Steris plc
Form 10-Q
August 09, 2016
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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D. C. 20549

FORM 10-Q
(Mark One)

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

For the quarterly period ended June 30, 2016

or

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

United Kingdom (State or other jurisdiction of incorporation or organization)	98-1203539 (IRS Employer Identification No.)
Chancery House, 190 Waterside Road, Hamilton Industrial Park Leicester (Address of principal executive offices)	LE51QZ (Zip code)

44-116-276-8636
(Registrant’s telephone number, including area code)

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

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

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

Large Accelerated Filer x	Accelerated Filer o
Non-Accelerated Filer o (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 o No x

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

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PART 1—FINANCIAL INFORMATION

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

ITEM 1. FINANCIAL STATEMENTS

STERIS PLC AND SUBSIDIARIES
CONSOLIDATED BALANCE SHEETS
(in thousands)

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

See notes to consolidated financial statements.

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

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

See notes to consolidated financial statements.

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STERIS PLC AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME
(in thousands)
(Unaudited)

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

See notes to consolidated financial statements.

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

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

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

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

See notes to consolidated financial statements.

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STERIS PLC AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Unaudited)
For the Three Months Ended June 30, 2016 and 2015
(dollars in thousands, except per share amounts)

1. Nature of Operations and Summary of Significant Accounting Policies

Nature of Operations

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

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

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

Interim Financial Statements

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

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

Principles of Consolidation

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

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STERIS PLC AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Unaudited)—(Continued)
For the Three Months Ended June 30, 2016 and 2015
(dollars in thousands)

Use of Estimates

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

Recently Issued Accounting Standards Impacting the Company

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

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

STERIS PLC AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Unaudited)—(Continued)
For the Three Months Ended June 30, 2016 and 2015
(dollars in thousands)

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

Accounting" (Topic 323)	investor's previously held interest and adopt the equity method of accounting as of the date the investment becomes qualified for equity method accounting. The standard is effective for annual periods beginning after December 15, 2016 and interim periods within that period. Early adoption is permitted.

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

STERIS PLC AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Unaudited)—(Continued)
For the Three Months Ended June 30, 2016 and 2015
(dollars in thousands)

2. Restructuring

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

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

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

Three Months Ended June 30, 2016	Fiscal 2014 Restructuring Plan
Lease termination obligation and other	$ 154
Total restructuring charges	$ 154

Three Months Ended June 30, 2015	Fiscal 2014 Restructuring Plan (1)
Severance and other compensation related costs	$ (806)
Lease termination obligation and other	80
Product rationalization	277
Total restructuring benefit	$ (449)

(1) Includes $277 in expense recorded to cost of revenues on Consolidated Statements of Income.

Liabilities related to restructuring activities were $688 and $700 at June 30, 2016 and March 31, 2016, respectively and are recorded as current liabilities on the accompanying Consolidated Balance Sheets within "Accrued payroll and other related liabilities" and "Accrued expenses and other."

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STERIS PLC AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Unaudited)—(Continued)
For the Three Months Ended June 30, 2016 and 2015
(dollars in thousands)

3. Property, Plant and Equipment

Information related to the major categories of our depreciable assets is as follows:

	June 30, 2016	March 31, 2016
Land and land improvements (1)	$39,054	$39,051
Buildings and leasehold improvements	443,234	446,277
Machinery and equipment	574,277	580,962
Linens	42,291	42,354
Information systems	131,487	126,180
Radioisotope	434,189	434,152
Construction in progress (1)	89,692	79,291
Total property, plant, and equipment	1,754,224	1,748,267
Less: accumulated depreciation and depletion	(698,518)	(683,948)
Property, plant, and equipment, net	$1,055,706	$1,064,319

(1) Land is not depreciated. Construction in progress is not depreciated until placed in service.

4. Inventories, Net

Inventories, net are stated at the lower of cost or market. We use the last-in, first-out (“LIFO”) and first-in, first-out cost methods. An actual valuation of inventory under the LIFO method is made only at the end of the fiscal year based on the inventory levels and costs at that time. Accordingly, interim LIFO calculations are based on management’s estimates of expected year-end inventory levels and are subject to the final fiscal year-end LIFO inventory valuation. Inventory costs include material, labor, and overhead. Inventories, net consisted of the following:

	June 30, 2016	March 31, 2016
Raw materials	$67,374	$62,673
Work in process	22,192	19,614
Finished goods	156,236	146,820
LIFO reserve	(17,270)	(17,608)
Reserve for excess and obsolete inventory	(18,887)	(18,707)
Inventories, net	$209,645	$192,792

5. Debt

Indebtedness was as follows:

	June 30, 2016	March 31, 2016
Private Placement	$666,000	$666,000
Deferred financing costs	(3,299)	(3,420)

Credit Agreement	889,137	905,216
Total long term debt	$1,551,838	$1,567,796

Additional information regarding our indebtedness is included in the notes to our consolidated financial statements included in our Annual Report on Form 10-K for the year ended March 31, 2016 dated May 31, 2016.

STERIS PLC AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Unaudited)—(Continued)
For the Three Months Ended June 30, 2016 and 2015
(dollars in thousands)

6. Additional Consolidated Balance Sheet Information

Additional information related to our Consolidated Balance Sheets is as follows:

	June 30, 2016	March 31, 2016
Accrued payroll and other related liabilities:		
Compensation and related items	$37,685	$30,175
Accrued vacation/paid time off	12,070	14,368
Accrued bonuses	8,679	31,502
Accrued employee commissions	8,727	13,809
Other postretirement benefit obligations-current portion	2,463	2,463
Other employee benefit plans obligations-current portion	899	1,659
Total accrued payroll and other related liabilities	$70,523	$93,976
Accrued expenses and other:		
Deferred revenues	$64,205	$56,238
Self-insured risk reserves-current portion	8,294	8,266
Accrued dealer commissions	13,982	12,717
Accrued warranty	5,856	5,909
Other	58,465	70,245
Total accrued expenses and other	$150,802	$153,375
Other liabilities:		
Self-insured risk reserves-long-term portion	$13,257	$13,257
Other postretirement benefit obligations-long-term portion	15,621	15,932
Defined benefit pension plans obligations-long-term portion	23,221	25,301
Other employee benefit plans obligations-long-term portion	4,186	4,366
Asset retirement obligation-long-term portion	10,059	10,342
Other	16,112	15,100
Total other liabilities	$82,456	$84,298

7. Income Tax Expense

Income tax expense includes United States federal, state and local, and foreign income taxes, and is based on reported pre-tax income. The effective income tax rates for the three-month periods ended June 30, 2016 and 2015 were 22.6% and 37.0%, respectively. The first quarter of fiscal 2017 was favorably impacted by benefits achieved in conjunction with the Synergy transaction and the adoption of ASU 2016-09: "Stock Compensation: Improvements to Employee Share-Based Payment Accounting" (Topic 718).

Income tax expense is provided on an interim basis based upon our estimate of the annual effective income tax rate, adjusted each quarter for discrete items. In determining the estimated annual effective income tax rate, we analyze various factors, including projections of our annual earnings and taxing jurisdictions in which the earnings will be generated, the impact of state and local income taxes, our ability to use tax credits and net operating loss carry forwards, and available tax planning alternatives.

We operate in numerous taxing jurisdictions and are subject to regular examinations by various United States federal, state and local authorities, as well as foreign jurisdictions. We are no longer subject to United States federal examinations for years before fiscal 2013 and, with limited exceptions, we are no longer subject to United States state and local or non-United States income tax examinations by tax authorities for years before fiscal 2012. We remain subject to tax authority audits in various jurisdictions wherever we do business. We do not expect the results of these examinations to have a material adverse affect on our consolidated financial statements.

STERIS PLC AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Unaudited)—(Continued)
For the Three Months Ended June 30, 2016 and 2015
(dollars in thousands)

8. Benefit Plans

In the United States we sponsor an unfunded postretirement welfare benefits plan for two groups of former employees. Benefits under this plan include retiree life insurance and retiree medical coverage, including prescription drug coverage.
During the second quarter of fiscal 2009, we amended our United States post-retirement welfare benefits plan, reducing the benefits to be provided to retirees under the plan and increasing their share of the costs. The amendments resulted in a decrease of $46,001 in the accumulated post-retirement benefit obligation. The impact of this change was recognized in our Consolidated Balance Sheets in fiscal 2009 and is being amortized as a component of the annual net periodic benefit cost over a period of approximately thirteen years.
In July 2014, the Board of Directors of American Sterilizer Company (“AMSCO”) approved the termination of the American Sterilizer Company Retirement Income Plan (“Plan”) effective October 1, 2014. The Pension Benefit Guaranty Corporation ("PBGC") did not object to this termination and AMSCO received a favorable determination from the IRS regarding the termination. On August 19, 2015, an annuity contract was purchased from Massachusetts Mutual Life Insurance Company to provide Plan benefits. Plan assets were converted to cash to fund the purchase. The purchase price of the annuity contract was $51,805. An additional employer contribution of $4,641 was made to the Plan to fund the annuity purchase obligation on August 26, 2015. As a result the purchase of the annuity, we recognized a pension settlement of $26,470 in fiscal 2016. In addition, plan benefits and benefit administration became the responsibility of the annuity provider. Additional information regarding this defined benefit pension plan and other postretirement benefits plan is included in our consolidated financial statements included in our Annual Report on Form 10-K for the year ended March 31, 2016, dated May 31, 2016.
In the United Kingdom, we sponsor a defined benefit arrangement administered by a single group of trustees. The arrangement is comprised of three merged schemes. The trustees hold the pension assets to meet long-term pension liabilities for past and present employees. The level of retirement benefit is principally based on the terms of the scheme and the final pensionable salary prior to leaving active service, and is linked to changes in inflation up to retirement.

In previous years, Synergy sponsored a funded defined benefit arrangement in the Netherlands. This was a separate fund holding the pension scheme assets to meet long term pension liabilities for past and present employees. Accrual of benefits ceased under the scheme effective January 1, 2013.

The Synergy Radeberg and Synergy Alleshausen Schemes are German defined benefit funded pension schemes which are closed to new entrants.
The Synergy Daniken Scheme is a Swiss defined benefit funded pension scheme.

Components of the net periodic benefit cost for our defined benefit pension plans and other postretirement medical benefits plan were as follows:

	AMSCO Plan	Other Defined Benefit Pension Plan	Other Postretirement Benefits Plan

Three Months Ended June 30,	2016	2015	2016	2015	2016	2015
Service cost	$ —	$ 16	$ 472	$ —	$ —	$ —
Interest cost	—	336	189	—	139	148
Expected return on plan assets	—	(605)	—	—	—	—
Amortization of loss	—	361	—	—	184	207
Amortization of prior service cost	—	—	—	—	(816)	(815)
Net periodic benefit cost	$ —	$ 108	$ 661	$ —	$ (493)	$ (460)

We contribute amounts to the defined benefit pension plan at least sufficient to meet the minimum requirements as stated in applicable employee benefit laws and local tax laws. We record liabilities for the difference between the fair value of the plan assets and the benefit obligation (the projected benefit obligation for pension plan and the accumulated postretirement benefit obligation for other postretirement benefits plan) on our accompanying Consolidated Balance Sheets.

Finally, the Dutch linen business acquired in the Synergy combination participates in a multi-employer industry-wide defined benefit scheme. Participation in this pension plan is mandatory. The pension scheme is an average pay scheme with a conditional fee (indexation). Indexation of assets and liabilities granted under the pension scheme takes place only if and insofar as the resources of the fund allow for it and this decision is taken by the pension fund. The pension entitlements under the pension plan are fully reinsured. It is not possible to identify the share of the underlying assets, liabilities, and overall surplus/deficit of the scheme attributable to the business, because the scheme is industry-wide. Under the guidance provided in ASC 715, "Compensation-Retirement Benefits", the scheme is treated as a defined contribution scheme within our financial statements. The total cost charged to the income statement in respect to this scheme was $661 for the three months ended June 30, 2016.

9. Commitments and Contingencies

We are, and will likely continue to be, involved in a number of legal proceedings, government investigations, and claims, which we believe generally arise in the course of our business, given our size, history, complexity, and the nature of our business, products, Customers, regulatory environment, and industries in which we participate. These legal proceedings, investigations and claims generally involve a variety of legal theories and allegations, including, without limitation, personal injury (e.g., slip and falls, burns, vehicle accidents), product liability or regulation (e.g., based on product operation or claimed malfunction, failure to warn, failure to meet specification, or failure to comply with regulatory requirements), product exposure (e.g., claimed exposure to chemicals, asbestos, contaminants, radiation), property damage (e.g., claimed damage due to leaking equipment, fire, vehicles, chemicals), commercial claims (e.g., breach of contract, economic loss, warranty, misrepresentation), financial (e.g., taxes, reporting), employment (e.g., wrongful termination, discrimination, benefits matters), and other claims for damage and relief.
We believe we have adequately reserved for our current litigation and claims that are probable and estimable, and further believe that the ultimate outcome of these pending lawsuits and claims will not have a material adverse effect on our consolidated financial position or results of operations taken as a whole. Due to their inherent uncertainty, however, there can be no assurance of the ultimate outcome or effect of current or future litigation, investigations, claims or other proceedings (including without limitation the matters discussed below). For certain types of claims, we presently maintain insurance coverage for personal injury and property damage and other liability coverages in amounts and with deductibles that we believe are prudent, but there can be no assurance that these coverages will be applicable or adequate to cover adverse outcomes of claims or legal proceedings against us.
On May 31, 2012, our Albert Browne Limited subsidiary received a warning letter from the FDA regarding chemical indicators manufactured in the United Kingdom. These devices are intended for the monitoring of certain sterilization and other processes. The FDA warning letter states that the agency has concerns regarding operational business processes. We do not believe that the FDA's concerns are related to product performance, or that they result from Customer complaints. We have reviewed our processes with the agency and finalized our remediation measures, and are awaiting FDA reinspection. We do not currently believe that the impact of this event will have a material adverse effect on our financial results.
On December 19, 2014, a purported shareholder of Old STERIS filed a Verified Stockholder Derivative Complaint in the Court of Common Pleas, Cuyahoga County, Ohio (the "Court"), against the members of Old STERIS's board of directors and certain officers of Old STERIS, challenging the excise tax make-whole payments approved by Old STERIS's board in connection with the Combination. Old STERIS was named as a nominal defendant in the action. The case is captioned St. Lucie County Fire District Firefighters' Pension Trust Fund v. Rosebrough, Jr., et al., Case No. CV 14 837749 (the "Action"). On September 28, 2015, the defendants reached an agreement in principle with

plaintiff, regarding a settlement of the Action, and that agreement is reflected in a memorandum of understanding. In connection with the contemplated settlement, Old STERIS agreed to make certain additional disclosures related to the make-whole payments, which disclosures were reported on Old STERIS's Form 8-K dated September 28, 2015, and also agreed not to grant any new stock compensation subject to
Section 4985 of the Internal Revenue Code to any of the individual defendants in the Action until six months following the closing date of the Combination. The parties have subsequently entered into and executed a stipulation of settlement, on a combined class and derivative basis, including agreement on a maximum fee/expense award to plaintiff's counsel. The stipulation of settlement, which is subject to customary conditions including approval of the Court following notice and hearing, has been filed with the Court along with a request for preliminary approval and the setting of a hearing date. The Court has not yet acted on the request. There can be no assurance that the Court will approve the proposed settlement and the settlement agreement may be terminated if Court approval is not obtained.

Other civil, criminal, regulatory or other proceedings involving our products or services could possibly result in judgments, settlements or administrative or judicial decrees requiring us, among other actions, to pay damages or fines or effect recalls, or be subject to other governmental, Customer or other third party claims or remedies, which could materially effect our business, performance, prospects, value, financial condition, and results of operations.

For additional information regarding these matters, see the following portions of our Annual Report on Form 10-K for the year ended March 31, 2016 dated May 31, 2016: “Business - Information with respect to our Business in General - Government Regulation”, and the “Risk Factor” titled “We may be adversely affected by product liability claims or other legal actions or regulatory or compliance matters.

From time to time, STERIS is also involved in legal proceedings as a plaintiff involving contract, patent protection, and other claims asserted by us. Gains, if any, from these proceedings are recognized when they are realized.

We are subject to taxation from United States federal, state and local, and foreign jurisdictions. Tax positions are settled primarily through the completion of audits within each individual jurisdiction or the closing of statutes of limitation. Changes in applicable tax law or other events may also require us to revise past estimates. We describe income taxes further in note 7 to our consolidated financial statements titled, “Income Taxes” in this Quarterly Report on Form 10-Q.

Additional information regarding our contingencies is included in Item 2 titled, “Management’s Discussion and Analysis of Financial Conditions and Results of Operations under "Contingencies".

10. Business Segment Information

We operate and report in four reportable business segments: Healthcare Products, Healthcare Specialty Services, Life Sciences, and Applied Sterilization Technologies. Corporate and other, which is presented separately, contains the Defense and Industrial business unit plus costs that are associated with being a publicly traded company and certain other corporate costs.
Our Healthcare Products segment offers infection prevention and procedural solutions for healthcare providers worldwide, including capital equipment and related maintenance and installation services, as well as consumables.
Our Healthcare Specialty Services segment provides a range of specialty services for healthcare providers including hospital sterilization services, instrument and scope repairs, and linen management.
Our Life Sciences segment offers capital equipment and consumable products, and equipment maintenance and specialty services for pharmaceutical manufacturers and research facilities.
Our Applied Sterilization Technologies segment offers a contract sterilization and laboratory services for medical device and pharmaceutical Customers and others.
The accounting policies for reportable segments are the same as those for the consolidated Company. Management evaluates performance and allocates resources based on a segment operating income measure. Operating income (loss) for each segment is calculated as the segment's gross profit less direct expenses and indirect cost allocations, which result in the full allocation of all distribution and research and development expenses, and the partial allocation of corporate costs. These allocations are based upon variables such as segment headcount and revenues. In addition, the Healthcare Products segment is responsible for the management of all but two manufacturing facilities and uses standard cost to sell products to the other segments. Corporate and other includes the gross profit and direct expenses of the Defense and Industrial business unit, as well as certain unallocated corporate costs related to being a publicly traded company and legacy pension and post-retirement benefits. Segment operating income excludes certain adjustments which include acquisition related costs, amortization of acquired intangibles, restructuring costs and other charges that management believes may or may not recur with similar materiality or impact on operating income in future periods. Management believes that by excluding these items they gain better insight and greater transparency of the operating performance of the segments, thus aiding them in more meaningful financial trend analysis and operational decision making
For the three month period ended June 30, 2016, revenues from a single Customer did not represent ten percent or more of any reportable segment's revenues. Additional information regarding our segments is included in our consolidated financial statements included in its Annual Report on Form 10-K for the year ended March 31, 2016, dated May 31, 2016.

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Financial information for each of our segments is presented in the following tables:

	Three Months Ended June 30,	
	2016	2015
Revenues:		
Healthcare Products	$281,298	$261,086
Healthcare Specialty Services	157,888	68,241
Life Sciences	81,189	56,772
Applied Sterilization Technologies	116,573	53,689
Corporate and other	1,430	114
Total revenues	$638,378	$439,902
Segment operating income:		
Healthcare Products	$34,637	$29,350
Healthcare Specialty Services	3,318	3,900
Life Sciences	24,462	13,450
Applied Sterilization Technologies	39,603	16,543
Corporate and other	(496)	(1,898)
Total segment operating income	$101,524	$61,345
Less: Adjustments		
Restructuring charges (1)	$154	$(449)
Amortization of acquired intangible assets (2)	19,529	6,021
Acquisition, divestiture and integration related charges (3)	5,233	11,546
Amortization of inventory and property "step up" to fair value (2)	3,086	11
Total operating income	$73,522	$44,216

(1) See Note 2 to our Consolidated Financial Statements titled, "Restructuring" for more information related to restructuring.
(2) For more information regarding our recent acquisitions see Note 18 titled, "Business Acquisitions", as well as our Annual Report on Form 10-K for the year ended March 31, 2016, dated May 31, 2016.
(3) Acquisition, divestiture and integration related charges include transaction costs and integration expenses associated with acquisitions and divestitures.

11. Shares and Preferred Shares

Common and Ordinary

We calculate basic earnings per share based upon the weighted average number of shares outstanding. We calculate diluted earnings per share based upon the weighted average number of shares outstanding plus the dilutive effect of share equivalents calculated using the treasury stock method. The following is a summary of shares and share equivalents outstanding used in the calculations of basic and diluted earnings per share:

	Three Months Ended June 30,	
	2016	2015
Denominator (shares in thousands):		
Weighted average shares outstanding—basic	86,038	59,768
Dilutive effect of share equivalents	481	518
Weighted average shares outstanding and share equivalents—diluted	86,519	60,286

Options to purchase the following number of shares were outstanding but excluded from the computation of diluted earnings per share because the combined exercise prices, unamortized fair values, and assumed tax benefits upon exercise were greater than the average market price for the shares during the periods, so including these options would be anti-dilutive:

	Three Months Ended June 30,	
	2016	2015
(shares in thousands)		
Number of share options	364	52

Preferred Shares

Pursuant to an engagement letter dated October 23, 2015, we issued 100,000 preferred shares, par value of £0.10 ($0.15) each, for an aggregate consideration of approximately $15, in satisfaction of debt owed to a service provider. The holders of the preferred shares are entitled to a fixed cumulative preferential annual dividend of 5 percent on the amount paid periodically on the preferred shares respectively held by them. On a return of capital of the Company whether on liquidation or otherwise, the holders of the preferred shares shall be entitled to receive out of the assets of the Company available for distribution to its shareholders the sum of £0.10 ($0.15) per preferred share plus any accrued but unpaid dividend, but will not be entitled to any further participation in the assets of the Company. The holders of the preferred shares will have no right to attend, speak or vote, whether in person or by proxy, at any general meeting of the Company or any meeting of a class of members of the Company in respect of the preferred shares and will not be entitled to receive any notice of meetings.

12. Repurchases of Shares

During the first quarter of fiscal 2017, we obtained 104,626 of our ordinary shares in connection with share based compensation award programs.

13. Share-Based Compensation

We maintain a long-term incentive plan that makes available shares for grants, at the discretion of the Compensation Committee of the Board of Directors, to officers, directors, and key employees in the form of stock options, restricted shares, restricted share units, stock appreciation rights and share grants.

Stock options provide the right to purchase our shares at the market price on the date of grant, subject to the terms of the option plans and agreements. Generally, one-fourth of the stock options granted become exercisable for each full year of employment following the grant date. Stock options granted generally expire 10 years after the grant date, or in some cases earlier if the option holder is no longer employed by us. Restricted shares and restricted share units generally may cliff vest after a four year period or vest in tranches of one-fourth of the number granted for each full year of employment after the grant date. As of June 30, 2016, 1,613,977 shares remained available for grant under the long-term incentive plan.

The fair value of share-based compensation awards was estimated at their grant date using the Black-Scholes-Merton option pricing model. This model was developed for use in estimating the fair value of traded options that have no vesting restrictions and are fully transferable, characteristics that are not present in our option grants. If the model permitted consideration of the unique characteristics of employee stock options, the resulting estimate of the fair value of the stock options could be different. The value of the portion of the award that is ultimately expected to vest is recognized as expense over the requisite service periods in our Consolidated Statements of Income. The expense is classified as cost of goods sold or selling, general and administrative expenses in a manner consistent with the employee's compensation and benefits.

(dollars in thousands)

The following weighted-average assumptions were used for options granted during the first three months of fiscal 2017 and fiscal 2016:

	Fiscal 2017	Fiscal 2016
Risk-free interest rate	1.29 %	1.46 %
Expected life of options	5.5 years	5.6 years
Expected dividend yield of stock	1.55 %	1.40 %
Expected volatility of stock	22.78 %	24.74 %

The risk-free interest rate is based upon the U.S. Treasury yield curve. The expected life of options is reflective of historical experience, vesting schedules and contractual terms. The expected dividend yield of stock represents our best estimate of the expected future dividend yield. The expected volatility of stock is derived by referring to our historical stock prices over a time frame similar to that of the expected life of the grant. An estimated forfeiture rate of 1.85% and 1.55% was applied in fiscal 2017 and 2016, respectively. This rate is calculated based upon historical activity and represents an estimate of the granted options not expected to vest. If actual forfeitures differ from this calculated rate, we may be required to make additional adjustments to compensation expense in future periods. The assumptions used above are reviewed at the time of each significant option grant, or at least annually.

A summary of share option activity is as follows:

	Number of Options	Weighted Average Exercise Price	Average Remaining Contractual Term	Aggregate Intrinsic Value
Outstanding at March 31, 2016	1,729,517	$ 44.01		
Granted	370,212	69.72		
Exercised	(18,131)	29.95		
Forfeited	(2,703)	59.41		
Canceled	—	—		
Outstanding at June 30, 2016	2,078,895	$ 48.69	6.7 years	$ 42,065
Exercisable at June 30, 2016	1,238,705	$ 38.35	5.2 years	$ 37,658

We estimate that 816,670 of the non-vested stock options outstanding at June 30, 2016 will ultimately vest.

The aggregate intrinsic value in the table above represents the total pre-tax difference between the $68.75 closing price of our ordinary shares on June 30, 2016 over the exercise prices of the stock options, multiplied by the number of options outstanding or outstanding and exercisable, as applicable. The aggregate intrinsic value is not recorded for financial accounting purposes and the value changes daily based on the daily changes in the fair market value of ordinary shares.

The total intrinsic value of stock options exercised during the first three months of fiscal 2017 and fiscal 2016 was $727 and $5,582, respectively. Net cash proceeds from the exercise of stock options were $758 and $4,881 for the first three months of fiscal 2017 and fiscal 2016, respectively.

The weighted average grant date fair value of stock option grants was $13.15 and $14.11 for the first three months of fiscal 2017 and fiscal 2016, respectively.

Stock appreciation rights (“SARS”) carry generally the same terms and vesting requirements as stock options except that they are settled in cash upon exercise and therefore, are classified as liabilities. The fair value of the outstanding SARS as of June 30, 2016 and 2015 was $1,857 and $1,966, respectively.

(dollars in thousands)

A summary of the non-vested restricted share activity is presented below:

	Number of Restricted Shares	Number of Restricted Share Units	Weighted-Average Grant Date Fair Value
Non-vested at March 31, 2016	872,972	41,641	$ 51.98
Granted	219,167	9,390	69.77
Vested	(186,856)	(10,589)	38.74
Canceled	(10,722)	(2,275)	60.54
Non-vested at June 30, 2016	894,561	38,167	$ 59.02

Restricted shares granted are valued based on the closing stock price at the grant date. The value of restricted shares that vested during the first three months of fiscal 2017 was $7,087.

Restricted share units carry generally the same terms and vesting requirements as restricted stock except that they may be settled in stock or cash upon vesting. Those that are settled in cash are classified as liabilities. All outstanding cash-settled restricted share units vested during fiscal year 2016. The fair value of cash-settled restricted share units are revalued at each reporting date and the related liability and expense are adjusted accordingly.

The tax benefit from share-based compensation was $2,440 and $3,910 for the first three months of fiscal 2017 and fiscal 2016, respectively.

As of June 30, 2016, there was a total of $47,882 in unrecognized compensation cost related to non-vested share-based compensation granted under our share-based compensation plans. We expect to recognize the cost over a weighted average period of 2.45 years.

14. Financial and Other Guarantees

We generally offer a limited parts and labor warranty on capital equipment. The specific terms and conditions of those warranties vary depending on the product sold and the countries where we conduct business. We record a liability for the estimated cost of product warranties at the time product revenues are recognized. The amounts we expect to incur on behalf of our Customers for the future estimated cost of these warranties are recorded as a current liability on the accompanying Consolidated Balance Sheets. Factors that affect the amount of our warranty liability include the number and type of installed units, historical and anticipated rates of product failures, and material and service costs per claim. We periodically assess the adequacy of our recorded warranty liabilities and adjust the amounts as necessary.

Changes in our warranty liability during the first three months of fiscal 2017 were as follows:

Balance, March 31, 2016	$5,909
Warranties issued during the period	2,742

Settlements made during the period	(2,795)
Balance, June 30, 2016	$5,856

We also sell product maintenance contracts to our Customers. These contracts range in terms from one to five years and require us to maintain and repair the product over the maintenance contract term. We initially record amounts due from Customers under these contracts as a liability for deferred service contract revenue on the accompanying Consolidated Balance Sheets within "Accrued expenses and other." The liability recorded for such deferred service revenue was $32,953 and $33,416 as of June 30, 2016 and March 31, 2016, respectively. Such deferred revenue is then amortized on a straight-line basis over the contract term and recognized as service revenue on our accompanying Consolidated Statements of Income. The activity related to the liability for deferred service contract revenue is excluded from the table presented above.

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15. Derivatives and Hedging

From time to time, we enter into forward contracts to hedge potential foreign currency gains and losses that arise from transactions denominated in foreign currencies, including inter-company transactions. We may also enter into commodity swap contracts to hedge price changes in nickel that impact raw materials included in our cost of revenues. We do not use derivative financial instruments for speculative purposes. These contracts are not designated as hedging instruments and do not receive hedge accounting treatment; therefore, changes in their fair value are not deferred but are recognized immediately in the Consolidated Statements of Income. At June 30, 2016, we held foreign currency forward contracts to buy 90.0 million Mexican pesos, 4.0 million British pounds sterling, 3.5 million euros, and 8.0 million Canadian dollars. At June 30, 2016 we held commodity swap contracts to buy 499.0 thousand pounds of nickel.

	Asset Derivatives		Liability Derivatives	
Balance Sheet Location	Fair Value at June 30, 2016	Fair Value at March 31, 2016	Fair Value at June 30, 2016	Fair Value at March 31, 2016
Prepaid & Other	$ 351	$ 145	$ —	$ —
Accrued expenses and other	$ —	$ —	$ 293	$ 122

The following table presents the impact of derivative instruments and their location within the Consolidated Statements of Income:

	Location of gain (loss) recognized in income	Amount of gain (loss) recognized in income Three Months Ended June 30, 2016	2015
Foreign currency forward contracts	Selling, general and administrative	$ (1,019)	$ 432
Commodity swap contracts	Cost of revenues	$ 211	$ (45)

Additionally, we hold our debt in multiple currencies to fund our operations and investments in certain subsidiaries. We designate portions of foreign currency denominated intercompany loans as hedges of portions of net investments in foreign operations. Net debt designated as non-derivative net investment hedging instruments totaled $123,811 at June 30, 2016. These hedges are designed to be fully effective and any associated gain or loss is recognized in Accumulated Other Comprehensive Income and will be reclassified to income in the same period when a gain or loss related to the net investment in the foreign operation is included in income.

16. Fair Value Measurements

Fair value is defined as the price that would be received to sell an asset or that would be paid to transfer a liability in an orderly transaction between market participants at the measurement date. We estimate the fair value of financial assets and liabilities using available market information and generally accepted valuation methodologies. The inputs used to measure fair value are classified into three tiers. These tiers include Level 1, defined as observable inputs such as quoted prices in active markets; Level 2, defined as inputs other than quoted prices in active markets that are either directly or indirectly observable; and Level 3, defined as unobservable inputs in which little or no market data exists, therefore requiring the entity to develop its own assumptions.

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The following table shows the fair value of our financial assets and liabilities at June 30, 2016 and March 31, 2016:

	Carrying Value		Fair Value Measurements at June 30, 2016 and March 31, 2016 Using Quoted Prices in Active Markets for Identical Assets Level 1		Significant Other Observable Inputs Level 2		Significant Unobservable Inputs Level 3	
	June 30	March 31	June 30	March 31	June 30	March 31	June 30	March 31
Assets:								
Cash and cash equivalents (1)	$242,423	$248,841	$217,246	$225,090	$25,177	$23,751	$ —	$ —
Forward and swap contracts (2)	351	145	—	—	351	145	—	—
Investments (3)	10,148	6,192	10,148	6,192	—	—	—	—
Liabilities:								
Forward and swap contracts (2)	$293	$122	$—	$—	$293	$122	$ —	$ —
Deferred compensation plans (3)	1,703	1,765	1,703	1,765	—	—	—	—
Long term debt (4)	1,551,838	1,567,796	—	—	1,601,514	1,592,184	—	—
Contingent consideration obligations (5)	5,956	5,886	—	—	—	—	5,956	5,886

(1) Money market fund holdings are classified as level two as active market quoted prices are not available.
(2) The fair values of forward and swap contracts are based on period-end forward rates and reflect the value of the amount that we would pay or receive for the contracts involving the same notional amounts and maturity dates.
(3) We maintain a frozen domestic non-qualified deferred compensation plan covering certain employees, which allows for the deferral of payment of previously earned compensation for an employee-specified term or until retirement or termination. Amounts deferred can be allocated to various hypothetical investment options (compensation deferrals have been frozen under the plan). We hold investments to satisfy the future obligations of the plan. Changes in the value of the investment accounts are recognized each period based on the fair value of the underlying investments. Employees who made deferrals are entitled to receive distributions of their hypothetical account balances (amounts deferred, together with earnings (losses)). We also hold an investment in the common stock of Servizi Italia, S.p.A, a leading provider of integrated linen washing and outsourced sterile processing services to hospital Customers including an incremental investment of $4,564 made in April 2016. Changes in the value of the investment are recognized each period based on the fair value of the investment.
(4) We estimate the fair value of our principal amount of long-term debt using discounted cash flow analyses, based on our current incremental borrowing rates for similar types of borrowing arrangements.
(5) Contingent consideration obligations arise from prior business acquisitions. The fair values are based on discounted cash flow analyses reflecting the possible achievement of specified performance measures or events and captures the contractual nature of the contingencies, commercial risk, and the time value of money. Contingent consideration obligations are classified in the consolidated balance sheets as accrued expense (short-term) and other liabilities (long-term), as appropriate based on the contractual payment dates.

The changes in Level 3 assets and liabilities measured at fair value on a recurring basis at June 30, 2016 are summarized as follows:

	Contingent Consideration
Balance at March 31, 2016	$ 5,886
Additions	—
Payments	—
Foreign currency translation adjustments (1)	70
Balance at June 30, 2016	$ 5,956

(1) Reported in other comprehensive income (loss).

(dollars in thousands)

Information regarding our investments is as follows:

	Investments at June 30, 2016 and March 31, 2016							
	Cost		Unrealized Gains		Unrealized Losses (2)		Fair Value	
	June 30	March 31	June 30	March 31	June 30	March 31	June 30	March 31
Available-for-sale securities:								
Marketable equity securities (1)	$9,245	$4,681	$—	$—	$(721)	$(185)	$8,524	$4,496
Mutual funds	1,206	1,289	418	407	—	—	1,624	1,696
Total available-for-sale securities	$10,451	$5,970	$418	$407	$(721)	$(185)	$10,148	$6,192

(1) Our marketable equity securities have been in a unrealized loss position for less than 12 months.
(2) Amounts reported include the impact of foreign currency movements relative to the U.S. dollar.

17. Reclassifications Out of Accumulated Other Comprehensive Income (Loss)

Amounts in Accumulated Other Comprehensive Income (Loss) are presented net of the related tax. Foreign Currency Translation is not adjusted for income taxes. Changes in our Accumulated Other Comprehensive Income (Loss) balances, net of tax, for the three months ended June 30, 2016 were as follows:

	Gain (Loss) on Available for Sale Securities (1)	Defined Benefit Plans (2)	Foreign Currency Translation (3)	Total Accumulated Other Comprehensive Income (Loss)
Balance at March 31, 2016	$ (673)	$5,108	$ (72,594)	$ (68,159)
Other Comprehensive Income (Loss) before reclassifications	(148)	103	(17,049)	(17,094)
Amounts reclassified from Accumulated Other Comprehensive Income (Loss)	28	(493)	—	(465)
Net current-period Other Comprehensive Income (Loss)	(120)	(390)	(17,049)	(17,559)
Balance at June 30, 2016	$ (793)	$4,718	$ (89,643)	$ (85,718)

Details of amounts reclassified from Accumulated Other Comprehensive Income (Loss) are as follows:

(1) Realized gain (loss) on available for sale securities is reported in the interest income and miscellaneous expense line of the Consolidated Statements of Income.
(2) Amortization (gain) of defined benefit pension items is reported in the selling, general and administrative expense line of the Consolidated Statements of Income.
(3) The effective portion of gain or loss on net debt designated as non-derivative net investment hedging instruments is recognized in Accumulated Other Comprehensive Income and is reclassified to income in the same period when a

gain or loss related to the net investment in the foreign operation is included in income.

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18. Business Acquisitions

Synergy Health plc

On November 2, 2015, STERIS acquired all outstanding shares of Synergy in a cash and stock transaction valued at £24.80 ($38.17) per Synergy share, or a total of approximately $2.3 billion based on the low trading price of Old STERIS's stock of $73.02 per share on November 2, 2015. Total costs of approximately $200 before tax were incurred during the first three months of fiscal year 2017 related to the Combination and are reported in selling, general and administrative expense.

Total consideration for the transaction is presented in the table below. At the closing date of the Combination, vested share option awards remained outstanding under Synergy's Save As You Earn Plans ("SAYE"). In accordance with the provisions of SAYE, vested option awards may be exercised to the extent that the exercise price funds have been accumulated in accordance with the option holder's savings contract. The number of Synergy shares that are expected to be issued have been fair valued based on the same cash and stock consideration available to other Synergy shareholders at the time of the Combination.

Cash consideration	$402,494
STERIS plc shares (25,848,798 ordinary shares issued)	1,887,479
Fair value of consideration available to vested Synergy share option holders	4,819
Total purchase consideration	$2,294,792

The acquisition of Synergy has been accounted for using the acquisition method of accounting which requires, among other things, the assets acquired, liabilities assumed and noncontrolling interests be recognized at their respective fair values as of the acquisition date. Acquisition accounting is dependent upon certain valuations and other studies that are in progress and are not yet to a stage where there is sufficient information for a definitive measurement. The process for estimating the fair values of identifiable intangible assets and certain tangible assets and assumed liabilities requires the use of judgment in determining the appropriate assumptions and estimates.

The purchase price allocation for Synergy is preliminary. As we finalize the fair values of assets acquired, liabilities assumed, and noncontrolling interests, additional purchase price adjustments will be recorded during the measurement period. Fair value estimates are based on a complex series of judgments about future events and uncertainties and rely heavily on estimates and assumptions. The judgments used to determine the estimated fair value assigned to each class of assets acquired and liabilities assumed, as well as asset lives, can materially impact our results of operations. The finalization of the purchase accounting assessment will result in changes in the valuation of assets acquired and liabilities assumed and may have a material impact on the our results of operations and financial position. Goodwill will be allocated to the Healthcare Products, Healthcare Specialty Services, and Applied Sterilization Technologies segments. Goodwill is the excess of the consideration transferred over the net assets recognized and represents the expected revenue and cost synergies of the combined company and assembled workforce, which are further described above. Goodwill recognized as a result of the acquisition is not deductible for tax purposes.

19. Subsequent Events

On July 1, 2016 we sold our UK Linen Management Services business to STAR Mayan Limited for approximately £50.0 million. For fiscal year 2017, the UK Linen Management Services business was expected to generate approximately £40.0 million in revenue. The UK Linen Management Services business was part of our Healthcare Specialty Services segment.

On July 22, 2016 we acquired Medisafe Holdings Ltd, a U.K. manufacturer of washer/disinfector equipment and related consumables and services for approximately £27.0 million. On an annual basis, the Medisafe product line generates approximately £14.0 million in revenue. The acquisition of Medisafe provides washer manufacturing and research and development in the U.K., and Medisafe's products and services complement our Healthcare product offering. Medisafe will be integrated into our Healthcare Product segment.

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Report of Independent Registered Public Accounting Firm

Board of Directors and Shareholders of STERIS plc

We have reviewed the consolidated balance sheet of STERIS plc and subsidiaries (“STERIS”) as of June 30, 2016, and the related consolidated statements of income, comprehensive income and cash flows for the three-month periods ended June 30, 2016 and 2015. These 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 consolidated financial statements referred to above for them to be in conformity with U.S. generally accepted accounting principles.

We have previously audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the consolidated balance sheet of STERIS plc and subsidiaries as of March 31, 2016, and the related consolidated statements of income, comprehensive income, shareholders' equity and cash flows for the year then ended (not presented herein) and we expressed an unqualified audit opinion on those consolidated financial statements in our report dated May 31, 2016. In our opinion, the accompanying consolidated balance sheet of STERIS plc and subsidiaries as of March 31, 2016, is fairly stated, in all material respects, in relation to the consolidated balance sheet from which it has been derived.

/s/ Ernst & Young LLP

Cleveland, Ohio
August 9, 2016

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

Introduction

In Management's Discussion and Analysis of Financial Condition and Results of Operations (the "MD&A"), we explain the general financial condition and the results of operations for STERIS including:

- what factors affect our business;
- what our earnings and costs were in each period presented;
- why those earnings and costs were different from prior periods;
- where our earnings came from;
- how this affects our overall financial condition;
- what our expenditures for capital projects were; and
- where cash will come from to fund future debt principal repayments, growth outside of core operations, repurchases of shares, pay cash dividends and fund future working capital needs.

As you read the MD&A, it may be helpful to refer to information in our consolidated financial statements, which present the results of our operations for the first quarter of fiscal 2017 and fiscal 2016. It may also be helpful to read the MD&A in our Annual Report on Form 10-K for the year ended March 31, 2016, dated May 31, 2016. In the MD&A, we analyze and explain the period-over-period changes in the specific line items in the Consolidated Statements of Income. Our analysis may be important to you in making decisions about your investments in STERIS.

Financial Measures

In the following sections of the MD&A, we may, at times, refer to financial measures that are not required to be presented in the consolidated financial statements under U.S. GAAP. We sometimes use the following financial measures in the context of this report: backlog; debt-to-total capital; net debt-to-total capital; and days sales outstanding. We define these financial measures as follows:

- Backlog – We define backlog as the amount of unfilled capital equipment purchase orders at a point in time. We use this figure as a measure to assist in the projection of short-term financial results and inventory requirements.
- Debt-to-total capital – We define debt-to-total capital as total debt divided by the sum of total debt and shareholders' equity. We use this figure as a financial liquidity measure to gauge our ability to borrow and fund growth.
- Net debt-to-total capital – We define net debt-to-total capital as total debt less cash ("net debt") divided by the sum of net debt and shareholders' equity. We also use this figure as a financial liquidity measure to gauge our ability to borrow and fund growth.
- Days sales outstanding ("DSO") – We define DSO as the average collection period for accounts receivable. It is calculated as net accounts receivable divided by the trailing four quarters' revenues, multiplied by 365 days. We use this figure to help gauge the quality of accounts receivable and expected time to collect.

We, at times, may also refer to other financial measures which are considered to be "non-GAAP financial measures" under SEC rules. We have presented these financial measures because we believe that meaningful analysis of our financial performance is enhanced by an understanding of certain additional factors underlying that performance. These financial measures should not be considered an alternative to measures required by accounting principles generally accepted in the United States. Our calculations of these measures may differ from calculations of similar measures used by other companies and you should be careful when comparing these financial measures to those of other companies. Additional information regarding these financial measures, including reconciliations of each non-GAAP financial measure, is available in the subsection of MD&A titled, "Non-GAAP Financial Measures."

Revenues – Defined

As required by Regulation S-X, we separately present revenues generated as either product revenues or service revenues on our Consolidated Statements of Income for each period presented. When we discuss revenues, we may, at times, refer to revenues summarized differently than the Regulation S-X requirements. The terminology, definitions, and applications of terms that we use to describe revenues may be different from terms used by other companies. We use the following terms to describe revenues:

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- Revenues – Our revenues are presented net of sales returns and allowances.
- Product Revenues – We define product revenues as revenues generated from sales of consumable and capital equipment products.
- Service Revenues – We define service revenues as revenues generated from parts and labor associated with the maintenance, repair, and installation of our capital equipment. Service revenues also include hospital sterilization services, instrument and scope repairs, and linen management as well as revenues generated from contract sterilization and laboratory services offered through our Applied Sterilization Technologies segment.
- Capital Revenues – We define capital revenues as revenues generated from sales of capital equipment, which includes steam sterilizers, low temperature liquid chemical sterilant processing systems, including SYSTEM 1 and 1E, washing systems, VHP® technology, water stills, and pure steam generators; surgical lights and tables; and integrated OR.
- Consumable Revenues – We define consumable revenues as revenues generated from sales of the consumable family of products, which includes SYSTEM 1 and 1E consumables, V-Pro consumables, gastrointestinal endoscopy accessories, sterility assurance products, skin care products, cleaning consumables, surgical instruments, and barrier products.
- Recurring Revenues – We define recurring revenues as revenues generated from sales of consumable products and service revenues.

General Company Overview and Executive Summary

STERIS plc, a public limited company organized under the laws of England and Wales, was incorporated on October 9, 2014 as a private limited company under the name New STERIS Limited and was re-registered effective November 2, 2015 as a public limited company under the name STERIS plc. New STERIS Limited was established to effect the combination ("Combination") of STERIS Corporation, an Ohio corporation ("Old STERIS"), and Synergy Health plc, a public limited company organized under the laws of the England and Wales ("Synergy"). This Combination closed on November 2, 2015 and as a result STERIS plc became the ultimate parent company of Old STERIS and Synergy. Synergy has been re-registered under the name Synergy Health Limited. The Combination was accounted for in the consolidated financial statements as a merger between entities under common control; accordingly the historical consolidated financial statements of Old STERIS for periods prior to November 2, 2015 are considered to be the historical financial statements of STERIS plc.

Due to the timing of the closing of the Combination, the results of Synergy are only reflected in the results of operations of the Company from November 2, 2015 forward, which will affect comparability to the prior period historical operations of the Company throughout this quarterly report on Form 10-Q.

As a result of the Combination, we have reorganized our operations into four reportable business segments: Healthcare Products, Healthcare Specialty Services, Life Sciences, and Applied Sterilization Technologies. We describe our business segments in note 10 to our consolidated financial statements titled, "Business Segment Information."

Our mission is to help our Customers create a healthier and safer world by providing innovative healthcare and life science product and service solutions around the globe. Our dedicated employees around the world work together to supply a broad range of solutions by offering a combination of capital equipment, consumables, medical devices and services to healthcare, pharmaceutical, industrial, and governmental Customers.

The bulk of our revenues are derived from the healthcare and pharmaceutical industries. Much of the growth in these industries is driven by the aging of the population throughout the world, as an increasing number of individuals are entering their prime healthcare consumption years, and is dependent upon advancement in healthcare delivery, acceptance of new technologies, government policies, and general economic conditions. In addition, each of our core industries is experiencing specific trends that could increase demand. Within healthcare, there is increased concern regarding the level of hospital-acquired infections around the world. The pharmaceutical industry has been impacted by increased FDA scrutiny of cleaning and validation processes, mandating that manufacturers improve their processes. The aging population increases the demand for medical procedures, which increases the consumption of single use medical devices and surgical kits processed by our Applied Sterilization Technologies segment.

We are actively pursuing new opportunities to adapt our proven technologies to meet the changing needs of the global marketplace. We are also pursuing a strategy of expanding into adjacent markets by seeking acquisition targets in the Healthcare Products, Healthcare Specialty Services and Life Sciences segments.

Fiscal 2017 first quarter revenues were $638.4 million, representing an increase of 45.1% over the fiscal 2016 first quarter revenues of $439.9 million, reflecting growth within all reportable business segments including growth resulting from the Combination.

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Fiscal 2017 first quarter gross margin percentage was 37.6% compared with 41.8% for the fiscal 2016 first quarter. As anticipated, the addition of Synergy's hospital sterilization services and linen management businesses is a key factor in the declines in gross margin percentages. Gross margin percentages in the first quarter of fiscal 2017 were favorably impacted by favorable currency movements and the suspension of the Medical Device excise tax.

Fiscal 2017 first quarter operating income was $73.5 million, compared to fiscal 2016 first quarter operating income of $44.2 million. The year over year increase is attributable to recent acquisitions, including the Combination, along with growth in all reportable business segments.

Cash flows from operations were $80.3 million and free cash flow was $49.5 million in the first three months of fiscal 2017 compared to cash flows from operations of $41.2 million and free cash flow $17.7 million in the first three months of fiscal 2016, respectively (see the subsection below titled "Non-GAAP Financial Measures") for additional information and related reconciliation of cash flows from operations to free cash flow). The higher cash flow from operations and free cash flow as compared to the prior year period are primarily due to higher net income. Our debt-to-total capital ratio was 33.8% at June 30, 2016 and 34.2% at March 31, 2016. During the first three months of fiscal 2017, we declared and paid quarterly cash dividends of $0.25 per ordinary share.

Additional information regarding our fiscal 2017 first quarter financial performance is included in the subsection below titled “Results of Operations.”

Matters Affecting Comparability

International Operations. Since we conduct operations outside of the United States using various foreign currencies, our operating results are impacted by foreign currency movements relative to the U.S. dollar. During the first quarter of fiscal 2017, our revenues were unfavorably impacted by $1.8 million, or 0.4%, and income before taxes was favorably impacted by $2.8 million, or 5.5%, as a result of foreign currency movements relative to the U.S. dollar.

NON-GAAP FINANCIAL MEASURES

We, at times, refer to financial measures which are considered to be “non-GAAP financial measures” under SEC rules. We, at times, also refer to our results of operations excluding certain transactions or amounts that are non-recurring or are not indicative of future results, in order to provide meaningful comparisons between the periods presented. These non-GAAP financial measures are not intended to be, and should not be, considered separately from or as an alternative to the most directly comparable GAAP financial measures.

These non-GAAP financial measures are presented with the intent of providing greater transparency to supplemental financial information used by management and the Board of Directors in their financial analysis and operational decision-making. These amounts are disclosed so that the reader has the same financial data that management uses with the belief that it will assist investors and other readers in making comparisons to our historical operating results and analyzing the underlying performance of our operations for the periods presented.

We believe that the presentation of these non-GAAP financial measures, when considered along with our GAAP financial measures and the reconciliation to the corresponding GAAP financial measures, provide the reader with a more complete understanding of the factors and trends affecting our business than could be obtained absent this disclosure. It is important for the reader to note that the non-GAAP financial measure used may be calculated differently from, and therefore may not be comparable to, a similarly titled measure used by other companies.

We define free cash flow as net cash provided by operating activities as presented in the Consolidated Statements of Cash Flows less purchases of property, plant, equipment, and intangibles plus proceeds from the sale of property, plant, equipment, and intangibles, which are also presented in the Consolidated Statements of Cash Flows. We use this as a measure to gauge our ability to fund future debt principal repayments, growth outside of core operations, repurchase shares, and pay cash dividends. The following table summarizes the calculation of our free cash flow for the three month periods ended June 30, 2016 and 2015:

	Three Months Ended June 30,

(dollars in thousands)	2016	2015
Net cash provided by operating activities	$80,316	$41,153
Purchases of property, plant, equipment and intangibles, net	(35,357)	(23,518)
Proceeds from the sale of property, plant, equipment and intangibles	4,526	28
Free cash flow	$49,485	$17,663

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Results of Operations

In the following subsections, we discuss our earnings and the factors affecting them for the first quarter of fiscal 2017 compared with the same fiscal 2016 period. We begin with a general overview of our operating results and then separately discuss earnings for our operating segments.

Revenues. The following table compares our revenues for the three months ended June 30, 2016 to the revenues for the three months ended June 30, 2015:

(dollars in thousands)	Three Months Ended June 30, 2016	2015	Change	Percent Change
Total revenues	$638,378	$439,902	$198,476	45.1 %
Revenues by type:				
Capital equipment revenues	126,085	118,220	7,865	6.7 %
Consumable revenues	145,665	114,087	31,578	27.7 %
Service revenues	366,628	207,595	159,033	76.6 %
Revenues by geography:				
United Kingdom revenues	70,439	10,168	60,271	592.8 %
United States revenues	428,105	360,469	67,636	18.8 %
Other foreign revenues	139,834	69,265	70,569	101.9 %

Revenues increased $198.5 million, or 45.1%, to $638.4 million for the quarter ended June 30, 2016, as compared to $439.9 million for the same quarter in the prior year. This increase is attributable to recent acquisitions including the Combination with Synergy along with growth in all reportable business segments. Recent acquisitions contributed 39.3% and impacted all three revenue types.

Capital equipment revenues increased 6.7% in the first quarter of fiscal 2017, as compared to the first quarter of fiscal 2016. Most of the capital equipment revenues increase was in the United States although revenues also increased in the EMEA and Asia Pacific regions. Consumable revenues increased 27.7% for the quarter ended June 30, 2016, as compared to the prior year quarter, due to recent acquisitions, along with strong growth in both the Healthcare Products and Life Sciences segments. Recent acquisitions contributed 18.4% of the consumable revenues increase. Service revenues increased 76.6% in the first quarter of fiscal 2017 driven by the Combination with Synergy and organic growth in all reportable business segments.

United Kingdom revenues increased $60.3 million, or 592.8%, to $70.4 million for the quarter ended June 30, 2016, as compared to $10.2 million for the same prior year quarter. This increase reflects growth in both consumable and service revenues and is primarily attributable to the Combination with Synergy.

United States revenues increased $67.6 million, or 18.8%, to $428.1 million for the quarter ended June 30, 2016, as compared to $360.5 million for the same prior year quarter. This increase reflects year over year growth of 6%, 19% and 24% in capital equipment, consumable and service revenues, respectively. The increases are attributable to acquisitions, including the Combination with Synergy, as well as organic growth.

Revenue from other foreign locations increased $70.6 million, or 101.9%, to $139.8 million for the quarter ended June 30, 2016, as compared to $69.3 million for the same prior year quarter. This increase reflects growth in the EMEA outside of the United Kingdom, as well as in the Asia Pacific and Latin American regions. The Combination with Synergy was a significant driver of the growth in the EMEA outside of the United Kingdom.

Revenues by segment are further discussed in the section of the MD&A titles, "Business Segment Results of Operations."

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Gross Profit. The following table compares our gross profit for the three months ended June 30, 2016 to the three months ended June 30, 2015:

(dollars in thousands)	Three Months Ended June 30, 2016	2015	Change	Percent Change
Gross profit:				
Product	$129,052	$102,451	$26,601	26.0 %
Service	110,938	81,639	29,299	35.9 %
Total gross profit	$239,990	$184,090	$55,900	30.4 %
Gross profit percentage:				
Product	47.5 %	44.1 %		
Service	30.3 %	39.3 %		
Total gross profit percentage	37.6 %	41.8 %		

Our gross margin percentage is affected by the volume, pricing, and mix of sales of our products and services, as well as the costs associated with the products and services that are sold. Gross margin increased $55.9 million and declined 420 basis points as a percentage of revenues in the fiscal 2017 first quarter as compared to the fiscal 2016 first quarter. The increase in product gross profit percentage is attributable to favorable foreign currency rate movements, the suspension of the Medical Device Excise Tax, and a shift towards higher margin consumable products. As anticipated, the addition of Synergy's hospital sterilization services and linen management businesses is a key factor in the decline in the service gross profit percentage.

Operating Expenses. The following table compares our operating expenses for the three months ended June 30, 2016 to the three months ended June 30, 2015:

(dollars in thousands)	Three Months Ended June 30, 2016	2015	Change	Percent Change
Operating expenses:				
Selling, general, and administrative	$151,886	$126,835	$25,051	19.8 %
Research and development	14,428	13,765	663	4.8 %
Restructuring expenses	154	(726)	880	NM
Total operating expenses	$166,468	$139,874	$26,594	19.0 %

NM - Not meaningful.

Selling, General, and Administrative Expenses. Significant components of total selling, general, and administrative expenses ("SG&A") are compensation and benefit costs, fees for professional services, travel and entertainment, facilities costs, and other general and administrative expenses. SG&A increased 19.8% in the first quarter of fiscal 2017 over the first quarter of fiscal 2016.The increase is primarily attributable to amortization of acquired intangible assets, associated with recently acquired businesses, which was partially offset by a decrease in acquisition and integration costs related to recent acquisitions, including Synergy.

For the three month period ended June 30, 2016, research and development expenses increased 4.8% over the same prior year period. The increase in the fiscal 2017 three month period is primarily attributable to additional spending in connection with the development of healthcare and Life Sciences products and accessories. Research and development expenses are influenced by the number and timing of in-process projects and labor hours and other costs associated with these projects. Our research and development initiatives continue to emphasize new product development, product improvements, and the development of new technological platform innovations. During the first quarter of fiscal 2017, our investments in research and development continued to be focused on, but were not limited to, enhancing capabilities of sterile processing combination technologies, procedural products and accessories, and devices and support accessories used in gastrointestinal endoscopy procedures.

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

Since the inception of the Fiscal 2014 Restructuring Plan, we have incurred pre-tax expenses totaling $19.1 million related to these actions, of which $11.0 million was recorded as restructuring expenses and $8.1 million was recorded in cost of revenues. These actions are intended to enhance profitability and improve efficiencies. We do not expect to incur any significant additional restructuring expenses related to this plan.

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

Three Months Ended June 30, 2016 (dollars in thousands)	Fiscal 2014 Restructuring Plan
Lease termination obligation and other	$ 154
Total restructuring expenses	$ 154

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

Three Months Ended June 30, 2015 (dollars in thousands)	Fiscal 2014 Restructuring Plan (1)
Severance and other compensation related costs	$ (806)
Lease termination obligation and other	80
Product rationalization	277
Total restructuring expenses	$ (449)

(1) Includes $277 in expense recorded in cost of revenues on Consolidated Statements of Income.

Non-Operating Expenses, Net. Non-operating expenses, net consists of interest expense on debt, offset by interest earned on cash, cash equivalents, short-term investment balances, and other miscellaneous income. The following table compares our net non-operating expenses for the three months ended June 30, 2016 and 2015:

	Three Months Ended June 30,		
(dollars in thousands)	2016	2015	Change
Non-operating expenses, net:			
Interest expense	$11,071	$6,120	$4,951
Interest income and miscellaneous expense	(493)	(482)	(11)
Non-operating expenses, net	$10,578	$5,638	$4,940

Interest expense during fiscal 2017 increased due to higher interest costs resulting from our May 2015 issuance of senior notes in a private placement offering, additional borrowings under our credit facilities to fund acquisitions, including the Combination and the operations of acquired companies, and payments associated with paying off Synergy's debt. Year over year our weighted average cost of borrowing has decreased due to an increase in the proportion of lower-cost, variable-rate bank debt. Interest income and miscellaneous expense is immaterial.

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Income Tax Expense. The following table compares our income tax expense and effective income tax rates for the three months ended June 30, 2016 to the three months ended June 30, 2015:

	Three Months Ended June 30,		Change	Percent Change
(dollars in thousands)	2016	2015		
Income tax expense	$14,234	$14,267	$ (33)	(0.2)%
Effective income tax rate	22.6 %	37.0 %		

The effective income tax rate for continuing operations for the three month period ended June 30, 2016 was 22.6% compared with 37.0% for the same prior year period. The first quarter of fiscal 2017 was favorably impacted by benefits achieved in conjunction with the Synergy transaction and the adoption of ASU 2016-09: "Stock Compensation: Improvements to Employee Share-Based Payment Accounting" (Topic 718).

We record income tax expense during interim periods based on our estimate of the annual effective income tax rate, adjusted each quarter for discrete items. We analyze various factors to determine the estimated annual effective income tax rate, including projections of our annual earnings and taxing jurisdictions in which the earnings will be generated, the impact of state and local income taxes, our ability to use tax credits and net operating loss carryforwards, and available tax planning alternatives.

Business Segment Results of Operations. As a result of the Combination with Synergy, we have reassessed the organization of our business. We have concluded that we operate and should report in four reportable business segments: Healthcare Products, Healthcare Specialty Serv