
| Increase (decrease) in:   |                           |             |
| Accounts payable  | 73,645                    | 78,095      |
| Accrued warranties  | 14,780                    | 8,510       |
| Accrued other liabilities   | (18,313)                  | 37,892      |
| Income taxes payable  | (48)                      | 525         |
| Net change in derivative assets and liabilities                                   | (11,892)                  | 7,626       |
| Other operating activities  | 3,818                     | 1,665       |
| Net cash provided by operating activities   | 13,702                    | 113,036     |
| <b>Cash flows from investing activities:</b>                                      |                           |             |
| Maturities of short-term investments  | 0                         | 10,008      |
| Proceeds from asset dispositions  | 4,467                     | 0           |
| Capital expenditures  | (35,046)                  | (28,227)    |
| Other items, net  | 218                       | 98          |
| Net cash used in investing activities   | (30,361)                  | (18,121)    |
| <b>Cash flows from financing activities:</b>                                      |                           |             |
| (Decrease) increase in short-term borrowings                                      | (770)                     | 6,970       |
| Repayments of long-term debt  | (7,500)                   | (7,500)     |
| Repayments under revolving credit facility  | (100,000)                 | 0           |
| Cash dividends to shareholders  | (22,525)                  | (20,454)    |
| Repurchase of common stock  | 0                         | (26,371)    |

Edgar Filing: HARMAN INTERNATIONAL INDUSTRIES INC /DE/ - Form 10-Q

|  |            |            |
|--|------------|------------|
| Exercise of stock options                                    | 6,009      | 17,062     |
| Repurchases related to share-based compensation arrangements | (21,670)   | (11,913)   |
| Excess tax benefit from share-based compensation             | 2,803      | 878        |
| Other items, net   | 188        | 653        |
| Net cash used in financing activities                        | (143,465)  | (40,675)   |
| Effect of exchange rate changes on cash                      | (23,426)   | 6,940      |
| Net (decrease) increase in cash and cash equivalents         | (183,550)  | 61,180     |
| Cash and cash equivalents at beginning of period             | 581,312    | 454,258    |
| Cash and cash equivalents at end of period                   | \$ 397,762 | \$ 515,438 |
| <b>Supplemental disclosure of cash flow information:</b>     |            |            |
| Interest paid, net   | \$ 1,926   | \$ 1,936   |
| Income taxes paid  | \$ 1,387   | \$ 3,552   |
| <b>Non-cash investing activities:</b>                        |            |            |
| Accrued and contingent acquisition-related liabilities       | \$ 886     | \$ (10)    |

See accompanying Notes to the Condensed Consolidated Financial Statements.

**Table of Contents**

**HARMAN INTERNATIONAL INDUSTRIES, INCORPORATED AND SUBSIDIARIES**

**Notes to the Condensed Consolidated Financial Statements**

**(In thousands, except per-share data and where otherwise noted)**

**(Unaudited)**

**Note 1 Basis of Presentation**

***Basis of Presentation***

References to we, us, our, the company and Harman refer to Harman International Industries, Incorporated and its consolidated subsidiaries unless the context specifically requires otherwise.

Our unaudited, condensed consolidated financial statements have been prepared pursuant to the rules and regulations of the Securities and Exchange Commission. These unaudited condensed consolidated financial statements have been prepared in accordance with the accounting policies described in our audited consolidated financial statements included in our Annual Report on Form 10-K for the fiscal year ended June 30, 2014 (our 2014 Annual Report ) and do not include all information and footnote disclosures included in our audited financial statements. In the opinion of management, the accompanying unaudited, condensed consolidated financial statements include all adjustments, consisting of normal recurring adjustments and accruals, necessary to present fairly, in all material respects, the consolidated financial condition, results of operations and cash flows for the periods presented. Operating results for the three months ended September 30, 2014 are not necessarily indicative of the results that may be expected for the full fiscal year ending June 30, 2015 due to seasonal, economic and other factors. Where necessary, information for prior periods has been reclassified to conform to the consolidated financial statement presentation in the current fiscal year. These unaudited condensed consolidated financial statements should be read in conjunction with our audited consolidated financial statements and accompanying notes included in our 2014 Annual Report.

The methods, estimates and judgments we use in applying our accounting policies, in conformity with generally accepted accounting principles in the United States ( GAAP ), have a significant impact on the results we report in our financial statements. We base our estimates on historical experience and on various other assumptions that we believe to be reasonable under the circumstances. The estimates affect the carrying values of assets and liabilities. Actual results may differ from these estimates under different assumptions or conditions.

**Note 2 New Accounting Standards**

***Recently Adopted Accounting Standards***

**Income Taxes:** In July 2013, the Financial Accounting Standards Board ( FASB ) issued Accounting Standards Update ( ASU ) 2013-11, Presentation of an Unrecognized Tax Benefit When a Net Operating Loss Carryforward, a Similar Tax Loss, or a Tax Credit Carryforward Exists. The new guidance requires that unrecognized tax benefits be presented on a net basis with the deferred tax assets for such carryforwards. This new guidance is effective for fiscal years and interim periods within those years beginning after December 15, 2013. We adopted the provisions of this new guidance on July 1, 2014. The adoption of the new provisions did not have a material impact on our financial condition or results of operations.

***Recently Issued Accounting Standards***

**Revenue Recognition:** In May 2014, the FASB issued ASU No. 2014-09, Revenue from Contracts with Customers (Topic 606), which amends the guidance for revenue recognition to replace numerous, industry-specific requirements and converges areas under this topic with those of the International Financial Reporting Standards. The new guidance implements a five-step process for customer contract revenue recognition that focuses on transfer of control, as opposed to transfer of risk and rewards. The new guidance also requires enhanced disclosures regarding the nature, amount, timing and uncertainty of revenues and cash flows from contracts with customers. Other major provisions include the capitalization and amortization of certain contract costs, ensuring the time value of money is considered in the transaction price, and allowing estimates of variable consideration to be recognized before contingencies are resolved in certain circumstances. The new guidance is effective for fiscal years and interim periods within those years beginning after December 15, 2016. Early adoption is prohibited. We expect to adopt the provisions of this new guidance on July 1, 2017. Entities can transition to the standard either retrospectively or as a cumulative-effect adjustment as of the date of adoption. We are currently assessing the impact the adoption of the new provisions will have on our financial condition and results of operations.

**Table of Contents**

**Discontinued Operations:** In April 2014, the FASB issued ASU 2014-08, Reporting Discontinued Operations and Disclosures of Disposals of Components of an Entity, which changes the criteria for determining which disposals can be presented as discontinued operations and modifies disclosure requirements. Under the new guidance, a discontinued operation is defined as a disposal of a component or group of components that is disposed of or is classified as held-for-sale and represents a strategic shift that has or will have a major effect on an entity's operations and financial results. The standard states that a strategic shift could include a disposal of (i) a major geographical area of operations, (ii) a major line of business, (iii) a major equity method investment, or (iv) other major parts of an entity. The new guidance also requires several new disclosures. This new guidance is effective for fiscal years and interim periods within those years beginning after December 15, 2014. Early adoption is permitted. We expect to adopt the provisions of this new guidance on July 1, 2015. We do not expect the adoption of the new provisions to have a material impact on our financial condition or results of operations.

**Note 3 Allowance for Doubtful Accounts**

We reserve an estimated amount for accounts receivable that may not be collected. Methodologies for estimating the allowance for doubtful accounts are based primarily on specific identification of uncollectible accounts. Historical collection rates and customer credit worthiness are considered in determining specific reserves. At September 30, 2014 and June 30, 2014, we had \$9.0 million and \$9.6 million, respectively, reserved for possible uncollectible accounts receivable.

**Note 4 Inventories**

At September 30, 2014 and June 30, 2014, inventories consisted of the following:

|                 | <b>September 30,<br/>2014</b> | <b>June 30,<br/>2014</b> |
|-----------------|-------------------------------|--------------------------|
| Finished goods  | \$ 326,932                    | \$ 273,756               |
| Work in process | 92,265                        | 93,586                   |
| Raw materials   | 326,486                       | 294,786                  |
| Inventories     | \$ 745,683                    | \$ 662,128               |

At September 30, 2014 and June 30, 2014, our inventory reserves were \$83.2 million and \$87.7 million, respectively.

**Note 5 Property, Plant and Equipment, net**

Property, plant and equipment, net consisted of the following:

|                            | <b>Estimated<br/>Useful Lives<br/>(in Years)</b> | <b>September 30,<br/>2014</b> | <b>June 30,<br/>2014</b> |
|----------------------------|--|-------------------------------|--------------------------|
| Land                       |  | \$ 10,430                     | \$ 11,077                |
| Buildings and improvements | 1-50   | 277,291                       | 296,401                  |
| Machinery and equipment    | 3-20   | 1,210,514                     | 1,240,750                |

Edgar Filing: HARMAN INTERNATIONAL INDUSTRIES INC /DE/ - Form 10-Q

|  |      |             |             |
|--|------|-------------|-------------|
| Furniture and fixtures                         | 3-10 | 32,131      | 33,414      |
| Property, plant and equipment, gross           |      | 1,530,366   | 1,581,642   |
| Less accumulated depreciation and amortization |      | (1,039,289) | (1,071,786) |
| Property, plant and equipment, net             |      | \$ 491,077  | \$ 509,856  |

Depreciation expense for the three months ended September 30, 2014 and 2013 was \$31.2 million and \$28.8 million, respectively.

**Table of Contents****Note 6 Accrued Warranties**

Details of our accrued warranties are as follows:

|                                     | <b>Three Months Ended<br/>September 30,</b> |             |
|-------------------------------------|---|-------------|
|                                     | <b>2014</b>                                 | <b>2013</b> |
| Accrued warranties, June 30,        | \$ 155,472                                  | \$ 128,411  |
| Warranty expense                    | 23,423                                      | 18,633      |
| Warranty payments (cash or in-kind) | (8,397)                                     | (9,595)     |
| Other <sup>(1)</sup>                | (10,471)                                    | 4,017       |
| Accrued warranties, September 30,   | \$ 160,027                                  | \$ 141,466  |

<sup>(1)</sup> Other primarily represents foreign currency translation.

**Note 7 Earnings Per Share**

We apply the two-class method when computing earnings per share, which requires that net income per share for each class of shares entitled to dividends be calculated assuming all of our net income is distributed as dividends to these shareholders based on their contractual rights.

The following table presents the calculation of basic and diluted earnings per share of common stock outstanding:

|  | <b>Three Months Ended September 30,</b> |                |              |                |
|--|---|----------------|--------------|----------------|
|  | <b>2014</b>                             |                | <b>2013</b>  |                |
|  | <b>Basic</b>                            | <b>Diluted</b> | <b>Basic</b> | <b>Diluted</b> |
| <b>Numerator for Basic and Diluted Earnings per Share:</b>               |   |                |              |                |
| Net income   | \$ 82,934                               | \$ 82,934      | \$ 46,452    | \$ 46,452      |
| Net loss attributable to noncontrolling interest                         | (39)                                    | (39)           | 0            | 0              |
| Net income attributable to Harman International Industries, Incorporated | \$ 82,973                               | \$ 82,973      | \$ 46,452    | \$ 46,452      |
| <b>Denominator for Basic and Diluted Earnings per Share:</b>             |   |                |              |                |
| Weighted average shares outstanding                                      | 69,301                                  | 69,301         | 69,547       | 69,547         |
| Employee stock options   | 0                                       | 893            | 0            | 824            |
| Total weighted average shares outstanding                                | 69,301                                  | 70,194         | 69,547       | 70,371         |
| <b>Earnings per Share:</b>   |   |                |              |                |
| Earnings per share   | \$ 1.20                                 | \$ 1.18        | \$ 0.67      | \$ 0.66        |



Unvested share-based payment awards that contain non-forfeitable rights to dividends or dividend equivalents (whether paid or unpaid) are considered participating securities, as defined under GAAP, and are included in the computation of earnings per share pursuant to the two-class method.

Certain options were outstanding and not included in the computation of diluted net earnings per share because the assumed exercise of these options would have been antidilutive. Options to purchase 272,317 and 1,056,810 shares of our common stock at September 30, 2014 and 2013, respectively, were outstanding and excluded from the computation of diluted earnings per share because they would have been antidilutive. In addition 145,266 and 178,870 restricted stock units at September 30, 2014 and 2013, respectively, were outstanding and excluded from the computation of diluted earnings per share as they also would have been antidilutive.

**Table of Contents****Note 8 Goodwill and Intangible Assets, Net****Goodwill**

During the three months ended September 30, 2014, we reduced the goodwill in our Professional segment associated with our acquisition of AMX LLC and AMX Holding Corporation (collectively AMX ) by \$2.9 million. During the three months ended September 30, 2013, we did not record any new additions to goodwill.

We did not recognize any goodwill impairment charges in our Condensed Consolidated Statements of Income in the three months ended September 30, 2014 and 2013.

The contingent purchase price associated with the acquisition of innovative Systems ( IS ) is calculated pursuant to the terms of an agreement between the parties. Certain terms of the agreement are currently subject to a dispute between the parties and the matter was submitted to arbitration. On November 5, 2013, the arbitration panel reached a partial judgment on some of the disputed matters covering the period from February 2009 through January 2012 awarding 16.3 million to the IS sellers. We contested the enforcement of the partial award. During the fiscal year ended June 30, 2014, we recorded approximately \$8.1 million of additional contingent purchase price in goodwill to accrue for this partial award. In July 2014, the partial award was upheld. Until such time as the other disputed matters are resolved, we cannot calculate the contingent purchase price related to these other disputed matters.

**Intangible Assets, Net**

Intangible assets, net were \$171.6 million and \$182.0 million at September 30, 2014 and June 30, 2014, respectively and were comprised of the following:

|                           | Weighted<br>Average<br>Amortization | September 30, 2014          |                             |               | June 30, 2014               |                             |               |
|---------------------------|-------------------------------------|-----------------------------|-----------------------------|---------------|-----------------------------|-----------------------------|---------------|
|                           |                                     | Gross<br>Carrying<br>Amount | Accumulated<br>Amortization | Net<br>Amount | Gross<br>Carrying<br>Amount | Accumulated<br>Amortization | Net<br>Amount |
| Customer relationships    | 3 Years                             | \$ 64,629                   | \$ (17,884)                 | \$ 46,745     | \$ 67,277                   | \$ (17,770)                 | \$ 49,507     |
| Technology                | 3 Years                             | 37,260                      | (8,299)                     | 28,961        | 39,331                      | (8,196)                     | 31,135        |
| Patents                   | 11 Years                            | 5,136                       | (1,265)                     | 3,871         | 11,418                      | (7,166)                     | 4,252         |
| Tradenames <sup>(1)</sup> | 5 Years                             | 88,266                      | (8,403)                     | 79,863        | 88,266                      | (7,489)                     | 80,777        |
| Non-compete<br>agreement  | 3 Years                             | 1,468                       | (1,301)                     | 167           | 2,212                       | (2,016)                     | 196           |
| Software                  | 4 Years                             | 11,813                      | (1,612)                     | 10,201        | 11,813                      | (431)                       | 11,382        |
| Other                     | 8 Years                             | 7,230                       | (5,432)                     | 1,798         | 7,463                       | (2,682)                     | 4,781         |
| Total                     |                                     | \$ 215,802                  | \$ (44,196)                 | \$ 171,606    | \$ 227,780                  | \$ (45,750)                 | \$ 182,030    |

(1) Includes \$55.7 million, \$19.0 million and \$3.3 million of indefinite-lived intangible assets related to the acquisition of AMX and Martin Professional A/S and substantially all of the assets of Verto Medical Solutions LLC d/b/a yurbuds and its wholly-owned subsidiary ( yurbuds ), respectively.

Amortization expense related to intangible assets was \$6.2 million and \$2.9 million for the three months ended September 30, 2014 and 2013, respectively.

At September 30, 2014, amortization expense is expected to approximate the following:

|              |                  |
|--------------|------------------|
| 2015         | \$ 20,777        |
| 2016         | 22,005           |
| 2017         | 14,856           |
| 2018         | 11,844           |
| 2019         | 8,793            |
| Thereafter   | 15,270           |
| <b>Total</b> | <b>\$ 93,545</b> |

## **Table of Contents**

### **Note 9 Debt**

#### ***Short Term Borrowings***

At September 30, 2014 and June 30, 2014, we had \$2.9 million and \$3.7 million of short-term borrowings outstanding, respectively. At September 30, 2014 and June 30, 2014, we maintained lines of credit of \$66.4 million and \$64.6 million, respectively, primarily in India, China, Hungary, Brazil and Denmark.

We classify our debt based on the contractual maturity dates of the underlying debt instruments. We defer costs associated with debt issuance over the applicable term of the debt. These costs are amortized to Interest expense, net in our Condensed Consolidated Statements of Income.

#### ***Credit Agreement***

On October 10, 2012, we and our wholly-owned subsidiary Harman Holding GmbH & Co. KG ( Harman KG ), entered into a Multi-Currency Credit Agreement (the Credit Agreement ) with a group of banks. The Credit Agreement provides for (i) a five-year unsecured multi-currency revolving credit facility (the Revolving Credit Facility ) in the amount of \$750.0 million (the Aggregate Revolving Commitment ) with availability in currencies other than the United States Dollar of up to \$550.0 million and (ii) a five-year unsecured United States Dollar term loan facility (the Term Facility ) and, collectively with the Revolving Credit Facility, the Facilities ) in the amount of \$300.0 million (the Aggregate Term Commitment ) and, collectively with the Aggregate Revolving Commitment, the Aggregate Commitment ). Up to \$60.0 million of the Aggregate Revolving Commitment is available for letters of credit. Subject to certain conditions set forth in the Credit Agreement, the Aggregate Commitment may be increased by up to \$250.0 million. We may select interest rates for the Facilities equal to (i) LIBOR plus an applicable margin or (ii) a base rate plus an applicable margin, which in each case is determined based on our credit rating. We pay a facility fee on the Aggregate Revolving Commitment, whether drawn or undrawn, which is determined based on our credit rating. Any proceeds from borrowings under the Facilities may be used for general corporate purposes.

At September 30, 2014, there was \$200.0 million of outstanding borrowings and approximately \$4.6 million of outstanding letters of credit under the Revolving Credit Facility and \$247.5 million of outstanding borrowings under the Term Facility, of which \$37.5 million is included in our Condensed Consolidated Balance Sheet as Current portion of long-term debt and \$210.0 million is classified as Long-term debt. At September 30, 2014, unused available credit under the Revolving Credit Facility was \$545.4 million.

At June 30, 2014, there was \$300.0 million of outstanding borrowings and approximately \$4.6 million of outstanding letters of credit under the Revolving Credit Facility and \$255.0 million of outstanding borrowings under the Term Facility, of which \$35.6 million is included in our Condensed Consolidated Balance Sheet as Current portion of long-term debt and \$219.4 million is classified as Long-term debt. At June 30, 2014, unused available credit under the Revolving Credit Facility was \$445.4 million.

#### ***Long-Term Debt and Current Portion of Long-Term-Debt***

At September 30, 2014 and June 30, 2014, long-term debt and current portion of long-term debt consisted of the following:

|  | <b>Fair Value at<br/>September 30, 2014</b> | <b>Book Value at<br/>September 30,<br/>2014</b> | <b>Fair Value at<br/>June 30, 2014</b> | <b>Book Value at<br/>June 30,<br/>2014</b> |
|--|---|---|--|--|
| Borrowings under revolving credit facility | \$ 200,000                                  | \$ 200,000                                      | \$ 300,000                             | \$ 300,000                                 |
| Term facility                              | 247,500                                     | 247,500   | 255,000                                | 255,000                                    |
| Other obligations                          | 30  | 30  | 32                                     | 32   |
| Total debt                                 | 447,530                                     | 447,530   | 555,032                                | 555,032                                    |
| Less: current portion of long-term debt    | (37,500)                                    | (37,500)  | (35,625)                               | (35,625)                                   |
| Total long-term debt                       | \$ 410,030                                  | \$ 410,030                                      | \$ 519,407                             | \$ 519,407                                 |

**Table of Contents**

At September 30, 2014, long-term debt maturing in each of the next five fiscal years and thereafter is as follows:

|              |                   |
|--------------|-------------------|
| 2015         | \$ 28,125         |
| 2016         | 43,155            |
| 2017         | 135,000           |
| 2018         | 241,250           |
| 2019         | 0                 |
| Thereafter   | 0                 |
| <b>Total</b> | <b>\$ 447,530</b> |

If we do not meet the forecast in our budgets, we could violate our debt covenants and, absent a waiver from our lenders or an amendment to the Credit Agreement, we could be in default under the Credit Agreement. As a result, our debt under the Credit Agreement could become due, which would have a material adverse effect on our financial condition and results of operations. As of September 30, 2014, we were in compliance with all the financial covenants of the Credit Agreement.

Interest expense is reported net of interest income in our Condensed Consolidated Statements of Income. Interest expense, net was \$2.7 million and \$2.0 million for the three months ended September 30, 2014 and 2013, respectively. Gross interest expense was \$3.1 million and \$2.4 million for the three months ended September 30, 2014 and 2013, respectively. The non-cash portion of gross interest expense was \$0.5 million for each of the three month periods ended September 30, 2014 and 2013, associated with the amortization of debt issuance costs on the Credit Agreement. The cash portion of gross interest expense was \$2.6 million and \$1.9 million in the three months ended September 30, 2014 and 2013, respectively, associated with interest on the Credit Agreement and our short-term borrowings. Interest income was \$0.4 million for each of the three month periods ended September 30, 2014 and 2013, associated with interest earned on our cash and cash equivalents.

**Note 10 Income Taxes**

Our provision for income taxes is based on an estimated annual tax rate for the year applied to federal, state and foreign income. Income tax expense for the three months ended September 30, 2014 and 2013 was \$27.8 million and \$18.7 million, respectively. The effective tax rate for the three months ended September 30, 2014 and 2013 was 25.1 percent and 28.6 percent, respectively. The change in the effective tax rate for the three months ended September 30, 2014 compared to the same period in the prior year was primarily due to discrete tax charges booked in the prior period.

As of September 30, 2014 unrecognized tax benefits and the related interest were \$43.5 million and \$2.3 million, respectively, all of which would affect the tax rate if recognized. During the three months ended September 30, 2014, the change in tax reserves on uncertain tax positions and the related interest were \$(0.7) million and less than \$(0.1) million, respectively.

**Note 11 Shareholders Equity*****Preferred Stock***

As of September 30, 2014 and June 30, 2014, we had no shares of preferred stock outstanding. We are authorized to issue 5 million shares of preferred stock, \$0.01 par value.

***Common Stock***

We have 200 million authorized shares of common stock, \$0.01 par value. At September 30, 2014 and June 30, 2014, we had 98,823,756 and 98,408,042 shares issued; 30,319,785 and 30,319,785 shares in treasury stock and 68,503,971 and 68,088,257 shares outstanding (net of treasury stock), respectively.

**Table of Contents****Changes in Equity:**

The following is a summary of the changes in Accumulated Other Comprehensive Income ( AOCI ) and changes in equity for the three months ended September 30, 2014 and 2013:

| (\$ in thousands, except<br>per share data)                           | Additional         |                 |                    |           | Retained<br>Earnings | Treasury<br>Stock | Total<br>Harman<br>International<br>Industries,<br>Incorporated Non |                         | Total<br>Equity |
|---|--------------------|-----------------|--------------------|-----------|----------------------|-------------------|---|-------------------------|-----------------|
|   | Preferred<br>Stock | Common<br>Stock | Paid-in<br>Capital | AOCI      |                      |                   | Shareholders'<br>Equity   | Controlling<br>Interest |                 |
| <b>Balance, June 30, 2014</b>   | \$ 0               | \$ 984          | \$ 1,040,254       | \$ 39,799 | \$ 1,979,234         | \$ (1,267,693)    | \$ 1,792,578  | \$ 443                  | \$ 1,793,021    |
| Net income  | 0                  | 0               | 0                  | 0         | 82,973               | 0                 | 82,973  | (39)                    | 82,934          |
| Other<br>comprehensive income,<br>net of tax                          |                    |                 |                    | 1,461     |                      |                   | 1,461   | 4                       | 1,465           |
| Exercise of stock options   | 0                  | 4               | 6,005              | 0         | 0                    | 0                 | 6,009   | 0                       | 6,009           |
| Repurchases related to<br>share-based<br>compensation<br>arrangements | 0                  | 0               | (21,670)           | 0         | 0                    | 0                 | (21,670)  | 0                       | (21,670)        |
| Share-based<br>compensation, net                                      | 0                  | 0               | 10,818             | 0         | 0                    | 0                 | 10,818  | 0                       | 10,818          |
| Excess tax benefit from<br>share-based<br>compensation                | 0                  | 0               | 2,803              | 0         | 0                    | 0                 | 2,803   | 0                       | 2,803           |
| Dividends (\$0.33 per<br>share)                                       | 0                  | 0               | 0                  | 0         | (22,735)             | 0                 | (22,735)  | 0                       | (22,735)        |
| <b>Balance, September 30,<br/>2014</b>                                | \$ 0               | \$ 988          | \$ 1,038,210       | \$ 41,260 | \$ 2,039,472         | \$ (1,267,693)    | \$ 1,852,237  | \$ 408                  | \$ 1,852,645    |

| (\$ in thousands, except<br>per share data) | Additional         |                 |                    |           | Retained<br>Earnings | Treasury<br>Stock | Total<br>Harman<br>International<br>Industries,<br>Incorporated Non |                         | Total<br>Equity |
|---|--------------------|-----------------|--------------------|-----------|----------------------|-------------------|---|-------------------------|-----------------|
|   | Preferred<br>Stock | Common<br>Stock | Paid-in<br>Capital | AOCI      |                      |                   | Shareholders'<br>Equity   | Controlling<br>Interest |                 |
| <b>Balance, June 30, 2013</b>               | \$ 0               | \$ 970          | \$ 971,748         | \$ 21,800 | \$ 1,827,267         | \$ (1,176,914)    | \$ 1,644,871  | \$ 0                    | \$ 1,644,871    |
| Net income                                  | 0                  | 0               | 0                  | 0         | 46,452               | 0                 | 46,452  | 0                       | 46,452          |
| Other<br>comprehensive income,              |                    |                 |                    | 18,694    |                      |                   | 18,694  |                         | 18,694          |



|  |      |        |            |           |              |                |              |      |              |
|--|------|--------|------------|-----------|--------------|----------------|--------------|------|--------------|
| net of tax   |      |        |            |           |              |                |              |      |              |
| Treasury stock repurchases                                   | 0    | 0      | 0          | 0         | 0            | (26,371)       | (26,371)     | 0    | (26,371)     |
| Exercise of stock options                                    | 0    | 8      | 17,054     | 0         | 0            | 0              | 17,062       | 0    | 17,062       |
| Repurchases related to share-based compensation arrangements | 0    | 0      | (11,913)   | 0         | 0            | 0              | (11,913)     | 0    | (11,913)     |
| Share-based compensation, net                                | 0    | 0      | 6,623      | 0         | 0            | 0              | 6,623        | 0    | 6,623        |
| Excess tax benefit from share-based compensation             | 0    | 0      | 878        | 0         | 0            | 0              | 878          | 0    | 878          |
| Dividends (\$0.30 per share)                                 | 0    | 0      | 0          | 0         | (20,732)     | 0              | (20,732)     | 0    | (20,732)     |
| <b>Balance, September 30, 2013</b>                           | \$ 0 | \$ 978 | \$ 984,390 | \$ 40,494 | \$ 1,852,987 | \$ (1,203,285) | \$ 1,675,564 | \$ 0 | \$ 1,675,564 |

## Note 12 Share-Based Compensation

On December 7, 2011 (the Effective Date), our shareholders approved the 2012 Stock Option and Incentive Plan (the 2012 Plan), which is effective through December 7, 2021. As of the Effective Date, no further grants may be granted under our former plan, the Amended and Restated 2002 Stock Option and Incentive Plan, as amended (the 2002 Plan and together with the 2012 Plan, the Plans). On December 4, 2013, we amended the 2012 Plan to (i) increase the number of shares available under the 2012 Plan for the grant of future awards by 2,869,821 shares to an aggregate amount not to exceed 7,269,821 shares of our common stock and (ii) modified certain share counting provisions related to the definition of a full-value grant from 1.71 to 1.5 ( Full-Value Grant ). The 2012 Plan provides for two types of awards: (i) a Full-Value Grant under which one award shall reduce the shares available for grant under the 2012 Plan by 1.71 shares if granted prior to December 4, 2013 or 1.5 shares if granted on or after December 4, 2013, and (ii) an option or stock appreciation right grant, under which one award shall reduce the shares available for grant under the 2012 Plan by one share. During the three months ended September 30, 2014, 1,145 options to purchase shares of our common stock, 385,427 stock-settled restricted stock units, 856 cash-settled restricted stock units and 1,486 cash-settled stock appreciation rights were granted under the 2012 Plan. As of September 30, 2014, there were 3,994,618 shares available for grant under the 2012 Plan.

Share-based compensation expense, net was \$10.8 million and \$6.6 million for the three months ended September 30, 2014 and 2013, respectively. The total income tax benefit recognized in the Condensed Consolidated Statements of Income for share-based compensation arrangements was \$3.0 million and \$1.5 million for the three months ended September 30, 2014 and 2013, respectively.

**Table of Contents*****Fair Value Determination***

The fair value of each option award is estimated on the date of grant using the Black-Scholes option valuation model, which uses the assumptions noted in the following table.

|                             | <b>Three Months Ended September 30,</b> |               |
|-----------------------------|---|---------------|
|                             | <b>2014</b>                             | <b>2013</b>   |
| Expected volatility         | 31.6% - 38.6%                           | 39.9% - 55.4% |
| Weighted-average volatility | 35.9%                                   | 46.1%         |
| Expected annual dividend    | \$ 1.32                                 | \$ 1.20       |
| Expected term (in years)    | 2.12 - 4.12                             | 2.61 - 4.66   |
| Risk-free rate              | 0.4% - 1.2%                             | 0.6% - 1.8%   |

Groups of option holders (directors, executives and non-executives) that have similar historical behavior are considered separately for valuation purposes. Expected volatilities are based on historical closing prices of our common stock over the expected option term. We use historical data to estimate option exercises and employee terminations within the valuation model. The expected term of options granted is derived using the option valuation model and represents the estimated period of time from the date of grant that the option is expected to remain outstanding. The risk-free rate for periods within the contractual life of the option is based on the U.S. Treasury yield curve in effect at the time of grant.

***Stock Option Activity***

A summary of option activity under our Plans as of September 30, 2014 and changes during the three months ended September 30, 2014 is presented below:

|  | <b>Shares</b>    | <b>Weighted<br/>Average<br/>Exercise<br/>Price Per<br/>Share</b> | <b>Weighted<br/>Average<br/>Remaining<br/>Contractual<br/>Term (Years)</b> | <b>Aggregate<br/>Intrinsic<br/>Value</b> |
|--|------------------|--|--|--|
| Outstanding at June 30, 2014             | 1,419,598        | \$ 65.90   | 6.70   | \$ 62,204                                |
| Granted                                  | 1,145            | 112.77   |  |  |
| Exercised                                | (120,361)        | 48.42  |  |  |
| Forfeited or expired                     | (29,269)         | 53.58  |  |  |
| <b>Outstanding at September 30, 2014</b> | <b>1,271,113</b> | <b>\$ 67.89</b>  | <b>6.35</b>  | <b>\$ 44,206</b>                         |
| Exercisable at September 30, 2014        | 795,427          | \$ 73.47   | 5.06   | \$ 25,345                                |

The weighted-average grant-date fair value of options granted for the three months ended September 30, 2014 and 2013 was \$26.68 and \$20.74, respectively. The total intrinsic value of options exercised for the three months ended September 30, 2014 and 2013 was \$7.6 million and \$11.0 million, respectively.

***Modification of Certain Stock Option Awards***

Prior to fiscal year 2011, certain of the award agreements under the 2002 Plan stated that vested options not exercised were forfeited upon termination of employment for any reason other than death or disability. However, such award agreements provided that the Compensation and Option Committee of our Board of Directors (the Compensation and Option Committee ) could extend the time period to exercise vested options 90 days beyond the employment termination date for certain employees. During the three months ended September 30, 2014 and 2013, the Compensation and Option Committee used this authority. This action represented a modification of the terms or conditions of an equity award and therefore was accounted for as an exchange of the original award for a new award. Incremental share-based compensation cost for the excess of the fair value of the new award over the fair value of the original award was immaterial.

#### *Restricted Stock Units*

In the three months ended September 30, 2014, we granted 98,586 restricted stock units with earnings per share ( EPS ) performance conditions, and 98,586 restricted stock units with market conditions under the 2012 Plan. Additionally, both the restricted stock units with EPS performance conditions and the restricted stock units with market conditions, secondarily vest based on the achievement of a return on invested capital ( ROIC ) performance condition, specifically, the achievement of a certain average ROIC level over fiscal years 2015 through 2017. The restricted stock units with EPS performance conditions cliff vest three years from the date of grant based on the achievement of certain cumulative EPS levels from fiscal years 2015 through 2017. The restricted stock units with

**Table of Contents**

market conditions cliff vest three years from the date of grant based on a comparison of our total shareholder return ( TSR ) to the TSR of a selected peer group of publicly listed multinational companies. The grant date fair value of the restricted stock units with market conditions of \$7.5 million was calculated using a Monte Carlo simulation model. Compensation expense is recognized ratably over the three-year vesting period based on the grant date fair value and our assessment of the probability that the applicable targets will be met for the performance conditions, which is reassessed each reporting period.

In the three months ended September 30, 2013, we granted 130,616 restricted stock units with EPS performance conditions, and 130,641 restricted stock units with market conditions under the 2012 Plan. Additionally, both the restricted stock units with EPS performance conditions and the restricted stock units with market conditions, secondarily vest based on the achievement of a ROIC performance condition, specifically, the achievement of a certain average ROIC level over fiscal years 2014 through 2016. The restricted stock units with EPS performance conditions cliff vest three years from the date of grant based on the achievement of certain cumulative EPS levels from fiscal years 2014 through 2016. The restricted stock units with market conditions cliff vest three years from the date of grant based on a comparison of our TSR to the TSR of a selected peer group of publicly listed multinational companies. The grant date fair value of the restricted stock units with market conditions of \$6.0 million was calculated using a Monte Carlo simulation model. Compensation expense is recognized ratably over the three-year vesting period based on the grant date fair value and our assessment of the probability that the applicable targets will be met for the performance conditions, which is reassessed each reporting period.

In the three months ended September 30, 2014 and 2013, we also granted 188,255 and 172,816 time vested restricted stock units, without performance or market conditions, respectively, under the 2012 Plan that vest three years from the date of grant.

In the three months ended September 30, 2014 and 2013, we granted 856 and 613 cash-settled restricted stock units, respectively, under the 2012 Plan. These restricted stock units are accounted for as liability awards and are recorded at the fair value at the end of the reporting period in accordance with their vesting schedules. During the three months ended September 30, 2014 and 2013, 1,150 and 0 of these restricted stock units were settled, respectively. At September 30, 2014, 2,338 cash-settled restricted stock units were outstanding.

A summary of equity classified restricted stock unit activity as of September 30, 2014 and changes during the three months ended September 30, 2014 is presented below:

|  | <b>Restricted Stock<br/>Units</b> |
|--|-----------------------------------|
| Nonvested at June 30, 2014             | 1,543,925                         |
| Granted                                | 385,427                           |
| Vested                                 | (485,435)                         |
| Forfeited                              | (78,213)                          |
| <b>Nonvested at September 30, 2014</b> | <b>1,365,704</b>                  |

At September 30, 2014, the aggregate intrinsic value of equity-classified restricted stock units was \$133.9 million and there was \$63.2 million of total unrecognized compensation cost related to equity classified restricted stock unit compensation arrangements. The weighted average recognition period was 1.8 years.

*Stock Appreciation Rights*

A summary of cash-settled stock appreciation rights as of September 30, 2014 and changes during the three months ended September 30, 2014 is presented below:

|                                  | <b>Stock<br/>Appreciation<br/>Rights</b> |
|----------------------------------|--|
| Non-vested at June 30, 2014      | 12,031                                   |
| Granted                          | 1,486                                    |
| Vested                           | (6,723)                                  |
| Forfeited                        | 0  |
| Non-vested at September 30, 2014 | 6,794                                    |
| Exercisable                      | 6,726                                    |

These stock appreciation rights are accounted for as liability awards and are recorded at the fair value at the end of the reporting period in accordance with their vesting schedules. The fair value is calculated using the Black-Scholes option valuation model using assumptions consistent with our stock options.

**Table of Contents**

**Note 13 Derivatives**

We are exposed to market risk from changes in foreign currency exchange rates and interest rates, which could affect our operating results, financial condition and cash flows. We manage our exposure to these risks through our regular operating and financial activities and, when appropriate, through the use of derivative financial instruments. These derivative instruments are utilized to hedge economic exposures, as well as to reduce earnings and cash flow volatility resulting from shifts in market rates. We enter into limited types of derivative contracts, including foreign currency spot and forward, as well as interest rate swap contracts, to manage foreign currency and interest rate exposures. Our primary foreign currency exposure is the Euro. The fair market values of all our derivative contracts change with fluctuations in interest rates and currency rates and are designed so that any changes in their values are offset by changes in the values of the underlying exposures. Derivative financial instruments are held solely as risk management tools and not for trading or speculative purposes.

We record all derivative instruments as either assets or liabilities at fair value in our Condensed Consolidated Balance Sheets. Certain of these derivative contracts have been designated as cash flow hedges, whereby gains and losses are reported within AOCI in our Condensed Consolidated Balance Sheets, until the underlying transaction occurs, at which point they are reported in earnings as gains and losses in our Condensed Consolidated Statements of Income. Certain of our derivatives, for which hedge accounting is not applied, are effective as economic hedges. These derivative contracts are required to be recognized each period at fair value, with gains and losses reported in earnings in our Condensed Consolidated Statements of Income and therefore do result in some level of earnings volatility. The level of volatility will vary with the type and amount of derivative hedges outstanding, as well as fluctuations in the currency and interest rate markets during the period. The related cash flow impacts of all our derivative activities are reflected as cash flows from operating activities.

Derivatives, by their nature, involve varying degrees of market and credit risk. The market risk associated with these instruments resulting from currency exchange and interest rate movements is expected to offset the market risk of the underlying transactions, assets and liabilities being hedged. We do not believe there is significant risk of loss in the event of non-performance by the counterparties associated with these instruments, because these transactions are executed with a diversified group of major financial institutions. Furthermore, our policy is to contract only with counterparties having a minimum investment grade or better credit rating. Credit risk is managed through the continuous monitoring of exposure to such counterparties.

**Foreign Exchange Risk Management**

We use foreign exchange contracts to hedge the price risk associated with foreign denominated forecasted purchases of materials used in our manufacturing process and to manage currency risk associated with operating costs in certain operating units, including foreign currency denominated intercompany loans and other foreign currency denominated assets. These contracts generally mature within two to five years. The majority of these contracts are designated as cash flow hedges.

**Table of Contents**

At September 30, 2014 and June 30, 2014, we had outstanding foreign exchange contracts, primarily forward contracts, which are summarized below:

|                                    | September 30, 2014   |  | June 30, 2014        |  |
|------------------------------------|----------------------|--|----------------------|--|
|                                    | Gross Notional Value | Fair Value Asset/ (Liability) <sup>(1)</sup> | Gross Notional Value | Fair Value Asset/ (Liability) <sup>(1)</sup> |
| <b>Currency Hedged (Buy/Sell):</b> |                      |  |                      |  |
| U.S. Dollar/Euro                   | \$ 1,597,500         | \$ 93,910                                    | \$ 1,558,950         | \$ (21,418)                                  |
| Euro/U.S. Dollar                   | 223,350              | (15,455)                                     | 214,781              | 1,077  |
| Euro/Swiss Franc                   | 36,649               | (34)   | 0                    | 0  |
| Swiss Franc/Euro                   | 36,649               | 97   | 0                    | 0  |
| U.S. Dollar/Indian Rupee           | 35,000               | 285  | 35,000               | (583)  |
| Chinese Yuan/U.S. Dollar           | 23,683               | 131  | 0                    | 0  |
| Japanese Yen/Euro                  | 20,378               | (224)  | 0                    | 0  |
| British Pound/U.S. Dollar          | 14,591               | (30)   | 0                    | 0  |
| Chinese Yuan/Euro                  | 11,110               | 579  | 0                    | 0  |
| Hungarian Forint/Euro              | 9,589                | 118  | 0                    | 0  |
| Euro/Russian Rubles                | 7,576                | 201  | 8,828                | (141)  |
| U.S. Dollar/Brazilian Real         | 1,836                | 100  | 5,052                | (95)   |
| U.S. Dollar/Russian Rubles         | 986                  | 26   | 0                    | 0  |
| Russian Rubles/U.S. Dollar         | 248                  | (7)  | 0                    | 0  |
| Euro/Brazilian Real                | 0                    | 0  | 8,490                | (123)  |
| <b>Total</b>                       | <b>\$ 2,019,145</b>  | <b>\$ 79,697</b>                             | <b>\$ 1,831,101</b>  | <b>\$ (21,283)</b>                           |

<sup>(1)</sup> Represents the net receivable/(payable) included in our Condensed Consolidated Balance Sheets.

**Cash Flow Hedges**

We designate a portion of our foreign exchange contracts as cash flow hedges of foreign currency denominated purchases. As of September 30, 2014 and June 30, 2014, we had \$1,535.4 million and \$1,467.7 million of forward contracts maturing through June 2018. These contracts are recorded at fair value in the accompanying Condensed Consolidated Balance Sheets. During the fiscal year ended June 30, 2014, we changed our election to now include forward points in our effectiveness assessment. Prior to this change, the changes in fair value for these contracts were calculated on a spot to spot rate basis. Effective September 30, 2013, the changes in fair value for these contracts are calculated on a forward to forward rate basis. These changes in fair value are reported in AOCI and are reclassified to either Cost of sales or Selling, general and administrative expenses ( SG&A ), depending on the nature of the underlying asset or liability that is being hedged, in our Condensed Consolidated Statements of Income, in the period or periods during which the underlying transaction occurs.

Changes in the fair value of the derivatives are highly effective in offsetting changes in the cash flows of the hedged items because the amounts and the maturities of the derivatives approximate those of the forecasted exposures. Any ineffective portion of the derivative is recognized in the current period in our Condensed Consolidated Statements of Income, in the same line item in which the foreign currency gain or loss on the underlying hedged transaction was

recorded. We recognized \$2.0 million and \$0.2 million of ineffectiveness in our Condensed Consolidated Statement of Income in the three months ended September 30, 2014 and 2013, respectively. Prior to September 30, 2013, all components of each derivative's gain or loss, with the exception of forward points (see below), were included in the assessment of hedge ineffectiveness. Effective September 30, 2013, we changed our election and now include forward points in our effectiveness assessment. At September 30, 2014 and June 30, 2014, the fair values of these contracts were a net asset of \$86.2 million and a net liability \$19.9 million, respectively. The amount associated with these hedges that is expected to be reclassified from AOCI to earnings within the next 12 months is a gain of \$32.8 million.

For the three months ended September 30, 2014, we did not recognize any gains or losses related to the change in forward points. For the three months ended September 30, 2013, we recognized \$0.5 million of net gains related to the change in forward points.



**Table of Contents*****Economic Hedges***

When hedge accounting is not applied to derivative contracts, or after former cash flow hedges have been de-designated as balance sheet hedges, we recognize the gain or loss on the associated contracts directly in current period earnings in our Condensed Consolidated Statements of Income as either Foreign exchange losses, net or Cost of sales according to the underlying exposure. As of September 30, 2014 and June 30, 2014, we had \$483.7 million and \$363.4 million, respectively, of forward contracts maturing through March 2015 and December 2014, respectively, in various currencies to hedge foreign currency denominated intercompany loans and other foreign currency denominated assets. At September 30, 2014 and June 30, 2014, the fair values of these contracts were net liabilities of \$6.5 million and \$1.4 million, respectively. Adjustments to the carrying value of the foreign currency forward contracts offset the gains and losses on the underlying loans and other foreign denominated assets in Foreign exchange losses, net in our Condensed Consolidated Statements of Income.

**Interest Rate Risk Management**

We had one interest rate swap contract which matured on September 30, 2013 with a notional amount of \$19.7 million in order to manage our interest rate exposure and effectively convert interest on an operating lease from a variable rate to a fixed rate. The objective of the swap was to offset changes in rent expenses caused by interest rate fluctuations. The interest rate swap contract was designated as a cash flow hedge. At the end of each reporting period, the discounted fair value of the swap contract was calculated and recorded in AOCI and reclassified to rent expense, within SG&A in our Condensed Consolidated Statements of Income, in the then applicable period when rent was paid. If the hedge was determined to be ineffective, the ineffective portion would have been reclassified from AOCI and recorded as rent expense, within SG&A. We recognized zero and less than \$0.1 million of ineffectiveness in each of the three months ended September 30, 2014 and 2013, respectively, in our Condensed Consolidated Statements of Income. All components of the derivative were included in the assessment of the hedges' effectiveness.

**Fair Value of Derivatives**

The following tables provide a summary of the fair value amounts of our derivative instruments as of September 30, 2014 and June 30, 2014:

|                                  | Balance Sheet Location | Fair Value         |               |
|----------------------------------|------------------------|--------------------|---------------|
|                                  |                        | September 30, 2014 | June 30, 2014 |
| <b>Derivatives Designated as</b> |                        |                    |               |
| <b>Cash Flow Hedges, Gross:</b>  |                        |                    |               |
| <b>Other assets:</b>             |                        |                    |               |
| Foreign exchange contracts       | Other current assets   | \$ 27,862          | \$ 1,141      |
| Foreign exchange contracts       | Other assets           | 58,491             | 0             |
| Total assets                     |                        | 86,353             | 1,141         |
| <b>Other liabilities:</b>        |                        |                    |               |
| Foreign exchange contracts       | Accrued liabilities    | 195                | 20,997        |
|                                  |                        | 86,158             | (19,856)      |

Net asset/(liability) for derivatives  
designated as hedging instruments

**Derivatives Designated as**

**Economic Hedges, Gross:**

**Other assets:**

|                            |                      |       |          |
|----------------------------|----------------------|-------|----------|
| Foreign exchange contracts | Other current assets | 9,093 | \$ 1,094 |
|----------------------------|----------------------|-------|----------|

**Other liabilities:**

|                            |                     |        |       |
|----------------------------|---------------------|--------|-------|
| Foreign exchange contracts | Accrued liabilities | 15,554 | 2,521 |
|----------------------------|---------------------|--------|-------|

|                                    |  |         |         |
|------------------------------------|--|---------|---------|
| Net liability for economic hedges: |  | (6,461) | (1,427) |
|------------------------------------|--|---------|---------|

|  |  |           |             |
|--|--|-----------|-------------|
| Total net derivative asset/(liability) |  | \$ 79,697 | \$ (21,283) |
|--|--|-----------|-------------|

**Table of Contents****Derivative Activity:**

The following tables show derivative activity for derivatives designated as cash flow hedges for the three months ended September 30, 2014 and 2013:

| Derivative                              | Location of Derivative Gain/(Loss) Recognized in Income | Gain/(Loss) Reclassified from AOCI into Income (Effective Portion) |               | Gain/(Loss) Recognized in Income on Derivatives (Ineffective Portion) |                 | Gain/(Loss) from Amounts Excluded from Effectiveness Testing |               |
|---|---|--|---------------|---|-----------------|--|---------------|
|   |   | 2014   | 2013          | 2014  | 2013            | 2014   | 2013          |
| <b>Three Months Ended September 30,</b> |   |  |               |   |                 |  |               |
| Foreign exchange contracts              | Cost of sales   | \$ (803)   | \$ 937        | \$ 2,042  | \$ (224)        | \$ 0   | \$ 0          |
| Foreign exchange contracts              | SG&A  | 53   | 0             | 0   | 0               | 0  | 0             |
| Foreign exchange contracts              | Foreign exchange losses, net                            | 0  | 0             | 0   | 0               | (4)  | 520           |
| Interest rate swap                      | SG&A  | 0  | (192)         | 0   | (1)             | 0  | 0             |
| <b>Total cash flow hedges</b>           |   | <b>\$ (750)</b>  | <b>\$ 745</b> | <b>\$ 2,042</b>   | <b>\$ (225)</b> | <b>\$ (4)</b>  | <b>\$ 520</b> |

| Derivative                              | Gain/(Loss) Recognized in AOCI (Effective Portion) |                    |
|---|--|--------------------|
|   | 2014   | 2013               |
| <b>Three Months Ended September 30,</b> |  |                    |
| Foreign exchange contracts              | \$ 107,431   | \$ (19,813)        |
| Interest rate swap                      | 0  | 35                 |
| <b>Total cash flow hedges</b>           | <b>\$ 107,431</b>                                  | <b>\$ (19,778)</b> |

The following table summarizes gains and losses from our derivative instruments that are not designated as hedging instruments for the three months ended September 30, 2014 and 2013:

| Derivative                          | Location of Derivative Gain/(Loss) | Three Months Ended September 30, |            |
|-------------------------------------|------------------------------------|----------------------------------|------------|
|                                     |                                    | 2014                             | 2013       |
| Foreign exchange contracts forwards | Cost of sales                      | \$ 8,337                         | \$ (3,509) |
| Foreign exchange contracts forwards | Foreign exchange gains, net        | (16,636)                         | 9,234      |

**Note 14 Fair Value Measurements**

Pursuant to the accounting guidance for fair value measurements, fair value is defined as the price we would receive to sell an asset or pay to transfer a liability in an orderly transaction with a market participant at the measurement date. When determining the fair value measurements for assets and liabilities, we consider the principal or most advantageous market in which the asset or liability would transact in and we consider assumptions that market participants would use when pricing the asset or liability.

*Fair Value Hierarchy*

Under fair value accounting guidance, there is a three-tier fair value hierarchy to prioritize the inputs used in measuring fair value. Observable inputs reflect market data obtained from independent sources, while unobservable inputs reflect our market assumptions.

The hierarchy gives the highest priority to quoted prices in active markets (Level 1) and the lowest priority to unobservable inputs (Level 3). The three levels are defined as follows:

- Level 1: Observable inputs, such as unadjusted quoted market prices in active markets for the identical asset or liability.
- Level 2: Inputs that are observable for the asset or liability, either directly or indirectly through market corroboration, for substantially the full term of the financial instrument.
- Level 3: Unobservable inputs that reflect the entity's own assumptions in measuring the asset or liability at fair value.

**Table of Contents****Assets and Liabilities Measured at Fair Value on a Recurring Basis**

For assets and liabilities measured at fair value on a recurring basis, fair value is the price we would receive to sell an asset or pay to transfer a liability in an orderly transaction with a market participant at the measurement date. In the absence of active markets for the identical assets and liabilities, such measurements involve developing assumptions based on market observable data, and in the absence of such data, internal information that is consistent with what market participants would use in a hypothetical transaction that occurs at the measurement date.

The following table provides the fair value hierarchy for assets and liabilities measured on a recurring basis.

| Description                   | Fair Value at September 30, 2014 |           |            | Fair Value at June 30, 2014 |             |            |
|-------------------------------|----------------------------------|-----------|------------|-----------------------------|-------------|------------|
|                               | Level 1                          | Level 2   | Level 3    | Level 1                     | Level 2     | Level 3    |
| Assets/(Liabilities)          |                                  |           |            |                             |             |            |
| Available-for-sale securities | \$ 2,540                         | \$ 0      | \$ 0       | \$ 2,472                    | \$ 0        | \$ 0       |
| Foreign exchange contracts    | 0                                | 79,697    | 0          | 0                           | (21,283)    | 0          |
| Pension assets                | 5,056                            | 0         | 0          | 6,641                       | 0           | 0          |
| Contingent consideration      | 0                                | 0         | (8,194)    | 0                           | 0           | (7,328)    |
| Net asset/(liability)         | \$ 7,596                         | \$ 79,697 | \$ (8,194) | \$ 9,113                    | \$ (21,283) | \$ (7,328) |

| Description of Liability | Total Gains (Losses) for the<br>Three Months Ended<br>September 30, |      |
|--------------------------|---|------|
|                          | 2014  | 2013 |
| Contingent Consideration | \$ (866)  | \$ 0 |

The following describes the valuation methodologies we use to measure assets and liabilities accounted for at fair value on a recurring basis:

**Available-for-Sale Securities:** Available-for-sale securities are classified as Level 1 as the fair value was determined from market quotes obtained from financial institutions in active markets.

**Foreign Exchange Contracts:** We use foreign exchange contracts to hedge market risks relating to possible adverse changes in foreign currency exchange rates. Our foreign exchange contracts were measured at fair value using Level 2 inputs. Such inputs include foreign currency exchange spot and forward rates for similar transactions in actively quoted markets.

**Pension Assets:** Our pension assets have been valued using Level 1 inputs as quoted prices in an active market exist for these assets. Refer to Note 17 *Retirement Benefits* for more information.

**Contingent Consideration:** A portion of our contingent consideration is associated with an earn-out related to our acquisition of substantially all of the assets of yurbuds. We use a discounted cash flow approach (a form of the income approach) in determining the fair value of the contingent consideration. The principal inputs to the approach include our expectations of the yurbuds gross profit, through June 30, 2017 and a discount rate that begins with our weighted average cost of capital and adjusts for the risks associated with the underlying yurbuds gross profit outcome, the

functional form of the payout and our credit risk associated with making the payment. During the three months ended September 30, 2014, we reassessed our expectations of the yurbuds gross profit outcome and confirmed our estimate of the \$6.2 million contingent consideration liability.

A portion of our contingent consideration is associated with an earn-out related to our acquisition of Duran Audio BV ( Duran ). We use a probability-weighted discounted cash flow approach (a form of the income approach) in determining the fair value of the contingent consideration. The principal inputs to the approach include our expectations of Duran gross profit related to the sale of certain specified products through June 30, 2020 and a discount rate that begins with our weighted average cost of capital and adjusts for the risks associated with the underlying Duran gross profit outcome, the functional form of the payout and our credit risk associated with making the payment. During the three months ended September 30, 2014, we reassessed our expectations of the Duran gross profit outcome and revised our estimate of the contingent consideration liability to increase it to \$1.9 million from the previously recorded balance of \$0.9 million. This increase of \$1.0 million was recorded within SG&A in our Condensed Consolidated Statement of Income for the three months ended September 30, 2014.

Given the use of significant inputs that are not observable in the market, our contingent consideration is classified within Level 3 of the fair value hierarchy.

**Table of Contents*****Assets and Liabilities Measured at Fair Value on a Non-Recurring Basis***

Certain assets are measured at fair value on a non-recurring basis. These assets are not measured at fair value on an ongoing basis but are subject to fair value adjustments only in certain circumstances. These assets can include loans and long-lived assets that have been reduced to fair value when they are held for sale, impaired loans that have been reduced based on the fair value of the underlying collateral, cost and equity method investments and long-lived assets that are written down to fair value when they are impaired and the remeasurement of retained investments in formerly consolidated subsidiaries upon a change in control that results in deconsolidation of a subsidiary if we sell a controlling interest and retain a noncontrolling stake in the entity. Assets that are written down to fair value when impaired and retained investments are not subsequently adjusted to fair value unless further impairment occurs.

The following table provides the carrying value for assets and liabilities measured on a non-recurring basis, all of which are measured under Level 3 of the fair value hierarchy, and the losses recorded during the periods presented. There were no gains or losses recognized in the three months ended September 30, 2014 and 2013.

| <b>Description of Assets</b> | <b>September 30, 2014</b> | <b>June 30, 2014</b> |
|------------------------------|---------------------------|----------------------|
| Equity method investments    | \$ 1,228                  | \$ 3,578             |
| Goodwill                     | 526,040                   | 540,952              |
| Long-lived assets            | 662,682                   | 691,887              |
| Total                        | \$ 1,189,950              | \$ 1,236,417         |

The following describes the valuation methodologies we use to measure financial and non-financial instruments accounted for at fair value on a non-recurring basis.

**Equity Method Investments:** Equity method investments are generally valued using a discounted cash flow model, comparative market multiples or a combination of both approaches as appropriate. These investments are generally included in Level 3.

**Goodwill:** Goodwill is evaluated for impairment annually or more frequently if an event or circumstance indicates that an impairment loss may have been incurred. This asset is included in Level 3. Refer to Note 8 *Goodwill and Intangible Assets, Net* for more information.

**Long-lived Assets:** Long-lived assets include Property, plant and equipment, net and intangible assets, and are valued using the best information available, including quoted market prices or market prices for similar assets when available or internal cash flow estimates discounted at an appropriate interest rate or independent appraisals, as appropriate. For real estate, cash flow estimates are based on current market estimates that reflect current and projected lease profiles and available industry information about expected trends in rental, occupancy and capitalization rates. These assets are generally included in Level 3.

**Table of Contents****Note 15 Other Comprehensive Income (Loss)**

Other comprehensive income (loss) is comprised of the following:

|  | Three Months Ended<br>September 30, 2014 |             | Three Months Ended<br>September 30, 2013 |            |
|--|--|-------------|--|------------|
|  | Pre-Tax                                  | Net of Tax  | Pre-Tax                                  | Net of Tax |
| Foreign currency translation (losses) gains  | \$ (81,415)                              | \$ (81,415) | \$ 34,085                                | \$ 34,085  |
| Changes in hedging derivatives:  |  |             |  |            |
| Reclassifications from AOCI into income (effective portion) <sup>(1)</sup>               | 803                                      | 607         | (937)                                    | (699)      |
| Reclassifications from AOCI into income (effective portion) <sup>(2)</sup>               | (53)                                     | (39)        | 192                                      | 143        |
| Reclassifications from AOCI into income (ineffective portion) <sup>(1)</sup>             | (2,042)                                  | (1,545)     | 224                                      | 167        |
| Reclassifications from AOCI into income (ineffective portion) <sup>(2)</sup>             | 0  | 0           | 1  | 1          |
| Gains (losses) recognized in AOCI (effective portion)                                    | 107,431                                  | 81,297      | (19,778)                                 | (14,757)   |
| Other gains (losses)   | 2,042                                    | 1,544       | (258)                                    | (191)      |
| Unrealized gains (losses) on hedging derivatives   | 108,181                                  | 81,864      | (20,556)                                 | (15,336)   |
| Pension liability adjustment:  |  |             |  |            |
| Amortization of prior service cost <sup>(3)</sup>  | 243                                      | 170         | 250                                      | 160        |
| Amortization of net loss <sup>(3)</sup>  | 948                                      | 664         | 754                                      | 499        |
| Expected return on plan assets <sup>(3)</sup>  | (66)                                     | (46)        | (62)                                     | (48)       |
| Other gains (losses) <sup>(4)</sup>  | 915                                      | 189         | (923)                                    | (673)      |
| Pension liability adjustment   | 2,040                                    | 977         | 19                                       | (62)       |
| Unrealized gains on available-for-sale securities  | 60                                       | 39          | 10                                       | 7          |
| Other comprehensive income   | 28,866                                   | 1,465       | 13,558                                   | 18,694     |
| Other comprehensive income attributable to noncontrolling interest                       | 4  | 4           | 0  | 0          |
| Other comprehensive income attributable to Harman International Industries, Incorporated | \$ 28,862                                | \$ 1,461    | \$ 13,558                                | \$ 18,694  |

(1) Reclassified to Cost of sales in our Condensed Consolidated Statements of Income. Refer to Note 13 *Derivatives* for more information.

(2) Reclassified to SG&A in our Condensed Consolidated Statements of Income. Refer to Note 13 *Derivatives* for more information.

(3) Reclassified to SG&A in our Condensed Consolidated Statements of Income. Refer to Note 17 *Retirement Benefits* for more information.

(4) Primarily represents currency impact on cumulative amount of benefit plan net actuarial losses and prior service credits included in AOCI.



**AOCI:** At September 30, 2014 and June 30, 2014 AOCI consisted of the following:

| <b>Income/(Loss):</b>                             | <b>September 30, 2014</b> | <b>June 30, 2014</b> |
|---|---------------------------|----------------------|
| Cumulative translation adjustment                 | \$ 14,735                 | \$ 96,154            |
| Pension liability adjustment                      | (41,559)                  | (42,536)             |
| Unrealized gains (losses) on hedging derivatives  | 67,645                    | (14,219)             |
| Unrealized gains on available-for-sale securities | 439                       | 400                  |
| <b>Total AOCI</b>                                 | <b>\$ 41,260</b>          | <b>\$ 39,799</b>     |

We had approximately \$2.5 million of investments at September 30, 2014 and June 30, 2014 included in Other current assets in our Condensed Consolidated Balance Sheets that have been classified as available-for-sale securities. These securities are recorded at fair value with realized gains and losses recorded in income and unrealized gains and losses recorded in AOCI, net of taxes.

#### **Note 16 Restructuring Program**

Our restructuring program that is designed to improve our global footprint, cost structure, technology portfolio, human resources and internal processes continues. For the three months ended September 30, 2014 and 2013, we continued to refine existing programs and launched significant new programs focused on achieving further productivity improvements to: (i) optimize certain research and development, supply chain and administrative functions; (ii) outsource certain manufacturing capabilities; (iii) divest or sublease facilities no longer needed to support current operations and (iv) relocate certain functions to best cost countries.

**Table of Contents**

A summary and components of our restructuring initiatives are presented below and include accruals for new programs as well as revisions to estimates, both increases and decreases, to programs accrued in prior periods:

|                                 | <b>Severance<br/>Related<br/>Costs</b> | <b>Third Party<br/>Contractor<br/>Termination Costs</b> | <b>Facility Closure<br/>and Other<br/>Related<br/>Costs</b> | <b>Asset<br/>Impairments<sup>(1)</sup></b> | <b>Total</b> |
|---------------------------------|--|---|---|--|--------------|
| Liability, June 30, 2014        | \$ 54,157                              | \$ 0  | \$ 30,262   | \$ 0                                       | \$ 84,419    |
| Expense <sup>(2)</sup>          | 5,093                                  | 0   | 439   | 1,394                                      | 6,926        |
| Accumulated depreciation offset | 0                                      | 0   | 0   | (1,394)                                    | (1,394)      |
| Payments                        | (3,834)                                | 0   | (1,010)   | 0  | (4,844)      |
| Foreign currency translation    | (3,879)                                | 0   | (1,772)   | 0  | (5,651)      |
| Liability, September 30, 2014   | \$ 51,537                              | \$ 0  | \$ 27,919   | \$ 0                                       | \$ 79,456    |
| Liability, June 30, 2013        | \$ 23,563                              | \$ 1,014  | \$ 33,848   | \$ 0                                       | \$ 58,425    |
| Expense <sup>(2)</sup>          | 20,694                                 | 12  | 1,309   | 2,020                                      | 24,035       |
| Accumulated depreciation offset | 0                                      | 0   | 0   | (2,020)                                    | (2,020)      |
| Payments                        | (9,990)                                | (61)  | (1,858)   | 0  | (11,909)     |
| Foreign currency translation    | 824                                    | 28  | 1,035   | 0  | 1,887        |
| Liability, September 30, 2013   | \$ 35,091                              | \$ 993  | \$ 34,334   | \$ 0                                       | \$ 70,418    |

(1) Credits related to restructuring charges for accelerated depreciation and inventory provisions are recorded against the related assets in Property, plant and equipment, net or Inventories in our Condensed Consolidated Balance Sheets and do not impact the restructuring liability.

(2) Restructuring expenses noted above are primarily in SG&A in our Condensed Consolidated Statements of Income. Asset impairments which consist of accelerated depreciation and inventory provisions are primarily in Cost of sales in our Condensed Consolidated Statements of Income.

Restructuring liabilities are recorded in Accrued liabilities and Other non-current liabilities in our Condensed Consolidated Balance Sheets.

Restructuring expenses by reporting business segment are presented below:

|              | <b>Three Months Ended<br/>September 30,</b> |             |
|--------------|---|-------------|
|              | <b>2014</b>                                 | <b>2013</b> |
| Infotainment | \$ (10)                                     | \$ 20,731   |
| Lifestyle    | 1,815                                       | 883         |
| Professional | 3,727                                       | 401         |
| Total        | 5,532                                       | 22,015      |

|                   |          |           |
|-------------------|----------|-----------|
| Asset impairments | 1,394    | 2,020     |
| Total             | \$ 6,926 | \$ 24,035 |

**Note 17 Retirement Benefits*****Plan Descriptions****Retirement savings plan*

We provide a Retirement Savings Plan (the Savings Plan ) for certain employees in the United States. Under the Savings Plan, and subject to certain limitations: (i) employees may contribute up to 50 percent of their pretax compensation; (ii) each business unit will make a safe harbor non-elective contribution in an amount equal to three percent of a participant's pre-tax compensation; and (iii) each business unit may also make a matching contribution of 50 percent of an employee's tax-deferred compensation, up to the first six percent of a participant's pre-tax compensation. Matching contributions vest at a rate of 25 percent for each year of service with the employer, beginning with the second year of service.

**Table of Contents***Pension benefits*

We provide defined pension benefits to certain eligible employees. The measurement date used for determining pension benefits is the last day of our fiscal year, June 30<sup>th</sup>. We have certain business units in Europe and Asia that maintain defined benefit pension plans for many of our current and former employees. The coverage provided and the extent to which the retirees share in the cost of the program vary by business unit. Generally, plan benefits are based on age, years of service and average compensation during the final years of service. In the United States, we have a Supplemental Executive Retirement Plan (the SERP) that provides retirement, death and termination benefits, as defined in the SERP, to certain key executives designated by our Board of Directors. The majority of our defined benefit plans do not have contractual or statutory provisions which specify minimum funding requirements. We are in compliance with all existing contractual obligations and statutory provisions.

The SERP is an unfunded plan for tax purposes and under the Employee Retirement Income Security Act of 1974 (ERISA) all obligations arising under the SERP are payable from our general assets. To assist in the funding of the benefits under the SERP, we maintain assets in an irrevocable trust whereby the use of these assets is restricted to funding our future benefit obligations under the SERP. These assets are not plan assets of the SERP, therefore, in the event of bankruptcy, the assets become unrestricted and the SERP would become a general creditor of our company. The assets and liabilities, and earnings and expenses, of the irrevocable trust are consolidated in our condensed consolidated financial statements. As of September 30, 2014 and June 30, 2014, there were \$97.5 million and \$97.4 million, respectively, of total assets included in the irrevocable trust of which \$58.1 million in each period consist of Cash and cash equivalents and \$39.4 million and \$39.3 million, respectively, consist of the cash surrender value of life insurance policies.

The following table presents the components of net periodic benefit cost for the three months ended September 30, 2014 and 2013:

|                                    | <b>Three Months Ended<br/>September 30,</b> |                 |
|------------------------------------|---|-----------------|
|                                    | <b>2014</b>                                 | <b>2013</b>     |
| Service cost                       | \$ 1,023                                    | \$ 610          |
| Interest cost                      | 1,724                                       | 1,776           |
| Expected return on plan assets     | (66)  | (62)            |
| Amortization of prior service cost | 243   | 247             |
| Amortization of net loss           | 948   | 754             |
| Settlement                         | 105   | 0               |
| <b>Net periodic benefit cost</b>   | <b>\$ 3,977</b>                             | <b>\$ 3,325</b> |

During the three months ended September 30, 2014 and 2013, we made contributions of \$2.6 million and \$2.2 million, respectively, to the defined benefit pension plans which were paid to participants. We expect to make approximately \$7.5 million in contributions for the remainder of the fiscal year ending June 30, 2015.

**Note 18 Business Segment Data**

We design, manufacture and market high-quality, high fidelity audio products and electronic systems for the infotainment, automotive audio, home audio and professional markets. Our chief operating decision maker evaluates

performance and allocates resources based on net sales, operating income and working capital in each of the reporting segments.

***Infotainment***

Our Infotainment segment designs, manufactures and markets infotainment systems for vehicle applications to be installed primarily as original equipment by automotive manufacturers.

***Lifestyle***

Our Lifestyle segment designs, manufactures and markets automotive audio systems for vehicle applications to be installed primarily as original equipment by automotive manufacturers and a wide range of mid-end to high-end audio and consumer electronics for home, multimedia and mobile applications. Our Lifestyle audio products feature some of the world's most recognized audio brands, including AKG®, Harman/Kardon®, Infinity®, JBL®, Lexicon®, Logic 7®, Mark Levinson®, Revel®, Selenium® and yurbuds® Powered by JBL.

**Table of Contents****Professional**

Our Professional segment designs, manufactures and markets an extensive range of loudspeakers, power amplifiers, digital signal processors, microphones, headphones, lighting systems, mixing consoles, video and control solutions and information delivery systems used by audio professionals in concert halls, stadiums, airports, houses of worship and other public spaces. We also provide high quality products to the sound reinforcement, music instrument support and broadcast and recording segments of the professional audio market. We offer complete systems solutions for professional installations and users around the world. Our Professional products are marketed globally under brand names including AKG, AMX®, BSS®, Crown®, dbx®, DigiTech®, JBL Professional, Lexicon, Martin®, Selenium, Soundcraft® and Studer®.

**Other**

Our Other segment includes compensation, benefits and occupancy costs for corporate employees, net of reporting segment allocations, expenses associated with new technology innovation and our corporate brand identity campaign.

The following table reports Net sales and Operating income (loss) by each reporting segment for the three months ended September 30, 2014 and 2013:

|                          | <b>Three Months Ended</b> |                     |
|--------------------------|---------------------------|---------------------|
|                          | <b>September 30,</b>      |                     |
|                          | <b>2014</b>               | <b>2013</b>         |
| Net sales:               |                           |                     |
| Infotainment             | \$ 748,097                | \$ 639,753          |
| Lifestyle                | 426,144                   | 334,488             |
| Professional             | 254,437                   | 197,431             |
| Other                    | 244                       | 133                 |
| <b>Total</b>             | <b>\$ 1,428,922</b>       | <b>\$ 1,171,805</b> |
| Operating income (loss): |                           |                     |
| Infotainment             | \$ 77,353                 | \$ 32,427           |
| Lifestyle                | 49,966                    | 41,240              |
| Professional             | 23,265                    | 26,480              |
| Other                    | (34,801)                  | (30,765)            |
| <b>Total</b>             | <b>\$ 115,783</b>         | <b>\$ 69,382</b>    |

**Note 19 Significant Customers**

Presented below are the percentages of net sales to, and net accounts receivables due from, customers who represent ten percent or more of our net sales or net accounts receivable, as follows:

| Net Sales | Accounts Receivable, Net |
|-----------|--------------------------|
|-----------|--------------------------|

|                           | <b>Three months Ended</b>     |                               |                               |                          |
|---------------------------|-------------------------------|-------------------------------|-------------------------------|--------------------------|
|                           | <b>September 30,<br/>2014</b> | <b>September 30,<br/>2013</b> | <b>September 30,<br/>2014</b> | <b>June 30,<br/>2014</b> |
| BMW                       | 15%                           | 18%                           | 12%                           | 11%                      |
| Fiat Chrysler Automobiles | 14%                           | 14%                           | 14%                           | 13%                      |
| Audi/Volkswagen           | 11%                           | 12%                           | 8%                            | 7%                       |
| Toyota/Lexus              | 7%                            | 10%                           | 4%                            | 4%                       |
| Other customers           | 53%                           | 46%                           | 62%                           | 65%                      |
| Total                     | 100%                          | 100%                          | 100%                          | 100%                     |

We anticipate that BMW, Fiat Chrysler Automobiles, Audi/Volkswagen and Toyota/Lexus will continue to account for a significant portion of our net sales and net accounts receivable for the foreseeable future. Our customers are not obligated to any long-term purchases of our products.

**Table of Contents**

**Note 20 Commitments and Contingencies**

At September 30, 2014, we were subject to legal claims and litigation arising in the ordinary course of business, including the matters described below. The outcome of these legal actions cannot be predicted with certainty; however, management, based upon advice from legal counsel, believes such actions are either without merit or will not have a material adverse effect on our financial condition, results of operations or cash flows.

**In re Harman International Industries, Inc. Securities Litigation**

On October 1, 2007, a purported class action lawsuit was filed by Cheolan Kim (the Kim Plaintiff ) against Harman and certain of our officers in the United States District Court for the District of Columbia (the Court ) seeking compensatory damages and costs on behalf of all persons who purchased our common stock between April 26, 2007 and September 24, 2007 (the Class Period ). The original complaint alleged claims for violations of Sections 10(b) and 20(a) of the Securities Exchange Act of 1934, as amended (the Exchange Act ) and Rule 10b-5 promulgated thereunder.

The complaint alleged that the defendants omitted to disclose material adverse facts about Harman's financial condition and business prospects. The complaint contended that had these facts not been concealed at the time the merger agreement with Kohlberg, Kravis, Roberts & Co. and Goldman Sachs Capital Partners was entered into, there would not have been a merger agreement, or it would have been at a much lower price, and the price of our common stock therefore would not have been artificially inflated during the Class Period. The Kim Plaintiff alleged that, following the reports that the proposed merger was not going to be completed, the price of our common stock declined, causing the plaintiff class significant losses.

On November 30, 2007, the Boca Raton General Employees Pension Plan filed a purported class action lawsuit against Harman and certain of our officers in the Court seeking compensatory damages and costs on behalf of all persons who purchased our common stock between April 26, 2007 and September 24, 2007. The allegations in the Boca Raton complaint are essentially identical to the allegations in the original Kim complaint, and like the original Kim complaint, the Boca Raton complaint alleges claims for violations of Sections 10(b) and 20(a) of the Exchange Act and Rule 10b-5 promulgated thereunder.

On January 16, 2008, the Kim Plaintiff filed an amended complaint. The amended complaint, which extended the Class Period through January 11, 2008, contended that, in addition to the violations alleged in the original complaint, Harman also violated Sections 10(b) and 20(a) of the Exchange Act and Rule 10b-5 promulgated thereunder by knowingly failing to disclose significant problems relating to its PND sales forecasts, production, pricing, and inventory prior to January 14, 2008. The amended complaint claimed that when Defendants revealed for the first time on January 14, 2008 that shifts in PND sales would adversely impact earnings per share by more than \$1.00 per share in fiscal 2008, that led to a further decline in our share value and additional losses to the plaintiff class.

On February 15, 2008, the Court ordered the consolidation of the Kim action with the Boca Raton action, the administrative closing of the Boca Raton action, and designated the short caption of the consolidated action as In re Harman International Industries, Inc. Securities Litigation, civil action no. 1:07-cv-01757 (RWR). That same day, the Court appointed the Arkansas Public Retirement System as lead plaintiff ( Lead Plaintiff ) and approved the law firm Cohen, Milstein, Hausfeld and Toll, P.L.L.C. to serve as lead counsel.

On March 24, 2008, the Court ordered, for pretrial management purposes only, the consolidation of Patrick Russell v. Harman International Industries, Incorporated, et al. with In re Harman International Industries, Inc. Securities Litigation.



On May 2, 2008, Lead Plaintiff filed a consolidated class action complaint (the Consolidated Complaint ). The Consolidated Complaint, which extended the Class Period through February 5, 2008, contended that Harman and certain of our officers and directors violated Sections 10(b) and 20(a) of the Exchange Act and Rule 10b-5 promulgated thereunder, by issuing false and misleading disclosures regarding our financial condition in fiscal year 2007 and fiscal year 2008. In particular, the Consolidated Complaint alleged that defendants knowingly or recklessly failed to disclose material adverse facts about MyGIG radios, personal navigation devices and our capital expenditures. The Consolidated Complaint alleged that when Harman's true financial condition became known to the market, the price of our common stock declined significantly, causing losses to the plaintiff class.

On July 3, 2008, defendants moved to dismiss the Consolidated Complaint in its entirety. Lead Plaintiff opposed the defendants' motion to dismiss on September 2, 2008, and defendants filed a reply in further support of their motion to dismiss on October 2, 2008.

On April 12, 2012, In re Harman International Industries, Inc. Securities Litigation, civil action no. 1:07-cv-01757 (D.D.C.) was reassigned to Judge Rudolph Contreras while Patrick Russell v. Harman International Industries, Incorporated, et al. remained before Judge Richard W. Roberts.

## **Table of Contents**

On September 5, 2012, the Court heard oral arguments on defendants' motion to dismiss. At the request of the Court, on September 24, 2012, each side submitted a supplemental briefing on defendants' motion to dismiss. On January 17, 2014, the Court granted a motion to dismiss, without prejudice, the *In re Harman International Industries, Inc. Securities Litigation*. The Lead Plaintiff has filed a notice of appeal and the matter has been fully briefed but no hearing has yet been set.

### ***Patrick Russell v. Harman International Industries, Incorporated, et al.***

Patrick Russell (the Russell Plaintiff) filed a complaint on December 7, 2007 in the United States District Court for the District of Columbia and an amended purported putative class action complaint on June 2, 2008 against Harman and certain of our officers and directors alleging violations of ERISA and seeking, on behalf of all participants in and beneficiaries of the Savings Plan, compensatory damages for losses to the Savings Plan as well as injunctive relief, imposition of a constructive trust, restitution, and other monetary relief. The amended complaint alleged that from April 26, 2007 to the present defendants failed to prudently and loyally manage the Savings Plan's assets, thereby breaching their fiduciary duties in violation of ERISA by causing the Savings Plan to invest in our common stock notwithstanding that the stock allegedly was no longer a prudent investment for the Participants' retirement savings. The amended complaint further claimed that, during the Class Period, defendants failed to monitor the Savings Plan's fiduciaries, failed to provide the Savings Plan's fiduciaries with, and to disclose to the Savings Plan's participants, adverse facts regarding Harman and our businesses and prospects. The Russell Plaintiff also contended that defendants breached their duties to avoid conflicts of interest and to serve the interests of participants in and beneficiaries of the Savings Plan with undivided loyalty. As a result of these alleged fiduciary breaches, the amended complaint asserted that the Savings Plan had suffered substantial losses, resulting in the depletion of millions of dollars of the retirement savings and anticipated retirement income of the Savings Plan's Participants.

On March 24, 2008, the Court ordered, for pretrial management purposes only, the consolidation of *Patrick Russell v. Harman International Industries, Incorporated, et al.* with *In re Harman International Industries, Inc. Securities Litigation*. Defendants moved to dismiss the complaint in its entirety on August 5, 2008. The Russell Plaintiff opposed the defendants' motion to dismiss on September 19, 2008, and defendants filed a reply in further support of their motion to dismiss on October 20, 2008. On May 22, 2013, the District Court dismissed the complaint in its entirety. The Russell Plaintiff filed a notice of appeal and oral arguments on the briefs submitted by the parties were heard on September 30, 2014, but no decision has yet been rendered by the Court.

### ***Infotainment Supply Arrangements***

We have arrangements with our infotainment customers to provide products that meet predetermined technical specifications and delivery dates. In the event that we do not satisfy the performance obligations under these arrangements, we may be required to indemnify the customer. We accrue for any loss that we expect to incur under these arrangements when that loss is probable and can be reasonably estimated. For the three months ended September 30, 2014 and 2013, we incurred \$4.9 million of costs relating to delayed delivery of product to an infotainment customer and \$6.1 million of gains relating to losses that we no longer expect to incur, respectively. An inability to meet performance obligations on infotainment platforms to be delivered in future periods could adversely affect our results of operations, cash flows and financial condition in future periods.

### ***Customs NAFTA Preferential Tariff Treatment***

We have submitted a prior disclosure (Prior Disclosure) related to our compliance with U.S. Customs regulations for our fiscal years 2008 through 2012. As we implement our corrective actions, we have submitted the updates to the Prior Disclosure quantifying our compliance through December 31, 2013. This Prior Disclosure and the related

updates address several areas of review including our compliance with (a) the North American Free Trade Agreement ( NAFTA ), (b) classification, (c) quantity, and (d) valuation, as defined by U.S. Customs.

We regularly import goods that qualify for preferential duty claims pursuant to NAFTA. NAFTA requires that an importer have a valid NAFTA Certificate of Origin in its possession at the time it makes a preferential duty claim. Our evaluation of our compliance with the NAFTA area of review has preliminarily determined that a number of preferential duty claims were made without first obtaining the required NAFTA certificate. U.S. Customs regulations, however, permit discretion to waive this requirement if the imported goods qualify for NAFTA preferential tariff treatment. We were advised in the fourth quarter of fiscal year 2013 that U.S. Customs has changed its internal practice and now intends to restrict the exercise of this discretion in this area. We believe that we will ultimately be able to demonstrate that a substantial amount of the goods imported qualified for NAFTA preferential tariff treatment. We intend to vigorously pursue a waiver of the NAFTA certificate requirement to minimize the duty and interest paid related to these claims, however, there is no assurance that we will prevail in obtaining this waiver.

In June 2014, we submitted our final Prior Disclosure supplement and we are now waiting for U.S. Customs regulations to accept our final Prior Disclosure. As of September 30, 2014 and June 30, 2014, we have estimated that our potential liability including interest

---

**Table of Contents**

related to this Prior Disclosure and the related updates is approximately \$18 million, which has been accrued for in our Condensed Consolidated Balance Sheets. Approximately \$12 million of payments were remitted during the fiscal year ended June 30, 2014. No further payments have been made in the three months ended September 30, 2014.

**Note 21 Related Party Transactions**

In December 2009, we entered into a three-year agreement for engineering and software development services with Neusoft Corporation ( Neusoft ), a Shanghai exchange listed technology solutions provider. A member of our Board of Directors is the Chairman and CEO of Neusoft. On April 20, 2010, our subsidiary, IS entered into an asset purchase and business transfer agreement (the Asset Purchase Agreement ) with Neusoft Technology Solutions GmbH ( Neusoft Technology ), a subsidiary of Neusoft, for the sale of certain tangible assets located at IS 's facility in Hamburg, Germany. This transaction closed on June 1, 2010. As part of the Asset Purchase Agreement, IS and Neusoft Technology entered into a five-year agreement for engineering and software development services related to IS 's vehicle navigation business (the Services Agreement ). Under the terms of the Asset Purchase Agreement, IS transferred at closing certain tangible assets and employment relationships to Neusoft Technology and received consideration of 6.0 million. Our indirect wholly-owned subsidiary, Harman Becker Automotive Systems GmbH ( HBAS ) and Neusoft Europe AG, a subsidiary of Neusoft, are guarantors under the terms of the Asset Purchase Agreement and the Services Agreement.

In the first quarter of fiscal year 2013, we entered into a contract with Neusoft to develop certain software to be integrated into certain infotainment platforms for a customer. In the third quarter of fiscal year 2013, we entered into a separate contract with Neusoft to develop digital map databases. As of June 30, 2014, we have paid Neusoft approximately \$11.9 million for this capitalized software asset which will be amortized over approximately four years, which is the future revenue stream of the products to which it relates.

During the three months ended September 30, 2014 and 2013, we incurred total expenses of \$6.8 million and \$7.7 million, respectively, for engineering and software development services with Neusoft Technology and Neusoft. During the three months ended September 30, 2014 and 2013, we paid Neusoft and Neusoft Technology approximately \$8.0 million and \$9.9 million, respectively.

In May 2013, we entered into a joint-venture agreement with Neusoft to establish the Harman Neusoft Automotive Infotech (Dalian) Co. Ltd. (the Harman Neusoft JV ). The purpose of the Harman Neusoft JV is to develop, manufacture, distribute and sell car aftermarket products including, without limitation, car aftermarket audio speakers, amplifiers and head units with or without navigation and telematics features and to provide relevant technical support and services.

The total investment amount of the Harman Neusoft JV is \$10.0 million and the registered capital is \$7.0 million. We will contribute 60 percent and Neusoft will contribute 40 percent of the registered capital. The Harman Neusoft JV was officially approved by the Chinese government in December 2013. We are still in the process of setting up the Harman Neusoft JV 's infrastructure. We and Neusoft began funding our respective share of the registered capital in the fourth quarter of fiscal year 2014. The total amount funded was 20 percent of the registered capital or \$1.4 million, with our contribution of \$0.8 million or 60 percent and Neusoft 's contribution of \$0.6 million or 40 percent. The operating results of the Harman Neusoft JV are included in our consolidated financial statements as a non-controlling interest. The portion of the Harman Neusoft JV that we do not own is eliminated from our consolidated operating results on the line Net income attributable to noncontrolling interest in our Condensed Consolidated Statements of Income. The Noncontrolling interest is reported in our Condensed Consolidated Balance Sheets within equity, stated separately from Harman 's equity.



**Table of Contents****Note 22 Transfer of Ownership of Manufacturing Facility**

On April 10, 2013 (the Schaidt Agreement Date), HBAS, an indirect wholly-owned subsidiary of Harman, entered into an agreement to transfer the ownership of an automotive manufacturing plant in Germany to a third party, Schaidt KG. Schaidt KG will manufacture and supply products for HBAS based on HBAS's orders. As consideration for the assumption by Schaidt KG of certain of HBAS's obligations, HBAS has agreed to pay Schaidt KG 41.1 million, or approximately \$53.5 million, plus a bonus of 4.0 million, or approximately \$5.2 million, if Schaidt KG meets certain supply obligations, as defined in the agreement. We have determined that the transfer of the manufacturing plant assets cannot be accounted for as a sale since Schaidt KG does not have adequate initial or ongoing investment in the manufacturing plant, and because we will maintain a level of continued involvement such that the risks of ownership have not transferred.

During the three months ended September 30, 2014 and 2013, no further payments were made nor expense recognized related to our payment obligations that have been made or which are deemed probable of being made to Schaidt KG to indemnify them for their assumption of certain of our obligations. Approximately 16.7 million, or approximately \$23.0 million, of accrued indemnification payments are expected to be paid over the next year and are accrued for in Accrued liabilities in our Condensed Consolidated Balance Sheet at September 30, 2014. We have revised our estimated useful life of the transferred manufacturing assets to accelerate the depreciation over the expected term of the manufacturing arrangement. Approximately \$1.4 million of accelerated depreciation was recorded in each of the three month periods ended September 30, 2014 and 2013. As a result, the manufacturing plant assets will be included in our consolidated financial statements from the Schaidt Agreement Date forward unless future circumstances warrant a change.

**Note 23 Acquisitions****AMX LLC**

On June 13, 2014, (the AMX Acquisition Date), we acquired all of the outstanding shares of AMX, a provider of enterprise automation and control and audio/video switching and distribution solutions, for a total purchase price of \$365.0 million (the AMX Acquisition), subject to both a net debt and working capital adjustment (the AMX Adjustments). We are in the process of finalizing the AMX Adjustments. There is an indemnification holdback of \$25.0 million and a working capital holdback of \$2.0 million (the Holdback Amounts) which are payable contingent on the outcome of certain events over the next 36 months. On the AMX Acquisition Date, based on the estimated closing balance sheet, we paid \$372.9 million which included \$27.0 million placed in escrow for the Holdback Amounts and \$7.9 million related to the AMX Adjustments.

The total cost of the AMX Acquisition was allocated on a preliminary basis, subject to final allocation, to the assets acquired and liabilities assumed based on their fair values at the AMX Acquisition Date, as follows:

|                           | <b>June 13, 2014</b> |
|---------------------------|----------------------|
| Cash and cash equivalents | \$ 4,351             |
| Accounts receivable, net  | 27,203               |
| Inventories, net          | 29,100               |
| Other current assets      | 4,877                |
| <b>Current assets</b>     | <b>65,531</b>        |

|                                    |         |
|------------------------------------|---------|
| Property, plant and equipment, net | 28,189  |
| Goodwill                           | 241,122 |
| Intangibles                        | 101,030 |
| Other assets                       | 4,275   |
| <br>                               |         |
| Total assets                       | 440,147 |
| <br>                               |         |
| Accounts payable                   | 11,834  |
| Accrued liabilities                | 9,698   |
| <br>                               |         |
| Total current liabilities          | 21,532  |
| Other non-current liabilities      | 45,674  |
| <br>                               |         |
| Total liabilities                  | 67,206  |
| <br>                               |         |
| Net assets                         | 372,941 |

Based on our preliminary valuation, goodwill and intangibles were recorded in connection with the AMX Acquisition based on third-party valuations and management's estimates for those acquired intangible assets. The valuation of the acquired net assets is subject to

## **Table of Contents**

change as we obtain additional information for our estimates during the measurement period. The primary areas of those purchase price allocations that are not yet finalized relate to identifiable intangible assets and residual goodwill. Goodwill was calculated as the excess of the consideration transferred over the net assets recognized and represents the future economic benefits arising from other assets acquired that could not be individually identified and separately recognized. Of the \$241.1 million of goodwill recognized, none is deductible for tax purposes. Intangible assets include a non-amortized indefinite useful life trade name of \$55.7 million, customer relationships of \$26.7 million with an approximate useful life of two to nine years, technology of \$17.0 million with an approximate useful life of five years, backlog of \$1.5 million with an approximate useful life of two months, and a covenant not-to-compete of \$0.1 million with an approximate useful life of three years. We also recorded adjustments of \$4.2 million to Inventories and \$2.7 million to Property, plant and equipment, net in our Condensed Consolidated Balance Sheet to adjust the opening balances to fair value. The adjustment to Inventories will be amortized over its estimated useful life of four months through Cost of sales in our Condensed Consolidated Statement of Income. The adjustment to Property, plant and equipment, net will be amortized over its estimated useful life of five to 35 years through depreciation expense within Cost of sales or SG&A in our Condensed Consolidated Statement of Income.

### **Note 24 Subsequent Events**

#### **Dividend Declaration**

On October 30, 2014 we declared a cash dividend of \$0.33 per share for the quarter ended September 30, 2014. The quarterly dividend will be paid on November 24, 2014 to each stockholder of record as of the close of business on November 10, 2014.

#### **Closure of Facility in France**

In October 2014, the Workers Council in France approved our plan to close the facility in Chateau du Loir, France. The closure will result in the termination of approximately 200 employees and we are expecting to reflect a charge of approximately \$25 million to \$30 million within restructuring expenses within the three months ended December 31, 2014.

#### **Approval of Share Buyback Program**

On October 28, 2014, our Board of Directors authorized the repurchase of up to \$500 million of our common stock over the next three years (the 2014 Buyback Program ). The 2014 Buyback Program allows us to purchase shares of our common stock in accordance with applicable securities laws on the open market or through privately negotiated transactions during the authorized three year period. The 2014 Buyback Program may be suspended or discontinued at any time. We will determine the timing and the amount of any repurchases based on an evaluation of market conditions, share price and other factors.



## **Table of Contents**

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

#### ***General***

*The following discussion should be read in conjunction with the accompanying unaudited Condensed Consolidated Financial Statements and the related notes included in Item 1 of this Quarterly Report on Form 10-Q, and Management's Discussion and Analysis of Financial Condition and Results of Operations included in our Annual Report on Form 10-K, for the fiscal year ended June 30, 2014 (our 2014 Annual Report). This discussion contains forward-looking statements which are based on our current expectations and experience and our perception of historical trends, current market conditions, including customer acceptance of our new products, current economic data, expected future developments, foreign currency exchange rates, and other factors that we believe are appropriate under the circumstances. These statements involve risks and uncertainties that could cause actual results to differ materially from those suggested in the forward-looking statements. Unless otherwise indicated, Harman, Company, we, our, and us are used interchangeably to refer to Harman International Industries, Incorporated and its consolidated subsidiaries. All amounts are in thousands unless otherwise indicated.*

#### ***Executive Overview***

We believe we are a worldwide leader in the development, manufacture and marketing of a wide range of audio and electronics for consumer and professional applications, lighting systems, video and control solutions and information delivery systems, as well as digitally integrated audio and infotainment systems for the automotive industry. We have developed a broad range of product offerings which we sell in our principal markets under our renowned brand names, including Aha<sup>®</sup>, AKG<sup>®</sup>, AMX<sup>®</sup>, Becker<sup>®</sup>, BSS<sup>®</sup>, Crown<sup>®</sup>, dbx<sup>®</sup>, DigiTech<sup>®</sup>, Harman/Kardon<sup>®</sup>, Infinity<sup>®</sup>, JBL<sup>®</sup>, JBL Professional, Lexicon<sup>®</sup>, Logic 7<sup>®</sup>, Mark Levinson<sup>®</sup>, Martin<sup>®</sup>, Revel<sup>®</sup>, Selenium<sup>®</sup>, Soundcraft<sup>®</sup>, Studer<sup>®</sup> and yurbuds<sup>®</sup> Powered by JBL. We have built these brands by developing our engineering, manufacturing and marketing competencies, and have employed these resources to establish our Company as a leader in the markets we serve.

We report our business on the basis of four segments. Our Infotainment, Lifestyle and Professional segments are based on our strategic approach to the markets and customers we serve. Our fourth segment, Other, primarily includes compensation, benefit and occupancy costs for corporate employees, net of allocations and expenses associated with new technology innovation and our corporate brand identity campaign.

We believe that innovation is an important element to gaining market acceptance of our products and strengthening our market position. We have a history of leveraging our continuous technological innovation across all of the markets we serve. We have a well-deserved reputation for delivering premium audio and infotainment solutions across a full spectrum of applications. We believe that our technological innovation, the quality of our products and our reputation for on-time delivery have resulted in Harman being awarded a substantial amount of Infotainment and Lifestyle business. As of June 30, 2014, we have a cumulative estimated \$20.5 billion of future awarded Infotainment and Lifestyle automotive business, which represents the estimated future lifetime net sales for all customers. This amount does not represent firm customer orders. We report our awarded business primarily based on award letters from our customers. To validate these awards, we use various assumptions, which we update annually, including global vehicle production forecasts, customer take rates for our products, revisions to product life cycle estimates and the impact of annual price reductions and exchange rates, among other factors. These assumptions are updated and reported externally on an annual basis. We update our estimated awarded business quarterly by adding the value of new awards received and subtracting sales recorded during the quarter. These quarterly updates do not include any assumptions for increased take rates, revisions to product life cycle, or any other factors. We believe our currently awarded automotive business will position us well for follow-on and new business with these existing customers.

Our management uses the amount of our future awarded business for short- and long-term budgeting and forecasting, development of earnings guidance and for planning future corporate investment and other activities, such as capital expenditures and restructuring. Our future awarded business is also an input used to approximate our enterprise value. We believe our investors utilize this information for a number of reasons, including evaluating our future financial performance over time, to model our financial results of operations, to understand the risks inherent in our current operating plan, and as an input to approximate our enterprise value. However, our estimates of future awarded automotive business are forward-looking statements and may not actually be achieved. See the risk factor "We may not realize sales represented by awarded business" in Item 1A "Risk Factors" of Part I of our 2014 Annual Report.

Our products are sold worldwide, with the largest markets located in the United States and Germany. In the United States, our primary manufacturing facilities are located in Kentucky, Indiana and Washington. Outside of the United States, we have manufacturing facilities in Austria, Brazil, China, Denmark, Hungary, France, Germany, Mexico, the Netherlands and the United Kingdom.

## **Table of Contents**

Our sales and earnings may vary due to the production schedules and model year changeovers of our automotive customers, the holiday buying season for home audio products, customer acceptance of our products, the timing of new product introductions, product offerings by our competitors, fluctuations in the timing of contractual agreements for customer reimbursements for research, development and engineering expenses ( RD&E ) and general economic conditions. Since most of our businesses operate using local currencies, our reported sales and earnings may also fluctuate due to fluctuations in foreign currency exchange rates, especially with respect to the value of the Euro and the U.S. Dollar.

We believe significant opportunities exist to grow our business in all three of our business segments in emerging markets such as Brazil, Russia, India and China ( BRIC ). During the three months ended September 30, 2014, sales increased \$38.0 million in these emerging markets to \$214.3 million, an increase of 21.6 percent over the same period in the prior fiscal year.

We continue to roll out our global marketing campaign featuring some of the world's most prominent artists and celebrities such as Maroon 5, Linkin Park, Mariano Rivera and Tim McGraw, in order to increase brand awareness and support growth and market share gains across our entire business.

### ***Critical Accounting Policies***

#### ***Recently Adopted Accounting Standards***

For the three months ended September 30, 2014, there were no significant changes to our critical accounting policies and estimates from those disclosed in the consolidated financial statements and the related notes included in our 2014 Annual Report, except for recently adopted accounting standards disclosed in Note 2 *New Accounting Standards* in the Notes to the Condensed Consolidated Financial Statements for the three months ended September 30, 2014.

#### ***Recently Issued Accounting Standards***

Refer to Note 2 *New Accounting Standards* in the Notes to the Condensed Consolidated Financial Statements for a summary of recently issued accounting standards.

### ***Results of Operations***

#### ***Net Sales***

Net sales for the three months ended September 30, 2014 were \$1.429 billion compared to \$1.172 billion in the same period in the prior year, an increase of 21.9 percent, or 22.0 percent excluding foreign currency translation. Net sales increased in all of our segments. The increase was primarily due to the expansion of recently launched platforms, stronger automotive production and higher take rates, new product introductions and the expansion of global distribution channels in the home and multimedia business, the expansion of our product portfolio into video switching and enterprise automation through the acquisition of AMX LLC and AMX Holding Corporation (collectively AMX ) and the acquisition of substantially all of the assets of Verto Medical Systems LLC d/b/a yurbuds and its wholly-owned subsidiary ( yurbuds ), partially offset by unfavorable foreign currency translation of \$0.7 million.

A summary of our net sales by business segment is presented below:

|              | <b>Three Months Ended September 30,</b> |            |                  |          |
|--------------|---|------------|------------------|----------|
|              | <b>2014</b>                             | <b>%</b>   | <b>2013</b>      | <b>%</b> |
| Net sales:   |   |            |                  |          |
| Infotainment | \$ 748,097                              | 52.4%      | \$ 639,753       | 54.6%    |
| Lifestyle    | 426,144                                 | 29.8%      | 334,488          | 28.5%    |
| Professional | 254,437                                 | 17.8%      | 197,431          | 16.9%    |
| Other        | 244                                     | 0%         | 133              | 0%       |
| <br>Total    | <br>\$ 1,428,922                        | <br>100.0% | <br>\$ 1,171,805 | <br>100% |

**Table of Contents**

*Infotainment* Net sales for the three months ended September 30, 2014 increased \$108.3 million, or 16.9 percent, compared to the same period in the prior year, or 17.0 percent excluding foreign currency translation. The increase in net sales was driven by the expansion of recently launched platforms, stronger automotive production and higher take rates, partially offset by unfavorable foreign currency translation of \$0.6 million.

*Lifestyle* Net sales for the three months ended September 30, 2014 increased \$91.7 million, or 27.4 percent, compared to the same period in the prior year, or 27.6 percent excluding foreign currency translation. The increase in net sales was driven by accelerated sales of new product introductions and the expansion of global distribution channels in the home and multimedia business, higher automotive audio sales as a result of the expansion of recently launched programs, stronger automotive production and higher take rates and the acquisition of yurbuds, partially offset by unfavorable foreign currency translation of \$0.5 million.

*Professional* Net sales for the three months ended September 30, 2014 increased \$57.0 million, or 28.9 percent, compared to the same period in the prior year, or 28.6 percent excluding foreign currency translation. The increase in net sales was driven by the expansion of our product portfolio into video switching and enterprise automation through the acquisition of AMX and favorable foreign currency translation of \$0.4 million.

*Gross Profit*

Gross profit as a percentage of net sales increased 1.6 percentage points to 29.0 percent for the three months ended September 30, 2014 compared to 27.4 percent in the same period in the prior year. The increase in overall gross profit as a percentage of net sales was driven by our Infotainment and Professional segments. In our Infotainment segment, our gross profit as a percentage of net sales increased due to improved leverage of fixed costs over a higher net sales base and lower costs due to productivity initiatives. In our Professional segment, our gross profit as a percentage of net sales increased due to higher margins due to the acquisition of AMX. Our gross profit as a percentage of net sales decreased in our Lifestyle segment due to integration costs associated with our yurbuds acquisition which occurred in June 2014.

A summary of our gross profit by business segment is presented below:

|                      | <b>Three Months Ended September 30,</b> |                                    |                   |                                    |
|----------------------|---|------------------------------------|-------------------|------------------------------------|
|                      | <b>2014</b>                             | <b>Percentage<br/>of Net Sales</b> | <b>2013</b>       | <b>Percentage<br/>of Net Sales</b> |
| <b>Gross profit:</b> |   |                                    |                   |                                    |
| Infotainment         | \$ 176,393                              | 23.6%                              | \$ 141,342        | 22.1%                              |
| Lifestyle            | 134,620                                 | 31.6%                              | 106,880           | 32.0%                              |
| Professional         | 103,468                                 | 40.7%                              | 73,311            | 37.1%                              |
| Other                | 151                                     | *                                  | 116               | *                                  |
| <b>Total</b>         | <b>\$ 414,632</b>                       | <b>29.0%</b>                       | <b>\$ 321,649</b> | <b>27.4%</b>                       |

\* Percent not meaningful.

*Infotainment* Gross profit as a percentage of net sales increased 1.5 percentage points to 23.6 percent for the three months ended September 30, 2014 compared to the same period in the prior year. The increase in gross profit as a

percentage of net sales was primarily due to improved leverage of fixed costs over a higher net sales base and lower costs due to productivity initiatives.

*Lifestyle* Gross profit as a percentage of net sales decreased 0.4 percentage points to 31.6 percent for the three months ended September 30, 2014 compared to the same period in the prior year. The decrease in gross profit as a percentage of net sales was due to yurbuds integration costs, partially offset by lower costs due to productivity initiatives.

*Professional* Gross profit as a percentage of net sales increased 3.6 percentage points to 40.7 percent for the three months ended September 30, 2014 compared to the same period in the prior year. The increase in gross profit as a percentage of net sales was primarily due to higher margins due to the acquisition of AMX and lower manufacturing expenses resulting from cost saving initiatives.

*Selling, General and Administrative Expenses*

Selling, general and administrative expenses ( SG&A ) were \$298.8 million for the three months ended September 30, 2014 compared to \$252.3 million in the same period in the prior year, an increase of \$46.6 million. As a percentage of net sales, SG&A decreased 0.6 percentage points in the three months ended September 30, 2014 compared to the same period in the prior year. The increase in SG&A was primarily in support of increased net sales, the inclusion of AMX, higher costs associated with estimated

**Table of Contents**

indemnifications related to infotainment supply arrangements, higher RD&E and higher marketing expenses, partially offset by lower restructuring expenses. RD&E increased \$17.3 million to \$90.9 million, or 6.4 percent of net sales in the three months ended September 30, 2014, compared to \$73.6 million, or 6.3 percent of net sales in the same period in the prior year primarily due to the acquisition of AMX, higher gross spending to support new product introductions and lower customer reimbursements.

A summary of SG&A by business segment is presented below:

|                  | <b>Three Months Ended September 30,</b> |                                    |                   |                                    |
|------------------|---|------------------------------------|-------------------|------------------------------------|
|                  | <b>2014</b>                             | <b>Percentage<br/>of Net Sales</b> | <b>2013</b>       | <b>Percentage<br/>of Net Sales</b> |
| <b>SG&amp;A:</b> |   |                                    |                   |                                    |
| Infotainment     | \$ 99,041                               | 13.2%                              | \$ 108,915        | 17.0%                              |
| Lifestyle        | 84,652                                  | 19.9%                              | 65,641            | 19.6%                              |
| Professional     | 80,203                                  | 31.5%                              | 46,830            | 23.7%                              |
| Other            | 34,950                                  | *                                  | 30,881            | *                                  |
| <b>Total</b>     | <b>\$ 298,846</b>                       | <b>20.9%</b>                       | <b>\$ 252,267</b> | <b>21.5%</b>                       |

\* Percent not meaningful.

*Infotainment* SG&A decreased \$9.9 million to \$99.0 million for the three months ended September 30, 2014 compared to the same period in the prior year. The decrease in SG&A was primarily due to lower restructuring expenses and improved operating leverage on higher sales, partially offset by higher costs associated with estimated indemnifications related to infotainment supply arrangements and higher RD&E. As a percentage of net sales, SG&A decreased 3.8 percentage points to 13.2 percent for the three months ended September 30, 2014 compared to the same period in the prior year. RD&E increased \$4.2 million to \$52.9 million, or 7.1 percent of net sales in the three months ended September 30, 2014, compared to \$48.7 million, or 7.6 percent of net sales in the same period in the prior year primarily due to lower customer reimbursements and higher gross spending to support new product introductions.

*Lifestyle* SG&A increased \$19.0 million to \$84.7 million for the three months ended September 30, 2014, compared to the same period in the prior year. The increase in SG&A was primarily in support of increased net sales and higher marketing costs related to our brand-awareness campaign. As a percentage of net sales, SG&A increased 0.3 percentage points to 19.9 percent for the three months ended September 30, 2014 compared to the same period in the prior year. RD&E increased \$3.5 million to \$17.9 million, or 4.2 percent of net sales in the three months ended September 30, 2014 compared to \$14.4 million, or 4.3 percent of net sales in the same period in the prior year due to higher gross spending to support new product introductions.

*Professional* SG&A increased \$33.4 million to \$80.2 million for the three months ended September 30, 2014, compared to the same period in the prior year. The increase in SG&A was primarily due to the acquisition of AMX. As a percentage of net sales, SG&A increased 7.8 percentage points to 31.5 percent for the three months ended September 30, 2014 compared to the same period in the prior year. RD&E increased \$9.1 million to \$17.1 million, or 6.7 percent of net sales in the three months ended September 30, 2014 compared to \$8.0 million, or 4.1 percent of net sales in the same period in the prior year primarily due to the acquisition of AMX.

*Other* Other SG&A includes compensation, benefit and occupancy costs for corporate employees, new technology innovation and expenses associated with our corporate brand identity campaign. Other SG&A increased \$4.1 million to \$35.0 million in the three months ended September 30, 2014 compared to the same period in the prior year primarily due to increased investments in marketing and RD&E.

*Restructuring*

Our restructuring program that is designed to improve our global footprint, cost structure, technology portfolio, human resources and internal processes continues. For the three months ended September 30, 2014 and 2013, we continued to refine existing programs and launched significant new programs focused on achieving further productivity improvements to: (i) optimize certain research and development, supply chain and administrative functions; (ii) outsource certain manufacturing capabilities; (iii) divest or sublease facilities no longer needed to support current operations and (iv) relocate certain functions to best cost countries.



**Table of Contents**

A summary and components of our restructuring initiatives are presented below and include accruals for new programs as well as revisions to estimates, both increases and decreases, to programs accrued in prior periods:

|                                 | <b>Severance<br/>Related<br/>Costs</b> | <b>Third Party<br/>Contractor<br/>Termination Costs</b> | <b>Facility Closure<br/>and Other<br/>Related<br/>Costs</b> | <b>Asset<br/>Impairments<sup>(1)</sup></b> | <b>Total</b> |
|---------------------------------|--|---|---|--|--------------|
| Liability, June 30, 2014        | \$ 54,157                              | \$ 0  | \$ 30,262   | \$ 0                                       | \$ 84,419    |
| Expense <sup>(2)</sup>          | 5,093                                  | 0   | 439   | 1,394                                      | 6,926        |
| Accumulated depreciation offset | 0                                      | 0   | 0   | (1,394)                                    | (1,394)      |
| Payments                        | (3,834)                                | (0)   | (1,010)   | 0  | (4,844)      |
| Foreign currency translation    | (3,879)                                | 0   | (1,772)   | 0  | (5,651)      |
| Liability, September 30, 2014   | \$ 51,537                              | \$ 0  | \$ 27,919   | \$ 0                                       | \$ 79,456    |
| Liability, June 30, 2013        | \$ 23,563                              | \$ 1,014  | \$ 33,848   | \$ 0                                       | \$ 58,425    |
| Expense <sup>(2)</sup>          | 20,694                                 | 12  | 1,309   | 2,020                                      | 24,035       |
| Accumulated depreciation offset | 0                                      | 0   | 0   | (2,020)                                    | (2,020)      |
| Payments                        | (9,990)                                | (61)  | (1,858)   | 0  | (11,909)     |
| Foreign currency translation    | 824                                    | 28  | 1,035   | 0  | 1,887        |
| Liability, September 30, 2013   | \$ 35,091                              | \$ 993  | \$ 34,334   | \$ 0                                       | \$ 70,418    |

(1) Credits related to restructuring charges for accelerated depreciation and inventory provisions are recorded against the related assets in Property, plant and equipment, net or Inventories in our Condensed Consolidated Balance Sheets and do not impact the restructuring liability.

(2) Restructuring expenses noted above are primarily in SG&A in our Condensed Consolidated Statements of Income. Asset impairments which consist of accelerated depreciation and inventory provisions are primarily in Cost of sales in our Condensed Consolidated Statements of Income.

Restructuring liabilities are recorded in Accrued liabilities and Other non-current liabilities in our Condensed Consolidated Balance Sheets.

Restructuring expenses by reporting business segment are presented below:

|              | <b>Three Months Ended<br/>September 30,</b> |             |
|--------------|---|-------------|
|              | <b>2014</b>                                 | <b>2013</b> |
| Infotainment | \$ (10)                                     | \$ 20,731   |
| Lifestyle    | 1,815                                       | 883         |
| Professional | 3,727                                       | 401         |
| Total        | 5,532                                       | 22,015      |

|                   |          |           |
|-------------------|----------|-----------|
| Asset impairments | 1,394    | 2,020     |
| Total             | \$ 6,926 | \$ 24,035 |

*Goodwill*

During the three months ended September 30, 2014, we reduced the goodwill in our Professional segment associated with our acquisition of AMX by \$2.9 million. During the three months ended September 30, 2013, we did not record any new additions to goodwill.

We did not recognize any goodwill impairment charges in our Condensed Consolidated Statements of Income in the three months ended September 30, 2014 and 2013.

The contingent purchase price associated with the acquisition of innovative Systems ( IS ) is calculated pursuant to the terms of an agreement between the parties. Certain terms of the agreement are currently subject to a dispute between the parties and the matter was submitted to arbitration. On November 5, 2013, the arbitration panel reached a partial judgment on some of the disputed matters covering the period from February 2009 through January 2012 awarding 16.3 million to the IS sellers. We contested the enforcement of the partial award. During the fiscal year ended June 30, 2014, we recorded approximately \$8.1 million of additional contingent purchase price in goodwill to accrue for this partial award. In July 2014, the partial award was upheld. Until such time as the other disputed matters are resolved, we cannot calculate the contingent purchase price related to these other disputed matters.

## **Table of Contents**

### *Operating Income*

Operating income for the three months ended September 30, 2014 was \$115.8 million, or 8.1 percent of net sales, compared to operating income of \$69.4 million, or 5.9 percent of net sales, in the same period in the prior year. The increase in operating income was primarily due to higher leverage of fixed costs based on higher sales volumes and lower restructuring expenses, partially offset by higher SG&A in support of increased net sales and the acquisition of AMX, higher RD&E and higher marketing costs related to our brand-awareness campaign.

### *Interest Expense, Net*

Interest expense is reported net of interest income in our Condensed Consolidated Statements of Income. Interest expense, net was \$2.7 million and \$2.0 million for the three months ended September 30, 2014 and 2013, respectively. Gross interest expense was \$3.1 million and \$2.4 million for the three months ended September 30, 2014 and 2013, respectively. The non-cash portion of gross interest expense was \$0.5 million for each of the three month periods ended September 30, 2014 and 2013, associated with the amortization of debt issuance costs on the Multi-Currency Credit Agreement entered into on October 10, 2012 (the Credit Agreement). The cash portion of gross interest expense was \$2.6 million and \$1.9 million in the three months ended September 30, 2014 and 2013, respectively, associated with interest on the Credit Agreement and our short-term borrowings. Interest income was \$0.4 million for each of the three month periods ended September 30, 2014 and 2013, associated with interest earned on our cash and cash equivalents.

### *Foreign Exchange Losses, Net*

Foreign currency exchange gains and losses resulting from the remeasurement of certain foreign currency denominated monetary assets and liabilities are included in Foreign exchange losses, net in our Condensed Consolidated Statements of Income.

### *Miscellaneous, Net*

Miscellaneous, net expenses of \$2.3 million primarily consisted of bank charges and interest expense related to a disputed claim for the three months ended September 30, 2014. Miscellaneous, net expenses of \$1.3 million primarily consisted of bank charges for the three months ended September 30, 2013.

### *Income Tax Expense, Net*

Our provision for income taxes is based on an estimated annual tax rate for the year applied to federal, state and foreign income. Income tax expense for the three months ended September 30, 2014 and 2013 was \$27.8 million and \$18.7 million, respectively. The effective tax rate for the three months ended September 30, 2014 and 2013 was 25.1 percent and 28.6 percent, respectively. The change in the effective tax rate for the three months ended September 30, 2014 compared to the same period in the prior year was primarily due to discrete tax charges booked in the prior period.

We have net deferred tax assets of \$210.9 million primarily consisting of deferred deductions, research and experimentation credits, and foreign tax credits. We have evaluated all available evidence, both positive and negative, and based on the weight of all available evidence we continue to believe that our net deferred tax assets are fairly reflected in our Condensed Consolidated Balance Sheets. If the results of our operations do not meet our current expectations, our net deferred tax assets may become impaired.

As of September 30, 2014 unrecognized tax benefits and the related interest were \$43.5 million and \$2.3 million, respectively, all of which would affect the tax rate if recognized. During the three months ended September 30, 2014, the change in tax reserves on uncertain tax positions and the related interest were \$(0.7) million and less than \$(0.1) million, respectively.

### ***Financial Condition***

#### *Liquidity and Capital Resources*

We primarily finance our working capital requirements through cash generated by operations, borrowings under the Credit Agreement and trade credit. Cash and cash equivalents were \$397.8 million at September 30, 2014 compared to \$581.3 million at June 30, 2014. During the three months ended September 30, 2014, our cash and cash equivalents balance decreased \$183.6 million. The decrease in cash was primarily due to \$100.0 million of repayments under our revolving credit facility, capital expenditures, dividends and repurchases of common stock related to share-based compensation arrangements, partially offset by net income and cash provided by operating activities. We also used cash to make investments in our manufacturing facilities, fund product development and meet the working capital needs of our business segments.

## **Table of Contents**

We believe that our existing cash and cash equivalents of \$397.8 million at September 30, 2014, together with our expected future operating cash flows, and our availability of \$545.4 million under the Credit Agreement, will be sufficient to cover our working capital needs, debt service, capital expenditures, including major investments related to manufacturing and research facilities in emerging markets, acquisitions, purchase commitments, restructuring projects and quarterly dividends for at least the next 12 months.

Our ability to maintain positive liquidity going forward depends on our ability to continue to generate cash from operations and maintain access to the financial markets, both of which are subject to general economic, financial, competitive, legislative, regulatory and other market factors beyond our control. We earn a significant amount of our operating income outside the U.S., the majority of which is deemed to be permanently reinvested in foreign jurisdictions. For at least the next 12 months, we have sufficient cash in the U.S., availability under our Credit Agreement and forecasted domestic cash flow to sustain our operating activities and cash commitments for investing and financing activities, such as quarterly dividends and repayment of debt. In addition, we expect existing foreign cash and cash equivalents and cash flows from operations to continue to be sufficient to fund our foreign operating activities and cash commitments for investing activities, such as material capital expenditures, for at least the next 12 months. As of September 30, 2014 Cash and cash equivalents of \$165.5 million were held in the U.S. and Cash and cash equivalents of \$232.3 million were held by us in foreign jurisdictions. As of June 30, 2014 Cash and cash equivalents of \$235.9 million were held in the U.S. and Cash and cash equivalents of \$345.4 million were held by us in foreign jurisdictions. Below is a more detailed discussion of our cash flow activities during the three months ended September 30, 2014 compared to the same period in the prior fiscal year.

### *Operating Activities*

For the three months ended September 30, 2014, our net cash provided by operations was \$13.7 million compared to \$113.0 million in the same period in the prior year. The decrease in operating cash flows compared to the same period in the prior year was primarily due to increases in inventories and other current assets and decreases in accrued other liabilities, partially offset by higher net income. At September 30, 2014, working capital, excluding cash and short-term debt, was \$546.2 million, compared with \$431.3 million at June 30, 2014. The increase was primarily due to higher inventory and other current assets balances, partially offset by higher accounts payable.

### *Investing Activities*

Net cash used in investing activities was \$30.4 million for the three months ended September 30, 2014, compared to \$18.1 million in the same period in the prior year. The increase in net cash used in investing activities compared to the same period in the prior year was primarily due to higher capital expenditures in the current year and lower maturities of short-term investments than in the same period in the prior year. Capital expenditures for the three months ended September 30, 2014 were \$35.0 million, in support of new Infotainment and Lifestyle awards, compared to \$28.2 million for the same period in the prior year. We expect that capital expenditures as a percentage of sales will remain in line with fiscal year 2014 levels.

### *Financing Activities*

Net cash used in financing activities was \$143.5 million in the three months ended September 30, 2014, compared to \$40.7 million used in financing activities in the same period in the prior year. The increase in cash used in financing activities was primarily due to higher repayments of debt under our revolving credit facility and higher repurchases of common stock related to share-based compensation arrangements, partially offset by lower repurchases of common stock under our share buyback program.

*Credit Agreement*

On October 10, 2012, we and our wholly-owned subsidiary Harman Holding GmbH & Co. KG ( Harman KG ), entered into the Credit Agreement with a group of banks. The Credit Agreement provides for (i) a five-year unsecured multi-currency revolving credit facility (the Revolving Credit Facility ) in the amount of \$750.0 million (the Aggregate Revolving Commitment ) with availability in currencies other than the United States Dollar of up to \$550.0 million and (ii) the Term Facility (collectively with the Revolving Credit Facility, the Facilities ) in the amount of \$300.0 million (the Aggregate Term Commitment and collectively with the Aggregate Revolving Commitment, the Aggregate Commitment ). Up to \$60.0 million of the Aggregate Revolving Commitment is available for letters of credit. Subject to certain conditions set forth in the Credit Agreement, the Aggregate Commitment may be increased by up to \$250.0 million. We may select interest rates for the Facilities equal to (i) LIBOR plus an applicable margin or (ii) a base rate plus an applicable margin, which in each case is determined based on our credit rating. We pay a facility fee on the Aggregate Revolving Commitment, whether drawn or undrawn, which is determined based on our credit rating. Any proceeds from borrowings under the Facilities may be used for general corporate purposes.

**Table of Contents**

At September 30, 2014, there was \$200.0 million of outstanding borrowings and approximately \$4.6 million of outstanding letters of credit under the Revolving Credit Facility and \$247.5 million of outstanding borrowings under the Term Facility, of which \$37.5 million is included in our Condensed Consolidated Balance Sheet as Current portion of long-term debt and \$210.0 million is classified as Long-term debt. At September 30, 2014, unused available credit under the Revolving Credit Facility was \$545.4 million.

At June 30, 2014, there was \$300.0 million of outstanding borrowings and approximately \$4.6 million of outstanding letters of credit under the Revolving Credit Facility and \$255.0 million of outstanding borrowings under the Term Facility, of which \$35.6 million is included in our Condensed Consolidated Balance Sheet as Current portion of long-term debt and \$219.4 million is classified as Long-term debt. At June 30, 2014, unused available credit under the Revolving Credit Facility was \$445.4 million.

At September 30, 2014, long-term debt maturing in each of the next five fiscal years and thereafter is as follows:

|              |                   |
|--------------|-------------------|
| 2015         | \$ 28,125         |
| 2016         | 43,155            |
| 2017         | 135,000           |
| 2018         | 241,250           |
| 2019         | 0                 |
| Thereafter   | 0                 |
| <b>Total</b> | <b>\$ 447,530</b> |

*Equity*

Total shareholders equity at September 30, 2014 was \$1.852 billion compared with \$1.793 billion at June 30, 2014. The increase is primarily due to higher net income and unrealized gains on hedging, partially offset by unfavorable foreign currency translation and dividends to shareholders.

*Off-Balance Sheet Arrangements*

We utilize off-balance sheet arrangements in our operations when we enter into operating leases for land, buildings and equipment in the normal course of business, which are not included in our Condensed Consolidated Balance Sheets. In addition, we had outstanding letters of credit of \$4.6 million at September 30, 2014 and June 30, 2014, that were not included in our Condensed Consolidated Balance Sheets.

*Business Outlook*

Our future outlook is largely dependent upon changes in global macro economic conditions, which are starting to show signs of a potential downturn in Europe and some developing markets. We believe that current consumer discretionary spending levels, foreign currency exchange rates, investments in capital expenditure projects, automotive production rates and projected increased take rates for our automotive products, will support our previously announced fiscal 2015 financial guidance. We remain committed to our investment plans in the areas of RD&E and marketing. We also remain committed to pursuing incremental productivity and restructuring programs, which are expected to provide an accelerated rate of earnings growth in future years. Capital expenditures as a percentage of sales are expected to remain in line with fiscal year 2014 levels.

***Subsequent Events***

***Dividend Declaration***

On October 30, 2014 we declared a cash dividend of \$0.33 per share for the quarter ended September 30, 2014. The quarterly dividend will be paid on November 24, 2014 to each stockholder of record as of the close of business on November 10, 2014.

***Closure of Facility in France***

In October 2014, the Workers' Council in France approved our plan to close the facility in Chateau du Loir, France. The closure will result in the termination of approximately 200 employees and we are expecting to reflect a charge of approximately \$25 million to \$30 million within restructuring expenses during the three months ended December 31, 2014.

***Approval of Share Buyback Program***

On October 28, 2014, our Board of Directors authorized the repurchase of up to \$500 million of our common stock over the next three years (the 2014 Buyback Program). The 2014 Buyback Program allows us to purchase shares of our common stock in accordance with applicable securities laws on the open market or through privately negotiated transactions during the authorized three year period. The 2014 Buyback Program may be suspended or discontinued at any time. We will determine the timing and the amount of any repurchases based on an evaluation of market conditions, share price and other factors.



**Table of Contents**

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

We are required to include information about potential effects of changes in interest rates and currency exchange rates in our periodic reports filed with the Securities and Exchange Commission. Since September 30, 2014, there have been no material changes in the quantitative or qualitative aspects of our market risk profile. See Item 7A, Quantitative and Qualitative Disclosure About Market Risk included in our 2014 Annual Report.

***Interest Rate Sensitivity/Risk***

At September 30, 2014, interest on 99 percent of our borrowings was determined on a variable rate basis. The interest rates on the balances of our debt, cash and cash equivalents and short-term investments are subject to changes in U.S. and European short-term interest rates. To assess exposure to interest rate changes, we have performed a sensitivity analysis assuming a hypothetical 100 basis point increase or decrease in interest rates across all outstanding debt and investments. Our analysis indicates that the effect on net income for the three months ended September 30, 2014 of such an increase or decrease in interest rates would be approximately \$0.3 million.

***Foreign Currency Risk***

We maintain significant operations in Germany, Hungary, China, the Netherlands, Denmark, France, Japan, Brazil, the United Kingdom, Austria and India. As a result, we are subject to market risks arising from changes in these foreign currency exchange rates, principally the change in the value of the Euro versus the U.S. Dollar. Refer to Note 13 *Derivatives* in the Notes to the Condensed Consolidated Financial Statements for additional discussion on our financial risk management.

Changes in currency exchange rates, principally the change in the value of the Euro compared to the U.S. dollar have an impact on our reported results when the financial statements of foreign subsidiaries are translated into U.S. dollars. Approximately 43 percent of our sales are denominated in Euros. The average exchange rate for the Euro versus the U.S. dollar for the three months ended September 30, 2014 decreased 0.1 percent from the same period in the prior fiscal year.

We presently estimate the effect on fiscal year 2015 income before income taxes, based upon a recent estimate of foreign exchange translation exposure (translating the operating performance of our foreign subsidiaries into U.S. Dollars), of a uniform strengthening or weakening of the U.S. Dollar by 10 percent, would be to increase or decrease income before income taxes by approximately \$1.0 million for the three months ended September 30, 2014.

Competitive conditions in the markets in which we operate may limit our ability to increase prices in the event of adverse changes in currency exchange rates. For example, certain products made in Europe are sold in the U.S. Sales of these products are affected by the value of the U.S. Dollar relative to the Euro. Any weakening of the U.S. Dollar could depress the demand for these European manufactured products in the U.S. and reduce sales. However, due to the multiple currencies involved in our business and the netting effect of various simultaneous transactions, our foreign currency positions are partially offsetting. In addition, our foreign currency hedging program is designed to limit our exposure.

Actual gains and losses in the future may differ materially from the hypothetical gains and losses discussed above based on changes in the timing and amount of interest rate and foreign currency exchange rate movements and our actual exposure and hedging transactions.



**Table of Contents**

**Item 4. Controls and Procedures**

***Evaluation of Disclosure Controls and Procedures***

Under the supervision and with the participation of our management, including our Chief Executive Officer and Chief Financial Officer, we have evaluated the effectiveness of our disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) promulgated by the Securities and Exchange Commission ( SEC ) under the Securities Exchange Act of 1934, as amended (the 1934 Act )) as of the end of the period covered by this Quarterly Report on Form 10-Q. Based on that evaluation, our Chief Executive Officer and Chief Financial Officer concluded that our disclosure controls and procedures are effective to provide reasonable assurance that information required to be disclosed in the reports that we file or submit under the 1934 Act is recorded, processed, summarized, and reported within the time periods specified in SEC rules and forms. We note that the design of any system of controls is based in part upon certain assumptions about the likelihood of future events, and there can be no assurance that any design will succeed in achieving our stated goals under all potential future conditions.

Interpretive guidance issued by the SEC staff permits the exclusion of an evaluation of the effectiveness of a registrant's disclosure controls and procedures as they relate to the internal control over financial reporting for acquired businesses during the first year following such acquisition. As discussed in Note 2 - *Acquisitions* in the Notes to the Consolidated Financial Statements contained in our Annual Report on Form 10-K for the fiscal year ended June 30, 2014 and in Note 23 *Acquisitions* in the Notes to the Condensed Consolidated Financial Statements in this Quarterly Report on Form 10-Q, we completed the acquisitions of AMX LLC and AMX Holding Corporation and substantially all of the assets of Verto Medical Solutions LLC, d/b/a yurbuds and its wholly-owned subsidiary (collectively the Acquired Businesses ) in June 2014. The Acquired Businesses had total assets representing three percent of consolidated assets, and total revenues representing four percent of consolidated revenues included in our consolidated financial statements as of and for three months ended September 30, 2014. Management's evaluation and conclusion as to the effectiveness of the design and operation of the Company's disclosure controls and procedures as of the end of the period covered by this Quarterly Report on Form 10-Q excludes any evaluation of the internal control over financial reporting of the Acquired Businesses.

***Changes in Internal Control Over Financial Reporting***

As a result of the acquisitions of the Acquired Businesses, we have begun to integrate certain business processes and systems of the Acquired Businesses.

There have been no other changes in our internal control over financial reporting (as defined in Rules 13a-15(f) and 15d-15(f) as promulgated by the SEC under the 1934 Act), during our most recently completed fiscal quarter that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

**Table of Contents****Item 6. Exhibits**

| <b>Exhibit No.</b> | <b>Exhibit Description</b>   |
|--------------------|--|
| 31.1               | Certification of Dinesh C. Paliwal pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.*   |
| 31.2               | Certification of Herbert K. Parker pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.*   |
| 32.1               | Certification of Dinesh Paliwal and Herbert Parker, pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.*   |
| 99.1               | Form of Indemnification Letter Agreement with Directors and Executive Officers (Filed as Exhibit 99.1 to the Current Report on Form 8-K filed with the Commission on September 10, 2014 and hereby incorporated by reference). |
| 101.INS            | XBRL Instance Document.*   |
| 101.SCH            | XBRL Taxonomy Extension Schema.*   |
| 101.CAL            | XBRL Taxonomy Extension Calculation Linkbase.*   |
| 101.DEF            | XBRL Taxonomy Extension Definition Linkbase.*  |
| 101.LAB            | XBRL Taxonomy Extension Label Linkbase.*   |
| 101.PRE            | XBRL Taxonomy Extension Presentation Linkbase.*  |

\* Filed electronically herewith.

Attached as Exhibit 101 to this report are the following financial information formatted in XBRL (Extensible Business Reporting Language): (i) Condensed Consolidated Balance Sheets at September 30, 2014 and June 30, 2014, (ii) Condensed Consolidated Statements of Income for the three months ended September 30, 2014 and 2013, (iii) Condensed Consolidated Statements of Comprehensive Income for the three months ended September 30, 2014 and 2013, (iv) Condensed Consolidated Statements of Cash Flows for the three months ended September 30, 2014 and 2013 and (v) Notes to the Condensed Consolidated Financial Statements.

Table of Contents

**SIGNATURES**

Pursuant to the requirements of the Securities Exchange Act of 1934, Harman International Industries, Incorporated has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

Harman International Industries, Incorporated

Date: October 30, 2014

By: **/s/ HERBERT K. PARKER**  
**Herbert K. Parker**  
**Executive Vice President and Chief Financial**  
**Officer**  
**(Principal Financial Officer)**