

HENRY SCHEIN INC  
Form 10-Q  
August 06, 2018

**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**

For the quarterly period ended June 30, 2018

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:** 0-27078

HENRY SCHEIN, INC.

(Exact name of registrant as specified in its charter)

Delaware 11-3136595  
(State or other jurisdiction of (I.R.S. Employer Identification No.)  
incorporation or organization)

135 Duryea Road

**Melville, New York**

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(Address of principal executive offices)

11747

(Zip Code)

(631) 843-5500

(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 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, a smaller reporting company, or an emerging growth company. See the definitions of "large accelerated filer," "accelerated filer," "smaller reporting company," and emerging growth company in Rule 12b-2 of the Exchange Act.

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

If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 7(a)(2)(B) of the Securities Act.

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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 July 30, 2018, there were 153,111,471 shares of the registrant's common stock outstanding.

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PART I. FINANCIAL INFORMATION

ITEM 1. CONSOLIDATED FINANCIAL STATEMENTS

HENRY SCHEIN, INC.

CONSOLIDATED BALANCE SHEETS

(in thousands, except share and per share data)

ASSETS

Current assets:

Cash and cash equivalents

Accounts receivable, net of reserves of \$53,609 and \$53,832

Inventories, net

Prepaid expenses and other

Total current assets

Property and equipment, net

Goodwill

Other intangibles, net

Investments and other

Total assets

LIABILITIES AND STOCKHOLDERS' EQUITY

Current liabilities:

Accounts payable

Bank credit lines

Current maturities of long-term debt

Accrued expenses:

Payroll and related

Taxes

Other

Total current liabilities

Long-term debt	.....
Deferred income taxes	.....
Other liabilities	.....
Total liabilities	.....
Redeemable noncontrolling interests	.....
Commitments and contingencies	.....
Stockholders' equity:	
Preferred stock, \$.01 par value, 1,000,000 shares authorized, none outstanding	.....
Common stock, \$.01 par value, 480,000,000 shares authorized, 153,231,669 outstanding on June 30, 2018 and 240,000,000 shares authorized, 153,690,146 outstanding on December 30, 2017	.....
Retained earnings	.....
Accumulated other comprehensive loss	.....
Total Henry Schein, Inc. stockholders' equity	.....
Noncontrolling interests	.....
Total stockholders' equity	.....
Total liabilities, redeemable noncontrolling interests and stockholders' equity	.....

See accompanying notes.



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HENRY SCHEIN, INC.

CONSOLIDATED STATEMENTS OF INCOME

(in thousands, except per share data)

(unaudited)

	THREE Months Ended June 30, 2014
Net sales .....	\$3,200,000
Cost of sales .....	2,200,000
Gross profit .....	900,000
Operating expenses:	
Selling, general and administrative .....	670,000
Transaction costs related to Animal Health spin-off.....	70,000
Restructuring costs .....	140,000
Operating income .....	200,000
Other income (expense):	
Interest income .....	50,000
Interest expense .....	(100,000)
Other, net .....	(100,000)
Income before taxes and equity in earnings of affiliates .....	180,000
Income taxes .....	(40,000)
Equity in earnings of affiliates .....	50,000
Net income .....	140,000
Less: Net income attributable to noncontrolling interests .....	(60,000)
Net income attributable to Henry Schein, Inc. ....	\$140,000

Earnings per share attributable to Henry Schein, Inc.:

Basic .....	\$0.
Diluted .....	\$0.

Weighted-average common shares outstanding:

Basic .....	15
Diluted .....	15

See accompanying notes.

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HENRY SCHEIN, INC.

CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME

(in thousands)

(unaudited)

	Thru Jun 201
Net income	\$14
Other comprehensive income (loss), net of tax:	
Foreign currency translation gain (loss).....	(1)
Unrealized gain (loss) from foreign currency hedging activities .....	1,
Unrealized investment loss	(1)
Pension adjustment gain (loss).....	96
Other comprehensive income (loss), net of tax	(1)
Comprehensive income	20
Comprehensive income attributable to noncontrolling interests:	
Net income .....	(6)
Foreign currency translation gain (loss).....	13
Comprehensive income attributable to noncontrolling interests .....	7,
Comprehensive income attributable to Henry Schein, Inc.	\$27

See accompanying notes.



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HENRY SCHEIN, INC.

CONSOLIDATED STATEMENT OF CHANGES IN STOCKHOLDERS' EQUITY

(in thousands, except share and per share data)

(unaudited)

Balance, December 30, 2017 .....	
Cumulative impact of adopting new accounting standards (Note 2).....	
Net income (excluding \$14,371 attributable to Redeemable noncontrolling interests) .....	
Foreign currency translation loss (excluding loss of \$11,535 attributable to Redeemable noncontrolling interests) .....	
Unrealized gain from foreign currency hedging activities, net of tax of \$432.....	
Unrealized investment loss, net of tax of \$0.....	
Pension adjustment gain, including tax of \$370.....	
Dividends paid .....	
Other adjustments .....	
Purchase of noncontrolling interests.....	
Change in fair value of redeemable securities .....	
Initial noncontrolling interests and adjustments related to business acquisitions.....	
Repurchase and retirement of common stock .....	
Stock issued upon exercise of stock options .....	
Stock-based compensation expense .....	
Shares withheld for payroll taxes .....	
Settlement of stock-based compensation awards .....	
Deferred tax benefit arising from acquisition of noncontrolling interest in partnership.....	
Transfer of charges in excess of capital.....	
Balance, June 30, 2018 .....	

See accompanying notes.

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HENRY SCHEIN, INC.

CONSOLIDATED STATEMENTS OF CASH FLOWS

(in thousands)

(unaudited)

Cash flows from operating activities:

Net income .....

Adjustments to reconcile net income to net cash provided by operating activities:

    Depreciation and amortization .....

    Stock-based compensation expense .....

    Provision for losses on trade and other accounts receivable .....

    Provision for (benefit from) deferred income taxes .....

    Equity in earnings of affiliates .....

    Distributions from equity affiliates .....

    Changes in unrecognized tax benefits .....

    Other .....

Changes in operating assets and liabilities, net of acquisitions:

    Accounts receivable .....

    Inventories .....

    Other current assets .....

    Accounts payable and accrued expenses .....

Net cash provided by operating activities .....

Cash flows from investing activities:

Purchases of fixed assets .....

Payments for equity investments and business acquisitions, net of cash acquired .....

Other .....

Net cash used in investing activities .....

Cash flows from financing activities:

Proceeds from bank borrowings	.....
Proceeds from issuance of long-term debt	.....
Debt issuance costs	.....
Principal payments for long-term debt	.....
Proceeds from issuance of stock upon exercise of stock options	.....
Payments for repurchases of common stock	.....
Payments for taxes related to shares withheld for employee taxes	.....
Distributions to noncontrolling stockholders	.....
Acquisitions of noncontrolling interests in subsidiaries	.....
Net cash provided by (used in) financing activities	.....
Effect of exchange rate changes on cash and cash equivalents	.....
Net change in cash and cash equivalents	.....
Cash and cash equivalents, beginning of period	.....
Cash and cash equivalents, end of period	.....

See accompanying notes.

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**HENRY SCHEIN, INC.**

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(in thousands, except per share data)

**(unaudited)**

**Note 1 – Basis of Presentation**

Our consolidated financial statements include our accounts, as well as those of our wholly owned and majority owned subsidiaries. Certain prior period amounts have been reclassified to conform to the current period presentation.

Our accompanying unaudited consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States (“U.S. GAAP”) for interim financial information and with the instructions to Form 10-Q and Article 10 of Regulation S-X. Accordingly, they do not include all of the information and footnote disclosures required by U.S. GAAP for complete financial statements.

The consolidated financial statements reflect all adjustments considered necessary for a fair presentation of the consolidated results of operations and financial position for the interim periods presented. All such adjustments are of a normal recurring nature. These unaudited interim consolidated financial statements should be read in conjunction with the audited consolidated financial statements and notes to the consolidated financial statements contained in our Annual Report on Form 10-K for the year ended December 30, 2017.

The preparation of financial statements in conformity with U.S. GAAP requires us to make estimates and assumptions that affect the reported amounts of assets and liabilities, and disclosure of contingent assets and liabilities, at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates. The results of operations for the six months ended June 30, 2018 are not necessarily indicative of the results to be expected for any other interim period or for the year ending December 29, 2018.

On August 16, 2017, we announced that our Board of Directors approved a 2-for-1 split of our common stock. Each Henry Schein, Inc. stockholder of record at the close of business on September 1, 2017 received a dividend of one additional share for every share held. Trading began on a split-adjusted basis on September 15, 2017 and has been retroactively reflected for all periods presented in this Form 10-Q. As a result of the stock split, we increased our authorized common shares from 240,000,000 to 480,000,000, effective May 31, 2018.



**Note 2 -Accounting Pronouncements Adopted and Critical Accounting Policies and Estimates**

**Accounting Pronouncements Adopted**

In May 2014, the Financial Accounting Standards Board (“FASB”) issued Accounting Standard Update (“ASU”) No. 2014-09, “Revenue from Contracts with Customers”, Accounting Standards Codification (“ASC”) 606 (“Topic 606”). We adopted the provisions of this standard as of December 31, 2017, on a modified retrospective basis. We applied the requirements of the new standard only to contracts that were not completed as of the adoption date. We recorded an immaterial adjustment to the opening balance of retained earnings for the adoption of Topic 606. The comparative information has not been restated and continues to be reported under the accounting standards in effect for those periods.

The impact of the new standard on our consolidated statements of income, which we expect to be immaterial on an ongoing basis, is primarily related to software sales and sales commissions and is described as follows:

**Software Sales**

For software licenses sold together with post contract support (PCS), we previously deferred software revenue if it did not have vendor-specific evidence of fair value of the PCS. Under Topic 606, the concept of vendor-specific objective evidence is eliminated and there are no cases where revenue is deferred due to a lack of standalone selling price. In addition, we previously recognized revenue from term licenses ratably over the contract term. Under Topic 606, such licenses represent a right to use intellectual property and therefore require

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**HENRY SCHEIN, INC.**

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(in thousands, except per share data)

**(unaudited)**

upfront recognition. Furthermore, certain upfront fees related to service arrangements were previously deferred and recognized over the estimated customer life. Under Topic 606, the period over which we will recognize these fees is reduced, as the upfront fee represents additional contract price which will be allocated to the performance obligations in the contract and recognized as those performance obligations are satisfied, rather than being amortized over the estimated customer life. Based on the aforementioned changes, such software revenue will be recognized sooner than under the previous revenue recognition standard.

*Sales Commissions*

We previously recognized sales commissions as an expense when incurred. Under Topic 606, we defer such sales commissions as costs to obtain a contract when the costs are incremental and expected to be recovered. Deferred sales commissions are amortized over the estimated customer relationship period. We apply the practical expedient to expense, as incurred, commissions with an expected amortization period of one year or less.

The impact of adoption on our consolidated balance sheet and income statement was as follows:

	As of June 30
Balance Sheet	As Reported
Assets:	
Prepaid expenses and other .....	\$459,320
Investments and other .....	510,400
Liabilities:	
Accrued expenses -Taxes.....	\$ 172,900
Accrued expenses - Other .....	419,100
Deferred income taxes .....	48,120
Other liabilities (long-term) .....	407,400
Stockholders' equity:	
Retained earnings .....	\$3,123,300
Accumulated other comprehensive loss .....	\$(211,300)

Statement of Income

Net sales:

Dental .....  
Animal Health .....  
Medical .....  
Total healthcare distribution .....  
Technology and value-added services .....  
Total .....

Costs and expenses:

Cost of sales .....  
Selling, general and administrative .....  
Income taxes.....  
.....  
Net income .....



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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(in thousands, except per share data)

**(unaudited)**

Additional information related to Topic 606 can be found below in “Critical Accounting Policies and Estimates” as well as in Note 3.

In October 2016, the FASB issued ASU No. 2016-16, “Income Taxes, Intra-Entity Transfers of Assets Other Than Inventory” (“Topic 740”). Topic 740 requires companies to recognize the income tax effects of intercompany sales and transfers of assets other than inventory in the period which the transfer occurs. Previously, companies were required to defer the income tax effects on intercompany transfer of assets until the asset has been sold to an outside party. On December 31, 2017, we adopted the guidance, which is effective for annual periods and related interim periods beginning after December 15, 2017 on a modified retrospective basis. As a result of the adoption of Topic 740, we have recorded an immaterial adjustment to the opening balance of retained earnings and a reduction to prepaid assets.

In May 2017, the FASB issued ASU No. 2017-09, “Compensation-Stock Compensation (Topic 718), Scope of Modification Accounting”. ASU No. 2017-09 provides guidance on determining which changes to the terms and conditions of share-based payment awards require an entity to apply modification accounting. ASU 2017-09 requires modification accounting if the fair value, vesting conditions, or equity or liability classification of the award is not the same immediately before and after a change to the terms and conditions of the award. ASU 2017-09 was adopted on a prospective basis as of December 31, 2017 and did not have a material impact on the consolidated financial statements or disclosures as of June 30, 2018.

The cumulative effect of the changes made to our consolidated balance sheet as of December 31, 2017 related to Topic 606 and Topic 740 were as follows:

	Balance December
	2017 (As Reported)
Assets:	
Prepaid expenses and other .....	\$454,752
Investments and other .....	432,000

Liabilities:

Accrued expenses - Taxes.....	\$ 188,877
Accrued expenses - Other .....	455,780
Deferred income taxes .....	50,431
Other liabilities (long-term) .....	420,288

Stockholders' equity:

Retained earnings .....	\$2,940,000
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**Critical Accounting Policies and Estimates**

There have been no material changes in our critical accounting policies and estimates from those disclosed in Item 7 of our Annual Report on Form 10-K for the year ended December 30, 2017 (the “2017 Form 10-K”), except as follows:

*Revenue Recognition*

On December 31, 2017, we adopted Topic 606 using the modified retrospective method applied to those contracts which were not completed as of the adoption date. Results for reporting periods beginning after December 30, 2017 are presented under Topic 606, while prior period amounts are not adjusted and continue to be reported under the accounting standards in effect for those periods. Our revenue recognition accounting

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**HENRY SCHEIN, INC.**

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(in thousands, except per share data)

**(unaudited)**

policies applied prior to adoption of Topic 606 are outlined in the financial statements in the 2017 Form 10-K. The disclosures included herein reflect our accounting policies under Topic 606.

We generate revenue from the sale of dental, animal health and medical consumable products, as well as equipment, software products and services and other sources. Provisions for discounts, rebates to customers, customer returns and other contra revenue adjustments are included in the transaction price at contract inception by estimating the most likely amount based upon historical data and estimates and are provided for in the period in which the related sales are recognized.

Revenue derived from the sale of consumable products is recognized at a point in time when control transfers to the customer. Such sales typically entail high-volume, low-dollar orders shipped using third-party common carriers. We believe that control has transferred to the customer because we have no post-shipment obligations and this is when legal title and risks and rewards of ownership transfer to the customer and the point at which we have an enforceable right to payment.

Revenue derived from the sale of equipment is recognized when control transfers to the customer. This occurs when the equipment is delivered. Such sales typically entail scheduled deliveries of large equipment primarily by equipment service technicians. Some equipment Our product generally carries standard warranty terms provided by the manufacturer, however, in instances where we provide warranty labor services, the warranty costs are accrued in accordance with ASC 460 "Guarantees".

Revenue derived from the sale of software products is recognized when products are shipped to customers or made available electronically. Such software is generally installed by customers and does not require extensive training due to the nature of its design. Revenue derived from post-contract customer support for software, including annual support and/or training, is generally recognized over time using time elapsed as the input method that best depicts the transfer of control to the customer.

Revenue derived from other sources including freight charges, equipment repairs and financial services is recognized when the related product revenue is recognized or when the services are provided. We apply the practical expedient to

treat shipping and handling activities performed after the customer obtains control as fulfillment activities, rather than a separate performance obligation in the contract.

Sales, value add and other taxes we collect concurrent with revenue-producing activities are excluded from revenue.

Certain of our revenue is derived from bundled arrangements that include multiple distinct performance obligations which are accounted for separately. When we sell software products together with related services (i.e., training and technical support), we allocate revenue to software using the residual method, using an estimate of the standalone selling price to estimate the fair value of the undelivered elements. There are no cases where revenue is deferred due to a lack of a standalone selling price. Bundled arrangements that include elements that are not considered software consist primarily of equipment and the related installation service. We allocate revenue for such arrangements based on the relative selling prices of the goods or services. If an observable selling price is not available (i.e., we do not sell the goods or services separately), we use one of the following techniques to estimate the standalone selling price: adjusted market approach; cost-plus approach; or the residual method. There is no specific hierarchy for the use of these methods, but the estimated selling price reflects our best estimate of what the selling prices of each deliverable would be if it were sold regularly on a standalone basis taking into consideration the cost structure of our business, technical skill required, customer location and other market conditions.

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**HENRY SCHEIN, INC.**

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(in thousands, except per share data)

**(unaudited)**

Accounts Receivable

The carrying amount of accounts receivable is reduced by a valuation allowance that reflects our best estimate of the amounts that will not be collected. In addition to reviewing delinquent accounts receivable, we consider many factors in estimating our reserve, including historical data, experience, customer types, credit worthiness and economic trends. From time to time, we adjust our assumptions for anticipated changes in any of these or other factors expected to affect collectability.

Contract Assets

Contract assets include amounts related to any conditional right to consideration for work completed but not billed as of the reporting date and generally represent amounts owed to us by customers, but not yet billed. Contract assets are transferred to accounts receivable when the right becomes unconditional. Current contract assets are included in Prepaid expenses and other and the non-current contract assets are included in Investments and other within our consolidated balance sheet.

Contract Liabilities

Contract liabilities are comprised of advance payments and deferred revenue amounts. Contract liabilities are transferred to revenue once the performance obligation has been satisfied. Current contract liabilities are included in Accrued expenses: Other and the non-current contract liabilities are included in Other liabilities within our consolidated balance sheet.

Deferred Commissions



Sales commissions earned by our sales force that relate to long term arrangements are capitalized as costs to obtain a contract when the costs incurred are incremental and are expected to be recovered. Deferred sales commissions are amortized over the estimated customer relationship period. We apply the practical expedient related to the capitalization of incremental costs of obtaining a contract, and recognize such costs as an expense when incurred if the amortization period of the assets that we would have recognized is one year or less.

#### Sales Returns

Sales returns are recognized as a reduction of revenue by the amount of expected returns and are recorded as refund liability within current liabilities. We estimate the amount of revenue expected to be reversed to calculate the sales return liability based on historical data for specific products, adjusted as necessary for new products. The allowance for returns is presented gross as a refund liability and we record an inventory asset (and a corresponding adjustment to cost of sales) for any goods or services that we expect to be returned.

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**HENRY SCHEIN, INC.**

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(in thousands, except per share data)

**(unaudited)**

**Note 3 -Revenue from Contracts with Customers**

Revenue (Net sales) is recognized in accordance with the policies discussed in Note 2 - Accounting Pronouncements Adopted and Critical Accounting Policies and Estimates.

Disaggregation of Net sales

The following table disaggregates our Net sales by reportable segment and geographic area:

Net sales:

Health care distribution.....	
Dental .....	
Animal health .....	
Medical .....	
Total health care distribution.....	
Technology and value-added services.....	
Total .....	

*Contract Balances*

Contract balances represent amounts presented in our consolidated balance sheet when either we have transferred goods or services to the customer or the customer has paid consideration to us under the contract. These contract balances include accounts receivable, contract assets and contract liabilities.

The contract assets primarily relate to our rights to consideration for work completed but not billed at the reporting date on contracts. The contract assets are transferred to receivables when the rights become unconditional. The contract assets primarily relate to our bundled arrangements for the sale of equipment and consumables and sales of term software licenses. Current and non-current contract asset balances as of June 30, 2018 and December 31, 2017

were not material.

The contract liabilities primarily relate to advance payments from customers and upfront payments for service arrangements provided over time. At December 31, 2017, the current portion of contract liabilities of \$85.7 million was reported in Accrued expenses: Other, and \$5.2 million related to non-current contract liabilities were reported in Other liabilities. During the six months ended June 30, 2018, we recognized \$58.5 million of the amount previously deferred at December 31, 2017. At June 30, 2018, the current and non-current portion of contract liabilities were \$73.2 million and \$5.6 million, respectively.

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**HENRY SCHEIN, INC.**

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(in thousands, except per share data)

**(unaudited)**

**Note 4 – Segment Data**

We conduct our business through two reportable segments: (i) health care distribution and (ii) technology and value-added services. These segments offer different products and services to the same customer base.

The health care distribution reportable segment aggregates our global dental, animal health and medical operating segments. This segment distributes consumable products, small equipment, laboratory products, large equipment, equipment repair services, branded and generic pharmaceuticals, vaccines, surgical products, diagnostic tests, infection-control products and vitamins. Our global dental group serves office-based dental practitioners, dental laboratories, schools and other institutions. Our global animal health group serves animal health practices and clinics. Our global medical group serves office-based medical practitioners, ambulatory surgery centers, other alternate-care settings and other institutions. Our global dental, animal health and medical groups serve practitioners in 34 countries worldwide.

Our global technology and value-added services group provides software, technology and other value-added services to health care practitioners. Our technology group offerings include practice management software systems for dental and medical practitioners and animal health clinics. Our value-added practice solutions include financial services on a non-recourse basis, e-services, continuing education services for practitioners, consulting and other services.

The following tables present information about our reportable and operating segments:

Net Sales:

Health care distribution (1):

Dental .....	
Animal health .....	
Medical .....	
Total health care distribution .....	

Technology and value-added services

(2).....

Total .....

\*CS

- (1) Consists of consumable products, small equipment, laboratory products, large equipment, equipment repair services, brand generic pharmaceuticals, vaccines, surgical products, diagnostic tests, infection-control products and vitamins.
- (2) Consists of practice management software and other value-added products, which are distributed primarily to health care and financial services on a non-recourse basis, e-services, continuing education services for practitioners, consulting and services.

Operating Income:

Health care distribution

.....

Technology and value-added services

.....

Total .....

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**HENRY SCHEIN, INC.**

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(in thousands, except per share data)

**(unaudited)**

**Note 5 -Debt**

Bank Credit Lines

On April 18, 2017, we entered into a new \$750 million revolving credit agreement (the “Credit Agreement”). This facility, which matures in April 2022, replaced our \$500 million revolving credit facility, which was scheduled to mature in September 2019. The interest rate is based on the USD LIBOR plus a spread based on our leverage ratio at the end of each financial reporting quarter. On June 29, 2018, we amended the Credit Agreement to, among other things, (i) permit the consummation of the spin-off of HS Spinco, Inc., a Delaware corporation and a direct, wholly owned subsidiary of Henry Schein, Inc. (the “Spin-off”), (ii) provide for swing-line commitments in the amount of \$75 million, and (iii) provide for the designation of subsidiary borrowers under the facility. The Credit Agreement provides, among other things, that we are required to maintain maximum leverage ratios, and contains customary representations, warranties and affirmative covenants. The Credit Agreement also contains customary negative covenants, subject to negotiated exceptions on liens, indebtedness, significant corporate changes (including mergers), dispositions and certain restrictive agreements.

As of June 30, 2018 and December 30, 2017, the borrowings on this revolving credit facility were \$325.0 million and \$320.0 million, respectively. As of June 30, 2018 and December 30, 2017, there were \$11.2 million and \$11.3 million of letters of credit, respectively, provided to third parties under the credit facility.

As of June 30, 2018 and December 30, 2017, we had various other short-term bank credit lines available, of which \$454.3 million and \$421.7 million, respectively, were outstanding. At June 30, 2018 and December 30, 2017, borrowings under all of our credit lines had a weighted average interest rate of 2.89% and 2.27%, respectively.

*Private Placement Facilities*

On September 15, 2017, we increased our available private placement facilities with three insurance companies to a total facility amount of \$1 billion, and extended the expiration date to September 15, 2020. These facilities are

available on an uncommitted basis at fixed rate economic terms to be agreed upon at the time of issuance, from time to time through September 15, 2020. The facilities allow us to issue senior promissory notes to the lenders at a fixed rate based on an agreed upon spread over applicable treasury notes at the time of issuance. The term of each possible issuance will be selected by us and can range from five to 15 years (with an average life no longer than 12 years). The proceeds of any issuances under the facilities will be used for general corporate purposes, including working capital and capital expenditures, to refinance existing indebtedness and/or to fund potential acquisitions. On June 29, 2018, we amended and restated the above private placement facilities to, among other things, (i) permit the consummation of the Spin-off and (ii) provide for the issuance of notes in Euros, British Pounds and Australian Dollars, in addition to U.S. Dollars. The agreements provide, among other things, that we maintain certain maximum leverage ratios, and contain restrictions relating to subsidiary indebtedness, liens, affiliate transactions, disposal of assets and certain changes in ownership. These facilities contain make-whole provisions in the event that we pay off the facilities prior to the applicable due dates.

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## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(in thousands, except per share data)

**(unaudited)**

The components of our private placement facility borrowings as of June 30, 2018 are presented in the following table (in thousands):

Date of Borrowing	Amount of Borrowing Outstanding	Borrowing Rate	Due Date
September 2, 2010	\$ 100,000	3.79 %	September 2, 2020
January 20, 2012	50,000	3.45	January 20, 2024
January 20, 2012 (1)	28,571	3.09	January 20, 2022
December 24, 2012	50,000	3.00	December 24, 2024
June 2, 2014	100,000	3.19	June 2, 2021
June 16, 2017	100,000	3.42	June 16, 2027
September 15, 2017	100,000	3.52	September 15, 2029
January 2, 2018	100,000	3.32	January 2, 2028
Less: Deferred debt issuance costs	(387)		
	\$ 628,184		

(1) Annual repayments of approximately \$7.1 million for this borrowing commenced on January 20, 2016.

*Committed Loan Associated with Animal Health Spin-off*

On May 21, 2018, we obtained a \$400 million committed loan which matures on the earlier of (i) March 31, 2019 and (ii) the consummation of the Spin-off. The proceeds of this loan were used, among other things, to fund our purchase of all of the equity interests in Butler Animal Health Holding Company, LLC (“BAHHC”) directly or indirectly owned by Darby Group Companies, Inc. (“Darby”) and certain other sellers pursuant to the terms of that certain Amendment to Put Rights Agreements, dated as of April 20, 2018, by and among us, Darby, BAHHC and the individual sellers party thereto for an aggregate purchase price of \$365 million. As of June 30, 2018, the balance outstanding on this loan was \$400 million and is included within the “Bank credit lines” caption within our consolidated balance sheet. At June 30, 2018, the interest rate on this loan was 3.0%.

## U.S. Trade Accounts Receivable Securitization



We have a facility agreement with a bank, as agent, based on the securitization of our U.S. trade accounts receivable that is structured as an asset-backed securitization program with pricing committed for up to three years. On June 1, 2016, we extended the expiration date of this facility agreement to April 29, 2019 and increased the purchase limit under the facility from \$300 million to \$350 million. On July 6, 2017, we extended the expiration date of this facility agreement to April 29, 2020. The borrowings outstanding under this securitization facility were \$335 million and \$350 million as of June 30, 2018 and December 30, 2017, respectively. At June 30, 2018, the interest rate on borrowings under this facility was based on the asset-backed commercial paper rate of 2.29% plus 0.70%, for a combined rate of 2.99%. At December 30, 2017, the interest rate on borrowings under this facility was based on the asset-backed commercial paper rate of 1.53% plus 0.75%, for a combined rate of 2.28%.

We are required to pay a commitment fee of 30 basis points on the daily balance of the unused portion of the facility if our usage is greater than or equal to 50% of the facility limit or a commitment fee of 35 basis points on the daily balance of the unused portion of the facility if our usage is less than 50% of the facility limit.

Borrowings under this facility are presented as a component of Long-term debt within our consolidated balance sheet.

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Long-term debt

Long-term debt consisted of the following:

Private placement facilities	Jun 201
.....	\$62
U.S. trade accounts receivable securitization	
.....	33
Various collateralized and uncollateralized loans payable with interest in varying installments through 2022 at interest rates ranging from 2.56% to 4.60% at June 30, 2018 and ranging from 2.56% to 12.90% at December 30, 2017	
.....	29
Capital lease obligations payable through 2029 with interest rates ranging from 0.07% to 19.79% at June 30, 2018 and ranging from 0.84% to 19.79% at December 30, 2017	
.....	4,
Total .....	99
Less current maturities	
.....	(1
Total long-term debt .....	\$98

**Note 6 – Redeemable Noncontrolling Interests**

Some minority stockholders in certain of our subsidiaries have the right, at certain times, to require us to acquire their ownership interest in those entities at fair value. ASC Topic 480-10 is applicable for noncontrolling interests where we are or may be required to purchase all or a portion of the outstanding interest in a consolidated subsidiary from the

noncontrolling interest holder under the terms of a put option contained in contractual agreements. The components of the change in the Redeemable noncontrolling interests for the six months ended June 30, 2018 and the year ended December 30, 2017 are presented in the following table:

	Jun
	201
	\$8
Balance, beginning of period .....	\$8
Decrease in redeemable noncontrolling interests due to redemptions .....	(6
Increase in redeemable noncontrolling interests due to business acquisitions.....	9,
Net income attributable to redeemable noncontrolling interests .....	14
Dividends declared .....	(1
Effect of foreign currency translation gain (loss) attributable to redeemable noncontrolling interests .....	(1
Change in fair value of redeemable securities .....	1
Balance, end of period .....	\$29

Changes in the estimated redemption amounts of the noncontrolling interests subject to put options are adjusted at each reporting period with a corresponding adjustment to Additional paid-in capital. Future reductions in the carrying amounts are subject to a floor amount that is equal to the fair value of the redeemable noncontrolling interests at the time they were originally recorded. The recorded value of the redeemable noncontrolling interests cannot go below the floor level. These adjustments do not impact the calculation of earnings per share.



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## Note 7 – Comprehensive Income

Comprehensive income includes certain gains and losses that, under U.S. GAAP, are excluded from net income as such amounts are recorded directly as an adjustment to stockholders' equity. Our comprehensive income is primarily comprised of net income, foreign currency translation gain (loss), unrealized gain (loss) on foreign currency hedging activities, unrealized investment loss and pension adjustment gain (loss).

The following table summarizes our Accumulated other comprehensive loss, net of applicable taxes as of:

	June 30, 2018	De 30 20
Attributable to Redeemable noncontrolling interests:		
Foreign currency translation adjustment .....	\$(17,099)	\$(
Attributable to noncontrolling interests:		
Foreign currency translation adjustment .....	\$(181)	\$5
Attributable to Henry Schein, Inc.:		
Foreign currency translation loss .....	\$(195,756)	\$(
Unrealized gain (loss) from foreign currency hedging activities .....	271	(
Unrealized investment loss .....	(4)	(
Pension adjustment loss .....	(15,903)	(
Accumulated other comprehensive loss .....	\$(211,392)	\$(
Total Accumulated other comprehensive loss .....	\$(228,672)	\$(

The following table summarizes the components of comprehensive income, net of applicable taxes as follows:

Net income .....	T J 2 \$
Foreign currency translation gain (loss).....	
Tax effect .....	
Foreign currency translation gain (loss) .....	
Unrealized gain (loss) from foreign currency hedging activities .....	
Tax effect .....	
Unrealized gain (loss) from foreign currency hedging activities .....	
Unrealized investment loss.....	
Unrealized investment loss.....	
Pension adjustment gain (loss).....	
Tax effect .....	
Pension adjustment gain (loss).....	
Comprehensive income .....	\$

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During the three months ended June 30, 2018 and July 1, 2017, we recognized, as a component of our comprehensive income, a foreign currency translation gain (loss) of \$(129.8) million and \$72.8 million, respectively, due to changes in foreign exchange rates from the beginning of the period to the end of the period. During the six months ended June 30, 2018 and July 1, 2017, we recognized, as a component of our comprehensive income, a foreign currency translation gain (loss) of \$(95.6) million and \$114.3 million, respectively, due to changes in foreign exchange rates from the beginning of the period to the end of the period. Our financial statements are denominated in the U.S. Dollar currency. Fluctuations in the value of foreign currencies as compared to the U.S. Dollar may have a significant impact on our comprehensive income. The foreign currency translation gain (loss) during the three and six months ended June 30, 2018 and July 1, 2017 was impacted by changes in foreign currency exchange rates as follows:

Currency	Foreign Currency Translation	FX Rate into USD		Foreign Currency Translation Gain (Loss)	FX Rate into USD	
	Loss for the Three Months Ended	June 30, 2018	March 31, 2018	for the Three Months Ended	July 1, 2017	April 1, 2017
Euro						
	\$ (51,029)	1.16	1.23	\$ 53,494	1.14	1.07
British Pound						
	(22,770)	1.31	1.40	10,938	1.30	1.25
Australian Dollar						
	(12,171)	0.74	0.77	1,737	0.77	0.76
Canadian Dollar						
	(2,023)	0.76	0.77	3,368	0.77	0.75
Polish Zloty						
	(5,872)	0.27	0.29	4,312	0.27	0.25
	(3,552)	1.00	1.04	3,742	1.04	1.00

Swiss Franc

Brazilian  
Real

All other currencies

Total

(26,006)	0.26	0.30	(7,902)	0.30	0.32
----------	------	------	---------	------	------

(6,373)			3,109		
\$ (129,796)			\$ 72,798		

Foreign  
Currency  
TranslationForeign  
Currency  
Translation  
GainLoss  
for the Six  
Months  
Ended(Loss)  
for the Six  
Months  
EndedCurrency  
Euro

	FX Rate into USD			FX Rate into USD	
	June 30,	December 30,		July 1,	December 26,
	2018	2017		2017	2016
	1.16	1.20	\$ 65,342	1.14	1.05
	1.31	1.35	15,544	1.30	1.23
	0.74	0.78	12,453	0.77	0.72
	0.76	0.80	4,180	0.77	0.74
	0.27	0.29	6,951	0.27	0.24
	1.00	1.03	4,898	1.04	0.98

British Pound

Australian Dollar

Canadian Dollar

Polish Zloty

Swiss Franc

Brazilian  
Real

All other currencies

Total





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The following table summarizes our total comprehensive income, net of applicable taxes, as follows:

	Three Months Ended June 30, 2018
Comprehensive income attributable to Henry Schein, Inc. ....	\$27,708
Comprehensive income (loss) attributable to noncontrolling interests .....	(693)
Comprehensive income (loss) attributable to Redeemable noncontrolling interests .....	(6,385)
Comprehensive income .....	\$20,630

**Note 8 -Fair Value Measurements**

ASC Topic 820 “Fair Value Measurements and Disclosures” (“ASC Topic 820”) provides a framework for measuring fair value in generally accepted accounting principles.

ASC Topic 820 defines fair value as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. ASC Topic 820 establishes a fair value hierarchy that distinguishes between (1) market participant assumptions developed based on market data obtained from independent sources (observable inputs) and (2) an entity’s own assumptions about market participant assumptions developed based on the best information available in the circumstances (unobservable inputs).

The fair value hierarchy consists of three broad levels, which gives the highest priority to unadjusted quoted prices in active markets for identical assets or liabilities (Level 1) and the lowest priority to unobservable inputs (Level 3). The three levels of the fair value hierarchy under ASC Topic 820 are described as follows:

- Level 1— Unadjusted quoted prices in active markets for identical assets or liabilities that are accessible at the measurement date.
  
- Level 2— Inputs other than quoted prices included within Level 1 that are observable for the asset or liability, either directly or indirectly. Level 2 inputs include: quoted prices for similar assets or liabilities in active markets; quoted prices for identical or similar assets or liabilities in markets that are not active; inputs other than quoted prices that are observable for the asset or liability; and inputs that are derived principally from or corroborated by observable market data by correlation or other means.
  
- Level 3— Inputs that are unobservable for the asset or liability.

The following section describes the valuation methodologies that we used to measure different financial instruments at fair value.

#### Investments and notes receivable

There are no quoted market prices available for investments in unconsolidated affiliates and notes receivable; however, we believe the carrying amounts are a reasonable estimate of fair value.

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**HENRY SCHEIN, INC.**

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Debt

The fair value of our debt, including bank credit lines, as of June 30, 2018 and December 30, 2017 was estimated at \$2,177.2 million and \$1,666.1 million, respectively. Factors that we considered when estimating the fair value of our debt include market conditions, prepayment and make-whole provisions, liquidity levels in the private placement market, variability in pricing from multiple lenders and term of debt.

Derivative contracts

Derivative contracts are valued using quoted market prices and significant other observable and unobservable inputs. We use derivative instruments to minimize our exposure to fluctuations in foreign currency exchange rates. Our derivative instruments primarily include foreign currency forward agreements related to intercompany loans and certain forecasted inventory purchase commitments with suppliers.

The fair values for the majority of our foreign currency derivative contracts are obtained by comparing our contract rate to a published forward price of the underlying market rates, which is based on market rates for comparable transactions and are classified within Level 2 of the fair value hierarchy.

*Redeemable noncontrolling interests*

Some minority stockholders in certain of our subsidiaries have the right, at certain times, to require us to acquire their ownership interest in those entities at fair value based on third-party valuations. The primary factor affecting the future value of redeemable noncontrolling interests is expected earnings and, if such earnings are not achieved, the value of the redeemable noncontrolling interests might be impacted. The noncontrolling interests subject to put options are adjusted to their estimated redemption amounts each reporting period with a corresponding adjustment to Additional paid-in capital. Future reductions in the carrying amounts are subject to a “floor” amount that is equal to the fair value of the redeemable noncontrolling interests at the time they were originally recorded. The recorded value of the redeemable noncontrolling interests cannot go below the floor level. These adjustments do not impact the

calculation of earnings per share. The values for Redeemable noncontrolling interests are classified within Level 3 of the fair value hierarchy. The details of the changes in Redeemable noncontrolling interests are presented in Note 6.

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The following table presents our assets and liabilities that are measured and recognized at fair value on a recurring basis classified under the appropriate level of the fair value hierarchy as of June 30, 2018 and December 30, 2017:

Assets:		J
Derivative contracts .....		\$
Total assets .....		\$
Liabilities:		
Derivative contracts .....		\$
Total liabilities .....		\$
Redeemable noncontrolling interests		
.....		\$
*CS		
		D
Assets:		
Derivative contracts .....		\$
Total assets .....		\$
Liabilities:		
Derivative contracts .....		\$
Total liabilities .....		\$
Redeemable noncontrolling interests		
.....		\$

**Note 9 – Business Acquisitions and Planned Divestiture**

## Acquisitions

The operating results of all acquisitions are reflected in our financial statements from their respective acquisition dates.

On April 3, 2018, we announced a joint venture with Internet Brands, a provider of web presence and online marketing software, to create a newly formed entity, Henry Schein One, LLC. The transaction closed on July 1, 2018. The joint venture includes Henry Schein Practice Solutions products and services, as well as Henry Schein's international dental practice management systems and the dental businesses of Internet Brands. We own 74% of the joint venture and Internet Brands owns the remaining 26% minority interest. Beginning with the second anniversary of the effective date of the formation of the joint venture, Henry Schein One will issue additional shares to Internet Brands through the fifth anniversary of the effective date, thereby increasing Internet Brands' ownership by approximately 7.6%. Internet Brands will also be entitled to receive additional shares, in the aggregate up to approximately 1.6% of the joint venture's ownership, if certain operating targets are met by the joint venture in its fourth, fifth and sixth operating years. Senior management from Henry Schein and Internet Brands serve on the board of Henry Schein One. The combined entity, which serves markets globally, had pro-forma 2017 sales of approximately \$400 million, of which approximately \$100 million originated at Internet Brands.

We did not complete any material acquisitions during the six months ended June 30, 2018.

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Some prior owners of acquired subsidiaries are eligible to receive additional purchase price cash consideration if certain financial targets are met. We have accrued liabilities for the estimated fair value of additional purchase price consideration at the time of the acquisition. Any adjustments to these accrual amounts are recorded in our consolidated statements of income. For the six months ended June 30, 2018 and July 1, 2017, there were no material adjustments recorded in our consolidated statement of income relating to changes in estimated contingent purchase price liabilities.

Planned Divestiture

On April 23, 2018, we announced that we entered into a definitive agreement with HS Spinco, Inc., a direct, wholly owned subsidiary of Henry Schein (“Spinco”), and Direct Vet Marketing, Inc. (d/b/a Vets First Choice) (“DVM”) to create a newly formed company, Vets First Corp. The transaction is intended to be tax-free to Henry Schein stockholders for U.S. tax purposes. As part of this transaction, subject to the terms and conditions set forth in certain definitive agreements, we will contribute the assets and entities comprising our animal health business to Spinco. In exchange for the contribution to Spinco of our animal health business, Spinco will issue to Henry Schein shares of common stock, par value \$0.01 per share, of Spinco (the “Spinco Common Stock”). We will subsequently distribute to our stockholders all of the shares of Spinco Common Stock held by us (the “Distribution”). Immediately after the Distribution, HS Merger Sub, Inc., a wholly owned subsidiary of Spinco, will merge with and into DVM, with DVM surviving the merger as a wholly owned subsidiary of Spinco (with such subsidiary to be renamed Vets First Corp.). Upon consummation of these transactions, on a fully-diluted basis, the stockholders of Henry Schein and, if applicable, certain third parties and minority holders of our animal health subsidiaries that are contributed to Spinco in exchange for their interests in these subsidiaries, will own approximately 63% of the outstanding shares of Spinco Common Stock, and the then former stockholders of DVM will own approximately 37% of the outstanding shares of Spinco Common Stock, subject to certain adjustments. Henry Schein will nominate six individuals to the Vets First Corp. Board of Directors and DVM will nominate five individuals to the Vets First Corp. Board of Directors.

Additionally, we expect to receive a cash dividend between \$1.0 billion and \$1.25 billion on a tax-free basis as part of the transaction. We plan to use the proceeds for general corporate purposes, including share repurchases and repayment of indebtedness.

The transaction has been unanimously approved by our Board of Directors and the Board of Directors of DVM, which we are working toward closing by the end of 2018. It is also subject to customary closing conditions, including

customary regulatory approvals, the receipt of tax opinions from counsel with respect to the transaction and the effectiveness of the registration statement on Form S-1/S-4 to be filed with the SEC in connection with the transaction.

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**Note 10 -Plans of Restructuring**

On July 9, 2018, we committed to an initiative to rationalize our operations and provide expense efficiencies. These actions will allow us to execute on our plan to reduce our cost structure and fund new initiatives that will drive future growth under our 2018 to 2020 strategic plan. This initiative is expected to include the elimination of approximately 2% to 3% of our workforce and the closing of certain facilities. The total 2018 costs associated with the actions to complete this restructuring are expected to be in the range of \$45 million to \$55 million pre-tax, or \$0.22 to \$0.27 per diluted share, consisting of \$40 million to \$45 million in employee severance pay and benefits and \$5 million to \$10 million in facility costs, representing primarily lease termination and other facility closure related costs.

During the three and six months ended June 30, 2018, we recorded restructuring costs of \$14.9 million and \$18.7 million, respectively, primarily for certain redundancies. The costs associated with these restructuring activities are included in a separate line item, “Restructuring costs” within our consolidated statements of income.

The following table shows the amounts expensed and paid for restructuring costs that were incurred during the six months ended June 30, 2018 and during our 2017 fiscal year and the remaining accrued balance of restructuring costs as of June 30, 2018, which is included in Accrued expenses: Other and Other liabilities within our consolidated balance sheet:

Balance, December 31, 2016	\$
.....	
Payments and other adjustments	\$
.....	
Balance, December 30, 2017	\$
.....	
Provision	\$
.....	
Payments and other adjustments	\$
.....	

Balance, June 30, 2018

.....

.....

The following table shows, by reportable segment, the amounts expensed and paid for restructuring costs that were incurred during the six months ended June 30, 2018 and the 2017 fiscal year and the remaining accrued balance of restructuring costs as of June 30, 2018:

	Health Care Distribution	Technology and Value-Added Services	Total
Balance, December 31, 2016	\$ 25,238	\$ 465	\$25,703
Payments and other adjustments	(20,681)	(465)	(21,146)
Balance, December 30, 2017	\$ 4,557	\$ -	\$4,557
Provision	18,315	343	18,658
Payments and other adjustments	(11,370)	(207)	(11,577)
Balance, June 30, 2018	\$ 11,502	\$ 136	\$11,638

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**Note 11 – Earnings Per Share**

Basic earnings per share is computed by dividing net income attributable to Henry Schein, Inc. by the weighted-average number of common shares outstanding for the period. Our diluted earnings per share is computed similarly to basic earnings per share, except that it reflects the effect of common shares issuable for presently unvested restricted stock and restricted stock units and upon exercise of stock options, using the treasury stock method in periods in which they have a dilutive effect.

A reconciliation of shares used in calculating earnings per basic and diluted share follows:

Basic .....	
Effect of dilutive securities:	
Stock options, restricted stock and restricted stock units .....	
Diluted .....	

**Note 12 – Income Taxes**

Our effective tax rate was 24.8% for the six months ended June 30, 2018 and the six months ended July 1, 2017. The difference between our effective tax rate and the federal statutory tax rate for the six months ended June 30, 2018 primarily relates to state and foreign income taxes and interest expense. The difference between our effective tax rate and the federal statutory tax rate for the six months ended July 1, 2017 primarily relates to the adoption of ASU No. 2016-09, “Stock Compensation” (Topic 718) (“ASU 2016-09”) in the first quarter of 2017, as well as state and foreign income taxes and interest expense.

Under ASU 2016-09, all excess tax benefits and tax deficiencies resulting from the difference between the deduction for tax purposes and the stock-based compensation cost recognized for financial reporting purposes are included as a component of income tax expense beginning January 1, 2017. Prior to the implementation of ASU 2016-09, excess tax benefits were recorded as a component of Additional paid in capital and tax deficiencies were recognized either as an offset to accumulated excess tax benefits or in the income statement if there were no accumulated excess tax benefits. For the six months ended June 30, 2018 and July 1, 2017, the application of ASU No. 2016-09 reduced income tax expense by approximately \$0.9 million and \$19.3 million, respectively.

On December 22, 2017, the U.S. government passed the Tax Cuts and Jobs Act (the “Tax Act”). The Tax Act is comprehensive tax legislation effective January 1, 2018 that implements complex changes to the U.S tax code including, but not limited to, the reduction of the corporate tax rate from 35% to 21%, modification of accelerated depreciation, the repeal of the domestic manufacturing deduction and changes to the limitations of the deductibility of interest. The Tax Act also includes provisions to tax global intangible low-taxed income (“GILTI”), Foreign Derived Intangible Income (“FDII”), a base erosion and anti-abuse tax (“BEAT”) that imposes tax on certain foreign related-party payments, and IRC Section 163(j) interest limitation (Interest Limitation). We are subject to the GILTI, FDII, BEAT and Interest Limitation provisions effective January 1, 2018. Under Topic 740, we have reasonably estimated the impact of each provision of the Tax Act on our effective tax rate, and as a result, we have recorded an estimate for the GILTI provision in our effective tax rate for the six months ended June 30, 2018. For the BEAT, FDII and Interest Limitation computations, we have not recorded an estimate in our effective tax rate for the six months ended June 30, 2018 because we currently estimate that these provisions of the Tax Act will not apply in 2018. Due to the complexity of the new GILTI tax rules and uncertainty of the application of the foreign tax credit rules in relation to GILTI, we have calculated GILTI based upon the law as we currently interpret it, and subsequent changes in law could cause us to revise our calculations in a later period.

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Due to the complexities of the Tax Act, the Staff of the U.S. Securities and Exchange Commission (the “SEC”) issued Staff Accounting Bulletin No. 118 (“SAB 118”) that requires us to record a provisional amount for any income tax effects of the Tax Act in accordance with Topic 740, to the extent that a reasonable estimate can be made. SAB 118 allows for a measurement period of up to one year after the enactment date of the Tax Act to finalize the recording of the related tax impacts.

As we continue to complete our analysis of the Tax Act, the ultimate impacts may differ from our estimates, possibly materially, due to additional guidance from the U.S. Department of Treasury, updates or changes in our assumptions, revision of accounting standards for income taxes or related interpretations and future information that may become available. In the fourth quarter of 2017, we recorded provisional amounts for income tax effects of the Tax Act that we could reasonably estimate. This included the one-time transition tax that we estimated to be \$140.0 million and a net deferred tax expense of \$3.0 million attributable to the revaluation of deferred tax assets and liabilities due to the lower enacted federal income tax rate of 21%. For the six months ended June 30, 2018, no material adjustments were recorded. If the information necessary to finalize and record the related tax impacts is available, we anticipate recording any resulting adjustments by the quarter ended September 29, 2018.

The total amount of unrecognized tax benefits as of June 30, 2018 was approximately \$102.2 million, of which \$80.9 million would affect the effective tax rate if recognized. It is expected that the amount of unrecognized tax benefits will change in the next 12 months; however, we do not expect the change to have a material impact on our consolidated financial statements.

The total amounts of interest and penalties, which are classified as a component of Other liabilities within our consolidated balance sheets, were approximately \$14.1 million and \$0.0, respectively, as of June 30, 2018.

In 2016, we reached a settlement on a portion of the IRS audit of tax years 2012 and 2013, and we filed a Mutual Agreement Procedure request with the IRS for assistance from the U.S. Competent Authority for an open Transfer Pricing issue which resulted in a partial settlement during the quarter ended December 30, 2017. During the quarter ended July 1, 2017, we filed a protest with the Appellate Division regarding the remaining open audit issues for the years 2012 and 2013. We do not expect this to have a material effect on our consolidated financial position, liquidity or results of operations.

**Note 13 – Derivatives and Hedging Activities**

We are exposed to market risks as well as changes in foreign currency exchange rates as measured against the U.S. dollar and each other, and changes to the credit risk. We attempt to minimize these risks by primarily using foreign currency forward contracts and by maintaining counter-party credit limits. These hedging activities provide only limited protection against currency exchange and credit risks. Factors that could influence the effectiveness of our hedging programs include currency markets and availability of hedging instruments and liquidity of the credit markets. All foreign currency forward contracts that we enter into are components of hedging programs and are entered into for the sole purpose of hedging an existing or anticipated currency exposure. We do not enter into such contracts for speculative purposes and we manage our credit risks by diversifying our counterparties, maintaining a strong balance sheet and having multiple sources of capital.

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(in thousands, except per share data)

**(unaudited)**

Fluctuations in the value of certain foreign currencies as compared to the U.S. dollar may positively or negatively affect our revenues, gross margins, operating expenses and retained earnings, all of which are expressed in U.S. dollars. Where we deem it prudent, we engage in hedging programs using primarily foreign currency forward contracts aimed at limiting the impact of foreign currency exchange rate fluctuations on earnings. We purchase short-term (i.e., 18 months or less) foreign currency forward contracts to protect against currency exchange risks associated with intercompany loans due from our international subsidiaries and the payment of merchandise purchases to our foreign suppliers. We do not hedge the translation of foreign currency profits into U.S. dollars, as we regard this as an accounting exposure, not an economic exposure. Our hedging activities have historically not had a material impact on our consolidated financial statements. Accordingly, additional disclosures related to derivatives and hedging activities required by ASC Topic 815 have been omitted.

**Note 14 – Stock-Based Compensation**

Our accompanying consolidated statements of income reflect pre-tax share-based compensation expense of \$14.6 million (\$11.0 million after-tax) and \$23.3 million (\$17.6 million after-tax) for the three and six months ended June 30, 2018, respectively, and \$10.9 million (\$7.8 million after-tax) and \$19.4 million (\$14.5 million after-tax) for the three and six months ended July 1, 2017, respectively.

Stock-based compensation represents the cost related to stock-based awards granted to employees and non-employee directors. We measure stock-based compensation at the grant date, based on the estimated fair value of the award, and recognize the cost (net of estimated forfeitures) as compensation expense on a straight-line basis over the requisite service period. Our stock-based compensation expense is reflected in selling, general and administrative expenses in our consolidated statements of income.

Stock-based awards are provided to certain employees and non-employee directors under the terms of our 2013 Stock Incentive Plan, as amended, and our 2015 Non-Employee Director Stock Incentive Plan (together, the “Plans”). The Plans are administered by the Compensation Committee of the Board of Directors. Prior to March 2009, awards under the Plans principally included a combination of at-the-money stock options and restricted stock/units. Since March 2009, equity-based awards have been granted solely in the form of restricted stock/units, with the exception of providing stock options to employees pursuant to certain pre-existing contractual obligations.

Grants of restricted stock/units are stock-based awards granted to recipients with specified vesting provisions. In the case of restricted stock, common stock is delivered on the date of grant, subject to vesting conditions. In the case of restricted stock units, common stock is generally delivered on or following satisfaction of vesting conditions. We issue restricted stock/units that vest solely based on the recipient's continued service over time (primarily four-year cliff vesting, except for grants made under the 2015 Non-Employee Director Stock Incentive Plan, which are primarily 12-month cliff vesting) and restricted stock/units that vest based on our achieving specified performance measurements and the recipient's continued service over time (primarily three-year cliff vesting).

With respect to time-based restricted stock/units, we estimate the fair value on the date of grant based on our closing stock price. With respect to performance-based restricted stock/units, the number of shares that ultimately vest and are received by the recipient is based upon our performance as measured against specified targets over a specified period, as determined by the Compensation Committee of the Board of Directors. Although there is no guarantee that performance targets will be achieved, we estimate the fair value of performance-based restricted stock/units based on our closing stock price at time of grant.



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The Plans provide for adjustments to the performance-based restricted stock/units targets for significant events, including, without limitation, acquisitions, divestitures, new business ventures, certain capital transactions (including share repurchases), restructuring costs, if any, certain litigation settlements or payments, if any, changes in accounting principles or in applicable laws or regulations and foreign exchange fluctuations. Over the performance period, the number of shares of common stock that will ultimately vest and be issued and the related compensation expense is adjusted upward or downward based upon our estimation of achieving such performance targets. The ultimate number of shares delivered to recipients and the related compensation cost recognized as an expense will be based on our actual performance metrics as defined under the Plans.

Total unrecognized compensation cost related to non-vested awards as of June 30, 2018 was \$106.6 million, which is expected to be recognized over a weighted-average period of approximately 2.4 years.

The following table summarizes stock option activity under the Plans during the six months ended June 30, 2018:

Outstanding at beginning of period .....	
Granted .....	
Exercised .....	
Forfeited .....	
Outstanding at end of period .....	
Options exercisable at end of period .....	

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The following tables summarize the activity of our non-vested restricted stock/units for the six months ended June 30, 2018:

Outstanding at beginning of period .....  
Granted .....  
Vested .....  
Forfeited .....  
Outstanding at end of period .....

Outstanding at beginning of period .....  
Granted .....  
Vested .....  
Forfeited .....  
Outstanding at end of period .....

**Note 15 – Supplemental Cash Flow Information**

Cash paid for interest and income taxes was:

	Six Months Ended
	June 30, 2018
Interest.....	\$32,000
Income taxes.....	142,000

During the six months ended June 30, 2018 and July 1, 2017, we had \$1.5 million and \$(1.3) million of non-cash net unrealized gains (losses) related to foreign currency hedging activities, respectively. During the first quarter of 2018, as part of a business acquisition, we increased our ownership in a subsidiary through a non-cash transaction of \$1.3 million.

**Note 16 – Legal Proceedings**

Beginning in January 2016, purported class action complaints were filed against Patterson Companies, Inc. (“Patterson”), Benco Dental Supply Co. (“Benco”) and Henry Schein, Inc. Although there were factual and legal variations among these complaints, each of these complaints alleges, among other things, that defendants conspired to fix prices, allocate customers and foreclose competitors by boycotting manufacturers, state dental associations and others that deal with defendants’ competitors. On February 9, 2016, the U.S. District Court for the Eastern District of New York ordered all of these actions, and all other actions filed thereafter asserting substantially similar claims against defendants, consolidated for pre-trial purposes. On February 26, 2016, a consolidated class action complaint was filed by Arnell Prato, D.D.S., P.L.L.C., d/b/a Down to Earth Dental, Evolution Dental Sciences, LLC, Howard M. May, DDS, P.C., Casey Nelson, D.D.S., Jim Peck, D.D.S., Bernard W. Kurek, D.M.D., Larchmont Dental Associates, P.C., and Keith Schwartz, D.M.D., P.A. (collectively, “putative class

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representatives”) in the U.S. District Court for the Eastern District of New York, entitled In re Dental Supplies Antitrust Litigation, Civil Action No. 1:16-CV-00696-BMC-GRB. In the consolidated class action complaint, putative class representatives allege a nationwide agreement among Henry Schein, Benco, Patterson and non-party Burkhart Dental Supply Company, Inc. (“Burkhart”) not to compete on price. The consolidated class action complaint asserts a single count under Section 1 of the Sherman Act, and seeks equitable relief, compensatory and treble damages, jointly and severally, and reasonable costs and expenses, including attorneys’ fees and expert fees. On February 22, 2018, plaintiffs moved to certify a class that, subject to certain exclusions, includes all private dental practices and laboratories that purchased dental supplies directly from Henry Schein, Patterson, Benco, Burkhart or any combination thereof, during the period beginning January 1, 2009 until March 31, 2016. That motion is currently pending. We intend to defend ourselves vigorously against these actions.

On August 31, 2012, Archer and White Sales, Inc. (“Archer”) filed a complaint against Henry Schein, Inc. as well as Danaher Corporation and its subsidiaries Instrumentarium Dental, Inc., Dental Equipment, LLC, Kavvo Dental Technologies, LLC and Dental Imaging Technologies Corporation (collectively, the “Danaher Defendants”) in the United States District Court for the Eastern District of Texas, Civil Action No. 2:12-CV-00572-JRG, styled as an antitrust action under Section 1 of the Sherman Act, and the Texas Free Enterprise Antitrust Act. Archer alleges a conspiracy between Henry Schein, an unnamed company and the Danaher Defendants to terminate or limit Archer’s distribution rights. On August 1, 2017, Archer filed an amended complaint, adding Patterson and Benco as defendants, and alleging that Henry Schein, Patterson, Benco and Burkhart conspired to fix prices and refused to compete with each other for sales of dental equipment to dental professionals and agreed to enlist their common suppliers, the Danaher Defendants, to join a price-fixing conspiracy and boycott by reducing the distribution territory of, and eventually terminating, their price-cutting competing distributor Archer. Archer seeks injunctive relief, and damages in an amount to be proved at trial, to be trebled with interest and costs, including attorneys’ fees, jointly and severally. On October 30, 2017, Archer filed a second amended complaint, to add additional allegations that it believes support its claims. The named parties and causes of action are the same as the August 1, 2017 amended complaint.

On October 1, 2012, we filed a motion for an order: (i) compelling Archer to arbitrate its claims against us; (2) staying all proceedings pending arbitration; and (3) joining the Danaher Defendants’ motion to arbitrate and stay. On May 28, 2013, the Magistrate Judge granted the motions to arbitrate and stayed proceedings pending arbitration. On June 10, 2013, Archer moved for reconsideration before the District Court judge. On December 7, 2016, the District Court Judge granted Archer’s motion for reconsideration and lifted the stay. Defendants appealed the District Court’s order. On December 21, 2017, the United States Court of Appeals for the Fifth Circuit affirmed the District Court’s order denying the motions to compel arbitration. On February 12, 2018, defendants filed an Application for Stay of Proceedings in the District Court in the Supreme Court of the United States, seeking to stay proceedings in the District Court pending a decision on defendants’ forthcoming petition for writ of certiorari. On March 2, 2018, the Supreme Court of the United States granted a stay of proceedings. On June 25, 2018, the Supreme Court of the United States granted defendants’ petition for writ of certiorari, pursuant to which it will review the lower court’s decision denying

our motion to compel arbitration. In the meantime, the trial court proceeding is stayed. We intend to defend ourselves vigorously against this action.

On August 17, 2017, IQ Dental Supply, Inc. (“IQ Dental”) filed a complaint in the United States District Court for the Eastern District of New York, entitled IQ Dental Supply, Inc. v. Henry Schein, Inc., Patterson Companies, Inc. and Benco Dental Supply Company, Case No. 2:17-cv-4834. Plaintiff alleges that it is a distributor of dental supplies and equipment, and sells dental products through an online dental distribution platform operated by SourceOne Dental (“SourceOne”). SourceOne had previously brought an antitrust lawsuit against Henry Schein, Patterson and Benco, which Henry Schein settled in the second quarter of 2017 and which is described in our prior filings with the SEC.

IQ Dental alleges, among other things, that defendants conspired to suppress competition from IQ Dental and SourceOne for the marketing, distribution and sale of dental supplies and equipment in the United States, and that

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defendants unlawfully agreed with one another to boycott dentists, manufacturers and state dental associations that deal with, or considered dealing with, plaintiff and SourceOne. Plaintiff claims that this alleged conduct constitutes unreasonable restraint of trade in violation of Section 1 of the Sherman Act, New York's Donnelly Act and the New Jersey Antitrust Act, and also makes pendant state law claims for tortious interference with prospective business relations, civil conspiracy and aiding and abetting. Plaintiff seeks injunctive relief, compensatory, treble and punitive damages, jointly and severally, and reasonable costs and expenses, including attorneys' fees and expert fees. On December 21, 2017, the District Court granted the defendants' motion to dismiss. On January 19, 2018, IQ Dental appealed the District Court's order. The appeal is pending. We intend to defend ourselves vigorously against this action.

On February 12, 2018, the United States Federal Trade Commission ("FTC") filed a complaint against Benco Dental Supply Co., Henry Schein, Inc. and Patterson Companies, Inc. The FTC alleges, among other things, that defendants violated U.S. antitrust laws by conspiring, and entering into an agreement, to refuse to provide discounts to or otherwise serve buying groups representing dental practitioners. The FTC alleges that defendants conspired in violation of Section 5 of the FTC Act. The complaint seeks equitable relief only and does not seek monetary damages. We deny the allegation that we conspired to refuse to provide discounts to or otherwise serve dental buying groups and intend to defend ourselves vigorously against this action. A hearing before an administrative law judge is scheduled for October 16, 2018. We believe this matter will not have a material adverse effect on our consolidated financial position, liquidity or results of operations.

On March 7, 2018, Joseph Salkowitz, individually and on behalf of all others similarly situated, filed a putative class action complaint for violation of the federal securities laws against Henry Schein, Inc., Stanley M. Bergman and Steven Paladino in the United States District Court for the Eastern District of New York, Case No. 1:18-cv-01428. The complaint seeks to certify a class consisting of all persons and entities who, subject to certain exclusions, purchased publicly traded Henry Schein securities from March 7, 2013 through February 12, 2018 (the "Class Period"). The complaint alleges, among other things, that the defendants made materially false and misleading statements about Henry Schein's business, operations and prospects during the Class Period, including matters relating to the issues in the antitrust class actions and the FTC action described above, thereby causing the plaintiff and members of the purported class to pay artificially inflated prices for Henry Schein securities. The complaint seeks unspecified monetary damages and a jury trial. Pursuant to the provisions of the Private Securities Litigation Reform Act of 1995 (the "PSLRA"), plaintiff's counsel published notice of the commencement of this action, and thereby provided notice of the 60-day period during which any putative class member could apply to be lead plaintiff under the PSLRA. The court appointed lead plaintiff and lead counsel on June 22, 2018 and recaptioned the putative class action as *In re Henry Schein, Inc. Securities Litigation*, under the same case number. Lead plaintiff intends to file a new complaint by September 14, 2018. We intend to defend ourselves vigorously against this action.

On May 3, 2018, a class action complaint, *Marion Diagnostic Center, LLC v. Dickinson, and Co.*, 3:18-cv-01509 (S.D. Ill), was filed in the Southern District of Illinois against Becton, Dickinson, and Co. ("Becton"); Vizient, Inc. ("Vizient"); Cardinal Health, Inc. ("Cardinal"); Owens & Minor Inc. ("O&M"); and Henry Schein, Inc. The complaint alleges that the defendants entered into a vertical conspiracy to force healthcare providers into long-term exclusionary

contracts that restrain trade in the nationwide markets for conventional and safety syringes and safety IV catheters and that inflate the prices of certain Becton products to above-competitive levels. The named plaintiffs seek to represent three separate classes consisting of all healthcare providers that purchased (i) Becton's conventional syringes, (ii) Becton's safety syringes, or (iii) Becton's safety catheters directly from Becton, Cardinal, O&M or Henry Schein on or after May 3, 2014. The complaint asserts a single count under Section 1 of the Sherman Act, and seeks equitable relief, compensatory and treble damages, jointly and severally, and reasonable costs and expenses, including attorneys' fees and expert fees. On June 15, 2018, an amended complaint was filed asserting the same allegations against the same parties and adding McKesson Medical-Surgical, Inc. as an additional defendant. We intend to defend ourselves vigorously against this action.

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On May 29, 2018, an amended complaint was filed in the MultiDistrict Litigation (MDL) proceeding In Re National Prescription Opiate Litigation (MDL No. 2804; Case No. 17-md-2804) in an action entitled The County of Summit, Ohio et al. v. Purdue Pharma, L.P., et al., Civil Action No. 1:18-op-45090-DAP, in the Northern District of Ohio, adding Henry Schein, Inc., Henry Schein Medical Systems, Inc. and others as defendants. Plaintiffs allege that pharmaceutical manufacturers of prescription opioid drugs engaged in a false advertising campaign to expand the market for such drugs and their own market share and that the entities in the supply chain (including Henry Schein, Inc. and Henry Schein Medical Systems, Inc.) reaped financial rewards by refusing to monitor and restrict the improper distribution of those drugs. Plaintiffs assert the following claims for relief against Henry Schein, Inc. and Henry Schein Medical Systems, Inc.: statutory public nuisance; common law absolute public nuisance; negligence; injury through criminal acts (R.C. 2307.60); unjust enrichment; and civil conspiracy. This case has been designated “Track 1” and is currently set for trial on March 18, 2019. We intend to defend ourselves vigorously against this action.

On July 3, 2018, the City of Barberton, Ohio (and related entities) filed a complaint in the same MDL proceeding (MDL No. 2804; Case No. 17-md-2804) in an action entitled City of Barberton, et al. v. Purdue Pharma, L.P., et al., Civil Action No. 1:18-op-45767-DAP, in the Northern District of Ohio, against Henry Schein, Inc., Henry Schein Medical Systems, Inc. and others, that is similar to The County of Summit complaint. We intend to defend ourselves vigorously against this action.

From time to time, we may become a party to other legal proceedings, including, without limitation, product liability claims, employment matters, commercial disputes, governmental inquiries and investigations (which may in some cases involve our entering into settlement arrangements or consent decrees), and other matters arising out of the ordinary course of our business. While the results of any legal proceeding cannot be predicted with certainty, in our opinion none of these other pending matters are currently anticipated to have a material adverse effect on our consolidated financial position, liquidity or results of operations.

As of June 30, 2018, we had accrued our best estimate of potential losses relating to claims that were probable to result in liability and for which we were able to reasonably estimate a loss. This accrued amount, as well as related expenses, was not material to our financial position, results of operations or cash flows. Our method for determining estimated losses considers currently available facts, presently enacted laws and regulations and other factors, including probable recoveries from third parties.





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ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

Cautionary Note Regarding Forward-Looking Statements

In accordance with the "Safe Harbor" provisions of the Private Securities Litigation Reform Act of 1995, we provide the following cautionary remarks regarding important factors that, among others, could cause future results to differ materially from the forward-looking statements, expectations and assumptions expressed or implied herein. All forward-looking statements made by us are subject to risks and uncertainties and are not guarantees of future performance. These forward-looking statements involve known and unknown risks, uncertainties and other factors that may cause our actual results, performance and achievements or industry results to be materially different from any future results, performance or achievements expressed or implied by such forward-looking statements. These statements are identified by the use of such terms as "may," "could," "expect," "intend," "believe," "plan," "estimate," "forecast," "project," "anticipate" or other comparable terms.

Risk factors and uncertainties that could cause actual results to differ materially from current and historical results include, but are not limited to: effects of a highly competitive and consolidating market; our dependence on third parties for the manufacture and supply of our products; our dependence upon sales personnel, customers, suppliers and manufacturers; our dependence on our senior management; fluctuations in quarterly earnings; risks from expansion of customer purchasing power and multi-tiered costing structures; increases in shipping costs for our products or other service issues with our third-party shippers; general global macro-economic conditions; risks associated with currency fluctuations; risks associated with political and economic uncertainty; disruptions in financial markets; volatility of the market price of our common stock; changes in the health care industry; implementation of health care laws; failure to comply with regulatory requirements and data privacy laws; risks associated with our global operations; transitional challenges associated with acquisitions and joint ventures, including the failure to achieve anticipated synergies; financial risks associated with acquisitions and joint ventures; litigation risks; new or unanticipated litigation developments; the dependence on our continued product development, technical support and successful marketing in the technology segment; our dependence on third parties for certain technologically advanced components; increased competition by third party online commerce sites; risks from disruption to our information systems; cyberattacks or other privacy or data security breaches; certain provisions in our governing documents that may discourage third-party acquisitions of us; changes in tax legislation; and risks associated with the ability to consummate the spin-off and merger of our Animal Health business with Direct Vet Marketing, Inc. (d/b/a Vets First Choice) and the timing of the closing of such transaction, as well as the ability to realize anticipated benefits and synergies of the transaction. The order in which these factors appear should not be construed to indicate their relative importance or priority.

We caution that these factors may not be exhaustive and that many of these factors are beyond our ability to control or predict. Accordingly, any forward-looking statements contained herein should not be relied upon as a prediction of actual results. We undertake no duty and have no obligation to update forward-looking statements.

## Where You Can Find Important Information

We may disclose important information through one or more of the following channels: SEC filings, public conference calls and webcasts, press releases, the investor relations page of our website ([www.henryschein.com](http://www.henryschein.com)) and the social media channels identified on the Newsroom page of our website.

## Recent Developments

### Common Stock Authorized

Effective May 31, 2018, as a result of the 2-for-1 stock split that became effective on September 15, 2017, we increased our authorized common shares from 240,000,000 to 480,000,000.

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## Executive-Level Overview

We believe we are the world's largest provider of health care products and services primarily to office-based dental, animal health and medical practitioners. We serve more than 1 million customers worldwide including dental practitioners and laboratories, animal health clinics and physician practices, as well as government, institutional health care clinics and other alternate care clinics. We believe that we have a strong brand identity due to our more than 86 years of experience distributing health care products.

We are headquartered in Melville, New York, employ more than 22,000 people (of which more than 12,000 are based outside the United States) and have operations or affiliates in 34 countries, including the United States, Australia, Austria, Belgium, Brazil, Canada, Chile, China, the Czech Republic, Denmark, France, Germany, Hong Kong SAR, Ireland, Israel, Italy, Japan, Liechtenstein, Luxembourg, Malaysia, the Netherlands, New Zealand, Norway, Poland, Portugal, Romania, Slovakia, South Africa, Spain, Sweden, Switzerland, Thailand, United Arab Emirates and the United Kingdom.

We have established strategically located distribution centers to enable us to better serve our customers and increase our operating efficiency. This infrastructure, together with broad product and service offerings at competitive prices, and a strong commitment to customer service, enables us to be a single source of supply for our customers' needs. Our infrastructure also allows us to provide convenient ordering and rapid, accurate and complete order fulfillment.

We conduct our business through two reportable segments: (i) health care distribution and (ii) technology and value-added services. These segments offer different products and services to the same customer base.

The health care distribution reportable segment aggregates our global dental, animal health and medical operating segments. This segment distributes consumable products, small equipment, laboratory products, large equipment, equipment repair services, branded and generic pharmaceuticals, vaccines, surgical products, diagnostic tests, infection-control products and vitamins. Our global dental group serves office-based dental practitioners, dental laboratories, schools and other institutions. Our global animal health group serves animal health practices and clinics. Our global medical group serves office-based medical practitioners, ambulatory surgery centers, other alternate-care settings and other institutions.

Our global technology and value-added services group provides software, technology and other value-added services to health care practitioners. Our technology group offerings include practice management software systems for dental and medical practitioners and animal health clinics. Our value-added practice solutions include financial services on a non-recourse basis, e-services, practice technology, network and hardware services, as well as continuing education

services for practitioners.

# Industry Overview

In recent years, the health care industry has increasingly focused on cost containment. This trend has benefited distributors capable of providing a broad array of products and services at low prices. It also has accelerated the growth of HMOs, group practices, other managed care accounts and collective buying groups, which, in addition to their emphasis on obtaining products at competitive prices, tend to favor distributors capable of providing specialized management information support. We believe that the trend towards cost containment has the potential to favorably affect demand for technology solutions, including software, which can enhance the efficiency and facilitation of practice management.

Our operating results in recent years have been significantly affected by strategies and transactions that we undertook to expand our business, domestically and internationally, in part to address significant changes in the health care industry, including consolidation of health care distribution companies, health care reform, trends toward managed care, cuts in Medicare and collective purchasing arrangements.

Our current and future results have been and could be impacted by the current economic environment and uncertainty, particularly impacting overall demand for our products and services.

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## Industry Consolidation

The health care products distribution industry, as it relates to office-based health care practitioners, is fragmented and diverse. This industry, which encompasses the dental, animal health and medical markets, was estimated to produce revenues of approximately \$45 billion in 2018 in the global markets. The industry ranges from sole practitioners working out of relatively small offices to group practices or service organizations ranging in size from a few practitioners to a large number of practitioners who have combined or otherwise associated their practices.

Due in part to the inability of office-based health care practitioners to store and manage large quantities of supplies in their offices, the distribution of health care supplies and small equipment to office-based health care practitioners has been characterized by frequent, small quantity orders, and a need for rapid, reliable and substantially complete order fulfillment. The purchasing decisions within an office-based health care practice are typically made by the practitioner or an administrative assistant. Supplies and small equipment are generally purchased from more than one distributor, with one generally serving as the primary supplier.

The trend of consolidation extends to our customer base. Health care practitioners are increasingly seeking to partner, affiliate or combine with larger entities such as hospitals, health systems, group practices or physician hospital organizations. In many cases, purchasing decisions for consolidated groups are made at a centralized or professional staff level; however, orders are delivered to the practitioners' offices.

We believe that consolidation within the industry will continue to result in a number of distributors, particularly those with limited financial, operating and marketing resources, seeking to combine with larger companies that can provide growth opportunities. This consolidation also may continue to result in distributors seeking to acquire companies that can enhance their current product and service offerings or provide opportunities to serve a broader customer base.

Our trend with regard to acquisitions and joint ventures has been to expand our role as a provider of products and services to the health care industry. This trend has resulted in our expansion into service areas that complement our existing operations and provide opportunities for us to develop synergies with, and thus strengthen, the acquired businesses.

As industry consolidation continues, we believe that we are positioned to capitalize on this trend, as we believe we have the ability to support increased sales through our existing infrastructure, although there can be no assurances that we will be able to successfully accomplish this. We also have invested in expanding our sales/marketing infrastructure to include a focus on building relationships with decision makers who do not reside in the office-based practitioner setting.



As the health care industry continues to change, we continually evaluate possible candidates for merger and joint venture or acquisition and intend to continue to seek opportunities to expand our role as a provider of products and services to the health care industry. There can be no assurance that we will be able to successfully pursue any such opportunity or consummate any such transaction, if pursued. If additional transactions are entered into or consummated, we would incur merger and/or acquisition-related costs, and there can be no assurance that the integration efforts associated with any such transaction would be successful.

#### Aging Population and Other Market Influences

The health care products distribution industry continues to experience growth due to the aging population, increased health care awareness, the proliferation of medical technology and testing, new pharmacology treatments and expanded third-party insurance coverage. In addition, the physician market continues to benefit from the shift of procedures and diagnostic testing from acute care settings to alternate-care sites, particularly physicians' offices.

According to the U.S. Census Bureau's International Data Base, in 2018 there were more than six million Americans aged 85 years or older, the segment of the population most in need of long-term care and elder-care

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services. By the year 2050, that number is projected to nearly triple to approximately 19 million. The population aged 65 to 84 years is projected to increase approximately 50% during the same time period.

As a result of these market dynamics, annual expenditures for health care services continue to increase in the United States. We believe that demand for our products and services will grow, while continuing to be impacted by current and future operating, economic and industry conditions. The Centers for Medicare and Medicaid Services, or CMS, published “National Health Expenditure Projections 2017-2026” indicating that total national health care spending reached approximately \$3.5 trillion in 2017, or 18.0% of the nation’s gross domestic product, the benchmark measure for annual production of goods and services in the United States. Health care spending is projected to reach approximately \$5.7 trillion in 2026, approximately 19.7% of the nation’s gross domestic product.

### Government

Certain of our businesses involve the distribution of pharmaceuticals and medical devices, and in this regard we are subject to extensive local, state, federal and foreign governmental laws and regulations applicable to the distribution and sale of pharmaceuticals and medical devices. Additionally, government and private insurance programs fund a large portion of the total cost of medical care, and there has been an emphasis on efforts to control medical costs, including laws and regulations lowering reimbursement rates for pharmaceuticals, medical devices, and/or medical treatments or services. Also, many of these laws and regulations are subject to change and may impact our financial performance. In addition, our businesses are generally subject to numerous other laws and regulations that could impact our financial performance, including securities, antitrust, anti-bribery and anti-kickback, customer interaction transparency, data privacy, data security and other laws and regulations. Failure to comply with law or regulations could have a material adverse effect on our business.

### Health Care Reform

The United States Patient Protection and Affordable Care Act as amended by the Health Care and Education Reconciliation Act, each enacted in March 2010 (the “Health Care Reform Law”), increased federal oversight of private health insurance plans and included a number of provisions designed to reduce Medicare expenditures and the cost of health care generally, to reduce fraud and abuse, and to provide access to increased health coverage.

The Health Care Reform Law requirements include a 2.3% excise tax on domestic sales of many medical devices by manufacturers and importers that began in 2013 and a fee on branded prescription drugs and biologics that was implemented in 2011, both of which may affect sales. However, with respect to the medical device excise tax, a two-year moratorium was imposed under the Consolidated Appropriations Act, 2016, suspending the imposition of the tax on device sales during the period beginning January 1, 2016 and ending on December 31, 2017, and on

### Industry Consolidation

January 22, 2018 an additional two-year moratorium was imposed under Public Law No. 115-120, suspending the imposition of the tax on device sales during the period beginning January 1, 2018 and ending on December 31, 2019. The Health Care Reform Law has also materially expanded the number of individuals in the United States with health insurance. The Health Care Reform Law has faced ongoing legal challenges, including litigation seeking to invalidate some of or all of the law or the manner in which it has been implemented. In addition, the President is seeking to repeal and replace the Health Care Reform Law and has taken a number of administrative actions to materially weaken it, including, without limitation, by permitting the use of less robust health plans with lower coverage and eliminating “premium support” for insurers providing policies under the Health Care Reform Law. On December 22, 2017, the President signed into law the Tax Cuts and Jobs Act, which contains a broad range of tax reform provisions that impact the individual and corporate tax rates, international tax provisions, income tax add-back provisions and deductions, and which also repealed the individual mandate of the Health Care Reform Law. The uncertain status of the Health Care Reform Law affects our ability to plan.

A Health Care Reform Law provision, generally referred to as the Physician Payment Sunshine Act or Open Payments Program, has imposed reporting and disclosure requirements for drug and device manufacturers and distributors with regard to payments or other transfers of value made to certain covered recipients (including physicians, dentists and teaching hospitals), and for such manufacturers and distributors and for group purchasing organizations, with regard to certain ownership interests held by physicians in the reporting entity. CMS publishes information from these reports on a publicly available website, including amounts transferred and physician, dentist and teaching hospital identities.

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Under the Physician Payment Sunshine Act, we are required to collect and report detailed information regarding certain financial relationships we have with physicians, dentists and teaching hospitals. We believe that we are substantially compliant with applicable Physician Payment Sunshine Act requirements. The Physician Payment Sunshine Act pre-empts similar state reporting laws, although we or our subsidiaries may be required to report under certain state transparency laws that address circumstances not covered by the Physician Payment Sunshine Act, and some of these state laws, as well as the federal law, can be ambiguous. We are also subject to foreign regulations requiring transparency of certain interactions between suppliers and their customers. While we believe we have substantially compliant programs and controls in place to comply with these requirements, our compliance with these rules imposes additional costs on us.

Another notable Medicare health care reform initiative, the Medicare Access and CHIP Reauthorization Act of 2015 (“MACRA”), enacted on April 16, 2015, establishes a new payment framework, called the Quality Payment Program, which modifies certain Medicare payments to “eligible clinicians,” including physicians, dentists and other practitioners. Under MACRA, eligible clinicians are required to participate in Medicare through the Merit-Based Incentive Payment System (“MIPS”) or Advanced Alternative Payment Models (“APMs”). MIPS generally consolidated three programs; the physician quality reporting system, the value-based payment modifier and the Medicare electronic health record (“EHR”) program, into a single program in which Medicare reimbursement to eligible clinicians includes both positive and negative payment adjustments that take into account quality, resource use, clinical practice improvement and meaningful use of certified EHR technology. Advanced APMs generally involve higher levels of financial and technology risk. A final rule was published in the Federal Register on November 4, 2016 and allows eligible Medicare clinicians to pick their pace of participation for the first performance period that began January 1, 2017. The data collected in the first performance year will determine payment adjustments beginning January 1, 2019. A final rule updating certain Quality Payment Program regulations was published on November 16, 2017, which became effective as of January 1, 2018. MACRA represents a fundamental change in physician reimbursement that is expected to provide substantial financial incentives for physicians to participate in risk contracts, and to increase physician information technology and reporting obligations. The implications of the implementation of MACRA are uncertain and will depend on future regulatory activity and physician activity in the marketplace. MACRA may encourage physicians to move from smaller practices to larger physician groups or hospital employment, leading to a consolidation of a portion of our customer base. Although we believe that we are positioned to capitalize on this consolidation trend, there can be no assurances that we will be able to successfully accomplish this.

Health Care Fraud

Certain of our businesses are subject to federal and state (and similar foreign) health care fraud and abuse, referral and reimbursement laws and regulations with respect to their operations. Some of these laws, referred to as “false claims laws,” prohibit the submission or causing the submission of false or fraudulent claims for reimbursement to federal, state and other health care payers and programs. Other laws, referred to as “anti-kickback laws,” prohibit soliciting, offering, receiving or paying remuneration in order to induce the referral of a patient or ordering, purchasing, leasing or arranging for, or recommending ordering, purchasing or leasing of, items or services that are paid for by federal,

state and other health care payers and programs.

The fraud and abuse laws and regulations have been subject to varying interpretations and significant enforcement activity has been the result of “relators,” who serve as whistleblowers by filing complaints in the name of the United States (and if applicable, particular states) under federal and state false claims laws. Under the federal False Claims Act, relators can be entitled to receive up to 30% of total recoveries. Violations of the federal False Claims Act can result in treble damages, and, in accordance with a final rule published by the Department of Justice on January 29, 2018, civil penalties will generally range from a minimum of \$11,181 to a maximum of \$22,363 per claim. In addition, the Bipartisan Budget Act of 2018, signed into law on February 9, 2018, revised the penalties imposed for violations of the Anti-Kickback Law. Civil penalties may include fines of up to \$100,000 for each violation, plus up to three times the total amount of remuneration offered, paid, solicited or received, and exclusion from federal health care programs. Maximum criminal penalties have been increased from \$25,000 to \$100,000, and maximum prison time has doubled from five years to ten years.

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Most states have adopted similar state false claims laws, and these state laws have their own penalties which may be in addition to federal False Claims Act penalties. The Health Care Reform Law significantly strengthened the federal False Claims Act and the federal Anti-Kickback Law provisions, which could lead to the possibility of increased whistleblower or relator suits, and among other things made clear that a federal Anti-Kickback Law violation can be a basis for federal False Claims Act liability.

The United States government (among others) has expressed concerns about financial relationships between suppliers on the one hand and physicians and dentists on the other. As a result, we regularly review and revise our marketing practices as necessary to facilitate compliance.

We also are subject to certain United States and foreign laws and regulations concerning the conduct of our foreign operations, including the U.S. Foreign Corrupt Practices Act, the U.K. Bribery Act, German anti-corruption laws and other anti-bribery laws and laws pertaining to the accuracy of our internal books and records, which have been the focus of increasing enforcement activity globally in recent years.

Failure to comply with fraud and abuse laws and regulations could result in significant civil and criminal penalties and costs, including the loss of licenses and the ability to participate in federal and state health care programs, and could have a material adverse effect on our business. Also, these measures may be interpreted or applied by a prosecutorial, regulatory or judicial authority in a manner that could require us to make changes in our operations or incur substantial defense and settlement expenses. Even unsuccessful challenges by regulatory authorities or private relators could result in reputational harm and the incurring of substantial costs. In addition, many of these laws are vague or indefinite and have not been interpreted by the courts, and have been subject to frequent modification and varied interpretation by prosecutorial and regulatory authorities, increasing the risk of noncompliance.

While we believe that we are substantially compliant with applicable fraud and abuse laws and regulations, and have adequate compliance programs and controls in place to ensure substantial compliance, we cannot predict whether changes in applicable law, or interpretation of laws, or changes in our services or marketing practices in response to changes in applicable law or interpretation of laws, could have a material adverse effect on our business.

Operating, Security and Licensure Standards

Certain of our businesses involve the distribution of pharmaceuticals and medical devices, and in this regard we are subject to various local, state, federal and foreign governmental laws and regulations applicable to the distribution of pharmaceuticals and medical devices. Among the United States federal laws applicable to us are the Controlled Substances Act, the Federal Food, Drug, and Cosmetic Act, as amended (“FDC Act”), and Section 361 of the Public Health Service Act. We are also subject to comparable foreign regulations.

The FDC Act and similar foreign laws generally regulate the introduction, manufacture, advertising, labeling, packaging, storage, handling, reporting, marketing and distribution of, and record keeping for, pharmaceuticals and medical devices shipped in interstate commerce, and states may similarly regulate such activities within the state. Section 361 of the Public Health Service Act, which provides authority to prevent the spread of communicable diseases, serves as the legal basis for the United States Food and Drug Administration's ("FDA") regulation of human cells, tissues and cellular and tissue-based products, also known as "HCT/P products."

The Federal Drug Quality and Security Act of 2013 brought about significant changes with respect to pharmaceutical supply chain requirements and pre-empts state law. Title II of this measure, known as the Drug Supply Chain Security Act ("DSCSA"), is being phased in over a period of ten years, and is intended to build a national electronic, interoperable system to identify and trace certain prescription drugs as they are distributed in the United States. The law's track and trace requirements applicable to manufacturers, wholesalers, repackagers and dispensers (e.g., pharmacies) of prescription drugs took effect in January 2015, and continues to be implemented. The DSCSA product tracing requirements replace the former FDA drug pedigree requirements and pre-empt state requirements that are inconsistent with, more stringent than, or in addition to, the DSCSA requirements.

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The DSCSA also establishes certain requirements for the licensing and operation of prescription drug wholesalers and third party logistics providers (“3PLs”), and includes the eventual creation of national wholesaler and 3PL licenses in cases where states do not license such entities. The DSCSA requires that wholesalers and 3PLs distribute drugs in accordance with certain standards regarding the recordkeeping, storage and handling of prescription drugs. According to FDA guidance, states are pre-empted from imposing any licensing requirements that are inconsistent with, less stringent than, directly related to, or covered by the standards established by federal law in this area. Current state licensing requirements will likely remain in effect until the FDA issues new regulations as directed by the DSCSA.

We believe that we are substantially compliant with applicable DSCSA requirements.

The Food and Drug Administration Amendments Act of 2007 and the Food and Drug Administration Safety and Innovation Act of 2012 amended the FDC Act to require the FDA to promulgate regulations to implement a unique device identification (“UDI”) system. The FDA is phasing in the implementation of the UDI regulations over seven years, generally beginning with the highest-risk devices (i.e., Class III medical devices) and ending with the lowest-risk devices. Most compliance dates will have been reached as of September 24, 2018, with a final set of requirements for low risk devices being reached on September 24, 2020, which will complete the phase in. The UDI regulations require “labelers” to include unique device identifiers (“UDIs”), with a content and format prescribed by the FDA and issued under a system operated by an FDA-accredited issuing agency, on the labels and packages of medical devices, and to directly mark certain devices with UDIs. The UDI regulations also require labelers to submit certain information concerning UDI-labeled devices to the FDA, much of which information is publicly available on an FDA database, the Global Unique Device Identification Database. The UDI regulations provide for certain exceptions, alternatives and time extensions. For example, the UDI regulations include a general exception for Class I devices exempt from the Quality System Regulation (other than record-keeping requirements and complaint files). Regulated labelers include entities such as device manufacturers, repackagers, reproducers and relabelers that cause a device’s label to be applied or modified, with the intent that the device will be commercially distributed without any subsequent replacement or modification of the label, and include certain of our businesses.

We believe that we are substantially compliant with applicable UDI requirements.

Under the Controlled Substances Act, as a distributor of controlled substances, we are required to obtain and renew annually registrations for our facilities from the United States Drug Enforcement Administration (“DEA”) permitting us to handle controlled substances. We are also subject to other statutory and regulatory requirements relating to the storage, sale, marketing, handling and distribution of such drugs, in accordance with the Controlled Substances Act and its implementing regulations, and these requirements have been subject to heightened enforcement activity in recent times. We are subject to inspection by the DEA.



Certain of our businesses are also required to register for permits and/or licenses with, and comply with operating and security standards of, the DEA, the FDA, the United States Department of Health and Human Services, and various state boards of pharmacy, state health departments and/or comparable state agencies as well as comparable foreign agencies, and certain accrediting bodies depending on the type of operations and location of product distribution, manufacturing or sale. These businesses include those that distribute, manufacture and/or repackage prescription pharmaceuticals and/or medical devices and/or HCT/P products, or own pharmacy operations, or install, maintain or repair equipment. In addition, Section 301 of the National Organ Transplant Act, and a number of comparable state laws, impose civil and/or criminal penalties for the transfer of certain human tissue (for example, human bone products) for valuable consideration, while generally permitting payments for the reasonable costs incurred in procuring, processing, storing and distributing that tissue. We are also subject to foreign government regulation of such products. The DEA, the FDA and state regulatory authorities have broad inspection and enforcement powers, including the ability to suspend or limit the distribution of products by our distribution centers, seize or order the recall of products and impose significant criminal, civil and administrative sanctions for violations of these laws and regulations. Foreign regulations subject us to similar foreign enforcement powers. Furthermore, compliance with legal requirements has required and may in the future require us to institute voluntary recalls of products we sell, which could result in financial losses and potential reputational harm. Our

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customers are also subject to significant federal, state, local and foreign governmental regulation.

Certain of our businesses are subject to various additional federal, state, local and foreign laws and regulations, including with respect to the sale, transportation, storage, handling and disposal of hazardous or potentially hazardous substances, and safe working conditions.

Certain of our businesses also maintain contracts with governmental agencies and are subject to certain regulatory requirements specific to government contractors.

Antitrust

The U.S. federal government, most U.S. states and many foreign countries have antitrust laws that prohibit certain types of conduct deemed to be anti-competitive. Violations of antitrust laws can result in various sanctions, including criminal and civil penalties. Private plaintiffs also could bring civil lawsuits against us in the United States for alleged antitrust law violations, including claims for treble damages.

Regulated Software and Data Processing; Electronic Health Records

The FDA has become increasingly active in addressing the regulation of computer software intended for use in health care settings, and has developed and continues to develop policies on regulating clinical decision support tools and other types of software as medical devices. Certain of our businesses involve the development and sale of software and related products to support physician and dental practice management, and it is possible that the FDA or foreign government authorities could determine that one or more of our products is a medical device, which could subject us or one or more of our businesses to substantial additional requirements with respect to these products.

In addition, the European Parliament and the Council of the European Union have adopted a new pan-European General Data Protection Regulation (“GDPR”), effective from May 25, 2018, which increases privacy rights for individuals in Europe, extends the scope of responsibilities for data controllers and data processors and imposes increased requirements and potential penalties on companies offering goods or services to individuals who are located in Europe (“Data Subjects”) or monitoring the behavior of such individuals (including by companies based outside of Europe). Noncompliance can result in penalties of up to the greater of EUR 20 million, or 4% of global company revenues. Individual member states may impose additional requirements and penalties as they relate to certain things such as employee personal data. Among other things, the GDPR requires with respect to data concerning Data Subjects, company accountability, consents from Data Subjects or other acceptable legal basis needed to process the

personal data, prompt breach notifications within 72 hours, fairness and transparency in how the personal data is stored, used or otherwise processed, and data integrity and security, and provides rights to Data Subjects relating to modification, erasure and transporting of the personal data. While we believe that we have substantially compliant programs and controls in place to comply with the GDPR requirements, our compliance with the new regulation is likely to impose additional costs on us, and we cannot predict whether the interpretations of the requirements, or changes in our practices in response to new requirements or interpretations of the requirements, could have a material adverse effect on our business.

We also sell products and services that health care providers, such as physicians and dentists, use to store and manage patient medical or dental records. These customers are subject to laws, regulations and industry standards, such as HIPAA and the Payment Card Industry Data Security Standards, which require that they protect the privacy and security of those records, and our products may be used as part of these customers' comprehensive data security programs, including in connection with their efforts to comply with applicable privacy and security laws. Perceived or actual security vulnerabilities in our products or services, or the perceived or actual failure by us or our customers who use our products to comply with applicable legal or contractual requirements, may not only cause us significant reputational harm, but may also lead to claims against us by our customers and/or governmental agencies and involve substantial fines, penalties and other liabilities and expenses and costs for remediation.

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Federal initiatives provide programs of incentive payments available to certain health care providers involving the adoption and use of certain electronic health care records systems and processes. These programs, now generally known as the Promoting Interoperability Programs, include providing, among others, physicians and dentists, with financial incentives if they use certified EHR technology in accordance with applicable and evolving requirements. These requirements involve measurements of quality, promoting interoperability, improvement activities and improving patient access to health information. Qualification for the incentive payments requires the use of EHRs that have certain capabilities pursuant to evolving standards adopted by CMS and by the Office of the National Coordinator for Health Information Technology (“ONC”) of the Department of Health and Human Services (“HHS”). The use of certified EHR technology will also continue as a feature of MACRA’s MIPS program. The first performance period for MIPS began January 1, 2017, and will afford eligible clinicians different reporting options linked to the amount of data reported and the duration of the reporting period, with positive payment adjustments generally linked to more robust reporting.

Certain of our businesses involve the manufacture and sale of certified EHR systems and other products linked to incentive programs. CMS and ONC establish criteria for certified EHR systems, and these criteria have been subject to change. In order to maintain certification of our EHR products, we must satisfy these changing governmental criteria. If any of our EHR systems do not meet these standards, yet have been relied upon by health care providers to receive federal incentive payments, as noted above, we are exposed to risk under federal health care fraud and abuse laws, such as the False Claims Act. For example, on May 31, 2017, the U.S. Department of Justice announced a \$155 million settlement and 5-year corporate integrity agreement involving a vendor of certified EHR systems, based on allegations that the vendor, by misrepresenting capabilities to the certifying body, caused its health care provider customers to submit false Medicare and Medicaid claims for meaningful use payments in violation of the False Claims Act. While we believe we are substantially in compliance with such certifications and with applicable fraud and abuse laws and regulations, and we have adequate compliance programs and controls in place to ensure substantial compliance, we cannot predict whether changes in applicable law, or interpretation of laws, or changes in our practices in response to changes in applicable law or interpretation of laws, could have a material adverse effect on our business. Moreover, in order to satisfy our customers, our products may need to incorporate increasingly complex reporting functionality. Although we believe we are positioned to accomplish this, the effort may involve increased costs, and our failure to implement product modifications, or otherwise satisfy applicable standards, could have a material adverse effect on our business.

Other health information standards, such as regulations under HIPAA, establish standards regarding electronic health data transmissions and transaction code set rules for specific electronic transactions, such as transactions involving claims submissions to third party payers. Certain of our businesses provide electronic practice management products that must meet these requirements. Failure to abide by electronic health data transmission standards could expose us to breach of contract claims, substantial fines, penalties, and other liabilities and expenses, costs for remediation and harm to our reputation.

Additionally, as electronic medical devices are increasingly connected to each other and to other technology, the ability of these connected systems safely and effectively to exchange and use exchanged information becomes increasingly important. On September 6, 2017, the FDA issued guidance to assist in identifying specific considerations related to the ability of electronic medical devices to safely and effectively exchange and use

exchanged information. As a medical device manufacturer, we must manage risks including those associated with an electronic interface that is incorporated into a medical device.

There may be additional legislative initiatives in the future impacting health care.

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E-Commerce

Electronic commerce solutions have become an integral part of traditional health care supply and distribution relationships. Our distribution business is characterized by rapid technological developments and intense competition. The continuing advancement of online commerce requires us to cost-effectively adapt to changing technologies, to enhance existing services and to develop and introduce a variety of new services to address the changing demands of consumers and our customers on a timely basis, particularly in response to competitive offerings.

Through our proprietary, technologically based suite of products, we offer customers a variety of competitive alternatives. We believe that our tradition of reliable service, our name recognition and large customer base built on solid customer relationships, position us well to participate in this significant aspect of the distribution business. We continue to explore ways and means to improve and expand our Internet presence and capabilities, including our online commerce offerings and our use of various social media outlets.

Table of Contents**Results of Operations**

The following table summarizes the significant components of our operating results for the three and six months ended June 30, 2018 and July 1, 2017 and cash flows for the six months ended June 30, 2018 and July 1, 2017 (in thousands):

	Three Months June 30, 2018
Operating results:	
Net sales .....	\$3,326
Cost of sales .....	2,425
Gross profit .....	901,0
Operating expenses:	
Selling, general and administrative .....	677,2
Transaction costs related to Animal Health spin-off.....	7,611
Restructuring costs .....	14,89
Operating income .....	\$201,3
Other expense, net .....	\$(12,8
Net income .....	147,5
Net income attributable to Henry Schein, Inc. .....	141,2
Cash flows:	
Net cash provided by operating activities .....	
Net cash used in investing activities .....	
Net cash provided by (used in) financing activities .....	

**Plan of Restructuring**

On July 9, 2018, we committed to an initiative to rationalize our operations and provide expense efficiencies. These actions will allow us to execute on our plan to reduce our cost structure and fund new initiatives that will drive future

growth under our 2018 to 2020 strategic plan. This initiative is expected to include the elimination of approximately 2% to 3% of our workforce and the closing of certain facilities. The total 2018 costs associated with the actions to complete this restructuring are expected to be in the range of \$45 million to \$55 million pre-tax, or \$0.22 to \$0.27 per diluted share, consisting of \$40 million to \$45 million in employee severance pay and benefits and \$5 million to \$10 million in facility costs, representing primarily lease termination and other facility closure related costs.

During the three and six months ended June 30, 2018, we recorded restructuring costs of \$14.9 million and \$18.7 million, respectively, primarily for certain redundancies. The costs associated with these restructuring activities are included in a separate line item, "Restructuring costs" within our consolidated statements of income.



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Three Months Ended June 30, 2018 Compared to Three Months Ended July 1, 2017

Net Sales

Net sales for the three months ended June 30, 2018 and July 1, 2017 were as follows (in thousands):

Health care distribution (1):

Dental .....	
Animal health .....	
Medical .....	
Total health care distribution .....	

Technology and value-added services

(2).....	
Total .....	

(1) Consists of consumable products, small equipment, laboratory products, large equipment, equipment repair services, branded generic pharmaceuticals, vaccines, surgical products, diagnostic tests, infection-control products and vitamins.

(2) Consists of practice management software and other value-added products, which are distributed primarily to health care providers and financial services on a non-recourse basis, e-services, continuing education services for practitioners, consulting and other services.

The \$267.2 million, or 8.7%, increase in net sales for the three months ended June 30, 2018 includes an increase of 6.5% local currency growth (4.8% increase in internally generated revenue and 1.7% growth from acquisitions) as well as an increase of 2.2% related to foreign currency exchange.

The \$124.7 million, or 8.4%, increase in dental net sales for the three months ended June 30, 2018 includes an increase of 5.9% in local currency growth (4.4% increase in internally generated revenue and 1.5% growth from acquisitions) as well as an increase of 2.5% related to foreign currency exchange. The 5.9% increase in local currency sales was due to increases in dental equipment sales and service revenues of 5.7% (5.6% growth from internally generated revenue and 0.1% growth from acquisitions) and dental consumable merchandise sales growth of 6.0% (4.0% growth from internally generated revenue and 2.0% growth from acquisitions).

The \$94.6 million, or 10.6%, increase in animal health net sales for the three months ended June 30, 2018 includes an increase of 7.4% local currency growth (4.4% increase in internally generated revenue and 3.0% growth from acquisitions) as well as an increase of 3.2% related to foreign currency exchange. The local currency growth in animal health revenue is affected by the revenue for certain products being recognized on an agency basis in 2018 that had been recognized on a gross basis in the prior year. When excluding the effects of this change, internally generated revenue grew by 8.5%.

The \$42.6 million, or 7.5%, increase in medical net sales for the three months ended June 30, 2018 includes an increase of 7.2% local currency growth (7.0% increase in internally generated revenue and 0.2% growth from acquisitions) as well as an increase of 0.3% related to foreign currency exchange.

The \$5.3 million, or 4.9%, increase in technology and value-added services net sales for the three months ended June 30, 2018 includes an increase of 3.7% local currency growth (3.0% internally generated revenue and 0.7% growth from acquisitions) as well as an increase of 1.2% related to foreign currency exchange. The local currency growth in technology and value-added services revenue is affected by the revenue for certain products being recognized on an agency basis in 2018 that had been recognized on a gross basis in the prior year. When excluding the effects of this change, internally generated revenue grew by 3.4%.

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Gross Profit

Gross profit and gross margin percentages by segment and in total for the three months ended June 30, 2018 and July 1, 2017 were as follows (in thousands):

Health care distribution	20
.....	\$
Technology and value-added services	/
.....	\$
Total	.....

Gross profit increased \$61.9 million, or 7.4%, for the three months ended June 30, 2018, compared to the prior year period. As a result of different practices of categorizing costs associated with distribution networks throughout our industry, our gross margins may not necessarily be comparable to other distribution companies. Additionally, we realize substantially higher gross margin percentages in our technology segment than in our health care distribution segment. These higher gross margins result from being both the developer and seller of software products and services, as well as certain financial services. The software industry typically realizes higher gross margins to recover investments in research and development.

Within our health care distribution segment, gross profit margins may vary from one period to the next. Changes in the mix of products sold as well as changes in our customer mix have been the most significant drivers affecting our gross profit margin. For example, sales of pharmaceutical products are generally at lower gross profit margins than other products. Conversely, sales of our private label products achieve gross profit margins that are higher than average. With respect to customer mix, sales to our large-group customers are typically completed at lower gross margins due to the higher volumes sold as opposed to the gross margin on sales to office-based practitioners who normally purchase lower volumes at greater frequencies.

Health care distribution gross profit increased \$60.2 million, or 7.8%, for the three months ended June 30, 2018 compared to the prior year period. Health care distribution gross profit margin decreased to 25.8% for the three months ended June 30, 2018 from 26.0% for the comparable prior year period. The overall increase in our health care distribution gross profit is attributable to a \$54.2 million gross profit increase from growth in internally generated revenue and \$14.5 million is attributable to acquisitions. These increases were partially offset by a \$8.5 million decline in gross profit due to the decrease in the gross margin rates.

Technology and value-added services gross profit increased \$1.7 million, or 2.3%, for the three months ended June 30, 2018 compared to the prior year period. Technology and value-added services gross profit margin decreased to 64.3% for the three months ended June 30, 2018 from 65.9% for the comparable prior year period. Acquisitions accounted for \$0.3 million of our gross profit increase within our technology and value-added services segment for the three months ended June 30, 2018 compared to the prior year period. The remaining increase of \$1.4 million in our technology and value-added services segment gross profit was primarily attributable to growth in internally generated revenue.

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Selling, General and Administrative

Selling, general and administrative expenses by segment and in total for the three months ended June 30, 2018 and July 1, 2017 were as follows (in thousands):

Health care distribution	Ju
.....	20
Technology and value-added services	\$
.....	.
Total	\$

Selling, general and administrative expenses increased \$48.7 million, or 7.7%, for the three months ended June 30, 2018 from the comparable prior year period. The \$45.4 million increase in selling, general and administrative expenses within our health care distribution segment for the three months ended June 30, 2018 as compared to the prior year period was attributable to \$19.6 million of additional costs from acquired companies, and \$25.8 million of additional operating costs. The \$3.3 million increase in selling, general and administrative expenses within our technology and value-added services segment for the three months ended June 30, 2018 as compared to the prior year period was attributable to \$0.5 million of additional costs from acquired companies and \$2.8 million of additional operating costs. As a percentage of net sales, selling, general and administrative expenses decreased to 20.4% from 20.5% for the comparable prior year period.

As a component of total selling, general and administrative expenses, selling expenses increased \$34.7 million, or 9.1% to \$416.8 million, for the three months ended June 30, 2018 from the comparable prior year period. As a percentage of net sales, selling expenses remained consistent at 12.5%.

As a component of total selling, general and administrative expenses, general and administrative expenses increased \$14.0 million, or 5.7% to \$260.4 million, for the three months ended June 30, 2018 from the comparable prior year period. As a percentage of net sales, general and administrative expenses decreased to 7.8% from 8.1% for the comparable prior year period.

Other Expense, Net

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Other expense, net, for the three months ended June 30, 2018 and July 1, 2017 was as follows (in thousands):

	June 2018
Interest income .....	\$5,10
Interest expense .....	(17,
Other, net .....	(118
Other expense, net .....	\$(12,

Other expense, net increased \$5.5 million to \$12.9 million for the three months ended June 30, 2018 from the comparable prior year period. Interest income increased \$1.0 million primarily due to increased interest and late fee income. Interest expense increased \$5.7 million primarily due to increased borrowings under our bank credit lines and our private placement facilities, as well as higher interest rates.

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Income Taxes

For the three months ended June 30, 2018, our effective tax rate was 24.9% compared to 28.7% for the prior year period. The difference between our effective tax rate and the federal statutory tax rate for the three months ended June 30, 2018 primarily relates to state and foreign income taxes and interest expense. The difference between our effective tax rate and the federal statutory tax rate for the three months ended July 1, 2017 primarily relates to the adoption of Accounting Standards Update No. 2016-09, "Stock Compensation" (Topic 718) ("ASU 2016-09") in the first quarter of 2017, as well as state and foreign income taxes and interest expense.

Net Income

Net income decreased \$2.1 million, or 1.4%, for the three months ended June 30, 2018, compared to the prior year period due to the factors noted above.

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Six Months Ended June 30, 2018 Compared to Six Months Ended July 1, 2017

Net Sales

Net sales for the six months ended June 30, 2018 and July 1, 2017 were as follows (in thousands):

Health care distribution (1):

Dental .....  
 Animal health .....  
 Medical .....  
 Total health care distribution .....

Technology and value-added services

(2).....  
 Total .....

(1) Consists of consumable products, small equipment, laboratory products, large equipment, equipment repair services, brand generic pharmaceuticals, vaccines, surgical products, diagnostic tests, infection-control products and vitamins.

(2) Consists of practice management software and other value-added products, which are distributed primarily to health care practitioners and financial services on a non-recourse basis, e-services, continuing education services for practitioners, consulting and other services.

The \$564.7 million, or 9.4%, increase in net sales for the six months ended June 30, 2018 includes an increase of 6.2% in local currency growth (4.3% increase in internally generated revenue and 1.9% growth from acquisitions) as well as an increase of 3.2% related to foreign currency exchange.

The \$267.3 million, or 9.2%, increase in dental net sales for the six months ended June 30, 2018 includes an increase of 5.6% in local currency growth (3.7% increase in internally generated revenue and 1.9% growth from acquisitions) as well as an increase of 3.6% related to foreign currency exchange. The 5.6% increase in local currency sales was due to an increase in dental consumable merchandise sales growth of 5.9% (3.4% growth from internally generated revenue and 2.5% growth from acquisitions) and dental equipment sales and service revenues of 4.5% (4.4% growth from internally generated revenue and 0.1% growth from acquisitions).



The \$201.5 million, or 11.8%, increase in animal health net sales for the six months ended June 30, 2018 includes an increase of 7.3% in local currency growth (4.0% internally generated revenue and 3.3% growth from acquisitions) as well as an increase of 4.5% related to foreign currency exchange. The local currency growth in animal health revenue is affected by the revenue for certain products being recognized on an agency basis in 2018 that had been recognized on a gross basis in the prior year. When excluding the effects of this change, internally generated revenue grew by 8.1%.

The \$84.1 million, or 7.2%, increase in medical net sales for the six months ended June 30, 2018 is the result of an increase of 6.8% in local currency growth (6.7% increase in internally generated revenue and 0.1% growth from acquisitions) as well as an increase of 0.4% related to foreign currency exchange.

The \$11.8 million, or 5.5%, increase in technology and value-added services net sales for the six months ended June 30, 2018 includes an increase of 3.9% in local currency growth (3.0% increase in internally generated revenue and 0.9% growth from acquisitions) as well as an increase of 1.6% related to foreign currency exchange. The local currency growth in technology and value-added services revenue is affected by the revenue for certain products being recognized on an agency basis in 2018 that had been recognized on a gross basis in the prior year. When excluding the effects of this change, internally generated revenue grew by 3.3%.

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Gross Profit

Gross profit and gross margin percentages by segment and in total for the six months ended June 30, 2018 and July 1, 2017 were as follows (in thousands):

Health care distribution	Ju
.....	20
Technology and value-added services	\$
.....	
Total	\$

For the six months ended June 30, 2018, gross profit increased \$134.6 million, or 8.1%, from the comparable prior year period. As a result of different practices of categorizing costs associated with distribution networks throughout our industry, our gross margins may not necessarily be comparable to other distribution companies. Additionally, we realize substantially higher gross margin percentages in our technology segment than in our health care distribution segment. These higher gross margins result from being both the developer and seller of software products and services, as well as certain financial services. The software industry typically realizes higher gross margins to recover investments in research and development.

Within our health care distribution segment, gross profit margins may vary from one period to the next. Changes in the mix of products sold as well as changes in our customer mix have been the most significant drivers affecting our gross profit margin. For example, sales of pharmaceutical products are generally at lower gross profit margins than other products. Conversely, sales of our private label products achieve gross profit margins that are higher than average. With respect to customer mix, sales to our large-group customers are typically completed at lower gross margins due to the higher volumes sold as opposed to the gross margin on sales to office-based practitioners who normally purchase lower volumes at greater frequencies.

Health care distribution gross profit increased \$128.5 million, or 8.4%, for the six months ended June 30, 2018 compared to the prior year period. Health care distribution gross profit margin decreased to 26.1% for the six months ended June 30, 2018 from 26.4% for the comparable prior year period. The overall increase in our health care distribution gross profit is attributable to a \$114.0 million gross profit increase from growth in internally generated revenue and \$33.8 million is attributable to acquisitions. These increases were partially offset by a \$19.3 million decline in gross profit due to the decrease in the gross margin rates.

Technology and value-added services gross profit increased \$6.0 million, or 4.3%, for the six months ended June 30, 2018 compared to the prior year period. Technology gross profit margin decreased to 64.9% for the six months ended June 30, 2018 from 65.6% for the comparable prior year period. The increase in gross profit in our technology and value-added services segment was attributable to \$4.8 million growth in internally generated revenue. Acquisitions accounted for the remaining \$1.2 million increase of gross profit within our technology and value-added services segment for the six months ended June 30, 2018 compared to the prior year period.

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Selling, General and Administrative

Selling, general and administrative expenses by segment and in total for the six months ended June 30, 2018 and July 1, 2017 were as follows (in thousands):

Health care distribution	\$
.....	
Technology and value-added services	\$
.....	
Total	\$

Selling, general and administrative expenses increased \$101.7 million, or 8.1%, to \$1,359.1 million for the six months ended June 30, 2018 from the comparable prior year period. The \$95.0 million increase in selling, general and administrative expenses within our health care distribution segment for the six months ended June 30, 2018 as compared to the prior year period was attributable to \$38.8 million of additional costs from acquired companies, and \$56.2 million of additional operating costs. The \$6.7 million increase in selling, general and administrative expenses within our technology and value-added services segment for the six months ended June 30, 2018 as compared to the prior year period was attributable to \$1.8 million of additional costs from acquired companies and \$4.9 million of additional operating costs. As a percentage of net sales, selling, general and administrative expenses decreased to 20.8% from 21.0% for the comparable prior year period.

As a component of selling, general and administrative expenses, selling expenses increased \$74.7 million, or 9.8%, to \$835.1 million for the six months ended June 30, 2018 from the comparable prior year period. As a percentage of net sales, selling expenses increased to 12.8% from 12.7% for the comparable prior year period.

As a component of selling, general and administrative expenses, general and administrative expenses increased \$27.0 million, or 5.4%, to \$524.0 million for the six months ended June 30, 2018 from the comparable prior year period. As a percentage of net sales, general and administrative expenses decreased to 8.0% from 8.3% for the comparable year period.

Other Expense, Net

Other expense, net, for the six months ended June 30, 2018 and July 1, 2017 was as follows (in thousands):

	June 2018
Interest income	
.....	\$10,2
Interest expense	
.....	(35,
Other, net .....	(45
Other expense, net .....	\$(25,

Other expense, net increased \$11.1 million to \$25.6 million for the six months ended June 30, 2018 from the comparable prior year period. Interest income increased \$1.9 million primarily due to increased interest and late fee income. Interest expense increased \$11.8 million primarily due to increased borrowings under our bank credit lines and our private placement facilities, as well as higher interest rates.

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### Income Taxes

Our effective tax rate was 24.8% for the six months ended June 30, 2018 and for the six months ended July 1, 2017. The difference between our effective tax rate and the federal statutory tax rate for the six months ended June 30, 2018 primarily relates to state and foreign income taxes and interest expense. The difference between our effective tax rate and the federal statutory tax rate for the six months ended July 1, 2017 primarily relates to the adoption of ASU 2016-09 in the first quarter of 2017, as well as state and foreign income taxes and interest expense.

### Net Income

Net income decreased \$3.7 million, or 1.2%, for the six months ended June 30, 2018, compared to the prior year period due to the factors noted above.

### Liquidity and Capital Resources

Our principal capital requirements include funding of acquisitions, purchases of additional noncontrolling interests, repayments of debt principal, the funding of working capital needs, purchases of fixed assets and repurchases of common stock. Working capital requirements generally result from increased sales, special inventory forward buy-in opportunities and payment terms for receivables and payables. Historically, sales have tended to be stronger during the third and fourth quarters and special inventory forward buy-in opportunities have been most prevalent just before the end of the year, and have caused our working capital requirements to be higher from the end of the third quarter to the end of the first quarter of the following year.

We finance our business primarily through cash generated from our operations, revolving credit facilities and debt placements. Our ability to generate sufficient cash flows from operations is dependent on the continued demand of our customers for our products and services, and access to products and services from our suppliers.

Our business requires a substantial investment in working capital, which is susceptible to fluctuations during the year as a result of inventory purchase patterns and seasonal demands. Inventory purchase activity is a function of sales activity, special inventory forward buy-in opportunities and our desired level of inventory. We anticipate future increases in our working capital requirements.

We finance our business to provide adequate funding for at least 12 months. Funding requirements are based on forecasted profitability and working capital needs, which, on occasion, may change. Consequently, we may change our funding structure to reflect any new requirements.

We believe that our cash and cash equivalents, our ability to access private debt markets and public equity markets, and our available funds under existing credit facilities provide us with sufficient liquidity to meet our currently foreseeable short-term and long-term capital needs. We have no off-balance sheet arrangements.

Net cash provided by operating activities was \$216.9 million for the six months ended June 30, 2018, compared to \$176.1 million for the comparable prior year period. The net change of \$40.8 million was primarily attributable to working capital requirements.

Net cash used in investing activities was \$74.6 million for the six months ended June 30, 2018, compared to \$191.4 million for the comparable prior year period. The net change of \$116.8 million was primarily due to reduced payments for equity investments and business acquisitions.

Net cash used in financing activities was \$222.3 million for the six months ended June 30, 2018, compared to net cash provided by financing activities of \$15.5 million for the comparable prior year period. The net change of \$237.8 million was primarily due to increased acquisitions of noncontrolling interests in subsidiaries, partially offset by increased net borrowings from debt and decreased repurchases of common stock.

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The following table summarizes selected measures of liquidity and capital resources (in thousands):

	June 30, 2018
Cash and cash equivalents .....	\$111,000
Working capital .....	909,000
Debt:	
Bank credit lines .....	\$1,170,000
Current maturities of long-term debt .....	12,400
Long-term debt .....	985,000
Total debt .....	\$2,177,400

Our cash and cash equivalents consist of bank balances and investments in money market funds representing overnight investments with a high degree of liquidity.

Accounts receivable days sales outstanding and inventory turns

Our accounts receivable days sales outstanding from operations increased to 43.3 days as of June 30, 2018 from 42.4 days as of July 1, 2017. During the six months ended June 30, 2018, we wrote off approximately \$3.8 million of fully reserved accounts receivable against our trade receivable reserve. Our inventory turns from operations decreased to 4.9 as of June 30, 2018 from 5.3 as of July 1, 2017. Our working capital accounts may be impacted by current and future economic conditions.

Bank Credit Lines

On April 18, 2017, we entered into a new \$750 million revolving credit agreement (the “Credit Agreement”). This facility, which matures in April 2022, replaced our \$500 million revolving credit facility, which was scheduled to mature in September 2019. The interest rate is based on the USD LIBOR plus a spread based on our leverage ratio at the end of each financial reporting quarter. On June 29, 2018, we amended the Credit Agreement to, among other things, (i) permit the consummation of the spin-off of HS Spinco, Inc., a Delaware corporation and a direct, wholly



owned subsidiary of Henry Schein, Inc. (the “Spin-off”), (ii) provide for swing-line commitments in the amount of \$75 million, and (iii) provide for the designation of subsidiary borrowers under the facility. The Credit Agreement provides, among other things, that we are required to maintain maximum leverage ratios, and contains customary representations, warranties and affirmative covenants. The Credit Agreement also contains customary negative covenants, subject to negotiated exceptions on liens, indebtedness, significant corporate changes (including mergers), dispositions and certain restrictive agreements.

As of June 30, 2018 and December 30, 2017, the borrowings on this revolving credit facility were \$325.0 million and \$320.0 million, respectively. As of June 30, 2018 and December 30, 2017, there were \$11.2 million and \$11.3 million of letters of credit, respectively, provided to third parties under the credit facility.

As of June 30, 2018 and December 30, 2017, we had various other short-term bank credit lines available, of which \$454.3 million and \$421.7 million, respectively, were outstanding. At June 30, 2018 and December 30, 2017, borrowings under all of our credit lines had a weighted average interest rate of 2.89% and 2.27%, respectively.

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## Private Placement Facilities

On September 15, 2017, we increased our available private placement facilities with three insurance companies to a total facility amount of \$1 billion, and extended the expiration date to September 15, 2020. These facilities are available on an uncommitted basis at fixed rate economic terms to be agreed upon at the time of issuance, from time to time through September 15, 2020. The facilities allow us to issue senior promissory notes to the lenders at a fixed rate based on an agreed upon spread over applicable treasury notes at the time of issuance. The term of each possible issuance will be selected by us and can range from five to 15 years (with an average life no longer than 12 years). The proceeds of any issuances under the facilities will be used for general corporate purposes, including working capital and capital expenditures, to refinance existing indebtedness and/or to fund potential acquisitions. On June 29, 2018, we amended and restated the above private placement facilities to, among other things, (i) permit the consummation of the Spin-off and (ii) provide for the issuance of notes in Euros, British Pounds and Australian Dollars, in addition to U.S. Dollars. The agreements provide, among other things, that we maintain certain maximum leverage ratios, and contain restrictions relating to subsidiary indebtedness, liens, affiliate transactions, disposal of assets and certain changes in ownership. These facilities contain make-whole provisions in the event that we pay off the facilities prior to the applicable due dates.

The components of our private placement facility borrowings as of June 30, 2018 are presented in the following table (in thousands):

Date of Borrowing	Amount of Borrowing Outstanding	Borrowing Rate	Due Date
September 2, 2010	\$ 100,000	3.79 %	September 2, 2020
January 20, 2012	50,000	3.45	January 20, 2024
January 20, 2012 (1)	28,571	3.09	January 20, 2022
December 24, 2012	50,000	3.00	December 24, 2024
June 2, 2014	100,000	3.19	June 2, 2021
June 16, 2017	100,000	3.42	June 16, 2027
September 15, 2017	100,000	3.52	September 15, 2029
January 2, 2018	100,000	3.32	January 2, 2028
Less: Deferred debt issuance costs	(387)		
	\$ 628,184		

(1) Annual repayments of approximately \$7.1 million for this borrowing commenced on January 20, 2016.

## Committed Loan Associated with Animal Health Spin-off

On May 21, 2018, we obtained a \$400 million committed loan which matures on the earlier of (i) March 31, 2019 and (ii) the consummation of the Spin-off. The proceeds of this loan were used, among other things, to fund our purchase of all of the equity interests in Butler Animal Health Holding Company, LLC (“BAHHC”) directly or indirectly owned by Darby Group Companies, Inc. (“Darby”) and certain other sellers pursuant to the terms of that certain Amendment to Put Rights Agreements, dated as of April 20, 2018, by and among us, Darby, BAHHC and the individual sellers party thereto for an aggregate purchase price of \$365 million. As of June 30, 2018, the balance outstanding on this loan was \$400 million and is included within the “Bank credit lines” caption within our consolidated balance sheet. At June 30, 2018, the interest rate on this loan was 3.0%.

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U.S. Trade Accounts Receivable Securitization

We have a facility agreement with a bank, as agent, based on the securitization of our U.S. trade accounts receivable that is structured as an asset-backed securitization program with pricing committed for up to three years. On June 1, 2016, we extended the expiration date of this facility agreement to April 29, 2019 and increased the purchase limit under the facility from \$300 million to \$350 million. On July 6, 2017, we extended the expiration date of this facility agreement to April 29, 2020. The borrowings outstanding under this securitization facility were \$335 million and \$350 million as of June 30, 2018 and December 30, 2017, respectively. At June 30, 2018, the interest rate on borrowings under this facility was based on the asset-backed commercial paper rate of 2.29% plus 0.70%, for a combined rate of 2.99%. At December 30, 2017, the interest rate on borrowings under this facility was based on the asset-backed commercial paper rate of 1.53% plus 0.75%, for a combined rate of 2.28%.

We are required to pay a commitment fee of 30 basis points on the daily balance of the unused portion of the facility if our usage is greater than or equal to 50% of the facility limit or a commitment fee of 35 basis points on the daily balance of the unused portion of the facility if our usage is less than 50% of the facility limit.

Borrowings under this facility are presented as a component of Long-term debt within our consolidated balance sheet.

Long-term debt

Long-term debt consisted of the following:

Private placement facilities

.....  
U.S. trade accounts receivable securitization

.....  
Various collateralized and uncollateralized loans payable with interest  
in varying installments through 2022 at interest rates  
ranging from 2.56% to 4.60% at June 30, 2018 and  
ranging from 2.56% to 12.90% at December 30, 2017

Jun  
201  
\$62  
33  
29

Capital lease obligations payable through 2029 with interest rates ranging from 0.07% to 19.79% at June 30, 2018 and ranging from 0.84% to 19.79% at December 30, 2017

.....	4,
Total .....	99
Less current maturities	
.....	(1
Total long-term debt .....	\$98

Acquisitions

On April 3, 2018, we announced a joint venture with Internet Brands, a provider of web presence and online marketing software, to create a newly formed entity, Henry Schein One, LLC. The transaction closed on July 1, 2018. The joint venture includes Henry Schein Practice Solutions products and services, as well as Henry Schein’s international dental practice management systems and the dental businesses of Internet Brands. We own 74% of the joint venture and Internet Brands owns the remaining 26% minority interest. Beginning with the second anniversary of the effective date of the formation of the joint venture, Henry Schein One will issue additional shares to Internet Brands through the fifth anniversary of the effective date, thereby increasing Internet Brands’ ownership by approximately 7.6%. Internet Brands will also be entitled to receive additional shares, in the aggregate up to approximately 1.6% of the joint venture’s ownership, if certain operating targets are met by the joint venture in its fourth, fifth and sixth operating years. Senior management from Henry Schein and Internet Brands serve on the board of Henry Schein One. The combined entity, which serves markets globally, had pro-forma 2017 sales of approximately \$400 million, of which approximately \$100million originated at Internet Brands.

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### Planned Divestiture

On April 23, 2018, we announced that we entered into a definitive agreement with HS Spinco, Inc., a direct, wholly owned subsidiary of Henry Schein (“Spinco”), and Direct Vet Marketing, Inc. (d/b/a Vets First Choice) (“DVM”) to create a newly formed company, Vets First Corp. The transaction is intended to be tax-free to Henry Schein stockholders for U.S. tax purposes. As part of this transaction, subject to the terms and conditions set forth in certain definitive agreements, we will contribute the assets and entities comprising our animal health business to Spinco. In exchange for the contribution to Spinco of our animal health business, Spinco will issue to Henry Schein shares of common stock, par value \$0.01 per share, of Spinco (the “Spinco Common Stock”). We will subsequently distribute to our stockholders all of the shares of Spinco Common Stock held by us (the “Distribution”). Immediately after the Distribution, HS Merger Sub, Inc., a wholly owned subsidiary of Spinco, will merge with and into DVM, with DVM surviving the merger as a wholly owned subsidiary of Spinco (with such subsidiary to be renamed Vets First Corp.). Upon consummation of these transactions, on a fully-diluted basis, the stockholders of Henry Schein and, if applicable, certain third parties and minority holders of our animal health subsidiaries that are contributed to Spinco in exchange for their interests in these subsidiaries, will own approximately 63% of the outstanding shares of Spinco Common Stock, and the then former stockholders of DVM will own approximately 37% of the outstanding shares of Spinco Common Stock, subject to certain adjustments. Henry Schein will nominate six individuals to the Vets First Corp. Board of Directors and DVM will nominate five individuals to the Vets First Corp. Board of Directors.

Additionally, we expect to receive a cash dividend between \$1.0 billion and \$1.25 billion on a tax-free basis as part of the transaction. We plan to use the proceeds for general corporate purposes, including share repurchases and repayment of indebtedness.

The transaction has been unanimously approved by our Board of Directors and the Board of Directors of DVM, which we are working toward closing by the end of 2018. It is also subject to customary closing conditions, including customary regulatory approvals, the receipt of tax opinions from counsel with respect to the transaction and the effectiveness of the registration statement on Form S-1/S-4 to be filed with the SEC in connection with the transaction.

### Stock Repurchases

From June 21, 2004 through June 30, 2018, we repurchased \$2.8 billion, or 56,415,270 shares, under our common stock repurchase programs, with \$146.6 million available as of June 30, 2018 for future common stock share repurchases.



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## Redeemable Noncontrolling Interests

Some minority stockholders in certain of our subsidiaries have the right, at certain times, to require us to acquire their ownership interest in those entities at fair value. Accounting Standards Codification (“ASC”) Topic 480-10 is applicable for noncontrolling interests where we are or may be required to purchase all or a portion of the outstanding interest in a consolidated subsidiary from the noncontrolling interest holder under the terms of a put option contained in contractual agreements. The components of the change in the Redeemable noncontrolling interests for the six months ended June 30, 2018 and the year ended December 30, 2017 are presented in the following table:

Balance, beginning of period .....	Jun 2018	\$8.0
Decrease in redeemable noncontrolling interests due to redemptions .....		(6.0)
Increase in redeemable noncontrolling interests due to business acquisitions.....		9.0
Net income attributable to redeemable noncontrolling interests .....		14.0
Dividends declared .....		(1.0)
Effect of foreign currency translation gain (loss) attributable to redeemable noncontrolling interests .....		(1.0)
Change in fair value of redeemable securities .....		1.0
Balance, end of period .....	Jun 2018	\$2.0

Changes in the estimated redemption amounts of the noncontrolling interests subject to put options are adjusted at each reporting period with a corresponding adjustment to Additional paid-in capital. Future reductions in the carrying amounts are subject to a floor amount that is equal to the fair value of the redeemable noncontrolling interests at the time they were originally recorded. The recorded value of the redeemable noncontrolling interests cannot go below the floor level. These adjustments do not impact the calculation of earnings per share.

Additionally, some prior owners of such acquired subsidiaries are eligible to receive additional purchase price cash consideration if certain financial targets are met. Any adjustments to these accrual amounts are recorded in our consolidated statement of income. For six months ended June 30, 2018 and July 1, 2017, there were no material adjustments recorded in our consolidated statement of income relating to changes in estimated contingent purchase price liabilities.



## Critical Accounting Policies and Estimates

There have been no material changes in our critical accounting policies and estimates from those disclosed in Item 7 of our Annual Report on Form 10-K for the year ended December 30, 2017 (the “2017 Form 10-K”), except as follows:

### Revenue Recognition

On December 31, 2017, we adopted Accounting Standard Update (“ASU”) No. 2014-09, “Revenue from Contracts with Customers”, ASC 606 (“Topic 606”) using the modified retrospective method applied to those contracts which were not completed as of the adoption date. Results for reporting periods beginning after December 30, 2017 are presented under Topic 606, while prior period amounts are not adjusted and continue to be reported under the accounting standards in effect for those periods. Our revenue recognition accounting policies applied prior to adoption of Topic 606 are outlined in the financial statements in the 2017 Form 10-K. The disclosures included herein reflect our accounting policies under Topic 606.

We generate revenue from the sale of dental, animal health and medical consumable products, as well as equipment, software products and services and other sources. Provisions for discounts, rebates to customers, customer returns and other contra revenue adjustments are included in the transaction price at contract inception by estimating the most likely amount based upon historical data and estimates and are provided for in the

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period in which the related sales are recognized.

Revenue derived from the sale of consumable products is recognized at a point in time when control transfers to the customer. Such sales typically entail high-volume, low-dollar orders shipped using third-party common carriers. We believe that control has transferred to the customer because we have no post-shipment obligations and this is when legal title and risks and rewards of ownership transfer to the customer and the point at which we have an enforceable right to payment.

Revenue derived from the sale of equipment is recognized when control transfers to the customer. This occurs when the equipment is delivered. Such sales typically entail scheduled deliveries of large equipment primarily by equipment service technicians. Some equipment Our product generally carries standard warranty terms provided by the manufacturer, however, in instances where we provide warranty labor services, the warranty costs are accrued in accordance with ASC 460 "Guarantees".

Revenue derived from the sale of software products is recognized when products are shipped to customers or made available electronically. Such software is generally installed by customers and does not require extensive training due to the nature of its design. Revenue derived from post-contract customer support for software, including annual support and/or training, is generally recognized over time using time elapsed as the input method that best depicts the transfer of control to the customer.

Revenue derived from other sources including freight charges, equipment repairs and financial services is recognized when the related product revenue is recognized or when the services are provided. We apply the practical expedient to treat shipping and handling activities performed after the customer obtains control as fulfillment activities, rather than a separate performance obligation in the contract.

Sales, value add and other taxes we collect concurrent with revenue-producing activities are excluded from revenue.

Certain of our revenue is derived from bundled arrangements that include multiple distinct performance obligations which are accounted for separately. When we sell software products together with related services (i.e., training and technical support), we allocate revenue to software using the residual method, using an estimate of the standalone selling price to estimate the fair value of the undelivered elements. There are no cases where revenue is deferred due to a lack of a standalone selling price. Bundled arrangements that include elements that are not considered software consist primarily of equipment and the related installation service. We allocate revenue for such arrangements based on the relative selling prices of the goods or services. If an observable selling price is not available (i.e., we do not sell the goods or services separately), we use one of the following techniques to estimate the standalone selling price:

adjusted market approach; cost-plus approach; or the residual method. There is no specific hierarchy for the use of these methods, but the estimated selling price reflects our best estimate of what the selling prices of each deliverable would be if it were sold regularly on a standalone basis taking into consideration the cost structure of our business, technical skill required, customer location and other market conditions.

*Accounts Receivable*

The carrying amount of accounts receivable is reduced by a valuation allowance that reflects our best estimate of the amounts that will not be collected. In addition to reviewing delinquent accounts receivable, we consider many factors in estimating our reserve, including historical data, experience, customer types, credit worthiness and economic trends. From time to time, we adjust our assumptions for anticipated changes in any of these or other factors expected to affect collectability.

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### Contract Assets

Contract assets include amounts related to any conditional right to consideration for work completed but not billed as of the reporting date and generally represent amounts owed to us by customers, but not yet billed. Contract assets are transferred to accounts receivable when the right becomes unconditional. Current contract assets are included in Prepaid expenses and other and the non-current contract assets are included in Investments and other within our consolidated balance sheet.

### Contract Liabilities

Contract liabilities are comprised of advance payments and deferred revenue amounts. Contract liabilities are transferred to revenue once the performance obligation has been satisfied. Current contract liabilities are included in Accrued expenses: Other and the non-current contract liabilities are included in Other liabilities within our consolidated balance sheet.

### *Deferred Commissions*

Sales commissions earned by our sales force that relate to long term arrangements are capitalized as costs to obtain a contract when the costs incurred are incremental and are expected to be recovered. Deferred sales commissions are amortized over the estimated customer relationship period. We apply the practical expedient related to the capitalization of incremental costs of obtaining a contract, and recognize such costs as an expense when incurred if the amortization period of the assets that we would have recognized is one year or less.

### *Sales Returns*

Sales returns are recognized as a reduction of revenue by the amount of expected returns and are recorded as refund liability within current liabilities. We estimate the amount of revenue expected to be reversed to calculate the sales return liability based on historical data for specific products, adjusted as necessary for new products. The allowance for returns is presented gross as a refund liability and we record an inventory asset (and a corresponding adjustment to cost of sales) for any goods or services that we expect to be returned.

### Accounting Pronouncements Adopted

### Critical Accounting Policies and Estimates

In May 2014, the Financial Accounting Standards Board (“FASB”) issued Topic 606. We adopted the provisions of this standard as of December 31, 2017, on a modified retrospective basis. We applied the requirements of the new standard only to contracts that were not completed as of the adoption date. We recorded an immaterial adjustment to the opening balance of retained earnings for the adoption of Topic 606. The comparative information has not been restated and continues to be reported under the accounting standards in effect for those periods.

The impact of the new standard on our consolidated statements of income, which we expect to be immaterial on an ongoing basis, is primarily related to software sales and sales commissions and is described as follows:

#### Software Sales

For software licenses sold together with post contract support (PCS), we previously deferred software revenue if it did not have vendor-specific evidence of fair value of the PCS. Under Topic 606, the concept of vendor-specific objective evidence is eliminated and there are no cases where revenue is deferred due to a lack of standalone selling price. In addition, we previously recognized revenue from term licenses ratably over the contract term. Under Topic 606, such licenses represent a right to use intellectual property and therefore require upfront recognition. Furthermore, certain upfront fees related to service arrangements were previously deferred and recognized over the estimated customer life. Under Topic 606, the period over which we will recognize these fees is reduced, as the upfront fee represents additional contract price which will be allocated to the

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performance obligations in the contract and recognized as those performance obligations are satisfied, rather than being amortized over the estimated customer life. Based on the aforementioned changes, such software revenue will be recognized sooner than under the previous revenue recognition standard.

### *Sales Commissions*

We previously recognized sales commissions as an expense when incurred. Under Topic 606, we defer such sales commissions as costs to obtain a contract when the costs are incremental and expected to be recovered. Deferred sales commissions are amortized over the estimated customer relationship period. We apply the practical expedient to expense, as incurred, commissions with an expected amortization period of one year or less.

In October 2016, the FASB issued ASU No. 2016-16, “Income Taxes, Intra-Entity Transfers of Assets Other Than Inventory” (“Topic 740”). Topic 740 requires companies to recognize the income tax effects of intercompany sales and transfers of assets other than inventory in the period which the transfer occurs. Previously, companies were required to defer the income tax effects on intercompany transfer of assets until the asset has been sold to an outside party. On December 31, 2017, we adopted the guidance, which is effective for annual periods and related interim periods beginning after December 15, 2017 on a modified retrospective basis. As a result of the adoption of Topic 740, we have recorded an immaterial adjustment to the opening balance of retained earnings and a reduction to prepaid assets.

In May 2017, the FASB issued ASU No. 2017-09, “Compensation-Stock Compensation, Scope of Modification Accounting” (“Topic 718”). Topic 718 provides guidance on determining which changes to the terms and conditions of share-based payment awards require an entity to apply modification accounting. Topic 718 requires modification accounting if the fair value, vesting conditions, or equity or liability classification of the award is not the same immediately before and after a change to the terms and conditions of the award. Topic 718 was adopted on a prospective basis as of December 31, 2017 and did not have a material impact on the consolidated financial statements or disclosures as of June 30, 2018.

### Recently Issued Accounting Standards

In February 2016, the FASB issued ASU No. 2016-02, “Leases” (Topic 842) (“ASU 2016-02”). ASU 2016-02 contains guidance on accounting for leases and requires that most lease assets and liabilities and the associated rights and obligations be recognized on the Company’s balance sheet. ASU 2016-02 focuses on lease assets and lease liabilities by lessees classified as operating leases under previous generally accepted accounting principles. For leases with a term of 12 months or less, a lessee is permitted to make an accounting policy election by class of underlying asset not to recognize lease assets and lease liabilities. ASU 2016-02 will require disclosures regarding the amount, timing and uncertainty of cash flows arising from leases. The standard, which requires the use of a modified retrospective

approach, will be effective for interim and annual periods beginning after December 15, 2018. Early adoption is permitted. We are currently exploring the methods we can use to gather and process our operating lease data at a worldwide consolidated level.

In June 2016, the FASB issued ASU No. 2016-13, "Financial Instruments-Credit Losses (Topic 326): Measurement of Credit Losses on Financial Instruments" which requires the measurement and recognition of expected credit losses for financial assets held at amortized cost. This ASU is effective for interim and annual reporting periods beginning after December 15, 2019, with early adoption permitted for interim and annual reporting periods beginning after December 15, 2018. This ASU is required to be adopted using the modified retrospective basis, with a cumulative-effect adjustment to retained earnings as of the beginning of the first reporting period in which the guidance of this ASU is effective. Based upon the level and makeup of our financial asset portfolio, past loan loss activity and current known activity regarding our outstanding loans, we do not expect that this ASU will have a material impact on our consolidated financial statements.

In January 2017, the FASB issued ASU No. 2017-04, "Intangibles-Goodwill and Other" (Topic 350) ("ASU 2017-04"). ASU 2017-04 eliminates step two from the goodwill impairment test, thereby eliminating the

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requirement to calculate the implied fair value of a reporting unit. ASU 2017-04 will require us to perform our annual goodwill impairment test by comparing the fair value of our reporting units to the carrying value of those units. If the carrying value exceeds the fair value, we will be required to recognize an impairment charge; however, the impairment charge should not exceed the amount of goodwill allocated to such reporting unit. ASU 2017-04 is required to be implemented on a prospective basis for fiscal years beginning after December 15, 2019. We do not expect that the requirements of ASU 2017-04 will have a material impact on our consolidated financial statements.

In August 2017, the FASB issued ASU No. 2017-12, "Derivatives and Hedging" (Topic 815) ("ASU 2017-12"), which simplifies the requirements for hedge accounting, more closely aligns hedge accounting with risk management activities and increases transparency of the scope and results of hedging activities. This ASU amends the presentation and disclosure requirements and changes how we can assess the effectiveness of our hedging relationships. This ASU will make more financial and nonfinancial hedging strategies eligible for hedge accounting. ASU 2017-12 is required to be implemented for fiscal years beginning after December 15, 2018, and interim periods within those fiscal years. Early adoption of ASU 2017-12 is permitted in any interim period after the issuance of this ASU. We do not expect that the requirements of ASU 2017-12 will have a material impact on our consolidated financial statements.

In February 2018, the FASB issued ASU No. 2018-02, "Treatment of Stranded Tax Effects in Accumulated Other Comprehensive Income Resulting From the Tax Cuts and Jobs Act of 2017 " which allows the reclassification from accumulated comprehensive income to retained earnings the income tax effects resulting from the Tax Cuts and Jobs Act of 2017. This ASU is effective for interim and annual reporting periods beginning after December 15, 2018, with early adoption permitted in any interim period after the issuance of this ASU. We do not expect that the requirements of ASU 2018-02 will have a material impact on our consolidated financial statements.

In June 2018, the FASB issued ASU 2018-07, "Compensation - Stock Compensation (Topic 718): Improvements to Nonemployee Share-Based Payment Accounting" ("ASU 2018-07"), which expands the scope of Topic 718 to include share-based payment transactions for acquiring goods and services from nonemployees. ASU 2018-07 simplifies the accounting for share-based payments to nonemployees by aligning it with the accounting for share-based payments to employees. ASU 2018-07 is effective for public business entities for fiscal years beginning after December 15, 2018, including interim periods within that fiscal year. Early adoption is permitted. We do not expect that the requirements of ASU-2018-07 will have a material impact on our consolidated financial statements.

**ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK**

There have been no material changes in our exposure to market risk from that disclosed in Item 7A of our Annual Report on Form 10-K for the year ended December 30, 2017.





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**ITEM 4. CONTROLS AND PROCEDURES**

Evaluation of Disclosure Controls and Procedures

Under the supervision and with the participation of management, including our principal executive officer and principal financial officer, we evaluated the effectiveness of the design and operation of our disclosure controls and procedures as of the end of the period covered by this quarterly report as such term is defined in Rules 13a-15(e) and 15d-15(e) promulgated under the Securities Exchange Act of 1934, as amended (the “Exchange Act”). Based on this evaluation, our management, including our principal executive officer and principal financial officer, concluded that our disclosure controls and procedures were effective as of June 30, 2018 to ensure that all material information required to be disclosed by us in reports that we file or submit under the Exchange Act is accumulated and communicated to them as appropriate to allow timely decisions regarding required disclosure and that all such information is recorded, processed, summarized and reported within the time periods specified in the SEC’s rules and forms.

Changes in Internal Control over Financial Reporting

The combination of continued acquisition integrations, systems implementations and revenue recognition controls enhancements carried over from prior quarters, when considered in the aggregate, represents a material change in our internal control over financial reporting.

During the quarter ended June 30, 2018, post-acquisition integration related activities continued for our global dental and animal health businesses acquired during prior quarters, representing aggregate annual revenues of approximately \$377 million. These acquisitions, the majority of which utilize separate information and financial accounting systems, have been included in our consolidated financial statements since their respective dates of acquisition.

Also, during the quarter ended June 30, 2018, post-implementation systems improvement activities continued for a new equipment system implemented during prior quarters for our U.S. dental business to centers representing approximate aggregate annual revenues of \$187 million and for the upgrade of an ERP system at an animal health business in Switzerland having approximate aggregate annual revenues of \$49 million.

Finally, in connection with the prior quarter implementation of Topic 606, we continued to enhance our activities relating to developing new policies and procedures based on the new revenue standard.

All acquisition integrations, systems implementations and revenue recognition controls enhancements involved necessary and appropriate change-management controls that are considered in our annual assessment of the design and operating effectiveness of our internal control over financial reporting.

#### Limitations of the Effectiveness of Internal Control

A control system, no matter how well conceived and operated, can provide only reasonable, not absolute, assurance that the objectives of the internal control system are met. Because of the inherent limitations of any internal control system, no evaluation of controls can provide absolute assurance that all control issues, if any, within a company have been detected.

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PART II. OTHER INFORMATION

ITEM 1. LEGAL PROCEEDINGS

Beginning in January 2016, purported class action complaints were filed against Patterson Companies, Inc. (“Patterson”), Benco Dental Supply Co. (“Benco”) and Henry Schein, Inc. Although there were factual and legal variations among these complaints, each of these complaints alleges, among other things, that defendants conspired to fix prices, allocate customers and foreclose competitors by boycotting manufacturers, state dental associations and others that deal with defendants’ competitors. On February 9, 2016, the U.S. District Court for the Eastern District of New York ordered all of these actions, and all other actions filed thereafter asserting substantially similar claims against defendants, consolidated for pre-trial purposes. On February 26, 2016, a consolidated class action complaint was filed by Arnell Prato, D.D.S., P.L.L.C., d/b/a Down to Earth Dental, Evolution Dental Sciences, LLC, Howard M. May, DDS, P.C., Casey Nelson, D.D.S., Jim Peck, D.D.S., Bernard W. Kurek, D.M.D., Larchmont Dental Associates, P.C., and Keith Schwartz, D.M.D., P.A. (collectively, “putative class representatives”) in the U.S. District Court for the Eastern District of New York, entitled *In re Dental Supplies Antitrust Litigation*, Civil Action No.

1:16-CV-00696-BMC-GRB. In the consolidated class action complaint, putative class representatives allege a nationwide agreement among Henry Schein, Benco, Patterson and non-party Burkhardt Dental Supply Company, Inc. (“Burkhardt”) not to compete on price. The consolidated class action complaint asserts a single count under Section 1 of the Sherman Act, and seeks equitable relief, compensatory and treble damages, jointly and severally, and reasonable costs and expenses, including attorneys’ fees and expert fees. On February 22, 2018, plaintiffs moved to certify a class that, subject to certain exclusions, includes all private dental practices and laboratories that purchased dental supplies directly from Henry Schein, Patterson, Benco, Burkhardt or any combination thereof, during the period beginning January 1, 2009 until March 31, 2016. That motion is currently pending. We intend to defend ourselves vigorously against these actions.

On August 31, 2012, Archer and White Sales, Inc. (“Archer”) filed a complaint against Henry Schein, Inc. as well as Danaher Corporation and its subsidiaries Instrumentarium Dental, Inc., Dental Equipment, LLC, Kavvo Dental Technologies, LLC and Dental Imaging Technologies Corporation (collectively, the “Danaher Defendants”) in the United States District Court for the Eastern District of Texas, Civil Action No. 2:12-CV-00572-JRG, styled as an antitrust action under Section 1 of the Sherman Act, and the Texas Free Enterprise Antitrust Act. Archer alleges a conspiracy between Henry Schein, an unnamed company and the Danaher Defendants to terminate or limit Archer’s distribution rights. On August 1, 2017, Archer filed an amended complaint, adding Patterson and Benco as defendants, and alleging that Henry Schein, Patterson, Benco and Burkhardt conspired to fix prices and refused to compete with each other for sales of dental equipment to dental professionals and agreed to enlist their common suppliers, the Danaher Defendants, to join a price-fixing conspiracy and boycott by reducing the distribution territory of, and eventually terminating, their price-cutting competing distributor Archer. Archer seeks injunctive relief, and damages in an amount to be proved at trial, to be trebled with interest and costs, including attorneys’ fees, jointly and severally. On October 30, 2017, Archer filed a second amended complaint, to add additional allegations that it believes support its claims. The named parties and causes of action are the same as the August 1, 2017 amended complaint.

On October 1, 2012, we filed a motion for an order: (i) compelling Archer to arbitrate its claims against us; (2) staying all proceedings pending arbitration; and (3) joining the Danaher Defendants’ motion to arbitrate and stay. On May 28, 2013, the Magistrate Judge granted the motions to arbitrate and stayed proceedings pending arbitration. On June 10,

2013, Archer moved for reconsideration before the District Court judge. On December 7, 2016, the District Court Judge granted Archer's motion for reconsideration and lifted the stay. Defendants appealed the District Court's order. On December 21, 2017, the United States Court of Appeals for the Fifth Circuit affirmed the District Court's order denying the motions to compel arbitration. On February 12, 2018, defendants filed an Application for Stay of Proceedings in the District Court in the Supreme Court of the United States, seeking to stay proceedings in the District Court pending a decision on defendants' forthcoming petition for writ of certiorari. On March 2, 2018, the Supreme Court of the United States granted a stay of proceedings. On June 25, 2018, the Supreme Court of the United States granted defendants' petition for writ of certiorari, pursuant to which it will review the lower court's decision denying our motion to compel arbitration. In the meantime, the trial court proceeding is stayed. We intend to defend ourselves vigorously against this action.

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On August 17, 2017, IQ Dental Supply, Inc. (“IQ Dental”) filed a complaint in the United States District Court for the Eastern District of New York, entitled IQ Dental Supply, Inc. v. Henry Schein, Inc., Patterson Companies, Inc. and Benco Dental Supply Company, Case No. 2:17-cv-4834. Plaintiff alleges that it is a distributor of dental supplies and equipment, and sells dental products through an online dental distribution platform operated by SourceOne Dental (“SourceOne”). SourceOne had previously brought an antitrust lawsuit against Henry Schein, Patterson and Benco, which Henry Schein settled in the second quarter of 2017 and which is described in our prior filings with the SEC.

IQ Dental alleges, among other things, that defendants conspired to suppress competition from IQ Dental and SourceOne for the marketing, distribution and sale of dental supplies and equipment in the United States, and that defendants unlawfully agreed with one another to boycott dentists, manufacturers and state dental associations that deal with, or considered dealing with, plaintiff and SourceOne. Plaintiff claims that this alleged conduct constitutes unreasonable restraint of trade in violation of Section 1 of the Sherman Act, New York’s Donnelly Act and the New Jersey Antitrust Act, and also makes pendant state law claims for tortious interference with prospective business relations, civil conspiracy and aiding and abetting. Plaintiff seeks injunctive relief, compensatory, treble and punitive damages, jointly and severally, and reasonable costs and expenses, including attorneys’ fees and expert fees. On December 21, 2017, the District Court granted the defendants’ motion to dismiss. On January 19, 2018, IQ Dental appealed the District Court’s order. The appeal is pending. We intend to defend ourselves vigorously against this action.

On February 12, 2018, the United States Federal Trade Commission (“FTC”) filed a complaint against Benco Dental Supply Co., Henry Schein, Inc. and Patterson Companies, Inc. The FTC alleges, among other things, that defendants violated U.S. antitrust laws by conspiring, and entering into an agreement, to refuse to provide discounts to or otherwise serve buying groups representing dental practitioners. The FTC alleges that defendants conspired in violation of Section 5 of the FTC Act. The complaint seeks equitable relief only and does not seek monetary damages. We deny the allegation that we conspired to refuse to provide discounts to or otherwise serve dental buying groups and intend to defend ourselves vigorously against this action. A hearing before an administrative law judge is scheduled for October 16, 2018. We believe this matter will not have a material adverse effect on our consolidated financial position, liquidity or results of operations.

On March 7, 2018, Joseph Salkowitz, individually and on behalf of all others similarly situated, filed a putative class action complaint for violation of the federal securities laws against Henry Schein, Inc., Stanley M. Bergman and Steven Paladino in the United States District Court for the Eastern District of New York, Case No. 1:18-cv-01428. The complaint seeks to certify a class consisting of all persons and entities who, subject to certain exclusions, purchased publicly traded Henry Schein securities from March 7, 2013 through February 12, 2018 (the “Class Period”). The complaint alleges, among other things, that the defendants made materially false and misleading statements about Henry Schein’s business, operations and prospects during the Class Period, including matters relating to the issues in the antitrust class actions and the FTC action described above, thereby causing the plaintiff and members of the purported class to pay artificially inflated prices for Henry Schein securities. The complaint seeks unspecified monetary damages and a jury trial. Pursuant to the provisions of the Private Securities Litigation Reform Act of 1995 (the “PSLRA”), plaintiff’s counsel published notice of the commencement of this action, and thereby provided notice of the 60-day period during which any putative class member could apply to be lead plaintiff under the PSLRA. The court appointed lead plaintiff and lead counsel on June 22, 2018 and recaptioned the putative class action as *In re Henry Schein, Inc. Securities Litigation*, under the same case number. Lead plaintiff intends to file a new complaint by September 14, 2018. We intend to defend ourselves vigorously against this action.

On May 3, 2018, a class action complaint, *Marion Diagnostic Center, LLC v. Dickinson, and Co.*, 3:18-cv-01509 (S.D. Ill), was filed in the Southern District of Illinois against Becton, Dickinson, and Co. (“Becton”); Vizient, Inc. (“Vizient”); Cardinal Health, Inc. (“Cardinal”); Owens & Minor Inc. (“O&M”); and Henry Schein, Inc. The complaint

alleges that the defendants entered into a vertical conspiracy to force healthcare providers into long-term exclusionary contracts that restrain trade in the nationwide markets for conventional and safety syringes and safety IV catheters and that inflate the prices of certain Becton products to above-competitive levels. The named plaintiffs seek to represent three separate classes consisting of all healthcare providers that purchased (i) Becton's conventional syringes, (ii) Becton's safety syringes, or (iii) Becton's safety catheters directly from Becton,

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Cardinal, O&M or Henry Schein on or after May 3, 2014. The complaint asserts a single count under Section 1 of the Sherman Act, and seeks equitable relief, compensatory and treble damages, jointly and severally, and reasonable costs and expenses, including attorneys' fees and expert fees. On June 15, 2018, an amended complaint was filed asserting the same allegations against the same parties and adding McKesson Medical-Surgical, Inc. as an additional defendant. We intend to defend ourselves vigorously against this action.

On May 29, 2018, an amended complaint was filed in the MultiDistrict Litigation (MDL) proceeding In Re National Prescription Opiate Litigation (MDL No. 2804; Case No. 17-md-2804) in an action entitled The County of Summit, Ohio et al. v. Purdue Pharma, L.P., et al., Civil Action No. 1:18-op-45090-DAP, in the Northern District of Ohio, adding Henry Schein, Inc., Henry Schein Medical Systems, Inc. and others as defendants. Plaintiffs allege that pharmaceutical manufacturers of prescription opioid drugs engaged in a false advertising campaign to expand the market for such drugs and their own market share and that the entities in the supply chain (including Henry Schein, Inc. and Henry Schein Medical Systems, Inc.) reaped financial rewards by refusing to monitor and restrict the improper distribution of those drugs. Plaintiffs assert the following claims for relief against Henry Schein, Inc. and Henry Schein Medical Systems, Inc.: statutory public nuisance; common law absolute public nuisance; negligence; injury through criminal acts (R.C. 2307.60); unjust enrichment; and civil conspiracy. This case has been designated "Track 1" and is currently set for trial on March 18, 2019. We intend to defend ourselves vigorously against this action.

On July 3, 2018, the City of Barberton, Ohio (and related entities) filed a complaint in the same MDL proceeding (MDL No. 2804; Case No. 17-md-2804) in an action entitled City of Barberton, et al. v. Purdue Pharma, L.P., et al., Civil Action No. 1:18-op-45767-DAP, in the Northern District of Ohio, against Henry Schein, Inc., Henry Schein Medical Systems, Inc. and others, that is similar to The County of Summit complaint. We intend to defend ourselves vigorously against this action.

From time to time, we may become a party to other legal proceedings, including, without limitation, product liability claims, employment matters, commercial disputes, governmental inquiries and investigations (which may in some cases involve our entering into settlement arrangements or consent decrees), and other matters arising out of the ordinary course of our business. While the results of any legal proceeding cannot be predicted with certainty, in our opinion none of these other pending matters are currently anticipated to have a material adverse effect on our consolidated financial position, liquidity or results of operations.

As of June 30, 2018, we had accrued our best estimate of potential losses relating to claims that were probable to result in liability and for which we were able to reasonably estimate a loss. This accrued amount, as well as related expenses, was not material to our financial position, results of operations or cash flows. Our method for determining estimated losses considers currently available facts, presently enacted laws and regulations and other factors, including probable recoveries from third parties.



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## ITEM 1A. RISK FACTORS

There have been no material changes from the risk factors disclosed in Part 1, Item 1A, of our Annual Report on Form 10-K for the year ended December 30, 2017.

**ITEM 2. UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS***Purchases of equity securities by the issuer*

Our share repurchase program, announced on June 21, 2004, originally allowed us to repurchase up to \$100 million of shares of our common stock, which represented approximately 3.5% of the shares outstanding at the commencement of the program. As summarized in the table below, subsequent additional increases totaling \$2.8 billion, authorized by our Board of Directors, to the repurchase program provide for a total of \$2.9 billion of shares of our common stock to be repurchased under this program.

Date of Authorization	Amount of Additional Repurchases Authorized
October 31, 2005	\$ 100,000,000
March 28, 2007	100,000,000
November 16, 2010	100,000,000
August 18, 2011	200,000,000
April 18, 2012	200,000,000
November 12, 2012	300,000,000
December 9, 2013	300,000,000
December 4, 2014	300,000,000
November 30, 2015	400,000,000
October 18, 2016	400,000,000
September 15, 2017	400,000,000

As of June 30, 2018, we had repurchased approximately \$2.8 billion of common stock (56,415,270 shares) under these initiatives, with \$146.6 million available for future common stock share repurchases.

The following table summarizes repurchases of our common stock under our stock repurchase program during the fiscal quarter ended June 30, 2018:

Fiscal Month	Total Number of Shares Purchased (1)	Average Price Paid Per Share	Total Number of Shares Purchased as Part of Our Publicly Announced Program	Maximum Number of Shares that May Yet Be Purchased Under Our Program (2)
04/01/18 through 04/28/18	-	\$ -	-	2,604,168
04/29/18 through 06/02/18	240,000	70.94	240,000	2,631,585
06/03/18 through 06/30/18	504,280	72.04	504,280	2,018,794
	744,280		744,280	

(1) All repurchases were executed in the open market under our existing publicly announced authorized program.

(2) The maximum number of shares that may yet be purchased under this program is determined at the end of each month based on the closing price of our common stock at that time.

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ITEM 5. OTHER INFORMATION

Plan of Restructuring

As previously disclosed, on July 9, 2018, we committed to an initiative to rationalize our operations and provide expense efficiencies. These actions will allow us to execute on our plan to reduce our cost structure and fund new initiatives that will drive future growth under our 2018 to 2020 strategic plan. This initiative is expected to include the elimination of approximately 2% to 3% of our workforce and the closing of certain facilities. The total 2018 costs associated with the actions to complete this restructuring are expected to be in the range of \$45 million to \$55 million pre-tax, or \$0.22 to \$0.27 per diluted share, consisting of \$40 million to \$45 million in employee severance pay and benefits and \$5 million to \$10 million in facility costs, representing primarily lease termination and other facility closure related costs.

During the three and six months ended June 30, 2018, we recorded restructuring costs of \$14.9 million and \$18.7 million, respectively, primarily for certain redundancies. The costs associated with these restructuring activities are included in a separate line item, "Restructuring costs" within our consolidated statements of income.

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ITEM 6. EXHIBITS

Exhibits.

- 2.1 Contribution and Distribution Agreement, dated as of April 20, 2018, by and among the Company, HS Spinco, Inc., Direct Vet Marketing, Inc. (d/b/a Vets First Choice) (“DVM”) and Shareholder Representative Services LLC, solely in its capacity as the representative of the DVM stockholders. (Incorporated by reference to Exhibit 2.1 to our Current Report on Form 8-K filed on April 23, 2018.)
  - 2.2 Agreement and Plan of Merger, dated as of April 20, 2018, by and among the Company, HS Spinco, Inc., HS Merger Sub, Inc., Direct Vet Marketing, Inc. (d/b/a Vets First Choice) (“DVM”) and Shareholder Representative Services LLC, solely in its capacity as the representative of the DVM stockholders. (Incorporated by reference to Exhibit 2.2 to our Current Report on Form 8-K filed on April 23, 2018.)
  - 4.1 Second Amended and Restated Multicurrency Private Shelf Agreement dated as of June 29, 2018, by and among the Company, PGIM, Inc. and each Prudential affiliate which becomes party thereto. (Incorporated by reference to Exhibit 4.1 to our Current Report on Form 8-K filed on July 2, 2018.)
  - 4.2 Second Amended and Restated Master Note Facility dated as of June 29, 2018, by and among the Company, NYL Investors LLC and each New York Life affiliate which becomes party thereto. (Incorporated by reference to Exhibit 4.2 to our Current Report on Form 8-K filed on July 2, 2018.)
  - 4.3 Second Amended and Restated Multicurrency Master Note Purchase Agreement dated as of June 29, 2018, by and among the Company, Metropolitan Life Insurance Company, MetLife Investment Advisors Company, LLC and each MetLife affiliate which becomes party thereto. (Incorporated by reference to Exhibit 4.3 to our Current Report on Form 8-K filed on July 2, 2018.)
  - 10.1 First Amendment, dated as of June 29, 2018, among the Company, the several lenders parties thereto, and JPMorgan Chase Bank, N.A., as administrative agent, lead arranger and lead bookrunner. (Incorporated by reference to Exhibit 10.1 to our Current Report on Form 8-K filed on July 2, 2018.)
  - 10.2 Promissory Note in favor of JPMorgan Chase Bank, N.A. dated as of May 21, 2018. (Incorporated by reference to Exhibit 10.1 to our Current Report on Form 8-K filed on May 21, 2018.)
  - 10.3 Employee Matters Agreement, dated as of April 20, 2018, by and among the Company, HS Spinco, Inc. and Direct Vet Marketing, Inc. (d/b/a Vets First Choice). (Incorporated by reference to Exhibit 10.1 to our Current Report on Form 8-K filed on April 23, 2018.)
  - 31.1 Certification Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.+
  - 31.2 Certification Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.+
  - 32.1 Certification Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.+
  - 101.INS XBRL Instance Document+
  - 101.SCH XBRL Taxonomy Extension Schema Document+
  - 101.CALXBRL Taxonomy Extension Calculation Linkbase Document+
  - 101.DEF XBRL Taxonomy Definition Linkbase Document+
  - 101.LAB XBRL Taxonomy Extension Label Linkbase Document+
  - 101.PRE XBRL Taxonomy Extension Presentation Linkbase Document+
- + Filed herewith.



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SIGNATURE

Pursuant to the requirements of the Securities Exchange Act of 1934, the Registrant has duly caused this Report to be signed on its behalf by the undersigned thereunto duly authorized.

Henry Schein, Inc.  
(Registrant)

By: /s/ Steven Paladino  
Steven Paladino  
Executive Vice President and  
Chief Financial Officer  
(Authorized Signatory and Principal Financial  
and Accounting Officer)

Dated: August 6, 2018

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