VARIAN MEDICAL SYSTEMS INC
Form 10-Q
May 10, 2016

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

FORM 10-Q

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

For the quarterly period ended April 1, 2016

or

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

For the transition period from to

Commission File Number 1-7598

VARIAN MEDICAL SYSTEMS, INC.
(Exact name of registrant as specified in its charter)

Delaware	94-2359345
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification Number)
3100 Hansen Way, Palo Alto, California	94304-1038
(Address of principal executive offices)	(Zip Code)

(650) 493-4000
(Registrant's telephone number, including area code)

Indicate by check mark whether the registrant: (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes ý 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 ý No ¨

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

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

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

Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date: 95,214,552 shares of common stock, par value $1 per share, outstanding as of April 29, 2016.

VARIAN MEDICAL SYSTEMS, INC.
FORM 10-Q for the Quarter Ended April 1, 2016
INDEX

PART I
FINANCIAL INFORMATION

Item 1. Financial Statements

VARIAN MEDICAL SYSTEMS, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF EARNINGS
(Unaudited)

	Three Months Ended		Six Months Ended	
(In thousands, except per share amounts)	April 1, 2016	April 3, 2015	April 1, 2016	April 3, 2015
Revenues:				
Product	$495,569	$513,765	$996,095	$989,595
Service	263,198	245,641	519,805	507,665
Total revenues	758,767	759,406	1,515,900	1,497,260
Cost of revenues:				
Product	330,987	330,458	674,443	636,275
Service	110,562	106,410	214,547	211,439
Total cost of revenues	441,549	436,868	888,990	847,714
Gross margin	317,218	322,538	626,910	649,546
Operating expenses:				
Research and development	62,108	59,312	122,089	116,388
Selling, general and administrative	121,127	117,190	254,188	257,672
Total operating expenses	183,235	176,502	376,277	374,060
Operating earnings	133,983	146,036	250,633	275,486
Interest income	4,298	3,044	8,247	6,084
Interest expense	(3,312)	(2,001)	(5,542)	(4,046)
Earnings before taxes	134,969	147,079	253,338	277,524
Taxes on earnings	37,986	41,110	67,313	78,241
Net earnings	96,983	105,969	186,025	199,283
Less: Net earnings attributable to noncontrolling interests	12	—	27	—
Net earnings attributable to Varian	$96,971	$105,969	$185,998	$199,283
Net earnings per share - basic	$1.01	$1.06	$1.93	$1.99
Net earnings per share - diluted	$1.01	$1.05	$1.92	$1.97
Shares used in the calculation of net earnings per share:				
Weighted average shares outstanding - basic	95,671	100,157	96,474	100,315
Weighted average shares outstanding - diluted	96,179	101,026	97,072	101,341

See accompanying notes to the condensed consolidated financial statements.

VARIAN MEDICAL SYSTEMS, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE EARNINGS
(Unaudited)

	Three Months Ended		Six Months Ended	
(In thousands)	April 1, 2016	April 3, 2015	April 1, 2016	April 3, 2015
Net earnings	$96,983	$105,969	$186,025	$199,283
Other comprehensive earnings (loss), net of tax:				
Defined benefit pension and post-retirement plans:				
Amortization of prior service cost included in net periodic benefit cost, net of tax benefit of $46 and $91 for the three and six months ended April 1, 2016, respectively, and $39 and $80 for the corresponding periods of fiscal year 2015, respectively.	(71)	(40)	(143)	(78)
Amortization of net actuarial loss included in net periodic benefit cost, net of tax expense of ($132) and ($264) for the three and six months ended April 1, 2016, respectively, and ($115) and ($231) for the corresponding periods of fiscal year 2015, respectively.	601	505	1,202	1,009
	530	465	1,059	931
Derivative instruments:				
Change in unrealized gain (loss), net of tax benefit (expense) of $534 and $480 for the three and six months ended April 1, 2016, respectively, and ($455) and ($739) for the corresponding periods of fiscal year 2015, respectively.	(893)	763	(802)	1,238
Reclassification adjustments, net of tax benefit of $29 for both the three and six months ended April 1, 2016, respectively, and $701 and $1,027 for the corresponding periods of fiscal year 2015, respectively.	(50)	(1,176)	(50)	(1,721)
	(943)	(413)	(852)	(483)
Available-for-sale securities:				
Change in unrealized gain (loss), net of tax benefit of $141 for the six months ended April 1, 2016.	—	—	(299)	—
Reclassification adjustments, net of tax expense of ($193) for the six months ended April 1, 2016.	—	—	411	—
	—	—	112	—
Currency translation adjustment	9,829	(18,170)	5,176	(30,460)
Other comprehensive earnings (loss)	9,416	(18,118)	5,495	(30,012)
Comprehensive earnings	106,399	87,851	191,520	169,271
Less: Comprehensive earnings attributable to noncontrolling interests	12	—	27	—
Comprehensive earnings attributable to Varian	$106,387	$87,851	$191,493	$169,271

See accompanying notes to the condensed consolidated financial statements.

VARIAN MEDICAL SYSTEMS, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED BALANCE SHEETS
(Unaudited)

(In thousands, except par values)	April 1, 2016	October 2, 2015 (1)
Assets		
Current assets:		
Cash and cash equivalents	$961,100	$845,468
Accounts receivable, net of allowance for doubtful accounts of $24,410 at April 1, 2016 and $21,218 at October 2, 2015	852,634	770,920
Inventories	653,328	612,607
Prepaid expenses and other current assets	177,251	163,984
Deferred tax assets	128,904	132,066
Total current assets	2,773,217	2,525,045
Property, plant and equipment, net	374,356	379,215
Goodwill	283,947	283,452
Other assets	434,738	413,036
Total assets	$3,866,258	$3,600,748
Liabilities, Redeemable Noncontrolling Interests and Equity		
Current liabilities:		
Accounts payable	$174,178	$202,918
Accrued liabilities	353,110	353,500
Deferred revenues	520,326	489,775
Advance payments from customers	164,891	178,265
Short-term borrowings	431,635	108,446
Current maturities of long-term debt	50,000	50,000
Total current liabilities	1,694,140	1,382,904
Long-term debt	312,500	337,500
Other long-term liabilities	155,748	154,000
Total liabilities	2,162,388	1,874,404
Commitments and contingencies (Note 9)		
Redeemable noncontrolling interests	10,331	—
Equity:		
Varian stockholders' equity:		
Preferred stock of $1 par value: 1,000 shares authorized; none issued and outstanding	—	—
Common stock of $1 par value: 189,000 shares authorized; 95,550 and 98,070 shares issued and outstanding at April 1, 2016 and at October 2, 2015, respectively	95,550	98,070
Capital in excess of par value	659,162	682,167
Retained earnings	1,016,027	1,017,826
Accumulated other comprehensive loss	(80,968)	(86,463)
Total Varian stockholders' equity	1,689,771	1,711,600
Noncontrolling interests	3,768	14,744
Total equity	1,693,539	1,726,344
Total liabilities, redeemable noncontrolling interests and equity	$3,866,258	$3,600,748

(1) The condensed consolidated balance sheet as of October 2, 2015 was derived from audited financial statements as of that date, but does not include all disclosures required by accounting principles generally accepted in the United States of America.

See accompanying notes to the condensed consolidated financial statements.

VARIAN MEDICAL SYSTEMS, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
(Unaudited)

	Six Months Ended	
(In thousands)	April 1, 2016	April 3, 2015
Cash flows from operating activities:		
Net earnings	$186,025	$199,283
Adjustments to reconcile net earnings to net cash provided by operating activities:		
Share-based compensation expense	23,805	25,238
Tax benefits from exercises of share-based payment awards	821	11,144
Excess tax benefits from share-based compensation	(1,579)	(11,138)
Depreciation	31,127	30,111
Amortization of intangible assets	6,801	3,286
Deferred taxes	644	16,399
Provision for doubtful accounts receivable	3,645	6,682
Other, net	(73)	1,514
Changes in assets and liabilities:		
Accounts receivable	(94,471)	(17,457)
Inventories	(39,652)	(92,951)
Prepaid expenses and other assets	(15,669)	(20,987)
Accounts payable	(13,637)	(12,833)
Accrued liabilities and other long-term liabilities	1,835	(43,159)
Deferred revenues and advance payments from customers	19,505	37,134
Net cash provided by operating activities	109,127	132,266
Cash flows from investing activities:		
Purchases of property, plant and equipment	(45,938)	(36,722)
Decrease (increase) in restricted cash	572	(35,710)
Sale of available-for-sale securities	8,638	—
Notes receivable	(6,159)	(5,000)
Net amounts received from (paid to) deferred compensation plan trust account	(2,907)	3,102
Other	(732)	(838)
Net cash used in investing activities	(46,526)	(75,168)
Cash flows from financing activities:		
Repurchases of common stock	(248,704)	(201,181)
Proceeds from issuance of common stock to employees	21,210	67,221
Excess tax benefits from share-based compensation	1,579	11,138
Employees' taxes withheld and paid for restricted stock and restricted stock units	(10,715)	(16,046)
Borrowings under credit facility agreement	83,000	—
Repayments under credit facility agreement	(108,000)	(25,000)
Net borrowings under credit facility agreements with maturities less than 90 days	322,000	100,000
Contingent consideration and hold back	(3,710)	(1,070)
Other	496	1,774
Net cash provided by (used in) financing activities	57,156	(63,164)
Effects of exchange rate changes on cash and cash equivalents	(4,125)	19,014
Net increase in cash and cash equivalents	115,632	12,948
Cash and cash equivalents at beginning of period	845,468	849,275
Cash and cash equivalents at end of period	$961,100	$862,223

See accompanying notes to the condensed consolidated financial statements.

VARIAN MEDICAL SYSTEMS, INC. AND SUBSDIARIES
NOTES TO THE CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited)

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Description of Business

Varian Medical Systems, Inc. (“VMS”) and its subsidiaries (collectively, the “Company”) designs, manufactures, sells and services hardware and software products for treating cancer with radiotherapy, stereotactic radiosurgery, stereotactic body radiotherapy, and brachytherapy. The Company also designs, manufactures, sells and services X-ray imaging components for use in a range of applications, including radiographic or fluoroscopic imaging, mammography, special procedures, computed tomography, computer-aided diagnostics and industrial applications. In addition, the Company designs, manufactures, sells and services linear accelerators, image processing software and image detection products for security and inspection purposes. The Company also develops, designs, manufactures, sells and services proton therapy products and systems for cancer treatment.

Basis of Presentation

The condensed consolidated financial statements have been prepared by the Company pursuant to the rules and regulations of the Securities and Exchange Commission (“SEC”). Certain information and note disclosures normally included in annual financial statements prepared in accordance with accounting principles generally accepted in the United States (“GAAP”) have been condensed or omitted pursuant to such rules and regulations. These condensed consolidated financial statements and the accompanying notes are unaudited and should be read in conjunction with the consolidated financial statements and the notes thereto included in the Company’s Annual Report on Form 10-K for the year ended October 2, 2015 (the “2015 Annual Report”). In the opinion of management, the condensed consolidated financial statements herein include adjustments (consisting only of normal recurring adjustments) necessary for a fair statement of the Company’s financial position as of April 1, 2016 and October 2, 2015, results of operations and statements of comprehensive earnings for the three and six months ended April 1, 2016 and April 3, 2015, and cash flows for the six months ended April 1, 2016 and April 3, 2015. The results of operations for the six months ended April 1, 2016 are not necessarily indicative of the operating results to be expected for the full fiscal year or any future period.

Reclassifications

Certain reclassifications have been made to the amounts for prior period in order to conform to the current period’s presentation.

Fiscal Year

The fiscal years of the Company as reported are the 52- or 53-week periods ending on the Friday nearest September 30. Fiscal year 2016 is the 52-week period ending September 30, 2016, and fiscal year 2015 was the 53-week period ended October 2, 2015. The fiscal quarters ended April 1, 2016 and April 3, 2015 were both 13-week periods.

Principles of Consolidation

The condensed consolidated financial statements include those of VMS and its wholly-owned and majority-owned or controlled subsidiaries. Intercompany balances, transactions and stock holdings have been eliminated in consolidation.

Use of Estimates

The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from these estimates.

Recent Accounting Pronouncements or Updates Not Yet Effective

In March 2016, the Financial Accounting Standards Board ("FASB") issued an amendment to its accounting guidance related to employee share-based payments. The amendment simplifies several aspects of the accounting for employee share-based

7

payments including the accounting for income taxes, forfeitures, and statutory tax withholding requirements, as well as classification in the statement of cash flows. The amendment will be effective for the Company beginning in its first quarter of fiscal year 2018 with early adoption permitted. The Company is evaluating the impact of adopting this amendment to its consolidated financial statements.

In February 2016, the FASB issued a new standard on accounting for leases. The new standard is intended to provide enhanced transparency and comparability by requiring lessees to record right-of-use assets and corresponding lease liabilities on the balance sheet. The new standard will continue to classify leases as either finance or operating, with classification affecting the pattern of expense recognition in the statement of earnings. The new standard is required to be adopted using a modified retrospective method to each prior reporting period presented with various optional practical expedients. The new standard will be effective for the Company beginning in its first quarter of fiscal year 2020 with early adoption permitted. The Company is evaluating the impact of adopting this new standard to its consolidated financial statements.

In January 2016, the FASB issued an amendment to its accounting guidance related to recognition and measurement of financial assets and financial liabilities. The amendment addresses certain aspects of recognition, measurement, presentation and disclosure of financial instruments. The amendment will be effective for the Company beginning in its first quarter of fiscal year 2019. The Company is evaluating the impact of adopting this guidance to its consolidated financial statements.

In November 2015, the FASB issued an amendment to its accounting guidance related to balance sheet classification of deferred taxes. The amendment requires that deferred tax liabilities and assets be classified as noncurrent in the statement of financial position. The amendment affects presentation only and will be effective for the Company beginning in its first quarter of fiscal year 2018. Early adoption is permitted. The amendment can be adopted either prospectively or retrospectively. The Company is evaluating the impact of adopting this guidance to its consolidated financial statements.

In September 2015, the FASB issued a new accounting standard that eliminates the requirement to restate prior period financial statements for measurement period adjustments following a business combination. The new guidance will be effective for the Company beginning in its first quarter of fiscal year 2017. The new guidance is not expected to have a material impact to the Company’s consolidated financial statements.

In July 2015, the FASB issued an amendment to its accounting guidance related to inventory measurement. The amendment requires inventory measured using first-in, first-out (FIFO) or average cost to be subsequently measured at the lower of cost and net realizable value, thereby simplifying the current guidance that requires an entity to measure inventory at the lower of cost or market. The amendment will be effective for the Company beginning in its first quarter of fiscal year 2018. The new guidance is not expected to have a material impact to the Company’s consolidated financial statements.

In April 2015, the FASB issued an amendment to its accounting guidance related to internal use software. The amendment clarifies that the software license element of a cloud computing arrangements should be accounted for consistent with the acquisition of other software licenses. The amendment will be effective for the Company beginning in its first quarter of fiscal year 2017. The Company is evaluating the impact of adopting this guidance to its consolidated financial statements.

In April 2015, the FASB issued an amendment to its accounting guidance related to retirement benefits. The amendment provides a practical expedient that permits an entity with a fiscal year-end that does not coincide with a month-end to measure defined benefit plan assets and obligations using the month-end that is closest to the entity’s fiscal year-end. The amendment also provides a practical expedient that permits an entity that has a significant event in an interim period to remeasure defined benefit plan assets and obligations using the month-end that is closest to the date of the significant event. The amendment will be effective for the Company beginning in its first quarter of fiscal year 2017. The amendment is not expected to have a material impact to the Company’s consolidated financial statements.

In March 2015, the FASB issued an amendment to its accounting guidance related to presentation of debt issuance costs. The amendment requires that debt issuance costs related to a recognized debt liability be presented in the balance sheet as a direct deduction from the carrying amount of that debt liability. The amendment will be effective for the Company beginning in its first quarter of fiscal year 2017. In August 2015, the FASB further clarified that entities are permitted to defer and present debt issuance costs related to line-of-credit arrangements as assets. These amendments are not expected to have a material impact to the Company’s consolidated financial statements.
In February 2015, the FASB issued an amendment to its accounting guidance related to consolidation. The amendment modifies the analysis that a reporting entity must perform to determine whether it should consolidate certain types of legal entities. The

VARIAN MEDICAL SYSTEMS, INC. AND SUBSIDIARIES
NOTES TO THE CONDENSED CONSOLIDATED FINANCIAL STATEMENTS - (CONTINUED)
(Unaudited)

amendment will be effective for the Company beginning in its first quarter of fiscal year 2017. The amendment is not expected to have a material impact to the Company’s consolidated financial statements.
In June 2014, the FASB issued an amendment to its accounting guidance related to stock-based compensation. The amendment requires that a performance target that could be achieved after the requisite service period be treated as a performance condition that affects vesting, rather than a condition that affects the grant-date fair value. The new guidance will be effective for the Company beginning in its first quarter of fiscal year 2017. The amendment is not expected to have a material impact to the Company's consolidated financial statements.
In May 2014, the FASB issued a new revenue standard, which sets forth a single, comprehensive revenue recognition model for all contracts with customers to improve comparability. The new standard requires revenue recognition to depict the transfer of goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. In March 2016, the FASB amended the principal-versus-agent implementation guidance and illustrations in the new standard. In April 2016, the FASB amended the guidance on identifying performance obligations and the implementation guidance on licensing in the new standard. In May 2016, the FASB amended the guidance on collectibility, noncash consideration, presentation of sales tax and transition in the new standard. The new standard will be effective for the Company beginning in its first quarter of fiscal year 2019, with early adoption permitted, but not before the first quarter of fiscal year 2018. The new standard can be applied either retrospectively to each prior reporting period presented (i.e., full retrospective adoption) or with the cumulative effect of initially applying the update recognized at the date of the initial application (i.e., modified retrospective adoption) along with additional disclosures. The Company is evaluating the impact of adopting this standard to its consolidated financial statements.

2. BALANCE SHEET COMPONENTS

(In millions)	April 1, 2016	October 2, 2015
Inventories:		
Raw materials and parts	$386.1	$ 348.3
Work-in-process	102.5	98.2
Finished goods	164.7	166.1
Total inventories	$653.3	$ 612.6

The following tables summarize the Company's available-for-sale securities:

	April 1, 2016			
(In millions)	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
Available-for-sale securities:				
Corporate debt securities:				
CPTC loans	$88.8	$ —	$ —	$88.8
Total available-for-sale securities	$88.8	$ —	$ —	$88.8

	October 2, 2015			
(In millions)	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
Available-for-sale securities:				

Corporate debt securities:				
CPTC loans	$83.9	$ —	$ —	$83.9
Other	8.6	0.1	(0.3)	8.4
Non-U.S. government security	0.7	—	—	0.7
Total available-for-sale securities	$93.2	$ 0.1	$ (0.3)	$93.0

VARIAN MEDICAL SYSTEMS, INC. AND SUBSIDIARIES
NOTES TO THE CONDENSED CONSOLIDATED FINANCIAL STATEMENTS - (CONTINUED)
(Unaudited)

See Note 15, "VPT Loans" for more information on California Proton Treatment Center, LLC (“CPTC”) loans.

Available-for-sale securities are recorded in other assets on the Condensed Consolidated Balance Sheets because their maturity dates are greater than one year, and the Company did not intend to sell all or a portion of its loans in the next twelve months. As of April 1, 2016, the Company anticipates that it will recover the entire amortized cost basis of all of its available-for-sale securities and determined that no other-than-temporary impairments were required to be recognized.

(In millions)	April 1, 2016	October 2, 2015
Other long-term liabilities:		
Long-term income taxes payable	$ 47.2	$ 44.5
Long-term deferred income taxes	44.5	47.5
Other	64.0	62.0
Total other long-term liabilities	$ 155.7	$ 154.0

3. FAIR VALUE

Fair value is defined as the exchange price that would be received for an asset or paid to transfer a liability (an exit price) in the principal or most advantageous market for the asset or liability in an orderly transaction between market participants at the measurement date. There is a three-level fair value hierarchy that prioritizes the inputs used to measure fair value. This hierarchy requires entities to maximize the use of observable inputs and minimize the use of unobservable inputs. The three levels of inputs used to measure fair value are as follows:

Level 1 — Quoted prices in active markets for identical assets or liabilities.

Level 2 — Observable inputs other than quoted prices included in Level 1, such as quoted prices for similar assets and liabilities in active markets; quoted prices for identical or similar assets and liabilities in markets that are not active; or other inputs that are observable or can be corroborated by observable market data.

Level 3 — Unobservable inputs that are supported by little or no market activity and that are significant to the fair value of the assets or liabilities.

VARIAN MEDICAL SYSTEMS, INC. AND SUBSIDIARIES
NOTES TO THE CONDENSED CONSOLIDATED FINANCIAL STATEMENTS - (CONTINUED)
(Unaudited)

Assets/Liabilities Measured at Fair Value on a Recurring Basis
In the tables below, the Company has segregated all assets and liabilities that are measured at fair value on a recurring basis into the most appropriate level within the fair value hierarchy based on the inputs used to determine the fair value at the measurement date.

	Fair Value Measurement Using			
Type of Instruments	Quoted Prices in Active Markets for Identical Instruments (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Total Balance
(In millions)				
Assets at April 1, 2016:				
Available-for-sale securities:				
Corporate debt securities	$—	$—	$ 88.8	$ 88.8
Total assets measured at fair value	$—	$—	$ 88.8	$ 88.8
Liabilities at April 1, 2016:				
Derivative liabilities	$—	$ (1.9)	$ —	$ (1.9)
Contingent consideration	—	—	(3.2)	(3.2)
Total liabilities measured at fair value	$—	$ (1.9)	$ (3.2)	$ (5.1)
Assets at October 2, 2015:				
Available-for-sale securities:				
Corporate debt securities	$—	$ 8.4	$ 83.9	$ 92.3
Non-U.S. government security	—	0.7	—	0.7
Total assets measured at fair value	$—	$ 9.1	$ 83.9	$ 93.0
Liabilities at October 2, 2015:				
Contingent consideration	$—	$—	$ (4.1)	$ (4.1)
Total liabilities measured at fair value	$—	$—	$ (4.1)	$ (4.1)

The Company's available-for-sale securities are included in other assets, derivative liabilities are included in accrued liabilities, and contingent consideration is included in accrued liabilities and other long-term liabilities on the Condensed Consolidated Balance Sheets.
The Company has elected to use the income approach to value its derivative instruments using standard valuation techniques and Level 2 inputs, such as currency spot rates, forward points and credit default swap spreads. The Company’s derivative instruments are generally short-term in nature, typically one month to thirteen months in duration. The fair value of the Company's Level 2 corporate debt securities and non-U.S. government security is priced using quoted market prices for similar instruments or non-binding market prices that are corroborated by observable market data.

The fair value of the Company's Level 3 corporate debt securities, the CPTC loans, is based on the income approach by using the discounted cash flow model with key assumptions that include discount rates corresponding to the terms and risks associated with the loans to CPTC. If the estimated discount rates used were to increase or decrease, the fair value of the debt securities would decrease or increase, respectively. However, the Company does not increase the fair value of these securities above their par values as ORIX Capital Markets, LLC ("ORIX"), the loan agent, has the option to purchase these loans from the Company under the original terms and conditions at par value.

The Company measures the fair value of its Level 3 contingent consideration liabilities based on the income approach by using a discounted cash flow model with key assumptions that include estimated sales units or revenues of the acquired business or completion of certain milestone targets during the earn-out period, volatility, and estimated discount rates corresponding to the periods of expected payments. If the estimated sales units, revenues or probability of completing certain milestones were to increase or decrease during the respective earn-out period, the fair value of the contingent consideration would increase or decrease, respectively. If the estimated discount rates were to increase or decrease, the fair value of contingent consideration

VARIAN MEDICAL SYSTEMS, INC. AND SUBSIDIARIES
NOTES TO THE CONDENSED CONSOLIDATED FINANCIAL STATEMENTS - (CONTINUED)
(Unaudited)

would decrease or increase, respectively. Changes in volatility may result in an increase or decrease in the fair value of contingent consideration.

The following table presents the reconciliation for all assets and liabilities measured and recorded at fair value on a recurring basis using significant unobservable inputs (Level 3):

(In millions)	CPTC Loans	Contingent Consideration
Balance at October 2, 2015	$ 83.9	$ (4.1)
Additions [1]	4.9	—
Settlements [2]	—	1.2
Change in fair value recognized in earnings	—	(0.3)
Balance at April 1, 2016	$ 88.8	$ (3.2)

[1] Amounts reported under CPTC loans represent draw downs and accrued interest.

[2] Amounts reported under Contingent Consideration represent cash payments to settle contingent consideration liabilities.

There were no transfers of assets or liabilities between fair value measurement levels during either the three and six months ended April 1, 2016, or the three and six months ended April 3, 2015. Transfers between fair value measurement levels are recognized at the end of the reporting period.

Fair Value of Other Financial Instruments

The fair values of certain of the Company’s financial instruments, including bank deposits included in cash and cash equivalents, accounts receivable, net of allowance for doubtful accounts, short-term notes receivable, accounts payable, and short-term borrowings approximate their carrying amounts due to their short maturities.

As of both April 1, 2016 and October 2, 2015, the fair value of current maturities of long-term debt approximated its carrying value of $50.0 million, due to its short-term maturity. The fair value of the long-term debt payable in installments through fiscal year 2018 approximated its carrying value of $312.5 million and $337.5 million, at April 1, 2016 and October 2, 2015, respectively, because it is carried at a market observable interest rate that resets periodically and is categorized as Level 2 in the fair value hierarchy.

The fair value of the outstanding long-term notes receivable approximated their carrying value of $37.1 million and $30.9 million at April 1, 2016 and October 2, 2015, respectively, because it is based on terms of recent comparable transactions and is categorized as Level 3 in the fair value hierarchy.

VARIAN MEDICAL SYSTEMS, INC. AND SUBSIDIARIES
NOTES TO THE CONDENSED CONSOLIDATED FINANCIAL STATEMENTS - (CONTINUED)
(Unaudited)

4. RECEIVABLES

The following table summarizes the Company's accounts receivable and notes receivable as of April 1, 2016 and October 2, 2015:

(In millions)	April 1, 2016	October 2, 2015
Accounts receivable, gross	$940.2	$ 838.2
Allowance for doubtful accounts	(24.4)	(21.2)
Accounts receivable, net	$915.8	$ 817.0
Short-term	$852.6	$ 770.9
Long-term [1]	$63.2	$ 46.1
Notes receivable	$47.1	$ 40.9
Short-term [2]	$10.0	$ 10.0
Long-term [1]	$37.1	$ 30.9

[1] Included in other assets on the Company's Condensed Consolidated Balance Sheets.
[2] Included in prepaid expenses and other current assets on the Company's Condensed Consolidated Balance Sheets.

A financing receivable represents a financing arrangement with a contractual right to receive money, on demand or on fixed or determinable dates, and that is recognized as an asset on the Company’s Condensed Consolidated Balance Sheets. The Company’s financing receivables consist of accounts receivable with contractual maturities of more than one year and notes receivable. A small portion of the Company's financing accounts receivables were within the short-term accounts receivable.

Allowance for doubtful accounts was entirely related to the short-term accounts receivable as of April 1, 2016 and October 2, 2015.

See Note 15, "VPT Loans" for more information on the Company's long-term notes receivable balances.

5. GOODWILL AND INTANGIBLE ASSETS

The following table reflects the activity of goodwill by reportable operating segment:

(In millions)	Oncology Systems	Imaging Components	Other	Total
Balance at October 2, 2015	$ 158.8	$ 74.7	$50.0	$283.5
Foreign currency translation adjustments	—	—	0.4	0.4
Balance at April 1, 2016	$ 158.8	$ 74.7	$50.4	$283.9

The following table reflects the gross carrying amount and accumulated amortization of the Company’s finite-lived intangible assets included in other assets on the Condensed Consolidated Balance Sheets:

(In millions)	April 1, 2016	October 2, 2015
Finite-lived intangible assets:		
Acquired existing technology	$73.0	$ 71.7
Patents, licenses and other	35.0	35.3
Customer contracts and supplier relationship	20.1	20.1
Accumulated amortization	(71.9)	(65.1)
Net carrying amount	$56.2	$ 62.0

VARIAN MEDICAL SYSTEMS, INC. AND SUBSIDIARIES
NOTES TO THE CONDENSED CONSOLIDATED FINANCIAL STATEMENTS - (CONTINUED)
(Unaudited)

As of April 1, 2016 and October 2, 2015, the Company also had $9.3 million and $10.6 million, respectively, of in-process research and development assets.

Amortization expense for intangible assets was $3.8 million and $1.7 million in the three months ended April 1, 2016 and April 3, 2015, respectively, and $6.8 million and $3.3 million in the six months ended April 1, 2016 and April 3, 2015, respectively. The Company estimates the amortization expense for the remaining six months of fiscal year 2016, fiscal years 2017 through 2020, and thereafter, will be as follows (in millions): $6.3, $13.5, $9.8, $9.2, $7.9, and $9.5, respectively.

6. RELATED PARTY TRANSACTIONS

VMS has a 40% ownership interest in dpiX Holding LLC ("dpiX Holding"), a two-member consortium which has a 100% ownership interest in dpiX LLC ("dpiX"), a supplier of amorphous silicon based thin film transistor arrays ("flat panels") for the Company's Imaging Components' digital image detectors, for its Oncology Systems' On-Board Imager® and PortalVision™ imaging products as well as the imaging system in its Varian Particle Therapy ProBeam® system. In accordance with the dpiX Holding agreement, net profits or losses are allocated to the members, in accordance with their ownership interests.

The equity investment in dpiX Holding is accounted for under the equity method of accounting. When VMS recognizes its share of net profits or losses of dpiX Holding, profits or losses in inventory purchased from dpiX are eliminated until realized by VMS. VMS recorded income of $0.6 million and $0.9 million in the three months ended April 1, 2016 and April 3, 2015, respectively, from its equity investment in dpiX Holding. VMS recorded a loss of $0.1 million and income of $0.5 million in the six months ended April 1, 2016 and April 3, 2015, respectively, from its equity investment in dpiX Holding. Income and loss on the equity investment in dpiX Holding is included in selling, general and administrative expenses in the Condensed Consolidated Statements of Earnings. The carrying value of the equity investment in dpiX Holding, which is included in other assets on the Condensed Consolidated Balance Sheets, was $47.7 million at April 1, 2016 and $47.3 million at October 2, 2015.

The Company purchased glass transistor arrays from dpiX totaling $5.4 million and $5.6 million in the three months ended April 1, 2016 and April 3, 2015, respectively, and $10.4 million and $9.9 million in the six months ended April 1, 2016 and April 3, 2015, respectively. These purchases of glass transistor arrays are included as a component of inventories on the Condensed Consolidated Balance Sheets or cost of revenues - product in the Condensed Consolidated Statements of Earnings for these fiscal periods.

In October 2013, VMS entered into an amended agreement with dpiX and other parties that, among other things, provides the Company with the right to 50% of dpiX's total manufacturing capacity produced after January 1, 2014. The amended agreement requires the Company to pay for 50% of the fixed costs (as defined in the amended agreement), as determined at the beginning of each calendar year. As of April 1, 2016, the Company had fixed cost commitments of $13.5 million related to this amended agreement through December 31, 2016. The fixed cost commitments for future periods will be determined and approved by the dpiX board of directors at the beginning of each calendar year. The amended agreement will continue unless the ownership structure of dpiX changes (as defined in the amended agreement).

The Company has determined that dpiX is a variable interest entity because at-risk equity holders, as a group, lack the characteristics of a controlling financial interest. Majority votes are required to direct the manufacturing activities, legal operations and other activities that most significantly affect dpiX's economic performance. The Company does not have majority voting rights and no power to direct the activities of dpiX and therefore is not the primary beneficiary of dpiX. The Company's exposure to loss as a result of its involvement with dpiX is limited to the carrying value of the Company's investment and fixed cost commitments.

VARIAN MEDICAL SYSTEMS, INC. AND SUBSIDIARIES
NOTES TO THE CONDENSED CONSOLIDATED FINANCIAL STATEMENTS - (CONTINUED)
(Unaudited)

7. BORROWINGS

The following table summarizes the Company's short-term and long-term debt:

	April 1, 2016		October 2, 2015	
(Dollars in millions)	Amount	Weighted-Average Interest Rate	Amount	Weighted-Average Interest Rate
Short-term debt:				
Current maturities of 2013 Term Loan Facility	$50.0	1.56 %	$50.0	1.32 %
2013 Revolving Credit Facility	412.0	1.81 %	90.0	1.57 %
Sumitomo Credit Facility	19.6	0.58 %	18.4	0.63 %
Total short-term debt	$481.6		$158.4	
Long-term debt:				
2013 Term Loan Facility	$312.5	1.56 %	$337.5	1.32 %
Total long-term debt	$312.5		$337.5	

On August 27, 2013, VMS entered into an agreement (as amended to date) with certain lenders and Bank of America, N.A. (“BofA”) as administrative agent ("Credit Agreement"). The Credit Agreement provides for (i) a five-year term loan facility in an aggregate principal amount of up to $500 million (the “2013 Term Loan Facility”) and (ii) a five-year revolving credit facility in an aggregate principal amount of up to $500 million (the “2013 Revolving Credit Facility” and, collectively with the 2013 Term Loan Facility, the “2013 Credit Facility”). The 2013 Revolving Credit Facility also includes a $50 million sub-facility for the issuance of letters of credit and permits swing line loans of up to $25 million. In November 2015, the Company amended its Credit Agreement to increase the aggregate commitments under its revolving credit facility from $300 million to $500 million, reduce commitment fees and interest rate margins applicable to borrowings and increase the maximum consolidated leverage ratio that the Company must maintain. The 2013 Credit Facility contains provisions that limit the Company’s ability to pay cash dividends. The Credit Agreement will expire in August 2018. The proceeds of the 2013 Credit Facility may be used for working capital, capital expenditures, Company share repurchases, acquisitions and other corporate purposes.

Borrowings under the 2013 Term Loan Facility accrue interest either (i) based on a Eurodollar Rate, as defined in the Credit Agreement (the “Eurodollar Rate”), plus a margin of 0.875% to 1.125% based on a leverage ratio involving funded indebtedness and EBITDA (earnings before interest, tax and depreciation and amortization) or (ii) based upon a base rate of (a) the federal funds rate plus 0.50%, (b) BofA’s announced prime rate, or (c) the Eurodollar Rate plus 1.00%, whichever is highest, plus a margin of up to 0.125% based on the same leverage Ratio, depending upon instructions from the Company.

Borrowings under the 2013 Revolving Credit Facility accrue interest either (i) based on the Eurodollar Rate plus a margin of 1.125% to 1.375% based on a leverage ratio involving funded indebtedness and EBITDA or (ii) based upon a base rate of (a) the federal funds rate plus 0.50%, (b) BofA’s announced prime rate, or (c) the Eurodollar Rate plus 1.00%, whichever is highest, plus a margin of 0.125% to 0.375% based on the same leverage ratio, depending upon instructions from the Company. Borrowings under the 2013 Revolving Credit Facility have a maturity of approximately 30 days if based on the Eurodollar Rate and the same maturity as the 2013 Term Loan Facility if based on the base rate.

The Credit Agreement provides that certain material domestic subsidiaries must guarantee the 2013 Credit Facility, subject to certain limitations on the amount guaranteed. As of April 1, 2016, the 2013 Credit Facility was not guaranteed by any VMS subsidiary. In March 2016, the Credit Agreement was amended to provide for the release of an existing subsidiary stock pledge securing the 2013 Credit Facility and to provide that the Company will no longer be required to pledge the stock of any of its subsidiaries.

The Credit Agreement contains affirmative and negative covenants applicable to the Company and its subsidiaries that are typical for credit facilities of this type, and that are subject to materiality and other qualifications, carve-outs, baskets and exceptions. The Company has also agreed to maintain certain financial covenants including (i) a

maximum consolidated leverage ratio, involving funded indebtedness and EBITDA , and (ii) a minimum cash flow coverage ratio. The Company was in compliance with all covenants under the Credit Agreement for all periods within these condensed consolidated financial statements in which it was in existence.

VARIAN MEDICAL SYSTEMS, INC. AND SUBSIDIARIES
NOTES TO THE CONDENSED CONSOLIDATED FINANCIAL STATEMENTS - (CONTINUED)
(Unaudited)

VMS's Japanese subsidiary ("VMS KK") has an unsecured uncommitted credit agreement with Sumitomo that enables VMS KK to borrow and have outstanding at any given time a maximum of 3 billion Japanese Yen (the "Sumitomo Credit Facility"). In February 2016, the Sumitomo Credit Facility was extended and will expire in February 2017. Borrowings under the Sumitomo Credit Facility accrue interest based on the basic loan rate announced by the Bank of Japan plus a margin of 0.5% per annum.

8. DERIVATIVE INSTRUMENTS AND HEDGING ACTIVITIES

The Company measures all derivatives at fair value on the Condensed Consolidated Balance Sheets. The accounting for gains or losses resulting from changes in the fair value of those derivatives depends upon the use of the derivative and whether it qualifies for hedge accounting.

The fair values of derivative instruments reported on the Company's Condensed Consolidated Balance Sheets were as follows:

	Liability Derivatives		
	Balance Sheet	April 1, 2016	October 2, 2015
(In millions)	Location	Fair Value	Fair Value
Derivatives designated as hedging instruments:			
Foreign exchange forward contracts	Accrued liabilities	$ 1.3	$ —
Derivatives not designated as hedging instruments:			
Foreign exchange forward contracts	Accrued liabilities	0.6	—
Total derivatives		$ 1.9	$ —

At April 1, 2016 and October 2, 2015, the fair value of the Company's derivative assets was immaterial. See Note 3, "Fair Value" regarding valuation of the Company's derivative instruments. Also see Note 1, "Summary of Significant Accounting Policies" in the Consolidated Financial Statements in the Company's 2015 Annual Report regarding credit risk associated with the Company's derivative instruments.

Offsetting of Derivatives

The Company presents its derivative assets and derivative liabilities on a gross basis on the Condensed Consolidated Balance Sheets. However, under agreements containing provisions on netting with certain counterparties of foreign exchange contracts, subject to applicable requirements, the Company is allowed to net-settle transactions on the same date in the same currency, with a single net amount payable by one party to the other. As of April 1, 2016 and October 2, 2015, there were no potential effects of rights of setoff associated with derivative instruments. The Company is neither required to pledge nor entitled to receive cash collateral related to these derivative transactions.

Cash Flow Hedging Activities

The Company designates and accounts for certain of its hedges of forecasted foreign currency revenues as cash flow hedges. The Company's designated cash flow hedges de-designate when the anticipated revenues associated with the transactions are recognized and the effective portion in accumulated other comprehensive loss on the Condensed Consolidated Balance Sheets is reclassified to revenues in the Condensed Consolidated Statements of Earnings. Subsequent changes in fair value of the derivative instrument are recorded in selling, general and administrative expenses in the Condensed Consolidated Statements of Earnings to offset changes in fair value of the resulting non-functional currency receivables. For derivative instruments that are designated and qualify as cash flow hedges, the Company formally documents for each derivative instrument at the hedge's inception the relationship between the hedging instrument (foreign currency forward contract) and hedged item (forecasted foreign currency revenues), the nature of the risk being hedged, and its risk management objective and strategy for undertaking the hedge. The Company records the effective portion of the gain or loss on the derivative instruments that are designated and qualify

as cash flow hedges in accumulated other comprehensive loss on the Condensed Consolidated Balance Sheets and reclassifies these amounts into revenues in the Condensed Consolidated Statements of Earnings in the period during which the hedged transaction is recognized in earnings. The Company assesses hedge effectiveness both at the onset of the hedge and on an ongoing basis using regression analysis. The Company measures hedge ineffectiveness by comparing the cumulative change in the fair value of the effective component of the hedge contract with the cumulative change in the fair value of the hedged item. The Company recognizes any over performance of the derivative as ineffectiveness in revenues, and time value amounts

VARIAN MEDICAL SYSTEMS, INC. AND SUBSIDIARIES
NOTES TO THE CONDENSED CONSOLIDATED FINANCIAL STATEMENTS - (CONTINUED)
(Unaudited)

excluded from the assessment of effectiveness in cost of revenues in the Condensed Consolidated Statements of Earnings. During the six months ended April 1, 2016, the Company did not discontinue any cash flow hedges. At the inception of the hedge relationship and quarterly thereafter, the Company assesses whether the likelihood of meeting the forecasted cash flow is highly probable. As of April 1, 2016, all forecasted cash flows were still probable to occur. As of April 1, 2016, the net unrealized loss on derivative instruments, before tax, of $1.4 million was included in accumulated other comprehensive loss and is expected to be reclassified to earnings over the next 12 months that follows.

The Company had the following outstanding foreign currency forward contracts that were entered into to hedge forecasted revenues and designated as cash flow hedges:

(In millions)	April 1, 2016 Notional Value Sold
Euro	$ 33.0
Totals	$ 33.0

The following table presents the amounts, before tax, recognized in accumulated other comprehensive loss on the Condensed Consolidated Balance Sheets and in the Condensed Consolidated Statements of Earnings that are related to the effective portion of the foreign currency forward contracts designated as cash flow hedges:

	Gain (Loss) Recognized in Other Comprehensive Income (Effective Portion)				Location of Gain (Loss) Reclassified from Accumulated Other Comprehensive Income into Net Earnings	Gain Reclassified from Accumulated Other Comprehensive Income into Net Earnings (Effective Portion)			
	Three Months Ended		Six Months Ended			Three Months Ended		Six Months Ended	
(In millions)	April 1, 2016	April 3, 2015	April 1, 2016	April 3, 2015		April 1, 2016	April 3, 2015	April 1, 2016	April 3, 2015
Foreign currency forward contracts	$(1.4)	$ 1.2	$(1.3)	$ 2.0	Revenues	$0.1	$ 1.8	$0.1	$ 2.7

Balance Sheet Hedging Activities

The Company also hedges balance sheet exposures from its various subsidiaries and business units where the U.S. Dollar is the functional currency. The Company enters into foreign currency forward contracts to minimize the short-term impact of foreign currency fluctuations on monetary assets and liabilities denominated in currencies other than the U.S. Dollar functional currency. The foreign currency forward contracts are short term in nature, typically with a maturity of approximately one month, and are based on the net forecasted balance sheet exposure. These hedging instruments do not qualify for hedge accounting treatment. For derivative instruments not designated as hedging instruments, changes in their fair values are recognized in selling, general and administrative expenses in the Condensed Consolidated Statements of Earnings. Changes in the values of these hedging instruments are offset by changes in the values of foreign-currency-denominated assets and liabilities. Variations from the forecasted foreign currency assets or liabilities, coupled with a significant currency rate movement, may result in a material gain or loss if the hedges are not effectively offsetting the change in value of the foreign currency asset or liability. Other than foreign exchange hedging activities, the Company has no other free-standing or embedded derivative instruments.

VARIAN MEDICAL SYSTEMS, INC. AND SUBSIDIARIES
NOTES TO THE CONDENSED CONSOLIDATED FINANCIAL STATEMENTS - (CONTINUED)
(Unaudited)

The Company had the following outstanding foreign currency forward contracts that were entered into to hedge balance sheet exposures from its various foreign subsidiaries and business units:

	April 1, 2016	
(In millions)	Notional Value Sold	Notional Value Purchased
Australian Dollar	$15.6	$ —
Brazilian Real	5.3	—
British Pound	65.1	—
Canadian Dollar	—	8.9
Danish Krone	—	0.3
Euro	218.6	2.0
Hungarian Forint	2.6	—
Indian Rupee	10.5	—
Japanese Yen	73.2	—
New Zealand Dollar	4.5	—
Norwegian Krone	1.1	—
Swedish Krona	6.2	—
Swiss Franc	—	68.9
Thai Baht	1.5	—
Totals	$404.2	$ 80.1

The following table presents the gains recognized in the Condensed Consolidated Statements of Earnings related to the foreign currency forward exchange contracts that are not designated as hedging instruments:

	Amount of Gain (Loss) Recognized in Net Earnings on Derivative			
Location of Gain (Loss) Recognized in Income on Derivative	Three Months Ended		Six Months Ended	
(In millions)	April 1, 2016	April 3, 2015	April 1, 2016	April 3, 2015
Selling, general and administrative expenses	$(12.3)	$ 22.5	$(4.9)	$ 34.0

The gains or losses on these derivative instruments were significantly offset by the gains or losses resulting from the remeasurement of monetary assets and liabilities denominated in currencies other than the U.S. Dollar functional currency.

Contingent Features

Certain of the Company’s derivative instruments are subject to master agreements which contain provisions that require the Company, in the event of a default, to settle the outstanding contracts in net liability positions by making settlement payments in cash or by setting off amounts owed to the counterparty against any credit support or collateral held by the counterparty. As of April 1, 2016 and October 2, 2015, the Company did not have significant outstanding derivative instruments with credit-risk-related contingent features that were in a net liability position.

VARIAN MEDICAL SYSTEMS, INC. AND SUBSIDIARIES
NOTES TO THE CONDENSED CONSOLIDATED FINANCIAL STATEMENTS - (CONTINUED)
(Unaudited)

9. COMMITMENTS AND CONTINGENCIES

Product Warranty

The following table reflects the changes in the Company's accrued product warranty:

	Six Months Ended	
	April 1,	April 3,
(In millions)	2016	2015
Accrued product warranty, at beginning of period	$45.9	$49.3
Charged to cost of revenues	23.9	21.8
Actual product warranty expenditures	(22.0)	(28.1)
Accrued product warranty, at end of period	$47.8	$43.0

Accrued product warranty was included in accrued liabilities and other long-term liabilities on the Condensed Consolidated Balance Sheets as of April 1, 2016 and October 2, 2015.

Other Commitments

See Note 15, "VPT Loans" for additional information about the Company's commitments for funding development and construction of various proton therapy centers.

Contingencies

Environmental Remediation Liabilities

The Company's operations and facilities, past and present, are subject to environmental laws, including laws that regulate the handling, storage, transport and disposal of hazardous substances. Certain of those laws impose cleanup liabilities under certain circumstances. In connection with those laws and certain of the Company's past and present operations and facilities, the Company oversees various environmental cleanup projects and also reimburses certain third parties for cleanup activities. Those include facilities sold as part of the Company's electron devices business in 1995 and thin film systems business in 1997. In addition, the U.S. Environmental Protection Agency ("EPA") or third parties have named the Company as a potentially responsible party under the amended Comprehensive Environmental Response Compensation and Liability Act of 1980 ("CERCLA"), at sites to which the Company or the facilities of the sold businesses were alleged to have shipped waste for recycling or disposal (the "CERCLA sites"). In connection with the CERCLA sites, the Company to date has been required to pay only a small portion of the total amount as its contributions to cleanup efforts. Under the agreement that governs the spin-offs of Varian, Inc., which was acquired by Agilent Technologies Inc. (the successor entity hereinafter referred to as "VI"), and Varian Semiconductor Equipment Associates, Inc., which was acquired by Applied Materials, Inc. (the successor entity hereinafter referred to as "VSEA"), VI and VSEA are each obligated to indemnify the Company for one-third of the environmental cleanup costs associated with corporate, discontinued or sold operations prior to the spin-offs (after adjusting for any insurance proceeds or tax benefits received by the Company), as well as fully indemnify the Company for other liabilities arising from the operations of the business transferred to it as part of the spin-offs.

The Company spent $0.2 million and $0.5 million (net of amounts borne by VI and VSEA) in the three months ended April 1, 2016 and April 3, 2015, respectively, on environmental cleanup costs, third-party claim costs, project management costs and legal costs. The Company spent $0.4 million and $0.8 million (net of amounts borne by VI and VSEA) in the six months ended April 1, 2016 and April 3, 2015, respectively, on such costs.

Inherent uncertainties make it difficult to estimate the likelihood of the cost of future cleanup, third-party claims, project management and legal services for the CERCLA sites and one of the Company's past facilities. Nonetheless, as of April 1, 2016, the Company estimated that, net of VI's and VSEA's indemnification obligations, future costs associated with the CERCLA sites and this facility would range in total from $1.4 million to $9.8 million. The time frames over which these cleanup project costs are estimated vary, ranging from one year to thirty years as of April 1, 2016. Management believes that no amount in that range is more probable of being incurred than any other amount

and therefore accrued $1.4 million for these cleanup projects as of April 1, 2016. The accrued amount has not been discounted to present value due to the uncertainties that make it difficult to develop a single best estimate.

VARIAN MEDICAL SYSTEMS, INC. AND SUBSIDIARIES
NOTES TO THE CONDENSED CONSOLIDATED FINANCIAL STATEMENTS - (CONTINUED)
(Unaudited)

The Company believes it has gained sufficient knowledge to better estimate the scope and cost of monitoring, cleanup and management activities for its other past and present facilities. This, in part, is based on agreements with other parties and also cleanup plans approved by or completed in accordance with the requirements of the governmental agencies having jurisdiction. As of April 1, 2016, the Company estimated that the Company's future exposure, net of VI's and VSEA's indemnification obligations, for the costs at these facilities, and reimbursements of third-party's claims for these facilities, ranged in total from $5.1 million to $25.5 million. The time frames over which these costs are estimated to be incurred vary, ranging from one year to thirty years as of April 1, 2016. As to each of these facilities, management determined that a particular amount within the range of estimated costs was a better estimate than any other amount within the range, and that the amount and timing of these future costs were reliably determinable. The best estimate within that range was $8.6 million at April 1, 2016. Accordingly, the Company has accrued $7.1 million for these costs, which represents the best estimate discounted at 4%, net of inflation. This accrual is in addition to the $1.4 million described in the preceding paragraph.

These amounts are only estimates of anticipated future costs. The amounts the Company will actually spend may be greater or less than these estimates, even as the Company believes the degree of uncertainty will narrow as cleanup activities progress. While the Company believes its reserve is adequate, as the scope of the Company's obligations becomes more clearly defined, the Company may modify the reserve, and charge or credit future earnings accordingly. Nevertheless, based on information currently known to management, and assuming VI and VSEA satisfy their indemnification obligations, management believes the costs of these environmental-related matters are not reasonably likely to have a material adverse effect on the consolidated financial statements of the Company in any one fiscal year.

The Company evaluates its liability for investigation and cleanup costs in light of the obligations and apparent financial strength of potentially responsible parties and insurance companies with respect to which the Company believes it has rights to indemnity or reimbursement. The Company has asserted claims for recovery of environmental investigation and cleanup costs already incurred, and to be incurred in the future against various insurance companies and other third parties. The Company receives certain cash payments in the form of settlements and judgments from defendants, insurers and other third parties from time to time. The Company has also reached an agreement with an insurance company under which that insurer has agreed to pay a portion of the Company's past and future environmental-related expenditures. Receivables, net of VI's and VSEA's portion, from that insurer amounted to $1.9 million at April 1, 2016 and $2.1 million at October 2, 2015, with the noncurrent receivables portion included in other assets and the payable portion to that insurer is included in other long-term liabilities on the Condensed Consolidated Balance Sheets. The Company believes that this receivable is recoverable because it is based on a binding, written settlement agreement with what appears to be a financially viable insurance company, and the insurance company has paid the Company's claims in the past.

The availability of the indemnities of VI and VSEA will depend upon the future financial strength of VI and VSEA. Given the long-term nature of some of the liabilities, VI and VSEA may be unable to fund the indemnities in the future. It is also possible that a court would disregard this contractual allocation among the parties and require the Company to assume responsibility for obligations allocated to another party, particularly if the other party were to refuse or was unable to pay any of its allocated share. The agreement governing the spin-offs generally provides that if a court prohibits a company from satisfying its shared indemnification obligations, the indemnification obligations will be shared equally by the two other companies.

Other Matters

From time to time, the Company is a party to or otherwise involved in legal proceedings, claims and government inspections or investigations and other legal matters, both inside and outside the United States, arising in the ordinary course of its business or otherwise. The Company accrues amounts, to the extent they can be reasonably estimated, that it believes are adequate to address any liabilities related to legal proceedings and other loss contingencies that the Company believes will result in a probable loss (including, among other things, probable settlement value). A loss or a range of loss is disclosed when it is reasonably possible that a material loss will be incurred and can be estimated or

when it is reasonably possible that the amount of a loss, when material, will exceed the recorded provision.
In September 2015, Elekta Ltd. and William Beaumont Hospital served the Company with a complaint alleging infringement of patents related to certain aspects of cone beam imaging in conjunction with radiotherapy. During September 2015 and October 2015, the Company filed several complaints in the U.S. and foreign courts and the U.S. International Trade Commission against Elekta AB and its subsidiaries alleging infringement of various patents relating to certain aspects of cone beam imaging, cone-beam imaging gantries, volumetric modulated arc therapy ("VMAT"), and MR-Linac. In February 2016, Elekta Ltd. filed several complaints in the U.S. and foreign courts alleging infringement of certain patents related to linear accelerator control

VARIAN MEDICAL SYSTEMS, INC. AND SUBSIDIARIES
NOTES TO THE CONDENSED CONSOLIDATED FINANCIAL STATEMENTS - (CONTINUED)
(Unaudited)

systems and treatment planning. These lawsuits are ongoing and at this time, the Company is unable to predict the ultimate outcomes of these matters. Therefore, no amounts have been accrued as of April 1, 2016.

In June 2015, a foreign subsidiary of the Company was charged by the Department for Investigation and Penal Action of Lisbon with alleged improper activities relating to three tenders of medical equipment in Portugal during the period of 2003 to 2009. The Company has requested a judicial review available under Portuguese criminal procedure processes as to whether or not such changes are proper under Portuguese law. The Company previously undertook an internal investigation of this matter and voluntarily disclosed the results of this investigation to the U.S. Department of Justice and the U.S. Securities and Exchange Commission. At this time, the Company is unable to predict the ultimate outcome of this matter, and therefore no amounts have been accrued as of April 1, 2016.

In addition to the above, the Company is involved in other legal matters. However, such matters are subject to many uncertainties and outcomes are not predictable with assurance. The Company is unable to estimate a range of reasonably possible losses with respect to such matters. There can be no assurances as to whether the Company will become subject to significant additional claims and liabilities with respect to ongoing or future proceedings. If actual liabilities significantly exceed the estimates made, the Company’s consolidated financial position, results of operations or cash flows could be materially adversely affected. Legal expenses relating to legal matters are expensed as incurred.

Restructuring Charges

As part of the Company's plan to enhance operational performance through productivity initiatives, the Company implemented a workforce reduction, primarily in its Oncology Systems and Imaging Components segments, in the first quarter of fiscal year 2016. The Company incurred $4.8 million in restructuring charges during the six months ended April 1, 2016, most of which was incurred in the first quarter of fiscal year 2016, in connection with the restructuring program, of which $3.1 million was paid in cash during the six months ended April 1, 2016. The restructuring charges are included in selling, general and administrative expenses in the Condensed Consolidated Statements of Earnings. The Company expects to substantially complete this restructuring program by the end of fiscal year 2016, and any remaining restructuring charges relating to this program are not expected to be material. The Company incurred $3.1 million and $13.6 million in restructuring charges related to an enhanced retirement program and workforce reduction during the three and six months ended April 3, 2015.

10. RETIREMENT PLANS

The Company sponsors seven defined benefit pension plans for regular full time employees in Germany, Japan, Switzerland, the Philippines and the United Kingdom. The Company also sponsors a post-retirement benefit plan that provides healthcare benefits to certain eligible retirees in the United States. Two of the Company's defined benefit pension plans including one in Germany and one in the Philippines and the Company's post-retirement benefit plan are not presented in any of the following information as they are not material.

The components of net defined benefit costs were as follows:

(In millions)	Three Months Ended		Six Months Ended	
	April 1, 2016	April 3, 2015	April 1, 2016	April 3, 2015
Defined Benefit Plans				
Service cost	$1.5	$ 1.2	$3.0	$ 2.4
Interest cost	1.0	1.3	2.0	2.6
Expected return on plan assets	(1.7)	(1.8)	(3.4)	(3.6)
Amortization of prior service cost	—	0.1	—	0.1
Recognized actuarial loss	0.8	0.6	1.5	1.2
Net periodic benefit cost	$1.6	$ 1.4	$3.1	$ 2.7

11. INCOME TAXES

The Company’s effective tax rate was 28.1% and 28.0% in the three months ended April 1, 2016 and April 3, 2015, respectively, and 26.6% and 28.2% in the six months ended April 1, 2016 and April 3, 2015, respectively. The decrease in the

VARIAN MEDICAL SYSTEMS, INC. AND SUBSIDIARIES
NOTES TO THE CONDENSED CONSOLIDATED FINANCIAL STATEMENTS - (CONTINUED)
(Unaudited)

Company’s effective tax rate during the six months ended April 1, 2016, compared to the year ago period, was primarily due to the geographic mix of earnings.
The Company’s effective income tax rate differs from the U.S. federal statutory rate primarily because the Company’s foreign earnings are taxed at rates that are, on average, lower than the U.S. federal rate, and because the Company’s domestic earnings are subject to state income taxes. The total amount of unrecognized tax benefits did not materially change during the six months ended April 1, 2016; however, the amount of unrecognized tax benefits has increased as a result of positions taken during the current and prior years, and has decreased as the result of the expiration of the statutes of limitation in various jurisdictions.

12. STOCKHOLDERS’ EQUITY AND NONCONTROLLING INTERESTS

Share Repurchase Program

In November 2015, the VMS Board of Directors authorized the repurchase of an additional 8.0 million shares of VMS common stock through December 31, 2016. Share repurchases under the Company's authorizations may be made in open market purchases, in privately negotiated transactions (including accelerated share repurchase programs), or under Rule 10b5-1 share repurchase plans, and may be made from time to time in one or more blocks. All shares that were repurchased under the Company's share repurchase programs have been retired.
The Company repurchased shares of VMS common stock under various authorizations during the periods presented as follows:

	Three Months Ended		Six Months Ended	
(In thousands, except per share amounts)	April 1, 2016	April 3, 2015	April 1, 2016	April 3, 2015
Number of shares	725	825	3,150	2,325
Average repurchase price per share	$78.12	$91.71	$78.95	$86.54
Total cost	$56,627	$75,646	$248,704	$201,181

Included in the number of shares repurchased in the three and six months ended April 1, 2016, the Company completed an accelerated share repurchase in which it paid $40.4 million and received 0.5 million shares of VMS common stock. Included in the number of shares repurchased in the three and six months ended April 3, 2015, the Company completed an accelerated share repurchase in which it paid $45.0 million and received 0.5 million shares of VMS common stock. As of April 1, 2016, 6.3 million shares of VMS common stock remained available for repurchase under the November 2015 authorization.

Other Comprehensive Earnings

The changes in accumulated other comprehensive earnings (loss) by component and related tax effects are summarized as follows:

(In thousands)	Net Unrealized Gains (Losses) Defined Benefit Pension and Post-Retirement Benefit Plans	Net Unrealized Gains (Losses) Cash Flow Hedging Instruments	Net Unrealized Gains (Losses) Available for Sale Securities	Cumulative Translation Adjustment	Accumulated Other Comprehensive Earnings (Loss)
Balance at October 2, 2015	$ (46,070)	$ —	$ (112)	$ (40,281)	$ (86,463)
Other comprehensive earnings before reclassifications	—	(1,282)	(440)	5,176	3,454
Amounts reclassified out of other comprehensive earnings	1,232	(79)	604	—	1,757

Tax benefit (expense)	(173)	509	(52)	—	284
Balance at April 1, 2016	$ (45,011)	$ (852)	$ —	$ (35,105)	$ (80,968)

VARIAN MEDICAL SYSTEMS, INC. AND SUBSIDIARIES
NOTES TO THE CONDENSED CONSOLIDATED FINANCIAL STATEMENTS - (CONTINUED)
(Unaudited)

(In thousands)	Net Unrealized Gain (Loss) Defined Benefit Pension and Post-Retirement Benefit Plans	Net Unrealized Gain (Loss) Cash Flow Hedging Instruments	Cumulative Translation Adjustment	Accumulated Other Comprehensive Earnings (Loss)
Balance at September 26, 2014	$ (44,060)	$ 965	$ (15,516)	$ (58,611)
Other comprehensive earnings before reclassifications	—	1,977	(30,460)	(28,483)
Amounts reclassified out of other comprehensive earnings	1,082	(2,748)	—	(1,666)
Tax benefit (expense)	(151)	288	—	137
Balance at April 3, 2015	$ (43,129)	$ 482	$ (45,976)	$ (88,623)

The amounts reclassified out of other comprehensive earnings into the Condensed Consolidated Statements of Earnings, with line item location, during each period were as follows:

(In thousands)	Three Months Ended		Six Months Ended		
	April 1, 2016	April 3, 2015	April 1, 2016	April 3, 2015	
Comprehensive Earnings Components	Income (Loss) Before Taxes		Income (Loss) Before Taxes		Line Item in Statements of Earnings
Unrealized loss on defined benefit pension and post-retirement benefit plans	$(616)	$(541)	$(1,232)	$(1,082)	Cost of revenues & Operating expenses
Unrealized gain on cash flow hedging instruments	79	1,877	79	2,748	Revenues
Unrealized loss on available-for-sale-investments	—	—	(604)	—	Operating expenses
Total amounts reclassified out of other comprehensive earnings	$(537)	$1,336	$(1,757)	$1,666	

Noncontrolling Interests

In April 2015, the Company completed the acquisition of 73.5% of the then outstanding shares of MeVis Medical Solutions AG ("MeVis"), a public company based in Bremen, Germany that provides image processing software and services for cancer screening.

In August 2015, the Company, through one of its German subsidiaries, entered into a domination and profit and loss transfer agreement (the “DPLTA”) with MeVis. In October 2015, the DPLTA became effective upon its registration at the local court of Bremen, Germany. Under the DPLTA, MeVis subordinates its management to the Company and undertakes to transfer all of its annual profits and losses to the Company. In return, the DPLTA grants the noncontrolling shareholders of MeVis: (1) an annual recurring net compensation of €0.95 per MeVis share starting from January 1, 2015 and (2) a put right for their MeVis shares at €19.77 per MeVis share. Upon effectiveness of the DPLTA, the noncontrolling interests in MeVis became redeemable as a result of the put right and were reclassified to temporary equity. As of April 1, 2016, the redemption value of redeemable noncontrolling interests in MeVis was $10.3 million.

During the six months ended April 1, 2016, an immaterial number of MeVis' shares were purchased under the put right. As of April 1, 2016, noncontrolling shareholders together held approximately 480,000 shares of MeVis, representing 26.4% of the outstanding shares.

Changes in noncontrolling interests and redeemable noncontrolling interests relating to MeVis and other subsidiaries of the Company were as follows:

23

VARIAN MEDICAL SYSTEMS, INC. AND SUBSIDIARIES
NOTES TO THE CONDENSED CONSOLIDATED FINANCIAL STATEMENTS - (CONTINUED)
(Unaudited)

(In thousands)	Noncontrolling Interests	Redeemable Noncontrolling Interests
Balance at October 2, 2015	$ 14,744	$ —
Net earnings (loss) attributable to noncontrolling interests	(95)	122
Reclassification of noncontrolling interests in MeVis to redeemable noncontrolling interests	(10,382)	10,382
Other	(499)	(173)
Balance at April 1, 2016	$ 3,768	$ 10,331

13. EMPLOYEE STOCK PLANS

The table below summarizes the net share-based compensation expense recognized for employee stock awards and for the option component of the employee stock purchase plan shares:

(In thousands)	Three Months Ended		Six Months Ended	
	April 1, 2016	April 3, 2015	April 1, 2016	April 3, 2015
Cost of revenues - Product	$1,117	$1,206	$2,108	$2,315
Cost of revenues - Service	960	986	1,949	1,938
Research and development	1,746	1,654	3,323	3,392
Selling, general and administrative	8,727	8,655	16,425	17,593
Total share-based compensation expense	$12,550	$12,501	$23,805	$25,238
Income tax benefit for share-based compensation	$(3,799)	$(3,943)	$(7,257)	$(7,916)

During the six months ended April 1, 2016 and April 3, 2015, the Company granted performance units to certain employees under the Third Amended 2005 Plan. The number of shares of VMS common stock ultimately issued under the performance units at vesting depend on the Company's business performance during the performance period, against specified performance targets, both of which are set by the Compensation and Management Development Committee of the Board of Directors. The performance units vest at the end of a three-year service period. Performance units granted prior to fiscal year 2015 have one three-year performance period for both the Company's performance and total shareholder return, performance units granted in fiscal year 2015 have a one year Company performance period and a three year total shareholder return, and performance units awarded in fiscal year 2016 have three separate one-year Company performance periods and a three year total shareholder return. Subject to certain exceptions, any unvested performance unit awards are forfeited at the time of termination.

The fair value of options granted was estimated at the date of grant using the Black-Scholes model with the following weighted average assumptions:

	Three Months Ended		Six Months Ended	
	April 1, 2016	April 3, 2015	April 1, 2016	April 3, 2015
Employee Stock Option Plans				
Expected term (in years)	4.13	4.13	4.13	4.15
Risk-free interest rate	1.1 %	1.3 %	1.1 %	1.3 %
Expected volatility	20.0 %	22.1 %	20.0 %	22.1 %
Expected dividend	— %	— %	— %	— %
Weighted average fair value at grant date	$13.67	$18.53	$13.70	$18.56

24

VARIAN MEDICAL SYSTEMS, INC. AND SUBSIDIARIES
NOTES TO THE CONDENSED CONSOLIDATED FINANCIAL STATEMENTS - (CONTINUED)
(Unaudited)

The option component of employee stock purchase plan shares was estimated at the date of grant using the Black-Scholes model with the following weighted average assumptions:

	Six Months Ended	
	April 1, 2016	April 3, 2015
Employee Stock Purchase Plan		
Expected term (in years)	0.50	0.50
Risk-free interest rate	0.3 %	0.1 %
Expected volatility	17.0 %	8.3 %
Expected dividend	— %	— %
Weighted average fair value at grant date	$15.59	$14.24

A summary of share-based awards available for grant is as follows:

(In thousands)	Shares Available for Grant
Balance at October 2, 2015	6,661
Granted	(2,309)
Cancelled or expired	256
Balance at April 1, 2016	4,608

Awards other than stock options set forth in the table were calculated under the Third Amended 2005 Plan as 2.6 shares for every one share awarded. The shares available for grant is further adjusted to reflect a maximum payout that could be issued for each performance unit granted. The maximum payouts that could be issued for each performance unit granted are 1.75 shares beginning in fiscal year 2016, 2.0 shares in fiscal year 2015 and 1.5 shares prior to fiscal year 2015.

Activity under the Company’s employee stock plans is presented below:

	Options Outstanding			
(In thousands, except per share amounts)	Number of Shares	Weighted Average Exercise Price	Weighted Average Remaining Term (in years)	Aggregate Intrinsic Value (1)
Balance at October 2, 2015	2,537	$ 72.58		
Granted	823	75.93		
Cancelled or expired	(20)	86.29		
Exercised	(256)	51.22		
Balance at April 1, 2016	3,084	$ 75.15	4.7	$ 26,818
Exercisable at April 1, 2016	1,678	$ 69.85	3.3	$ 22,411

(1) The aggregate intrinsic value represents the total pre-tax intrinsic value of options, which is computed based on the difference between the exercise price and VMS’s closing common stock price of $81.15 as of April 1, 2016, the last trading date of the second quarter of fiscal year 2016, and which would have been received by the option holders had all option holders exercised and sold their options as of that date.

As of April 1, 2016, there was $16.3 million of total unrecognized compensation expense related to outstanding stock options. This unrecognized compensation expense is expected to be recognized over a weighted average period of 1.8 years.

25

VARIAN MEDICAL SYSTEMS, INC. AND SUBSIDIARIES
NOTES TO THE CONDENSED CONSOLIDATED FINANCIAL STATEMENTS - (CONTINUED)
(Unaudited)

The activity for restricted stock, restricted stock units, deferred stock units and performance units is summarized as follows:

(In thousands, except per share amounts)	Number of Shares	Weighted Average Grant-Date Fair Value
Balance at October 2, 2015	950	$ 84.11
Granted	480	77.84
Vested	(384)	81.04
Cancelled or expired	(67)	81.81
Balance at April 1, 2016	979	$ 82.33

As of April 1, 2016, unrecognized compensation expense totaling $53.7 million was related to awards of restricted stock, restricted stock units, deferred stock units and performance units. This unrecognized compensation expense is expected to be recognized over a weighted average period of 2.0 years.

14. EARNINGS PER SHARE

Basic net earnings per share is computed by dividing net earnings attributable to Varian by the weighted average number of shares of VMS common stock outstanding for the period. Diluted net earnings per share is computed by dividing net earnings attributable to Varian by the sum of the weighted average number of common shares outstanding and dilutive common shares under the treasury stock method.

The following table sets forth the computation of basic and diluted net earnings per share:

(In thousands, except per share amounts)	Three Months Ended		Six Months Ended	
	April 1, 2016	April 3, 2015	April 1, 2016	April 3, 2015
Net earnings attributable to Varian	$96,971	$105,969	$185,998	$199,283
Weighted average shares outstanding - basic	95,671	100,157	96,474	100,315
Dilutive effect of potential common shares	508	869	598	1,026
Weighted average shares outstanding - diluted	96,179	101,026	97,072	101,341
Net earnings per share attributable to Varian - basic	$1.01	$1.06	$1.93	$1.99
Net earnings per share attributable to Varian - diluted	$1.01	$1.05	$1.92	$1.97
Anti-dilutive employee shared based awards, excluded	2,031	956	2,031	1,194

The Company excludes potentially dilutive common shares (consisting of shares underlying stock options and the employee stock purchase plan) from the computation of diluted weighted average shares outstanding if the per share value, either the exercise price of the awards or the sum of (a) the exercise price of the awards and (b) the amount of the compensation cost attributed to future services and not yet recognized and (c) the amount of tax benefit or shortfall that would be recorded in additional paid-in capital when the award becomes deductible, is greater than the average market price of the shares, because the inclusion of the shares underlying these stock awards would be anti-dilutive to earnings per share.

VARIAN MEDICAL SYSTEMS, INC. AND SUBSIDIARIES
NOTES TO THE CONDENSED CONSOLIDATED FINANCIAL STATEMENTS - (CONTINUED)
(Unaudited)

15. VPT LOANS

The following table lists the Company's outstanding loans and commitments for funding development and construction of various proton therapy centers:

	April 1, 2016		October 2, 2015	
(In millions)	Balance	Commitment	Balance	Commitment
Long-term notes receivable [1]:				
NYPC loan	$24.9	$ 66.6	$18.7	$ 72.8
MPTC loan	12.2	22.8	12.2	22.8
	$37.1	$ 89.4	$30.9	$ 95.6
Available-for-sale Securities [1]:				
CPTC loans	$88.8	$ 3.4	$83.9	$ —
	$88.8	$ 3.4	$83.9	$ —

(1) Included in other assets on the Company's Condensed Consolidated Balance Sheets.

New York Proton Center ("NYPC") Loan

In July 2015, the Company, through one of its subsidiaries, committed to loan up to $91.5 million to MM Proton I, LLC in connection with a purchase agreement to supply a proton system to equip NYPC. The commitment includes a $73.0 million “Senior First Lien Loan” with a six-year term at 9% interest and an $18.5 million “Subordinate Loan” with a six-and-a-half-year term at up to 13.5% interest. The Company's entire commitment of the Subordinate Loan was drawn down in fiscal year 2015. The Company expects the remaining draw downs of the Senior First Lien Loan to take place primarily through fiscal year 2018. Other lenders participating in the NYPC loans include J.P. Morgan and an affiliate of The Goldman Sachs Group, Inc. The Senior First Lien Loan is collateralized by all of the assets of the NYPC.

As of April 1, 2016, the Company had recorded $12.1 million in accounts receivable, which includes unbilled accounts receivable, from NYPC. As of October 2, 2015, the Company did not have accounts receivable from NYPC.

Maryland Proton Therapy Center ("MPTC") Loan

In May 2015, the Company, through one of its subsidiaries, committed to loan up to $35.0 million to MPTC, which included rolling over an existing loan for $10.0 million plus $2.2 million of previously accrued interest. The Company had previously entered into an agreement with MPTC to supply it with a proton system. Varian's commitment is in the form of a subordinated loan that is due, with accrued interest, in three annual payments from 2020 to 2022. The Company's outstanding commitment under the loan to MPTC is to be paid in four installments of $5.7 million each on June 30, 2016, September 30, 2016, December 30, 2016 and March 31, 2017. The interest on the loan accrues at 12%. As of April 1, 2016 and October 2, 2015, the Company had recorded $22.0 million and $28.6 million, respectively, in accounts receivable, which includes unbilled accounts receivable, from MPTC.

CPTC Loans

As of October 2, 2015, the Company had loaned $73.5 million under a Tranche A loan and $10.4 million under a Tranche B loan to CPTC to fund the development, construction and initial operations of the Scripps Proton Therapy Center in San Diego, California under a loan agreement with ORIX and J.P. Morgan. ORIX is the loan agent for this facility and, along with CPTC and Scripps, has budgetary approval authority for the Scripps Proton Therapy Center. In November 2015, ORIX, J.P. Morgan and the Company (collectively the “Lenders”) and CPTC entered into a forbearance agreement whereby the lenders will not enforce their rights to principal and interest payments until April 2017, subject to CPTC maintaining certain covenants and achieving certain targets, with additional extensions through September 2017 based on hitting additional targets largely around patient volume and cash flow. In connection with the forbearance agreement the Lenders agreed to make available up to an additional $9.7 million of loan proceeds (based on their pro-rata share of the existing loan) with terms similar to the Tranche A loan for additional working capital needs; the Company's proportionate share of this commitment is $4.4 million ("Tranche C loan"). There were no other significant changes to the loan agreements. As of April 1, 2016, the Company's remaining commitment under

the Tranche C loan is expected to be drawn down over the next 12 months. The Tranche A, Tranche B and Tranche C loans are collectively, referred to as the “CPTC Loans.” As of April 1, 2016, the Company had loaned $76.9 million

VARIAN MEDICAL SYSTEMS, INC. AND SUBSIDIARIES
NOTES TO THE CONDENSED CONSOLIDATED FINANCIAL STATEMENTS - (CONTINUED)
(Unaudited)

under the Tranche A loan, $10.9 million under the Tranche B loan and $1.0 million under the Tranche C loan. No amounts were available for draw down under the Tranche A and Tranche B loans.

The amounts loaned under the CPTC Loans include accrued interest. ORIX has the option to purchase the Company's share of the CPTC loans at par. The CPTC loans meet the definition of a debt security and therefore are accounted for as available-for-sale securities and recorded at fair value as of April 1, 2016 and October 2, 2015. The Company's CPTC loans are included in other assets on the Company's Condensed Consolidated Balance Sheets as of April 1, 2016 and October 2, 2015 because the Company did not expect to be repaid and did not intend to sell all or a portion of its CPTC loans in the next twelve months. The Tranche B loan is subordinated to the Tranche A loan in the event of default, but otherwise has the same terms as the Tranche A loan. The CPTC Loans are collateralized by all of the assets of the Scripps Proton Therapy Center. The CPTC Loans mature in September 2017 and bear interest at the London Interbank Offer Rate (“LIBOR”) plus 7.00% per annum with a minimum interest rate of 9.00% per annum. Interest only payments on the CPTC Loans were due monthly in arrears until January 1, 2015, at which time monthly payments based on amortization of the principal balance over a 15-year period at the above mentioned interest rate become due and payable. To date no amortizing principal payments have been made. The principal and interest payments are subject to the forbearance agreement mentioned above.

As of April 1, 2016 and October 2, 2015, the Company had recorded $27.7 million and $25.2 million, respectively, in accounts receivable, which includes unbilled accounts receivable, from CPTC.

The Company has determined that MM Proton I, LLC, MPTC and CPTC are variable interest entities and that the Company holds a significant variable interest of each of the entities through its participation in the loan facilities and its agreements to supply and service the proton therapy equipment. The Company has concluded that it is not the primary beneficiary of any of these entities. The Company has no voting rights, has no approval authority or veto rights for these centers' budget, and does not have the power to direct patient recruitment, clinical operations and management of these Centers, which the Company believes are the matters that most significantly affect their economic performance. The Company’s exposure to loss as a result of its involvement with MM Proton I, LLC, MPTC and CPTC is limited to the carrying amounts of the above mentioned assets on its Condensed Consolidated Balance Sheets.

16. SEGMENT INFORMATION

The Company’s operations are grouped into two reportable operating segments: Oncology Systems and Imaging Components. The Company’s Ginzton Technology Center ("GTC") and Varian Particle Therapy ("VPT") business are reflected in the “Other” category because these operating segments do not meet the criteria of a reportable operating segment. The operating segments were determined based on how the Company’s Chief Executive Officer, its Chief Operating Decision Maker (“CODM”), views and evaluates the Company’s operations. The CODM allocates resources to and evaluates the financial performance of each operating segment primarily based on operating earnings.

Description of Segments

The Oncology Systems segment designs, manufactures, sells and services hardware and software products for treating cancer with conventional radiation therapy, and advanced treatments such as fixed field intensity-modulated radiation therapy (“IMRT”), image-guided radiation therapy (“IGRT”), VMAT, stereotactic radiosurgery (“SRS”), stereotactic body radiotherapy (“SBRT”) and brachytherapy. Products include linear accelerators, brachytherapy afterloaders, treatment simulation and verification equipment and accessories; as well as information management, treatment planning and image processing software. Oncology Systems’ products enable radiation oncology departments in hospitals and clinics to perform conventional radiotherapy treatments and offer advanced treatments such as IMRT, IGRT, VMAT, SRS and SBRT, as well as to treat patients using brachytherapy techniques, which involve temporarily implanting radioactive sources. The Company’s Oncology Systems products are also used by neurosurgeons to perform stereotactic radiosurgery. Oncology Systems’ customers worldwide include university research and community hospitals, private and governmental institutions, healthcare agencies, physicians’ offices and cancer care clinics.

The Imaging Components segment designs, manufactures, sells and services X-ray imaging components for use in a range of applications, including radiographic or fluoroscopic imaging, mammography, special procedures, computed tomography, computer-aided diagnostics and industrial applications. The Company provides a broad range of X-ray imaging components including X-ray tubes, flat panel digital image detectors, high voltage connectors, image processing software and workstations, ionization chambers and automatic exposure control systems. The Company's X-ray imaging components are sold to imaging system OEM customers that incorporate them into their medical diagnostic, dental, veterinary and industrial imaging systems to independent service companies and directly to end-users for replacement purposes. The Imaging Components segment also

VARIAN MEDICAL SYSTEMS, INC. AND SUBSIDIARIES
NOTES TO THE CONDENSED CONSOLIDATED FINANCIAL STATEMENTS - (CONTINUED)
(Unaudited)

designs, manufactures, sells and services security and inspection products, which include Linatron® X-ray accelerators, imaging processing software and image detection products for security and inspection purposes, such as cargo screening at ports and borders and nondestructive examination in a variety of applications. The Company generally sells security and inspection products to OEM customers who incorporate its products into their inspection systems.

The Company's GTC and VPT business are reported together under the "Other" category.

The VPT business develops, designs, manufactures, sells and services products and systems for delivering proton therapy, a form of external beam radiotherapy using proton beams for the treatment of cancer.

GTC develops technologies that enhance the Company's current businesses or may lead to new business areas, including technology to improve radiation therapy and X-ray imaging, as well as other technology for a variety of applications.

The following table summarizes selected operating results information for each reportable segment:

	Three Months Ended		Six Months Ended	
(In millions)	April 1, 2016	April 3, 2015	April 1, 2016	April 3, 2015
Revenues				
Oncology Systems	$584.1	$589.4	$1,173.4	$1,152.7
Imaging Components	143.7	155.5	285.1	321.5
Total reportable segments	727.8	744.9	1,458.5	1,474.2
Other	31.0	14.5	57.4	23.1
Total Company	$758.8	$759.4	$1,515.9	$1,497.3
Operating Earnings (Loss)				
Oncology Systems	$129.5	$125.9	$244.7	$252.0
Imaging Components	25.7	40.0	50.9	81.2
Total reportable segments	155.2	165.9	295.6	333.2
Other	(12.7)	(12.7)	(25.0)	(26.3)
Corporate	(8.6)	(7.2)	(20.0)	(31.4)
Total Company	$133.9	$146.0	$250.6	$275.5

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM
To the Board of Directors and
Stockholders of Varian Medical Systems, Inc.:

We have reviewed the accompanying condensed consolidated balance sheet of Varian Medical Systems, Inc. and its subsidiaries as of April 1, 2016 and the related condensed consolidated statements of earnings and of comprehensive earnings for the three-month and six-month periods ended April 1, 2016 and April 3, 2015, and the condensed consolidated statement of cash flows for the six-month periods ended April 1, 2016 and April 3, 2015. These interim financial statements are the responsibility of the Company's management.

We conducted our review in accordance with the standards of the Public Company Accounting Oversight Board (United States). A review of interim financial information consists principally of applying analytical procedures and making inquiries of persons responsible for financial and accounting matters. It is substantially less in scope than an audit conducted in accordance with the standards of the Public Company Accounting Oversight Board (United States), the objective of which is the expression of an opinion regarding the financial statements taken as a whole. Accordingly, we do not express such an opinion.

Based on our review, we are not aware of any material modifications that should be made to the accompanying condensed consolidated interim financial statements for them to be in conformity with accounting principles generally accepted in the United States of America.

We previously audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the consolidated balance sheet as of October 2, 2015, and the related consolidated statements of earnings and of comprehensive earnings, of equity, and of cash flows for the year then ended (not presented herein), and in our report dated November 25, 2015, we expressed an unqualified opinion on those consolidated financial statements. In our opinion, the information set forth in the accompanying condensed consolidated balance sheet as of October 2, 2015, is fairly stated in all material respects in relation to the consolidated balance sheet from which it has been derived.

/s/ PRICEWATERHOUSECOOPERS LLP
PricewaterhouseCoopers LLP
San Jose, California
May 10, 2016

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

Forward-Looking Statements

This Quarterly Report on Form 10-Q contains "forward-looking" statements within the meaning of the Private Securities Litigation Reform Act of 1995, which provides a "safe harbor" for statements about future events, products and future financial performance that are based on the beliefs of, estimates made by, and information currently available to the management of Varian Medical Systems, Inc. ("VMS") and its subsidiaries (collectively "we," "our" or the "Company"). The outcome of the events described in these forward-looking statements is subject to risks and uncertainties. Actual results and the outcome or timing of certain events may differ significantly from those projected in these forward-looking statements or management's current expectations due to the factors cited in this "Management's Discussion and Analysis of Financial Condition and Results of Operations" ("MD&A"), the Risk Factors listed under Part II, Item 1A of this Quarterly Report on Form 10-Q, and other factors described from time to time in our other filings with the Securities and Exchange Commission ("SEC"), or other reasons. For this purpose, statements concerning: industry or market segment outlook; market acceptance of or transition to new products or technology such as fixed field intensity-modulated radiation therapy, image-guided radiation therapy, stereotactic radiosurgery, volumetric modulated arc therapy, brachytherapy, software, treatment techniques, proton therapy and advanced X-ray tube and flat panel products; growth drivers; future orders, revenues, backlog, earnings or other financial results; and any statements using the terms "believe," "expect," "anticipate," "can," "should," "would," "could," "estimate," "may," "intend "potential," and "possible" or similar statements are forward-looking statements that involve risks and uncertainties that could cause our actual results and the outcome and timing of certain events to differ materially from those projected or management's current expectations. By making forward-looking statements, we have not assumed any obligation to, and you should not expect us to, update or revise those statements because of new information, future events or otherwise.

Overview

Our operations are currently grouped into two reportable operating segments: Oncology Systems and Imaging Components. Our Ginzton Technology Center ("GTC") and Varian Particle Therapy ("VPT") business are reflected in the "Other" category because these operating segments do not meet the criteria of a reportable operating segment. The operating segments were determined based on how our Chief Executive Officer, who is our Chief Operating Decision Maker ("CODM"), views and evaluates our operations. The CODM allocates resources to and evaluates the financial performance of each operating segment primarily based on operating earnings.

Total revenues decreased slightly, gross margin decreased 0.7 percentage points, net earnings attributable to Varian decreased 8%, and net earnings per diluted share decreased 4%, in the second quarter of fiscal year 2016, compared to the year-ago period.

Gross orders increased 6% in Oncology Systems and decreased 12% in Imaging Components in the second quarter of fiscal year 2016, compared to the year-ago period. Our backlog at April 1, 2016 was 6% higher than at the end of the second quarter of fiscal year 2015.

In order to assist with the assessment of how our underlying businesses performed, we compare the percentage change in revenues and gross orders from one period to another, excluding the effect of foreign currency fluctuations (i.e., using constant currency exchange rates). To present this information on a constant currency basis, we convert current period revenues and gross orders in currencies other than U.S. Dollars into U.S. Dollars using the comparable prior period's average exchange rate.

The U.S. Dollar strengthened against the Euro and certain foreign currencies and weakened against the Japanese Yen in the second quarter of fiscal year 2016, compared to the year-ago period, which had a net unfavorable impact on our revenues and gross orders. We expect that fluctuations of foreign currencies against the U.S. Dollar will continue to cause variability in our financial performance.

In December 2015, the U.S. President signed into law the Protecting Americans from Tax Hikes Act of 2015 ("PATH Act"), which suspended the 2.3% medical device excise tax implemented as part of the Affordable Care Act for a two-year period through December 31, 2017. The suspension of the medical device excise tax had a positive impact in

the second quarter of fiscal year 2016, and we expect the suspension to have a positive impact on our gross margin for the remainder of fiscal year 2016 and fiscal year 2017. Additionally, the PATH Act permanently extended the research and development ("R&D") tax credit, which has a favorable impact on our effective tax rate.

Oncology Systems. Our largest business segment is Oncology Systems, which designs, manufactures, sells and services hardware and software products for treating cancer with conventional radiotherapy and advanced treatments, such as intensity-

modulated radiation therapy ("IMRT"), image-guided radiation therapy ("IGRT"), volumetric modulated arc therapy ("VMAT"), stereotactic radiotherapy, stereotactic body radiotherapy and brachytherapy, as well as informatics software for information management, clinical knowledge exchange, patient care management, practice management and decision-making support for comprehensive cancer clinics, radiotherapy centers and medical oncology practices. Our primary goal in the Oncology Systems business is to promote the adoption of more advanced and effective cancer treatments. In our view, the fundamental market forces that drive long-term growth in our Oncology Systems business are the rise in cancer cases; technology advances and product developments that are leading to improvements in patient care; customer demand for the more advanced and effective cancer treatments that we enable; competitive conditions among hospitals and clinics to offer such advanced treatments; continued improvement in safety and cost efficiency in delivering radiation therapy; and underserved medical needs outside of the United States. Over the last few years, we have seen a greater percentage of Oncology Systems gross orders and revenues coming from emerging markets within our international region, which typically purchase lower-priced products, which generally have lower gross margin percentages compared to developed markets. We have also seen an increased portion of gross orders and revenues coming from services and software licenses, both of which have higher gross margin percentages than our hardware products. We have been investing a higher portion of our Oncology Systems research and development budget in software and software-related products.

The radiation oncology market in North America is largely characterized by replacements of older machines, with periodic increases in demand driven by the introduction of new technologies. Reimbursement rates in the United States have generally supported a favorable return on investment for the purchase of new radiotherapy equipment. While we believe that improved product functionality, greater cost-effectiveness and prospects for better clinical outcomes with new capabilities such as IMRT, IGRT and VMAT tend to drive demand for radiotherapy products, large changes in reimbursement rates or reimbursement structure can affect customer demand and cause market shifts. We do not know what impact the Patient Protection and Affordable Care Act (the “Affordable Care Act”) in the United States will have on long-term growth or demand for our products and services. We believe, however, that growth of the radiation oncology market in the United States is being impacted as customers’ decision-making processes are complicated by the uncertainties surrounding the Affordable Care Act and reimbursement rates for radiotherapy and radiosurgery, and that this uncertainty will continue during fiscal year 2016 and result in a high degree of variability of gross orders and revenues from quarter-to-quarter. We also believe that the Affordable Care Act, Accountable Care Organizations and bundled payment arrangements are causing healthcare providers to re-evaluate their business models and we are seeing increased consolidation of hospitals and clinics and more integration of systems and equipment across multi-site healthcare networks, which is impacting transaction size, timing and purchasing processes, and also contributing to the increased business variability.

In the radiation oncology markets outside of North America, we expect the long-term market to grow in EMEA with mixed performance across the region. In APAC, we expect China to lead longer term regional growth, off-setting a slower Japanese market. Our long-term outlook for Latin America is positive despite volatility. Overall, we believe the longer-term global radiation oncology market can grow, on average and in constant currencies, in the mid-single-digit range.

In the second quarter of fiscal year 2016, Oncology Systems revenues decreased 1% and gross margin increased by 0.5 percentage points compared to the year-ago period.

In the second quarter of fiscal year 2016, Oncology Systems gross orders increased 6%, compared to the year-ago period, due to increases in gross orders of 7% and 6% from our North America and international regions, respectively. On a constant currency basis, Oncology Systems international gross orders increased 8% in the second quarter of fiscal year 2016, compared to the year-ago period.

Imaging Components. Our Imaging Components business segment designs, manufactures, sells and services X-ray imaging components for use in a range of applications, including radiographic or fluoroscopic imaging, mammography, special procedures, computed tomography, computer-aided diagnostics, and industrial applications. We provide a broad range of X-ray imaging components including X-ray tubes, flat panel digital image detectors, high voltage connectors, image processing software and workstations, ionization chambers and automatic exposure control systems. Our Imaging Components business segment also designs, manufactures, sells and services security and

inspection products, which include Linatron® X-ray accelerators, imaging processing software and image detection products for security and inspection purposes, such as cargo screening at ports and borders and nondestructive examination in a variety of applications. We continue to view the long-term driver for this business to be the ongoing success of key X-ray imaging original equipment manufacturers (“OEMs”) that incorporate our products into their medical diagnostic, dental, veterinary, security and industrial imaging systems. Orders and revenues for our security and inspection products have been and may continue to be unpredictable as governmental agencies may place large orders with us or our OEM customers in a short time period, and then may not place any orders for a long time period thereafter.

Our success in Imaging Components depends upon our ability to anticipate changes in our markets, the direction of technological innovation and the demands of our customers. A significant portion of our Imaging Components customers are outside of the United States and products in this business are generally priced in U.S. Dollars. As a result, the demand for Imaging Components products has been negatively impacted by pricing pressures resulting from the strengthening of the U.S. Dollar. In addition, some customers have asked for additional discounts, delayed purchasing decisions, or moved to in-sourcing supply of such components or migrated to lower cost alternatives. In the event of a strengthening U.S. Dollar, we expect that demand and pricing will continue to be negatively impacted for Imaging Component products. The market for border protection systems has slowed significantly and end customers, particularly in oil-based economies and war zones in which we have a significant customer base, are delaying tenders, resulting in a decline in the demand for security and inspection products which is expected to continue.

In the second quarter of fiscal year 2016, Imaging Components revenues, gross orders, and gross margin decreased by 8%, 12% and 2.6 percentage points, respectively, compared to the year-ago period.

Other. The “Other” category is comprised of VPT and the operations of the GTC.

VPT develops, designs, manufactures, sells and services products and systems for delivering proton therapy, another form of external beam radiotherapy using proton beams, for the treatment of cancer. Our current focus is bringing our expertise in traditional radiation therapy to proton therapy to improve its clinical utility and to reduce its cost of treatment per patient, so that it is more widely accepted and deployed. Orders and revenues for our VPT products have been and may continue to be subject to significant variability due to the size of each individual transaction, and the timing of each transaction may be impacted by numerous factors, including items outside of our control such as customer project financing.

GTC, our scientific research facility, develops technologies that enhance our current businesses or may lead to new business areas, including technology to improve radiation therapy and X-ray imaging, as well as other technology for a variety of applications, including security and cargo screening. GTC is also actively engaged in searching for chemical or biological agents that work synergistically with radiation to improve treatment outcomes.

In the second quarter of fiscal year 2016, the "Other" category revenues increased $16.5 million and gross orders decreased $41.3 million compared to the year-ago period.

This discussion and analysis of our financial condition and results of operations is based upon and should be read in conjunction with the Condensed Consolidated Financial Statements and the Notes included elsewhere in this Quarterly Report on Form 10-Q and the Consolidated Financial Statements and the Notes to the Consolidated Financial Statements and the related Management’s Discussion and Analysis of Financial Condition and Results of Operations in our Annual Report on Form 10-K for the fiscal year ended October 2, 2015 (the “2015 Annual Report”), as well as the Risk Factors contained in Part II, Item 1A of this Quarterly Report on Form 10-Q, and other information provided from time to time in our other filings with the SEC.

Critical Accounting Estimates

The preparation of our financial statements and related disclosures in conformity with accounting principles generally accepted in the United States (“GAAP”) requires us to make estimates and assumptions that affect the reported amounts of assets, liabilities, revenues and expenses. These estimates and assumptions are based on historical experience and on various other factors that we believe are reasonable under the circumstances. We periodically review our accounting policies, estimates and assumptions and make adjustments when facts and circumstances dictate. In addition to the accounting policies that are more fully described in the Notes to the Consolidated Financial Statements included in our 2015 Annual Report on Form 10-K, we consider the critical accounting policies described below to be affected by critical accounting estimates. Our critical accounting policies that are affected by accounting estimates include revenue recognition, share-based compensation expense, valuation of allowance for doubtful accounts, impairment of investments and notes receivable, valuation of inventories, assessment of recoverability of goodwill and intangible assets, valuation of warranty obligations, assessment of loss contingencies, valuation of defined benefit pension and post-retirement benefit plans, valuation of derivative instruments, and taxes on earnings. Such accounting policies require us to use judgments, often as a result of the need to make estimates and assumptions regarding matters that are inherently uncertain, and actual results could differ materially from these estimates. For a discussion of how

these estimates and other factors may affect our business, see Part II, Item 1A, “Risk Factors.”

Revenue Recognition

Our revenues are derived primarily from the sale of hardware and software products, and services from our Oncology Systems, Imaging Components and VPT businesses. We recognize revenues net of any value added or sales tax and net of sales discounts.

We frequently enter into sales arrangements with customers that contain multiple elements or deliverables such as hardware, software and services. Judgments as to the allocation of consideration from an arrangement to the multiple elements of the arrangement, and the appropriate timing of revenue recognition are critical with respect to these arrangements to ensure compliance with GAAP.

The allocation of consideration in a multiple element arrangement is affected by the determination of whether any software deliverables that function together with other hardware components to deliver the hardware products' essential functionality are considered as non-software products for purpose of revenue recognition. The allocation of consideration to each non-software deliverable is based on the assumptions we use to establish its selling price, which are based on vendor-specific objective evidence ("VSOE") of selling price, if it exists, otherwise, third-party evidence of selling price, if it exists, and, if not, on estimated selling prices. In addition, the allocation of consideration to each software deliverable in a multiple element arrangement is affected by our judgment as to whether VSOE of its fair value exists in these arrangements.

Changes to the elements in an arrangement and the amounts allocated to each element could affect the timing and amount of revenue recognition. Revenue recognition also depends on the timing of shipment, readiness of customers' facilities for installation, installation requirements, availability of products or customer acceptance terms. If shipments or installations are not made on scheduled timelines or if the products are not accepted by the customer in a timely manner, our reported revenues may differ materially from expectations.

Service revenues include revenues from hardware service contracts, software service agreements, bundled support arrangements, paid services and trainings, and parts that are sold by the service department. Revenues allocated to service contracts are generally recognized ratably over the period of the related contracts.

In addition, revenues related to proton therapy systems and proton therapy system commissioning contracts are recognized in accordance with contract accounting. We recognize contract revenues under the percentage-of-completion method which are based on contract costs incurred to date compared with total estimated contract costs. Changes in estimates of total contract revenue, total contract cost or the extent of progress towards completion are recognized in the period in which the changes in estimates are identified. Estimated losses on contracts are recognized in the period in which the loss is identified. In circumstances in which the final outcome of a contract cannot be precisely estimated but a loss on the contract is not expected, we recognize revenues under the percentage-of-completion method based on a zero profit margin until more precise estimates can be made. If and when we can make more precise estimates, revenues and costs of revenues are adjusted in the same period. Because the percentage-of-completion method involves considerable use of estimates in determining revenues, costs and profits and in assigning the dollar amounts to relevant accounting periods, and because the estimates must be periodically reviewed and appropriately adjusted, if our estimates prove to be inaccurate or circumstances change over time, we may be forced to adjust revenues or even record a contract loss in later periods.

Share-based Compensation Expense

We grant restricted stock units, deferred stock units, performance units, and stock options to employees and permit employees to purchase shares under the VMS employee stock purchase plan. We value our stock options granted and the option component of the shares of VMS common stock purchased under the employee stock purchase plan using the Black-Scholes option-pricing model. We value our performance units using the Monte Carlo simulation model. The determination of fair value of share-based payment awards on the date of grant under both the Black-Scholes option-pricing model and the Monte Carlo simulation model is affected by VMS's stock price, as well as the input of other subjective assumptions, including the expected terms of share-based awards and the expected price volatilities of shares of VMS common stock and peer companies that are used to assess certain performance targets over the expected term of the awards, and the expected dividend yield of shares of VMS common stock.

The expected term of our stock options is based on the observed and expected time to post-vesting exercise and post-vesting cancellations of stock options by our employees. We use a blended volatility in deriving the expected

volatility assumption for our stock options. Blended volatility represents the weighted average of implied volatility and historical volatility. Implied volatility is derived based on traded options on VMS common stock. Implied volatility is weighted in the calculation of blended volatility based on the ratio of the term of the exchange-traded options to the expected terms of the employee stock options.

Historical volatility represents the remainder of the weighting. Our decision to incorporate implied volatility was based on our assessment that implied volatility of publicly traded options on VMS common stock is reflective of market conditions and is generally reflective of both historical volatility and expectations of how future volatility will differ from historical volatility. In determining the extent of use of implied volatility, we considered: (i) the volume of market activity of traded options; (ii) the ability to reasonably match the input variables of traded options to those of stock options granted by us, including the date of grant; (iii) the similarity of the exercise prices; and (iv) the length of term of traded options. After considering the above factors, we determined that we could not rely exclusively on implied volatility based on the fact that the term of VMS exchange-traded options is less than one year and that it is different from the expected terms of the stock options we grant. Therefore, we believe a combination of the historical volatility over the expected terms of the stock options we grant and the implied volatility of exchange-traded options best reflects the expected volatility of VMS common stock. In determining the grant date fair value of our performance units, historical volatilities of shares of VMS common stock, as well as the shares of common stock of peer companies, were used to assess certain performance targets. The risk-free interest rate assumption is based upon observed interest rates appropriate for the term of our stock awards. The dividend yield assumption is based on our history and expectation of no dividend payouts. If factors change and we employ different assumptions in future periods, the compensation expense that we record may differ significantly from what we have recorded in the current period. In addition, we are required to estimate the expected forfeiture rate, as well as the probability that certain performance conditions that affect the vesting of performance units will be achieved, and recognize expense only for those awards expected to vest. If the actual forfeiture rate and/or the actual number of performance units that vest based on achievement of performance conditions are materially different from our estimates, the share-based compensation expense could be significantly different from what we have recorded in the current period.

Allowance for Doubtful Accounts

We evaluate the creditworthiness of our customers prior to authorizing shipment for all major sale transactions. Except for government tenders, group purchases and orders with letters of credit in Oncology Systems and for security and inspection products, our payment terms usually require payment of a small portion of the total amount due when the customer signs the purchase order, a significant amount upon transfer of risk of loss to the customer and the remaining amount upon completion of the installation. On a quarterly basis, we evaluate aged items in the accounts receivable aging report and provide an allowance in an amount we deem adequate for doubtful accounts. If our evaluation of our customers' financial conditions does not reflect our future ability to collect outstanding receivables, additional provisions may be needed and our operating results could be negatively affected.

Impairment of Investments and Notes Receivable

We recognize an impairment charge when the declines in the fair values of our available-for-sale investments below their cost basis are determined to be other than temporary impairments ("OTTI"). Our available-for-sale investments primarily include California Proton Treatment Center, LLC ("CPTC") loans. We monitor our available-for-sale investments for possible OTTI on an ongoing basis. When there has been a decline in fair value of a debt security below the amortized cost basis, we recognize OTTI if: (i) we have the intent to sell the security; (ii) it is more likely than not that we will be required to sell the security before recovery of the entire amortized cost basis; or (iii) we do not expect to recover the entire amortized cost basis of the security. We assess the fair value of the CPTC loans, which is classified in the level 3 fair value hierarchy based on the income approach by using the discounted cash flow model with key assumptions that include discount rates corresponding to the terms and risks associated with the loans to CPTC (see Note 3, "Fair Value" of the Notes to the Condensed Consolidated Financial Statements).

We also have investments in privately-held companies, some of which are in the startup or development stages. We monitor these investments for events or circumstances indicative of potential impairment, and we make appropriate reductions in carrying values if we determine that an impairment charge is required, based primarily on the financial condition, near-term prospects and recent financing activities of the investee. These investments are inherently risky because the markets for the technologies or products these companies are developing are typically in the early stages and may never materialize.

At times, we advance notes to third parties, including our customers. We assess these notes for collectibility and regularly review them for impairment by considering internal factors such as historical experience, credit quality, age of the note balances as well as external factors such as economic conditions that may affect the note holder's ability to pay.

Our ongoing consideration of all the factors described above could result in impairment charges in the future, which could adversely affect our operating results.

Inventories

Our inventories include high technology parts and components that are highly specialized in nature and that are subject to rapid technological obsolescence. We have programs to minimize the required inventories on hand and we regularly review inventory quantities on hand and on order and adjust for excess and obsolete inventory based primarily on historical usage rates and our estimates of product demand and production. Actual demand may differ from our estimates, in which case we may have understated or overstated the provision required for obsolete and excess inventory, which would have an impact on our operating results.

Goodwill and Intangible Assets

Goodwill is initially recorded when the purchase price paid for a business acquisition exceeds the estimated fair value of the net identified tangible and intangible assets acquired. Our future operating performance will be impacted by the future amortization of these acquired intangible assets and potential impairment charges related to these intangibles or to goodwill if indicators of impairment exist. The allocation of the purchase price from business acquisitions to goodwill and intangible assets could have a significant impact on our future operating results. In addition, the allocation of the purchase price of the acquired businesses to goodwill and intangible assets requires us to make significant estimates and assumptions, including estimates of future cash flows expected to be generated by the acquired assets and the appropriate discount rate for those cash flows. Should conditions differ from management's estimates at the time of the acquisition, material write-downs of intangible assets and/or goodwill may be required, which would adversely affect our operating results.

We evaluate goodwill for impairment at least annually or whenever an event occurs or circumstances change that would more likely than not reduce the fair value of a reporting unit below its carrying amount. The evaluation includes consideration of qualitative factors including industry and market considerations, overall financial performance, and other relevant events and factors affecting the reporting unit. If we determine that a quantitative analysis is necessary, the impairment test for goodwill is a two-step process. Step one consists of a comparison of the fair value of a reporting unit against its carrying amount, including the goodwill allocated to each reporting unit. We determine the fair value of our reporting units based on a combination of income and market approaches. The income approach is based on the present value of estimated future cash flows of the reporting units and the market approach is based on a market multiple calculated for each business unit based on market data of other companies engaged in similar business. If the carrying amount of the reporting unit is in excess of its fair value, step two requires the comparison of the implied fair value of the reporting unit's goodwill against the carrying amount of the reporting unit's goodwill. Any excess of the carrying value of the reporting unit's goodwill over the implied fair value of the reporting unit's goodwill is recorded as an impairment loss. The impairment test for intangible assets with indefinite useful lives, if any, consists of a comparison of fair value to carrying value, with any excess of carrying value over fair value being recorded as an impairment loss.

We have four reporting units with goodwill: (i) Oncology Systems, (ii) X-ray tubes and flat panel products, (iii) Security and inspection products, and (iv) VPT. For all four reporting units, based upon the most recent annual goodwill analysis that we performed as of the end of the third quarter of fiscal year 2015, either step one of the impairment test was not completed based on evaluation of qualitative factors or, for those which step one was completed, the fair value was substantially in excess of carrying value. However, significant changes in our projections about our operating results or other factors could cause us to make interim assessments of impairments in any quarter that could result in some or all of the goodwill being impaired. For our VPT reporting unit in particular, which had $50.4 million in goodwill as of April 1, 2016, our estimates as to future operating results include certain assumptions about factors that cannot be predicted with certainty, including future market conditions, revenue growth rates, and operating margins.

We will continue to make assessments of impairment on an annual basis or more frequently if indicators of potential impairment arise.

Warranty Obligations

We warrant most of our products for a specific period of time, usually 12 months from installation, against material defects. We provide for the estimated future costs of warranty obligations in cost of revenues when the related revenues are recognized. The accrued warranty costs represent our best estimate at the time of sale of the total costs

that we will incur to repair or replace product parts that fail while still under warranty. The amount of accrued estimated warranty costs obligation for established products is primarily based on historical experience as to product failures adjusted for current information on repair costs. For new products, estimates will include historical experience of similar products, as well as reasonable allowance for start-up expenses. Actual warranty costs could differ from the estimated amounts. On a quarterly basis, we review the accrued balances

of our warranty obligations and update the historical warranty cost trends, if required. If we were required to accrue additional warranty costs in the future, it would have a negative effect on our operating results.

Loss Contingencies

From time to time, we are a party to or otherwise involved in legal proceedings, claims and government inspections or investigations or other legal matters, both inside and outside the United States, arising in the ordinary course of our business or otherwise. We accrue amounts, to the extent they can be reasonably estimated, that we believe are adequate to address any liabilities related to legal proceedings and other loss contingencies that we believe will result in a probable loss. Such matters are subject to many uncertainties, outcomes are not predictable with assurance, and actual liabilities could significantly exceed our estimates of potential liabilities. In addition, we are subject to a variety of environmental laws around the world. Those laws regulate multiple aspects of our operations, including the handling, storage, transport and disposal of hazardous substances. They impose costs on our operations. In connection with our past and present operations and facilities, we record environmental remediation liabilities when we conclude that environmental assessments or remediation efforts are probable and we believe we can reasonably estimate the costs of those efforts. Our accrued environmental costs represent our best estimate of the total costs of assessments and remediation and the time period over which we expect to incur those costs. We review these accrued balances quarterly. If we were required to increase or decrease the accrued environmental costs in the future, it would adversely or favorably impact our operating results.

Defined Benefit Pension and Post-Retirement Benefit Plans

We sponsor seven defined benefit pension plans in Germany (where we have three defined benefit pension plans), Japan, Switzerland, the Philippines and the United Kingdom covering employees who meet the applicable eligibility requirements in these countries. Several statistical and other factors that attempt to anticipate future events are used in calculating the expenses and liabilities related to the aforementioned plans. These factors include assumptions about the discount rate, expected return on plan assets, and rate of future compensation increases, all of which we determine within certain guidelines. In addition, we also use assumptions, such as withdrawal and mortality rates, to calculate the expenses and liabilities. The actuarial assumptions we use are long-term assumptions and may differ materially from actual experience particularly in the short term due to changing market and economic conditions and changing participant demographics. These differences may have a significant impact on the amount of defined benefit pension plan expenses we record.

The expected rates of return on the various defined benefit pension plans' assets are based on the asset allocation of each plan and the long-term projected return on those assets. The discount rate enables us to state expected future cash flows at a present value on the measurement date. The discount rates used for defined benefit plans are primarily based on the current effective yield of long-term corporate bonds that are of high quality with satisfactory liquidity and credit rating with durations corresponding to the expected durations of the benefit obligations. A change in the discount rate may cause the present value of benefit obligations to change significantly.

Valuation of Derivative Instruments

We use foreign currency forward contracts to reduce the effects of currency rate fluctuations on sales transactions denominated in foreign currencies and on assets and liabilities denominated in foreign currencies. These foreign currency forward contracts are derivative instruments and are measured at fair value. There are three levels of inputs that may be used to measure fair value (see Note 3, "Fair Value" of the Notes to the Condensed Consolidated Financial Statements). The fair value of foreign currency forward contracts are calculated primarily using Level 2 inputs, which include currency spot and forward rates, interest rate and credit or non-performance risk. The spot rate for each currency is the same spot rate used for all balance sheet translations at the measurement date and sourced from our major trading banks. The forward point values for each currency and the London Interbank Offered Rate ("LIBOR") to discount assets and liabilities are interpolated from commonly quoted broker services. One year credit default swap spreads of the counterparty at the measurement date are used to adjust derivative assets, all of which mature in 13 months or less, for non-performance risk. We are required to adjust derivative liabilities to reflect the potential non-performance risk to lenders based on our incremental borrowing rate. Each contract is individually adjusted using the counterparty credit default swap rates (for net assets) or our borrowing rate (for net liabilities). The use of Level 2 inputs in determining fair values requires certain management judgment and subjectivity. Changes to

these Level 2 inputs could have a material impact on the valuation of our derivative instruments, as well as on our result of operations. There were no transfers of assets or liabilities between fair value measurement levels during the first half of fiscal years 2016 and 2015.

Taxes on Earnings

We are subject to taxes on earnings in both the United States and numerous foreign jurisdictions. As a global taxpayer, significant judgments and estimates are required in evaluating our tax positions and determining our provision for taxes on earnings. The accounting for uncertainty in income taxes requires a two-step approach to recognizing, derecognizing and measuring uncertain tax positions. The first step is to evaluate the tax position for recognition by determining whether the weight of available evidence indicates that it is more likely than not that, based on the technical merits, the position will be sustained on audit, including resolution of related appeals or litigation processes, if any. The second step is to measure the tax benefit as the largest amount that is more than 50% likely of being realized upon settlement. Recognition, derecognition and measurement are based on management's best judgment given the facts, circumstances and information available at the end of the accounting period. A tax benefit should be recognized in the first period in which it meets the more likely than not recognition threshold, and conversely, a tax benefit previously recognized should be derecognized in the first period in which new information results in a change in judgment in which the position fails to meet the recognition threshold. A benefit not previously recognized would be recognized when the tax position is effectively settled through examination, negotiation or litigation with tax authorities, or when the statute of limitations for the relevant taxing authority to examine and challenge the position has expired. Our policy is to include interest and penalties related to unrecognized tax benefits within the provision for taxes on earnings.

Generally, the carrying value of our net deferred tax assets assumes that we will be able to generate sufficient future taxable earnings in the applicable tax jurisdictions to utilize these deferred tax assets. Should we conclude it is more likely than not that we will be unable to recover our net deferred tax assets in these tax jurisdictions, we would increase our valuation allowance and our tax provision would increase in the period in which we make such a determination.

Our foreign earnings are generally taxed at rates lower than U.S. rates. Our effective tax rate is impacted by existing tax laws in both the United States and in the respective countries in which our foreign subsidiaries do business. In addition, a decrease in the percentage of our total earnings from our foreign countries, or a change in the mix of foreign countries among particular tax jurisdictions could increase or decrease our effective tax rate. Our current effective tax rate does not assume U.S. taxes on certain undistributed profits of certain foreign subsidiaries. These earnings could become subject to incremental foreign withholding or U.S. federal and state taxes should they either be deemed or actually remitted to the United States.

Results of Operations

Fiscal Year

Our fiscal year is the 52- or 53-week period ending on the Friday nearest September 30. Fiscal year 2016 is the 52-week period ending September 30, 2016, and fiscal year 2015 was the 53-week period ended October 2, 2015. The fiscal quarters ended April 1, 2016 and April 3, 2015 were both 13-week periods.

Discussion of Results of Operations for the Second Quarter and First Half of Fiscal Year 2016 Compared to the Second Quarter and First Half of Fiscal Year 2015

Total Revenues

Revenues by sales classification (Dollars in millions)	Three Months Ended			Six Months Ended		
	April 1, 2016	April 3, 2015	Percent Change	April 1, 2016	April 3, 2015	Percent Change
Product	$495.6	$513.8	(4)%	$996.1	$989.6	1 %
Service	263.2	245.6	7 %	519.8	507.7	2 %
Total Revenues	$758.8	$759.4	— %	$1,515.9	$1,497.3	1 %
Product as a percentage of total revenues	65 %	68 %		66 %	66 %	
Service as a percentage of total revenues	35 %	32 %		34 %	34 %	

Total revenues decreased slightly in the second quarter of fiscal year 2016, compared to the year-ago period, due to decreases in revenues from Imaging Components and Oncology Systems, mostly offset by an increase in revenues from the "Other" category. Total revenues increased in the first half of fiscal year 2016, compared to the year-ago

period, due to increases in revenues from the "Other" category and Oncology Systems, partially offset by a decrease in revenues from Imaging Components.

Product revenues decreased in the second quarter of fiscal year 2016, compared to the year-ago period, due to decreases in revenues from Oncology Systems and Imaging Components, partially offset by an increase in revenues from the "Other" category. Product revenues increased in the first half of fiscal year 2016, compared to the year-ago period, due to increases in revenues from the "Other" category and Oncology Systems, partially offset by a decrease in revenues from Imaging Components.

Service revenues increased in the second quarter of fiscal year 2016, compared to the year-ago period, primarily due to an increase in revenues from Oncology Systems. Service revenues increased in the first half of fiscal year 2016, compared to the year-ago period, primarily due to increases in revenues from Imaging Components and Oncology Systems.

Revenues by region	Three Months Ended				Six Months Ended			
(Dollars in millions)	April 1, 2016	April 3, 2015	Percent Change	Constant Currency (1)	April 1, 2016	April 3, 2015	Percent Change	Constant Currency (1)
Americas	$366.6	$377.3	(3)%	(2)%	$715.1	$748.0	(4)%	(4)%
EMEA	212.8	207.7	2 %	7 %	482.9	416.9	16 %	23 %
APAC	179.4	174.4	3 %	4 %	317.9	332.4	(4)%	(2)%
Total Revenues	$758.8	$759.4	— %	2 %	$1,515.9	$1,497.3	1 %	4 %
North America	$348.2	$357.4	(3)%	(2)%	$672.8	$712.7	(6)%	(5)%
International [2]	410.6	402.0	2 %	5 %	843.1	784.6	7 %	13 %
Total Revenues	$758.8	$759.4	— %	2 %	$1,515.9	$1,497.3	1 %	4 %
North America as a percentage of total revenues	46 %	47 %			44 %	48 %		
International as a percentage of total revenues	54 %	53 %			56 %	52 %		

(1) Constant currency is the percent change excluding the effect of foreign currency fluctuations against the U.S. Dollar.

(2) We consider international revenues to be revenues outside of North America.

The Americas revenues decreased in the second quarter and the first half of fiscal year 2016, compared to the year-ago periods, due to decreases in revenues from Oncology Systems and Imaging Components, partially offset by an increase in revenues from the "Other" category.

EMEA revenues increased in the second quarter of fiscal year 2016, compared to the year-ago period, due to increases in revenues from the "Other" category and Imaging Components, partially offset by a decrease in revenues from Oncology Systems. EMEA revenues increased in the first half of fiscal year 2016, compared to the year-ago period, due to increases in revenues from Oncology Systems, the "Other" category, and Imaging Components.

APAC revenues increased in the second quarter of fiscal year 2016, compared to the year-ago period, primarily due to an increase in revenues from Oncology Systems, partially offset by a decrease in revenues from Imaging Components. APAC revenues decreased in the first half of fiscal year 2016, compared to the year-ago period, primarily due to a decrease in revenues from Imaging Components, partially offset by an increase in revenues from Oncology Systems.

Oncology Systems Revenues

Revenues by sales classification (Dollars in millions)	Three Months Ended				Six Months Ended			
	April 1, 2016	April 3, 2015	Percent Change	Constant Currency	April 1, 2016	April 3, 2015	Percent Change	Constant Currency
Product	$332.5	$351.1	(5)%	(3)%	$675.5	$659.9	2 %	5 %
Service	251.6	238.3	6 %	8 %	497.9	492.8	1 %	5 %
Total Oncology Systems Revenues	$584.1	$589.4	(1)%	1 %	$1,173.4	$1,152.7	2 %	5 %
Product as a percentage of total Oncology Systems revenues	57 %	60 %			58 %	57 %		
Service as a percentage of total Oncology Systems revenues	43 %	40 %			42 %	43 %		
Oncology Systems revenues as a percentage of total revenues	77 %	78 %			77 %	77 %		

Oncology Systems product revenues decreased in the second quarter of fiscal year 2016, compared to the year-ago period, due to a decrease from hardware products, partially offset by an increase from software licenses. Oncology Systems product revenues increased in the first half of fiscal year 2016, compared to the year-ago period, due to increases from hardware products and software licenses.

Oncology Systems service revenues increased in the second quarter and first half of fiscal year 2016, compared to the year-ago periods, primarily due to increased customer adoption of service contracts as the warranty period on our TrueBeam systems expire and an increase in the number of customers as the installed base of our products continues to grow. In addition, the first half of fiscal year 2015 benefited from an extra week of operations.

The overall fluctuations in currency exchange rates had a negative impact on the revenues of Oncology Systems during the second quarter and first half of fiscal year 2016, as compared to the year-ago periods.

Revenues by region (Dollars in millions)	Three Months Ended				Six Months Ended			
	April 1, 2016	April 3, 2015	Percent Change	Constant Currency	April 1, 2016	April 3, 2015	Percent Change	Constant Currency
Americas	$305.9	$313.9	(3)%	(2)%	$590.2	$622.3	(5)%	(5)%
EMEA	151.6	161.7	(6)%	(1)%	364.2	329.5	11 %	18 %
APAC	126.6	113.8	11 %	13 %	219.0	200.9	9 %	13 %
Total Oncology Systems Revenues	$584.1	$589.4	(1)%	1 %	$1,173.4	$1,152.7	2 %	5 %
North America	$288.9	$296.0	(2)%	(2)%	$552.7	$591.1	(6)%	(6)%
International	295.2	293.4	1 %	4 %	620.7	561.6	11 %	17 %
Total Oncology Systems Revenues	$584.1	$589.4	(1)%	1 %	$1,173.4	$1,152.7	2 %	5 %
North America as a percentage of total Oncology Systems revenues	49 %	50 %			47 %	51 %		
International as a percentage of total Oncology Systems revenues	51 %	50 %			53 %	49 %		

The Americas Oncology Systems revenues decreased in the second quarter and first half of fiscal year 2016, compared to the year-ago periods, due to a decrease in revenues from North American hardware products, partially offset by an increase in service revenues.

EMEA Oncology Systems revenues decreased in the second quarter of fiscal year 2016, compared to the year-ago period, primarily due to a decrease in revenues from hardware products. EMEA Oncology Systems revenues increased in the first half of fiscal year 2016, compared to the year-ago period, primarily due to an increase in product revenues resulting from an increase in volume from hardware products and the timing of shipments.

APAC Oncology Systems revenues increased in the second quarter and first half of fiscal year 2016, compared to the year-ago periods, due to an increase in revenues from hardware products and software licenses.

Varying cycles of higher and lower revenues between the North American and international regions are impacted by regional influences, which recently have included government programs, economic and political instability in some countries, uncertainty created by health care reform (such as the excise tax on the sale of most medical devices, Medicare reimbursement rates and consolidation of free standing clinics in the United States), and different technology adoption cycles that are consistent with the gross order patterns. See further discussion of orders under "Gross Orders."

Imaging Components Revenues

Revenues by sales classification (Dollars in millions)	Three Months Ended			Six Months Ended		
	April 1, 2016	April 3, 2015	Percent Change	April 1, 2016	April 3, 2015	Percent Change
Product	$134.4	$150.0	(10)%	$267.6	$309.8	(14)%
Service	9.3	5.5	71 %	17.5	11.7	51 %
Total Imaging Components Revenues	$143.7	$155.5	(8)%	$285.1	$321.5	(11)%
Product as a percentage of total Imaging Components revenues	94 %	96 %		94 %	96 %	
Service as a percentage of total Imaging Components revenues	6 %	4 %		6 %	4 %	
Imaging Components revenues as a percentage of total revenues	19 %	20 %		19 %	21 %	

Imaging Components product revenues decreased in the second quarter and first half of fiscal year 2016, compared to the year-ago periods, due to a decrease in revenues from X-ray flat panel and tube products, and to a lesser extent, a decrease in revenues from security and inspection products, partially offset by product revenues from acquisitions completed in the second half of fiscal year 2015. The decreases in revenues from X-ray flat panel and tube products were primarily due to pricing pressures resulting from the strengthening of the U.S. Dollar, customers migrating to lower cost alternatives, and the decision of a customer to in-source some of its X-ray flat panel products in the second half of fiscal year 2015. In addition, lower purchases from a key customer with higher X-ray tube inventory, due in part to longer tube life, also contributed to the declines in revenues. The decrease in revenues from security and inspection products was due to pricing pressures and delays in tenders in which our customers participate.

Imaging Components service revenues increased in the second quarter and first half of fiscal year 2016, compared to the year-ago periods, primarily due to service revenues from acquisitions completed in the second half of fiscal year 2015.

Because sales transactions in Imaging Components are generally denominated in U.S. Dollars, fluctuations in currency exchange rates did not have a material direct impact on Imaging Components international revenues. However, demand from X-ray tube and flat panel products and, consequently revenues, were negatively impacted by pricing pressures resulting from the strengthening of the U.S. Dollar against certain foreign currencies in the first half of fiscal year 2016, compared to the year-ago period, which made our products relatively more expensive as compared to non-U.S. manufacturers and to customers outside the U.S.

Revenues by region (Dollars in millions)	Three Months Ended			Six Months Ended		
	April 1, 2016	April 3, 2015	Percent Change	April 1, 2016	April 3, 2015	Percent Change
Americas	$46.1	$56.0	(18)%	$99.3	$114.2	(13)%
EMEA	45.0	38.9	16 %	87.0	75.9	15 %
APAC	52.6	60.6	(13)%	98.8	131.4	(25)%
Total Imaging Components Revenues	$143.7	$155.5	(8)%	$285.1	$321.5	(11)%
North America	$44.6	$54.1	(17)%	$94.4	$110.1	(14)%
International	99.1	101.4	(2)%	190.7	211.4	(10)%
Total Imaging Components Revenues	$143.7	$155.5	(8)%	$285.1	$321.5	(11)%
North America as a percentage of total Imaging Components revenues	31 %	35 %		33 %	34 %	
International as a percentage of total Imaging Components revenues	69 %	65 %		67 %	66 %	

The Americas Imaging Components revenues decreased in the second quarter and first half of fiscal year 2016, compared to the year-ago periods, primarily due to a decrease in revenues from X-ray flat panel products, partially offset by revenues from acquisitions completed in the second half of fiscal year 2015. The decrease in revenues from X-ray flat panel products in the second quarter and first half of fiscal year 2016, compared to the year-ago periods, was primarily due to a decision of a customer to in-source some of its X-ray flat panel products in the second half of fiscal year 2015.

EMEA Imaging Components revenues increased in the second quarter and first half of fiscal year 2016, compared to the year-ago periods, primarily due to revenues from acquisitions completed in the second half of fiscal year 2015.

APAC Imaging Components revenues decreased in the second quarter of fiscal year 2016, compared to the year-ago period, primarily due to a decrease in revenues from X-ray tube products. APAC Imaging Components revenues decreased in the first half of fiscal year 2016, compared to the year-ago period, primarily due to a decrease in revenues from X-ray tubes and flat panel products. The decrease in revenues from X-ray flat panel products, and to a lesser extent X-ray tube products, was due to pricing pressures resulting from the strengthening of the U.S. Dollar. In addition, lower purchases from a key customer with higher X-ray tube inventory, due in part to longer tube life, primarily contributed to the declines in revenues from X-ray tube products. The decrease in revenues from the APAC region in the second quarter and first half of fiscal year 2016, compared to the year-ago periods, was partially offset by revenues from acquisitions completed in the second half of fiscal year 2015.

Other Revenues

Revenues by sales classification (Dollars in millions)	Three Months Ended			Six Months Ended		
	April 1, 2016	April 3, 2015	Percent Change	April 1, 2016	April 3, 2015	Percent Change
Product	$28.7	$12.7	126 %	$53.0	$19.9	167 %
Service	2.3	1.8	29 %	4.4	3.2	37 %
Total Other Revenues	$31.0	$14.5	114 %	$57.4	$23.1	148 %
Other revenues as a percentage of total revenues	4 %	2 %		4 %	2 %	

Revenues in our “Other” category increased in the second quarter and first half of fiscal year 2016, compared to the year-ago periods, primarily due to an increase in VPT product revenues, resulting from continued production and installation of VPT projects that are in our backlog.

Gross Margin

Dollars by segment (Dollars in millions)	Three Months Ended			Six Months Ended		
	April 1, 2016	April 3, 2015	Percent Change	April 1, 2016	April 3, 2015	Percent Change
Oncology Systems	$254.2	$253.4	— %	$502.8	$510.1	(1)%
Imaging Components	59.1	67.9	(13)%	116.2	137.9	(16)%
Other	3.9	1.2	215 %	7.9	1.5	413 %
Gross margin	$317.2	$322.5	(2)%	$626.9	$649.5	(3)%
Percentage by segment						
Oncology Systems	43.5 %	43.0 %		42.9 %	44.3 %	
Imaging Components	41.1 %	43.7 %		40.8 %	42.9 %	
Total Company	41.8 %	42.5 %		41.4 %	43.4 %	

Total gross margin percentage decreased in the second quarter and first half of fiscal year 2016, compared to the year-ago period, primarily due to a decrease in revenues and gross margin percentage from Imaging Components, and an increase in revenues in the "Other" category, which has a lower gross margin percentage. Total product gross margin percentage was 33.2% and 32.3% in the second quarter and first half of fiscal year 2016, compared to 35.7% for both of the respective year-ago periods. Total service gross margin percentage was 58.0% and 58.7% in the second quarter and first half of fiscal year 2016, compared to 56.7% and 58.4% for the respective year-ago periods.

Oncology Systems product gross margin percentage was 33.2% and 31.5% in the second quarter and first half of fiscal year 2016, compared to 33.7% for both of the respective year-ago periods. The decrease in Oncology Systems product gross margin percentage in the first half of fiscal year 2016, compared to the year-ago period was primarily due to a shift to geographies which generally have lower margins and an unfavorable foreign currency impact, partially offset by the suspension of the medical device excise tax in fiscal year 2016 and an increase in software license revenues which has a higher gross margin percentage.

Oncology Systems service gross margin percentage was 57.2% and 58.2% in the second quarter and first half of fiscal year 2016, compared to 56.6% and 58.4% in the respective year-ago periods. The increase in service gross margin percentage in the second quarter of fiscal year 2016 was due to cost control measures.

Imaging Components gross margin percentage decreased in the second quarter and first half of fiscal year 2016, compared to the respective year-ago periods, primarily due to a decrease from X-ray tube and flat panel products, partially offset by an increase from acquisitions completed in the second half of fiscal year 2015. The decrease in gross margin percentage from X-ray tube and flat panel products in the second quarter and first half of fiscal year 2016, compared to the year-ago periods, was primarily due to increased pricing pressures resulting from the strengthening of the U.S. Dollar, higher material costs and lower volumes in X-ray tube products, partially offset by a favorable mix in X-ray flat panel products in the first half of fiscal year 2016.

Research and Development

(Dollars in millions)	Three Months Ended			Six Months Ended		
	April 1, 2016	April 3, 2015	Percent Change	April 1, 2016	April 3, 2015	Percent Change
Research and development	$62.1	$59.3	5 %	$122.1	$116.4	5 %
Research and development as a percentage of total revenues	8 %	8 %		8 %	8 %	

Research and development expenses increased $2.8 million in the second quarter of fiscal year 2016, compared to the year-ago period, primarily due to an increase in expenses of $2.8 million in Imaging Components, which was primarily attributable to research and development expenses related to acquisitions completed in the second half of fiscal year 2015.

43

Research and development expenses increased $5.7 million in the first half of fiscal year 2016, compared to the year-ago period, primarily due to an increase in expenses of $4.3 million in Imaging Components and $2.5 million in the "Other" category. The $4.3 million increase in Imaging Components was primarily due to research and development expenses related to acquisitions completed in the second half of fiscal year 2015, partially offset by a reduction in research and development expense for our X-ray tube and flat panel products. The $2.5 million increase in the "Other" category was primarily due to an increase in new development projects and employee-related costs in VPT, partially offset by a favorable currency impact when foreign-currency denominated research and development expenses were translated into U.S. Dollars.

Selling, General and Administrative

(Dollars in millions)	Three Months Ended			Six Months Ended		
	April 1, 2016	April 3, 2015	Percent Change	April 1, 2016	April 3, 2015	Percent Change
Selling, general and administrative	$121.1	$117.2	3 %	$254.2	$257.7	(1)%
Selling, general and administrative as a percentage of total revenues	16 %	15 %		17 %	17 %	

Selling, general and administrative expenses increased $3.9 million in the second quarter of fiscal year 2016, compared to the year-ago period, primarily due to a $6.1 million increase in legal expenses primarily relating to significant litigation matters, and a $3.2 million increase in expenses from acquisitions completed in the second half of fiscal year 2015. These increases were partially offset by an approximately $3 million in favorable currency impact when foreign-currency denominated expenses were translated into U.S. dollars, and a $3.1 million decrease in restructuring charges.

Selling, general and administrative expenses decreased $3.5 million in the first half of fiscal year 2016, compared to the year-ago period, primarily due to a $8.8 million decrease in restructuring charges, an approximately $7 million favorable currency impact when foreign-currency denominated expenses were translated into U.S. dollars, and a $3.0 million decrease in bad debt expense. The decreases were partially offset by a $8.2 million increase in legal expenses primarily relating to significant litigation matters, and a $6.6 million increase in expenses from acquisitions completed in the second half of fiscal year 2015.

Interest Income, Net

(Dollars in millions)	Three Months Ended			Six Months Ended		
	April 1, 2016	April 3, 2015	Percent Change	April 1, 2016	April 3, 2015	Percent Change
Interest income, net	$1.0	$ 1.0	(5)%	$2.7	$ 2.0	33 %

Interest income, net of interest expense, decreased slightly in the second quarter of fiscal year 2016, compared to the year-ago period, with higher interest expense associated with increased borrowings from our credit facility offset by higher interest income generated primarily from our loans to fund the development and construction of various proton therapy centers.

Interest income, net of interest expense, increased in the first half of fiscal year 2016, compared to the year-ago period, primarily due to higher interest income generated primarily from our loans to fund the development and construction of various proton therapy centers being partially offset by higher interest expense associated with increased borrowings from our credit facility.

Taxes on Earnings

	Three Months Ended			Six Months Ended		
	April 1, 2016	April 3, 2015	Percent Change	April 1, 2016	April 3, 2015	Percent Change
Effective tax rate	28.1%	28.0 %	0.1 %	26.6%	28.2 %	(1.6)%

Our effective tax rate decreased in the first half of fiscal year 2016, compared to the year ago period, primarily due to the geographic mix of earnings.

Our effective tax rate is impacted by the percentage of our total earnings that come from our international region, the mix of particular tax jurisdictions within our international region, changes in the valuation of our deferred tax assets or liabilities, and changes in tax laws or interpretations of those laws. We also expect that our effective tax rate may experience increased fluctuations from period to period. See Note 14, “Taxes on Earnings” of the Notes to the Consolidated Financial Statements in our 2015 Annual Report.

Diluted Net Earnings Per Share

	Three Months Ended			Six Months Ended		
	April 1, 2016	April 3, 2015	Percent Change	April 1, 2016	April 3, 2015	Percent Change
Diluted net earnings per share	$1.01	$ 1.05	(4)%	$1.92	$ 1.97	(3)%

Diluted net earnings per share decreased in the second quarter and first half of fiscal year 2016, compared to the year-ago periods, primarily due to a decrease in operating earnings, partially offset by a reduction in the number of diluted shares of common stock outstanding due to stock repurchases. The decrease in diluted net earnings per share in the first half of fiscal year 2016, compared to the year-ago period, was further offset by a decrease in the effective tax rate.

Gross Orders

Total Gross Orders (by segment)	Three Months Ended			Six Months Ended		
(Dollars in millions)	April 1, 2016	April 3, 2015	Percent Change	April 1, 2016	April 3, 2015	Percent Change
Oncology Systems	$617.8	$581.1	6 %	$1,150.4	$1,142.8	1 %
Imaging Components	137.9	156.3	(12)%	265.0	319.0	(17)%
Other	2.7	44.0	(94)%	15.0	45.4	(67)%
Total Gross Orders	$758.4	$781.4	(3)%	$1,430.4	$1,507.2	(5)%

Gross orders are defined as the sum of new orders recorded during the period adjusted for any revisions to existing orders during the period. New orders are recorded for the total contractual amount, excluding certain pass-through items, once a written agreement for the delivery of goods or provision of services is in place and, for businesses other than VPT, when shipment of the product is expected to occur within two years, so long as any contingencies are deemed perfunctory. However, we will not record security and inspection products orders from governmental agencies with bid protest provisions until the expiration of the bid protest period. For our VPT business, we record orders when construction of the related proton therapy treatment center is reasonably expected to start within two years, but only if any contingencies are either deemed perfunctory or if the existence and nature of material contingencies is disclosed. However, we will not record VPT orders if there are major financing contingencies, if a substantial portion of the financing for the project is not reasonably assured or if customer board approval contingencies are pending. We perform a quarterly review to verify that outstanding orders remain valid.

Gross orders in any period may not be directly correlated to the level of revenues in any particular future quarter or period since the timing of revenue recognition will vary significantly based on the delivery requirements of individual orders, acceptance schedules and the readiness of individual customer sites for installation of our products. Moreover, certain types of orders, such as orders for software or newly introduced products in our Oncology Systems segment, typically take more time from order to completion of installation and acceptance than hardware or older products. Gross orders and revenues for our security and inspection products in our Imaging Components segment have been and may continue to be unpredictable as governmental agencies may place large orders with us or with our OEM customers over a short period of time and then may not place any orders for a long time period thereafter. Because an order for a proton therapy system can be relatively large, an order in one fiscal period will cause gross orders in our VPT business to vary significantly, making comparisons between fiscal periods more difficult. Furthermore, bid awards, primarily in our VPT business, may be subject to challenge by third parties, which can make these orders more unpredictable than other products.

Oncology Systems Gross Orders

Gross Orders by region (Dollars in millions)	Three Months Ended				Six Months Ended			
	April 1, 2016	April 3, 2015	Percent Change	Constant Currency	April 1, 2016	April 3, 2015	Percent Change	Constant Currency
Americas	$331.5	$324.7	2 %	3 %	$614.2	$599.4	2 %	3 %
EMEA	174.3	147.0	19 %	23 %	329.2	326.6	1 %	8 %
APAC	112.0	109.4	2 %	3 %	207.0	216.8	(5)%	(2)%
Total Oncology Systems Gross Orders	$617.8	$581.1	6 %	8 %	$1,150.4	$1,142.8	1 %	3 %
North America	$313.0	$293.1	7 %	7 %	$569.4	$544.2	5 %	5 %
International	304.8	288.0	6 %	8 %	581.0	598.6	(3)%	2 %
Total Oncology Systems Gross Orders	$617.8	$581.1	6 %	8 %	$1,150.4	$1,142.8	1 %	3 %

The Americas Oncology Systems gross orders increased in the second quarter and first half of fiscal year 2016, compared to the year-ago periods, primarily due to increases in gross orders from services and hardware products in North America, partially offset by a decrease in gross orders from hardware products in Latin America.

EMEA Oncology Systems gross orders increased in the second quarter of fiscal year 2016, compared to the respective year-ago period, due to an increase in gross orders from hardware products, and to a lesser extent, increases in gross orders from services and software licenses. EMEA Oncology System gross orders increased in the first half of fiscal year 2016, compared to the year-ago period, primarily due to an increase in services, partially offset by a decrease in hardware products.

APAC Oncology Systems gross orders increased in the second quarter of fiscal year 2016, compared to the year-ago period, primarily due to an increase in gross orders from software licenses and services. APAC Oncology Systems gross orders decreased in the first half of fiscal year 2016, compared to the year-ago period, primarily due to a decrease from hardware products.

The trailing 12 months growth in gross orders for Oncology Systems at the end of the second quarter of fiscal year 2016 and at the end of each of the previous three fiscal quarters were:

	April 1, 2016	January 1, 2016	October 2, 2015	July 3, 2015
Americas	—%	2%	1%	8%
EMEA	4%	(5)%	—%	(3)%
APAC	(1)%	(5)%	—%	—%
North America	3%	4%	3%	6%
International	(1)%	(7)%	(2)%	1%
Total Oncology Systems Gross Orders	1%	(2)%	—%	3%

Consistent with the historical pattern, we expect that Oncology Systems gross orders will continue to experience regional fluctuations, with an overall shift of gross orders towards international regions and emerging markets. Oncology Systems gross orders are affected by foreign currency fluctuations. In addition, government programs that stimulate the purchase of healthcare products could affect the demand for our products from period to period, and could therefore make it difficult to compare our financial results.

Imaging Components Gross Orders

Gross Orders by region	Three Months Ended			Six Months Ended		
(Dollars in millions)	April 1, 2016	April 3, 2015	Percent Change	April 1, 2016	April 3, 2015	Percent Change
Americas	$36.5	$33.0	11 %	$79.6	$82.4	(3)%
EMEA	35.8	47.6	(25)%	78.8	81.0	(3)%
APAC	65.6	75.7	(13)%	106.6	155.6	(31)%
Total Imaging Components Gross Orders	$137.9	$156.3	(12)%	$265.0	$319.0	(17)%
North America	$35.3	$30.9	14 %	$76.9	$78.2	(2)%
International	102.6	125.4	(18)%	188.1	240.8	(22)%
Total Imaging Components Gross Orders	$137.9	$156.3	(12)%	$265.0	$319.0	(17)%

The Americas Imaging Components gross orders increased in the second quarter of fiscal year 2016, compared to the year-ago period, primarily due to gross orders from acquisitions completed in the second half fiscal year 2015, partially offset by a decrease in gross orders from X-ray flat panel products. The Americas Imaging Components gross orders decreased in the first half of fiscal year 2016, compared to the year-ago period, primarily due to a decrease in gross orders from X-ray flat panel products, partially offset by gross orders from acquisitions completed in the second half fiscal year 2015. The decrease in gross orders from X-ray flat panel products was primarily due to a decision of a customer to in-source some of their X-ray flat panel products in the second half of fiscal year 2015.

EMEA Imaging Components gross orders decreased in the second quarter and first half of fiscal year 2016, compared to the year-ago period, primarily due to a decrease in gross orders from X-ray flat panel products and to a lesser extent, a decrease in gross orders from security and inspection products, partially offset by gross orders from acquisitions completed in the second half of fiscal year 2015.

APAC Imaging Components gross orders decreased in the second quarter of fiscal year 2016, compared to the year-ago period, primarily due to a decrease in gross orders from X-ray flat panel products, partially offset by gross orders from X-ray tube products and gross orders from acquisitions completed in the second half of fiscal year 2015.

APAC Imaging Components gross orders decreased in the first half of fiscal year 2016, compared to the year-ago period, primarily due to a decrease in gross orders X-ray flat panel products, and to a lesser extent, a decrease from X-ray tubes products, partially offset by gross orders from acquisitions completed in the second half of fiscal year 2015. X-ray flat panel and tube products gross orders from the APAC region decreased in the first half of fiscal year 2016, compared to the year-ago period, primarily due to the timing of several large orders in X-ray flat panel products in the prior comparable period and higher X-ray tube inventory at a key customer, due in part to longer tube life.

The difference in currency exchange rates between the U.S. Dollar and foreign currencies in the second quarter and first half of fiscal year 2016, compared to the respective year-ago periods, did not have a material impact on Imaging Components international orders because orders in Imaging Components are generally denominated in U.S. Dollars. However, overall, gross orders from Imaging Components in the second quarter and first half of fiscal year 2016, compared to the respective year-ago periods, were impacted by the pricing pressures resulting from strengthening of the U.S. Dollar against certain foreign currencies which caused a decline in demand for X-ray tube and flat panel products from some customers in APAC and EMEA.

Other Gross Orders

The “Other” category gross orders decreased in the second quarter and first half of fiscal year 2016, compared to the year-ago period, due to the timing of gross orders in VPT.

Backlog

Backlog is the accumulation of all gross orders for which revenues have not been recognized and are still considered valid. Backlog also includes a small portion of billed service contracts that are included in deferred revenue. Backlog is stated at historical foreign currency exchange rates and revenue is released from backlog at current exchange rates, with any difference recorded as a backlog adjustment. Our backlog at April 1, 2016 was $3.3 billion, including approximately $296 million in VPT

47

backlog, which was an increase of 6% over the backlog at April 3, 2015. Our Oncology Systems backlog at April 1, 2016 was 6% higher than the backlog at April 3, 2015, which reflected increases of 10% and 2% for the North America and international regions, respectively.

We perform a quarterly review to verify that outstanding orders in the backlog remain valid. Aged orders that are not expected to be converted to revenues are deemed dormant and are reflected as a reduction in the backlog amounts in the period identified. Backlog adjustments are comprised of dormancies, cancellations, foreign currency exchange rate adjustments, backlog acquired from acquisitions, and other adjustments. In the second quarter of fiscal years 2016 and 2015, our backlog adjustments were $51.1 million and $52.6 million, respectively. In the first half of fiscal year 2016 and 2015, our backlog adjustments were $105.7 million and $86.4 million, respectively.

Liquidity and Capital Resources

Liquidity is the measurement of our ability to meet potential cash requirements, including ongoing commitments to repay borrowings, acquire businesses or make other investments or loans, repurchase shares of VMS common stock, and fund continuing operations and capital expenditures. Our sources of cash have included operations, borrowings, stock option exercises, and employee stock purchases. Our cash usage is actively managed on a daily basis to ensure the maintenance of sufficient funds to meet our needs.

Cash and Cash Equivalents

The following table summarizes our cash and cash equivalents:

(In millions)	April 1, 2016	October 2, 2015	Increase
Cash and cash equivalents	$961.1	$ 845.5	$115.6

The increase in cash and cash equivalents in the first half of fiscal year 2016 was primarily due to $297.0 million of net borrowings under our credit facility agreements and $109.1 million of cash provided by operating activities. These increases were partially offset by $248.7 million of cash used for the repurchase of shares of VMS common stock and $45.9 million used for purchases of property, plant, and equipment.

At April 1, 2016, we had approximately $17.5 million, or 2%, of cash and cash equivalents in the United States. Approximately $943.6 million, or 98%, of cash and cash equivalents was held abroad and a portion of this amount could be subject to additional taxation if it were repatriated to the United States. As of April 1, 2016, most of our cash and cash equivalents that were held abroad were in U.S. Dollars and were primarily held as bank deposits. In addition to cash flows generated from operations, a significant portion of which are generated in the United States, we have used our credit facilities to meet our cash needs from time to time and expect to continue to do so in the future. Borrowings under our credit facilities may be used for working capital, capital expenditures, VMS share repurchases, acquisitions and other corporate purposes.

Cash Flows

(In millions)	Six Months Ended	
	April 1, 2016	April 3, 2015
Net cash flow provided by (used in):		
Operating activities	$109.1	$132.3
Investing activities	(46.5)	(75.2)
Financing activities	57.2	(63.2)
Effects of exchange rate changes on cash and cash equivalents	(4.2)	19.0
Net increase in cash and cash equivalents	$115.6	$12.9

Our primary cash inflows and outflows for the first half of fiscal year 2016, as compared to the first half of fiscal year 2015, were as follows:

- In the first half of fiscal year 2016, we generated net cash from operating activities of $109.1 million compared to $132.3 million in the first half of fiscal year 2015. The $23.2 million decrease in net cash from operating activities in the first half of fiscal year 2016, compared to the year-ago period, was driven by a $18.0 million decrease in non-cash

48

items, and a $13.3 million decrease in net earnings, partially offset by a $8.1 million increase in net change from operating assets and liabilities.

- The major contributors to the net change in operating assets and liabilities in the first half of fiscal year 2016 were as follows:

Accounts receivable increased $94.5 million primarily due to higher revenues and longer payment cycles in Oncology Systems and VPT.

Inventory increased $39.7 million mainly due to increases in inventories in VPT and Imaging Components in anticipation of future demand.

Deferred revenues and advance payments from customers increased $19.5 million due to receipts of down payments for orders for which revenues have not been recognized and due to the nature of contracts and timing of customer acceptances, primarily in Oncology Systems.

We expect that cash provided by operating activities may fluctuate in future periods as a result of a number of factors, including fluctuations in our operating results, timing of product shipments, product installation or customer acceptance, accounts receivable collections, inventory management, and the timing and amount of tax and other payments. For additional discussion, please refer to the “Risk Factors” in Item 1A.

- In the first half of fiscal year 2016, cash used for investing activities was $46.5 million, compared to cash used of $75.2 million in the first half of fiscal year 2015. The reduction in cash used was primarily driven by a $35.7 million increase in restricted cash during the first half of fiscal year 2015, partially offset by an increase in cash used for purchases of property, plant and equipment. In the first half of fiscal year 2016, we used $45.9 million to purchase property, plant and equipment, compared to $36.7 million in the first half of fiscal year 2015.

- In the first half of fiscal year 2016, cash provided by financing activities was $57.2 million compared to $63.2 million used in the first half of fiscal year 2015. In the first half of fiscal year 2016, we had net borrowings of $297.0 million under our credit facility agreements and received $21.2 million of proceeds from employee stock option exercises and employee stock purchases. These proceeds were partially offset by $248.7 million used for the repurchase of VMS common stock and $10.7 million used to satisfy employee tax withholding requirements for employees who tendered shares of VMS common stock upon vesting of restricted common stock and restricted stock units. In the first half of fiscal year 2015, we used $201.2 million for the repurchase of VMS common stock, partially offset by $75.0 million of net borrowings under our credit facility agreements and $67.2 million of proceeds received from employee stock option exercises and employee stock purchases.

We expect our capital expenditures, which typically represent construction and/or purchases of facilities, manufacturing equipment, office equipment and furniture and fixtures, as well as capitalized costs related to the implementation of software applications, will be approximately 3% of revenues in fiscal year 2016.

On August 27, 2013, VMS entered into an agreement (as amended to date) with certain lenders and Bank of America, N.A. (“BofA”) as administrative agent (the "Credit Agreement").

The Credit Agreement provides for (i) a five-year term loan facility in an aggregate principal amount of up to $500 million (the “2013 Term Loan Facility”) and (ii) a five-year revolving credit facility in an aggregate principal amount of up to $500 million (the “2013 Revolving Credit Facility” and, collectively with the 2013 Term Loan Facility, the “2013 Credit Facility”). The 2013 Revolving Credit Facility also includes a $50 million sub-facility for the issuance of letters of credit and permits swing line loans of up to $25 million. We may prepay, reduce or terminate the commitments without penalty. The 2013 Credit Facility contains provisions that limit our ability to pay cash dividends. The Credit Agreement will expire in August 2018. The proceeds of the 2013 Credit Facility will be used for working capital, capital expenditures, Company share repurchases, permitted acquisitions and other corporate purposes.

In addition, our Japanese subsidiary (“VMS KK”) has an unsecured uncommitted credit agreement with Sumitomo Mitsui Banking Corporation that enables VMS KK to borrow and have outstanding at any given time a maximum of 3 billion Japanese Yen (the “Sumitomo Credit Facility”). In February 2016, the Sumitomo Credit Facility was extended and will expire in February 2017.

The following table summarizes our short-term and long-term debt:

	April 1, 2016		October 2, 2015
(Dollars in millions)	Amount	Weighted-Average Interest Rate	