

STERIS CORP  
Form 10-Q/A  
June 23, 2011  
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UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION  
WASHINGTON, D. C. 20549

FORM 10-Q/A  
Amendment No. 1  
(Mark One)

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

For the quarterly period ended December 31, 2010

or

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

For the transition period from \_\_\_\_\_ to \_\_\_\_\_

Commission File Number 1-14643

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STERIS Corporation  
(Exact name of registrant as specified in its charter)

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Ohio  
(State or other jurisdiction of  
incorporation or organization)

34-1482024  
(IRS Employer  
Identification No.)

5960 Heisley Road,  
Mentor, Ohio  
(Address of principal executive offices)  
440-354-2600  
(Registrant's telephone number, including area code)

44060-1834  
(Zip code)

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

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

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, 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   
Non-Accelerated Filer

Accelerated Filer   
Smaller Reporting Company

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(Do not check if a smaller reporting company)

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

The number of common shares outstanding as of January 31, 2011: 59,341,368

This Amendment No. 1 on Form 10-Q/A to the Quarterly Report on Form 10-Q for the quarter ended December 31, 2010 of STERIS Corporation (the "Company"), originally filed with the Securities and Exchange Commission on February 9, 2011, reformats the "Matters Affecting Comparability" and "Results of Operations" portions, and adds a new "Non-GAAP Financial Measures" portion, of Management's Discussion & Analysis contained in Item 2 of the previously filed Form 10-Q to present the reconciliation of GAAP and Non-GAAP numbers and the discussion thereof in a different manner, adds cross references and updates the dates of the certifications contained in Exhibits 31.1 and 31.2 of such Quarterly Report as of the filing date of this Amendment No. 1.

Except for the reformatted presentation of the reconciliations and discussion, cross references, and the referenced certification updates, this Amendment No. 1 to the Company's Quarterly Report on Form 10-Q/A does not change any of the previously filed information or results for the quarter, and does not update any disclosure from, or reflect any event occurring subsequent to February 9, 2011, which is the filing date of the Quarterly Report on Form 10-Q as originally filed.

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PART 1—FINANCIAL INFORMATION

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, repurchase common 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 third quarter and first nine months of fiscal 2011 and fiscal 2010. It may also be helpful to read the MD&A in our Annual Report on Form 10-K for the year ended March 31, 2010, filed with the SEC on May 28, 2010. 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 and to measure the risk of our financial structure.

**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.

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:

**Revenues** – Our revenues are presented net of sales returns and allowances.

**Product Revenues** – We define product revenues as revenues generated from sales of capital equipment, which includes steam and low temperature liquid sterilizers, washing systems, VHP technology, water stills, and pure steam generators; integrated OR; surgical lights and tables; and the consumable family of products, which includes SYSTEM 1 and SYSTEM 1E consumables, sterility assurance products, skin care products, and cleaning consumables.

**Service Revenues** – We define service revenues as revenues generated from parts and labor associated with the maintenance, repair, and installation of our capital equipment, as well as revenues generated from contract sterilization offered through our Isomedix segment.

**Capital Revenues** – We define capital revenues as revenues generated from sales of capital equipment, which includes

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steam and low temperature liquid sterilizers, 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 SYSTEM 1E consumables, sterility assurance products, skin care products, and cleaning consumables.

**Recurring Revenues** – We define recurring revenues as revenues generated from sales of consumable products and service revenues.

**Acquired Revenues** – We define acquired revenues as base revenues generated from acquired businesses or assets and additional volumes driven through acquired businesses or assets. We will use such measure for up to a year after acquisition.

## General Company Overview and Executive Summary

Our mission is to provide a healthier today and safer tomorrow through knowledgeable people and innovative infection prevention, decontamination and health science technologies, products, and services. Our dedicated employees around the world work together to supply a broad range of solutions by offering a combination of capital equipment, consumables, 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. In the contract sterilization industry, the aging population increases the demand for medical procedures, which can increase the consumption of single use medical devices and surgical kits.

Beyond our core markets, infection-control issues are becoming a global concern, and emerging threats are prominent in the news. We are actively pursuing new opportunities to adapt our proven technologies to meet the changing needs of the global marketplace.

During the first nine months of fiscal 2011, we recorded a pre-tax liability related to the SYSTEM 1 Rebate Program. The Rebate Program reduced Healthcare revenues by \$102.3 million, increased Healthcare cost of revenues by \$7.7 million, decreased gross margin and operating margin by \$110.0 million. The accrual of these estimated rebates and costs increased current liabilities by \$110.0 million and did not have a material impact on free cash flow during the period.

Fiscal 2011 third quarter revenues were \$328.3 million representing an increase of 0.1% over prior year period reflecting increases in the Healthcare and Isomedix business segments offset by a decrease in the Life Science business segment. Our gross margin percentage for the fiscal 2011 third quarter was 41.7%, representing a 80 basis point decrease over the prior year period, driven primarily by unfavorable product mix and lower SYSTEM 1 consumable volume. Revenues for the first nine months of fiscal 2011 were \$829.7 million and gross margin percentage was 35.0%. Adjusted revenues for the first nine months of fiscal 2011, excluding the impact of the Rebate Program, were \$932.0 million (see subsection of MD&A titled "Non-GAAP Financial measures" for additional information and related reconciliation of non-GAAP financial measures to the most comparable GAAP measures) compared to \$925.6 million in the first nine months of fiscal 2010, representing an increase of \$6.4 million, or 0.7%. Increases in the Healthcare and Isomedix business segments were offset by a decrease in the Life Science business segment. Our adjusted gross profit percentage, excluding the impact of the Rebate Program, for the first nine months

of fiscal 2011 was 42.9% (see subsection of MD&A titled "Non-GAAP Financial measures" for additional information and related reconciliation of non-GAAP financial measures to the most comparable GAAP measures), consistent with the first nine months of the prior fiscal year. The benefits of productivity improvements and price increases were offset by unfavorable impacts of a shift in product mix and reductions in SYSTEM 1 consumable volumes.

Fiscal 2011 third quarter operating expenses include a pre-tax charge of \$19.8 million related to the proposed settlement of SYSTEM 1 class action litigation. This settlement is subject to, among other things, certification of the class and approval of the settlement by the court. After tax, the impact of the charge was a reduction in net income of \$13.1 million, or \$0.22 per diluted share.

Free cash flow was \$28.3 million in the first nine months of fiscal 2011 compared to \$129.4 million in the prior year first nine months, reflecting higher capital spending levels and a higher use of cash to fund changes in operating assets and

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liabilities. Our debt-to-total capital ratio was 21.9% at December 31, 2010 and 21.8% at March 31, 2010. During the first nine months of fiscal 2011, we declared and paid quarterly cash dividends of \$0.41 per common share.

Additional information regarding our fiscal 2011 third quarter financial performance is included in the subsection below titled "Results of Operations."

### Matters Affecting Comparability

SYSTEM 1 Rebate Program and class action settlement. In April 2010, we introduced the SYSTEM 1 Rebate Program ("Rebate Program") to Customers as a component of our Transition Plan for SYSTEM 1. Generally, U.S. Customers that purchased SYSTEM 1 processors directly from us or who are current users of SYSTEM 1 and who return their units will have the option of either a pro-rated cash value or rebate toward the future purchase of new STERIS capital equipment or consumable products. In addition, we will provide credits for SYSTEM 1 consumables in unbroken packaging and within shelf life and for the unused portion of prepaid SYSTEM 1 services contracts.

During the first quarter of fiscal 2011, we recorded a pre-tax liability related to the Rebate Program. Of the \$110.0 million recorded, \$102.3 million is attributable to the Customer Rebate portion of the Program and was recorded as a reduction to revenue, and \$7.7 million is attributable to the disposal liability of the SYSTEM 1 units to be returned and was recorded in cost of revenues.

Fiscal 2011 third quarter operating expenses include a pre-tax charge of \$19.8 million related to the proposed settlement of SYSTEM 1 class action litigation. This settlement is subject to, among other things, certification of the class and approval of the settlement by the court. After tax, the impact of the charge was a reduction in net income of \$13.1 million, or \$0.22 per diluted share.

Restructuring. During the first nine months of fiscal 2011, we did not incur any significant additional expenses related to previously announced restructuring actions.

Additional information regarding our restructuring actions is included in our Annual Report on Form 10-K for the year ended March 31, 2010, filed with the SEC on May 28, 2010.

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 third quarter of fiscal 2011, our revenues were unfavorably impacted by \$1.4 million, or 0.4%, and income before taxes was unfavorably impacted by \$0.4 million, or 1.3%, as a result of foreign currency movements relative to the U.S. dollar. During the first nine months of fiscal 2011, our revenues were unfavorably impacted by \$2.0 million, or 0.2%, and income before income taxes was unfavorably impacted by \$0.2 million, or 1.1% as compared to the same prior year period.

### Non-GAAP Financial Measures

We, at times, refer to financial measures which are considered to be "non-GAAP financial measures" under SEC rules. We may 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 flows 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,

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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 common shares, and pay cash dividends. The following table summarizes the calculation of our free cash flow for the nine months ended December 31, 2010 and 2009:

(dollars in thousands)	Nine Months Ended December 31,	
	2010	2009
Net cash flows provided by operating activities	\$83,397	\$158,668
Purchases of property, plant, equipment and intangibles, net	(56,390 )	(29,839 )
Proceeds from the sale of property, plant, equipment and intangibles	1,298	574
Free cash flow	\$28,305	\$129,403

To supplement our financial results presented in accordance with U.S. GAAP, we have sometimes referred to certain measures of revenues, gross profit, and the Healthcare segment results of operations in the section of MD&A titled, "Results of Operations" excluding the impact of the SYSTEM 1 Rebate Program and proposed class action settlement recorded in fiscal 2011. These two items had a significant impact on the fiscal 2011 measures and the corresponding trend in each of these measures. We provide adjusted measures to give the reader a more complete understanding of the factors and trends affecting our business than could be obtained absent this disclosure. These measures are used by management and the Board of Directors in making comparisons to our historical operating results and analyzing the underlying performance of our operations. The tables below provide a reconciliation of each of these measures to its most directly comparable GAAP financial measure.

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(dollars in thousands)	Nine months ended December 31, 2010	
Reported revenues	\$829,688	
Impact of the SYSTEM 1 Rebate Program	102,313	
Adjusted revenues	\$932,001	
Reported capital revenues	\$256,368	
Impact of the SYSTEM 1 Rebate Program	102,313	
Adjusted capital revenues	\$358,681	
Reported United States revenues	\$601,703	
Impact of the SYSTEM 1 Rebate Program	102,313	
Adjusted United States Revenues	\$704,016	
Reported Healthcare revenues	\$561,723	
Impact of the SYSTEM 1 Rebate Program	102,313	
Adjusted Healthcare revenues	\$664,036	
Reported gross profit	\$290,135	
Impact of the SYSTEM 1 Rebate Program	110,004	
Adjusted gross profit	\$400,139	
Reported gross profit percentage	35.0	%
Impact of the SYSTEM 1 Rebate Program	7.9	%
Adjusted gross profit percentage	42.9	%
Reported Healthcare operating income	\$(19,460	)
Impact of the SYSTEM 1 Rebate Program and proposed class action settlement	129,800	
Adjusted Healthcare operating income	\$110,340	
	Three months ended December 31, 2010	
Reported Healthcare operating income	\$20,389	
Impact of the proposed SYSTEM 1 class action settlement	19,796	
Adjusted Healthcare operating income	\$40,185	

## Results of Operations

In the following subsections, we discuss our earnings and the factors affecting them for the third quarter and first nine months of fiscal 2011 compared with the same fiscal 2010 periods. 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 and nine months ended December 31, 2010 to the revenues for the three and nine months ended December 31, 2009:

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(dollars in thousands)	Three Months Ended December 31,			Percent	
	2010	2009	Change	Change	
Total Revenues	\$328,283	\$327,832	\$451	0.1	%
Revenues by type:					
Capital Revenues	135,121	132,541	2,580	1.9	%
Consumable Revenues	77,501	81,531	(4,030)	(4.9)	%
Service Revenues	115,661	113,760	1,901	1.7	%
Revenues by geography:					
United States	239,975	244,067	(4,092)	(1.7)	%
International	88,308	83,765	4,543	5.4	%
(dollars in thousands)	Nine Months Ended December 31,			Percent	
	2010	2009	Change	Change	
Total Revenues	\$829,688	\$925,604	\$(95,916)	(10.4)	%
Revenues by type:					
Capital Revenues	256,368	344,391	(88,023)	(25.6)	%
Consumable Revenues	230,618	242,315	(11,697)	(4.8)	%
Service Revenues	342,702	338,898	3,804	1.1	%
Revenues by geography:					
United States	601,703	706,165	(104,462)	(14.8)	%
International	227,985	219,439	8,546	3.9	%

## Quarter over Quarter Comparison

Revenues increased \$0.5 million, or 0.1%, to \$328.3 million for the quarter ended December 31, 2010, as compared to \$327.8 million for the same prior year quarter. Capital revenues increased \$2.6 million in the third quarter of fiscal 2011, driven by higher demand from Healthcare Customers. Service revenues increased \$1.9 million in the third quarter of fiscal 2011 due to an increase in Isomedix segment revenues, although this increase was largely offset by decreases within the Healthcare and Life Sciences business segments. Consumable revenues decreased \$4.0 million for the quarter ended December 31, 2010, primarily driven by decreases within the Healthcare segment attributable to reductions in SYSTEM 1 consumables and lower H1N1 related product sales as compared to the prior year quarter.

International revenues increased \$4.5 million, or 5.4%, to \$88.3 million for the quarter ended December 31, 2010, as compared to \$83.8 million for the same prior year quarter. International revenues were favorably affected by increases in capital equipment revenues, which increased 6.3% primarily due to increases within Europe and Asia Pacific. International recurring revenues increased during the third quarter of fiscal 2011 by 4.3%, reflecting increases within Canada, and the Asia Pacific and Latin American regions partially offset by a decrease in Europe.

United States revenues decreased \$4.1 million, or 1.7%, to \$240.0 million for the quarter ended December 31, 2010, as compared to \$244.1 million for the same prior year quarter. United States recurring revenues decreased 2.3% for

the third quarter of fiscal 2011, and reflected a decrease of 7.0% in consumable revenues, partially offset by an increase of 0.8% in service revenues. The decrease in United States consumable revenues was driven by decreases in SYSTEM 1 consumables and H1N1 related products. Capital equipment revenues decreased 0.5% in the United States as the decline in Life Sciences capital equipment revenues of 36.8% more than offset the increase in Healthcare capital equipment revenues of 5.1%.

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First Nine Months over First Nine Months Comparison

Revenues decreased \$95.9 million, or (10.4)%, to \$829.7 million for the first nine months of fiscal 2011, as compared to revenues of \$925.6 million during the first nine months of fiscal 2010. The decline reflects the \$102.3 million negative impact of the Rebate Program. Adjusted revenues, excluding the impact of the Rebate Program, increased \$6.4 million, or 0.7%, to \$932.0 million for the first nine months of fiscal 2011 (see subsection of MD&A titled "Non-GAAP Financial Measures" for additional information and related reconciliation of non-GAAP financial measures to the most comparable GAAP measures) as compared to revenues for the first nine months of fiscal 2010. Capital equipment revenues decreased \$88.0 million or 25.6%. The decrease in capital equipment revenues reflects the \$102.3 million negative impact of the Rebate Program on Healthcare capital equipment revenues. Adjusted capital equipment revenues, excluding the impact of the Rebate Program (see subsection of MD&A titled "Non-GAAP Financial Measures" for additional information and related reconciliation of non-GAAP financial measures to the most comparable GAAP measures), increased \$14.3 million or 4.1%, driven by improved demand within the United States and the Asia Pacific and Latin America regions partially offset by declines in Canada and Europe. Recurring revenues decreased \$7.9 million or 1.4% driven by weaker demand in United States and Europe attributable to reductions in SYSTEM 1 consumables in the United States and lower H1N1 product sales.

International revenues for the first nine months of fiscal 2011 were \$228.0 million, an increase of \$8.5 million, or 3.9% , as compared to the first nine months of fiscal 2010. Fiscal 2011 year-to-date international revenues were favorably impacted by a 3.1% increase in capital equipment revenue and a 4.8% increase in recurring revenues, reflecting increases in both consumable and service revenues of 3.2% and 6.4%, respectively.

United States revenues for the first nine months of fiscal 2011 were \$601.7 million, a decrease of \$104.5 million, or 14.8%, as compared to the first nine months of fiscal 2010. The fiscal 2011 year-to-date decrease in United States revenues was primarily driven by the \$102.3 million negative impact of the Rebate Program on capital equipment revenues within the Healthcare segment in the United States. The remaining decrease of \$2.1 million was driven by a 7.0% decrease in consumable revenues as a result of reductions in SYSTEM 1 consumables and H1N1 related products, which was partially offset by an increase in capital equipment revenues and higher service revenues generated by our Isomedix segment.

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

Gross Profit. The following table compares our gross profit for the three and nine months ended December 31, 2010 to the three and nine months ended December 31, 2009:

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(dollars in thousands)	Three Months Ended		Change	Percent Change	
	December 31, 2010	2009			
Gross Profit:					
Product	\$89,241	\$91,748	\$(2,507)	(2.7)	)%
Service	47,773	47,735	38	0.1	%
Total Gross Profit	\$137,014	\$139,483	\$(2,469)	(1.8)	)%
Gross Profit Percentage:					
Product	42.0	% 42.9	%		
Service	41.3	% 42.0	%		
Total Gross Profit Percentage	41.7	% 42.5	%		

(dollars in thousands)	Nine Months Ended		Change	Percent Change	
	December 31, 2010	2009			
Gross Profit:					
Product	\$146,293	\$254,148	\$(107,855)	(42.4)	)%
Service	143,842	142,826	1,016	0.7	%
Total Gross Profit	\$290,135	\$396,974	\$(106,839)	(26.9)	)%
Gross Profit Percentage:					
Product	30.0	% 43.3	%		
Service	42.0	% 42.1	%		
Total Gross Profit Percentage	35.0	% 42.9	%		

Our gross profit 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 profit percentage for the third quarter of fiscal 2011 amounted to 41.7%, representing a decrease of 80 basis points as compared to the same prior year period. The fiscal 2011 period was negatively impacted by a higher portion of revenues coming from lower margin capital equipment products and lower SYSTEM 1 consumable volume. For the first nine months of fiscal 2011, gross profit percentage amounted to 35.0%. The most significant driver of this decrease is the \$110.0 million negative impact of the Rebate Program. On an adjusted basis, the gross profit percentage for the first nine months of fiscal 2011, gross margin amounted to 42.9% (see subsection of MD&A titled "Non-GAAP Financial Measures" for additional information and related reconciliation of non-GAAP financial measures to the most comparable GAAP measures), equal to the same prior year period. The negative impact of a higher portion of revenue coming from lower margin capital equipment products and lower SYSTEM 1 consumable volume offset the benefits of productivity improvements and price increases.

Operating Expenses. The following table compares our operating expenses for the three and nine months ended December 31, 2010 to the three and nine months ended December 31, 2009:

(dollars in thousands)	Three Months Ended		Change	Percent Change	
	December 31, 2010	2009			
Operating Expenses:					
Selling, General, and Administrative	\$93,467	\$71,776	\$21,691	30.2	%
Research and Development	7,739	8,265	(526)	(6.4)	)%
Restructuring Expenses	(23)	) 14	(37)	) NM	
Total Operating Expenses	\$101,183	\$80,055	\$21,128	26.4	%

NM - Not meaningful.

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(dollars in thousands)	Nine Months Ended		Change	Percent Change	
	December 31, 2010	2009			
Operating Expenses:					
Selling, General, and Administrative	\$237,583	\$220,897	\$16,686	7.6	%
Research and Development	24,391	24,035	356	1.5	%
Restructuring Expenses	423	(313)	736	NM	
Total Operating Expenses	\$262,397	\$244,619	\$17,778	7.3	%

NM - Not meaningful.

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 \$21.7 million or 30.2% in the third quarter of fiscal 2011 compared to the same prior year period. SG&A increased \$16.7 million or 7.6% during the first nine months of fiscal 2011 compared to the first nine months of fiscal 2010. The three and nine month periods in fiscal 2011 include \$19.8 million associated with the proposed SYSTEM 1 class action settlement. The remaining change in SG&A in the third quarter of fiscal 2011 is an increase of \$1.9 million is attributable to higher commissions associated with the increase in capital equipment revenues. The remaining change in SG&A in the first nine months of fiscal 2011 is a decrease of \$3.1 million and is attributable to the benefits of cost reduction actions previously implemented as well as improved operating efficiencies.

As a percentage of total revenues, research and development expenses were 2.4% and 2.5% for the three month periods ended December 31, 2010 and 2009, respectively. For the three month period ended December 31, 2010, research and development expenses decreased 6.4% to \$7.7 million as compared to \$8.3 million during the same prior year period. For the first nine months of fiscal 2011, research and development expenses increased 1.5% to \$24.4 million, as compared to \$24.0 million, during the same prior year period. 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 third quarter of fiscal 2011, our investments in research and development continued to be focused on, but were not limited to, enhancing capabilities of sterile processing combination technologies, surgical tables and accessories, and the areas of emerging infectious agents such as Prions and Nanobacteria.

Expenses incurred during the third quarter of fiscal 2011 related to our previously announced restructuring plans. In the third quarter of fiscal 2010, we settled certain obligations for less than originally expected. The following tables summarize our total pre-tax restructuring expenses for the third quarter and first nine months of fiscal 2011 and fiscal 2010:

Three months ended December 31, 2010	Fiscal 2010	Fiscal 2008	Total
	Restructuring Plan (1)	Restructuring Plan	
Severance, payroll and other related costs	\$489	\$—	\$489
Asset impairment and accelerated depreciation	—	(289)	(289)
Other	7	—	7
Total restructuring charges	\$496	\$(289)	\$(207)

(1) Includes \$230 in charges recorded in cost of revenues on Consolidated Statements of Income.

Three Months Ended December 31, 2009

Fiscal 2009

	Restructuring Plan (1)
Severance, payroll and other related costs	\$(23 )
Product rationalization	(232 )
Asset impairment	9
Lease termination obligations and other	18
Total restructuring charges	\$(228 )

(1)Includes \$(242) in charges recorded in cost of revenues on Consolidated Statements of Income.

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Nine Months Ended December 31, 2010	Fiscal 2010	Fiscal 2008	Total
	Restructuring Plan (1)	Restructuring Plan	
Severance, payroll and other related costs	\$498	—	498
Asset impairment and accelerated depreciation	356	(289)	) 67
Other	88	—	88
Total restructuring charges	\$942	(289)	) 653

(1) Includes \$230 in charges recorded in cost of revenues on Consolidated Statements of Income.

Nine Months Ended December 31, 2009	Fiscal 2009	
	Restructuring Plan (2)	
Severance, payroll and other related costs	\$ (36	)
Product rationalization	(466	)
Asset impairment and accelerated depreciation	(5	)
Lease termination obligations and other	(290	)
Total restructuring charges	\$ (797	)

(2) Includes \$(484) in charges recorded in cost of revenues on Consolidated Statements of Income.

Liabilities related to restructuring activities are recorded as current liabilities on the accompanying Consolidated Balance Sheets within “Accrued payroll and other related liabilities” and “Accrued expenses and other.” The following table summarizes our liabilities related to these restructuring activities:

(dollars in thousands)	Fiscal 2010 Restructuring Plan			
	March 31, 2010	Fiscal 2011 Provision	Payments/ Impairments	December 31, 2010
Severance and termination benefits	\$ 1,894	\$ 498	\$ (325	) \$ 2,067
Asset impairments	—	356	(356	) —
Lease termination obligations	1,200	—	—	1,200
Other	509	88	(125	) 472
Total	\$ 3,603	\$ 942	\$ (806	) \$ 3,739

(dollars in thousands)	Fiscal 2008 Restructuring Plan			
	March 31, 2010	Fiscal 2011 Provision	Payments/ Impairments	December 31, 2010
Severance and termination benefits	\$ 102	\$ —	\$ (102	) \$ —
Asset impairments	289	(289	) —	—
Lease termination obligations	411	—	(228	) 183
Total	\$ 802	\$ (289	) \$ (330	) \$ 183

Non-Operating Expenses, Net. Non-operating expense (income), 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 expense for the three and nine months ended December 31, 2010 and 2009:



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(dollars in thousands)	Three Months Ended		
	December 31,		Change
	2010	2009	
Non-Operating Expenses, Net:			
Interest Expense	\$3,049	\$3,291	\$(242 )
Interest and Miscellaneous Income	(321 )	(535 )	214
Non-Operating Expenses, Net	\$2,728	\$2,756	\$(28 )
(dollars in thousands)	Nine Months Ended		
	December 31,		Change
	2010	2009	
Non-Operating Expenses, Net:			
Interest Expense	\$9,052	\$9,504	\$(452 )
Interest and Miscellaneous Income	(671 )	(1,031 )	360
Non-Operating Expenses, Net	\$8,381	\$8,473	\$(92 )

Interest expense decreased \$0.2 million and \$0.5 million during the three month period and first nine months of fiscal 2011, respectively, as compared to the same prior year period as a result of repayment of borrowings and higher capitalized interest. Interest and miscellaneous income decreased \$0.2 million and \$0.4 million for the three month period and first nine months of fiscal 2011, respectively, as compared with the same prior year period.

Income Tax Expense. The following table compares our income tax expense and effective income tax rates for operations for the three and nine months ended December 31, 2010 to the three and nine months ended December 31, 2009:

(dollars in thousands)	Three Months Ended		Change	Percent Change
	December 31,			
	2010	2009		
Income Tax Expense	\$11,338	\$15,666	\$(4,328 )	(27.6 )%
Effective Income Tax Rate	34.3	% 27.6	%	
(dollars in thousands)	Nine Months Ended December		Change	Percent Change
	31,			
	2010	2009		
Income Tax Expense	\$7,091	\$45,250	\$(38,159 )	(84.3 )%
Effective Income Tax Rate	36.6	% 31.4	%	

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 and nine month periods ended December 31, 2010 were 34.3% and 36.6%, respectively, compared with 27.6% and 31.4%, respectively, for the same prior year periods. We benefited from favorable discrete item adjustments and tax planning initiatives during the three and nine month periods ended December 31, 2009.

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. We operate in three reportable business segments: Healthcare, Life Sciences, and Isomedix. "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. These costs include executive office costs, Board of Directors compensation, shareholder services and investor relations, external audit fees, and legacy pension and post-retirement benefit costs. Our Annual Report on Form 10-K for the year ended March 31, 2010, filed with the SEC on May 28, 2010, provides additional information regarding each business segment. The following table compares business segment revenues for the three and nine months ended December 31, 2010 to the three and nine months ended December 31,

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2009:

(dollars in thousands)	Three Months Ended		Change	Percent Change	
	December 31, 2010	2009			
Revenues:					
Healthcare	\$237,843	\$233,277	\$4,566	2.0	%
Life Sciences	51,247	58,910	(7,663)	(13.0)	)%
Isomedix	38,081	34,987	3,094	8.8	%
Total reportable segments	327,171	327,174	(3)	—	%
Corporate and other	1,112	658	454	69.0	%
Total Revenues	\$328,283	\$327,832	\$451	0.1	%

(dollars in thousands)	Nine Months Ended		Change	Percent Change	
	December 31, 2010	2009			
Revenues:					
Healthcare (1)	\$561,723	\$656,887	\$(95,164)	(14.5)	)%
Life Sciences	151,374	159,427	(8,053)	(5.1)	)%
Isomedix	113,721	105,129	8,592	8.2	%
Total reportable segments	826,818	921,443	(94,625)	(10.3)	)%
Corporate and other	2,870	4,161	(1,291)	(31.0)	)%
Total Revenues	\$829,688	\$925,604	\$(95,916)	(10.4)	)%

(1) Includes a reduction of \$102.3 million resulting from the SYSTEM 1 Rebate Program in the nine months ended December 31, 2010.

Healthcare segment revenues represented 72.5% of total revenues for the third quarter of fiscal 2011 compared with 71.2% for the same prior year period. Healthcare revenues increased \$4.6 million, or 2.0%, to \$237.8 million for the quarter ended December 31, 2010, as compared to \$233.3 million for the same prior year quarter. Capital equipment revenues grew 10.8% because of higher demand for our surgical and infection prevention products. This increase was partially offset by declines in revenues from consumables and services of 7.4% and 3.3%, respectively. The decline in consumable revenues was driven by lower demand in the United States for SYSTEM 1 consumables and reductions in consumables associated with H1N1. At December 31, 2010, the Healthcare segment's backlog amounted to \$178.5 million, increasing \$44.1 million, or 32.8%, compared to the backlog of \$134.4 million at December 31, 2009 and increasing \$24.2 million, or 15.7% compared to the backlog of \$154.3 million at September 30, 2010. The increase is driven by new products, particularly SYSTEM 1E.

Healthcare revenues decreased \$95.2 million, or (14.5)%, to \$561.7 million for the nine months ended December 31, 2010. The primary driver of the decline is the \$102.3 million negative impact of the Rebate Program. Adjusted Healthcare revenues increased \$7.1 million, or 1.1%, to \$664.0 million for the nine months ended December 31, 2010 (see subsection of MD&A titled "Non-GAAP Financial Measures" for additional information and related reconciliation of non-GAAP financial measures to the most comparable GAAP measures), as compared to \$656.9 million for the same prior year period. This increase is primarily attributable to higher capital equipment revenues within the United States which increased \$18.1 million. Consumable revenues decreased 7.5%, driven primarily by decreases within the United States attributable to lower demand for SYSTEM 1 consumables and reductions in H1N1 related products. Service revenues also decreased 2.2% with decreases in all geographies.

Life Sciences segment revenues were 15.6% of total revenues for the third quarter of fiscal 2011 as compared to 18.0% for the same prior year quarter. Life Sciences revenues decreased \$7.7 million, or 13.0%, to \$51.2 million for

the quarter ended December 31, 2010, as compared to \$58.9 million for the same prior year quarter. The decrease in Life Sciences revenues was driven by a decrease of 34.7% in capital equipment revenues, partially offset by increases in consumable and services revenues of 6.1% and 1.8%, respectively. The decline in capital equipment revenues occurred throughout key geographies although was most notable within the United States reflecting low order rates during the first half of the fiscal year. At December 31, 2010, the Life Sciences segment's backlog amounted to \$42.5 million, decreasing \$2.9 million, or 6.3% compared to the backlog of \$45.4 million at December 31, 2009. However, backlog has increased \$4.5 million, or 12.0%, compared to the backlog of \$38.0 million at September 30, 2010.



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Life Sciences revenues decreased \$8.1 million, or 5.1%, to \$151.4 million for the first nine months of fiscal 2011, as compared to \$159.4 million for the same prior year period. The decrease in Life Sciences revenues was primarily driven by a 18.9% decrease in capital equipment revenues reflecting declines in North America, Europe and Latin America. Capital equipment revenues continue to be impacted by consolidations within the industry limiting order levels from our pharmaceutical Customers. Recurring revenues grew \$3.5 million or 3.5%, reflecting consumables revenue growth of 6.8% and service revenue growth of 0.7%.

Isomedix segment revenues were 11.6% of total revenues for the third quarter of fiscal 2011 as compared to 10.7% for the same prior year quarter. The segment's revenues increased \$3.1 million, or 8.8%, to \$38.1 million for the quarter ended December 31, 2010, as compared to \$35.0 million for the same prior year quarter. Revenues were favorably impacted by increased demand from our medical device Customers, as well as modest market share gains.

The Isomedix segment experienced increased revenue of \$8.6 million, or 8.2%, to \$113.7 million during the first nine months of fiscal 2011 as compared to \$105.1 million for the same prior year period. Revenues were favorably impacted by increased demand from our medical device Customers, as well as modest market share gains.

The following table compares our business segment operating results for the three and nine months ended December 31, 2010 to the three and nine months ended December 31, 2009:

(dollars in thousands)	Three Months Ended		Change	Percent Change	
	December 31, 2010	2009			
Operating Income (Loss):					
Healthcare (1)	\$20,389	\$45,254	\$(24,865)	(54.9)	)%
Life Sciences	7,345	10,123	(2,778)	(27.4)	)%
Isomedix	10,250	6,929	3,321	47.9	%
Total reportable segments	37,984	62,306	(24,322)	(39.0)	)%
Corporate and other	(2,153)	(2,878)	) 725	(25.2)	)%
Total Operating Income	\$35,831	\$59,428	\$(23,597)	(39.7)	)%
(dollars in thousands)	Nine Months Ended		Change	Percent Change	
	December 31, 2010	2009			
Operating Income (Loss):					
Healthcare (1) (2)	\$(19,460)	) \$113,722	\$(133,182)	(117.1)	)%
Life Sciences	23,075	23,442	(367)	(1.6)	)%
Isomedix	30,858	22,669	8,189	36.1	%
Total reportable segments	34,473	159,833	(125,360)	(78.4)	)%
Corporate and other	(6,735)	(7,478)	) 743	(9.9)	)%
Total Operating Income	\$27,738	\$152,355	\$(124,617)	(81.8)	)%

(1) Includes a reduction of \$19.8 million from a class action settlement in the three and nine month periods ended December 31, 2010.

(2) Includes a reduction of \$110.0 million from the SYSTEM 1 Rebate Program in the nine month period ended December 31, 2010.

Segment operating income is calculated as the segment's gross profit less direct expenses and indirect cost allocations, which results in the full allocation of all distribution and research and development expenses, and the partial allocation of corporate costs. Corporate cost allocations are based on each segment's percentage of revenues, headcount, or other

variables in relation to those of the total Company. In addition, the Healthcare segment is responsible for the management of all but one manufacturing facility and uses standard cost to sell products to the Life Sciences segment. “Corporate and other” includes the service revenues, 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, as previously discussed.

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The Healthcare segment's operating income decreased \$24.9 million for the third quarter and \$133.2 million first nine months of fiscal 2011 as compared to the same prior year periods. The segment's operating income for the third quarter of fiscal 2011 includes the negative impact of the \$19.8 million proposed SYSTEM 1 class action settlement. The segment's operating income for the first nine months of fiscal 2011 includes the negative impacts of both the \$110.0 million Rebate Program and the \$19.8 million proposed SYSTEM 1 class action settlement. Adjusted Healthcare operating income for the third quarter of fiscal 2011 was \$40.2 million reflecting a decrease of \$5.1 million or 11.2% (see subsection of MD&A titled "Non-GAAP Financial Measures" for additional information and related reconciliation of non-GAAP financial measures to the most comparable GAAP measures). Adjusted Healthcare operating income for the first nine months of fiscal 2011 was \$110.3 million reflecting a decrease of \$3.4 million, or 3.0% when compared to the prior year period (see subsection of MD&A titled "Non-GAAP Financial Measures" for additional information and related reconciliation of non-GAAP financial measures to the most comparable GAAP measures). The decreases in operating income during the fiscal 2011 periods were driven primarily by a higher proportion of revenues coming from lower margin capital equipment revenues, lower SYSTEM 1 consumable volumes and higher commissions.

The Life Sciences segment's operating income decreased \$2.8 million and \$0.4 million for the third quarter and first nine months of fiscal 2011, respectively, as compared to the same prior year periods. The segment's operating margins were 14.3% and 15.2% for the third quarter and first nine months of fiscal 2011, respectively, representing decreases of 290 basis points and 50 basis points, respectively, over the comparable prior year periods. The decline was driven by lower volumes partially offset by favorable product mix and operating efficiencies.

The Isomedix segment's operating income increased \$3.3 million and \$8.2 million for the third quarter and first nine months of fiscal 2011, respectively, as compared to the same prior year periods. The segment's operating margins were 26.9% and 27.1% for the third quarter and first nine months of fiscal 2011, representing increases of 710 basis points and 550 basis points, respectively, over the comparable prior year periods. Fiscal 2010 third quarter operating income was negatively impacted by expenses of \$1.7 million related to the Company's decision to consolidate a facility and exit the E-beam materials modification business. Operating income in both fiscal 2011 periods reflect the benefit of increased revenues.

Liquidity and Capital Resources

The following table summarizes significant components of our cash flows for the nine months ended December 31, 2010 and 2009:

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(dollars in thousands)	Nine Months Ended December 31,	
	2010	2009
Operating activities:		
Net income	\$12,266	\$98,632
Non-cash items	430	54,304
Change in Accrued SYSTEM 1 Rebate Program and proposed class action settlement	128,770	—
Changes in operating assets and liabilities	(58,069 )	5,732
Net cash provided by operating activities	\$83,397	\$158,668
Investing activities:		
Purchases of property, plant, equipment, and intangibles, net	\$(56,390 )	\$(29,839 )
Proceeds from the sale of property, plant, equipment, and intangibles	1,298	574
Equity investment in joint venture	(16,900 )	(1,500 )
Investments in businesses, net of cash acquired	(4,000 )	—
Net cash used in investing activities	\$(75,992 )	\$(30,765 )
Financing activities:		
Proceeds under credit facilities, net	—	100,000
Repurchases of common shares	(19,900 )	(289 )
Cash dividends paid to common shareholders	\$(24,344 )	\$(137,509 )
Stock option and other equity transactions, net	10,813	12,339
Tax benefit from stock options exercised	2,197	1,927
Net cash used in financing activities	\$(31,234 )	\$(23,532 )
Debt-to-total capital ratio	21.9	% 29.7 %
Free cash flow	\$28,305	\$129,403

Net Cash Provided by Operating Activities. The net cash provided by our operating activities was \$83.4 million for the first nine months of fiscal 2011 as compared with \$158.7 million for the first nine months of fiscal 2010. The following discussion summarizes the significant changes in our operating cash flows:

Non-cash items – Our non-cash items include depreciation, depletion and amortization, share-based compensation expense, changes in deferred income taxes, and other items. Changes in our non-cash items were \$0.4 million for the first nine months of fiscal 2011 and \$54.3 million for the first nine months of fiscal 2010. Significant changes in these items for the first nine months of fiscal 2011 as compared to the same prior year period are summarized below:

Depreciation, depletion, and amortization – Depreciation, depletion, and amortization are a significant component of non-cash items. This expense totaled \$39.7 million and \$42.0 million for the first nine months of fiscal 2011 and fiscal 2010, respectively

Deferred income taxes – The change in deferred income taxes was negative \$52.7 million for the first nine months of fiscal 2011, compared with a change in deferred income taxes of positive \$1.2 million for the first nine months of fiscal 2010. The increase is attributable to the recognition of a deferred tax asset in connection with the recording of the SYSTEM 1 Rebate Program and proposed class action settlement accruals.

Share-based compensation expense – We recorded share-based compensation expense of \$8.5 million and \$5.6 million for the first nine months of fiscal 2011 and fiscal 2010, respectively.

Changes in operating assets and liabilities – Changes to our operating assets and liabilities, including the change in Accrued SYSTEM 1 Rebate Program and class action settlement, provided cash of \$70.7 million and \$5.7 million during the first nine months of fiscal 2011 and fiscal 2010, respectively.

Accounts receivable, net – Changes in our net accounts receivable balances provided cash of \$2.2 million and \$38.1 million during the first nine months of fiscal 2011 and fiscal 2010, respectively. Our accounts receivable balances may change from period to period due to the timing of revenues and Customer payments.

Inventories, net – An increase in our net inventory balances drove use of cash of \$44.9 million in the first nine months of fiscal 2011 and a decrease in net inventory balances in the first nine months of fiscal 2010 provided cash of \$9.3 million. The increase in inventory levels in fiscal 2011 is due to \$36.7 million of SYSTEM 1E inventory.

Other current assets – Our other current assets primarily consist of prepaid expenses for insurance, taxes, and other general corporate items. Changes in other current asset balances provided cash of \$4.2 million and \$3.4 million during the first nine months of fiscal 2011 and 2010, respectively.

Accounts payable – An increase in our accounts payable balance provided cash of \$7.4 million during the

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first nine months of fiscal 2011 while a decrease in our accounts payable balance used cash of \$14.8 million during the first nine months of fiscal 2010, respectively. Cash flows related to accounts payable may change from period to period due to varying payment due dates and other terms of our accounts payable obligations.

Accrued SYSTEM 1 Rebate Program and proposed class action settlement – The increase results from the establishment of the accrual in the amount of \$110.0 million for liabilities resulting from the SYSTEM 1 Rebate Program and the establishment of the accrual in the amount of \$19.8 million resulting from the proposed settlement of the SYSTEM 1 class action litigation during the first nine months of fiscal 2011, offset by rebate settlements to date of approximately \$1.0 million.

Accruals and other, net – Changes in our net accruals and other liabilities balance used cash of \$27.0 million and \$30.1 million during the first nine months of fiscal 2011 and fiscal 2010, respectively. Cash flows related to our accruals and other liabilities balances may change from period to period primarily due to the timing of accruals and payments under our incentive compensation programs. Accruals under our various incentive compensation programs rise during the course of the fiscal year and decline significantly in the first fiscal quarter as payments are made under these programs. Changes in accruals for deferred revenues also contribute to the increase or decrease in these balances.

Net Cash Used In Investing Activities – The net cash we used in investing activities totaled \$76.0 million for the first nine months of fiscal 2011 compared with \$30.8 million for the first nine months of fiscal 2010. The following discussion summarizes the significant changes in our investing cash flows for the first nine months of fiscal 2011 and fiscal 2010:

Purchases of property, plant, equipment, and intangibles, net – Capital expenditures were \$56.4 million for the first nine months of fiscal 2011 as compared to \$29.8 million during the same prior year period. Fiscal 2011 purchases include the acquisition of two previously leased Isomedix facilities totaling \$8.4 million. In addition, radioisotope purchases were higher during the first nine months of fiscal 2011 in comparison to fiscal 2010.

Proceeds from the sale of property, plant, equipment, and intangibles – During the first nine months of fiscal 2011, we recorded proceeds of \$1.3 million compared with proceeds of \$0.6 million during the first nine months of fiscal 2010.

Equity investments in joint ventures – During fiscal 2011, we increased our investment by \$16.9 million in our joint venture with VTS Medical Systems, Inc. We invested \$1.5 million in the same joint venture in fiscal 2010.

Investment in business, net of cash acquired – During fiscal 2011, we acquired a company which provides process management technology solutions designed to improve a hospital's perioperative process for \$4.0 million.

Net Cash Used In Financing Activities – The net cash used in financing activities amounted to \$31.2 million for the first nine months of fiscal 2011 compared with net cash used in financing activities of \$23.5 million for the first nine months of fiscal 2010. The following discussion summarizes the significant changes in our financing cash flows for the first nine months of fiscal 2011 and fiscal 2010:

Proceeds under credit facilities – There were no borrowing or payment activities under our credit facilities during the first nine months of fiscal 2011. Net borrowings under credit facilities totaled \$100.0 million during the first nine months of fiscal 2010.

Repurchases of common shares – The Company's Board of Directors has provided authorization to repurchase the Company's common shares. During the first nine months of fiscal 2011, we paid for the repurchase of 630,259 of our common shares under this authorization at an average purchase price of \$30.92 per common share. We also obtained 13,031 and 11,220 of our common shares during the first nine months of fiscal 2011 and fiscal 2010, respectively, in connection with stock – based compensation award programs.

Cash dividends paid to common shareholders – During the first nine months of fiscal 2011, we paid total cash dividends of \$24.3 million, or \$0.41 per outstanding common share. During the first nine months of fiscal 2010, we paid total cash dividends of \$137.5 million, or \$2.33 per outstanding common share.

Stock option and other equity transactions, net – We receive cash in some cases for issuing common shares under our various employee stock compensation programs. During the first nine months of fiscal 2011 and fiscal 2010, we

received cash proceeds totaling \$10.8 million and \$12.3 million, respectively, under these programs.

Tax benefit from stock options exercised – During the first nine months of fiscal 2011, our income taxes were reduced by \$2.2 million as a result of deductions allowed for stock options exercised. The reduction in the fiscal 2010 comparable period was \$1.9 million.

Cash Flow Measures. Free cash flow was \$28.3 million in the first nine months of fiscal 2011 compared to \$129.4 million in the prior year first nine months due to higher capital spending levels and changes in operating assets and liabilities. Our debt-to-total capital ratio was 21.9% at December 31, 2010 and 21.8% at March 31, 2010.

Sources of Credit and Contractual and Commercial Commitments. Information related to our sources of credit and contractual and commercial commitments is included in our Annual Report on Form 10-K for the year ended March 31, 2010,

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filed with the SEC on May 28, 2010. Our commercial commitments were approximately \$36.6 million at December 31, 2010 reflecting a net decrease of \$0.1 million in surety bonds and other commercial commitments from March 31, 2010. In conjunction with facility consolidation projects, we have entered into commitments aggregating approximately \$13.1 million with general contractors as of December 31, 2010. These obligations are comprised principally of construction contracts and payments are generally due within 24 months. The related construction costs are incurred and financed through operating cash flow. The maximum aggregate borrowing limits under our revolving credit facility (“Facility”) have not changed since March 31, 2010. At December 31, 2010, there was \$378.1 million available under the Facility for borrowing. The maximum aggregate borrowing limit of \$400.0 million under the Facility is reduced by outstanding borrowings and letters of credit issued under a sub-limit within the Facility (\$21.9 million at December 31, 2010).

Cash Requirements. Currently, we intend to use our existing cash and cash equivalent balances, cash generated from operations, and our existing credit facilities for short-term and long-term capital expenditures and our other liquidity needs. We believe that these amounts will be sufficient to meet working capital needs, capital requirements, and commitments for at least the next twelve months. However, our capital requirements will depend on many uncertain factors, including our rate of sales growth, our Customers’ acceptance of our products and services, the costs of obtaining adequate manufacturing capacities, the timing and extent of our research and development projects, and changes in our operating expenses. To the extent that our existing sources of cash are not sufficient to fund our future activities, we may need to raise additional funds through additional borrowings or selling equity securities. We cannot assure you that we will be able to obtain additional funds on terms favorable to us, or at all.

## Critical Accounting Policies, Estimates, and Assumptions

Information related to our critical accounting policies, estimates, and assumptions is included in our Annual Report on Form 10-K for the year ended March 31, 2010, filed with the SEC on May 28, 2010. Our critical accounting policies, estimates, and assumptions have not changed materially from March 31, 2010.

## SYSTEM 1 Rebate Program

In April 2010, we introduced the Rebate Program to Customers as a component of our transition plan for SYSTEM 1. Generally, U.S. Customers that purchased SYSTEM 1 processors directly from us or who are current users of SYSTEM 1 and who return their units have the option of either a pro-rated cash value or rebate toward the future purchase of new STERIS capital equipment or consumable products. In addition, we will provide credits for SYSTEM 1 consumables in unbroken packaging and within shelf life and for the unused portion of prepaid SYSTEM 1 service contracts.

Recording the obligations associated with the Rebate Program requires the use of estimates and assumptions. The use of estimates and assumptions involves judgments with respect to factors that may impact the ultimate outcome and may be beyond management’s control. The amount recognized during the first nine months of fiscal 2011 is based upon the quantity of SYSTEM 1 processors eligible for rebates and the estimated value of rebates to be provided upon their return. Rebates of \$102.3 million are recognized as contra-revenue consistent with other returns and allowances offered to Customers. The estimated cost of \$7.7 million to facilitate the disposal of the processors has been recognized as cost of revenues. Both components are recorded as current liabilities. Minor rebate obligations were settled during the nine months ended December 31, 2010. The key assumptions involved in the estimates associated with the Rebate Program include: the number and age of SYSTEM 1 processors eligible for rebates under the program, the number of Customers that will elect to participate in the Rebate Program, the proportion of Customers that will choose each rebate option, and the estimated per unit costs of disposal.



The number and age of SYSTEM 1 processors has been estimated based on our historical sales and service records and we have assumed that 100% of these Customers will elect to participate in the Rebate Program. In order to estimate the portion of Customers that will choose each available rebate option, we first assessed recent trends in sales of the proprietary consumable products utilized in the SYSTEM 1 processor. We noted a decline of approximately 19% in shipments which indicates that a portion of our Customers have already transitioned away from the SYSTEM 1 technology. The remaining 81%, provides the best available indication of the portion of Customers likely to elect the rebate for the SYSTEM 1E processor. Order and quote data for fiscal 2011 year to date provides indications of the proportion of Customers that are expected to choose each of the other rebate options. The per unit costs associated with disposal were estimated based on the service hours involved and quotes from our vendors which are based on current freight and disposal contracts.

Our assumptions regarding the response of our Customers to the Rebate Program could be wrong and actual results could be different from these estimates. For example, if all Customers elected the maximum incentive rebate associated with the SYSTEM 1E processor rebate, the total estimated rebate liability of \$102.3 million would increase to approximately \$111.0

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million. Conversely, if all Customers elected the cash rebate option, the total estimated rebate liability would decrease to approximately \$52.0 million.

In December of 2010, we began shipping SYSTEM 1E units in limited numbers, after having received FDA clearance for the SYSTEM 1E chemical indicator, which is used in conjunction with the SYSTEM 1E. We have also requested FDA clearance or approval of certain other accessories for SYSTEM 1E, although neither the chemical indicator nor these other accessories are required by regulation to sell or operate the device. No assurance can be made that the FDA will agree with our submissions or requests.

## Contingencies

We are involved in various patent, product liability, consumer, commercial, environmental, tax proceedings and claims, governmental investigations, and other legal and regulatory proceedings that arise from time to time in the course of our business. We record a liability for such contingencies to the extent that we conclude that their occurrence is both probable and estimable. We consider many factors in making these assessments, including the professional judgment of experienced members of management and our legal counsel. We have made estimates as to the likelihood of unfavorable outcomes and the amounts of such potential losses. In our opinion, the ultimate outcome of these proceedings and of claims that are probable and estimable is not anticipated to have a material adverse affect on our consolidated financial position, results of operations, or cash flows. However, the ultimate outcome of claims, litigation, and other proceedings is unpredictable and actual results could be materially different from our estimates. We record anticipated recoveries under applicable insurance contracts when assured of recovery. Refer to Part II, Item 1, "Legal Proceedings" for additional information.

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 tax jurisdiction or the closing of a statute of limitation. Changes in applicable tax law or other events may also require us to revise past estimates. The IRS routinely conducts audits of our federal income tax returns. In the second quarter of fiscal 2010, we reached a settlement with the IRS on all material tax matters for fiscal 2006 through fiscal 2007. The IRS also began its audit of fiscal 2008 and fiscal 2009 in fiscal 2010. We remain subject to tax authority audits in various other jurisdictions in which we operate. If we prevail in matters for which accruals have been recorded, or are required to pay amounts in excess of recorded accruals, our effective income tax rate in a given financial statement period could be materially impacted.

Additional information regarding our commitments and contingencies is included in note 10 to our consolidated financial statements titled, "Contingencies."

## 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 third quarter of fiscal 2011, our revenues were unfavorably impacted by \$1.4 million, or 0.4%, and income before taxes was unfavorably impacted by \$0.4 million, or 1.3%, as a result of foreign currency movements relative to the U.S. dollar. During the first nine months of fiscal 2011, our revenues were unfavorably impacted by \$2.0 million, or 0.2%, and income before income taxes was unfavorably impacted by \$0.2 million, or 1.1% as compared to the same prior year period.

## Forward-Looking Statements

This Quarterly Report on Form 10-Q may contain statements concerning certain trends, expectations, forecasts, estimates, or other forward-looking information affecting or relating to the Company or its industry, products or

activities that are intended to qualify for the protections afforded “forward-looking statements” under the Private Securities Litigation Reform Act of 1995 and other laws and regulations. Forward-looking statements speak only as to the date of this report, and may be identified by the use of forward-looking terms such as “may,” “will,” “expects,” “believes,” “anticipates,” “plans,” “estimates,” “projects,” “targets,” “forecasts,” “outlook,” “impact,” “potential,” “confidence,” “improve,” “comfortable,” “trend”, and “seeks,” or the negative of such terms or other variations on such terms or comparable terminology. Many important factors could cause actual results to differ materially from those in the forward-looking statements including, without limitation, disruption of production or supplies, changes in market conditions, political events, pending or future claims or litigation, competitive factors, technology advances, actions of regulatory agencies, and changes in laws, government regulations, labeling or product approvals or the application or interpretation thereof. Other risk factors are described herein and in the Company's Form 10-K and other securities filings. Many of these important factors are outside STERIS's control. No assurances can be provided as to any result or the timing of any outcome regarding matters described herein or otherwise with

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respect to any regulatory action, administrative proceedings, government investigations, litigation, warning letters, consent decree, rebate program, transition, cost reductions, business strategies, earnings and revenue trends, expense reduction or other future financial results, including the outcome of the proposed settlement of the SYSTEM 1 class action litigation. References to products, the consent decree, the transition or rebate program, or the settlement agreement are summaries only and do not alter or modify the specific terms of the decree, agreement, program or product clearance or literature. Unless legally required, the Company does not undertake to update or revise any forward-looking statements even if events make clear that any projected results, express or implied, will not be realized. Other potential risks and uncertainties that could cause actual results to differ materially from those in the forward-looking statements include, without limitation, (a) the potential for increased pressure on pricing that leads to erosion of profit margins, (b) the possibility that market demand will not develop for new technologies, products or applications or the Company's rebate program, transition plan or other business initiatives will take longer, cost more or produce lower benefits than anticipated, (c) the possibility that application of or compliance with laws, court rulings, certifications, regulations, regulatory actions, including without limitation those relating to previously disclosed FDA warning letters, government investigations, the December 3, 2009 or February 22, 2010 FDA notices, the April 20, 2010 consent decree and related transition plan and rebate program, the SYSTEM 1E device, the Reliance EPS System, the outcome of any pending FDA requests and clearances or other requirements or standards may delay, limit or prevent new product introductions, affect the production and marketing of existing products or services or otherwise affect Company performance, results, prospects or value, (d) the potential of international unrest or effects of fluctuations in currencies, tax assessments or anticipated rates, raw material costs, benefit or retirement plan costs, or other regulatory compliance costs, (e) the possibility of reduced demand, or reductions in the rate of growth in demand, for the Company's products and services, (f) the possibility that anticipated growth, cost savings, rebate assumptions, new product acceptance or approvals, including without limitation SYSTEM 1E and accessories thereto, or other results may not be achieved, or that transition, labor, competition, timing, execution, regulatory, governmental, or other issues or risks associated with our business, industry or initiatives including, without limitation, the consent decree, the transition from the SYSTEM 1 processing system, or those matters described in our Form 10-K for the year ended March 31, 2010 and this Form 10-Q and other securities filings may adversely impact company performance, results, prospects or value, (g) the effect of the contraction in credit availability, as well as the ability of our Customers and suppliers to adequately access the credit markets when needed, and (h) those risks described in our Annual Report on Form 10-K for the year ended March 31, 2010 and this Form 10-Q for the quarter ended December 31, 2010.

Availability of Securities and Exchange Commission Filings

We make available free of charge on or through our website our Annual Reports on Form 10-K, Quarterly Reports on Form 10-Q, Current Reports on Form 8-K, and amendments to these reports as soon as reasonably practicable after we file such material with, or furnish such material to, the SEC. You may access these documents on the Investor Relations page of our website at <http://www.steris-ir.com>. The information on our website is not incorporated by reference into this report. You may also obtain copies of these documents by visiting the SEC's Public Reference Room at 100 F Street, NE, Washington, D.C. 20549, or by accessing the SEC's website at <http://www.sec.gov>. You may obtain information on the Public Reference Room by calling the SEC at 1-800-SEC-0330.

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PART II—OTHER INFORMATION

ITEM 6. EXHIBITS

Exhibits required by Item 601 of Regulation S-K

Exhibit Number	Exhibit Description
31.1	Certification of the Principal Executive Officer Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
31.2	Certification of the Principal Financial Officer Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.

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SIGNATURE

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

STERIS Corporation

/S/ MICHAEL J. TOKICH

Michael J. Tokich

Senior Vice President and Chief Financial Officer

June 23, 2011

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