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Hill-Rom Holdings, Inc.
Form 10-Q
April 27, 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 March 31, 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 No. 1-6651

HILL-ROM HOLDINGS, INC.

(Exact name of registrant as specified in its charter)

Indiana

35-1160484

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

130 E. Randolph St., Suite 1000

60601

Chicago, IL

(Address of principal executive offices)

(Zip Code)

(312) 819-7200

(Registrant's telephone number, including area code)

Not Applicable

(Former name, former address and former fiscal year, if changed since last report)

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

Yes ☐ No ☒

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files).

Yes ☐ No ☒

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

Large accelerated filer ☐ Accelerated filer ☐ Non-accelerated filer ☐ Smaller reporting company ☐ Emerging growth company ☒

If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the Exchange Act. ☐

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).

Yes ☐ No ☒

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

Common Stock, without par value – 66,277,670 shares as of April 23, 2018.

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HILL-ROM HOLDINGS, INC.

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PART I – FINANCIAL INFORMATION

Item 1. FINANCIAL STATEMENTS

Hill-Rom Holdings, Inc. and Subsidiaries

Condensed Consolidated Statements of Income (Unaudited)

(In millions, except per share data)

| | Quarter Ended March 31 | | Year to Date Ended March 31 | |
|---------------------------------------------------------------------------|---------------------------|---------|--------------------------------|-----------|
| | 2018 | 2017 | 2018 | 2017 |
| Net Revenue | | | | |
| Product sales and service | \$610.7 | \$579.6 | \$1,185.9 | \$1,121.5 |
| Rental revenue | 99.8 | 99.3 | 194.3 | 194.8 |
| Total revenue | 710.5 | 678.9 | 1,380.2 | 1,316.3 |
| Cost of Revenue | | | | |
| Cost of goods sold | 313.7 | 305.7 | 617.8 | 594.1 |
| Rental expenses | 46.4 | 48.8 | 92.4 | 95.2 |
| Total cost of revenue | 360.1 | 354.5 | 710.2 | 689.3 |
| Gross Profit | 350.4 | 324.4 | 670.0 | 627.0 |
| Research and development expenses | 34.7 | 35.3 | 67.0 | 67.3 |
| Selling and administrative expenses | 232.7 | 222.4 | 454.4 | 431.2 |
| Special charges (Note 8) | 36.9 | 3.1 | 50.4 | 8.9 |
| Operating Profit | 46.1 | 63.6 | 98.2 | 119.6 |
| Interest expense | (24.2) | (21.9) | (47.3) | (41.4) |
| Investment income and other, net | (0.4) | (0.4) | 1.4 | (1.6) |
| Income Before Income Taxes | 21.5 | 41.3 | 52.3 | 76.6 |
| Income tax expense (benefit) (Note 9) | (7.0) | 7.3 | (64.5) | 19.1 |
| Net Income | 28.5 | 34.0 | 116.8 | 57.5 |
| Less: Net loss attributable to noncontrolling interests | — | (0.4) | — | (0.7) |
| Net Income Attributable to Common Shareholders | \$28.5 | \$34.4 | \$116.8 | \$58.2 |
| Net Income Attributable to Common Shareholders per Common Share - Basic | \$0.43 | \$0.52 | \$1.77 | \$0.89 |
| Net Income Attributable to Common Shareholders per Common Share - Diluted | \$0.42 | \$0.51 | \$1.73 | \$0.87 |
| Dividends per Common Share | \$0.20 | \$0.18 | \$0.38 | \$0.35 |
| Average Common Shares Outstanding - Basic (thousands) (Note 10) | 66,192 | 65,462 | 66,040 | 65,473 |

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| | | | | |
|-------------------------------------------------------------------|--------|--------|--------|--------|
| Average Common Shares Outstanding - Diluted (thousands) (Note 10) | 67,597 | 67,132 | 67,508 | 67,057 |
|-------------------------------------------------------------------|--------|--------|--------|--------|

See Notes to Condensed Consolidated Financial Statements (unaudited)

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Hill-Rom Holdings, Inc. and Subsidiaries

Condensed Consolidated Statements of Comprehensive Income (Unaudited)

(In millions)

| | Quarter Ended March 31 | | Year to Date Ended March 31 | |
|----------------------------------------------------------------------|------------------------------|--------|-----------------------------------|---------|
| | 2018 | 2017 | 2018 | 2017 |
| Net Income | \$28.5 | \$34.0 | \$116.8 | \$57.5 |
| Other Comprehensive Income (Loss), net of tax (Note 7): | | | | |
| Derivative instruments and hedges | 7.9 | (0.2) | 11.3 | 10.0 |
| Foreign currency translation adjustment | 16.5 | 14.0 | 22.6 | (25.5) |
| Change in pension and postretirement defined benefit plans | 0.8 | 0.8 | 1.6 | 2.1 |
| Total Other Comprehensive Income (Loss), net of tax | 25.2 | 14.6 | 35.5 | (13.4) |
| Total Comprehensive Income | 53.7 | 48.6 | 152.3 | 44.1 |
| Less: Comprehensive loss attributable to noncontrolling interests | — | (0.4) | — | (0.7) |
| Total Comprehensive Income Attributable to Common Shareholders | \$53.7 | \$49.0 | \$152.3 | \$44.8 |
| See Notes to Condensed Consolidated Financial Statements (unaudited) | | | | |

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

| | March 31, 2018 | September 30, 2017 |
|----------------------------------------------------------------------|-------------------|-----------------------|
| ASSETS | | |
| Current Assets | | |
| Cash and cash equivalents | \$239.0 | \$ 231.8 |
| Trade accounts receivable, net of allowances (Note 2) | 537.9 | 579.3 |
| Inventories (Note 2) | 315.1 | 284.5 |
| Other current assets | 109.0 | 70.6 |
| Total current assets | 1,201.0 | 1,166.2 |
| Property, plant and equipment, net (Note 2) | 341.8 | 355.4 |
| Goodwill (Note 4) | 1,754.2 | 1,759.6 |
| Other intangible assets and software, net (Note 2) | 1,088.1 | 1,144.0 |
| Deferred income taxes (Notes 1 and 9) | 41.5 | 40.9 |
| Other assets | 78.1 | 62.6 |
| Total Assets | \$4,504.7 | \$ 4,528.7 |
| LIABILITIES | | |
| Current Liabilities | | |
| Trade accounts payable | \$159.6 | \$ 167.9 |
| Short-term borrowings (Note 5) | 221.3 | 188.9 |
| Accrued compensation | 97.7 | 126.9 |
| Accrued product warranties (Note 12) | 25.0 | 25.5 |
| Accrued rebates | 38.0 | 39.7 |
| Other current liabilities | 108.9 | 109.8 |
| Total current liabilities | 650.5 | 658.7 |
| Long-term debt (Note 5) | 2,025.6 | 2,120.4 |
| Accrued pension and postretirement benefits (Note 6) | 78.7 | 78.1 |
| Deferred income taxes (Notes 1 and 9) | 180.0 | 266.2 |
| Other long-term liabilities | 59.5 | 39.7 |
| Total Liabilities | 2,994.3 | 3,163.1 |
| Commitments and Contingencies (Note 14) | | |
| SHAREHOLDERS' EQUITY | | |
| Common Stock (Note 2) | 4.4 | 4.4 |
| Additional paid-in capital | 596.7 | 584.4 |
| Retained earnings | 1,767.6 | 1,676.2 |
| Accumulated other comprehensive loss (Note 7) | (74.5) | (110.0) |
| Treasury stock, at cost (Note 2) | (783.8) | (796.8) |
| Total Shareholders' Equity Attributable to Common Shareholders | 1,510.4 | 1,358.2 |
| Noncontrolling interests | — | 7.4 |
| Total Shareholders' Equity | 1,510.4 | 1,365.6 |
| Total Liabilities and Shareholders' Equity | \$4,504.7 | \$ 4,528.7 |
| See Notes to Condensed Consolidated Financial Statements (unaudited) | | |

Table of ContentsHill-Rom Holdings, Inc. and Subsidiaries
Condensed Consolidated Statements of Cash Flows (Unaudited)

| (In millions) | Year to Date | |
|----------------------------------------------------------------------------------------------|----------------|----------|
| | Ended March 31 | |
| | 2018 | 2017 |
| Operating Activities | | |
| Net income | \$116.8 | \$57.5 |
| Adjustments to reconcile net income to net cash provided by operating activities: | | |
| Depreciation | 39.2 | 40.6 |
| Amortization | 9.6 | 10.0 |
| Acquisition-related intangible asset amortization | 53.7 | 52.1 |
| Provision for deferred income taxes | (89.2) | (14.6) |
| Gain on disposal of property, equipment leased to others, intangible assets, and impairments | (0.6) | (3.0) |
| (Gain) loss on disposition of businesses | 22.4 | (1.0) |
| Stock compensation | 15.8 | 12.2 |
| Change in working capital excluding cash, current debt, acquisitions and dispositions: | | |
| Trade accounts receivable | 45.7 | 25.4 |
| Inventories | (29.0) | 2.9 |
| Other current assets | (37.9) | 2.8 |
| Trade accounts payable | (8.7) | (5.7) |
| Accrued expenses and other liabilities | (35.8) | (55.0) |
| Other, net | 23.6 | 2.2 |
| Net cash provided by operating activities | 125.6 | 126.4 |
| Investing Activities | | |
| Capital expenditures and purchases of intangible assets | (51.4) | (47.3) |
| Proceeds on sale of property and equipment leased to others | 3.7 | 10.6 |
| Payment for acquisition of businesses, net of cash acquired | — | (314.3) |
| Proceeds on sale of businesses | 1.0 | 4.5 |
| Other | (1.0) | (0.4) |
| Net cash used in investing activities | (47.7) | (346.9) |
| Financing Activities | | |
| Proceeds from borrowings on long-term debt | 1.0 | 300.0 |
| Payment of long-term debt | (54.9) | (36.6) |
| Borrowings on Revolving Credit Facility | 75.0 | 53.0 |
| Payments on Revolving Credit Facility | (95.0) | (60.8) |
| Borrowings on Securitization Program | 51.4 | — |
| Payments on Securitization Program | (37.3) | — |
| Debt issuance costs | — | (4.3) |
| Payment of cash dividends | (25.1) | (22.9) |
| Proceeds on exercise of stock options | 10.5 | 14.6 |
| Proceeds from stock issuance | 3.0 | 2.3 |
| Treasury stock acquired | (4.4) | (33.6) |
| Net cash provided by (used in) financing activities | (75.8) | 211.7 |
| Effect of exchange rate changes on cash | 5.1 | (4.7) |
| Net Cash Flows | 7.2 | (13.5) |
| Cash and Cash Equivalents: | | |
| At beginning of period | 231.8 | 232.2 |
| At end of period | \$239.0 | \$218.7 |

See Notes to Condensed Consolidated Financial Statements (unaudited)

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Hill-Rom Holdings, Inc. and Subsidiaries

Notes to Condensed Consolidated Financial Statements (Unaudited)

(Dollars in millions, except per share data)

Note 1. Summary of Significant Accounting Policies

Basis of Presentation and Principles of Consolidation

Unless the context otherwise requires, the terms “Hill-Rom,” “the Company,” “we,” “our,” and “us” refer to Hill-Rom Holding Inc. and its wholly-owned subsidiaries. The unaudited Condensed Consolidated Financial Statements appearing in this Quarterly Report on Form 10-Q should be read in conjunction with the audited Consolidated Financial Statements and notes thereto included in Hill-Rom’s latest Annual Report on Form 10-K for the fiscal year ended September 30, 2017 (“2017 Form 10-K”) as filed with the United States (“U.S.”) Securities and Exchange Commission. The September 30, 2017 Condensed Consolidated Balance Sheet was derived from audited Consolidated Financial Statements, but does not include all disclosures required by accounting principles generally accepted in the U.S. In the opinion of management, the Condensed Consolidated Financial Statements herein include all adjustments, consisting only of normal recurring adjustments, necessary to state fairly the financial position, results of operations and cash flows for the interim periods presented. Quarterly results are not necessarily indicative of annual results.

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

Use of Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the U.S. requires management to make estimates and assumptions that affect the reported amounts of certain assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenue and expense during the period. Actual results could differ from those estimates and such differences could be material. Examples of such estimates include, but are not limited to, income taxes (Notes 1 and 9), accounts receivable reserves (Note 2), accrued warranties (Note 12), the impairment of intangibles and goodwill (Note 4), pension expense (Note 6), and commitments and contingencies (Note 14).

Fair Value Measurements

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

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

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

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

We record cash and cash equivalents, as disclosed on our Condensed Consolidated Balance Sheets, as Level 1 instruments and certain other derivatives and investments as either Level 2 or 3 instruments. Investments measured at Net Asset Value as a practical expedient are not categorized in the fair value hierarchy. There have not been significant changes in our classification among assets and liabilities during the fiscal quarter. Refer to Note 5 for disclosure of our debt instrument and interest rate swap fair values.

Taxes Collected from Customers and Remitted to Governmental Units

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

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Income Taxes

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

As of March 31, 2018, we had \$60.0 million of valuation allowances on deferred tax assets, on a tax-effected basis, primarily related to certain foreign deferred tax attributes that are not expected to be utilized. The valuation allowance total was not materially impacted by the Tax Cuts and Jobs Act enacted in December 2017. We believe that our estimates for the valuation allowances recorded against deferred tax assets are appropriate based on current facts and circumstances.

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

Dispositions

During the second quarter of fiscal 2018, we entered into an agreement to convey certain net assets related to the Company's third-party rental business, which is comprised of purchased moveable medical equipment that can be rented to customers, to Universal Hospital Services, Inc. ("UHS") in exchange for UHS's agreement to dismiss its previously disclosed litigation against the Company subject to satisfaction of customary closing conditions ("Settlement Agreement"). We recorded a loss of \$23.4 million in special charges, which includes approximately \$20.4 million related to the non-cash loss reserve for the assets to be conveyed, and other Settlement Agreement related costs of approximately \$3.0 million. The third-party rental business is part of our Patient Support Systems segment. The transaction is expected to close during our fiscal third quarter.

During the fourth quarter of fiscal 2017, we sold our Völker business. During the first quarter of fiscal 2018, we recorded a gain of \$1.0 million attributable to the final working capital settlement associated with the transaction.

Recently Issued Accounting Standards

In May 2014, the FASB issued ASU 2014-09, "Revenue from Contracts with Customers," which provides guidance for revenue recognition. The standard's core principle is that a company will recognize revenue when it transfers promised goods or services to customers in an amount that reflects the consideration to which the company expects to be entitled in exchange for those goods or services. In August 2015, the FASB issued ASU 2015-14 which delayed the effective date of the new revenue guidance by one year, while permitting companies to early adopt the new standard as of the original effective date. As a result, the provisions of ASU 2014-09 and subsequent amendments, are effective for us in the first quarter of fiscal 2019 using either of the following transition methods: (i) a full retrospective approach reflecting the application of the standard in each prior reporting period with the option to elect certain practical expedients, or (ii) a modified retrospective approach with the cumulative effect of initially adopting ASU 2014-09 recognized at the date of adoption. We plan to adopt the new standard effective October 1, 2018 and are continuing to evaluate the impact of adoption on our Consolidated Financial Statements and the implementation

approach to be used.

In February 2016, the FASB issued ASU 2016-02, Leases (Topic 842). From the lessee's perspective, the new standard establishes a right-of-use ("ROU") model that requires a lessee to record a ROU asset and a lease liability on the balance sheet for all leases with terms longer than 12 months. Leases will be classified as either finance or operating, with classification affecting the pattern of expense recognition in the income statement for a lessee. From the lessor's perspective, the new standard requires a lessor to classify leases as either sales-type, finance or operating. A lease will be treated as a sale if it transfers all of the risks and rewards, as well as control of the underlying asset, to the lessee. If risks and rewards are conveyed without the transfer of control, the lease is treated as a financing lease. If the lessor does not convey risks and rewards or control, an operating lease results. ASU 2016-02 is effective for our first quarter of fiscal 2020. A modified retrospective transition approach is required for leases existing at, or entered into after, the beginning of the earliest comparative period presented in the financial statements, with certain practical expedients available. We are currently in the process of evaluating the impact of the amended guidance on our Consolidated Financial Statements.

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Except as noted above, there have been no significant changes to our assessment of the impact of recently issued accounting standards included in Note 1 of our Consolidated Financial Statements in our 2017 Form 10-K.

Note 2. Supplementary Balance Sheet Information

| | March 31, 2018 | September 30, 2017 |
|------------------------------------------------------------------|-------------------|-----------------------|
| Allowance for possible losses and discounts on trade receivables | \$ 23.9 | \$ 25.1 |
| Inventories: | | |
| Finished products | \$ 156.5 | \$ 147.5 |
| Raw materials and work in process | 158.6 | 137.0 |
| Total inventory | \$ 315.1 | \$ 284.5 |
| Accumulated depreciation of property, plant and equipment | \$ 659.3 | \$ 624.2 |
| Accumulated amortization of software and other intangible assets | \$ 553.2 | \$ 492.3 |
| Preferred stock, without par value: | | |
| Shares authorized | 1,000,000 | 1,000,000 |
| Shares issued | None | None |
| Common stock, without par value: | | |
| Shares authorized | 199,000,000 | 199,000,000 |
| Shares issued | 88,457,634 | 88,457,634 |
| Shares outstanding | 66,230,972 | 65,813,794 |
| Treasury shares | 22,226,662 | 22,643,840 |

Note 3. Acquisitions

Mortara Instrument

On February 14, 2017, we completed the acquisition of Mortara Instrument, Inc. ("Mortara") for consideration of \$330.0 million in cash (\$311.2 million, net of cash acquired), primarily financed through a private offering of \$300.0 million of senior unsecured notes (see Note 5 of our Condensed Consolidated Financial Statements). Mortara provides a portfolio of diagnostic cardiology devices designed to serve the full continuum of clinical care, from acute care to primary care and clinical research organizations.

The results of Mortara are included in the Condensed Consolidated Financial Statements since the date of acquisition. The impact to our comparable quarter and year to date fiscal 2017 revenue and net income on an unaudited proforma basis, as if the Mortara acquisition had been consummated at the beginning of our fiscal 2017 year, would not have been significant.

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The following summarizes the fair value of assets acquired and liabilities assumed at the date of the Mortara acquisition. The results are considered final.

| | Amount |
|---------------------------------------------------|---------|
| Trade receivables | \$16.4 |
| Inventory | 21.5 |
| Other current assets | 2.8 |
| Property, plant and equipment | 18.2 |
| Goodwill | 165.5 |
| Trade names (7-year weighted average useful life) | 15.8 |
| Customer relationships (8-year useful life) | 37.9 |
| Developed technology (7-year useful life) | 52.3 |
| Other noncurrent assets | 4.8 |
| Current liabilities | (22.8) |
| Noncurrent liabilities | (1.2) |
| Total purchase price, net of cash acquired | \$311.2 |

Goodwill in connection with the Mortara acquisition was allocated entirely to our Front Line Care segment. A majority of the goodwill is attributable to the acquired U.S. operations which is deductible for tax purposes.

Note 4. Goodwill and Indefinite-Lived Intangible Assets

The following summarizes goodwill activity by reportable segment:

| | Patient Support Systems | Front Line Care | Surgical Solutions | Total |
|----------------------------------------|-------------------------------|-----------------------|-----------------------|-----------|
| Balances at September 30, 2017 | | | | |
| Goodwill | \$545.0 | \$1,375.6 | \$311.8 | \$2,232.4 |
| Accumulated impairment losses | (472.8) | — | — | (472.8) |
| Goodwill, net at September 30, 2017 | 72.2 | 1,375.6 | 311.8 | 1,759.6 |
| Changes in Goodwill during the period: | | | | |
| Goodwill related to acquisitions | — | 0.8 | — | 0.8 |
| Deconsolidation of VIE | — | — | (13.2) | (13.2) |
| Currency translation effect | 1.3 | 1.0 | 4.7 | 7.0 |
| Balances at March 31, 2018 | | | | |
| Goodwill | 546.3 | 1,377.4 | 303.3 | 2,227.0 |
| Accumulated impairment losses | (472.8) | — | — | (472.8) |
| Goodwill, net at March 31, 2018 | \$73.5 | \$1,377.4 | \$303.3 | \$1,754.2 |

During the second fiscal quarter of 2018, the Company deconsolidated a variable interest entity as a result of no longer having a controlling financial interest in the entity upon the termination of an exclusive distribution agreement. The portion of this entity's assets, including goodwill, liabilities and operating results that are not attributable to the Company are excluded from our Consolidated Financial Statements as of the effective date of the termination.

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Note 5. Financing Agreements

Total debt consists of the following:

| | March 31, 2018 | September 30, 2017 |
|-------------------------------------------------------|-------------------|-----------------------|
| Revolving credit facilities | \$ 70.0 | \$ 90.0 |
| Current portion of long-term debt | 128.1 | 109.8 |
| Senior secured Term Loan A, long-term portion | 1,195.6 | 1,266.7 |
| Senior unsecured 5.75% notes due on September 1, 2023 | 420.4 | 419.9 |
| Senior unsecured 5.00% notes due on February 14, 2025 | 296.1 | 295.8 |
| Unsecured 7.00% debentures due on February 15, 2024 | 13.6 | 13.6 |
| Unsecured 6.75% debentures due on December 15, 2027 | 29.6 | 29.6 |
| Securitization Program | 93.2 | 79.1 |
| Other | 0.3 | 4.8 |
| Total debt | 2,246.9 | 2,309.3 |
| Less Short-term borrowings | 221.3 | 188.9 |
| Total Long-term debt | \$ 2,025.6 | \$ 2,120.4 |

In May 2017, we entered into a 364-day \$110.0 million accounts receivable securitization program (the “Securitization Program”) with certain financial institutions. Under the terms of the Securitization Program, certain of our accounts receivable secure the amounts borrowed and cannot be used to pay our other debts or liabilities. The amount that we may borrow at a given point in time is determined based on the amount of qualifying accounts receivable that are present at such point in time. As of March 31, 2018, \$93.2 million was borrowed under the Securitization Program. Borrowings outstanding under the Securitization Program bear interest at the London Interbank Offered Rate (“LIBOR”) plus the applicable margin of 0.675% and are included as a component of Short-term borrowings, while the accounts receivable securing these obligations remain as a component of Trade accounts receivable, net of allowances in our Condensed Consolidated Balance Sheets. In addition, the agreement governing the Securitization Program contains various customary affirmative and negative covenants, and customary default and termination provisions. As of March 31, 2018, we were in compliance with these covenants and provisions.

In February 2017, we entered into \$300.0 million of senior unsecured notes maturing February 2025 for purposes of financing the Mortara acquisition. These notes bear interest at a fixed rate of 5.00% annually. We also have outstanding senior unsecured notes of \$425.0 million maturing in September 2023 that bear interest at a fixed rate of 5.75% annually (collectively, the “Senior Notes”). These Senior Notes were issued at par in private placement offerings and are not registered securities on any public market. All of the notes were outstanding as of March 31, 2018. We are not required to make any mandatory redemption or sinking fund payments with respect to the Senior Notes, other than in certain circumstances such as a change in control or material sale of assets. We may redeem the 5.75% and 5.00% notes prior to maturity, but doing so prior to September 1, 2021 and February 15, 2023, respectively, would require payment of a premium on any amounts redeemed, the amount of which varies based on the timing of the redemption. The indentures governing the Senior Notes contain certain covenants which impose limitations on the amount of dividends we may pay and the amount of common shares we may repurchase in the open market, but we do not expect these covenants to affect our current dividend policy or open share repurchase program. The terms of these indentures also impose certain restrictions on the amount and type of additional indebtedness we may obtain in the future, as well as the types of liens and guarantees we may provide.

Our Senior Credit Agreement consists of two facilities as follows:

\$1,462.5 million senior secured Term Loan A facility (“TLA Facility”), maturing in September 2021

Revolving Credit Facility, providing borrowing capacity of up to \$700.0 million, maturing in September 2021

The TLA Facility and Revolving Credit Facility bear interest at variable rates which currently approximate 3.4%. These interest rates are based primarily on LIBOR, but under certain conditions could also be based on the U.S. Federal Funds Rate or the U.S. Prime Rate, at our option. The TLA Facility requires minimum principal payments of \$109.7 million in fiscal 2018 and \$146.3 million annually thereafter, with the remaining unpaid principal balance due at maturity. We are able to voluntarily prepay outstanding loans under the TLA Facility at any time. During the year to date period ended March 31, 2018, we made required minimum payments of \$54.8 million on the TLA Facility.

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At March 31, 2018, there were \$70.0 million of borrowings on the Revolving Credit Facility, and available borrowing capacity was \$622.0 million after giving effect to \$8.0 million of outstanding standby letters of credit. The availability of borrowings under our Revolving Credit Facility is subject to our ability at the time of borrowing to meet certain specified conditions, including compliance with covenants contained in the Senior Credit Agreement.

The facilities provided by the Senior Credit Agreement are held with a syndicate of banks, which includes over 30 institutions. Our general corporate assets, including those of our subsidiaries, collateralize these obligations. The credit agreement governing these facilities contains financial covenants which specify a maximum secured net leverage ratio and a minimum interest coverage ratio, as such terms are defined in the credit agreement. These financial covenants are measured at the end of each fiscal quarter. The required ratios vary providing a gradually decreasing maximum secured net leverage ratio and a gradually increasing minimum interest coverage ratio, as set forth in the table below:

| Any Fiscal Quarter Ended During the Calendar Year Ending: | Maximum Secured Net Leverage Ratio | Minimum Interest Coverage Ratio |
|-----------------------------------------------------------|------------------------------------------|------------------------------------------|
| December 31, 2017 | 4.00x | 3.50x |
| December 31, 2018 | 3.50x | 3.75x |
| December 31, 2019 and thereafter | 3.00x | 4.00x |

We were in compliance with all financial covenants under our Senior Credit Agreement as of March 31, 2018.

We are exposed to market risk from fluctuations in interest rates. We sometimes manage our exposure to interest rate fluctuations through the use of interest rate swaps. As of March 31, 2018, we had seven interest rate swap agreements, with notional amounts of \$750.0 million, in aggregate, to hedge the variability of cash flows associated with a portion of the variable interest rate payments through September 2021 on the Senior Secured Credit Facilities. The interest rate swaps have effective start dates ranging between December 31, 2017 and September 8, 2020 and were designated as cash flow hedges. As of March 31, 2018, these swaps were in a net asset position with an aggregate fair value of \$21.7 million, all of which were classified as Other assets. As of September 30, 2017, these swaps were in a net asset position with an aggregate fair value of \$7.3 million, of which \$8.5 million were classified as Other assets and \$1.2 million were classified as Other current liabilities. We classify fair value measurements on our interest rate swaps as Level 2, as described in Note 1.

The fair value of our debt is estimated based on the quoted market prices for the same or similar issues or on the current rates offered to us for debt of the same remaining maturities. The book values of our short-term debt instruments and Revolving Credit Facility approximate fair value.

The estimated fair values of our long-term debt instruments, including the current portion, are described in the table below:

| | March 31, 2018 | September 30, 2017 |
|-------------------------------------------------------|-------------------|-----------------------|
| Senior secured Term Loan A | \$ 1,309.3 | \$ 1,364.8 |
| Senior unsecured 5.75% notes due on September 1, 2023 | 440.5 | 449.3 |
| Senior unsecured 5.00% notes due on February 14, 2025 | 297.9 | 311.9 |
| Unsecured debentures | 44.3 | 46.8 |
| Total | \$ 2,092.0 | \$ 2,172.8 |

The estimated fair values of our long-term unsecured debentures were based on observable inputs such as quoted prices in markets that are not active. The estimated fair values of our term loans and the Senior Notes were based on

quoted prices for similar liabilities. These fair value measurements are classified as Level 2, as described in Note 1.

Note 6. Retirement and Postretirement Plans

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

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| | Quarter Ended | | Year to Date Ended | |
|------------------------------------------------------|---------------|--------|--------------------|--------|
| | March 31 | | March 31 | |
| | 2018 | 2017 | 2018 | 2017 |
| Service cost | \$1.2 | \$1.5 | \$2.4 | \$2.9 |
| Interest cost | 2.8 | 2.4 | 5.5 | 4.9 |
| Expected return on plan assets | (4.0) | (3.6) | (7.9) | (7.3) |
| Amortization of unrecognized prior service cost, net | — | — | — | 0.1 |
| Amortization of net loss | 1.0 | 1.6 | 2.2 | 3.1 |
| Net pension expense | \$1.0 | \$1.9 | \$2.2 | \$3.7 |

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

We have defined contribution savings plans that cover substantially all U.S. employees and certain non-U.S. employees. The general purpose of these plans is to provide additional financial security during retirement by providing employees with an incentive to make regular savings. Our contributions to the plans are based on eligibility and employee contributions. Expense under these plans was \$7.5 million and \$7.1 million in each of the quarterly periods ended March 31, 2018 and 2017, and \$13.9 million and \$13.1 million in the year to date periods ended March 31, 2018 and 2017.

Note 7. Other Comprehensive Income (Loss)

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

| | Quarter Ended March 31, 2018 | | | | | | Accumulated other comprehensive income (loss) | | |
|------------------------------------------------------------|-----------------------------------|-----------------------|----------|------------|------------|-------------------|-----------------------------------------------|----------------|--|
| | Other comprehensive income (loss) | | | | | | Accumulated other comprehensive income (loss) | | |
| | Prior to reclassification | Reclassification from | Pre-tax | Tax effect | Net of tax | Beginning balance | Net activity | Ending balance | |
| Derivative instruments and hedges | \$9.7 | \$ (0.5) | \$ 9.2 | \$(1.3) | \$7.9 | \$7.7 | \$ 7.9 | \$15.6 | |
| Foreign currency translation adjustment | 16.5 | — | 16.5 | — | 16.5 | (75.2) | 16.5 | (58.7) | |
| Change in pension and postretirement defined benefit plans | (0.1) | 1.0 | 0.9 | (0.1) | 0.8 | (32.2) | 0.8 | (31.4) | |
| Total | \$26.1 | \$ 0.5 | \$ 26.6 | \$(1.4) | \$25.2 | \$(99.7) | \$ 25.2 | \$(74.5) | |
| | Quarter Ended March 31, 2017 | | | | | | Accumulated other comprehensive income (loss) | | |
| | Other comprehensive income (loss) | | | | | | Accumulated other comprehensive income (loss) | | |
| | Prior to reclassification | Reclassification from | Pre-tax | Tax effect | Net of tax | Beginning balance | Net activity | Ending balance | |
| Derivative instruments and hedges | \$0.4 | \$ (0.5) | \$(0.1) | \$(0.1) | \$(0.2) | \$7.1 | \$(0.2) | \$6.9 | |
| Foreign currency translation adjustment | 14.0 | — | 14.0 | — | 14.0 | (154.7) | 14.0 | (140.7) | |
| Change in pension and postretirement defined benefit plans | — | 1.4 | 1.4 | (0.6) | 0.8 | (49.5) | 0.8 | (48.7) | |

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| | | | | | | | | |
|-------|--------|--------|--------|---------|--------|-----------|--------|-----------|
| Total | \$14.4 | \$ 0.9 | \$15.3 | \$(0.7) | \$14.6 | \$(197.1) | \$14.6 | \$(182.5) |
|-------|--------|--------|--------|---------|--------|-----------|--------|-----------|

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| Year to Date Ended March 31, 2018 | | | | | | | | |
|------------------------------------------------------------|---------------------------|-----------------------|-----------|------------|------------|-----------------------------------------------|--------------|----------------|
| Other comprehensive income (loss) | | | | | | Accumulated other comprehensive income (loss) | | |
| | Prior to reclassification | Reclassification from | Pre-tax | Tax effect | Net of tax | Beginning balance | Net activity | Ending balance |
| Derivative instruments and hedges | \$15.5 | \$ (0.9) | \$ 14.6 | \$ (3.3) | \$ 11.3 | \$ 4.3 | \$ 11.3 | \$ 15.6 |
| Foreign currency translation adjustment | 22.6 | — | 22.6 | — | 22.6 | (81.3) | 22.6 | (58.7) |
| Change in pension and postretirement defined benefit plans | (0.2) | 2.2 | 2.0 | (0.4) | 1.6 | (33.0) | 1.6 | (31.4) |
| Total | \$37.9 | \$ 1.3 | \$ 39.2 | \$ (3.7) | \$ 35.5 | \$ (110.0) | \$ 35.5 | \$ (74.5) |
| Year to Date Ended March 31, 2017 | | | | | | | | |
| Other comprehensive income (loss) | | | | | | Accumulated other comprehensive income (loss) | | |
| | Prior to reclassification | Reclassification from | Pre-tax | Tax effect | Net of tax | Beginning balance | Net activity | Ending balance |
| Derivative instruments and hedges | \$16.6 | \$ (0.7) | \$ 15.9 | \$ (5.9) | \$ 10.0 | \$ (3.1) | \$ 10.0 | \$ 6.9 |
| Foreign currency translation adjustment | (25.5) | — | (25.5) | — | (25.5) | (115.2) | (25.5) | (140.7) |
| Change in pension and postretirement defined benefit plans | 0.4 | 2.9 | 3.3 | (1.2) | 2.1 | (50.8) | 2.1 | (48.7) |
| Total | \$ (8.5) | \$ 2.2 | \$ (6.3) | \$ (7.1) | \$ (13.4) | \$ (169.1) | \$ (13.4) | \$ (182.5) |

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

| Quarter Ended March 31 | | | | | |
|----------------------------------------------------------------|---------|------------|---------|------------|------------|
| 2018 | | | 2017 | | |
| | Amount | Tax effect | Amount | Tax effect | Net of tax |
| Derivative instruments and hedges (a) | \$(0.5) | \$— | \$(0.5) | \$0.1 | \$(0.4) |
| Change in pension and postretirement defined benefit plans (b) | \$1.0 | \$(0.1) | \$0.9 | \$1.4 | \$(0.6) |
| Year to Date Ended March 31 | | | | | |
| 2018 | | | 2017 | | |
| | Amount | Tax effect | Amount | Tax effect | Net of tax |
| Derivative instruments and hedges (a) | \$(0.9) | \$0.2 | \$(0.7) | \$0.2 | \$(0.5) |
| Change in pension and postretirement defined benefit plans (b) | \$2.2 | \$(0.4) | \$1.8 | \$2.9 | \$(1.1) |

(a) Reclassified from accumulated other comprehensive income (loss) into Interest expense.

(b) Reclassified from accumulated other comprehensive income (loss) into Cost of goods sold and Selling and administrative expenses. These components are included in the computation of net periodic pension expense.

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Note 8. Special Charges

In connection with various organizational changes to improve our business alignment and cost structure, we recognized special charges of \$36.9 million and \$3.1 million for the quarters ended March 31, 2018 and 2017, and \$50.4 million and \$8.9 million for the year to date periods ended March 31, 2018 and 2017. These charges are summarized as follows:

Dispositions

During the second quarter of fiscal 2018, we entered into an agreement to convey certain assets related to the Company's third-party rental business to UHS and recorded an after-tax loss of \$23.4 million in special charges.

Business Optimization

During the first quarter of fiscal 2018, we initiated a global transformation program focused on reducing complexity, increasing efficiency, improving our cost structure and accelerating growth with targeted investments that align with our strategic priorities. For the quarter and year to date periods ended March 31, 2018, this program resulted in charges of \$9.6 million and \$18.8 million, of which \$4.8 million and \$10.8 million were severance and benefit costs. We continue to evaluate additional actions related to this program and expect additional special charges to be incurred. However, it is not practicable to estimate the amount of these future expected costs until such time as the evaluations are complete.

Site Consolidation

In the third quarter of fiscal 2015, we initiated a plan to streamline our operations and simplify our supply chain by consolidating certain manufacturing and distribution operations ("Site Consolidation"). As part of this action, we have announced the closure of five sites. During the quarter and year to date periods ended March 31, 2018, we recorded total charges of \$3.8 million and \$7.8 million, related to these efforts, of which \$0.5 million and \$0.7 million were severance and benefit costs. These amounts compare to charges of \$6.2 million and \$9.8 million, during the quarter and year to date periods ended March 31, 2017, of which \$1.7 million were severance and benefit costs for the quarter and year to date periods ended March 31, 2017.

During the second quarter of fiscal 2017, we sold our Charleston property for \$6.1 million in cash proceeds and recorded a gain of \$5.2 million.

Since the inception of the Site Consolidation program through March 31, 2018, we have recognized aggregate special charges of \$42.8 million. We continue to evaluate our facilities footprint and expect to incur additional costs with respect to other actions in the future, however, it is not practicable to estimate the amount of these future expected costs until such time as the evaluations are complete.

Integration and Business Realignment

We acquired Mortara and Tridien and initiated integration activities to optimize the available synergies of our combined company. Additionally, with the acquisition of Welch Allyn in September 2015, we initiated plans to realign our business structure to facilitate the integration, take full advantage of available synergies, and position our existing businesses to capitalize on opportunities for growth. We also incurred costs, including severance and benefit costs, associated with other business realignment and integration activities. During the quarter and year to date periods ended March 31, 2018, we incurred total integration and business realignment charges of approximately \$0.1 million and \$0.4 million. These amounts compare to charges of \$2.1 million and \$2.3 million during the quarter and year to date periods ended March 31, 2017, of which \$1.4 million were severance and benefit costs for the quarter and year to date periods ended March 31, 2017. We do not expect to incur significant additional special charges in relation to these activities.

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For all accrued severance and other benefit charges described above, we record restructuring reserves within Other current liabilities. The reserve activity for severance and other benefits during the year to date period ended March 31, 2018 was as follows:

| | |
|-------------------------------|--------|
| Balance at September 30, 2017 | \$ 9.0 |
| Expenses | 11.5 |
| Cash Payments | (12.6) |
| Balance at March 31, 2018 | \$ 7.9 |

Note 9. Income Taxes

The effective tax rate for the quarter and year to date periods ended March 31, 2018 was (32.6)% and (123.3)% compared to 17.7% and 24.9% for the quarter and year to date periods in the prior year. The effective tax rate for the current quarter is lower than the comparable period in fiscal 2017 due to period tax benefits of \$11.2 million primarily related to a change in a tax accounting

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method approved by the Internal Revenue Service in the current period. The change in accounting method resulted in a reduction in U.S. tax for prior year currency exchange losses. The effective tax rate for the year to date period is lower than the comparable period in fiscal 2017 due to the lower corporate tax rate and period tax benefits of \$75.6 million primarily related to recording the items attributable to the new tax legislation in the U.S. as described below and the change in tax accounting method. The comparable prior year period included period tax benefits of \$3.5 million primarily related to the adoption of the ASU 2016-09 partially offset by the expense to revalue the France deferred tax assets due to the law change that reduced the future corporate income tax rate in France.

On December 22, 2017, the U.S. government enacted comprehensive tax legislation commonly referred to as the Tax Cuts and Jobs Act (the “Tax Act”). The Tax Act makes broad and complex changes to the U.S. tax code which will impact our fiscal year ended September 30, 2018 including, but not limited to (1) reducing the U.S. federal corporate tax rate, (2) requiring a one-time transition tax on certain unrepatriated earnings of foreign subsidiaries that may electively be paid over eight years, and (3) accelerated first year expensing of certain capital expenditures. The Tax Act reduces the federal corporate tax rate from 35 percent to 21 percent effective January 1, 2018. Internal Revenue Code Section 15 provides that our fiscal year ended September 30, 2018 will have a blended corporate tax rate of 24.5 percent, which is based on a proration of the applicable tax rates before and after effective date of the Tax Act. The statutory tax rate of 21 percent will apply for fiscal 2019 and beyond.

The Tax Act also puts in place new tax laws that will impact our taxable income beginning in fiscal 2019, which include, but are not limited to (1) creating a Base Erosion Anti-abuse Tax (BEAT), which is a new minimum tax, (2) generally eliminating U.S. federal income taxes on dividends from foreign subsidiaries, (3) a new provision designed to tax currently global intangible low-taxed income (GILTI), which allows for the possibility of utilizing foreign tax credits and a deduction equal to 50 percent to offset the income tax liability (subject to some limitations), (4) a provision that could limit the amount of deductible interest expense, (5) the repeal of the domestic production activity deduction, (6) limitations on the deductibility of certain executive compensation, and (7) limitations on the utilization of foreign tax credits to reduce the U.S. income tax liability.

Shortly after the Tax Act was enacted, the SEC staff issued Staff Accounting Bulletin No. 118, Income Tax Accounting Implications of the Tax Cuts and Jobs Act (SAB 118) which provides guidance on accounting for the Tax Act’s impact. SAB 118 provides a measurement period, which in no case should extend beyond one year from the Tax Act enactment date, during which a company acting in good faith may complete the accounting for the impacts of the Tax Act under ASC Topic 740. In accordance with SAB 118, the Company must reflect the income tax effects of the Tax Act in the reporting period in which the accounting under ASC Topic 740 is complete.

To the extent that a company’s accounting for certain income tax effects of the Tax Act is incomplete, the Company can determine a reasonable estimate for those effects and record a provisional estimate in the financial statements in the first reporting period in which a reasonable estimate can be determined. If a Company cannot determine a provisional estimate to be included in the financial statements, the Company should continue to apply ASC 740 based on the provisions of the tax laws that were in effect immediately prior to the Tax Act being enacted. If a Company is unable to provide a reasonable estimate of the impacts of the Tax Act in a reporting period, a provisional amount must be recorded in the first reporting period in which a reasonable estimate can be determined.

We have recorded a provisional discrete net tax benefit of \$61.4 million related to the Tax Act in the year to date period ending March 31, 2018. No additional adjustments were recorded in the current quarter. This net benefit primarily consists of a net benefit of \$93.8 million due to the remeasurement of our deferred tax accounts to reflect the corporate rate reduction impact to our net deferred tax balances and a net expense for the transition tax of \$32.4 million.

Reduction in U.S. Corporate Rate: The Tax Act reduces the U.S. federal statutory corporate tax rate to 24.5 percent in fiscal year ending September 30, 2018 and 21 percent for fiscal year ending September 30, 2019 and beyond. We have recorded a provisional adjustment to our net deferred tax balances, with a corresponding discrete net tax benefit of \$93.8 million in the current year to date period. In our annual effective tax rate we have reflected the tax effect of the temporary differences that will originate subsequent to the Tax Act and are required to be remeasured at the 21 percent tax rate. While we are able to make a reasonable estimate of the impact of the reduction in corporate rate, we are continuing to analyze the temporary differences that existed on the date of enactment, and the temporary differences originating in the current fiscal year.

Transition Tax: The transition tax is a fiscal 2018 tax on the previously untaxed accumulated and current earnings and profits (E&P) of certain of our foreign subsidiaries. In order to determine the amount of the Transition Tax, we must determine, in addition to other factors, the amount of post-1986 E&P of the relevant subsidiaries, as well as the amount of non-U.S. income taxes paid on such earnings. E&P is similar to retained earnings of the subsidiary, but requires other adjustments to conform to U.S. tax rules. We are able to make a reasonable estimate of the transition tax and recorded a provisional transition tax obligation of \$32.4 million which we expect to elect to pay, net of certain tax credit carryforwards, over eight years beginning in fiscal 2019. This

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amount is presented in Other long-term liabilities. However, we are awaiting further interpretative guidance, continuing to assess available tax methods and elections, and continuing to gather additional information to more precisely compute the amount of the transition tax.

Global intangible low-taxed income (GILTI): The Tax Act includes a provision designed to currently tax global intangible low-taxed income starting in fiscal 2019. Due to the complexity of the new GILTI tax rules, we are continuing to evaluate this provision of the Tax Act, the application of ASC 740, and are considering available accounting policy alternatives to adopt to either record the U.S. income tax effect of future GILTI inclusions in the period in which they arise or establish deferred taxes with respect to the expected future tax liabilities associated with future GILTI inclusions. Our accounting policies depend, in part, on analyzing our global income to determine whether we expect a tax liability resulting from the application of this provision, and, if so, whether and when to record related current and deferred income taxes. Whether we intend to recognize deferred tax liabilities related to the GILTI provisions is dependent, in part, on our assessment of the Company's future operating structure. In addition, we are awaiting further interpretive guidance in connection with the computation of the GILTI tax. For these reasons, we are not yet able to reasonably estimate the effect of this provision of the Tax Act. Therefore, we have not made any adjustments relating to potential GILTI tax in our financial statements and have not made a policy decision regarding our accounting for GILTI.

As of September 30, 2017, our practice and intention was to reinvest the earnings in our non-U.S. subsidiaries outside of the U.S., and no U.S. deferred income taxes or foreign withholding taxes were recorded. The transition tax noted above will result in the previously untaxed foreign earnings being included in the federal and state fiscal 2018 taxable income. We are currently analyzing our global working capital requirements and the potential tax liabilities that would be incurred if the non-U.S. subsidiaries distribute cash to the U.S. parent, which include local country withholding tax and potential U.S. state taxation. Furthermore, the transition tax will close a majority of the outside basis differences in our foreign corporations and any remaining temporary difference will potentially have some interaction with the GILTI tax noted above. For these reasons, we are not yet able to reasonably estimate the effect of this provision of the Tax Act and have not recorded any withholding or state tax liabilities, any deferred taxes attributable to GILTI (as noted above) or any deferred taxes attributable to our investment in our foreign subsidiaries.

We are also currently analyzing other provisions of the Tax Act that come into effect for tax years starting October 1, 2018 to determine if these items would impact the effective tax rate. These provisions include BEAT, eliminating U.S. federal income taxes on dividends from foreign subsidiaries, the treatment of amounts in accumulated other comprehensive income, the new provision that could limit the amount of deductible interest expense, and the limitations on the deductibility of certain executive compensation.

Note 10. Earnings per Common Share

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

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

| | Quarter Ended | | Year to Date Ended | |
|------------------------------------------------------------------------------------|---------------|--------|--------------------|--------|
| | March 31 | | March 31 | |
| | 2018 | 2017 | 2018 | 2017 |
| Net income attributable to common shareholders | \$28.5 | \$34.4 | \$116.8 | \$58.2 |
| Average shares outstanding - Basic | 66,192 | 65,462 | 66,040 | 65,473 |
| Add potential effect of exercise of stock options and other unvested equity awards | 1,405 | 1,670 | 1,468 | 1,584 |
| Average shares outstanding - Diluted | 67,597 | 67,132 | 67,508 | 67,057 |
| Net income attributable to common shareholders per common share - Basic | \$0.43 | \$0.52 | \$1.77 | \$0.89 |
| Net income attributable to common shareholders per common share - Diluted | \$0.42 | \$0.51 | \$1.73 | \$0.87 |
| Shares with anti-dilutive effect excluded from the computation of Diluted EPS | 280 | 348 | 225 | 500 |

Note 11. Common Stock

The stock-based compensation cost that was charged against income, net of tax, for all plans was \$7.0 million and \$4.5 million in the quarterly periods ended March 31, 2018 and 2017, and \$11.6 million and \$7.7 million in the year to date periods ended March 31, 2018 and 2017.

During the first quarter of fiscal 2017, we purchased 0.6 million shares of our common stock for \$30.0 million in the open market.

As of March 31, 2018, a cumulative total of \$175.3 million of our share repurchase program had been used, leaving us with approximately \$165.0 million of availability. This program does not have an expiration date and there are no plans to terminate this program in the future.

Note 12. Guarantees

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

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

| | Quarter Ended | | Year to Date Ended | |
|--------------------------------------------|---------------|--------|--------------------|--------|
| | March 31 | | March 31 | |
| | 2018 | 2017 | 2018 | 2017 |
| Balance at beginning of period | \$25.3 | \$26.3 | \$25.5 | \$27.5 |
| Provision for warranties during the period | 4.0 | 3.7 | 7.5 | 6.3 |
| Warranty reserves acquired | — | 1.9 | — | 1.9 |
| Warranty claims during the period | (4.3) | (4.5) | (8.0) | (8.3) |

| | | | | |
|--------------------------|--------|--------|--------|--------|
| Balance at end of period | \$25.0 | \$27.4 | \$25.0 | \$27.4 |
|--------------------------|--------|--------|--------|--------|

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

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

Note 13. Segment Reporting

We disclose segment information that is consistent with the way in which management operates and views the business. Our operating structure contains the following reporting segments:

Patient Support Systems – globally provides our specialty bed frames and surfaces and mobility solutions, as well as our clinical workflow solutions which specializes in software and information technologies to improve care and deliver actionable insight to caregivers and patients.

Front Line Care – globally provides and sells patient monitoring and diagnostic technologies, including a diversified portfolio of physical assessment tools that help diagnose, treat and manage a wide variety of illnesses and diseases, as well as a portfolio of respiratory care devices.

Surgical Solutions – globally provides products that improve surgical safety and efficiency in the operating room including tables, lights, pendants, positioning devices and various other surgical products and accessories.

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

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Non-allocated operating costs, administrative costs, and other includes functional expenses that support the entire organization such as administration, finance, legal and human resources, expenses associated with strategic developments, acquisition-related intangible asset amortization, and other events that are not indicative of operating trends. We exclude such amounts from divisional income to allow management to evaluate and understand divisional operating trends. The chief operating decision maker does not receive any asset information by operating segment and, accordingly, we do not report asset information by operating segment.

| | Quarter Ended March 31 | | Year to Date Ended March 31 | |
|----------------------------------------------------------------|---------------------------|---------|--------------------------------|-----------|
| | 2018 | 2017 | 2018 | 2017 |
| Revenue: | | | | |
| Patient Support Systems | \$355.0 | \$362.9 | \$689.4 | \$698.1 |
| Front Line Care | 237.9 | 211.0 | 462.5 | 412.8 |
| Surgical Solutions | 117.6 | 105.0 | 228.3 | 205.4 |
| Total revenue | \$710.5 | \$678.9 | \$1,380.2 | \$1,316.3 |
| Divisional income: | | | | |
| Patient Support Systems | \$67.2 | \$63.2 | \$120.6 | \$111.3 |
| Front Line Care | 60.5 | 50.7 | 115.9 | 103.9 |
| Surgical Solutions | 15.5 | 9.2 | 25.2 | 17.3 |
| Other operating costs: | | | | |
| Non-allocated operating costs, administrative costs, and other | 60.2 | 56.4 | 113.1 | 104.0 |
| Special charges | 36.9 | 3.1 | 50.4 | 8.9 |
| Operating profit | 46.1 | 63.6 | 98.2 | 119.6 |
| Interest expense | (24.2) | (21.9) | (47.3) | (41.4) |
| Investment income and other, net | (0.4) | (0.4) | 1.4 | (1.6) |
| Income before income taxes | \$21.5 | \$41.3 | \$52.3 | \$76.6 |

Note 14. Commitments and Contingencies

General

We are subject to various claims and contingencies arising out of the normal course of business, including those relating to governmental investigations and proceedings, commercial transactions, product liability, employee related matters, antitrust, safety, health, taxes, environmental and other matters. Litigation is subject to many uncertainties and the outcome of individual litigated matters is not predictable with assurance. It is possible that some litigation matters for which reserves have not been established could be decided unfavorably to us, and that any such unfavorable decisions could have a material adverse effect on our financial condition, results of operations, and cash flows.

Self Insurance

We are also involved in other possible claims, including product and general liability, workers' compensation, auto liability and employment related matters. Such claims in the United States have deductibles and self-insured retentions ranging from \$25 thousand to \$1.0 million per occurrence or per claim, depending upon the type of coverage and policy period. International deductibles and self-insured retentions are lower. We are also generally self-insured up to certain stop-loss limits for certain employee health benefits, including medical, drug and dental. Our policy is to estimate reserves based upon a number of factors including known claims, estimated incurred but not reported claims

and outside actuarial analysis, which are based on historical information along with certain assumptions about future events. Such estimated reserves are classified as Other Current Liabilities and Other Long-Term Liabilities within the Condensed Consolidated Balance Sheets.

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Universal Hospital Services, Inc. Litigation

On March 7, 2018, we entered into a Settlement Agreement with UHS related to previously disclosed litigation which, among other things, provided for the conveyance of certain net assets relating to our third party rental business, subject to the satisfaction of customary closing conditions. UHS has agreed to drop its lawsuit against the Company as part of the Settlement Agreement. We have recorded a loss of \$23.4 million in special charges, which includes approximately \$20.4 million related to the non-cash loss reserve for the assets to be conveyed, and other Settlement Agreement related costs of approximately \$3.0 million.

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

Forward-Looking Statements and Factors That May Affect Future Results

Certain statements in this Quarterly Report on Form 10-Q contain forward-looking statements, within the meanings of the Private Securities Litigation Reform Act of 1995, regarding our future plans, objectives, beliefs, expectations, representations and projections.

Forward-looking statements are not guarantees of future performance, and our actual results could differ materially from those set forth in any forward-looking statements. For a more in depth discussion of factors that could cause actual results to differ from those contained in forward-looking statements, see the discussions under the heading “Risk Factors” in our previously filed most recent Annual Report on Form 10-K for the fiscal year ended September 30, 2017 (“2017 Form 10-K”) as well as the discussions in this “Management’s Discussion and Analysis”. We assume no obligation to update or revise any forward-looking statements unless required by law.

Overview

The following discussion and analysis should be read in conjunction with the accompanying interim financial statements and our 2017 Form 10-K.

Hill-Rom Holdings, Inc. (“we,” “us,” “our,” or the “Company”), is a leading global medical technology company and more than 10,000 employees worldwide help people get better care inside and outside the hospital. Our innovations in five core areas – Advancing Mobility, Wound Care and Prevention, Patient Monitoring and Diagnostics, Surgical Safety and Efficiency, and Respiratory Health – improve clinical and economic outcomes and ensure caregivers in more than 100 countries have the products they need to protect their patients, speed up recoveries and manage conditions. Every day, around the world, we enhance outcomes for patients and their caregivers.

Use of Non-GAAP Financial Measures

The accompanying Condensed Consolidated Financial Statements, including the related notes, are presented in accordance with accounting principles generally accepted in the U.S. (“GAAP”). We routinely provide gross margin, operating margin, income tax expense and earnings per share results on an adjusted basis because the Company’s management believes these measures contribute to an understanding of our financial performance, provide additional analytical tools to understand our results from core operations and reveal underlying trends. These measures exclude strategic developments, acquisition and integration costs, special charges, the one-time impact of the Tax Act as described in Note 9 or other unusual events. The Company also excludes the amortization of intangible assets associated with prior business acquisitions. These adjustments are made to allow investors to evaluate and understand operating trends excluding the non-cash impact of acquired intangible amortization on operating income and earnings per share.

Management uses these measures internally for planning, forecasting and evaluating the performance of the business. Investors should consider non-GAAP measures in addition to, not as a substitute for, or as superior to, measures of financial performance prepared in accordance with GAAP.

In addition, we present certain results on a constant currency basis which compares results between periods as if foreign currency exchange rates had remained consistent period-over-period. We monitor sales performance on an adjusted basis that eliminates the positive or negative effects that result from translating international sales into U.S. dollars. We calculate constant currency by applying the foreign currency exchange rate for the prior period to the local

currency results for the current period. We believe that evaluating growth in net revenue on a constant currency basis provides an additional and meaningful assessment to both management and investors.

Results of Operations

In this section, we provide an overview of our results of operations. We disclose segment information that is consistent with the way in which management operates and views the business. Our operating structure contains the following reporting segments:

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Patient Support Systems – globally provides our specialty bed frames and surfaces and mobility solutions, as well as our clinical workflow solutions which specializes in software and information technologies to improve care and deliver actionable insight to caregivers and patients.

Front Line Care – globally provides and sells patient monitoring and diagnostic technologies, including a diversified portfolio of physical assessment tools that help diagnose, treat and manage a wide variety of illnesses and diseases, as well as a portfolio of respiratory care devices.

Surgical Solutions – globally provides products that improve surgical safety and efficiency in the operating room including tables, lights, pendants, positioning devices and various other surgical products and accessories.

Net Revenue

| | Quarter Ended | | Change | | Constant | | U.S. | | OUS | | Constant | |
|---------------------------|---------------|----------|----------|---|----------|---|----------|---|----------|---|----------|---|
| | March 31 | March 31 | As | % | Currency | % | As | % | As | % | Currency | % |
| | 2018 | 2017 | Reported | | | | Reported | | Reported | | | |
| Revenue: | | | | | | | | | | | | |
| Product sales and service | \$610.7 | \$579.6 | 5.4 | % | 2.2 | % | 1.1 | % | 13.0 | % | 4.1 | % |
| Rental revenue | 99.8 | 99.3 | 0.5 | % | (0.8) | % | 0.1 | % | 3.6 | % | (8.0) | % |
| Total revenue | \$710.5 | \$678.9 | 4.7 | % | 1.8 | % | 1.0 | % | 12.5 | % | 3.5 | % |

| | | | | | | | | | | | | |
|-------------------------|---------|---------|-------|---|-------|---|-------|---|------|---|-------|---|
| Revenue: | | | | | | | | | | | | |
| Patient Support Systems | \$355.0 | \$362.9 | (2.2) | % | (4.5) | % | (5.5) | % | 6.5 | % | (2.0) | % |
| Front Line Care | 237.9 | 211.0 | 12.7 | % | 10.7 | % | 10.9 | % | 17.0 | % | 10.1 | % |
| Surgical Solutions | 117.6 | 105.0 | 12.0 | % | 5.6 | % | 5.4 | % | 18.4 | % | 5.8 | % |
| Total revenue | \$710.5 | \$678.9 | 4.7 | % | 1.8 | % | 1.0 | % | 12.5 | % | 3.5 | % |

OUS - Outside of the U.S.

| | Year to Date | | Change | | Constant | | U.S. | | OUS | | Constant | |
|---------------------------|----------------|----------------|----------|---|----------|---|----------|---|----------|---|----------|---|
| | Ended March 31 | Ended March 31 | As | % | Currency | % | As | % | As | % | Currency | % |
| | 2018 | 2017 | Reported | | | | Reported | | Reported | | | |
| Revenue: | | | | | | | | | | | | |
| Product sales and service | \$1,185.9 | \$1,121.5 | 5.7 | % | 3.0 | % | 1.7 | % | 13.4 | % | 5.5 | % |
| Rental revenue | 194.3 | 194.8 | (0.3) | % | (1.3) | % | (0.8) | % | 4.1 | % | (5.5) | % |
| Total revenue | \$1,380.2 | \$1,316.3 | 4.9 | % | 2.4 | % | 1.2 | % | 12.9 | % | 4.9 | % |

| | | | | | | | | | | | | |
|-------------------------|-----------|-----------|-------|---|-------|---|-------|---|------|---|-------|---|
| Revenue: | | | | | | | | | | | | |
| Patient Support Systems | \$689.4 | \$698.1 | (1.2) | % | (3.3) | % | (3.8) | % | 5.6 | % | (2.0) | % |
| Front Line Care | 462.5 | 412.8 | 12.0 | % | 10.2 | % | 9.0 | % | 19.6 | % | 13.3 | % |
| Surgical Solutions | 228.3 | 205.4 | 11.1 | % | 5.7 | % | 3.6 | % | 18.5 | % | 7.7 | % |
| Total revenue | \$1,380.2 | \$1,316.3 | 4.9 | % | 2.4 | % | 1.2 | % | 12.9 | % | 4.9 | % |

OUS - Outside of the U.S.

Consolidated Revenue

Product sales and service revenue increased 5.4% and 5.7% on a reported basis, or 2.2% and 3.0% on a constant currency basis, for the three and six months ended March 31, 2018 primarily due to our acquisition of Mortara in February 2017 and OUS growth.

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This growth was partially offset by declines from businesses we recently divested within our Patient Support Systems segment. Excluding Mortara up to the anniversary date of the acquisition and businesses we recently divested, revenue increased approximately 2% on a constant currency basis in comparison to the prior year for the three and six month periods.

Rental revenue increased 0.5% and decreased (0.3)% on a reported basis, or (0.8)% and (1.3)% on a constant currency basis, for the three and six months ended March 31, 2018 primarily due to volume declines.

Business Segment Revenue

Patient Support Systems revenue decreased (2.2)% and (1.2)% on a reported basis, or (4.5)% and (3.3)% on a constant currency basis, compared to the prior year. Both periods were impacted by lower revenue from businesses we recently divested or non-strategic assets the Company plans to exit. Excluding revenue from the these businesses and non-strategic assets, revenue decreased (1)% on a constant currency basis for the three months ended March 31, 2018 and is flat for the year to date period in comparison to the prior year.

Front Line Care revenue increased 12.7% and 12.0% on a reported basis, or 10.7% and 10.2% on a constant currency basis, for the three and six months ended March 31, 2018 compared to the prior year, primarily due to the additional revenue from our Mortara acquisition in February 2017 as well as strong second quarter growth in our Welch Allyn business.

Surgical Solutions revenue increased 12.0% and 11.1% on a reported basis, or 5.6% and 5.7% on a constant currency basis, for the three and six months ended March 31, 2018 compared to the prior year, mainly due to strong OUS growth in Europe and the Middle East as well as second quarter growth in the U.S. from new products.

Gross Profit

| | Quarter Ended March 31 | | Year to Date Ended March 31 | |
|----------------------------|---------------------------|---------|--------------------------------|---------|
| | 2018 | 2017 | 2018 | 2017 |
| Gross Profit | | | | |
| Product sales and service | \$297.0 | \$273.9 | \$568.1 | \$527.4 |
| Percent of Related Revenue | 48.6 | % 47.3 | % 47.9 | % 47.0 |
| Rental | 53.4 | 50.5 | 101.9 | 99.6 |
| Percent of Related Revenue | 53.5 | % 50.9 | % 52.4 | % 51.1 |
| Total Gross Profit | \$350.4 | \$324.4 | \$670.0 | \$627.0 |
| Percent of Total Revenue | 49.3 | % 47.8 | % 48.5 | % 47.6 |

Product sales and service gross margin increased 130 and 90 basis points for the three and six months ended March 31, 2018 compared to the prior year primarily due to product mix and supply chain improvements.

Rental gross margin increased 260 and 130 basis points for the three and six months ended March 31, 2018 compared to the prior year due to product mix and cost improvements in our fleet and field service infrastructure.

Operating Expenses

| Quarter Ended March 31 | | Year to Date Ended March 31 | |
|---------------------------|------|--------------------------------|------|
| 2018 | 2017 | 2018 | 2017 |

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| | | | | | | | |
|-------------------------------------|---------|---|---------|---|---------|---|---------|
| Research and development expenses | \$34.7 | | \$35.3 | | \$67.0 | | \$67.3 |
| Percent of Total Revenue | 4.9 | % | 5.2 | % | 4.9 | % | 5.1 |
| | | | | | | | % |
| Selling and administrative expenses | \$232.7 | | \$222.4 | | \$454.4 | | \$431.2 |
| Percent of Total Revenue | 32.8 | % | 32.8 | % | 32.9 | % | 32.8 |
| | | | | | | | % |

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Research and development expenses decreased (1.7)% and (0.4)% for the three and six months ended March 31, 2018 compared to the prior year, primarily due to timing of projects. As a percentage of revenue, research and development expenses remained relatively consistent.

As a percentage of total revenue, selling and administrative expenses were relatively consistent during the quarter and year to date periods compared to the prior year. Selling and administrative expenses include acquisition-related intangible asset amortization, acquisition and integration costs and significant litigation related costs totaling \$32.2 million and \$65.3 million for the three and six months ended March 31, 2018 and \$33.8 million and \$65.2 million for the three and six months ended March 31, 2017. Excluding these items, selling and administrative expenses increased 40 basis points for the quarter and year to date periods as compared to prior periods due to the acquisition of Mortara in February 2017 and investment in sales and marketing.

Business Segment Divisional Income

| | Quarter Ended | | Change As Reported | Year to Date Ended | | Change As Reported | | |
|-------------------------|---------------|---------------|--------------------|--------------------|---------------|--------------------|--|--|
| | March 31 2018 | March 31 2017 | | March 31 2018 | March 31 2017 | | | |
| Divisional income: | | | | | | | | |
| Patient Support Systems | \$67.2 | \$63.2 | 6.3 % | \$120.6 | \$111.3 | 8.4 % | | |
| Front Line Care | 60.5 | 50.7 | 19.3 % | 115.9 | 103.9 | 11.5 % | | |
| Surgical Solutions | 15.5 | 9.2 | 68.5 % | 25.2 | 17.3 | 45.7 % | | |

Refer to Note 13 of our Condensed Consolidated Financial Statements for a description of how divisional income is determined.

Patient Support Systems divisional income increased 6.3% and 8.4% for the three and six months ended March 31, 2018 compared to the prior year, primarily due to lower operating expenses and an increase in margins from product mix and operational improvements.

Front Line Care divisional income increased 19.3% and 11.5% for the three and six months ended March 31, 2018 compared to the prior year as a result of revenue growth and higher margins from product mix.

Surgical Solutions divisional income increased 68.5% and 45.7% for the three and six months ended March 31, 2018 compared to the prior year, primarily due to revenue growth and higher margins from supply chain improvements.

Special Charges and Other

| | Quarter Ended | | Year to Date | |
|----------------------------------|---------------|---------------|---------------------|---------------------|
| | March 31 2018 | March 31 2017 | Ended March 31 2018 | Ended March 31 2017 |
| Special charges | \$36.9 | \$3.1 | \$50.4 | \$8.9 |
| Interest expense | \$(24.2) | \$(21.9) | \$(47.3) | \$(41.4) |
| Investment income and other, net | \$(0.4) | \$(0.4) | \$1.4 | \$(1.6) |

In connection with various organizational changes to improve our business alignment and cost structure, we recognized special charges of \$36.9 million and \$3.1 million for the quarters ended March 31, 2018 and 2017, and \$50.4 million and \$8.9 million for the year to date periods ended March 31, 2018. These charges relate to the initiatives described in Note 8 of our Condensed Consolidated Financial Statements.

Interest expense was higher in the three and six months ended March 31, 2018 primarily due to the interest expense on our private offering of \$300.0 million of senior unsecured notes in connection with the Mortara acquisition in February 2017. See Note 5 of our Condensed Consolidated Financial Statements for additional information.

Investment income and other, net increased in the six months ended March 31, 2018 primarily due to the gain we recorded related to the working capital settlement of the Völker disposition as well as favorable movements in foreign exchange rates.

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GAAP and Adjusted Earnings

Operating margin, income before income taxes, income tax expense, and earnings attributable to common shareholders per diluted share are summarized in the table below. GAAP amounts are adjusted for certain items to aid management in evaluating the performance of the business. Income tax expense is computed by applying a blended statutory tax rate based on the jurisdictional mix of the respective before tax adjustment.

| | Quarter Ended March 31, 2018 | | | | Quarter Ended March 31, 2017 | | | |
|---------------------------------------------------|------------------------------|----------------------------|--------------------|-------------|------------------------------|----------------------------|--------------------|-------------|
| | Operating Margin | Income Before Income Taxes | Income Tax Expense | Diluted EPS | Operating Margin | Income Before Income Taxes | Income Tax Expense | Diluted EPS |
| GAAP Basis | 6.5 % | \$ 21.5 | \$ (7.0) | \$ 0.42 | 9.4 % | \$ 41.3 | \$ 7.3 | \$ 0.51 |
| Adjustments: | | | | | | | | |
| Acquisition and integration costs | 0.4 % | 2.6 | 0.7 | 0.03 | 1.1 % | 7.2 | 3.4 | 0.06 |
| Acquisition-related intangible asset amortization | 3.8 % | 27.0 | 6.9 | 0.30 | 3.9 % | 26.6 | 9.0 | 0.26 |
| Field corrective actions | — % | — | — | — | 0.1 % | 0.5 | (0.1) | 0.01 |
| Litigation expenses | 0.3 % | 1.8 | 0.4 | 0.02 | 0.1 % | 0.9 | 0.3 | 0.01 |
| Special charges | 5.2 % | 36.9 | 9.7 | 0.40 | 0.5 % | 3.1 | 0.9 | 0.03 |
| Tax method and law changes and related costs | — % | 0.8 | 8.7 | (0.12) | — % | — | — | — |
| Adjusted Basis | 16.2 % | \$ 90.6 | \$ 19.4 | \$ 1.05 | 15.0 % | \$ 79.6 | \$ 20.8 | \$ 0.88 |

¹ Total does not add due to rounding

| | Year to Date Ended March 31, 2018 | | | | Year to Date Ended March 31, 2017 | | | |
|---------------------------------------------------|-----------------------------------|----------------------------|--------------------|-------------|-----------------------------------|----------------------------|--------------------|-------------|
| | Operating Margin | Income Before Income Taxes | Income Tax Expense | Diluted EPS | Operating Margin | Income Before Income Taxes | Income Tax Expense | Diluted EPS |
| GAAP Basis | 7.1 % | \$ 52.3 | \$ (64.5) | \$ 1.73 | 9.1 % | \$ 76.6 | \$ 19.1 | \$ 0.87 |
| Adjustments: | | | | | | | | |
| Acquisition and integration costs | 0.4 % | 5.0 | 1.3 | 0.05 | 1.0 % | 13.2 | 5.6 | 0.11 |
| Acquisition-related intangible asset amortization | 3.9 % | 53.7 | 13.5 | 0.60 | 4.0 % | 52.1 | 17.3 | 0.52 |
| Field corrective actions | — % | — | — | — | — % | 0.5 | (0.1) | 0.01 |
| Litigation expenses | 0.4 % | 5.8 | 1.5 | 0.06 | 0.1 % | 0.9 | 0.3 | 0.01 |
| Special charges | 3.7 % | 50.4 | 13.2 | 0.55 | 0.7 % | 8.9 | 2.8 | 0.09 |
| Tax method and law changes and related costs | — % | 0.8 | 69.0 | (1.01) | — % | — | (2.2) | 0.03 |
| Gain on disposition | — % | (1.0) | — | (0.01) | — % | (1.0) | (0.4) | (0.01) |
| Adjusted Basis | 15.5 % | \$ 167.0 | \$ 34.0 | \$ 1.97 | 14.8 % | \$ 151.2 | \$ 42.4 | \$ 1.63 |

¹ Total does not add due to rounding

The effective tax rate for the quarter and year to date periods ended March 31, 2018 was (32.6)% and (123.3)% compared to 17.7% and 24.9% for the quarter and year to date periods in the prior year. The effective tax rate for the current quarter is lower than the comparable period in fiscal 2017 due to period tax benefits of \$11.2 million primarily related to a change in a tax accounting method approved by the Internal Revenue Service in the current period. The change in accounting method resulted in a reduction

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in U.S. tax for prior year currency exchange losses. The effective tax rate for the year to date period is lower than the comparable period in fiscal 2017 due to the lower corporate tax rate and period tax benefits of \$75.6 million primarily related to recording the items attributable to the new tax legislation in the U.S. as described in Note 9 and the change in tax accounting method. The comparable prior year period included period tax benefits of \$3.5 million primarily related to the adoption of the ASU 2016-09 partially offset by the expense to revalue the France deferred tax assets due to the law change that reduced the future corporate income tax rate in France.

The adjusted effective tax rate for the three and six months ended March 31, 2018 was 21.4% and 20.4% compared to 26.1% and 28.0% for the comparable period in the prior year. The lower adjusted tax rate in the current year is due primarily to the reduction in the U.S. federal corporate tax rate from the Tax Act legislation as described in Note 9 and period tax items related to the excess tax benefits on deductible stock compensation.

Diluted earnings per share decreased 17.6% and increased 98.9% on a reported basis and increased 19.3% and 20.9% on an adjusted basis for the three and six months ended March 31, 2018.

Liquidity and Capital Resources

| | Year to Date Ended March 31 | |
|-----------------------------------------|--------------------------------|-----------|
| | 2018 | 2017 |
| Cash Flows Provided By (Used In): | | |
| Operating activities | \$125.6 | \$126.4 |
| Investing activities | (47.7) | (346.9) |
| Financing activities | (75.8) | 211.7 |
| Effect of exchange rate changes on cash | 5.1 | (4.7) |
| Decrease in Cash and Cash Equivalents | \$7.2 | \$(13.5) |

Operating Activities

Cash provided by operating activities decreased \$0.8 million compared to the prior year as higher net income, adjusted for non-cash items including the impact of the Tax Act legislation as described in Note 9, the conveyance of certain third party rental assets as described in Note 1, depreciation, amortization and stock compensation expense, was offset by changes in working capital activities. During the year to date period, net income adjusted for non-cash items and collection of receivables were partially offset by the payout of performance-based compensation related to our 2017 fiscal year and timing of other working capital activities.

Investing Activities

Cash used in investing activities decreased \$299.2 million compared to the prior year, primarily due to our acquisition of Mortara in the second quarter of fiscal 2017. During the year to date period, cash used in investing activities consisted mainly of capital expenditures.

Financing Activities

Cash used in financing activities increased \$287.5 million primarily due to proceeds from borrowings on long-term debt of \$300.0 million during the prior year for the Mortara acquisition, partially offset by \$30.0 million of share repurchases in the open market during the first quarter of fiscal 2017. During the year to date period, payments of long term debt totaled \$54.9 million, while net borrowings decreased \$20.0 million on our Revolving Credit Facility and increased \$14.1 million on our Securitization Program. See Note 5 of our Condensed Consolidated Financial

Statements for additional information on our financing agreements.

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Other Liquidity Matters

In addition to the discussion of our financing agreements and share repurchases detailed in Note 5 and Note 11 of our Condensed Consolidated Financial Statements, our primary pension plan invests in a variety of equity and debt securities. At September 30, 2017, our latest measurement date, our pension plans were underfunded by approximately \$61.4 million. Based on our current funded status, we are not required to make any contributions to our primary pension plan in fiscal 2018.

We intend to continue to pay quarterly cash dividends comparable to those paid in the periods covered by these financial statements. However, the declaration and payment of dividends by us will be subject to the sole discretion of our Board and will depend upon many factors, including our financial condition, earnings, capital requirements, covenants associated with debt obligations, legal requirements, and other factors deemed relevant by our Board.

Over the long term, we intend to continue to pursue inorganic growth in certain areas of our business, but the timing, size or success of any acquisition effort and the related potential capital commitments cannot be predicted.

As of March 31, 2018, approximately 82.7% of our cash and cash equivalents were held by our foreign subsidiaries. As of September 30, 2017, our practice and intention was to reinvest the earnings in our non-U.S. subsidiaries outside of the U.S. As a result of the Tax Act described in Note 9, we are currently analyzing our global working capital requirements and potential tax liabilities that would be incurred if the non-U.S. subsidiaries distribute cash to the U.S. parent.

We believe that cash on hand and cash generated from operations, along with amounts available under our Revolving Credit Facility and Securitization Program, will be sufficient to fund operations, working capital needs, capital expenditure requirements, and financing obligations for at least the next twelve months. Our \$700.0 million Revolving Credit Facility is with a syndicate of banks, which we believe reduces our exposure to any one institution and would still leave us with significant borrowing capacity in the event that any one of the institutions within the group is unable to comply with the terms of our amended and restated credit agreement. However, disruption and volatility in the credit markets could impede our access to capital.

Contractual Obligations and Contingent Liabilities and Commitments

Other than the transition tax obligation discussed in Note 9, there have not been any significant changes since September 30, 2017 impacting our contractual obligations and contingent liabilities and commitments.

Critical Accounting Policies

Our accounting policies require management to make significant estimates and assumptions using information available at the time the estimates are made. Such estimates and assumptions significantly affect various reported amounts of assets, liabilities, revenue, and expenses. If future experience differs materially from these estimates and assumptions, our results of operations and financial condition could be affected. A detailed description of our accounting policies is included in Note 1 of our Condensed Consolidated Financial Statements and the Critical Accounting Policies Section of Management's Discussion and Analysis of Financial Condition and Results of Operations included in our 2017 Form 10-K. There have been no material changes to such policies since September 30, 2017.

For a further summary of certain accounting policies and estimates and recently issued accounting pronouncements applicable to us, see Note 1 of our Condensed Consolidated Financial Statements in this Form 10-Q.

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Item 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT
MARKET RISKS

We are exposed to various market risks, including fluctuations in interest rates, collection risk associated with our accounts and notes receivable portfolio and variability in currency exchange rates. We have established policies, procedures, and internal processes governing our management of market risks and the use of financial instruments to manage our exposure to such risks.

We are subject to variability in foreign currency exchange rates in our international operations. Exposure to this variability is periodically managed primarily through the use of natural hedges, whereby funding obligations and assets are both managed in the local currency. We, from time-to-time, enter into currency exchange agreements to manage our exposure arising from fluctuating exchange rates related to specific and forecasted transactions. We operate this program pursuant to documented corporate risk management policies and do not enter into derivative transactions for speculative purposes. The sensitivity of earnings and cash flows to variability in exchange rates is assessed by applying an appropriate range of potential rate fluctuations to our assets, obligations and projected results of operations denominated in foreign currencies.

Our currency risk consists primarily of foreign currency denominated firm commitments and forecasted foreign currency denominated intercompany and third-party transactions. At March 31, 2018, the notional amount of open foreign exchange contracts was \$33.8 million. These contracts were in a net liability position with an aggregate fair value of \$0.3 million. The maximum length of time over which we hedge transaction exposures is generally 15 months. Derivative gains/(losses), initially reported as a component of Accumulated Other Comprehensive Loss, are reclassified to earnings in the period when the transaction affects earnings.

Refer to Note 5 of our Condensed Consolidated Financial Statements for discussions about our interest rate swap agreements.

For additional information on market risks related to our pension plan assets, see Item 7A, Quantitative and Qualitative Disclosures About Market Risk, in our 2017 Form 10-K.

Item 4. CONTROLS AND PROCEDURES

Our management, with the supervision and participation of our President and Chief Executive Officer and our Senior Vice President and Chief Financial Officer (the “Certifying Officers”), has evaluated the effectiveness of the design and operation of our disclosure controls and procedures as of March 31, 2018. Our disclosure controls and procedures are designed to ensure that information required to be disclosed in the reports we file or submit under the Securities Exchange Act of 1934, as amended, is recorded, processed, summarized and reported, within the time periods specified in the SEC’s rules and forms and such information is accumulated and communicated to management, including our Certifying Officers and our Board of Directors, as appropriate to allow timely decisions regarding required disclosure. Based upon that evaluation, the Certifying Officers concluded that our disclosure controls and procedures were effective as of March 31, 2018.

There have been no other changes to our internal controls over financial reporting (as such term is defined in Rules 13a-15(f) and 15d-15(f) under the Exchange Act) that occurred during our most recent completed fiscal quarter that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

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Item 5. OTHER INFORMATION

Amendment to Employment Agreements

On April 24, 2018, the Company entered into amended employment agreements with each of Mr. Andreas Frank, Mr. Paul Johnson, Mr. Carlos Alonso-Marum, Mr. Kenneth Meyers, Ms. Deborah Rasin, Mr. Alton Shader and Mr. Steven J. Strobel, and on April 23, 2018, the Company entered into an amended employment agreement with Mr. Francisco Canal Vega (collectively, the “Amended Employment Agreements”). Messrs. Frank’s and Shader’s employment agreements were initially entered into in 2011. Mr. Strobel’s employment agreement was initially entered into in 2014. Ms. Rasin’s and Messrs. Alonso-Marum’s and Meyers’ employment agreements were initially entered into in 2015. Mr. Johnson’s employment agreement was initially entered into in 2016. Mr. Canal Vega’s employment agreement was initially entered into in 2017.

The Amended Employment Agreements provide that in the event the executive’s employment is terminated by the Company without cause on or before November 16, 2019, the executive will be entitled to receive cash payments for all outstanding unvested equity awards that are forfeited as a result of termination of employment that otherwise would have vested on before November 16, 2019, calculated as follows:

For each unvested stock option, an amount equal to the difference between the closing price of the Company’s (i) common stock on the date of termination of employment and the stock option’s exercise price, with such payment to be made as soon as practicable following the date of termination of employment.

For each unvested restricted stock unit, an amount equal to the closing price of the Company’s common stock on (ii) the date of termination of employment, with such cash payment to be made as soon as practicable following the effective date of termination of employment.

For each unvested performance share unit, an amount equal to the closing price of the Company’s common stock on the last day of the applicable three-year performance period for such performance share unit, with the number (iii) of performance share units earned to be determined as of the end of the performance period based on actual Company financial performance for the full performance period and with such cash payment to be made as soon as practicable following the completion of the performance period.

Other than as set forth above, the respective employment agreements of the executive officers listed above remain unchanged. The description of these Amended Employment Agreements does not purport to be complete and is subject to, and qualified in its entirety by, the complete text of the Amended Employment Agreements, copies of which are included herein as Exhibits 10.1, 10.2, 10.3, 10.4, 10.5, 10.6, 10.7, 10.8 and 10.9, which exhibits are incorporated by reference.

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PART II – OTHER INFORMATION

Item 1. LEGAL PROCEEDINGS

Refer to Note 14 of our Condensed Consolidated Financial Statements in this Form 10-Q for further information on our legal proceedings.

Item 1A. RISK FACTORS

For information regarding the risks we face, see the discussion under “Item 1A. Risk Factors” in our 2017 Form 10-K for the year ended September 30, 2017. There have been no material changes to the risk factors described in that report.

Item 2. UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS

| Period | Total Number of Shares Purchased (1) | Average Price Paid per Share | Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs (2) | Approximate Dollar Value of Shares That May Yet Be Purchased Under the Programs (2) |
|--------------------------------------|--------------------------------------------------|------------------------------------------|--------------------------------------------------------------------------------------------------------------------|-------------------------------------------------------------------------------------------------------------|
| January 1, 2018 - January 31, 2018 | 9,903 | \$ 85.60 | — | \$ 164.7 |
| February 1, 2018 - February 28, 2018 | 358 | \$ 84.83 | — | \$ 164.7 |
| March 1, 2018 - March 31, 2018 | 176 | \$ 87.63 | — | \$ 164.7 |
| Total | 10,437 | | — | |

(1) Shares purchased during the quarter ended March 31, 2018 were in connection with employee payroll tax withholding for restricted and deferred stock distributions.

(2) In September 2017, the Board approved an increase to its previously announced share repurchase authorization to a total of \$340.0 million. As of March 31, 2018, a cumulative total of \$175.3 million had been used, leaving the Company with approximately \$165.0 million of availability under the share repurchase program. The plan does not have an expiration date and currently there are no plans to terminate this program in the future.

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Item 6. EXHIBITS

A. Exhibits

- 10.1 First Amendment to Employment Agreement between Andreas Frank and Hill-Rom Holdings, Inc. dated April 24, 2018
- 10.2 Employment Agreement between Paul Johnson and Hill-Rom Holdings, Inc. dated May 2, 2016
- 10.3 First Amendment to Employment Agreement between Paul Johnson and Hill-Rom Holdings, Inc. dated April 24, 2018
- 10.4 First Amendment to Employment Agreement between Carlos Alonso-Marum and Hill-Rom Holdings, Inc. dated April 24, 2018
- 10.5 First Amendment to Employment Agreement between Kenneth Meyers and Hill-Rom Holdings, Inc. dated April 24, 2018
- 10.6 First Amendment to Employment Agreement between Deborah Rasin and Hill-Rom Holdings, Inc. dated April 24, 2018
- 10.7 First Amendment to Employment Agreement between Alton Shader and Hill-Rom Holdings, Inc. dated April 24, 2018
- 10.8 First Amendment to Employment Agreement between Steven J. Strobel and Hill-Rom Holdings, Inc. dated April 24, 2018
- 10.9 First Amendment to Employment Agreement between Francisco Canal Vega and Hill-Rom Holdings, Inc. dated April 23, 2018
- 31.1 Certification of Chief Executive Officer Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
- 31.2 Certification of Chief Financial Officer Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
- 32.1 Certification of Chief Executive Officer Pursuant to 18 U.S.C. Section 1350, as Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002
- 32.2 Certification of Chief Financial Officer Pursuant to 18 U.S.C. Section 1350, as Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002
- 101.INS XBRL Instance Document
- 101.SCH XBRL Taxonomy Extension Schema Document
- 101.CAL XBRL Taxonomy Extension Calculation Linkbase Document
- 101.LAB XBRL Extension Labels Linkbase Document
- 101.DEF XBRL Taxonomy Extension Definition Linkbase Document

101.PRE XBRL Taxonomy Extension Presentation Linkbase Document

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SIGNATURES

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.

HILL-ROM HOLDINGS, INC.
(Registrant)

DATE: April 27, 2018 By: /s/ Steven J. Strobel
Name: Steven J. Strobel
Title: Senior Vice President and Chief Financial Officer
(duly authorized officer and principal financial officer)