

Steris plc
Form 10-Q
August 09, 2016
Table of Contents

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

FORM 10-Q
(Mark One)

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

For the quarterly period ended June 30, 2016
or

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

For the transition period from _____ to _____

Commission File Number 1-37614
STERIS plc
(Exact name of registrant as specified in its charter)

United Kingdom
(State or other jurisdiction of
incorporation or organization)

98-1203539
(IRS Employer
Identification No.)

Chancery House, 190 Waterside Road, Hamilton Industrial Park Leicester LE51QZ
(Address of principal executive offices) (Zip code)
44-116-276-8636
(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 x No o

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes x No o

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

Large Accelerated Filer x Accelerated Filer o
Non-Accelerated Filer o Smaller Reporting Company o
(Do not check if a smaller reporting company)

Edgar Filing: Steris plc - Form 10-Q

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

The number of ordinary shares outstanding as of July 29, 2016: 86,148,639

1

Table of Contents

STERIS plc and Subsidiaries
Form 10-Q
Index

	Page
<u>Part I—Financial Information</u>	
<u>Item 1. Financial Statements</u>	<u>3</u>
<u>Item 2. Management’s Discussion and Analysis of Financial Condition and Results of Operations</u>	<u>26</u>
<u>Item 3. Quantitative and Qualitative Disclosures About Market Risk</u>	<u>38</u>
<u>Item 4. Controls and Procedures</u>	<u>38</u>
<u>Part II—Other Information</u>	
<u>Item 1. Legal Proceedings</u>	<u>39</u>
<u>Item 1A. Risk Factors</u>	<u>39</u>
<u>Item 2. Unregistered Sales of Equity Securities and Use of Proceeds</u>	<u>40</u>
<u>Item 6. Exhibits</u>	<u>41</u>
<u>Signature</u>	<u>42</u>

Table of Contents

PART 1—FINANCIAL INFORMATION

As used in this Quarterly Report on Form 10-Q, STERIS plc and its subsidiaries together are called “STERIS,” the “Company,” “we,” “us,” or “our,” unless otherwise noted.

ITEM 1. FINANCIAL STATEMENTS

STERIS PLC AND SUBSIDIARIES
CONSOLIDATED BALANCE SHEETS
(in thousands)

	June 30, 2016 (Unaudited)	March 31, 2016
Assets		
Current assets:		
Cash and cash equivalents	\$242,423	\$248,841
Accounts receivable (net of allowances of \$9,420 and \$11,185, respectively)	439,845	471,523
Inventories, net	209,645	192,792
Prepaid expenses and other current assets	53,972	59,369
Total current assets	945,885	972,525
Property, plant, and equipment, net	1,055,706	1,064,319
Goodwill and intangibles, net	3,258,546	3,279,942
Other assets	33,034	29,630
Total assets	\$5,293,171	\$5,346,416
Liabilities and equity		
Current liabilities:		
Accounts payable	\$123,253	\$139,572
Accrued income taxes	14,882	13,683
Accrued payroll and other related liabilities	70,523	93,976
Accrued expenses and other	150,802	153,375
Total current liabilities	359,460	400,606
Long-term indebtedness	1,551,838	1,567,796
Deferred income taxes, net	250,932	254,824
Other liabilities	82,456	84,298
Total liabilities	\$2,244,686	\$2,307,524
Commitments and contingencies (see note 9)		
Preferred shares, with £0.10 par value; 100 shares authorized; 100 issued and outstanding	15	15
Ordinary shares, with £0.10 par value; £17,006 shares aggregate par amount authorized; 86,151 and 85,920 ordinary shares issued and outstanding, respectively	2,161,050	2,151,719
Retained earnings	961,924	939,459
Accumulated other comprehensive (loss) income	(85,718)	(68,159)
Total shareholders' equity	3,037,271	3,023,034
Noncontrolling interests	11,214	15,858
Total equity	3,048,485	3,038,892
Total liabilities and equity	\$5,293,171	\$5,346,416

See notes to consolidated financial statements.

Table of Contents

STERIS PLC AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF INCOME
(in thousands, except per share amounts)
(Unaudited)

	Three Months Ended June 30,	
	2016	2015
Revenues:		
Product	\$271,750	\$232,307
Service	366,628	207,595
Total revenues	638,378	439,902
Cost of revenues:		
Product	142,698	129,856
Service	255,690	125,956
Total cost of revenues	398,388	255,812
Gross profit	239,990	184,090
Operating expenses:		
Selling, general, and administrative	151,886	126,835
Research and development	14,428	13,765
Restructuring expenses	154	(726)
Total operating expenses	166,468	139,874
Income from operations	73,522	44,216
Non-operating expenses, net:		
Interest expense	11,071	6,120
Interest income and miscellaneous expense	(493)	(482)
Total non-operating expenses, net	10,578	5,638
Income before income tax expense	62,944	38,578
Income tax expense	14,234	14,267
Net income	48,710	24,311
Less: Net income attributable to noncontrolling interests	309	20
Net income attributable to shareholders	\$48,401	\$24,291
Net income per share		
Basic	\$0.56	\$0.41
Diluted	\$0.56	\$0.40
Cash dividends declared per share outstanding	\$0.25	\$0.23

See notes to consolidated financial statements.

Table of Contents

STERIS PLC AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME

(in thousands)

(Unaudited)

	Three Months Ended June 30,	
	2016	2015
Net income	\$48,710	\$24,311
Less: Net income attributable to noncontrolling interests	309	20
Net income attributable to shareholders	48,401	24,291
Other comprehensive income (loss)		
Unrealized loss on available for sale securities, (net of taxes of \$34 and \$226, respectively)	(120)	(848)
Amortization of pension and postretirement benefit plans costs, (net of taxes of \$241 and \$95, respectively)	(390)	(153)
Change in cumulative foreign currency translation adjustment	(17,049)	13,798
Total other comprehensive loss	(17,559)	12,797
Comprehensive income	\$30,842	\$37,088

See notes to consolidated financial statements.

Table of Contents

STERIS PLC AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF CASH FLOWS
(in thousands)
(Unaudited)

	Three Months Ended June 30, 2016	2015
Operating activities:		
Net income	\$ 48,710	\$ 24,311
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation, depletion, and amortization	53,784	22,353
Deferred income taxes	989	5,629
Share-based compensation expense	4,187	3,145
Loss on the disposal of property, plant, equipment, and intangibles, net	126	3
Excess tax benefit from share-based compensation	—	(3,910)
Other items	(17,713)	(19,838)
Changes in operating assets and liabilities, net of effects of acquisitions:		
Accounts receivable, net	23,248	38,869
Inventories, net	(19,765)	(18,174)
Other current assets	3,687	463
Accounts payable	(13,246)	(5,696)
Accruals and other, net	(3,691)	(6,002)
Net cash provided by operating activities	80,316	41,153
Investing activities:		
Purchases of property, plant, equipment, and intangibles, net	(35,357)	(23,518)
	4,526	28

Edgar Filing: Steris plc - Form 10-Q

Proceeds from the sale of property, plant, equipment, and intangibles			
Purchase of investments	(4,564))	—
Acquisition of business, net of cash acquired	(250))	(44,310)
Net cash used in investing activities	(35,645))	(67,800)
Financing activities:			
Proceeds from issuance of long-term obligations	—		350,000
Payments on long-term obligations	(5,000))	—
Payments under credit facilities, net	(11,079))	(283,250)
Deferred financing fees and debt issuance costs	—		(1,978)
Acquisition related deferred or contingent consideration	(6,000))	—
Repurchases of ordinary shares	(5,171))	(9,573)
Cash dividends paid to ordinary shareholders	(21,538))	(13,758)
Proceeds from issuance of equity to minority shareholders	5,022		—
Stock option and other equity transactions, net	758		4,881
Excess tax benefit from share-based compensation	—		3,910
Net cash (used in) provided by financing activities	(43,008))	50,232
Effect of exchange rate changes on cash and cash equivalents	(8,081))	4,919
(Decrease) increase in cash and cash equivalents	(6,418))	28,504
Cash and cash equivalents at beginning of period	248,841		167,689

Cash and cash equivalents at end of period	\$	242,423	\$	196,193
--	----	---------	----	---------

See notes to consolidated financial statements.

Table of Contents

STERIS PLC AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Unaudited)

For the Three Months Ended June 30, 2016 and 2015

(dollars in thousands, except per share amounts)

1. Nature of Operations and Summary of Significant Accounting Policies

Nature of Operations

STERIS plc, a public limited company organized under the laws of England and Wales, was incorporated on October 9, 2014 as a private limited company under the name New STERIS Limited and was re-registered effective November 2, 2015 as a public limited company under the name STERIS plc. New STERIS Limited was established to effect the combination (“Combination”) of STERIS Corporation, an Ohio corporation (“Old STERIS”), and Synergy Health plc, a public limited company organized under the laws of England and Wales (“Synergy”). The Combination closed on November 2, 2015 and as a result STERIS plc became the ultimate parent company of Old STERIS and Synergy. Synergy has been re-registered under the name Synergy Health Limited. The acquisition of Old STERIS was accounted for in the consolidated financial statements as a merger between entities under common control; accordingly the historical consolidated financial statements of Old STERIS for periods prior to November 2, 2015, are considered to be the historical financial statements of STERIS plc. Due to the timing of the Combination, the results of Synergy are only reflected in the results of operations of the Company from November 2, 2015 forward which affects comparability to the prior period historical operations of the Company throughout this Quarterly Report on Form 10-Q.

STERIS offers Customers capital equipment products, such as sterilizers and surgical tables; connectivity solutions such as operating room integration; consumable products, such as detergents, gastrointestinal endoscopy accessories, barrier product solutions, and other products and services, including: equipment installation and maintenance, microbial reduction of medical devices, instrument and scope repair solutions, among other services.

Our fiscal year ends on March 31. References in this Quarterly Report to a particular “year” or “year-end” mean our fiscal year. The significant accounting policies applied in preparing the accompanying consolidated financial statements of the Company are summarized below:

Interim Financial Statements

We prepared the accompanying unaudited consolidated financial statements of the Company according to accounting principles generally accepted in the United States (“U.S. GAAP”) for interim financial information and the instructions to the Quarterly Report on Form 10-Q and Rule 10-01 of Regulation S-X. This means that they do not include all of the information and footnotes required by U.S. GAAP for complete financial statements. Our unaudited interim consolidated financial statements contain all material adjustments (including normal recurring accruals and adjustments) management believes are necessary to fairly state our financial condition, results of operations, and cash flows for the periods presented.

These interim consolidated financial statements should be read together with the consolidated financial statements and related notes included in our Annual Report on Form 10-K for the year ended March 31, 2016 dated May 31, 2016. The Consolidated Balance Sheet at March 31, 2016 was derived from the audited consolidated financial statements at that date, but does not include all of the information and footnotes required by U.S. GAAP for complete financial statements.

Principles of Consolidation

We use the consolidation method to report our investment in our subsidiaries. Therefore, the accompanying consolidated financial statements include the accounts of the Company and its wholly-owned and majority-owned subsidiaries. We eliminate inter-company accounts and transactions when we consolidate these accounts. Investments in equity of unconsolidated affiliates, over which the Company has significant influence, but not control, over the financial and operating policies, are accounted for primarily using the equity method. These investments are immaterial to the Company's Consolidated Financial Statements. In prior periods we presented income attributable to noncontrolling interests in the "Interest income and miscellaneous expense" line of our Consolidated Statements of Income and the amounts were not material.

Table of Contents

STERIS PLC AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Unaudited)—(Continued)

For the Three Months Ended June 30, 2016 and 2015

(dollars in thousands)

Use of Estimates

We make certain estimates and assumptions when preparing financial statements according to U.S. GAAP that affect the reported amounts of assets and liabilities at the financial statement dates and the reported amounts of revenues and expenses during the periods presented. These estimates and assumptions involve judgments with respect to many factors that are difficult to predict and are beyond our control. Actual results could be materially different from these estimates. We revise the estimates and assumptions as new information becomes available. This means that operating results for the three month period ended June 30, 2016 are not necessarily indicative of results that may be expected for future quarters or for the full fiscal year ending March 31, 2017.

Recently Issued Accounting Standards Impacting the Company

Recently issued accounting standards impacting the Company are presented in the following table:

Standard	Date of Issuance	Description	Date of Adoption	Effect on the financial statements or other significant matters
Standards that have recently been adopted				
ASU 2015-05, "Goodwill and other-Internal-Use Software" (Subtopic 350-40)	April 2015	The standard provides guidance on a customer's accounting for fees paid in cloud computing arrangements. Previously, there was no U.S. GAAP guidance on accounting for such fees from the customer's perspective. Under the standard, customers will apply the same criteria as vendors to determine whether the arrangement contains a software license or is solely a service contract. The determination could impact the classification of advance payments in the statements of financial position and cash flows as well as the classification of the expenses in the results of operations. The standard is effective for annual periods beginning after December 15, 2015 and interim periods within that period. Early adoption is permitted.	First Quarter Fiscal 2017	The adoption of this standard did not have a material impact on our statements of consolidated financial position, results of operations and cash flows.

Table of Contents

STERIS PLC AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Unaudited)—(Continued)

For the Three Months Ended June 30, 2016 and 2015

(dollars in thousands)

ASU 2016-09, "Stock Compensation: Improvements to Employee Share-Based Payment Accounting" (Topic 718)	March 2016	The update simplifies several aspects of the accounting for share-based payment award transactions, including income tax consequences, the classification of awards as either equity or liabilities, and the classification on the statement of cash flows. The standard is effective for annual periods beginning after December 15, 2016 and interim periods within that period. Early adoption is permitted.	First Quarter Fiscal 2017	As a result of the adoption of this standard, we recorded \$2.4 million of excess tax benefits associated with share based compensation in the statement of income for the three months ended June 30, 2016 and have included the associated cash flows as cash provided by operating activities. Prior periods have not been restated.
Standards that have yet to be adopted				
ASU 2014-09, "Revenue from Contracts with Customers"	May 2014	The standard will replace existing revenue recognition standards and significantly expand the disclosure requirements for revenue arrangements. It may be adopted either retrospectively or on a modified retrospective basis to new contracts and existing contracts with remaining performance obligations as of the effective date. The standard update is effective for annual periods beginning after December 15, 2017 and interim periods within that period, early adoption is not permitted before the original public entity effective date of December 15, 2016.	N/A	We are currently in the process of evaluating the impact that the standard will have on our consolidated financial position, results of operations and cash flows.
ASU 2016-02, "Leases" (Topic 842)	February 2016	The update will require lessees to record all leases, whether finance or operating, on the balance sheet. An asset will be recorded to represent the right to use the leased asset, and a liability will be recorded to represent the lease obligation. The standard is effective for annual periods beginning after December 15, 2018 and interim periods within that period. Early adoption is permitted.	N/A	We are in the process of evaluating the impact that the standard will have on our statements of consolidated financial position, results of operations and cash flows.
ASU 2016-07, "Investments - Equity Method and Joint Ventures, Simplifying the Transition to the Equity Method of	March 2016	The update replaces the previous requirement to retroactively adopt the equity method. The new standard requires that the equity method investor add the cost of acquiring the additional interest in the investee to the current basis of the	N/A	We do not expect the adoption of this standard to have a material impact on our statements of consolidated financial position, results of operations and cash flows.

Accounting" (Topic
323)

investor's previously held interest and adopt the equity method of accounting as of the date the investment becomes qualified for equity method accounting. The standard is effective for annual periods beginning after December 15, 2016 and interim periods within that period. Early adoption is permitted.

A detailed description of our significant and critical accounting policies, estimates, and assumptions is included in our consolidated financial statements included in our Annual Report on Form 10-K for the year ended March 31, 2016 dated May 31, 2016. Our significant and critical accounting policies, estimates, and assumptions have not changed materially from March 31, 2016.

Table of Contents

STERIS PLC AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Unaudited)—(Continued)

For the Three Months Ended June 30, 2016 and 2015

(dollars in thousands)

2. Restructuring

Fiscal 2014 Restructuring Plan. During the fourth quarter of fiscal 2014, we adopted and announced a targeted restructuring plan primarily focused on the closure of our Hopkins manufacturing facility located in Mentor, Ohio (the “Fiscal 2014 Restructuring Plan”). As a result of this plan, we will transfer operations located at Hopkins to other North American locations. We believe that by closing the operations at Hopkins we will more effectively utilize our existing North American manufacturing network while reducing operating costs.

Since the inception of the Fiscal 2014 Restructuring Plan, we have incurred pre-tax expenses totaling \$19,128 related to these actions, of which \$11,032 was recorded as restructuring expenses and \$8,096 was recorded in cost of revenues, with restructuring expenses of \$15,726, \$1,293, \$829, and \$1,280 related to the Healthcare Products, Healthcare Specialty Services, Life Sciences and Applied Sterilization Technologies segments, respectively.

The following table summarizes our total pre-tax restructuring expenses for the first quarters of fiscal 2017 and fiscal 2016: