BOSTON SCIENTIFIC CORP
Form 10-Q
November 05, 2013
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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549
FORM 10-Q

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

For the quarterly period ended September 30, 2013
OR

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

Commission File No. 1-11083
BOSTON SCIENTIFIC CORPORATION
(Exact name of registrant as specified in its charter)

DELAWARE	04-2695240
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)

ONE BOSTON SCIENTIFIC PLACE, NATICK, MASSACHUSETTS 01760-1537
(Address of principal executive offices) (zip code)
(508) 650-8000
(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 þ No o

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

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

Class	Shares outstanding as of October 31, 2013
Common Stock, $.01 par value	1,335,221,407

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PART I
FINANCIAL INFORMATION

ITEM 1. CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

BOSTON SCIENTIFIC CORPORATION AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS (UNAUDITED)

in millions, except per share data	Three Months Ended September 30, 2013	Three Months Ended September 30, 2012	Nine Months Ended September 30, 2013	Nine Months Ended September 30, 2012
Net sales	$1,735	$1,735	$5,305	$5,428
Cost of products sold	510	558	1,618	1,767
Gross profit	1,225	1,177	3,687	3,661
Operating expenses:				
Selling, general and administrative expenses	658	589	1,950	1,895
Research and development expenses	217	220	644	648
Royalty expense	28	29	115	125
Amortization expense	101	99	305	294
Goodwill impairment charges	—	748	423	4,350
Intangible asset impairment charges	—	13	53	142
Contingent consideration (benefit) expense	23	(20)	(18)	(9)
Restructuring charges	19	54	55	93
Litigation-related charges	76	50	206	119
Gain on divestiture	—	(11)	(40)	(11)
	1,122	1,771	3,693	7,646
Operating income (loss)	103	(594)	(6)	(3,985)
Other income (expense):				
Interest expense	(137)	(65)	(266)	(197)
Other, net	(6)	(4)	(10)	23
Income (loss) before income taxes	(40)	(663)	(282)	(4,159)
Income tax expense (benefit)	(35)	1	(53)	(30)
Net income (loss)	$(5)	$(664)	$(229)	$(4,129)
Net income (loss) per common share — basic	$0.00	$(0.48)	$(0.17)	$(2.91)
Net income (loss) per common share — assuming dilution	$0.00	$(0.48)	$(0.17)	$(2.91)
Weighted-average shares outstanding				
Basic	1,340.3	1,392.5	1,345.2	1,420.3
Assuming dilution	1,340.3	1,392.5	1,345.2	1,420.3

See notes to the unaudited condensed consolidated financial statements.

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BOSTON SCIENTIFIC CORPORATION AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME (LOSS) (UNAUDITED)

	Three Months Ended September 30,		Nine Months Ended September 30,	
(in millions)	2013	2012	2013	2012
Net income (loss)	$(5)	$(664)	$(229)	$(4,129)
Other comprehensive income:				
Foreign currency translation adjustment	10	2	8	9
Net change in unrealized gains and losses on derivative financial instruments, net of tax	(38)	(27)	81	17
Total other comprehensive income (loss)	(28)	(25)	89	26
Total comprehensive income (loss)	$(33)	$(689)	$(140)	$(4,103)

See notes to the unaudited condensed consolidated financial statements.

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BOSTON SCIENTIFIC CORPORATION AND SUBSIDIARIES
CONDENSED CONSOLIDATED BALANCE SHEETS

in millions, except share and per share data	As of September 30, 2013 (Unaudited)	December 31, 2012
ASSETS		
Current assets:		
Cash and cash equivalents	$571	$207
Trade accounts receivable, net	1,238	1,217
Inventories	895	884
Deferred income taxes	536	433
Prepaid expenses and other current assets	285	281
Total current assets	3,525	3,022
Property, plant and equipment, net	1,530	1,564
Goodwill	5,553	5,973
Other intangible assets, net	5,936	6,289
Other long-term assets	373	306
	$16,917	$17,154
LIABILITIES AND STOCKHOLDERS’ EQUITY		
Current liabilities:		
Current debt obligations	$3	$4
Accounts payable	238	232
Accrued expenses	1,346	1,284
Other current liabilities	315	252
Total current liabilities	1,902	1,772
Long-term debt	4,246	4,252
Deferred income taxes	1,623	1,713
Other long-term liabilities	2,583	2,547
Commitments and contingencies		
Stockholders’ equity		
Preferred stock, $.01 par value - authorized 50,000,000 shares, none issued and outstanding		
Common stock, $.01 par value - authorized 2,000,000,000 shares and issued 1,557,892,509 shares as of September 30, 2013 and 1,542,347,188 shares as of December 31, 2012	16	15
Treasury stock, at cost - 219,056,477 shares as of September 30, 2013 and 186,635,532 shares as of December 31, 2012	(1,367)	(1,092)
Additional paid-in capital	16,536	16,429
Accumulated deficit	(8,678)	(8,449)
Accumulated other comprehensive income (loss), net of tax	56	(33)
Total stockholders’ equity	6,563	6,870
	$16,917	$17,154

See notes to the unaudited condensed consolidated financial statements.

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BOSTON SCIENTIFIC CORPORATION AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS (UNAUDITED)

	Nine Months Ended September 30,	
in millions	2013	2012
Cash provided by operating activities	$809	$891
Investing activities:		
Purchases of property, plant and equipment	(161)	(164)
Proceeds from sale of property, plant and equipment	53	—
Purchases of privately held securities	(13)	—
Purchase of notes receivable	(8)	—
Payments for acquisitions of businesses, net of cash acquired	—	(134)
Payments for investments in companies and acquisitions of certain technologies	(13)	(18)
Proceeds from business divestitures, net of costs	30	10
Cash used for investing activities	(112)	(306)
Financing activities:		
Payments on long-term borrowings	(1,450)	(9)
Proceeds from long-term borrowings, net of debt issuance costs	1,440	—
Payments on borrowings from credit facilities	(240)	(260)
Proceeds from borrowings on credit facilities	240	251
Payment of contingent consideration	(107)	(4)
Payments for acquisitions of treasury stock	(275)	(500)
Proceeds from issuances of shares of common stock	59	20
Cash used for financing activities	(333)	(502)
Effect of foreign exchange rates on cash	—	2
Net increase in cash and cash equivalents	364	85
Cash and cash equivalents at beginning of period	207	267
Cash and cash equivalents at end of period	$571	$352
Supplemental Information		
Non-cash operating activities:		
Stock-based compensation expense	$77	$85

See notes to the unaudited condensed consolidated financial statements.

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NOTES TO THE CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

NOTE A – BASIS OF PRESENTATION

The accompanying unaudited condensed consolidated financial statements of Boston Scientific Corporation have been prepared in accordance with accounting principles generally accepted in the United States (U.S. GAAP) and with the instructions to Form 10-Q and Article 10 of Regulation S-X. Accordingly, they do not include all of the information and footnotes required by U.S. GAAP for complete financial statements. In the opinion of management, all adjustments (consisting only of normal recurring adjustments) considered necessary for fair presentation have been included. Operating results for the three and nine months ended September 30, 2013 are not necessarily indicative of the results that may be expected for the year ending December 31, 2013. For further information, refer to the consolidated financial statements and footnotes thereto included in Item 8 of our 2012 Annual Report filed on Form 10-K.

Effective as of January 1, 2013, we reorganized our business from geographic regions to fully operationalized global business units. Our reorganization changed our reporting structure and changed the composition of our reporting units. As a result, we have reclassified certain prior year amounts to conform to the current year's presentation. See Note D - Goodwill and Other Intangible Assets and Note L – Segment Reporting for further details.

Subsequent Events

We evaluate events occurring after the date of our most recent accompanying unaudited condensed consolidated balance sheets for potential recognition or disclosure in our financial statements. We did not identify any material subsequent events requiring adjustment to our accompanying unaudited condensed consolidated financial statements (recognized subsequent events) for the three and nine month periods ended September 30, 2013. Those items requiring disclosure (unrecognized subsequent events) in the financial statements have been disclosed accordingly. Refer to Note J - Commitments and Contingencies and Note B - Acquisitions for more information.

NOTE B – ACQUISITIONS

We did not close any material acquisitions during the first nine months of 2013. On November 1, 2013, we completed the acquisition of the electrophysiology business of C.R. Bard Inc., for $275 million in cash. We believe that this transaction brings a strong commercial team and complementary portfolio of ablation catheters, diagnostic tools, and electrophysiology recording systems, and will allow us to better serve the global Electrophysiology market through a more comprehensive portfolio offering and sales infrastructure.

2012 Acquisition

Cameron Health, Inc.

On June 8, 2012, we completed the acquisition of the remaining equity of Cameron Health, Inc. (Cameron). Cameron has developed the world's first and only commercially available subcutaneous implantable cardioverter defibrillator - the S-ICD® system.

Our unaudited condensed consolidated financial statements include the operating results for the acquired entity from its date of acquisition. We do not present pro forma financial information for this acquisition given the results are not material to our consolidated financial statements. Transaction costs associated with this acquisition were expensed as incurred and were not material for the three and nine months ended September 30, 2013 and 2012.

Purchase Price Allocation

The components of the Cameron purchase price as of the acquisition date were as follows (in millions):

Cash, net of cash acquired	$134
Fair value of contingent consideration	259
Fair value of prior interests	79
Fair value of debt assumed	9
	$481

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Prior to the acquisition, we had an equity interest in Cameron and held $40 million of notes receivable. We re-measured our previously held investments to their estimated acquisition-date fair value of $79 million and recorded a gain of $39 million in other, net in the accompanying condensed consolidated statements of operations during the second quarter of 2012. We measured the fair values of the previously held investments based on the liquidation preferences and priority of the equity interests and debt, including accrued interest. In addition, we prepaid the assumed debt obligation of Cameron for approximately $9 million during the second quarter of 2012.

Total consideration includes an initial $150 million cash payment at closing of the transaction, a payment of $150 million upon FDA approval of the S-ICD® system and up to an additional $1.050 billion of potential payments upon achievement of specified revenue-based milestones through the third quarter of 2018, which represents the end of a six-year period following FDA approval. Due to our receipt of FDA approval of Cameron's S-ICD® system, we paid the related $150 million milestone payment to the former shareholders of Cameron during the fourth quarter of 2012.
The following summarizes the Cameron purchase price allocation (in millions):

Goodwill	$314
Amortizable intangible assets	42
Indefinite-lived intangible assets	48
Other net assets	1
Deferred income taxes	76
	$481

We allocated a portion of the Cameron purchase price to specific intangible asset categories as follows:

	Amount Assigned (in millions)	Weighted Average Amortization Period (in years)	Risk-Adjusted Discount Rates used in Purchase Price Allocation	
Amortizable intangible assets:				
Technology-related	40	11	14.0	%
Customer relationships	2	5	14.0	%
Indefinite-lived intangible assets:				
Purchased research and development	48		14.0	%
	90			

The technology-related intangible assets consist of technical processes, intellectual property, and institutional understanding with respect to products and processes that we expect to leverage in future products or processes and carry forward from one product generation to the next. The technology-related intangible assets are being amortized on a straight-line basis over their assigned estimated useful lives.

Purchased research and development represents the estimated fair value of acquired in-process research and development projects which have not yet reached technological feasibility. These indefinite-lived intangible assets are tested for impairment on an annual basis, or more frequently if impairment indicators are present, in accordance with U.S. GAAP and our accounting policies described in our 2012 Annual Report filed on Form 10-K. Upon completion of the associated research and development efforts, we determine the useful life of the technology and begin amortizing the assets to reflect their use over their remaining lives. Upon receiving FDA approval for Cameron's S-ICD® system in September 2012, we reclassified approximately $47 million of in-process research and development (IPR&D) to technology-related amortizable intangible assets. The total estimated costs to complete the remaining IPR&D program associated with Cameron are immaterial.
We believe that the estimated intangible asset values represent the fair value at the date of acquisition and do not exceed the amount a third party would pay for the assets. We used the income approach, specifically the discounted

cash flow method and excess earnings method, to derive the fair value of the amortizable intangible assets and purchased research and development. These fair value measurements are based on significant unobservable inputs, including management estimates and assumptions and, accordingly, are classified as Level 3 within the fair value hierarchy prescribed by ASC Topic 820, Fair Value Measurements and Disclosures.

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We recorded the excess of the aggregate purchase price over the estimated fair values of the identifiable assets acquired as goodwill, which is non-deductible for tax purposes. Goodwill was established due primarily to revenue and cash flow projections associated with future technologies, as well as synergies expected to be gained from the integration of this business into our Cardiac Rhythm Management (CRM) business and was allocated to our former geographic reportable segments based on the relative expected benefit from the business combination. Effective as of January 1, 2013, we reorganized our business from geographic regions to fully operationalized global business units. Our reorganization changed our reporting structure and changed the composition of our reporting units for goodwill impairment testing purposes. Following the reorganization, based on information regularly reviewed by our chief operating decision maker, we have three new global reportable segments consisting of: Cardiovascular, Rhythm Management, and MedSurg. See Note D - Goodwill and Other Intangible Assets for further details.

Contingent Consideration

Certain of our acquisitions involve contingent consideration arrangements. Payment of additional consideration is generally contingent on the acquired company reaching certain performance milestones, including attaining specified revenue levels, achieving product development targets or obtaining regulatory approvals. In accordance with U.S. GAAP, we recognize a liability equal to the fair value of the contingent payments we expect to make as of the acquisition date. We remeasure this liability each reporting period and record changes in the fair value through a separate line item within our consolidated statements of operations.

We recorded a net expense related to the change in fair value of our contingent consideration liabilities of $23 million in the third quarter of 2013 and a net benefit of $18 million in the first nine months of 2013, and recorded $20 million and $9 million of a net benefit during the third quarter and first nine months of 2012, respectively. We paid $100 million and $115 million in the third quarter and first nine months of 2013, respectively, we did not make any payments in the third quarter of 2012 and made payments of $4 million during the first nine months of 2012. As of September 30, 2013, the maximum amount of future contingent consideration (undiscounted) that we could be required to pay is approximately $2.179 billion.

Changes in the fair value of our contingent consideration liability were as follows (in millions):

Balance as of December 31, 2012	$(663	)
Amounts recorded to acquisition purchase accounting	(6	)
Net fair value adjustments	18	
Payments made	115	
Balance as of September 30, 2013	$(536	)

Contingent consideration liabilities are remeasured to fair value each reporting period using projected revenues, discount rates, probabilities of payment and projected payment dates. The recurring Level 3 fair value measurements of our contingent consideration liability include the following significant unobservable inputs:

Contingent Consideration Liability	Fair Value as of September 30, 2013	Valuation Technique	Unobservable Input	Range
Research and Development, Regulatory and Commercialization-based Milestones	$126 million	Probability Weighted Discounted Cash Flow	Discount Rate	0.8% - 1.1%
			Probability of Payment	70% - 98%
			Projected Year of Payment	2013 - 2014
Revenue-based Payments	$144 million	Discounted Cash Flow	Discount Rate	12% - 18%
			Probability of Payment	15% - 100%
			Projected Year of Payment	2013 - 2018
	$266 million	Monte Carlo	Revenue Volatility	13% - 28%
			Risk Free Rate	LIBOR Term Structure
			Projected Year of Payment	2013 - 2018

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Increases or decreases in the fair value of our contingent consideration liability can result from changes in discount periods and rates, as well as changes in the timing and amount of revenue estimates or in the timing or likelihood of achieving regulatory-, revenue- or commercialization-based milestones. Projected contingent payment amounts related to research and development, regulatory- and commercialization-based milestones and certain revenue-based milestones are discounted back to the current period using a discounted cash flow (DCF) model. Other revenue-based payments are valued using a Monte Carlo valuation model, which simulates future revenues during the earn out-period using management's best estimates. Projected revenues are based on our most recent internal operational budgets and long-range strategic plans. Increases in projected revenues and probabilities of payment may result in higher fair value measurements. Increases in discount rates and the time to payment may result in lower fair value measurements. Increases or decreases in any of those inputs in isolation may result in a significantly lower or higher fair value measurement.

NOTE C – DIVESTITURES

In January 2011, we closed the sale of our Neurovascular business to Stryker Corporation for a purchase price of $1.500 billion, $1.450 billion of which we received at closing. We received an additional $10 million during 2012, $30 million during the second quarter of 2013, and we will receive the final $10 million of consideration contingent upon the FDA approval of the transfer of certain manufacturing facilities.

Due to our continuing involvement in the operations of the Neurovascular business, the divestiture does not meet the criteria for presentation as a discontinued operation. Revenue generated by the Neurovascular business was $2 million in the third quarter of 2013, $56 million in the first nine months of 2013, $32 million in the third quarter of 2012, and $91 million in the first nine months of 2012.

NOTE D – GOODWILL AND OTHER INTANGIBLE ASSETS

The gross carrying amount of goodwill and other intangible assets and the related accumulated amortization for intangible assets subject to amortization and accumulated write-offs of goodwill as of September 30, 2013 and December 31, 2012 is as follows:

	As of September 30, 2013		December 31, 2012	
(in millions)	Gross Carrying Amount	Accumulated Amortization/ Write-offs	Gross Carrying Amount	Accumulated Amortization/ Write-offs
Amortizable intangible assets				
Technology-related	$8,118	$(3,254)	$8,020	$(3,005)
Patents	504	(322)	559	(352)
Other intangible assets	815	(465)	810	(428)
	$9,437	$(4,041)	$9,389	$(3,785)
Unamortizable intangible assets				
Goodwill	$15,453	$(9,900)	$15,450	$(9,477)
Technology-related	197	—	242	—
	$15,650	$(9,900)	$15,692	$(9,477)

During the third quarter of 2013, we reclassified approximately $45 million of core technology not previously subject to amortization to amortizable intangible assets due to projected changes in the market for this technology. We tested the intangible asset for impairment prior to this reclassification and determined that the asset was not impaired. In addition, we had $343 million and $443 million of purchased research and development intangible assets as of September 30, 2013 and December 31, 2012, respectively.

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2013 Reorganization

We assess goodwill for impairment at the reporting unit level, which is defined as an operating segment or one level below an operating segment, referred to as a component. Effective as of January 1, 2013, we reorganized our business from geographic regions to fully operationalized global business units. Our reorganization changed our reporting structure and changed the composition of our reporting units for goodwill impairment testing purposes. Following the reorganization, based on information regularly reviewed by our chief operating decision maker, we have three new global reportable segments consisting of: Cardiovascular, Rhythm Management, and MedSurg. We determined our new global reporting units by identifying our operating segments and assessing whether any components of these segments constituted a business for which discrete financial information is available and whether segment management regularly reviews the operating results of any components. Through this process, we identified the following new global reporting units effective as of January 1, 2013: Interventional Cardiology, Peripheral Interventions, Cardiac Rhythm Management (CRM), Electrophysiology, Endoscopy, Urology/Women's Health, and Neuromodulation.

To determine the amount of goodwill within our new global reporting units, on a relative fair value basis we reallocated $1.764 billion of goodwill previously allocated to our former Europe, Middle East and Africa (EMEA), Asia Pacific, Japan, and Americas international reporting units to our new global reporting units. In addition, we reallocated the goodwill previously allocated to the former U.S. divisional reporting units to each respective new global reporting unit, with the exception of the goodwill allocated to the former U.S. Cardiovascular reporting unit. The $2.380 billion of goodwill allocated to the former U.S. Cardiovascular reporting unit was reallocated between the new global Interventional Cardiology and global Peripheral Interventions reporting units on a relative fair value basis.

The following represents our goodwill balance by new global reportable segment. We restated the prior period information to conform to the current presentation:

(in millions)	Cardiovascular	Rhythm Management	MedSurg	Total
Balance as of December 31, 2012 (restated)	$3,249	$577	$2,147	$5,973
Purchase price adjustments	3	—	—	3
Goodwill acquired	—	—	—	—
Goodwill written off	—	(423)	—	(423)
Balance as of September 30, 2013	$3,252	$154	$2,147	$5,553

2013 Goodwill Impairment Testing and Charge

We test our goodwill balances during the second quarter of each year for impairment, or more frequently if indicators are present or changes in circumstances suggest that impairment may exist. Following our reorganization from regions to global business units and our reallocation of goodwill on a relative fair value basis, we conducted the first step of the goodwill impairment test for all new global reporting units as of January 1, 2013. The first step requires a comparison of the carrying value of the reporting units to the fair value of these units. The fair value of each new global reporting unit exceeded its carrying value, with the exception of the global CRM reporting unit. The global CRM reporting unit carrying value exceeded its fair value primarily due to the carrying value of its amortizable intangible assets. The carrying value of amortizable intangible assets allocated to the global CRM reporting unit was $4.636 billion as of January 1, 2013. In accordance with ASC Topic 350, Intangibles—Goodwill and Other (Topic 350), we tested the global CRM amortizable intangible assets for impairment in conjunction with the interim goodwill impairment test of our global CRM reporting unit. We performed the impairment analysis of the amortizable intangible assets on an undiscounted cash flow basis, and concluded that these assets were not impaired.

The second step of the goodwill impairment test compares the estimated fair value of a reporting unit’s goodwill to its carrying value. We performed the second step of the goodwill impairment test on the global CRM reporting unit and recorded a non-cash goodwill impairment charge of $423 million ($421 million after-tax) to write-down the goodwill to its implied fair value as of January 1, 2013. The primary driver of this impairment charge was our reorganization from geographic regions to global business units as of January 1, 2013, which changed the composition of our reporting units. As a result of the reorganization, any goodwill allocated to the global CRM reporting unit was no longer supported by the cash flows of other businesses. Under our former reporting unit structure, the goodwill

allocated to our regional reporting units was supported by the cash flows from all businesses in each international region. The hypothetical tax structure of the global CRM business and the global CRM business discount rate applied were also contributing factors to the goodwill impairment charge. We finalized the second step of the global CRM goodwill impairment test during the second quarter of 2013, in accordance with ASC Topic 350, Intangibles - Goodwill and Other, and determined that no adjustments to the charge were required. After recording the impairment charge in the first quarter of 2013, there was no remaining goodwill allocated to the global CRM reporting unit as of March 31, 2013.

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The goodwill impairment charge taken during the first quarter of 2013 was determined on a global CRM basis pursuant to our new organizational structure. We used the income approach, specifically the DCF method, to derive the fair value of the global CRM reporting unit. We completed a DCF model associated with our new global CRM business, including the amount and timing of future expected cash flows, tax attributes, the terminal value growth rate of approximately two percent and the appropriate market-participant risk-adjusted weighted average cost of capital (WACC) of approximately 12 percent.

In the second quarter of 2013, we performed our annual goodwill impairment test for all of our reporting units. In conjunction with our annual test, the fair value of each reporting unit exceeded its carrying value except CRM, for which no goodwill remains. Therefore, it was deemed not necessary to proceed to the second step of the impairment test. We have identified our global Neuromodulation reporting unit as being at higher risk of potential failure of the first step of the goodwill impairment test in future reporting periods. Our global Neuromodulation reporting unit holds $1.356 billion of allocated goodwill. The level of excess fair value over carrying value for this reporting unit identified during our annual goodwill impairment test was approximately 16 percent. Future changes in our reporting units or in the structure of our business as a result of future reorganizations, acquisitions or divestitures of assets or businesses could result in future impairments of goodwill within our reporting units including global CRM. Further, the recoverability of our CRM-related amortizable intangibles ($4.442 billion globally as of September 30, 2013) is sensitive to future cash flow assumptions and our global CRM business performance. The $4.442 billion of CRM-related amortizable intangibles are at higher risk of potential failure of the first step of the amortizable intangible recoverability test in future reporting periods. An impairment of a material portion of our CRM-related amortizable intangibles carrying value would occur if the second step of the amortizable intangible test is required in a future reporting period. Refer to Critical Accounting Policies and Estimates within our Management's Discussion and Analysis of Financial Condition and Results of Operations contained in Item 2 of this Quarterly Report on Form 10-Q for a discussion of key assumptions used in our testing.

On a quarterly basis, we monitor the key drivers of fair value to detect events or other changes that would warrant an interim impairment test of our goodwill and intangible assets. The key variables that drive the cash flows of our reporting units and amortizable intangibles are estimated revenue growth rates and levels of profitability. Terminal value growth rate assumptions, as well as the WACC rate applied are additional key variables for reporting unit cash flows. These assumptions are subject to uncertainty, including our ability to grow revenue and improve profitability levels. Relatively small declines in the future performance and cash flows of a reporting unit or asset group or small changes in other key assumptions may result in the recognition of significant asset impairment charges. For example, keeping all other variables constant, an increase in the WACC applied of 80 basis points or a 200 basis point decrease in the terminal value growth rate would require that we perform the second step of the goodwill impairment test for the global Neuromodulation reporting unit. The estimates used for our future cash flows and discount rates represent management's best estimates, which we believe to be reasonable, but future declines in business performance may impair the recoverability of our goodwill and intangible asset balances.

Future events that could have a negative impact on the levels of excess fair value over carrying value of our reporting units and/or amortizable intangible assets include, but are not limited to:

- decreases in estimated market sizes or market growth rates due to greater-than-expected declines in procedural volumes, pricing pressures, reductions in reimbursement levels, product actions, and/or competitive technology developments;
- declines in our market share and penetration assumptions due to increased competition, an inability to develop or launch new and next-generation products and technology features in line with our commercialization strategies, and market and/or regulatory conditions that may cause significant launch delays or product recalls;
- decreases in our forecasted profitability due to an inability to successfully implement and achieve timely and sustainable cost improvement measures consistent with our expectations, increases in our market-participant tax rate, and/or changes in tax laws;
- negative developments in intellectual property litigation that may impact our ability to market certain products or increase our costs to sell certain products;

- the level of success of on-going and future research and development efforts, including those related to recent acquisitions, and increases in the research and development costs necessary to obtain regulatory approvals and launch new products;
- the level of success in managing the growth of acquired companies, achieving sustained profitability consistent with our expectations, establishing government and third-party payer reimbursement, supplying the market, and increases in the costs and time necessary to integrate acquired businesses into our operations successfully;
- changes in our reporting units or in the structure of our business as a result of future reorganizations, acquisitions or divestitures of assets or businesses;

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- increases in our market-participant risk-adjusted WACC; and
- declines in revenue as a result of loss of key members of our sales force or other key personnel.

Negative changes in one or more of these factors, among others, could result in additional impairment charges.

2012 Charges

In the second quarter of 2012, we performed our annual goodwill impairment test for all of our reporting units and concluded that the goodwill within our former EMEA reporting unit was impaired and recorded a $3.602 billion ($3.579 billion after-tax) charge in the second quarter of 2012. As a result of revised estimates developed during our annual strategic planning process and analysis performed in conjunction with our annual goodwill impairment test, we concluded that the revenue growth rates projected for the EMEA reporting unit were slightly lower than our previous estimates primarily driven by macro-economic factors and our performance in the European market. We updated short-term operating projections based on our most recent strategic plan for EMEA prepared by management. We reduced the EMEA long-term growth rates and terminal value growth rate projections and increased the discount rate within our 15-year DCF model for EMEA by approximately 100 basis points due to increased risk associated with our projections in this market primarily as a result of economic uncertainty in Europe. In addition, our expectations for future growth and profitability were lowered as compared to our previous estimates and reflected declines in average selling prices and volume pressures due to austerity measures. The declines expected in the EMEA market did not impact our assumptions related to other reporting units.

In the third quarter of 2012, we performed an interim goodwill impairment test and recorded a non-cash $748 million (pre- and after-tax) charge associated with our former U.S. Cardiac Rhythm Management (U.S. CRM) reporting unit, primarily driven by a reduction in the estimated size of the U.S. CRM market, related adjustments to our business and other competitive factors, which led to lower projected U.S. CRM results compared to prior forecasts. The U.S. CRM market is dynamic, highly competitive and difficult to forecast; in the third quarter of 2012, we lowered our projections for the U.S. CRM market size and our future revenue levels within this market, primarily to reflect changes in expectations of average selling prices and unit growth, adjustments to our business and other competitive factors. The increased pricing pressure and lower unit volumes were primarily due to physician alignment with hospitals, efforts to reduce health care costs, focus on appropriate device usage, replacement volumes and competition, and were more impactful to the U.S. CRM business than previously estimated. In addition, we adjusted certain elements of our business and shifted investments to focus on areas expected to provide the highest future growth and financial return. As a result of these factors, we reduced the compound annual revenue growth rate of our 15 year DCF model for the U.S. CRM reporting unit by approximately 250 basis points. The declines expected in the U.S. CRM market did not impact our assumptions related to other reporting units.

The following is a rollforward of accumulated goodwill write-offs by global reportable segment. We restated the prior period information to conform to the current period presentation:

(in millions)	Cardiovascular	Rhythm Management	MedSurg	Total
Accumulated write-offs as of December 31, 2012 (restated)	$(1,479)	$(6,537)	$(1,461)	$(9,477)
Goodwill written off	—	(423)	—	(423)
Accumulated write-offs as of September 30, 2013	$(1,479)	$(6,960)	$(1,461)	$(9,900)

Intangible Asset Impairment Charges

On a quarterly basis, we monitor for events or other potential indicators of impairment that would warrant an interim impairment test of our intangible assets. See Goodwill Impairment Charges above for discussion of future events that could have a negative impact on the recoverability of our amortizable intangible assets.

2013 Charges

During the third quarter of 2013, we performed our annual impairment test of all in-process research and development projects, and our indefinite lived core technology assets, and recorded no impairments based on the results of our testing. These indefinite-lived intangible assets are tested for impairment on an annual basis, or more frequently if impairment indicators are present, in accordance with U.S. GAAP and our accounting policies described in our 2012 Annual Report filed on Form 10-K.

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During the second quarter of 2013 as a result of revised estimates developed in conjunction with our annual strategic planning process and annual goodwill impairment test, we performed an interim impairment test of our in-process research and development projects associated with certain of our acquisitions. Based on the results of our impairment analyses, we revised our expectations of the market size related to Sadra Medical, Inc. (Sadra), and the resulting timing and amount of future revenue and cash flows associated with the technology acquired from Sadra. As a result of these changes, we recorded pre-tax impairment charges of $51 million to write-down the balance of these intangible assets to their fair value during the second quarter of 2013. During the second quarter of 2013, we also recorded an additional $2 million intangible asset impairment charge associated with changes in the amount of the expected cash flows related to certain other acquired in-process research and development projects.

In-process research and development fair value is measured using projected revenues, projected expenses, discount rates, and
probability of expected launch. The nonrecurring Level 3 fair value measurements of the impairment analysis performed in the second quarter of 2013 included the following significant unobservable inputs:

Intangible Asset	Valuation Date	Fair Value	Valuation Technique	Unobservable Input	Rate
In-Process R&D	June 30, 2013	$178 million	Income Approach - Excess Earnings Method	Discount Rate	16.5%

2012 Charges

During the third quarter of 2012, we recorded a $13 million intangible asset impairment charge attributable to increased expectations in the cost to bring an in-process project to market in a certain geographic region and lower future revenue expectations associated with an in-process project. During the second quarter of 2012, we recorded a $129 million intangible asset impairment charge attributable to in-process research and development assets associated with Sadra due to revised expectations of the required effort, time and cost involved in completing the in-process projects and bringing the related products to market.

We recorded these amounts in the intangible assets impairment charges caption in our accompanying unaudited condensed consolidated statements of operations.

NOTE E – FAIR VALUE MEASUREMENTS

Derivative Instruments and Hedging Activities

We develop, manufacture and sell medical devices globally and our earnings and cash flows are exposed to market risk from changes in foreign currency exchange rates and interest rates. We address these risks through a risk management program that includes the use of derivative financial instruments, and operate the program pursuant to documented corporate risk management policies. We recognize all derivative financial instruments in our consolidated financial statements at fair value in accordance with ASC Topic 815, Derivatives and Hedging (Topic 815). In accordance with Topic 815, for those derivative instruments that are designated and qualify as hedging instruments, the hedging instrument must be designated, based upon the exposure being hedged, as a fair value hedge, cash flow hedge, or a hedge of a net investment in a foreign operation. The accounting for changes in the fair value (i.e. gains or losses) of a derivative instrument depends on whether it has been designated and qualifies as part of a hedging relationship and, further, on the type of hedging relationship. Our derivative instruments do not subject our earnings or cash flows to material risk, as gains and losses on these derivatives generally offset losses and gains on the item being hedged. We do not enter into derivative transactions for speculative purposes and we do not have any non-derivative instruments that are designated as hedging instruments pursuant to Topic 815.

Currency Hedging

We are exposed to currency risk consisting primarily of foreign currency denominated monetary assets and liabilities, forecasted foreign currency denominated intercompany and third-party transactions and net investments in certain subsidiaries. We manage our exposure to changes in foreign currency exchange rates on a consolidated basis to take advantage of offsetting transactions. We use both derivative instruments (currency forward contracts), and non-derivative transactions (primarily European manufacturing and distribution operations) to reduce the risk that our earnings and cash flows associated with these foreign currency denominated balances and transactions will be adversely affected by foreign currency exchange rate changes.

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Designated Foreign Currency Hedges

All of our designated currency hedge contracts outstanding as of September 30, 2013 and December 31, 2012 were cash flow hedges under Topic 815 intended to protect the U.S. dollar value of our forecasted foreign currency denominated transactions. We record the effective portion of any change in the fair value of foreign currency cash flow hedges in other comprehensive income (OCI) until the related third-party transaction occurs. Once the related third-party transaction occurs, we reclassify the effective portion of any related gain or loss on the foreign currency cash flow hedge to earnings. In the event the hedged forecasted transaction does not occur, or it becomes no longer probable that it will occur, we reclassify the amount of any gain or loss on the related cash flow hedge to earnings at that time. We had currency derivative instruments designated as cash flow hedges outstanding in the contract amount of $2.647 billion as of September 30, 2013 and $2.469 billion as of December 31, 2012.

We recognized net gains of $15 million in earnings on our cash flow hedges during the third quarter of 2013 and $15 million for the first nine months of 2013, as compared to net losses of $3 million during the third quarter of 2012 and $29 million for the first nine months of 2012. All currency cash flow hedges outstanding as of September 30, 2013 mature within 36 months. As of September 30, 2013, $113 million of net gains, net of tax, were recorded in accumulated other comprehensive income (AOCI) to recognize the effective portion of the fair value of any currency derivative instruments that are, or previously were, designated as foreign currency cash flow hedges, as compared to net gains of $31 million as of December 31, 2012. As of September 30, 2013, $58 million of net gains, net of tax, may be reclassified to earnings within the next twelve months.

The success of our hedging program depends, in part, on forecasts of transaction activity in various currencies (primarily Japanese yen, Euro, British pound sterling, Australian dollar and Canadian dollar). We may experience unanticipated currency exchange gains or losses to the extent that there are differences between forecasted and actual activity during periods of currency volatility. In addition, changes in foreign currency exchange rates related to any unhedged transactions may impact our earnings and cash flows.

Non-designated Foreign Currency Contracts

We use currency forward contracts as a part of our strategy to manage exposure related to foreign currency denominated monetary assets and liabilities. These currency forward contracts are not designated as cash flow, fair value or net investment hedges under Topic 815; are marked-to-market with changes in fair value recorded to earnings; and are entered into for periods consistent with currency transaction exposures, generally less than one year. We had currency derivative instruments not designated as hedges under Topic 815 outstanding in the contract amount of $1.757 billion as of September 30, 2013 and $1.942 billion as of December 31, 2012.

Interest Rate Hedging

Our interest rate risk relates primarily to U.S. dollar borrowings, partially offset by U.S. dollar cash investments. We have historically used interest rate derivative instruments to manage our earnings and cash flow exposure to changes in interest rates by converting floating-rate debt into fixed-rate debt or fixed-rate debt into floating-rate debt.

We designate these derivative instruments either as fair value or cash flow hedges under Topic 815. We record changes in the value of fair value hedges in interest expense, which is generally offset by changes in the fair value of the hedged debt obligation. Interest payments made or received related to our interest rate derivative instruments are included in interest expense. We record the effective portion of any change in the fair value of derivative instruments designated as cash flow hedges as unrealized gains or losses in OCI, net of tax, until the hedged cash flow occurs, at which point the effective portion of any gain or loss is reclassified to earnings. We record the ineffective portion of our cash flow hedges in interest expense. In the event the hedged cash flow does not occur, or it becomes no longer probable that it will occur, we reclassify the amount of any gain or loss on the related cash flow hedge to interest expense at that time. We had no interest rate derivative contracts outstanding as of September 30, 2013 or December 31, 2012.

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In prior years, we terminated certain interest rate derivative contracts, including fixed-to-floating interest rate contracts, designated as fair value hedges, and floating-to-fixed treasury locks, designated as cash flow hedges. We are amortizing the gains and losses on these derivative instruments upon termination into earnings as a reduction of interest expense over the remaining term of the hedged debt, in accordance with Topic 815. The carrying amount of certain of our senior notes included unamortized gains of $56 million as of September 30, 2013 and $64 million as of December 31, 2012, and unamortized losses of $3 million as of September 30, 2013 and $3 million as of December 31, 2012, related to the fixed-to-floating interest rate contracts. In addition, we had pre-tax net gains within AOCI related to terminated floating-to-fixed treasury locks of $3 million as of September 30, 2013 and $4 million as of December 31, 2012. We recorded $3 million during the third quarter of 2013 and $8 million during the first nine months of 2013 as a reduction to interest expense, resulting from the amortization of previously terminated interest rate derivative contracts. As of September 30, 2013, $9 million of pre-tax net gains may be reclassified to earnings within the next twelve months as a reduction to interest expense from amortization of our previously terminated interest rate derivative contracts.

Counterparty Credit Risk

We do not have significant concentrations of credit risk arising from our derivative financial instruments, whether from an individual counterparty or a related group of counterparties. We manage our concentration of counterparty credit risk on our derivative instruments by limiting acceptable counterparties to a diversified group of major financial institutions with investment grade credit ratings, limiting the amount of credit exposure to each counterparty, and by actively monitoring their credit ratings and outstanding fair values on an on-going basis. Furthermore, none of our derivative transactions are subject to collateral or other security arrangements and none contain provisions that are dependent on our credit ratings from any credit rating agency.

We also employ master netting arrangements that reduce our counterparty payment settlement risk on any given maturity date to the net amount of any receipts or payments due between us and the counterparty financial institution. Thus, the maximum loss due to counterparty credit risk is limited to the unrealized gains in such contracts net of any unrealized losses should any of these counterparties fail to perform as contracted. Although these protections do not eliminate concentrations of credit risk, as a result of the above considerations, we do not consider the risk of counterparty default to be significant.

Fair Value of Derivative Instruments

The following presents the effect of our derivative instruments designated as cash flow hedges under Topic 815 on our accompanying unaudited condensed consolidated statements of operations during the third quarter and first nine months of 2013 and 2012 (in millions):

	Amount of Pre-tax Gain (Loss) Recognized in OCI (Effective Portion)	Amount of Pre-tax Gain (Loss) Reclassified from AOCI into Earnings (Effective Portion)	Location in Statement of Operations
Three Months Ended September 30, 2013			
Currency hedge contracts	$(45)	$15	Cost of products sold
	$(45)	$15	
Three Months Ended September 30, 2012			
Currency hedge contracts	$(44)	$(3)	Cost of products sold
	$(44)	$(3)	
Nine Months Ended September 30, 2013			
Currency hedge contracts	$144	$15	Cost of products sold
	$144	$15	
Nine Months Ended September 30, 2012			

Currency hedge contracts	$2	$(29)	Cost of products sold
	$2	$(29)	

The amount of gain (loss) recognized in earnings related to the ineffective portion of hedging relationships was de minimis for all periods presented.

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Net gains and losses on currency hedge contracts not designated as hedging instruments were offset by net losses and gains from foreign currency transaction exposures, as shown in the following table:

(in millions)	Location in Statement of Operations	Three Months Ended September 30, 2013	2012	Nine Months Ended September 30, 2013	2012
Gain (loss) on currency hedge contracts	Other, net	$12	$(14)	$66	$—
Gain (loss) on foreign currency transaction exposures	Other, net	(15)	11	(72)	(13)
Net foreign currency gain (loss)	Other, net	$(3)	$(3)	$(6)	$(13)

Topic 815 requires all derivative instruments to be recognized at their fair values as either assets or liabilities on the balance sheet. We determine the fair value of our derivative instruments using the framework prescribed by ASC Topic 820, Fair Value Measurements and Disclosures (Topic 820), by considering the estimated amount we would receive or pay to transfer these instruments at the reporting date and by taking into account current interest rates, foreign currency exchange rates, the creditworthiness of the counterparty for assets, and our creditworthiness for liabilities. In certain instances, we may utilize financial models to measure fair value. Generally, we use inputs that include quoted prices for similar assets or liabilities in active markets; quoted prices for identical or similar assets or liabilities in markets that are not active; other observable inputs for the asset or liability; and inputs derived principally from, or corroborated by, observable market data by correlation or other means. As of September 30, 2013, we have classified all of our derivative assets and liabilities within Level 2 of the fair value hierarchy prescribed by Topic 820, as discussed below, because these observable inputs are available for substantially the full term of our derivative instruments.

The following are the balances of our derivative assets and liabilities as of September 30, 2013 and December 31, 2012:

(in millions)	Location in Balance Sheet (1)	As of September 30, 2013	December 31, 2012
Derivative Assets:			
Designated Hedging Instruments			
Currency hedge contracts	Prepaid and other current assets	$88	$25
Currency hedge contracts	Other long-term assets	95	63
		183	88
Non-Designated Hedging Instruments			
Currency hedge contracts	Prepaid and other current assets	17	33
Total Derivative Assets		$200	$121
Derivative Liabilities:			
Designated Hedging Instruments			
Currency hedge contracts	Other current liabilities	$8	$20
Currency hedge contracts	Other long-term liabilities	9	10
		17	30
Non-Designated Hedging Instruments			
Currency hedge contracts	Other current liabilities	27	27
Total Derivative Liabilities		$44	$57

(1) We classify derivative assets and liabilities as current when the remaining term of the derivative contract is one year or less.

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Other Fair Value Measurements

Recurring Fair Value Measurements

On a recurring basis, we measure certain financial assets and financial liabilities at fair value based upon quoted market prices, where available. Where quoted market prices or other observable inputs are not available, we apply valuation techniques to estimate fair value. Topic 820 establishes a three-level valuation hierarchy for disclosure of fair value measurements. The categorization of financial assets and financial liabilities within the valuation hierarchy is based upon the lowest level of input that is significant to the measurement of fair value. The three levels of the hierarchy are defined as follows:

- Level 1 – Inputs to the valuation methodology are quoted market prices for identical assets or liabilities.
- Level 2 – Inputs to the valuation methodology are other observable inputs, including quoted market prices for similar assets or liabilities and market-corroborated inputs.
- Level 3 – Inputs to the valuation methodology are unobservable inputs based on management's best estimate of inputs market participants would use in pricing the asset or liability at the measurement date, including assumptions about risk.

Assets and liabilities measured at fair value on a recurring basis consist of the following as of September 30, 2013 and December 31, 2012:

	As of September 30, 2013				As of December 31, 2012			
(in millions)	Level 1	Level 2	Level 3	Total	Level 1	Level 2	Level 3	Total
Assets								
Money market and government funds	$155	—	—	$155	$39	—	—	$39
Currency hedge contracts	—	$200	—	200	—	$121	—	121
	$155	$200	—	$355	$39	$121	—	$160
Liabilities								
Currency hedge contracts	—	$44	—	$44	—	$57	—	$57
Accrued contingent consideration	—	—	$536	536	—	—	$663	663
	—	$44	$536	$580	—	$57	$663	$720

Our investments in money market and government funds are generally classified within Level 1 of the fair value hierarchy because they are valued using quoted market prices. These investments are classified as cash and cash equivalents within our accompanying unaudited condensed consolidated balance sheets, in accordance with U.S. GAAP and our accounting policies.

In addition to $155 million invested in money market and government funds as of September 30, 2013, we had $281 million in short-term time deposits and $135 million in interest bearing and non-interest bearing bank accounts. In addition to $39 million invested in money market and government funds as of December 31, 2012, we had $168 million in interest bearing and non-interest bearing bank accounts.

Changes in the fair value of assets and liabilities measured on a recurring basis using significant unobservable inputs (Level 3) during the first nine months of 2013 related solely to our contingent consideration liabilities. Refer to Note B - Acquisitions for a discussion of the fair value measurements related to our contingent consideration liabilities.

Non-Recurring Fair Value Measurements

We have certain assets and liabilities that are measured at fair value on a non-recurring basis in periods subsequent to initial recognition. The fair value of a cost method investment is not estimated if there are no identified events or changes in circumstances that may have a significant adverse effect on the fair value of the investment. The aggregate carrying amount of our cost method investments was $22 million as of September 30, 2013 and $13 million as of December 31, 2012.

During the third quarter of 2013, we recorded $4 million of losses to write down certain investments to their fair values. These adjustments fall within Level 3 of the fair value hierarchy, due to the use of significant unobservable inputs to determine fair value.

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During the second quarter of 2013, we recorded $53 million of intangible asset impairment charges, representing a decrease in the estimated fair value of the related intangible asset balances. During the first quarter of 2013, we recorded a $423 million charge to adjust our goodwill balances to their fair value. As a result, during the first nine months of 2013, we recorded $476 million of losses, to adjust our goodwill and certain other intangible asset balances to their fair value. Refer to Note D - Goodwill and Other Intangible Assets, for further detailed information related to these charges and significant unobservable inputs (Level 3).
The fair value of our outstanding debt obligations was $4.599 billion as of September 30, 2013 and $4.793 billion as of December 31, 2012, which was determined by using primarily quoted market prices for our publicly registered senior notes, classified as Level 1 within the fair value hierarchy. Refer to Note F – Borrowings and Credit Arrangements for a discussion of our debt obligations.

NOTE F – BORROWINGS AND CREDIT ARRANGEMENTS
We had total debt of $4.249 billion as of September 30, 2013 and $4.256 billion as of December 31, 2012. During the third quarter of 2013, we refinanced our public debt obligations maturing in June 2014 and January 2015 (see Senior Notes below). The debt maturity schedule for the significant components of our debt obligations as of September 30, 2013 is as follows:

(in millions)	2013	2014	2015	2016	2017	Thereafter	Total
Senior notes	—	$—	$400	$600	$250	$2,550	$3,800
Term loan	—	$—	$—	$80	$80	$240	$400
	—	$—	$400	$680	$330	$2,790	$4,200

Note: The table above does not include unamortized discounts associated with our senior notes, or amounts related to interest rate contracts used to hedge the fair value of certain of our senior notes.

Revolving Credit Facility
We maintain a $2.0 billion revolving credit facility, maturing in April 2017, with a global syndicate of commercial banks. Eurodollar and multicurrency loans under this revolving credit facility bear interest at LIBOR plus an interest margin of between 0.875 percent and 1.475 percent, based on our corporate credit ratings and consolidated leverage ratio (1.275 percent as of September 30, 2013). In addition, we are required to pay a facility fee based on our credit ratings, consolidated leverage ratio, and the total amount of revolving credit commitments, regardless of usage, under the agreement (0.225 percent as of September 30, 2013). There were no amounts borrowed under our revolving credit facility as of September 30, 2013 or December 31, 2012.
Our revolving credit facility agreement in place as of September 30, 2013 requires that we maintain certain financial covenants, as follows:

	Covenant Requirement	Actual as of September 30, 2013
Maximum leverage ratio (1)	3.5 times	2.4 times
Minimum interest coverage ratio (2)	3.0 times	5.4 times

(1) Ratio of total debt to consolidated EBITDA, as defined by the credit agreement, for the preceding four consecutive fiscal quarters.

(2) Ratio of consolidated EBITDA, as defined by the credit agreement, to interest expense for the preceding four consecutive fiscal quarters.

The credit agreement provides for an exclusion from the calculation of consolidated EBITDA, as defined by the agreement, through the credit agreement maturity, of any non-cash charges up to $500 million in restructuring charges and restructuring-related expenses related to our current or future restructuring plans. As of September 30, 2013, we had $287 million of the restructuring charge exclusion remaining. In addition, any cash litigation payments (net of any cash litigation receipts), as defined by the agreement, are excluded from the calculation of consolidated EBITDA and any new debt issued to fund any tax deficiency payments is excluded from consolidated total debt, as defined in the agreement, provided that the sum of any excluded net cash litigation payments and any new debt issued to fund any

tax deficiency payments shall not exceed $2.300 billion in the aggregate. As of September 30, 2013, we had approximately $2.278 billion of the combined legal and debt exclusion remaining. As of and through September 30, 2013, we were in compliance with the required covenants.

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Any inability to maintain compliance with these covenants could require us to seek to renegotiate the terms of our credit facilities or seek waivers from compliance with these covenants, both of which could result in additional borrowing costs. Further, there can be no assurance that our lenders would agree to such new terms or grant such waivers.

Term Loan

In August 2013, we entered into a new $400 million, unsecured term loan facility. Term loan borrowings under this facility bear interest at LIBOR plus an interest margin of between 1.0 percent and 1.75 percent (currently 1.5 percent), based on our corporate credit ratings and consolidated leverage ratio. The term loan borrowings are payable over a 5-year period, with quarterly principal payments of $20 million commencing in the first quarter of 2016 and the remaining principal amount due at the final maturity date in August 2018, and are repayable at any time without premium or penalty. Our term loan facility requires that we comply with certain covenants, including financial covenants with respect to maximum leverage and minimum interest coverage; the maximum leverage ratio requirement is 3.5 times, our actual leverage ratio as of September 30, 2013 is 2.4 times and the minimum interest coverage ratio requirement is 3.0 times, our actual interest coverage ratio as of September 30, 2013 is 5.4 times. We had $400 million outstanding under this facility as of September 30, 2013 and no borrowings outstanding as of December 31, 2012.

Senior Notes

We had senior notes outstanding of $3.800 billion and $4.200 billion as of September 30, 2013 and December 31, 2012 respectively. In August 2013, we issued $600 million of 2.650% senior notes due in 2018, and $450 million of 4.125% senior notes due in 2023. In September 2013, we used the proceeds, together with borrowings under our new $400 million term loan facility, to prepay $600 million of senior notes maturing in June 2014 and $850 million maturing in January 2015. We recorded a one-time charge of $70 million ($44 million after-tax) for premiums, accelerated amortization of debt issuance costs and investor discount costs net of interest rate hedge gains related to the early debt extinguishment. Our senior notes are publicly registered securities, are redeemable prior to maturity and are not subject to any sinking fund requirements. Our senior notes are unsecured, unsubordinated obligations and rank on parity with each other. These notes are effectively junior to borrowings under our credit and security facility and liabilities of our subsidiaries (see Other Arrangements below).

Other Arrangements

We also maintain a credit and security facility secured by our U.S. trade receivables. In June 2013, we extended the maturity of this facility through June 2015, subject to further extension, reduced the size of the facility from $350 million to $300 million and added a maximum leverage covenant consistent with our revolving credit facility. The maximum leverage ratio requirement is 3.5 times and our actual leverage ratio as of September 30, 2013 is 2.4 times. We had no borrowings outstanding under this facility as of September 30, 2013 and December 31, 2012.

We have accounts receivable factoring programs in certain European countries that we account for as sales under ASC Topic 860, Transfers and Servicing. These agreements provide for the sale of accounts receivable to third parties, without recourse, of up to approximately $306 million as of September 30, 2013. We have no retained interests in the transferred receivables, other than collection and administrative responsibilities and, once sold, the accounts receivable are no longer available to satisfy creditors in the event of bankruptcy. We de-recognized $166 million of receivables as of September 30, 2013 at an average interest rate of 3.3 percent, and $191 million as of December 31, 2012 at an average interest rate of 1.6 percent. Within Italy, Spain, Portugal and Greece the number of days our receivables are outstanding has increased above historical levels. We believe we have adequate allowances for doubtful accounts related to our Italy, Spain, Portugal and Greece accounts receivable; however, we continue to monitor the European economic environment for any collectibility issues related to our outstanding receivables. As of September 30, 2013, our net receivables in these countries greater than 180 days past due totaled $78 million, of which $28 million were past due greater than 365 days.

In addition, we have uncommitted credit facilities with a commercial Japanese bank that provide for borrowings, promissory notes discounting, and receivables factoring of up to 21.0 billion Japanese yen (approximately $214 million as of September 30, 2013). We de-recognized $156 million of notes receivable as of September 30, 2013 at an average interest rate of 1.8 percent and $182 million of notes receivable as of December 31, 2012 at an average

interest rate of 1.6 percent. De-recognized accounts and notes receivable are excluded from trade accounts receivable, net in the accompanying unaudited condensed consolidated balance sheets.

As of September 30, 2013, we had outstanding letters of credit of $74 million, as compared to $94 million as of December 31, 2012, which consisted primarily of bank guarantees and collateral for workers' compensation insurance arrangements. As of September 30, 2013 and December 31, 2012, none of the beneficiaries had drawn upon the letters of credit or guarantees; accordingly, we did not recognize a related liability for our outstanding letters of credit in our consolidated balance sheets as of September 30, 2013 or December 31, 2012. We believe we will generate sufficient cash from operations to fund these payments and intend to fund these payments without drawing on the letters of credit.

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NOTE G – RESTRUCTURING-RELATED ACTIVITIES

On an on-going basis, we monitor the dynamics of the economy, the healthcare industry, and the markets in which we compete. We continue to assess opportunities for improved operational effectiveness and efficiency, and better alignment of expenses with revenues, while preserving our ability to make the investments in research and development projects, capital and our people that we believe are essential to our long-term success. As a result of these assessments, we have undertaken various restructuring initiatives in order to enhance our growth potential and position us for long-term success. These initiatives are described below.

2014 Restructuring plan

On October 22, 2013, the Board of Directors approved, and we committed to, a restructuring initiative (the 2014 Restructuring plan). The 2014 Restructuring plan is intended to build on the progress we have made to address financial pressures in a changing global marketplace, further strengthen its operational effectiveness and efficiency and support new growth investments. Key activities under the plan include continued implementation of our ongoing Plant Network Optimization (PNO) strategy, continued focus on driving operational efficiencies and ongoing business and commercial model changes. The PNO strategy is intended to simplify our manufacturing plant structure by transferring certain production lines among facilities. Other activities involve rationalizing organizational reporting structures to streamline various functions, eliminate bureaucracy, increase productivity and better align resources to business strategies and marketplace dynamics. These activities will start to be initiated in the fourth quarter of 2013 and are expected to be substantially completed by the end of 2015.

We estimate that the implementation of the 2014 Restructuring plan will result in total pre-tax charges of approximately $175 million to $225 million, of which approximately $160 million to $210 million is expected to result in future cash outlays. The following table provides a summary of our estimates of costs associated with the 2014 Restructuring plan by major type of cost:

Type of cost	Total estimated amount expected to be incurred
Restructuring charges:	
Termination benefits	$120 million to $150 million
Other (1)	$5 million to $15 million
Restructuring-related expenses:	
Other (2)	$50 million to $60 million
	$175 million to $225 million

(1) Consists primarily of consultant fees and costs associated with contractual cancellations.
(2) Comprised of other costs directly related to the 2014 Restructuring plan, including program management, accelerated depreciation, and costs to transfer product lines among facilities.

2011 Restructuring plan

On July 26, 2011, our Board of Directors approved, and we committed to, a restructuring initiative (the 2011 Restructuring plan) designed to strengthen operational effectiveness and efficiencies, increase competitiveness and support new investments, thereby increasing stockholder value. Key activities under the 2011 Restructuring plan include standardizing and automating certain processes and activities; relocating select administrative and functional activities; rationalizing organizational reporting structures; leveraging preferred vendors; and other efforts to eliminate inefficiency. Among these efforts, we are expanding our ability to deliver best-in-class global shared services for certain functions and divisions at several locations in emerging markets. This action is intended to enable us to grow our global commercial presence in key geographies and take advantage of many cost-reducing and productivity-enhancing opportunities. In addition, we are undertaking efforts to streamline various corporate functions, eliminate bureaucracy, increase productivity and better align corporate resources to our key business strategies. On January 25, 2013, our Board of Directors approved, and we committed to, an expansion of the 2011

Restructuring plan (the Expansion). The Expansion is intended to further strengthen our operational effectiveness and efficiencies and support new investments. Activities under the 2011 Restructuring plan were initiated in the third quarter of 2011 and all activities, including those related to the Expansion, are expected to be substantially complete by the end of 2013.

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We estimate that the 2011 Restructuring plan, including the Expansion, will result in total pre-tax charges of approximately $300 million to $355 million, and that approximately $270 million to $300 million of these charges will result in future cash outlays, of which we have made payments of $235 million, which were partially offset by proceeds of $53 million on facility and fixed asset sales, as of September 30, 2013. As of September 30, 2013, we recorded costs of $260 million since the inception of the 2011 Restructuring plan, including the Expansion, and recorded a portion of these expenses as restructuring charges and the remaining portion through other lines within our unaudited condensed consolidated statements of operations.
The following provides a summary of our expected total costs associated with the 2011 Restructuring plan, including the Expansion, by major type of cost:

Type of cost	Total estimated amount expected to be incurred
Restructuring charges:	
Termination benefits	$160 million to $185 million
Other (1)	$100 million to $120 million
Restructuring-related expenses:	
Other (2)	$40 million to $50 million
	$300 million to $355 million

(1) Includes primarily consulting fees, gains and losses on disposals of fixed assets and costs associated with contractual cancellations.

(2) Comprised of other costs directly related to the 2011 Restructuring plan, including the Expansion, such as program management, accelerated depreciation, retention and infrastructure-related costs.

2010 Restructuring plan

On February 6, 2010, our Board of Directors approved, and we committed to, a series of management changes and restructuring initiatives (the 2010 Restructuring plan) designed to focus our business, drive innovation, accelerate profitable revenue growth and increase both accountability and stockholder value. Key activities under the 2010 Restructuring plan included the restructuring of certain of our businesses and corporate functions; the re-alignment of our international structure to reduce our administrative costs and invest in expansion opportunities including significant investments in emerging markets; and the re-prioritization and diversification of our product portfolio. Activities under the 2010 Restructuring plan were initiated in the first quarter of 2010 and were complete by the end of 2012.
The execution of the 2010 Restructuring plan resulted in total pre-tax charges of $160 million, and required cash outlays of $145 million.
The following provides a summary of our costs associated with the 2010 Restructuring plan by major type of cost:

Type of cost	Total amount incurred
Restructuring charges:	
Termination benefits	$90 million
Fixed asset write-offs	$11 million
Other (1)	$51 million
Restructuring-related expenses:	
Other (2)	$8 million
	$160 million

(1) Includes primarily consulting fees and costs associated with contractual cancellations.

(2) Comprised of other costs directly related to the 2010 Restructuring plan, including accelerated depreciation and infrastructure-related costs.

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Plant Network Optimization program

In January 2009, our Board of Directors approved, and we committed to, a plant network optimization initiative (the Plant Network Optimization program), intended to simplify our manufacturing plant structure by transferring certain production lines among facilities and by closing certain other facilities. The program was a complement to the restructuring initiatives approved by our Board of Directors in 2007, and was intended to improve overall gross profit margins. Activities under the Plant Network Optimization program were initiated in the first quarter of 2009 and were substantially completed during 2012.

We estimate that the execution of the Plant Network Optimization program will result in total pre-tax charges of approximately $130 million, and that approximately $105 million to $110 million of these charges will result in cash outlays, of which we made payments of $103 million as of September 30, 2013. As of September 30, 2013, we recorded costs of $127 million since the inception of the plan, and recorded a portion of these expenses as restructuring charges and the remaining portion through cost of products sold within our unaudited condensed consolidated statements of operations.

The following provides a summary of our estimates of costs associated with the Plant Network Optimization program by major type of cost:

Type of cost	Total estimated amount expected to be incurred
Restructuring charges:	
Termination benefits	$33 million
Restructuring-related expenses:	
Accelerated depreciation	$22 million
Transfer costs (1)	$75 million
	$130 million

(1) Consists primarily of costs to transfer product lines among facilities, including costs of transfer teams, freight, idle facility and product line validations.

In the aggregate, we recorded net restructuring charges pursuant to our restructuring plans of $19 million in the third quarter of 2013, $54 million in the third quarter of 2012, $55 million in the first nine months of 2013, and $93 million in the first nine months of 2012. During the first nine months of 2013, our restructuring charges were partially offset by a $19 million gain recognized on the sale of our Natick, Massachusetts headquarters. We are currently in the process of consolidating our Natick, Massachusetts headquarters into our Marlborough, Massachusetts location, where we are establishing a new global headquarters campus. In addition, we recorded expenses within other lines of our accompanying unaudited condensed consolidated statements of operations related to our restructuring initiatives of $7 million in the third quarter of 2013 and $4 million in the third quarter of 2012, and $16 million in the first nine months of 2013 and $15 million in the first nine months of 2012.

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The following presents these costs (credits) by major type and line item within our accompanying unaudited condensed consolidated statements of operations, as well as by program:

Three Months Ended September 30, 2013

(in millions)	Termination Benefits	Accelerated Depreciation	Transfer Costs	Fixed Asset Write-offs	Other	Total
Restructuring charges	$5	$—	$—	$—	$14	$19
Restructuring-related expenses:						
Cost of products sold	—	—	—	—	—	—
Selling, general and administrative expenses	—	1	—	—	6	7
	—	1	—	—	6	7
	$5	$1	$—	$—	$20	$26

(in millions)	Termination Benefits	Accelerated Depreciation	Transfer Costs	Fixed Asset Write-offs	Other	Total
2011 Restructuring plan	$5	$1	$—	$—	$20	$26
2010 Restructuring plan	—	—	—	—	—	—
Plant Network Optimization program	—	—	—	—	—	—
	$5	$1	$—	$—	$20	$26

Three Months Ended September 30, 2012

(in millions)	Termination Benefits	Accelerated Depreciation	Transfer Costs	Fixed Asset Write-offs	Other	Total
Restructuring charges	$44	$—	$—	$—	$10	$54
Restructuring-related expenses:						
Cost of products sold	—	—	1	—	—	1
Selling, general and administrative expenses	—	—	—	—	3	3
	—	—	1	—	3	4
	$44	$—	$1	$—	$13	$58

(in millions)	Termination Benefits	Accelerated Depreciation	Transfer Costs	Fixed Asset Write-offs	Other	Total
2011 Restructuring plan	$43	$—	$—	$—	$13	$56
2010 Restructuring plan	2	—	—	—	—	2
Plant Network Optimization program	(1)	—	1	—	—	—
	$44	$—	$1	$—	$13	$58

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Nine Months Ended September 30, 2013

(in millions)	Termination Benefits	Accelerated Depreciation	Transfer Costs	Fixed Asset Write-offs	Other	Total
Restructuring charges	$26	$—	$—	$(16)	$45	$55
Restructuring-related expenses:						
Cost of products sold	—	—	—	—	—	—
Selling, general and administrative expenses	—	2	—	—	14	16
	—	2	—	—	14	16
	$26	$2	$—	$(16)	$59	$71

(in millions)	Termination Benefits	Accelerated Depreciation	Transfer Costs	Fixed Asset Write-offs	Other	Total
2011 Restructuring plan	$30	$2	$—	$(16)	$59	$75
2010 Restructuring plan	—	—	—	—	—	—
Plant Network Optimization program	(4)	—	—	—	—	(4)
	$26	$2	$—	$(16)	$59	$71

Nine Months Ended September 30, 2012

(in millions)	Termination Benefits	Accelerated Depreciation	Transfer Costs	Fixed Asset Write-offs	Other	Total
Restructuring charges	$64	$—	$—	$—	$29	$93
Restructuring-related expenses:						
Cost of products sold	—	—	7	—	—	7
Selling, general and administrative expenses	—	—	—	—	8	8
	—	—	7	—	8	15
	$64	$—	$7	$—	$37	$108

(in millions)	Termination Benefits	Accelerated Depreciation	Transfer Costs	Fixed Asset Write-offs	Other	Total
2011 Restructuring plan	$65	$—	$—	$—		