

UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION  
Washington, D.C. 20549  
FORM 10-Q

(Mark One)

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

For the quarterly period ended September 29, 2018

or

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

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

Commission File Number: 0-27078

**HENRY SCHEIN, INC.**

(Exact name of registrant as specified in its charter)

**Delaware**  
(State or other jurisdiction of  
incorporation or organization)

**11-3136595**  
(I.R.S. Employer Identification No.)

**135 Duryea Road**  
**Melville, New York**  
(Address of principal executive offices)

**11747**  
(Zip Code)

**(631) 843-5500**  
(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

No

Indicate by check mark whether the registrant has submitted electronically 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 such files).

Yes

No

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

Large accelerated filer

Accelerated filer

Non-accelerated filer

Smaller reporting company

Emerging growth company

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

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

Yes

No

As of October 29, 2018, there were 152,437,680 shares of the registrant's common stock outstanding.

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HENRY SCHEIN, INC.

INDEX

Page

**PART I. FINANCIAL INFORMATION**

**ITEM 1. Consolidated Financial Statements:**

<u>Balance Sheets as of September 29, 2018 and December 30, 2017</u> .....	3
<u>Statements of Income for the three and nine months ended</u> <u>September 29, 2018 and September 30, 2017</u> .....	4
<u>Statements of Comprehensive Income for the three and nine months ended</u> <u>September 29, 2018 and September 30, 2017</u> .....	5
<u>Statement of Changes in Stockholders' Equity for the nine months ended</u> <u>September 29, 2018</u> .....	6
<u>Statements of Cash Flows for the nine months ended</u> <u>September 29, 2018 and September 30, 2017</u> .....	7
<u>Notes to Consolidated Financial Statements</u> .....	8
<u>Note 1 - Basis of Presentation</u> .....	8
<u>Note 2 – Accounting Pronouncements Adopted and Critical Accounting Policies and Estimates</u> .....	9
<u>Note 3 – Revenue from Contracts with Customers</u> .....	14
<u>Note 4 – Segment Data</u> .....	15
<u>Note 5 - Debt</u> .....	16
<u>Note 6 – Redeemable Noncontrolling Interests</u> .....	18
<u>Note 7 – Comprehensive Income</u> .....	19
<u>Note 8 – Fair Value Measurements</u> .....	21
<u>Note 9 – Business Acquisitions and Planned Divestiture</u> .....	24
<u>Note 10 – Plans of Restructuring</u> .....	26
<u>Note 11 – Earnings Per Share</u> .....	27
<u>Note 12 – Income Taxes</u> .....	27
<u>Note 13 – Derivatives and Hedging Activities</u> .....	29
<u>Note 14 – Stock-Based Compensation</u> .....	29
<u>Note 15 – Supplemental Cash Flow Information</u> .....	31
<u>Note 16 – Legal Proceedings</u> .....	32

**ITEM 2. Management's Discussion and Analysis of**

<u>Financial Condition and Results of Operations</u> .....	36
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<b><u>ITEM 3. Quantitative and Qualitative Disclosures About Market Risk</u></b> .....	65
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<b><u>ITEM 4. Controls and Procedures</u></b> .....	66
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**PART II. OTHER INFORMATION**

<b><u>ITEM 1. Legal Proceedings</u></b> .....	67
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<b><u>ITEM 1A. Risk Factors</u></b> .....	71
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<b><u>ITEM 2. Unregistered Sales of Equity Securities and Use of Proceeds</u></b> .....	71
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<a href="#">ITEM 6. Exhibits</a> .....	72
<a href="#">Signature</a> .....	73



**PART I. FINANCIAL INFORMATION**  
**ITEM 1. CONSOLIDATED FINANCIAL STATEMENTS**  
**HENRY SCHEIN, INC.**  
**CONSOLIDATED BALANCE SHEETS**  
(in thousands, except share and per share data)

	September 29, December 30,	
	2018	2017
	(unaudited)	
<b>ASSETS</b>		
Current assets:		
Cash and cash equivalents .....	\$ 119,740	\$ 174,658
Accounts receivable, net of reserves of \$55,289 and \$53,832.....	1,627,640	1,522,807
Inventories, net .....	1,932,855	1,933,803
Prepaid expenses and other .....	513,717	454,752
<b>Total current assets .....</b>	<b>4,193,952</b>	<b>4,086,020</b>
Property and equipment, net .....	374,051	375,001
Goodwill .....	2,685,681	2,301,331
Other intangibles, net .....	618,201	669,641
Investments and other .....	518,425	432,002
<b>Total assets .....</b>	<b>\$ 8,390,310</b>	<b>\$ 7,863,995</b>
<b>LIABILITIES AND STOCKHOLDERS' EQUITY</b>		
Current liabilities:		
Accounts payable .....	\$ 1,136,120	\$ 1,153,012
Bank credit lines .....	1,144,881	741,653
Current maturities of long-term debt .....	12,482	16,659
Accrued expenses:		
Payroll and related .....	259,180	272,998
Taxes .....	180,163	188,873
Other .....	496,959	455,780
<b>Total current liabilities .....</b>	<b>3,229,785</b>	<b>2,828,975</b>
Long-term debt .....	1,000,315	907,756
Deferred income taxes .....	45,947	50,431
Other liabilities .....	415,045	420,285
<b>Total liabilities .....</b>	<b>4,691,092</b>	<b>4,207,447</b>
Redeemable noncontrolling interests .....	282,502	832,138
Commitments and contingencies .....		
Stockholders' equity:		
Preferred stock, \$.01 par value, 1,000,000 shares authorized, none outstanding .....	-	-
Common stock, \$.01 par value, 480,000,000 shares authorized, 152,437,680 outstanding on September 29, 2018 and 240,000,000 shares authorized, 153,690,146 outstanding on December 30, 2017.....	1,524	1,537
Retained earnings .....	3,191,260	2,940,029
Accumulated other comprehensive loss .....	(219,649)	(130,067)
<b>Total Henry Schein, Inc. stockholders' equity .....</b>	<b>2,973,135</b>	<b>2,811,499</b>
Noncontrolling interests .....	443,581	12,911
<b>Total stockholders' equity .....</b>	<b>3,416,716</b>	<b>2,824,410</b>
<b>Total liabilities, redeemable noncontrolling interests and stockholders' equity.....</b>	<b>\$ 8,390,310</b>	<b>\$ 7,863,995</b>

See accompanying notes.

**HENRY SCHEIN, INC.**  
**CONSOLIDATED STATEMENTS OF INCOME**  
(in thousands, except per share data)  
(unaudited)

	Three Months Ended		Nine Months Ended	
	September 29, 2018	September 30, 2017	September 29, 2018	September 30, 2017
Net sales .....	\$ 3,279,678	\$ 3,161,083	\$ 9,826,793	\$ 9,143,489
Cost of sales .....	2,391,118	2,325,029	7,141,569	6,645,342
Gross profit .....	888,560	836,054	2,685,224	2,498,147
Operating expenses:				
Selling, general and administrative .....	668,011	622,506	2,027,138	1,874,644
Litigation settlements .....	38,488	-	38,488	5,325
Transaction costs related to Animal Health spin-off.....	7,282	-	18,670	-
Restructuring costs .....	8,853	-	27,511	-
Operating income .....	165,926	213,548	573,417	618,178
Other income (expense):				
Interest income .....	5,163	4,793	15,429	13,204
Interest expense .....	(21,045)	(13,428)	(56,466)	(37,056)
Other, net .....	(346)	(194)	(802)	489
Income before taxes and equity in earnings				
of affiliates .....	149,698	204,719	531,578	594,815
Income taxes .....	(29,401)	(59,340)	(124,084)	(156,276)
Equity in earnings of affiliates .....	6,679	5,569	15,622	12,244
Net income .....	126,976	150,948	423,116	450,783
Less: Net income attributable to noncontrolling interests .....	(5,498)	(12,917)	(20,208)	(35,949)
Net income attributable to Henry Schein, Inc. ....	\$ 121,478	\$ 138,031	\$ 402,908	\$ 414,834
<b>Earnings per share attributable to Henry Schein, Inc.:</b>				
Basic .....	\$ 0.80	\$ 0.88	\$ 2.63	\$ 2.64
Diluted .....	\$ 0.79	\$ 0.87	\$ 2.62	\$ 2.61
Weighted-average common shares outstanding:				
Basic .....	152,533	156,914	152,970	157,386
Diluted .....	153,614	158,271	153,982	158,866

See accompanying notes.

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**HENRY SCHEIN, INC.**  
**CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME**  
**(in thousands)**  
**(unaudited)**

	Three Months Ended		Nine Months Ended	
	September 29, 2018	September 30, 2017	September 29, 2018	September 30, 2017
Net income .....	\$ 126,976	\$ 150,948	\$ 423,116	\$ 450,783
Other comprehensive income (loss), net of tax:				
Foreign currency translation gain (loss).....	(10,582)	58,916	(106,154)	173,166
Unrealized gain (loss) from foreign currency hedging activities .....	(379)	(34)	674	(1,274)
Unrealized investment loss .....	(1)	(2)	(2)	(2)
Pension adjustment gain (loss).....	116	(353)	1,056	(1,063)
Other comprehensive income (loss), net of tax .....	(10,846)	58,527	(104,426)	170,827
Comprehensive income .....	116,130	209,475	318,690	621,610
Comprehensive income attributable to noncontrolling interests:				
Net income .....	(5,498)	(12,917)	(20,208)	(35,949)
Foreign currency translation (gain) loss.....	2,589	(3,473)	14,844	(8,258)
Comprehensive income attributable to noncontrolling interests .....	(2,909)	(16,390)	(5,364)	(44,207)
Comprehensive income attributable to Henry Schein, Inc. ....	\$ 113,221	\$ 193,085	\$ 313,326	\$ 577,403

See accompanying notes.

**HENRY SCHEIN, INC.**  
**CONSOLIDATED STATEMENT OF CHANGES IN STOCKHOLDERS' EQUITY**  
(in thousands, except share and per share data)  
(unaudited)

	Common Stock		Additional Paid-in Capital	Retained Earnings	Accumulated Other		Noncontrolling Interests	Total Stockholders' Equity
	Shares	Amount			Income/Loss			
Balance, December 30, 2017	153,690,146	\$ 1,537	\$ -	\$ 2,940,029	\$ (130,067)	\$ -	12,911	\$ 2,824,410
Cumulative impact of adopting new accounting standards (Note 2)	-	-	-	2,594	-	-	-	2,594
Net income (excluding \$17,019 attributable to Redeemable noncontrolling interests)	-	-	-	402,908	-	-	3,189	406,097
Foreign currency translation loss (excluding loss of \$13,752 attributable to Redeemable noncontrolling interests)	-	-	-	-	(91,310)	(1,092)	-	(92,402)
Unrealized gain from foreign currency hedging activities, net of tax of \$405	-	-	-	-	-	674	-	674
Unrealized investment loss, net of tax of \$0	-	-	-	-	(2)	-	-	(2)
Pension adjustment gain, including tax of \$593	-	-	-	-	-	1,056	-	1,056
Dividends paid	-	-	-	-	-	-	(396)	(396)
Other adjustments	-	-	(11)	-	-	-	712	701
Purchase of noncontrolling interests	-	-	-	-	-	-	(207)	(207)
Change in fair value of redeemable securities	-	-	(119,695)	-	-	-	-	(119,695)
Initial noncontrolling interests and adjustments related to business acquisitions	-	-	-	-	-	-	428,464	428,464
Repurchase and retirement of common stock	(1,521,208)	(15)	(20,865)	(93,226)	-	-	-	(114,106)
Stock issued upon exercise of stock options	153,516	1	3,075	-	-	-	-	3,076
Stock-based compensation expense	379,428	4	34,231	-	-	-	-	34,235
Shares withheld for payroll taxes	(267,573)	(3)	(18,107)	-	-	-	-	(18,110)
Settlement of stock-based compensation awards	3,371	-	(642)	-	-	-	-	(642)
Deferred tax benefit arising from acquisition of noncontrolling interest in partnership	-	-	60,969	-	-	-	-	60,969
Transfer of charges in excess of capital	-	-	61,045	(61,045)	-	-	-	-
Balance, September 29, 2018	152,437,680	\$ 1,524	\$ -	\$ 3,191,260	\$ (219,649)	\$ -	443,581	\$ 3,416,716

See accompanying notes.

**HENRY SCHEIN, INC.**  
**CONSOLIDATED STATEMENTS OF CASH FLOWS**  
(in thousands)  
(unaudited)

	Nine Months Ended	
	September 29, 2018	September 30, 2017
<b>Cash flows from operating activities:</b>		
Net income .....	\$ 423,116	\$ 450,783
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization .....	155,089	141,278
Stock-based compensation expense .....	34,235	31,987
Provision for losses on trade and other accounts receivable .....	7,870	6,981
Provision for (benefit from) deferred income taxes .....	(6,282)	8,600
Equity in earnings of affiliates .....	(15,622)	(12,244)
Distributions from equity affiliates .....	15,534	16,826
Changes in unrecognized tax benefits .....	2,853	(6,653)
Other .....	590	6,031
Changes in operating assets and liabilities, net of acquisitions:		
Accounts receivable .....	(155,579)	(226,577)
Inventories .....	(35,300)	27,336
Other current assets .....	(81,774)	(70,833)
Accounts payable and accrued expenses .....	46,024	(66,014)
Net cash provided by operating activities .....	<u>390,754</u>	<u>307,501</u>
<b>Cash flows from investing activities:</b>		
Purchases of fixed assets .....	(61,826)	(55,315)
Payments for equity investments and business acquisitions, net of cash acquired .....	(47,325)	(258,786)
Other .....	(37,206)	(6,694)
Net cash used in investing activities .....	<u>(146,357)</u>	<u>(320,795)</u>
<b>Cash flows from financing activities:</b>		
Proceeds from bank borrowings .....	404,098	193,550
Proceeds from issuance of long-term debt .....	115,000	200,440
Principal payments for long-term debt .....	(27,621)	(59,531)
Debt issuance costs .....	(395)	(1,771)
Proceeds from issuance of stock upon exercise of stock options .....	3,076	4,941
Payments for repurchases of common stock .....	(114,106)	(225,005)
Payments for taxes related to shares withheld for employee taxes .....	(17,903)	(44,721)
Distributions to noncontrolling stockholders .....	(15,767)	(23,921)
Acquisitions of noncontrolling interests in subsidiaries .....	(664,898)	(27,914)
Net cash provided by (used in) financing activities .....	<u>(318,516)</u>	<u>16,068</u>
Effect of exchange rate changes on cash and cash equivalents .....	19,201	14,724
Net change in cash and cash equivalents .....	(54,918)	17,498
Cash and cash equivalents, beginning of period .....	174,658	62,381
Cash and cash equivalents, end of period .....	<u>\$ 119,740</u>	<u>\$ 79,879</u>

See accompanying notes.



**HENRY SCHEIN, INC.**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**  
**(in thousands, except per share data)**  
**(unaudited)**

**Note 1 – Basis of Presentation**

Our consolidated financial statements include our accounts, as well as those of our wholly owned and majority owned subsidiaries. Certain prior period amounts have been reclassified to conform to the current period presentation.

Our accompanying unaudited consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States (“U.S. GAAP”) for interim financial information 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 footnote disclosures required by U.S. GAAP for complete financial statements.

The consolidated financial statements reflect all adjustments considered necessary for a fair presentation of the consolidated results of operations and financial position for the interim periods presented. All such adjustments are of a normal recurring nature. These unaudited interim consolidated financial statements should be read in conjunction with the audited consolidated financial statements and notes to the consolidated financial statements contained in our Annual Report on Form 10-K for the year ended December 30, 2017.

The preparation of financial statements in conformity with U.S. GAAP requires us to make estimates and assumptions that affect the reported amounts of assets and liabilities, and disclosure of contingent assets and liabilities, at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates. The results of operations for the nine months ended September 29, 2018 are not necessarily indicative of the results to be expected for any other interim period or for the year ending December 29, 2018.

On August 16, 2017, we announced that our Board of Directors approved a 2-for-1 split of our common stock. Each Henry Schein, Inc. stockholder of record at the close of business on September 1, 2017 received a dividend of one additional share for every share held. Trading began on a split-adjusted basis on September 15, 2017 and has been retroactively reflected for all periods presented in this Form 10-Q. As a result of the stock split, we increased our authorized common shares from 240,000,000 to 480,000,000, effective May 31, 2018.



**HENRY SCHEIN, INC.**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**  
**(in thousands, except per share data)**  
**(unaudited)**

**Note 2 – Accounting Pronouncements Adopted and Critical Accounting Policies and Estimates**

**Accounting Pronouncements Adopted**

In May 2014, the Financial Accounting Standards Board (“FASB”) issued Accounting Standard Update (“ASU”) No. 2014-09, “Revenue from Contracts with Customers”, Accounting Standards Codification (“ASC”) 606 (“Topic 606”). We adopted the provisions of this standard as of December 31, 2017, on a modified retrospective basis. We applied the requirements of the new standard only to contracts that were not completed as of the adoption date. We recorded an immaterial adjustment to the opening balance of retained earnings for the adoption of Topic 606. The comparative information has not been restated and continues to be reported under the accounting standards in effect for those periods.

The impact of the new standard on our consolidated statements of income, which we expect to be immaterial on an ongoing basis, is primarily related to software sales and sales commissions and is described as follows:

*Software Sales*

For software licenses sold together with post contract support (PCS), we previously deferred software revenue if it did not have vendor-specific evidence of fair value of the PCS. Under Topic 606, the concept of vendor-specific objective evidence is eliminated and there are no cases where revenue is deferred due to a lack of standalone selling price. In addition, we previously recognized revenue from term licenses ratably over the contract term. Under Topic 606, such licenses represent a right to use intellectual property and therefore require upfront recognition. Furthermore, certain upfront fees related to service arrangements were previously deferred and recognized over the estimated customer life. Under Topic 606, the period over which we will recognize these fees is reduced, as the upfront fee represents additional contract price which will be allocated to the performance obligations in the contract and recognized as those performance obligations are satisfied, rather than being amortized over the estimated customer life. Based on the aforementioned changes, such software revenue will be recognized sooner than under the previous revenue recognition standard.

*Sales Commissions*

We previously recognized sales commissions as an expense when incurred. Under Topic 606, we defer such sales commissions as costs to obtain a contract when the costs are incremental and expected to be recovered. Deferred sales commissions are amortized over the estimated customer relationship period. We apply the practical expedient to expense, as incurred, commissions with an expected amortization period of one year or less.



**HENRY SCHEIN, INC.**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**  
(in thousands, except per share data)  
(unaudited)

The impact of adoption on our consolidated balance sheet and income statement was as follows:

Balance Sheet	As of September 29, 2018		
	As Reported	Balances Without Adoption of Topic 606	Effect of Change Increase/(Decrease)
<b>Assets:</b>			
Prepaid expenses and other .....	\$ 513,717	\$ 514,043	\$ (326)
Investments and other .....	518,425	516,409	2,016
<b>Liabilities:</b>			
Accrued expenses - Taxes.....	\$ 180,163	\$ 179,748	\$ 415
Accrued expenses - Other .....	496,959	499,603	(2,644)
Deferred income taxes .....	45,947	45,340	607
Other liabilities (long-term) .....	415,045	415,594	(549)
<b>Stockholders' equity:</b>			
Retained earnings .....	\$ 3,191,260	\$ 3,187,304	\$ 3,956
Accumulated other comprehensive loss .....	\$ (219,649)	\$ (219,554)	\$ (95)

Statement of Income	Three Months Ended September 29, 2018			Nine Months Ended September 29, 2018		
	As Reported	Balances Without Adoption of Topic 606	Effect of Change Increase/(Decrease)	As Reported	Balances Without Adoption of Topic 606	Effect of Change Increase/(Decrease)
<b>Net sales:</b>						
Dental .....	\$1,514,538	\$ 1,514,538	\$ -	\$4,675,212	\$ 4,675,212	\$ -
Animal Health .....	899,295	899,295	-	2,805,031	2,805,031	-
Medical .....	721,942	721,942	-	1,976,367	1,976,367	-
Total healthcare distribution .....	\$3,135,775	\$ 3,135,775	\$ -	\$9,456,610	\$ 9,456,610	\$ -
Technology and value-added services .....	143,903	143,420	483	370,183	369,459	724
<b>Total .....</b>	<b>\$3,279,678</b>	<b>\$ 3,279,195</b>	<b>\$ 483</b>	<b>\$9,826,793</b>	<b>\$ 9,826,069</b>	<b>\$ 724</b>
<b>Costs and expenses:</b>						
Cost of sales .....	2,391,118	2,391,118	-	7,141,569	7,141,569	-
Selling, general and administrative .....	722,634	722,842	(208)	2,111,807	2,112,058	(251)
Income taxes .....	(29,401)	(29,265)	136	(124,084)	(123,861)	223
<b>Net income .....</b>	<b>\$ 126,976</b>	<b>\$ 126,421</b>	<b>\$ 555</b>	<b>\$ 423,116</b>	<b>\$ 422,364</b>	<b>\$ 752</b>

Additional information related to Topic 606 can be found below in "Critical Accounting Policies and Estimates" as well as in Note 3.

In October 2016, the FASB issued ASU No. 2016-16, "Income Taxes, Intra-Entity Transfers of Assets Other Than Inventory" ("Topic 740"). Topic 740 requires companies to recognize the income tax effects of intercompany sales and transfers of assets other than inventory in the period which the transfer occurs. Previously, companies were required to defer the income tax effects on intercompany transfer of assets until the asset has been sold to an outside party. On December 31, 2017, we adopted the guidance, which is effective for annual periods and related interim periods beginning after December 15, 2017 on a modified retrospective basis. As a result of the adoption of Topic 740, we have recorded an immaterial adjustment to the opening balance of retained earnings and a reduction to prepaid assets.

In May 2017, the FASB issued ASU No. 2017-09, "Compensation-Stock Compensation (Topic 718), Scope of Modification Accounting". ASU No. 2017-09 provides guidance on determining which changes to the terms



**HENRY SCHEIN, INC.**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**  
(in thousands, except per share data)  
(unaudited)

and conditions of share-based payment awards require an entity to apply modification accounting. ASU 2017-09 requires modification accounting if the fair value, vesting conditions, or equity or liability classification of the award is not the same immediately before and after a change to the terms and conditions of the award. ASU 2017-09 was adopted on a prospective basis as of December 31, 2017 and did not have a material impact on the consolidated financial statements or disclosures as of September 29, 2018.

The cumulative effect of the changes made to our consolidated balance sheet as of December 31, 2017 related to Topic 606 and Topic 740 were as follows:

	Balance at December 30, 2017 (As Reported)	Adjustments Due To Topic 606	Adjustments Due To Topic 740	Balance at December 31, 2017
<b>Assets:</b>				
Prepaid expenses and other .....	\$ 454,752	\$ 119	\$ (610)	\$ 454,261
Investments and other .....	432,002	1,133	-	433,135
<b>Liabilities:</b>				
Accrued expenses - Taxes.....	\$ 188,873	\$ 437	\$ -	\$ 189,310
Accrued expenses - Other .....	455,780	(2,614)	-	453,166
Deferred income taxes .....	50,431	471	-	50,902
Other liabilities (long-term) .....	420,285	(246)	-	420,039
<b>Stockholders' equity:</b>				
Retained earnings .....	\$ 2,940,029	\$ 3,204	\$ (610)	\$ 2,942,623

**Critical Accounting Policies and Estimates**

There have been no material changes in our critical accounting policies and estimates from those disclosed in Item 7 of our Annual Report on Form 10-K for the year ended December 30, 2017 (the "2017 Form 10-K"), except as follows:

*Revenue Recognition*

On December 31, 2017, we adopted Topic 606 using the modified retrospective method applied to those contracts which were not completed as of the adoption date. Results for reporting periods beginning after December 30, 2017 are presented under Topic 606, while prior period amounts are not adjusted and continue to be reported under the accounting standards in effect for those periods. Our revenue recognition accounting policies applied prior to adoption of Topic 606 are outlined in the financial statements in the 2017 Form 10-K. The disclosures included herein reflect our accounting policies under Topic 606.

We generate revenue from the sale of dental, animal health and medical consumable products, as well as equipment, software products and services and other sources. Provisions for discounts, rebates to customers, customer returns and other contra revenue adjustments are included in the transaction price at contract inception by estimating the most likely amount based upon historical data and estimates and are provided for in the period in which the related sales are recognized.

Revenue derived from the sale of consumable products is recognized at a point in time when control transfers to the customer. Such sales typically entail high-volume, low-dollar orders shipped using third-party common carriers. We believe that the shipment date is the most appropriate point in time indicating control has transferred to the customer because we have no post-shipment obligations and this is when legal title and risks and rewards of ownership transfer to the customer and the point at which we have an enforceable right to



**HENRY SCHEIN, INC.**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**  
**(in thousands, except per share data)**  
**(unaudited)**

payment.

Revenue derived from the sale of equipment is recognized when control transfers to the customer. This occurs when the equipment is delivered.

Such sales typically entail scheduled deliveries of large equipment primarily by equipment service technicians. Some equipment sales require minimal installation, which is typically Our product generally carries standard warranty terms provided by the manufacturer, however, in instances where we provide warranty labor services, the warranty costs are accrued in accordance with ASC 460 "Guarantees".

Revenue derived from the sale of software products is recognized when products are shipped to customers or made available electronically. Such software is generally installed by customers and does not require extensive training due to the nature of its design. Revenue derived from post-contract customer support for software, including annual support and/or training, is generally recognized over time using time elapsed as the input method that best depicts the transfer of control to the customer.

Revenue derived from other sources, including freight charges, equipment repairs and financial services, is recognized when the related product revenue is recognized or when the services are provided. We apply the practical expedient to treat shipping and handling activities performed after the customer obtains control as fulfillment activities, rather than a separate performance obligation in the contract.

Sales, value-add and other taxes we collect concurrent with revenue-producing activities are excluded from revenue.

Certain of our revenue is derived from bundled arrangements that include multiple distinct performance obligations which are accounted for separately. When we sell software products together with related services (i.e., training and technical support), we allocate revenue to software using the residual method, using an estimate of the standalone selling price to estimate the fair value of the undelivered elements. There are no cases where revenue is deferred due to a lack of a standalone selling price. Bundled arrangements that include elements that are not considered software consist primarily of equipment and the related installation service. We allocate revenue for such arrangements based on the relative selling prices of the goods or services. If an observable selling price is not available (i.e., we do not sell the goods or services separately), we use one of the following techniques to estimate the standalone selling price: adjusted market approach; cost-plus approach; or the residual method. There is no specific hierarchy for the use of these methods, but the estimated selling price reflects our best estimate of what the selling prices of each deliverable would be if it were sold regularly on a standalone basis taking into consideration the cost structure of our business, technical skill required, customer location and other market conditions.

*Accounts Receivable*

The carrying amount of accounts receivable is reduced by a valuation allowance that reflects our best estimate of the amounts that will not be collected. In addition to reviewing delinquent accounts receivable, we consider many factors in estimating our reserve, including historical data, experience, customer types, credit worthiness and economic trends. From time to time, we adjust our assumptions for anticipated changes in any of these or other factors expected to affect collectability.

*Contract Assets*

Contract assets include amounts related to any conditional right to consideration for work completed but not billed as of the reporting date and generally represent amounts owed to us by customers, but not yet billed. Contract assets are transferred to accounts receivable when the right becomes unconditional. Current contract assets are included in Prepaid expenses and other and the non-current contract assets are included in Investments



**HENRY SCHEIN, INC.**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**  
**(in thousands, except per share data)**  
**(unaudited)**

and other within our consolidated balance sheet.

*Contract Liabilities*

Contract liabilities are comprised of advance payments and deferred revenue amounts. Contract liabilities are transferred to revenue once the performance obligation has been satisfied. Current contract liabilities are included in Accrued expenses: Other and the non-current contract liabilities are included in Other liabilities within our consolidated balance sheet.

*Deferred Commissions*

Sales commissions earned by our sales force that relate to long term arrangements are capitalized as costs to obtain a contract when the costs incurred are incremental and are expected to be recovered. Deferred sales commissions are amortized over the estimated customer relationship period. We apply the practical expedient related to the capitalization of incremental costs of obtaining a contract, and recognize such costs as an expense when incurred if the amortization period of the assets that we would have recognized is one year or less.

*Sales Returns*

Sales returns are recognized as a reduction of revenue by the amount of expected returns and are recorded as refund liability within current liabilities. We estimate the amount of revenue expected to be reversed to calculate the sales return liability based on historical data for specific products, adjusted as necessary for new products. The allowance for returns is presented gross as a refund liability and we record an inventory asset (and a corresponding adjustment to cost of sales) for any goods or services that we expect to be returned.



**HENRY SCHEIN, INC.**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**  
(in thousands, except per share data)  
(unaudited)

**Note 3 – Revenue from Contracts with Customers**

Revenue (Net sales) is recognized in accordance with the policies discussed in Note 2 - Accounting Pronouncements Adopted and Critical Accounting Policies and Estimates.

*Disaggregation of Net sales*

The following table disaggregates our Net sales by reportable segment and geographic area:

	Three Months Ended September 29, 2018			Nine Months Ended September 29, 2018		
	North America	International	Global	North America	International	Global
<b>Net sales:</b>						
Health care distribution.....						
Dental.....	\$ 951,412	\$ 563,126	\$1,514,538	\$2,831,062	\$ 1,844,150	\$4,675,212
Animal health.....	460,838	438,457	899,295	1,425,273	1,379,758	2,805,031
Medical.....	702,758	19,184	721,942	1,915,944	60,423	1,976,367
Total health care distribution.....	2,115,008	1,020,767	3,135,775	6,172,279	3,284,331	9,456,610
Technology and value-added services.....	123,823	20,080	143,903	307,826	62,357	370,183
Total.....	\$2,238,831	\$ 1,040,847	\$3,279,678	\$6,480,105	\$ 3,346,688	\$9,826,793

*Contract Balances*

Contract balances represent amounts presented in our consolidated balance sheet when either we have transferred goods or services to the customer or the customer has paid consideration to us under the contract. These contract balances include accounts receivable, contract assets and contract liabilities.

The contract assets primarily relate to our rights to consideration for work completed but not billed at the reporting date on contracts. The contract assets are transferred to receivables when the rights become unconditional. The contract assets primarily relate to our bundled arrangements for the sale of equipment and consumables and sales of term software licenses. Current and non-current contract asset balances as of September 29, 2018 and December 31, 2017 were not material.

The contract liabilities primarily relate to advance payments from customers and upfront payments for service arrangements provided over time. At December 31, 2017, the current portion of contract liabilities of \$85.7 million was reported in Accrued expenses: Other, and \$5.2 million related to non-current contract liabilities were reported in Other liabilities. During the nine months ended September 29, 2018, we recognized \$69.7 million of the amount previously deferred at December 31, 2017. At September 29, 2018, the current and non-current portion of contract liabilities were \$73.7 million and \$5.5 million, respectively.



**HENRY SCHEIN, INC.**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**  
(in thousands, except per share data)  
(unaudited)

**Note 4 – Segment Data**

We conduct our business through two reportable segments: (i) health care distribution and (ii) technology and value-added services. These segments offer different products and services to the same customer base.

The health care distribution reportable segment aggregates our global dental, animal health and medical operating segments. This segment distributes consumable products, small equipment, laboratory products, large equipment, equipment repair services, branded and generic pharmaceuticals, vaccines, surgical products, diagnostic tests, infection-control products and vitamins. Our global dental group serves office-based dental practitioners, dental laboratories, schools and other institutions. Our global animal health group serves animal health practices and clinics. Our global medical group serves office-based medical practitioners, ambulatory surgery centers, other alternate-care settings and other institutions. Our global dental, animal health and medical groups serve practitioners in 34 countries worldwide.

Our global technology and value-added services group provides software, technology and other value-added services to health care practitioners. Our technology group offerings include practice management software systems for dental and medical practitioners and animal health clinics. Our value-added practice solutions include financial services on a non-recourse basis, e-services, continuing education services for practitioners, consulting and other services.

The following tables present information about our reportable and operating segments:

	Three Months Ended		Nine Months Ended	
	September 29, 2018	September 30, 2017	September 29, 2018	September 30, 2017
<b>Net Sales:</b>				
Health care distribution (1):				
Dental .....	\$ 1,514,538	\$ 1,478,730	\$ 4,675,212	\$ 4,372,055
Animal health .....	899,295	882,580	2,805,031	2,586,850
Medical .....	721,942	690,761	1,976,367	1,861,074
Total health care distribution .....	3,135,775	3,052,071	9,456,610	8,819,979
Technology and value-added services (2).....	143,903	109,012	370,183	323,510
Total .....	\$ 3,279,678	\$ 3,161,083	\$ 9,826,793	\$ 9,143,489

(1) Consists of consumable products, small equipment, laboratory products, large equipment, equipment repair services, branded and generic pharmaceuticals, vaccines, surgical products, diagnostic tests, infection-control products and vitamins.

(2) Consists of practice management software and other value-added products, which are distributed primarily to health care providers, and financial services on a non-recourse basis, e-services, continuing education services for practitioners, consulting and other services.

	Three Months Ended		Nine Months Ended	
	September 29, 2018	September 30, 2017	September 29, 2018	September 30, 2017
<b>Operating Income:</b>				
Health care distribution .....	\$ 127,990	\$ 181,612	\$ 471,543	\$ 521,278
Technology and value-added services .....	37,936	31,936	101,874	96,900
Total .....	\$ 165,926	\$ 213,548	\$ 573,417	\$ 618,178



**HENRY SCHEIN, INC.**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**  
**(in thousands, except per share data)**  
**(unaudited)**

**Note 5 – Debt**

*Bank Credit Lines*

On April 18, 2017, we entered into a new \$750 million revolving credit agreement (the “Credit Agreement”). This facility, which matures in April 2022, replaced our \$500 million revolving credit facility, which was scheduled to mature in September 2019. The interest rate is based on the USD LIBOR plus a spread based on our leverage ratio at the end of each financial reporting quarter. On June 29, 2018, we amended the Credit Agreement to, among other things, (i) permit the consummation of the spin-off of our Animal Health business (the “Spin-off”) (See Note 9), (ii) provide for swing-line commitments in the amount of \$75 million, and (iii) provide for the designation of subsidiary borrowers under the facility. The Credit Agreement provides, among other things, that we are required to maintain maximum leverage ratios, and contains customary representations, warranties and affirmative covenants. The Credit Agreement also contains customary negative covenants, subject to negotiated exceptions on liens, indebtedness, significant corporate changes (including mergers), dispositions and certain restrictive agreements.

As of September 29, 2018 and December 30, 2017, the borrowings under this revolving credit facility were \$350.0 million and \$320.0 million, respectively. As of September 29, 2018 and December 30, 2017, there were \$11.2 million and \$11.3 million of letters of credit, respectively, provided to third parties under the credit facility.

As of September 29, 2018 and December 30, 2017, we had various other short-term bank credit lines available, of which \$394.9 million and \$421.7 million, respectively, were outstanding. At September 29, 2018 and December 30, 2017, borrowings under all of our credit lines had a weighted average interest rate of 3.06% and 2.27%, respectively.

*Private Placement Facilities*

On September 15, 2017, we increased our available private placement facilities with three insurance companies to a total facility amount of \$1 billion, and extended the expiration date to September 15, 2020. These facilities are available on an uncommitted basis at fixed rate economic terms to be agreed upon at the time of issuance, from time to time through September 15, 2020. The facilities allow us to issue senior promissory notes to the lenders at a fixed rate based on an agreed upon spread over applicable treasury notes at the time of issuance. The term of each possible issuance will be selected by us and can range from five to 15 years (with an average life no longer than 12 years). The proceeds of any issuances under the facilities will be used for general corporate purposes, including working capital and capital expenditures, to refinance existing indebtedness and/or to fund potential acquisitions. On June 29, 2018, we amended and restated the above private placement facilities to, among other things, (i) permit the consummation of the Spin-off and (ii) provide for the issuance of notes in Euros, British Pounds and Australian Dollars, in addition to U.S. Dollars. The agreements provide, among other things, that we maintain certain maximum leverage ratios, and contain restrictions relating to subsidiary indebtedness, liens, affiliate transactions, disposal of assets and certain changes in ownership. These facilities contain make-whole provisions in the event that we pay off the facilities prior to the applicable due dates.



**HENRY SCHEIN, INC.**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**  
(in thousands, except per share data)  
(unaudited)

The components of our private placement facility borrowings as of September 29, 2018 are presented in the following table (in thousands):

Date of Borrowing	Amount of Borrowing Outstanding	Borrowing Rate	Due Date
September 2, 2010	\$ 100,000	3.79%	September 2, 2020
January 20, 2012	50,000	3.45	January 20, 2024
January 20, 2012 (1)	28,571	3.09	January 20, 2022
December 24, 2012	50,000	3.00	December 24, 2024
June 2, 2014	100,000	3.19	June 2, 2021
June 16, 2017	100,000	3.42	June 16, 2027
September 15, 2017	100,000	3.52	September 15, 2029
January 2, 2018	100,000	3.32	January 2, 2028
Less: Deferred debt issuance costs	(439)		
	<u>\$ 628,132</u>		

(1) Annual repayments of approximately \$7.1 million for this borrowing commenced on January 20, 2016.

*Committed Loan Associated with Animal Health Spin-off*

On May 21, 2018, we obtained a \$400 million committed loan which matures on the earlier of (i) March 31, 2019 and (ii) the consummation of the Spin-off. The proceeds of this loan were used, among other things, to fund our purchase of all of the equity interests in Butler Animal Health Holding Company, LLC ("BAHHC") directly or indirectly owned by Darby Group Companies, Inc. ("Darby") and certain other sellers pursuant to the terms of that certain Amendment to Put Rights Agreements, dated as of April 20, 2018, by and among us, Darby, BAHHC and the individual sellers party thereto for an aggregate purchase price of \$365 million. As of September 29, 2018, the balance outstanding on this loan was \$400 million and is included within the "Bank credit lines" caption within our consolidated balance sheet. At September 29, 2018, the interest rate on this loan was 3.125%.

*U.S. Trade Accounts Receivable Securitization*

We have a facility agreement with a bank, as agent, based on the securitization of our U.S. trade accounts receivable that is structured as an asset-backed securitization program with pricing committed for up to three years. On June 1, 2016, we extended the expiration date of this facility agreement to April 29, 2019 and increased the purchase limit under the facility from \$300 million to \$350 million. On July 6, 2017, we extended the expiration date of this facility agreement to April 29, 2020. The borrowings outstanding under this securitization facility were \$350 million and \$350 million as of September 29, 2018 and December 30, 2017, respectively. At September 29, 2018, the interest rate on borrowings under this facility was based on the asset-backed commercial paper rate of 2.31 % plus 0.75%, for a combined rate of 3.06%. At December 30, 2017, the interest rate on borrowings under this facility was based on the asset-backed commercial paper rate of 1.53% plus 0.75%, for a combined rate of 2.28%.

We are required to pay a commitment fee of 30 basis points on the daily balance of the unused portion of the facility if our usage is greater than or equal to 50% of the facility limit or a commitment fee of 35 basis points on the daily balance of the unused portion of the facility if our usage is less than 50% of the facility limit.

Borrowings under this facility are presented as a component of Long-term debt within our consolidated balance sheet.



**HENRY SCHEIN, INC.**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**  
(in thousands, except per share data)  
(unaudited)

*Long-term debt*

Long-term debt consisted of the following:

	September 29, December 30,	
	2018	2017
Private placement facilities .....	\$ 628,132	\$ 535,295
U.S. trade accounts receivable securitization .....	350,000	350,000
Various collateralized and uncollateralized loans payable with interest in varying installments through 2022 at interest rates ranging from 2.61% to 4.73% at September 29, 2018 and ranging from 2.56% to 12.90% at December 30, 2017 .....	29,719	34,027
Capital lease obligations payable through 2029 with interest rates ranging from 0.07% to 19.79% at September 29, 2018 and ranging from 0.84% to 19.79% at December 30, 2017 .....	4,946	5,093
Total .....	1,012,797	924,415
Less current maturities .....	(12,482)	(16,659)
Total long-term debt .....	<u>\$ 1,000,315</u>	<u>\$ 907,756</u>

**Note 6 – Redeemable Noncontrolling Interests**

Some minority stockholders in certain of our subsidiaries have the right, at certain times, to require us to acquire their ownership interest in those entities at fair value. ASC Topic 480-10 is applicable for noncontrolling interests where we are or may be required to purchase all or a portion of the outstanding interest in a consolidated subsidiary from the noncontrolling interest holder under the terms of a put option contained in contractual agreements. The components of the change in the Redeemable noncontrolling interests for the nine months ended September 29, 2018 and the year ended December 30, 2017 are presented in the following table:

	September 29, December 30,	
	2018	2017
Balance, beginning of period .....	\$ 832,138	\$ 607,636
Decrease in redeemable noncontrolling interests due to redemptions .....	(666,363)	(48,669)
Increase in redeemable noncontrolling interests due to business acquisitions .....	10,058	78,939
Net income attributable to redeemable noncontrolling interests .....	17,019	52,203
Dividends declared .....	(16,293)	(28,161)
Effect of foreign currency translation gain (loss) attributable to redeemable noncontrolling interests .....	(13,752)	7,461
Change in fair value of redeemable securities .....	119,695	162,729
Balance, end of period .....	<u>\$ 282,502</u>	<u>\$ 832,138</u>

Changes in the estimated redemption amounts of the noncontrolling interests subject to put options are adjusted at each reporting period with a corresponding adjustment to Additional paid-in capital. Future reductions in the carrying amounts are subject to a floor amount that is equal to the fair value of the redeemable noncontrolling interests at the time they were originally recorded. The recorded value of the redeemable noncontrolling interests cannot go below the floor level. These adjustments do not impact the calculation of earnings per share.



**HENRY SCHEIN, INC.**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**  
(in thousands, except per share data)  
(unaudited)

**Note 7 – Comprehensive Income**

Comprehensive income includes certain gains and losses that, under U.S. GAAP, are excluded from net income as such amounts are recorded directly as an adjustment to stockholders' equity. Our comprehensive income is primarily comprised of net income, foreign currency translation gain (loss), unrealized gain (loss) on foreign currency hedging activities, unrealized investment loss and pension adjustment gain (loss).

The following table summarizes our Accumulated other comprehensive loss, net of applicable taxes as of:

	September 29, 2018	December 30, 2017
<b>Attributable to Redeemable noncontrolling interests:</b>		
Foreign currency translation adjustment .....	\$ (19,316)	\$ (5,564)
<b>Attributable to noncontrolling interests:</b>		
Foreign currency translation adjustment .....	\$ (553)	\$ 539
<b>Attributable to Henry Schein, Inc.:</b>		
Foreign currency translation loss .....	\$ (203,749)	\$ (112,439)
Unrealized loss from foreign currency hedging activities .....	(108)	(782)
Unrealized investment loss .....	(5)	(3)
Pension adjustment loss .....	(15,787)	(16,843)
Accumulated other comprehensive loss .....	<u>\$ (219,649)</u>	<u>\$ (130,067)</u>
Total Accumulated other comprehensive loss .....	<u>\$ (239,518)</u>	<u>\$ (135,092)</u>

The following table summarizes the components of comprehensive income, net of applicable taxes as follows:

	Three Months Ended		Nine Months Ended	
	September 29, 2018	September 30, 2017	September 29, 2018	September 30, 2017
Net income .....	\$ 126,976	\$ 150,948	\$ 423,116	\$ 450,783
Foreign currency translation gain (loss).....	(10,582)	58,916	(106,154)	173,166
Tax effect .....	-	-	-	-
Foreign currency translation gain (loss) .....	<u>(10,582)</u>	<u>58,916</u>	<u>(106,154)</u>	<u>173,166</u>
Unrealized gain (loss) from foreign currency hedging				
activities .....	(406)	26	1,079	(1,278)
Tax effect .....	27	(60)	(405)	4
Unrealized gain (loss) from foreign currency hedging				
activities .....	<u>(379)</u>	<u>(34)</u>	<u>674</u>	<u>(1,274)</u>
Unrealized investment loss.....	(1)	(3)	(2)	(3)
Tax effect .....	-	1	-	1
Unrealized investment loss.....	<u>(1)</u>	<u>(2)</u>	<u>(2)</u>	<u>(2)</u>
Pension adjustment gain (loss).....	139	(529)	1,449	(1,571)
Tax effect .....	(23)	176	(393)	508
Pension adjustment gain (loss).....	<u>116</u>	<u>(353)</u>	<u>1,056</u>	<u>(1,063)</u>
Comprehensive income .....	<u>\$ 116,130</u>	<u>\$ 209,475</u>	<u>\$ 318,690</u>	<u>\$ 621,610</u>



**HENRY SCHEIN, INC.**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**  
(in thousands, except per share data)  
(unaudited)

During the three months ended September 29, 2018 and September 30, 2017, we recognized, as a component of our comprehensive income, a foreign currency translation gain (loss) of \$(10.6) million and \$58.9 million, respectively, due to changes in foreign exchange rates from the beginning of the period to the end of the period. During the nine months ended September 29, 2018 and September 30, 2017, we recognized, as a component of our comprehensive income, a foreign currency translation gain (loss) of \$(106.2) million and \$173.2 million, respectively, due to changes in foreign exchange rates from the beginning of the period to the end of the period. Our financial statements are denominated in the U.S. Dollar currency. Fluctuations in the value of foreign currencies as compared to the U.S. Dollar may have a significant impact on our comprehensive income. The foreign currency translation gain (loss) during the three and nine months ended September 29, 2018 and September 30, 2017 was impacted by changes in foreign currency exchange rates as follows:

Currency	Foreign Currency Translation Gain (Loss) for the Three Months Ended			Foreign Currency Translation Gain for the Three Months Ended		
	FX Rate into USD			FX Rate into USD		
	September 29, 2018	September 29, 2018	June 30, 2018	September 30, 2017	September 30, 2017	July 1, 2017
Euro	\$ (144)	1.16	1.16	\$ 30,373	1.18	1.14
British Pound	(1,804)	1.31	1.31	9,168	1.34	1.30
Australian Dollar	(5,507)	0.72	0.74	3,767	0.78	0.77
Canadian Dollar	1,488	0.77	0.76	5,640	0.80	0.77
Polish Zloty	1,253	0.27	0.27	940	0.27	0.27
Swiss Franc	266	1.02	1.00	407	1.03	1.04
Brazilian Real	(6,001)	0.25	0.26	6,400	0.32	0.30
All other currencies	(133)			2,221		
<b>Total</b>	<b>\$ (10,582)</b>			<b>\$ 58,916</b>		

Currency	Foreign Currency Translation Loss for the Nine Months Ended			Foreign Currency Translation Gain for the Nine Months Ended		
	FX Rate into USD			FX Rate into USD		
	September 29, 2018	September 29, 2018	December 30, 2017	September 30, 2017	September 30, 2017	December 26, 2016
Euro	\$ (27,896)	1.16	1.20	\$ 95,715	1.18	1.05
British Pound	(11,886)	1.31	1.35	24,712	1.34	1.23
Australian Dollar	(21,227)	0.72	0.78	16,220	0.78	0.72
Canadian Dollar	(4,366)	0.77	0.80	9,820	0.80	0.74
Polish Zloty	(3,907)	0.27	0.29	7,891	0.27	0.24
Swiss Franc	(1,741)	1.02	1.03	5,305	1.03	0.98
Brazilian Real	(32,701)	0.25	0.30	4,136	0.32	0.31
All other currencies	(2,430)			9,367		
<b>Total</b>	<b>\$ (106,154)</b>			<b>\$ 173,166</b>		



**HENRY SCHEIN, INC.**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**  
(in thousands, except per share data)  
(unaudited)

The following table summarizes our total comprehensive income, net of applicable taxes, as follows:

	<u>Three Months Ended</u>		<u>Nine Months Ended</u>	
	<u>September</u>	<u>September</u>	<u>September</u>	<u>September</u>
	<u>29,</u>	<u>30,</u>	<u>29,</u>	<u>30,</u>
	<u>2018</u>	<u>2017</u>	<u>2018</u>	<u>2017</u>
Comprehensive income attributable to				
Henry Schein, Inc. ....	\$ 113,221	\$ 193,085	\$ 313,326	\$ 577,403
Comprehensive income attributable to				
noncontrolling interests .....	2,478	372	2,097	848
Comprehensive income attributable to				
Redeemable noncontrolling interests .....	431	16,018	3,267	43,359
Comprehensive income .....	<u>\$ 116,130</u>	<u>\$ 209,475</u>	<u>\$ 318,690</u>	<u>\$ 621,610</u>

**Note 8 – Fair Value Measurements**

ASC Topic 820 “Fair Value Measurements and Disclosures” (“ASC Topic 820”) provides a framework for measuring fair value in generally accepted accounting principles.

ASC Topic 820 defines fair value as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. ASC Topic 820 establishes a fair value hierarchy that distinguishes between (1) market participant assumptions developed based on market data obtained from independent sources (observable inputs) and (2) an entity’s own assumptions about market participant assumptions developed based on the best information available in the circumstances (unobservable inputs).

The fair value hierarchy consists of three broad levels, which gives the highest priority to unadjusted quoted prices in active markets for identical assets or liabilities (Level 1) and the lowest priority to unobservable inputs (Level 3). The three levels of the fair value hierarchy under ASC Topic 820 are described as follows:

- Level 1— Unadjusted quoted prices in active markets for identical assets or liabilities that are accessible at the measurement date.
- Level 2— Inputs other than quoted prices included within Level 1 that are observable for the asset or liability, either directly or indirectly. Level 2 inputs 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; inputs other than quoted prices that are observable for the asset or liability; and inputs that are derived principally from or corroborated by observable market data by correlation or other means.
- Level 3— Inputs that are unobservable for the asset or liability.

The following section describes the valuation methodologies that we used to measure different financial instruments at fair value.

*Investments and notes receivable*

There are no quoted market prices available for investments in unconsolidated affiliates and notes receivable; however, we believe the carrying amounts are a reasonable estimate of fair value.



**HENRY SCHEIN, INC.**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**  
**(in thousands, except per share data)**  
**(unaudited)**

*Debt*

The fair value of our debt, including bank credit lines, as of September 29, 2018 and December 30, 2017 was estimated at \$2,157.7 million and \$1,666.1 million, respectively. Factors that we considered when estimating the fair value of our debt include market conditions, prepayment and make-whole provisions, liquidity levels in the private placement market, variability in pricing from multiple lenders and term of debt.

*Derivative contracts*

Derivative contracts are valued using quoted market prices and significant other observable and unobservable inputs. We use derivative instruments to minimize our exposure to fluctuations in foreign currency exchange rates. Our derivative instruments primarily include foreign currency forward agreements related to intercompany loans and certain forecasted inventory purchase commitments with suppliers.

The fair values for the majority of our foreign currency derivative contracts are obtained by comparing our contract rate to a published forward price of the underlying market rates, which is based on market rates for comparable transactions and are classified within Level 2 of the fair value hierarchy.

*Redeemable noncontrolling interests*

Some minority stockholders in certain of our subsidiaries have the right, at certain times, to require us to acquire their ownership interest in those entities at fair value based on third-party valuations. The primary factor affecting the future value of redeemable noncontrolling interests is expected earnings and, if such earnings are not achieved, the value of the redeemable noncontrolling interests might be impacted. The noncontrolling interests subject to put options are adjusted to their estimated redemption amounts each reporting period with a corresponding adjustment to Additional paid-in capital. Future reductions in the carrying amounts are subject to a "floor" amount that is equal to the fair value of the redeemable noncontrolling interests at the time they were originally recorded. The recorded value of the redeemable noncontrolling interests cannot go below the floor level. These adjustments do not impact the calculation of earnings per share. The values for Redeemable noncontrolling interests are classified within Level 3 of the fair value hierarchy. The details of the changes in Redeemable noncontrolling interests are presented in Note 6.



**HENRY SCHEIN, INC.**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**  
(in thousands, except per share data)  
(unaudited)

The following table presents our assets and liabilities that are measured and recognized at fair value on a recurring basis classified under the appropriate level of the fair value hierarchy as of September 29, 2018 and December 30, 2017:

	September 29, 2018			
	Level 1	Level 2	Level 3	Total
<b>Assets:</b>				
Derivative contracts .....	\$ -	\$ 18,135	\$ -	\$ 18,135
<b>Total assets .....</b>	<b>\$ -</b>	<b>\$ 18,135</b>	<b>\$ -</b>	<b>\$ 18,135</b>
<b>Liabilities:</b>				
Derivative contracts .....	\$ -	\$ 2,824	\$ -	\$ 2,824
<b>Total liabilities .....</b>	<b>\$ -</b>	<b>\$ 2,824</b>	<b>\$ -</b>	<b>\$ 2,824</b>
Redeemable noncontrolling interests .....	\$ -	\$ -	\$ 282,502	\$ 282,502

	December 30, 2017			
	Level 1	Level 2	Level 3	Total
<b>Assets:</b>				
Derivative contracts .....	\$ -	\$ 11,799	\$ -	\$ 11,799
<b>Total assets .....</b>	<b>\$ -</b>	<b>\$ 11,799</b>	<b>\$ -</b>	<b>\$ 11,799</b>
<b>Liabilities:</b>				
Derivative contracts .....	\$ -	\$ 2,089	\$ -	\$ 2,089
<b>Total liabilities .....</b>	<b>\$ -</b>	<b>\$ 2,089</b>	<b>\$ -</b>	<b>\$ 2,089</b>
Redeemable noncontrolling interests .....	\$ -	\$ -	\$ 832,138	\$ 832,138



**HENRY SCHEIN, INC.**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**  
**(in thousands, except per share data)**  
**(unaudited)**

**Note 9 – Business Acquisitions and Planned Divestiture**

*Acquisitions*

The operating results of all acquisitions are reflected in our financial statements from their respective acquisition dates.

On July 1, 2018, we closed on a joint venture with Internet Brands, a provider of web presence and online marketing software, to create a newly formed entity, Henry Schein One, LLC. The joint venture includes Henry Schein Practice Solutions products and services, as well as Henry Schein's international dental practice management systems and the dental businesses of Internet Brands. We own 74% of the joint venture and Internet Brands owns the remaining 26% minority interest. Beginning with the second anniversary of the effective date of the formation of the joint venture, Henry Schein One will issue a fixed number of additional interests to Internet Brands through the fifth anniversary of the effective date, thereby increasing Internet Brands' ownership by approximately 7.6%. Internet Brands will also be entitled to receive a fixed number of additional interests, in the aggregate up to approximately 1.6% of the joint venture's ownership, if certain operating targets are met by the joint venture in its fourth, fifth and sixth operating years. Senior management from Henry Schein and Internet Brands serve on the board of Henry Schein One. The combined entity, which serves markets globally, had pro-forma 2017 sales of approximately \$400 million, of which approximately \$100 million originated at Internet Brands. As a result of this acquisition, \$412.8 million of initial goodwill resulted which reflects the excess of our purchase price over the fair value of the net assets acquired. The initial goodwill recorded as part of the acquisition primarily reflects the value of future synergies. We allocated all of the goodwill to our Technology and value-added services reporting segment. None of the goodwill recognized is deductible for income tax purposes, and as such, no deferred taxes have been recorded related to goodwill.

Concurrent with the formation of Henry Schein One, LLC, we entered into a separate agreement with Internet Brands whereby (1) beginning July 1, 2023, Internet Brands will have the right to require Henry Schein to purchase all or a portion of Internet Brands ownership interests in Henry Schein One, LLC for fair market value, and (2) beginning July 1, 2028, or earlier if certain events occur, Henry Schein will have the right to require Internet Brands to sell all or a portion of its ownership interests in Henry Schein One, LLC to Henry Schein for fair market value.

We did not complete any other material acquisitions during the nine months ended September 29, 2018.

Some prior owners of acquired subsidiaries are eligible to receive additional purchase price cash consideration if certain financial targets are met. We have accrued liabilities for the estimated fair value of additional purchase price consideration at the time of the acquisition. Any adjustments to these accrual amounts are recorded in our consolidated statements of income. For the nine months ended September 29, 2018 and September 30, 2017, there were no material adjustments recorded in our consolidated statement of income relating to changes in estimated contingent purchase price liabilities.



**HENRY SCHEIN, INC.**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**  
**(in thousands, except per share data)**  
**(unaudited)**

*Planned Divestiture*

On April 23, 2018, we announced that we entered into a definitive agreement with HS Spinco, Inc., a direct, wholly owned subsidiary of Henry Schein ("Spinco"), and Direct Vet Marketing, Inc. (d/b/a Vets First Choice) ("DVM") to create a newly formed company, Vets First Corp. The transaction is intended to be tax-free to Henry Schein stockholders for U.S. tax purposes. As part of this transaction, subject to the terms and conditions set forth in certain definitive agreements, we will contribute the assets and entities comprising our animal health business to Spinco. In exchange for the contribution to Spinco of our animal health business, Spinco will issue to Henry Schein shares of common stock, par value \$0.01 per share, of Spinco (the "Spinco Common Stock"). We will subsequently distribute to our stockholders all of the shares of Spinco Common Stock held by us (the "Distribution"). Immediately after the Distribution, HS Merger Sub, Inc., a wholly owned subsidiary of Spinco, will merge with and into DVM, with DVM surviving the merger as a wholly owned subsidiary of Spinco (with such subsidiary to be renamed Vets First Corp.). Upon consummation of these transactions, on a fully-diluted basis, the stockholders of Henry Schein and, if applicable, certain third parties and minority holders of our animal health subsidiaries that are contributed to Spinco in exchange for their interests in these subsidiaries, are expected to own approximately 63% of the outstanding shares of Spinco Common Stock, and the then former stockholders of DVM are expected to own approximately 37% of the outstanding shares of Spinco Common Stock, subject to certain adjustments. Henry Schein will nominate six individuals to the Vets First Corp. Board of Directors and DVM will nominate five individuals to the Vets First Corp. Board of Directors.

Additionally, we expect to receive a cash dividend between \$1.0 billion and \$1.25 billion on a tax-free basis as part of the transaction. We plan to use the proceeds for general corporate purposes, including share repurchases and repayment of indebtedness.

The transaction has been unanimously approved by our Board of Directors and the Board of Directors of DVM. We are working toward closing the transaction by the end of 2018 or early 2019. The transaction is subject to customary closing conditions, including customary regulatory approvals, the receipt of tax opinions from counsel with respect to the transaction and the effectiveness of a registration statement on Form S-1/S-4 to be filed with the Securities and Exchange Commission (the "SEC") in connection with the transaction.



**HENRY SCHEIN, INC.**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**  
(in thousands, except per share data)  
(unaudited)

**Note 10 – Plans of Restructuring**

On July 9, 2018, we committed to an initiative to rationalize our operations and provide expense efficiencies. These actions will allow us to execute on our plan to reduce our cost structure and fund new initiatives that will drive future growth under our 2018 to 2020 strategic plan. This initiative is expected to include the elimination of approximately 2% to 3% of our workforce and the closing of certain facilities. The total 2018 costs associated with the actions to complete this restructuring are expected to be in the range of \$45 million to \$55 million pre-tax, or \$0.22 to \$0.27 per diluted share, consisting of \$40 million to \$45 million in employee severance pay and benefits and \$5 million to \$10 million in facility costs, representing primarily lease termination and other facility closure related costs.

During the three and nine months ended September 29, 2018, we recorded restructuring costs of \$8.9 million and \$27.5 million, respectively, primarily for certain redundancies. The costs associated with these restructuring activities are included in a separate line item, “Restructuring costs” within our consolidated statements of income.

The following table shows the amounts expensed and paid for restructuring costs that were incurred during the nine months ended September 29, 2018 and during our 2017 fiscal year and the remaining accrued balance of restructuring costs as of September 29, 2018, which is included in Accrued expenses: Other and Other liabilities within our consolidated balance sheet:

	Severance Costs	Facility Closing Costs	Other	Total
Balance, December 31, 2016	\$ 22,354	\$ 2,454	\$ 895	\$ 25,703
Payments and other adjustments	(19,136)	(1,139)	(871)	(21,146)
Balance, December 30, 2017	\$ 3,218	\$ 1,315	\$ 24	\$ 4,557
Provision	26,474	757	280	27,511
Payments and other adjustments	(16,908)	(1,441)	(206)	(18,555)
Balance, September 29, 2018	\$ 12,784	\$ 631	\$ 98	\$ 13,513

The following table shows, by reportable segment, the amounts expensed and paid for restructuring costs that were incurred during the nine months ended September 29, 2018 and the 2017 fiscal year and the remaining accrued balance of restructuring costs as of September 29, 2018:

	Health Care Distribution	Technology and Value-Added Services	Total
Balance, December 31, 2016	\$ 25,238	\$ 465	\$ 25,703
Payments and other adjustments	(20,681)	(465)	(21,146)
Balance, December 30, 2017	\$ 4,557	\$ -	\$ 4,557
Provision	25,625	1,886	27,511
Payments and other adjustments	(18,065)	(490)	(18,555)
Balance, September 29, 2018	\$ 12,117	\$ 1,396	\$ 13,513



**HENRY SCHEIN, INC.**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**  
(in thousands, except per share data)  
(unaudited)

**Note 11 – Earnings Per Share**

Basic earnings per share is computed by dividing net income attributable to Henry Schein, Inc. by the weighted-average number of common shares outstanding for the period. Our diluted earnings per share is computed similarly to basic earnings per share, except that it reflects the effect of common shares issuable for presently unvested restricted stock and restricted stock units and upon exercise of stock options, using the treasury stock method in periods in which they have a dilutive effect.

A reconciliation of shares used in calculating earnings per basic and diluted share follows:

	Three Months Ended		Nine Months Ended	
	September 29, 2018	September 30, 2017	September 29, 2018	September 30, 2017
Basic .....	152,533	156,914	152,970	157,386
Effect of dilutive securities:				
Stock options, restricted stock and restricted stock units .....	1,081	1,357	1,012	1,480
Diluted .....	153,614	158,271	153,982	158,866

**Note 12 – Income Taxes**

Our effective tax rate was 23.3% for the nine months ended September 29, 2018 and 26.3% for the nine months ended September 30, 2017. The difference between our effective tax rate and the federal statutory tax rate for the nine months ended September 29, 2018 primarily relates to the Tax Cuts and Jobs Act (“the Tax Act”), as well as state and foreign income taxes and interest expense. The difference between our effective tax rate and the federal statutory tax rate for the nine months ended September 30, 2017 primarily relates to the adoption of ASU No. 2016-09, “Stock Compensation” (Topic 718) (“ASU 2016-09”) in the first quarter of 2017, as well as state and foreign income taxes and interest expense.

Under ASU 2016-09, all excess tax benefits and tax deficiencies resulting from the difference between the deduction for tax purposes and the stock-based compensation cost recognized for financial reporting purposes are included as a component of income tax expense beginning January 1, 2017. Prior to the implementation of ASU 2016-09, excess tax benefits were recorded as a component of Additional paid in capital and tax deficiencies were recognized either as an offset to accumulated excess tax benefits or in the income statement if there were no accumulated excess tax benefits. For the nine months ended September 29, 2018 and September 30, 2017, the application of ASU No. 2016-09 reduced income tax expense by approximately \$1.0 million and \$19.5 million, respectively.

On December 22, 2017, the U.S. government passed the Tax Act. The Tax Act is comprehensive tax legislation effective January 1, 2018 that implements complex changes to the U.S. tax code including, but not limited to, the reduction of the corporate tax rate from 35% to 21%, modification of accelerated depreciation, the repeal of the domestic manufacturing deduction and changes to the limitations of the deductibility of interest. The Tax Act also includes provisions to tax global intangible low-taxed income (“GILTI”), a beneficial tax rate for Foreign Derived Intangible Income (“FDII”), a base erosion and anti-abuse tax (“BEAT”) that imposes tax on certain foreign related-party payments, and IRC Section 163(j) interest limitation (Interest Limitation). We are subject to the GILTI, FDII, BEAT and Interest Limitation provisions effective January 1, 2018.



**HENRY SCHEIN, INC.**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**  
**(in thousands, except per share data)**  
**(unaudited)**

The FASB Staff Q&A, Topic 740 No. 5, Accounting for Global Intangible Low-Taxed Income, states that an entity can make an accounting policy election to either recognize deferred taxes for temporary differences expected to reverse as GILTI in future years or provide for the tax expense related to GILTI in the year the tax is incurred. We have elected to recognize the tax on GILTI as a period expense in the period the tax is incurred. Under Topic 740, we have reasonably estimated the impact of each provision of the Tax Act on our effective tax rate. We have recorded an estimate for the GILTI provision in our effective tax rate for the nine months ended September 29, 2018. For the BEAT, FDI and Interest Limitation computations, we have not recorded an estimate in our effective tax rate for the nine months ended September 29, 2018 because we currently estimate that these provisions of the Tax Act will not apply to us or will have an immaterial impact in 2018. Due to the complexity of the new GILTI tax rules and uncertainty of the application of the foreign tax credit rules in relation to GILTI, we have calculated GILTI based upon the law as we currently interpret it, and subsequent changes in law could cause us to revise our calculations in a later period.

Due to the complexities of the Tax Act, the Staff of the SEC issued Staff Accounting Bulletin No. 118 (“SAB 118”) that requires us to record a provisional amount for any income tax effects of the Tax Act in accordance with Topic 740, to the extent that a reasonable estimate can be made. SAB 118 allows for a measurement period of up to one year after the enactment date of the Tax Act to finalize the recording of the related tax impacts.

In the fourth quarter of 2017, we recorded provisional amounts for income tax effects of the Tax Act that we could reasonably estimate. This included the one-time transition tax that we estimated to be \$140.0 million and a net deferred tax expense of \$3.0 million attributable to the revaluation of deferred tax assets and liabilities due to the lower enacted federal income tax rate of 21%. For the nine months ended September 29, 2018, we recorded a provisional benefit of \$10 million related to transition tax adjustments and a net deferred tax benefit of \$1.5 million attributable to the revaluation of deferred tax assets and liabilities. We will continue to refine provisional amounts for the impacts of the Tax Act as anticipated guidance, clarifying certain aspects of the Tax Act, becomes available. We will record any adjustments in the fourth quarter of 2018 when our analysis is complete, although we do not expect any material adjustments.

The total amount of unrecognized tax benefits as of September 29, 2018 was approximately \$104.6 million, of which \$83.0 million would affect the effective tax rate if recognized. It is expected that the amount of unrecognized tax benefits will change in the next 12 months; however, we do not expect the change to have a material impact on our consolidated financial statements.

The total amounts of interest and penalties, which are classified as a component of Other liabilities within our consolidated balance sheets, were approximately \$15.3 million and \$0.0, respectively, as of September 29, 2018.

In 2016, we reached a settlement on a portion of the IRS audit of tax years 2012 and 2013, and we filed a Mutual Agreement Procedure request with the IRS for assistance from the U.S. Competent Authority for an open Transfer Pricing issue which resulted in a partial settlement during the quarter ended December 30, 2017. During the quarter ended June 30, 2017, we filed a protest with the Appellate Division regarding the remaining open audit issues for the years 2012 and 2013. We had an initial Appeals Conference during the third quarter of 2018. In addition, we are working on finalizing our submission for an Advanced Pricing Agreement pursuant to which Henry Schein, Inc. and the IRS would agree on an appropriate transfer pricing methodology for future tax years. We do not expect this to have a material effect on our consolidated financial position, liquidity or results of operations.



**HENRY SCHEIN, INC.**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**  
**(in thousands, except per share data)**  
**(unaudited)**

**Note 13 – Derivatives and Hedging Activities**

We are exposed to market risks as well as changes in foreign currency exchange rates as measured against the U.S. dollar and each other, and changes to the credit risk. We attempt to minimize these risks by primarily using foreign currency forward contracts and by maintaining counter-party credit limits. These hedging activities provide only limited protection against currency exchange and credit risks. Factors that could influence the effectiveness of our hedging programs include currency markets and availability of hedging instruments and liquidity of the credit markets. All foreign currency forward contracts that we enter into are components of hedging programs and are entered into for the sole purpose of hedging an existing or anticipated currency exposure. We do not enter into such contracts for speculative purposes and we manage our credit risks by diversifying our counterparties, maintaining a strong balance sheet and having multiple sources of capital.

Fluctuations in the value of certain foreign currencies as compared to the U.S. dollar may positively or negatively affect our revenues, gross margins, operating expenses and retained earnings, all of which are expressed in U.S. dollars. Where we deem it prudent, we engage in hedging programs using primarily foreign currency forward contracts aimed at limiting the impact of foreign currency exchange rate fluctuations on earnings. We purchase short-term (i.e., 18 months or less) foreign currency forward contracts to protect against currency exchange risks associated with intercompany loans due from our international subsidiaries and the payment of merchandise purchases to our foreign suppliers. We do not hedge the translation of foreign currency profits into U.S. dollars, as we regard this as an accounting exposure, not an economic exposure. Our hedging activities have historically not had a material impact on our consolidated financial statements. Accordingly, additional disclosures related to derivatives and hedging activities required by ASC Topic 815 have been omitted.

**Note 14 – Stock-Based Compensation**

Our accompanying consolidated statements of income reflect pre-tax share-based compensation expense of \$10.9 million (\$8.7 million after-tax) and \$34.2 million (\$26.2 million after-tax) for the three and nine months ended September 29, 2018, respectively, and \$12.6 million (\$9.0 million after-tax) and \$32.0 million (\$23.6 million after-tax) for the three and nine months ended September 30, 2017, respectively.

Stock-based compensation represents the cost related to stock-based awards granted to employees and non-employee directors. We measure stock-based compensation at the grant date, based on the estimated fair value of the award, and recognize the cost (net of estimated forfeitures) as compensation expense on a straight-line basis over the requisite service period. Our stock-based compensation expense is reflected in selling, general and administrative expenses in our consolidated statements of income.

Stock-based awards are provided to certain employees and non-employee directors under the terms of our 2013 Stock Incentive Plan, as amended, and our 2015 Non-Employee Director Stock Incentive Plan (together, the “Plans”). The Plans are administered by the Compensation Committee of the Board of Directors. Prior to March 2009, awards under the Plans principally included a combination of at-the-money stock options and restricted stock/units. Since March 2009, equity-based awards have been granted solely in the form of restricted stock/units, with the exception of providing stock options to employees pursuant to certain pre-existing contractual obligations.

Grants of restricted stock/units are stock-based awards granted to recipients with specified vesting provisions. In the case of restricted stock, common stock is delivered on the date of grant, subject to vesting conditions. In the case of restricted stock units, common stock is generally delivered on or following satisfaction of vesting conditions. We issue restricted stock/units that vest solely based on the recipient’s continued service over time (primarily four-year cliff vesting, except for grants made under the 2015 Non-Employee Director Stock Incentive Plan, which are primarily 12-month cliff vesting) and restricted stock/units that vest based on our achieving specified performance measurements and the recipient’s continued service over time (primarily three-year cliff vesting).



**HENRY SCHEIN, INC.**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**  
(in thousands, except per share data)  
(unaudited)

With respect to time-based restricted stock/units, we estimate the fair value on the date of grant based on our closing stock price. With respect to performance-based restricted stock/units, the number of shares that ultimately vest and are received by the recipient is based upon our performance as measured against specified targets over a specified period, as determined by the Compensation Committee of the Board of Directors. Although there is no guarantee that performance targets will be achieved, we estimate the fair value of performance-based restricted stock/units based on our closing stock price at time of grant.

The Plans provide for adjustments to the performance-based restricted stock/units targets for significant events, including, without limitation, acquisitions, divestitures, new business ventures, certain capital transactions (including share repurchases), restructuring costs, if any, certain litigation settlements or payments, if any, changes in accounting principles or in applicable laws or regulations and foreign exchange fluctuations. Over the performance period, the number of shares of common stock that will ultimately vest and be issued and the related compensation expense is adjusted upward or downward based upon our estimation of achieving such performance targets. The ultimate number of shares delivered to recipients and the related compensation cost recognized as an expense will be based on our actual performance metrics as defined under the Plans.

Total unrecognized compensation cost related to non-vested awards as of September 29, 2018 was \$91.4 million, which is expected to be recognized over a weighted-average period of approximately 2.2 years.

The following table summarizes stock option activity under the Plans during the nine months ended September 29, 2018:

	Shares	Weighted Average Exercise Price	Weighted Average	
			Remaining Life in Years	Aggregate Intrinsic Value
Outstanding at beginning of period .....	155	\$ 29.65		
Granted .....	-	-		
Exercised .....	(154)	29.81		
Forfeited .....	-	-		
Outstanding at end of period .....	1	\$ 17.22	0.4	\$ 136
Options exercisable at end of period .....	1	\$ 17.22	0.4	\$ 136



**HENRY SCHEIN, INC.**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**  
(in thousands, except per share data)  
(unaudited)

The following tables summarize the activity of our non-vested restricted stock/units for the nine months ended September 29, 2018:

	<u>Time-Based Restricted Stock/Units</u>		
	Weighted Average		
	Grant Date	Fair Value	Intrinsic Value
	Shares/Units	Value Per Share	Per Share
Outstanding at beginning of period .....	1,233	\$ 70.28	
Granted .....	363	65.88	
Vested .....	(311)	62.96	
Forfeited .....	(78)	77.96	
Outstanding at end of period .....	<u>1,207</u>	<u>\$ 70.34</u>	<u>\$ 85.03</u>

  

	<u>Performance-Based Restricted Stock/Units</u>		
	Weighted Average		
	Grant Date	Fair Value	Intrinsic Value
	Shares/Units	Value Per Share	Per Share
Outstanding at beginning of period .....	1,226	\$ 60.81	
Granted .....	397	68.76	
Vested .....	(426)	71.33	
Forfeited .....	(72)	77.39	
Outstanding at end of period .....	<u>1,125</u>	<u>\$ 55.75</u>	<u>\$ 85.03</u>

**Note 15 – Supplemental Cash Flow Information**

Cash paid for interest and income taxes was:

	<u>Nine Months Ended</u>	
	September 29, 2018	September 30, 2017
Interest.....	\$ 52,108	\$ 33,640
Income taxes.....	207,474	179,445

During the nine months ended September 29, 2018 and September 30, 2017, we had \$1.1 million and \$(1.3) million of non-cash net unrealized gains (losses) related to foreign currency hedging activities, respectively. During the first quarter of 2018, as part of a business acquisition, we increased our ownership in a subsidiary through a non-cash transaction of \$1.3 million.

During the third quarter of 2018, we closed on a joint venture with Internet Brands to create a newly formed entity, Henry Schein One, LLC, through a non-cash transaction resulting in an initial estimate of approximately \$337 million of noncontrolling interest representing Internet Brands' current 26% minority interest and an initial estimate of \$95 million of deferred additional ownership interests of Internet Brands in Henry Schein One, representing up to an additional 9.2% ownership interests, a portion of which is contingent upon the achievement of certain operating targets (See Note 9).



**HENRY SCHEIN, INC.**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**  
**(in thousands, except per share data)**  
**(unaudited)**

**Note 16 – Legal Proceedings**

Beginning in January 2016, purported class action complaints were filed against Patterson Companies, Inc. (“Patterson”), Benco Dental Supply Co. (“Benco”) and Henry Schein, Inc. Although there were factual and legal variations among these complaints, each of these complaints alleges, among other things, that defendants conspired to fix prices, allocate customers and foreclose competitors by boycotting manufacturers, state dental associations and others that deal with defendants’ competitors. On February 9, 2016, the U.S. District Court for the Eastern District of New York ordered all of these actions, and all other actions filed thereafter asserting substantially similar claims against defendants, consolidated for pre-trial purposes. On February 26, 2016, a consolidated class action complaint was filed by Arnell Prato, D.D.S., P.L.L.C., d/b/a Down to Earth Dental, Evolution Dental Sciences, LLC, Howard M. May, DDS, P.C., Casey Nelson, D.D.S., Jim Peck, D.D.S., Bernard W. Kurek, D.M.D., Larchmont Dental Associates, P.C., and Keith Schwartz, D.M.D., P.A. (collectively, “putative class representatives”) in the U.S. District Court for the Eastern District of New York, entitled *In re Dental Supplies Antitrust Litigation*, Civil Action No. 1:16-CV-00696-BMC-GRB. In the consolidated class action complaint, putative class representatives allege a nationwide agreement among Henry Schein, Benco, Patterson and non-party Burkhardt Dental Supply Company, Inc. (“Burkhardt”) not to compete on price. The consolidated class action complaint asserts a single count under Section 1 of the Sherman Act, and seeks equitable relief, compensatory and treble damages, jointly and severally, and reasonable costs and expenses, including attorneys’ fees and expert fees. On February 22, 2018, plaintiffs moved to certify a class that, subject to certain exclusions, includes all private dental practices and laboratories that purchased dental supplies directly from Henry Schein, Patterson, Benco, Burkhardt or any combination thereof, during the period beginning January 1, 2009 until March 31, 2016. On September 28, 2018, the parties executed a settlement agreement that proposes a full and final settlement of the lawsuit on a classwide basis, subject to court approval. As a result, we recorded a charge of \$38.5 million in our third quarter 2018 results.

On August 31, 2012, Archer and White Sales, Inc. (“Archer”) filed a complaint against Henry Schein, Inc. as well as Danaher Corporation and its subsidiaries Instrumentarium Dental, Inc., Dental Equipment, LLC, Kavio Dental Technologies, LLC and Dental Imaging Technologies Corporation (collectively, the “Danaher Defendants”) in the U.S. District Court for the Eastern District of Texas, Civil Action No. 2:12-CV-00572-JRG, styled as an antitrust action under Section 1 of the Sherman Act, and the Texas Free Enterprise Antitrust Act. Archer alleges a conspiracy between Henry Schein, an unnamed company and the Danaher Defendants to terminate or limit Archer’s distribution rights. On August 1, 2017, Archer filed an amended complaint, adding Patterson and Benco as defendants, and alleging that Henry Schein, Patterson, Benco and Burkhardt conspired to fix prices and refused to compete with each other for sales of dental equipment to dental professionals and agreed to enlist their common suppliers, the Danaher Defendants, to join a price-fixing conspiracy and boycott by reducing the distribution territory of, and eventually terminating, their price-cutting competing distributor Archer. Archer seeks damages in an amount to be proved at trial, to be trebled with interest and costs, including attorneys’ fees, jointly and severally, as well as injunctive relief. On October 30, 2017, Archer filed a second amended complaint, to add additional allegations that it believes support its claims. The named parties and causes of action are the same as the August 1, 2017 amended complaint.

On October 1, 2012, we filed a motion for an order: (i) compelling Archer to arbitrate its claims against us; (2) staying all proceedings pending arbitration; and (3) joining the Danaher Defendants’ motion to arbitrate and stay. On May 28, 2013, the Magistrate Judge granted the motions to arbitrate and stayed proceedings pending arbitration. On June 10, 2013, Archer moved for reconsideration before the District Court judge. On December 7, 2016, the District Court Judge granted Archer’s motion for reconsideration and lifted the stay. Defendants appealed the District Court’s order. On December 21, 2017, the U.S. Court of Appeals for the Fifth Circuit affirmed the District Court’s order denying the motions to compel arbitration. On February 12, 2018, defendants filed an Application for Stay of Proceedings in the District Court in the Supreme Court of the United States, seeking to stay proceedings in the District Court pending a decision on defendants’ forthcoming petition for writ of certiorari. On March 2, 2018, the Supreme Court of the United States granted a stay of proceedings. On June 25,



**HENRY SCHEIN, INC.**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**  
**(in thousands, except per share data)**  
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2018, the Supreme Court of the United States granted defendants' petition for writ of certiorari, pursuant to which it will review the lower court's decision affirming the District Court's decision denying our motion to compel arbitration. On October 29, 2018, the Supreme Court heard oral argument. The Supreme Court's decision is pending. We intend to defend ourselves vigorously against this action.

On August 17, 2017, IQ Dental Supply, Inc. ("IQ Dental") filed a complaint in the U.S. District Court for the Eastern District of New York, entitled IQ Dental Supply, Inc. v. Henry Schein, Inc., Patterson Companies, Inc. and Benco Dental Supply Company, Case No. 2:17-cv-4834. Plaintiff alleges that it is a distributor of dental supplies and equipment, and sells dental products through an online dental distribution platform operated by SourceOne Dental ("SourceOne"). SourceOne had previously brought an antitrust lawsuit against Henry Schein, Patterson and Benco, which Henry Schein settled in the second quarter of 2017 and which is described in our prior filings with the SEC.

IQ Dental alleges, among other things, that defendants conspired to suppress competition from IQ Dental and SourceOne for the marketing, distribution and sale of dental supplies and equipment in the United States, and that defendants unlawfully agreed with one another to boycott dentists, manufacturers and state dental associations that deal with, or considered dealing with, plaintiff and SourceOne. Plaintiff claims that this alleged conduct constitutes unreasonable restraint of trade in violation of Section 1 of the Sherman Act, New York's Donnelly Act and the New Jersey Antitrust Act, and also makes pendant state law claims for tortious interference with prospective business relations, civil conspiracy and aiding and abetting. Plaintiff seeks injunctive relief, compensatory, treble and punitive damages, jointly and severally, and reasonable costs and expenses, including attorneys' fees and expert fees. On December 21, 2017, the District Court granted the defendants' motion to dismiss. On January 19, 2018, IQ Dental appealed the District Court's order. The U.S. Court of Appeals for the Second Circuit heard oral argument on the appeal on September 13, 2018. The court's decision is pending. We intend to defend ourselves vigorously against this action.

On February 12, 2018, the United States Federal Trade Commission ("FTC") filed a complaint against Benco Dental Supply Co., Henry Schein, Inc. and Patterson Companies, Inc. The FTC alleges, among other things, that defendants violated U.S. antitrust laws by conspiring, and entering into an agreement, to refuse to provide discounts to or otherwise serve buying groups representing dental practitioners. The FTC alleges that defendants conspired in violation of Section 5 of the FTC Act. The complaint seeks equitable relief only and does not seek monetary damages. We deny the allegation that we conspired to refuse to provide discounts to or otherwise serve dental buying groups and intend to defend ourselves vigorously against this action. A hearing before an administrative law judge began on October 16, 2018 and is ongoing. We believe this matter will not have a material adverse effect on our consolidated financial position, liquidity or results of operations.

On March 7, 2018, Joseph Salkowitz, individually and on behalf of all others similarly situated, filed a putative class action complaint for violation of the federal securities laws against Henry Schein, Inc., Stanley M. Bergman and Steven Paladino in the U.S. District Court for the Eastern District of New York, Case No. 1:18-cv-01428. The complaint sought to certify a class consisting of all persons and entities who, subject to certain exclusions, purchased Henry Schein securities from March 7, 2013 through February 12, 2018 (the "Class Period"). The complaint alleged, among other things, that the defendants had made materially false and misleading statements about Henry Schein's business, operations and prospects during the Class Period, including matters relating to the issues in the antitrust class action and the FTC action described above, thereby causing the plaintiff and members of the purported class to pay artificially inflated prices for Henry Schein securities. The complaint sought unspecified monetary damages and a jury trial. Pursuant to the provisions of the Private Securities Litigation Reform Act of 1995 (the "PSLRA"), the court appointed lead plaintiff and lead counsel on June 22, 2018 and recaptioned the putative class action as In re Henry Schein, Inc. Securities Litigation, under the same case number. Lead plaintiff filed a consolidated class action complaint on September 14, 2018. The consolidated class action complaint asserts similar claims against the same defendants (plus Timothy Sullivan) on behalf of the same putative class of purchasers during the Class Period. It alleges that Henry Schein's stock price was inflated during that period.



**HENRY SCHEIN, INC.**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**  
**(in thousands, except per share data)**  
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because Henry Schein had misleadingly portrayed its dental-distribution business “as successfully producing excellent profits while operating in a highly competitive environment” even though, “in reality, [Henry Schein] had engaged for years in collusive and anticompetitive practices in order to maintain Schein’s margins, profits, and market share.” The complaint alleges that the stock price started to fall from August 8, 2017, when the company announced below-expected financial performance that allegedly “revealed that Schein’s poor results were a product of abandoning prior attempts to inflate sales volume and margins through anticompetitive collusion,” through February 13, 2018, after the FTC filed a complaint against Benco, Henry Schein and Patterson alleging that they violated U.S. antitrust laws. The complaint alleges violations of Section 10(b) of the Exchange Act and Rule 10b-5 and Section 20(a) of the Exchange Act. We intend to defend ourselves vigorously against this action. Henry Schein has also received a request under 8 Del. C. § 220 to inspect corporate books and records relating to the issues raised in the securities class action and the antitrust matters discussed above.

On May 3, 2018, a class action complaint, Marion Diagnostic Center, LLC, et al. v. Becton, Dickinson, and Co., et al., Case No. 3:18-cv-010509 (S.D. Ill), was filed in the U.S. District Court for the Southern District of Illinois against Becton, Dickinson, and Co. (“Becton”); Premier, Inc. (“Premier”), Vizient, Inc. (“Vizient”), Cardinal Health, Inc. (“Cardinal”), Owens & Minor Inc. (“O&M”), Henry Schein, Inc., and Unnamed Becton Distributor Co-Conspirators. The complaint alleges that the defendants entered into a vertical conspiracy to force healthcare providers into long-term exclusivity contracts that restrain trade in the nationwide markets for conventional and safety syringes and safety IV catheters and inflate the prices of certain Becton products to above-competitive levels. The named plaintiffs seek to represent three separate classes consisting of all healthcare providers that purchased (i) Becton’s conventional syringes, (ii) Becton’s safety syringes, or (iii) Becton’s safety catheters directly from Becton, Premier, Vizient, Cardinal, O&M or Henry Schein on or after May 3, 2014. The complaint asserts a single count under Section 1 of the Sherman Act, and seeks equitable relief, treble damages, reasonable attorneys’ fees and costs and expenses, and pre-judgment and post-judgment interest. On June 15, 2018, an amended complaint was filed asserting the same allegations against the same parties and adding McKesson Medical-Surgical, Inc. as an additional defendant. We intend to defend ourselves vigorously against this action.

On May 29, 2018, an amended complaint was filed in the MultiDistrict Litigation (MDL) proceeding In Re National Prescription Opiate Litigation (MDL No. 2804; Case No. 17-md-2804) in an action entitled The County of Summit, Ohio et al. v. Purdue Pharma, L.P., et al., Civil Action No. 1:18-op-45090-DAP, in the U.S. District Court for the Northern District of Ohio, adding Henry Schein, Inc., Henry Schein Medical Systems, Inc. and others as defendants. Plaintiffs allege that manufacturers of prescription opioid drugs engaged in a false advertising campaign to expand the market for such drugs and their own market share and that the entities in the supply chain (including Henry Schein, Inc. and Henry Schein Medical Systems, Inc.) reaped financial rewards by refusing or otherwise failing to monitor appropriately and restrict the improper distribution of those drugs. Plaintiffs assert the following claims for relief against Henry Schein, Inc. and Henry Schein Medical Systems, Inc.: statutory public nuisance; common law absolute public nuisance; negligence; injury through criminal acts (R.C. 2307.60); unjust enrichment; and civil conspiracy. This case has been designated “Track 1” and is currently set for trial on September 3, 2019. We intend to defend ourselves vigorously against this action.

On July 3, 2018, the City of Barberton, Ohio (and related entities) filed a complaint in the same MDL proceeding (MDL No. 2804; Case No. 17-md-2804) in an action entitled City of Barberton, et al. v. Purdue Pharma, L.P., et al., Civil Action No. 1:18-op-45767-DAP, in the Northern District of Ohio, against Henry Schein, Inc., Henry Schein Medical Systems, Inc. and others, that is similar to The County of Summit complaint. This case has been designated “Track 2” and is currently stayed. On September 20, 2018, Southeast Alaska Regional Health Consortium filed a complaint entitled Southeast Alaska Regional Health Consortium v. Purdue Pharma L.P., et al., Case No. 3:18-cv-00217-TMB, in the U.S. District Court for the District of Alaska, against Henry Schein, Inc., Henry Schein Medical Systems, Inc. and others. That case was transferred to the MDL proceeding referenced above (MDL Civil Action No. 1:17-md-02804; Case No. 1:18-op-46149), designated a “Track 2” case and is currently stayed. On September 20, 2018, Tucson Medical Center filed a complaint entitled Tucson Medical Center v. Purdue Pharma L.P., et al., Case No. C20184213, in the Superior Court of Arizona, County of Pima, against



**HENRY SCHEIN, INC.**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**  
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Henry Schein, Inc. and others. On September 27, 2018, Defendants removed that case to the U.S. District Court for the District of Arizona (Case No. 4:18-cv-00481-RCC). On October 8, 2018, Tucson Medical Center voluntarily dismissed the lawsuit pending in the District of Arizona without prejudice. On October 9, 2018, Tucson Medical Center refiled the lawsuit in the Superior Court of Arizona, County of Pima (Case No. C20184991). On October 29, 2018, defendants removed the case to the U.S. District Court for the District of Arizona (Case No. CV-18-00532). Sales of opioids in North America last year were less than 1% of all North American sales. We intend to defend ourselves vigorously against these actions.

On October 9, 2018, a purported class action complaint entitled *Kramer v. Henry Schein, Inc., Patterson Co., Inc., Benco Dental Supply Co., and Unnamed Co-Conspirators*, was filed in the U.S. District Court for the Northern District of California. The complaint alleges that members of the proposed class, comprised of purchasers of dental services from dental practices in California, suffered antitrust injury due to an unlawful boycott, price-fixing or otherwise anticompetitive conspiracy among Henry Schein, Patterson and Benco. The complaint alleges that the alleged conspiracy overcharged California dental practices, orthodontic practices and dental laboratories on their purchase of dental supplies, which in turn passed on some or all of such overcharges to members of the California class purchasing dental services. Subject to certain exclusions, the complaint defines the class as “all persons residing in California purchasing and/or reimbursing for dental services from California dental practices on or after August 31, 2012.” The complaint alleges violations of California antitrust laws, including the Cartwright Act (Cal. Bus. and Prof. Code § 16720) and the Unfair Competition Act (Cal. Bus. and Prof. Code § 17200), and seeks a permanent injunction, actual damages to be determined at trial, trebled, reasonable attorneys’ fees and costs, and pre- and post-judgment interest. We intend to defend ourselves vigorously against this action.

From time to time, we may become a party to other legal proceedings, including, without limitation, product liability claims, employment matters, commercial disputes, governmental inquiries and investigations (which may in some cases involve our entering into settlement arrangements or consent decrees), and other matters arising out of the ordinary course of our business. While the results of any legal proceeding cannot be predicted with certainty, in our opinion none of these other pending matters are currently anticipated to have a material adverse effect on our consolidated financial position, liquidity or results of operations.

As of September 29, 2018, we had accrued our best estimate of potential losses relating to claims that were probable to result in liability and for which we were able to reasonably estimate a loss. This accrued amount, as well as related expenses, was not material to our financial position, results of operations or cash flows. Our method for determining estimated losses considers currently available facts, presently enacted laws and regulations and other factors, including probable recoveries from third parties.



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

### Cautionary Note Regarding Forward-Looking Statements

In accordance with the "Safe Harbor" provisions of the Private Securities Litigation Reform Act of 1995, we provide the following cautionary remarks regarding important factors that, among others, could cause future results to differ materially from the forward-looking statements, expectations and assumptions expressed or implied herein. All forward-looking statements made by us are subject to risks and uncertainties and are not guarantees of future performance. These forward-looking statements involve known and unknown risks, uncertainties and other factors that may cause our actual results, performance and achievements or industry results to be materially different from any future results, performance or achievements expressed or implied by such forward-looking statements. These statements are identified by the use of such terms as "may," "could," "expect," "intend," "believe," "plan," "estimate," "forecast," "project," "anticipate" or other comparable terms.

Risk factors and uncertainties that could cause actual results to differ materially from current and historical results include, but are not limited to: effects of a highly competitive and consolidating market; our dependence on third parties for the manufacture and supply of our products; our dependence upon sales personnel, customers, suppliers and manufacturers; our dependence on our senior management; fluctuations in quarterly earnings; risks from expansion of customer purchasing power and multi-tiered costing structures; increases in shipping costs for our products or other service issues with our third-party shippers; general global macro-economic conditions; risks associated with currency fluctuations; risks associated with political and economic uncertainty; disruptions in financial markets; volatility of the market price of our common stock; changes in the health care industry; implementation of health care laws; failure to comply with regulatory requirements and data privacy laws; risks associated with our global operations; transitional challenges associated with acquisitions and joint ventures, including the failure to achieve anticipated synergies; financial risks associated with acquisitions and joint ventures; litigation risks; new or unanticipated litigation developments; the dependence on our continued product development, technical support and successful marketing in the technology segment; our dependence on third parties for certain technologically advanced components; increased competition by third party online commerce sites; risks from disruption to our information systems; cyberattacks or other privacy or data security breaches; certain provisions in our governing documents that may discourage third-party acquisitions of us; changes in tax legislation; and risks associated with the ability to consummate the spin-off and merger of our Animal Health business with Direct Vet Marketing, Inc. (d/b/a Vets First Choice) and the timing of the closing of such transaction, as well as the ability to realize anticipated benefits and synergies of the transaction. The order in which these factors appear should not be construed to indicate their relative importance or priority.

We caution that these factors may not be exhaustive and that many of these factors are beyond our ability to control or predict. Accordingly, any forward-looking statements contained herein should not be relied upon as a prediction of actual results. We undertake no duty and have no obligation to update forward-looking statements.

### Where You Can Find Important Information

We may disclose important information through one or more of the following channels: SEC filings, public conference calls and webcasts, press releases, the investor relations page of our website ([www.henryschein.com](http://www.henryschein.com)) and the social media channels identified on the Newsroom page of our website.

### Recent Developments

#### *Common Stock Authorized*

Effective May 31, 2018, as a result of the 2-for-1 stock split that became effective on September 15, 2017, we increased our authorized common shares from 240,000,000 to 480,000,000.



## Executive-Level Overview

We believe we are the world's largest provider of health care products and services primarily to office-based dental, animal health and medical practitioners. We serve more than 1 million customers worldwide including dental practitioners and laboratories, animal health clinics and physician practices, as well as government, institutional health care clinics and other alternate care clinics. We believe that we have a strong brand identity due to our more than 86 years of experience distributing health care products.

We are headquartered in Melville, New York, employ more than 22,000 people (of which nearly 12,000 are based outside the United States) and have operations or affiliates in 34 countries, including the United States, Australia, Austria, Belgium, Brazil, Canada, Chile, China, the Czech Republic, Denmark, France, Germany, Hong Kong SAR, Ireland, Israel, Italy, Japan, Liechtenstein, Luxembourg, Malaysia, the Netherlands, New Zealand, Norway, Poland, Portugal, Romania, Slovakia, South Africa, Spain, Sweden, Switzerland, Thailand, United Arab Emirates and the United Kingdom.

We have established strategically located distribution centers to enable us to better serve our customers and increase our operating efficiency. This infrastructure, together with broad product and service offerings at competitive prices, and a strong commitment to customer service, enables us to be a single source of supply for our customers' needs. Our infrastructure also allows us to provide convenient ordering and rapid, accurate and complete order fulfillment.

Our common stock is traded on the Nasdaq Global Select Market tier of the Nasdaq Stock Market under the symbol HSIC.

### *Industry Overview*

In recent years, the health care industry has increasingly focused on cost containment. This trend has benefited distributors capable of providing a broad array of products and services at low prices. It also has accelerated the growth of HMOs, group practices, other managed care accounts and collective buying groups, which, in addition to their emphasis on obtaining products at competitive prices, tend to favor distributors capable of providing specialized management information support. We believe that the trend towards cost containment has the potential to favorably affect demand for technology solutions, including software, which can enhance the efficiency and facilitation of practice management.

Our operating results in recent years have been significantly affected by strategies and transactions that we undertook to expand our business, domestically and internationally, in part to address significant changes in the health care industry, including consolidation of health care distribution companies, health care reform, trends toward managed care, cuts in Medicare and collective purchasing arrangements.

Our current and future results have been and could be impacted by the current economic environment and uncertainty, particularly impacting overall demand for our products and services.



### *Industry Consolidation*

The health care products distribution industry, as it relates to office-based health care practitioners, is fragmented and diverse. This industry, which encompasses the dental, animal health and medical markets, was estimated to produce revenues of approximately \$45 billion in 2018 in the global markets. The industry ranges from sole practitioners working out of relatively small offices to group practices or service organizations ranging in size from a few practitioners to a large number of practitioners who have combined or otherwise associated their practices.

Due in part to the inability of office-based health care practitioners to store and manage large quantities of supplies in their offices, the distribution of health care supplies and small equipment to office-based health care practitioners has been characterized by frequent, small quantity orders, and a need for rapid, reliable and substantially complete order fulfillment. The purchasing decisions within an office-based health care practice are typically made by the practitioner or an administrative assistant. Supplies and small equipment are generally purchased from more than one distributor, with one generally serving as the primary supplier.

The trend of consolidation extends to our customer base. Health care practitioners are increasingly seeking to partner, affiliate or combine with larger entities such as hospitals, health systems, group practices or physician hospital organizations. In many cases, purchasing decisions for consolidated groups are made at a centralized or professional staff level; however, orders are delivered to the practitioners' offices.

We believe that consolidation within the industry will continue to result in a number of distributors, particularly those with limited financial, operating and marketing resources, seeking to combine with larger companies that can provide growth opportunities. This consolidation also may continue to result in distributors seeking to acquire companies that can enhance their current product and service offerings or provide opportunities to serve a broader customer base.

Our trend with regard to acquisitions and joint ventures has been to expand our role as a provider of products and services to the health care industry. This trend has resulted in our expansion into service areas that complement our existing operations and provide opportunities for us to develop synergies with, and thus strengthen, the acquired businesses.

As industry consolidation continues, we believe that we are positioned to capitalize on this trend, as we believe we have the ability to support increased sales through our existing infrastructure, although there can be no assurances that we will be able to successfully accomplish this. We also have invested in expanding our sales/marketing infrastructure to include a focus on building relationships with decision makers who do not reside in the office-based practitioner setting.

As the health care industry continues to change, we continually evaluate possible candidates for merger and joint venture or acquisition and intend to continue to seek opportunities to expand our role as a provider of products and services to the health care industry. There can be no assurance that we will be able to successfully pursue any such opportunity or consummate any such transaction, if pursued. If additional transactions are entered into or consummated, we would incur merger and/or acquisition-related costs, and there can be no assurance that the integration efforts associated with any such transaction would be successful.



### *Seasonality*

Our business is subject to seasonal and other quarterly fluctuations. Revenues and profitability generally have been higher in the third and fourth quarters due to the timing of sales of seasonal products (including influenza vaccine, equipment and software products), purchasing patterns of office-based health care practitioners and year-end promotions. Revenues and profitability generally have been lower in the first quarter, primarily due to increased sales in the prior two quarters.

### *Aging Population and Other Market Influences*

The health care products distribution industry continues to experience growth due to the aging population, increased health care awareness, the proliferation of medical technology and testing, new pharmacology treatments and expanded third-party insurance coverage. In addition, the physician market continues to benefit from the shift of procedures and diagnostic testing from acute care settings to alternate-care sites, particularly physicians' offices.

According to the U.S. Census Bureau's International Data Base, in 2018 there were more than six million Americans aged 85 years or older, the segment of the population most in need of long-term care and elder-care services. By the year 2050, that number is projected to nearly triple to approximately 19 million. The population aged 65 to 84 years is projected to increase approximately 50% during the same time period.

As a result of these market dynamics, annual expenditures for health care services continue to increase in the United States. We believe that demand for our products and services will grow, while continuing to be impacted by current and future operating, economic and industry conditions. The Centers for Medicare and Medicaid Services, or CMS, published "National Health Expenditure Projections 2017-2026" indicating that total national health care spending reached approximately \$3.5 trillion in 2017, or 18.0% of the nation's gross domestic product, the benchmark measure for annual production of goods and services in the United States. Health care spending is projected to reach approximately \$5.7 trillion in 2026, approximately 19.7% of the nation's gross domestic product.

### *Government*

Certain of our businesses involve the distribution of pharmaceuticals and medical devices, and in this regard we are subject to extensive local, state, federal and foreign governmental laws and regulations applicable to the distribution and sale of pharmaceuticals and medical devices. Additionally, government and private insurance programs fund a large portion of the total cost of medical care, and there has been an emphasis on efforts to control medical costs, including laws and regulations lowering reimbursement rates for pharmaceuticals, medical devices, and/or medical treatments or services. Also, many of these laws and regulations are subject to change and may impact our financial performance. In addition, our businesses are generally subject to numerous other laws and regulations that could impact our financial performance, including securities, antitrust, anti-bribery and anti-kickback, customer interaction transparency, data privacy, data security and other laws and regulations. Failure to comply with law or regulations could have a material adverse effect on our business.

### *Health Care Reform*

The United States Patient Protection and Affordable Care Act as amended by the Health Care and Education Reconciliation Act, each enacted in March 2010 (the "Health Care Reform Law"), increased federal oversight of private health insurance plans and included a number of provisions designed to reduce Medicare expenditures and the cost of health care generally, to reduce fraud and abuse, and to provide access to increased health coverage.

The Health Care Reform Law requirements include a 2.3% excise tax on domestic sales of many medical devices by manufacturers and importers that began in 2013 and a fee on branded prescription drugs and biologics that was implemented in 2011, both of which may affect sales. However, with respect to the medical device excise tax, a two-year moratorium was imposed under the Consolidated Appropriations Act, 2016, suspending the imposition of the tax on device sales during the period beginning January 1, 2016 and ending on December 31, 2017, and on January 22, 2018 an additional two-year moratorium was imposed under Public Law No. 115-120, suspending the imposition of the tax on device sales during the period beginning January 1, 2018 and ending on December 31, 2019. The Health Care Reform Law has also materially expanded the number of individuals in the



United States with health insurance. The Health Care Reform Law has faced ongoing legal challenges, including litigation seeking to invalidate some of or all of the law or the manner in which it has been implemented. In addition, the President is seeking to repeal and replace the Health Care Reform Law and has taken a number of administrative actions to materially weaken it, including, without limitation, by permitting the use of less robust health plans with lower coverage and eliminating “premium support” for insurers providing policies under the Health Care Reform Law. On December 22, 2017, the President signed into law the Tax Cuts and Jobs Act (the “Tax Act”), which contains a broad range of tax reform provisions that impact the individual and corporate tax rates, international tax provisions, income tax add-back provisions and deductions, and which also repealed the individual mandate of the Health Care Reform Law. The uncertain status of the Health Care Reform Law affects our ability to plan.

A Health Care Reform Law provision, generally referred to as the Physician Payment Sunshine Act or Open Payments Program, has imposed reporting and disclosure requirements for drug and device manufacturers and distributors with regard to payments or other transfers of value made to certain covered recipients (including physicians, dentists and teaching hospitals), and for such manufacturers and distributors and for group purchasing organizations, with regard to certain ownership interests held by physicians in the reporting entity. CMS publishes information from these reports on a publicly available website, including amounts transferred and physician, dentist and teaching hospital identities.

Under the Physician Payment Sunshine Act, we are required to collect and report detailed information regarding certain financial relationships we have with physicians, dentists and teaching hospitals. We believe that we are substantially compliant with applicable Physician Payment Sunshine Act requirements. The Physician Payment Sunshine Act pre-empts similar state reporting laws, although we or our subsidiaries may be required to report under certain state transparency laws that address circumstances not covered by the Physician Payment Sunshine Act, and some of these state laws, as well as the federal law, can be ambiguous. We are also subject to foreign regulations requiring transparency of certain interactions between suppliers and their customers. While we believe we have substantially compliant programs and controls in place to comply with these requirements, our compliance with these rules imposes additional costs on us.

Another notable Medicare health care reform initiative, the Medicare Access and CHIP Reauthorization Act of 2015 (“MACRA”), enacted on April 16, 2015, establishes a new payment framework, called the Quality Payment Program, which modifies certain Medicare payments to “eligible clinicians,” including physicians, dentists and other practitioners. Under MACRA, eligible clinicians are required to participate in Medicare through the Merit-Based Incentive Payment System (“MIPS”) or Advanced Alternative Payment Models (“APMs”). MIPS generally consolidated three programs; the physician quality reporting system, the value-based payment modifier and the Medicare electronic health record (“EHR”) program, into a single program in which Medicare reimbursement to eligible clinicians includes both positive and negative payment adjustments that take into account quality, resource use, clinical practice improvement and meaningful use of certified EHR technology. Advanced APMs generally involve higher levels of financial and technology risk. A final rule was published in the Federal Register on November 4, 2016 and allows eligible Medicare clinicians to pick their pace of participation for the first performance period that began January 1, 2017. The data collected in the first performance year will determine payment adjustments beginning January 1, 2019. A final rule updating certain Quality Payment Program regulations was published on November 16, 2017, which became effective as of January 1, 2018. MACRA represents a fundamental change in physician reimbursement that is expected to provide substantial financial incentives for physicians to participate in risk contracts, and to increase physician information technology and reporting obligations. The implications of the implementation of MACRA are uncertain and will depend on future regulatory activity and physician activity in the marketplace. MACRA may encourage physicians to move from smaller practices to larger physician groups or hospital employment, leading to a consolidation of a portion of our customer base. Although we believe that we are positioned to capitalize on this consolidation trend, there can be no assurances that we will be able to successfully accomplish this.



## *Health Care Fraud*

Certain of our businesses are subject to federal and state (and similar foreign) health care fraud and abuse, referral and reimbursement laws and regulations with respect to their operations. Some of these laws, referred to as “false claims laws,” prohibit the submission or causing the submission of false or fraudulent claims for reimbursement to federal, state and other health care payers and programs. Other laws, referred to as “anti-kickback laws,” prohibit soliciting, offering, receiving or paying remuneration in order to induce the referral of a patient or ordering, purchasing, leasing or arranging for, or recommending ordering, purchasing or leasing of, items or services that are paid for by federal, state and other health care payers and programs.

The fraud and abuse laws and regulations have been subject to varying interpretations and significant enforcement activity has been the result of “relators,” who serve as whistleblowers by filing complaints in the name of the United States (and if applicable, particular states) under federal and state false claims laws. Under the federal False Claims Act, relators can be entitled to receive up to 30% of total recoveries. Violations of the federal False Claims Act can result in treble damages, and, in accordance with a final rule published by the Department of Justice on January 29, 2018, civil penalties will generally range from a minimum of \$11,181 to a maximum of \$22,363 per claim. In addition, the Bipartisan Budget Act of 2018, signed into law on February 9, 2018, revised the penalties imposed for violations of the Anti-Kickback Law. Civil penalties may include fines of up to \$100,000 for each violation, plus up to three times the total amount of remuneration offered, paid, solicited or received, and exclusion from federal health care programs. Maximum criminal penalties have been increased from \$25,000 to \$100,000, and maximum prison time has doubled from five years to ten years.

Most states have adopted similar state false claims laws, and these state laws have their own penalties which may be in addition to federal False Claims Act penalties. The Health Care Reform Law significantly strengthened the federal False Claims Act and the federal Anti-Kickback Law provisions, which could lead to the possibility of increased whistleblower or relator suits, and among other things made clear that a federal Anti-Kickback Law violation can be a basis for federal False Claims Act liability.

The United States government (among others) has expressed concerns about financial relationships between suppliers on the one hand and physicians and dentists on the other. As a result, we regularly review and revise our marketing practices as necessary to facilitate compliance.

We also are subject to certain United States and foreign laws and regulations concerning the conduct of our foreign operations, including the U.S. Foreign Corrupt Practices Act, the U.K. Bribery Act, German anti-corruption laws and other anti-bribery laws and laws pertaining to the accuracy of our internal books and records, which have been the focus of increasing enforcement activity globally in recent years.

Failure to comply with fraud and abuse laws and regulations could result in significant civil and criminal penalties and costs, including the loss of licenses and the ability to participate in federal and state health care programs, and could have a material adverse effect on our business. Also, these measures may be interpreted or applied by a prosecutorial, regulatory or judicial authority in a manner that could require us to make changes in our operations or incur substantial defense and settlement expenses. Even unsuccessful challenges by regulatory authorities or private relators could result in reputational harm and the incurring of substantial costs. In addition, many of these laws are vague or indefinite and have not been interpreted by the courts, and have been subject to frequent modification and varied interpretation by prosecutorial and regulatory authorities, increasing the risk of noncompliance.

While we believe that we are substantially compliant with applicable fraud and abuse laws and regulations, and have adequate compliance programs and controls in place to ensure substantial compliance, we cannot predict whether changes in applicable law, or interpretation of laws, or changes in our services or marketing practices in response to changes in applicable law or interpretation of laws, could have a material adverse effect on our business.



### *Operating, Security and Licensure Standards*

Certain of our businesses involve the distribution of pharmaceuticals and medical devices, and in this regard we are subject to various local, state, federal and foreign governmental laws and regulations applicable to the distribution of pharmaceuticals and medical devices. Among the United States federal laws applicable to us are the Controlled Substances Act, the Federal Food, Drug, and Cosmetic Act, as amended (“FDC Act”), and Section 361 of the Public Health Service Act. We are also subject to comparable foreign regulations.

The FDC Act and similar foreign laws generally regulate the introduction, manufacture, advertising, labeling, packaging, storage, handling, reporting, marketing and distribution of, and record keeping for, pharmaceuticals and medical devices shipped in interstate commerce, and states may similarly regulate such activities within the state. Section 361 of the Public Health Service Act, which provides authority to prevent the spread of communicable diseases, serves as the legal basis for the United States Food and Drug Administration’s (“FDA”) regulation of human cells, tissues and cellular and tissue-based products, also known as “HCT/P products.”

The Federal Drug Quality and Security Act of 2013 brought about significant changes with respect to pharmaceutical supply chain requirements and pre-empts state law. Title II of this measure, known as the Drug Supply Chain Security Act (“DSCSA”), is being phased in over a period of ten years, and is intended to build a national electronic, interoperable system to identify and trace certain prescription drugs as they are distributed in the United States. The law’s track and trace requirements applicable to manufacturers, wholesalers, repackagers and dispensers (e.g., pharmacies) of prescription drugs took effect in January 2015, and continues to be implemented. The DSCSA product tracing requirements replace the former FDA drug pedigree requirements and pre-empt state requirements that are inconsistent with, more stringent than, or in addition to, the DSCSA requirements.

The DSCSA also establishes certain requirements for the licensing and operation of prescription drug wholesalers and third party logistics providers (“3PLs”), and includes the eventual creation of national wholesaler and 3PL licenses in cases where states do not license such entities. The DSCSA requires that wholesalers and 3PLs distribute drugs in accordance with certain standards regarding the recordkeeping, storage and handling of prescription drugs. According to FDA guidance, states are pre-empted from imposing any licensing requirements that are inconsistent with, less stringent than, directly related to, or covered by the standards established by federal law in this area. Current state licensing requirements will likely remain in effect until the FDA issues new regulations as directed by the DSCSA.

We believe that we are substantially compliant with applicable DSCSA requirements.

The Food and Drug Administration Amendments Act of 2007 and the Food and Drug Administration Safety and Innovation Act of 2012 amended the FDC Act to require the FDA to promulgate regulations to implement a unique device identification (“UDI”) system. The FDA is phasing in the implementation of the UDI regulations over seven years, generally beginning with the highest-risk devices (i.e., Class III medical devices) and ending with the lowest-risk devices. Most compliance dates will have been reached as of September 24, 2018, with a final set of requirements for low risk devices being reached on September 24, 2022, which will complete the phase in. The UDI regulations require “labelers” to include unique device identifiers (“UDIs”), with a content and format prescribed by the FDA and issued under a system operated by an FDA-accredited issuing agency, on the labels and packages of medical devices, and to directly mark certain devices with UDIs. The UDI regulations also require labelers to submit certain information concerning UDI-labeled devices to the FDA, much of which information is publicly available on an FDA database, the Global Unique Device Identification Database. The UDI regulations provide for certain exceptions, alternatives and time extensions. For example, the UDI regulations include a general exception for Class I devices exempt from the Quality System Regulation (other than record-keeping requirements and complaint files). Regulated labelers include entities such as device manufacturers, repackagers, reproducers and relabelers that cause a device’s label to be applied or modified, with the intent that the device will be commercially distributed without any subsequent replacement or modification of the label, and include certain of our businesses.



We believe that we are substantially compliant with applicable UDI requirements.

Under the Controlled Substances Act, as a distributor of controlled substances, we are required to obtain and renew annually registrations for our facilities from the United States Drug Enforcement Administration (“DEA”) permitting us to handle controlled substances. We are also subject to other statutory and regulatory requirements relating to the storage, sale, marketing, handling and distribution of such drugs, in accordance with the Controlled Substances Act and its implementing regulations, and these requirements have been subject to heightened enforcement activity in recent times. We are subject to inspection by the DEA.

Certain of our businesses are also required to register for permits and/or licenses with, and comply with operating and security standards of, the DEA, the FDA, the United States Department of Health and Human Services, and various state boards of pharmacy, state health departments and/or comparable state agencies as well as comparable foreign agencies, and certain accrediting bodies depending on the type of operations and location of product distribution, manufacturing or sale. These businesses include those that distribute, manufacture and/or repack prescription pharmaceuticals and/or medical devices and/or HCT/P products, or own pharmacy operations, or install, maintain or repair equipment. In addition, Section 301 of the National Organ Transplant Act, and a number of comparable state laws, impose civil and/or criminal penalties for the transfer of certain human tissue (for example, human bone products) for valuable consideration, while generally permitting payments for the reasonable costs incurred in procuring, processing, storing and distributing that tissue. We are also subject to foreign government regulation of such products. The DEA, the FDA and state regulatory authorities have broad inspection and enforcement powers, including the ability to suspend or limit the distribution of products by our distribution centers, seize or order the recall of products and impose significant criminal, civil and administrative sanctions for violations of these laws and regulations. Foreign regulations subject us to similar foreign enforcement powers. Furthermore, compliance with legal requirements has required and may in the future require us to institute voluntary recalls of products we sell, which could result in financial losses and potential reputational harm. Our customers are also subject to significant federal, state, local and foreign governmental regulation.

Certain of our businesses are subject to various additional federal, state, local and foreign laws and regulations, including with respect to the sale, transportation, storage, handling and disposal of hazardous or potentially hazardous substances, and safe working conditions.

Certain of our businesses also maintain contracts with governmental agencies and are subject to certain regulatory requirements specific to government contractors.

#### *Antitrust*

The U.S. federal government, most U.S. states and many foreign countries have antitrust laws that prohibit certain types of conduct deemed to be anti-competitive. Violations of antitrust laws can result in various sanctions, including criminal and civil penalties. Private plaintiffs also could bring civil lawsuits against us in the United States for alleged antitrust law violations, including claims for treble damages.

#### *Regulated Software and Data Processing; Electronic Health Records*

The FDA has become increasingly active in addressing the regulation of computer software intended for use in health care settings. The 21<sup>st</sup> Century Cures Act (Cures Act), signed into law on December 13, 2016, amended the device definition to exclude certain software, including clinical decision support software that meet certain criteria. In December 2017, the FDA issued draft guidance documents describing its proposed interpretation of the statutory language regarding which types of clinical decision support tools and other software are exempt from regulation as medical devices. Certain of our businesses involve the development and sale of software and related products to support physician and dental practice management, and it is possible that the FDA or foreign government authorities could determine that one or more of our products is a medical device, which could subject us or one or more of our businesses to substantial additional requirements with respect to these products.



In addition, the European Parliament and the Council of the European Union have adopted a new pan-European General Data Protection Regulation (“GDPR”), effective from May 25, 2018, which increases privacy rights for individuals in Europe, extends the scope of responsibilities for data controllers and data processors and imposes increased requirements and potential penalties on companies offering goods or services to individuals who are located in Europe (“Data Subjects”) or monitoring the behavior of such individuals (including by companies based outside of Europe). Noncompliance can result in penalties of up to the greater of EUR 20 million, or 4% of global company revenues. Individual member states may impose additional requirements and penalties as they relate to certain things such as employee personal data. Among other things, the GDPR requires with respect to data concerning Data Subjects, company accountability, consents from Data Subjects or other acceptable legal basis needed to process the personal data, prompt breach notifications within 72 hours, fairness and transparency in how the personal data is stored, used or otherwise processed, and data integrity and security, and provides rights to Data Subjects relating to modification, erasure and transporting of the personal data. While we believe that we have substantially compliant programs and controls in place to comply with the GDPR requirements, our compliance with the new regulation is likely to impose additional costs on us, and we cannot predict whether the interpretations of the requirements, or changes in our practices in response to new requirements or interpretations of the requirements, could have a material adverse effect on our business.

We also sell products and services that health care providers, such as physicians and dentists, use to store and manage patient medical or dental records. These customers are subject to laws, regulations and industry standards, such as HIPAA and the Payment Card Industry Data Security Standards, which require that they protect the privacy and security of those records, and our products may be used as part of these customers’ comprehensive data security programs, including in connection with their efforts to comply with applicable privacy and security laws. Perceived or actual security vulnerabilities in our products or services, or the perceived or actual failure by us or our customers who use our products to comply with applicable legal or contractual requirements, may not only cause us significant reputational harm, but may also lead to claims against us by our customers and/or governmental agencies and involve substantial fines, penalties and other liabilities and expenses and costs for remediation.

Federal initiatives provide programs of incentive payments available to certain health care providers involving the adoption and use of certain electronic health care records systems and processes. These programs, now generally known as the Promoting Interoperability Programs, include providing, among others, physicians and dentists, with financial incentives if they use certified EHR technology in accordance with applicable and evolving requirements. These requirements involve measurements of quality, promoting interoperability, improvement activities and improving patient access to health information. Qualification for the incentive payments requires the use of EHRs that have certain capabilities pursuant to evolving standards adopted by CMS and by the Office of the National Coordinator for Health Information Technology (“ONC”) of the Department of Health and Human Services. The use of certified EHR technology will also continue as a feature of MACRA’s MIPS program. The first performance period for MIPS began January 1, 2017, and will afford eligible clinicians different reporting options linked to the amount of data reported and the duration of the reporting period, with positive payment adjustments generally linked to more robust reporting.

Certain of our businesses involve the manufacture and sale of certified EHR systems and other products linked to incentive programs. CMS and ONC establish criteria for certified EHR systems, and these criteria have been subject to change. In order to maintain certification of our EHR products, we must satisfy these changing governmental criteria. If any of our EHR systems do not meet these standards, yet have been relied upon by health care providers to receive federal incentive payments, as noted above, we are exposed to risk under federal health care fraud and abuse laws, such as the False Claims Act. For example, on May 31, 2017, the U.S. Department of Justice announced a \$155 million settlement and 5-year corporate integrity agreement involving a vendor of certified EHR systems, based on allegations that the vendor, by misrepresenting capabilities to the certifying body, caused its health care provider customers to submit false Medicare and Medicaid claims for meaningful use payments in violation of the False Claims Act. While we believe we are substantially in compliance with such certifications and with applicable fraud and abuse laws and regulations, and we have adequate compliance programs and controls in place to ensure substantial compliance, we cannot predict whether changes in applicable law, or interpretation of laws, or changes in our practices in response to changes in applicable



law or interpretation of laws, could have a material adverse effect on our business. Moreover, in order to satisfy our customers, our products may need to incorporate increasingly complex reporting functionality. Although we believe we are positioned to accomplish this, the effort may involve increased costs, and our failure to implement product modifications, or otherwise satisfy applicable standards, could have a material adverse effect on our business.

Other health information standards, such as regulations under HIPAA, establish standards regarding electronic health data transmissions and transaction code set rules for specific electronic transactions, such as transactions involving claims submissions to third party payers. Certain of our businesses provide electronic practice management products that must meet these requirements. Failure to abide by electronic health data transmission standards could expose us to breach of contract claims, substantial fines, penalties, and other liabilities and expenses, costs for remediation and harm to our reputation.

Additionally, as electronic medical devices are increasingly connected to each other and to other technology, the ability of these connected systems safely and effectively to exchange and use exchanged information becomes increasingly important. On September 6, 2017, the FDA issued guidance to assist in identifying specific considerations related to the ability of electronic medical devices to safely and effectively exchange and use exchanged information. As a medical device manufacturer, we must manage risks including those associated with an electronic interface that is incorporated into a medical device.

There may be additional legislative initiatives in the future impacting health care.

#### **E-Commerce**

Electronic commerce solutions have become an integral part of traditional health care supply and distribution relationships. Our distribution business is characterized by rapid technological developments and intense competition. The continuing advancement of online commerce requires us to cost-effectively adapt to changing technologies, to enhance existing services and to develop and introduce a variety of new services to address the changing demands of consumers and our customers on a timely basis, particularly in response to competitive offerings.

Through our proprietary, technologically based suite of products, we offer customers a variety of competitive alternatives. We believe that our tradition of reliable service, our name recognition and large customer base built on solid customer relationships, position us well to participate in this significant aspect of the distribution business. We continue to explore ways and means to improve and expand our Internet presence and capabilities, including our online commerce offerings and our use of various social media outlets.



## Results of Operations

The following table summarizes the significant components of our operating results for the three and nine months ended September 29, 2018 and September 30, 2017 and cash flows for the nine months ended September 29, 2018 and September 30, 2017 (in thousands):

	Three Months Ended		Nine Months Ended	
	September 29, 2018	September 30, 2017	September 29, 2018	September 30, 2017
<b>Operating results:</b>				
Net sales .....	\$ 3,279,678	\$ 3,161,083	\$ 9,826,793	\$ 9,143,489
Cost of sales .....	2,391,118	2,325,029	7,141,569	6,645,342
Gross profit .....	888,560	836,054	2,685,224	2,498,147
Operating expenses:				
Selling, general and administrative .....	668,011	622,506	2,027,138	1,874,644
Litigation settlements.....	38,488	-	38,488	5,325
Transaction costs related to Animal Health spin-off.....	7,282	-	18,670	-
Restructuring costs .....	8,853	-	27,511	-
Operating income .....	\$ 165,926	\$ 213,548	\$ 573,417	\$ 618,178
Other expense, net .....	\$ (16,228)	\$ (8,829)	\$ (41,839)	\$ (23,363)
Net income .....	126,976	150,948	423,116	450,783
Net income attributable to Henry Schein, Inc. ....	121,478	138,031	402,908	414,834
<b>Cash flows:</b>				
Net cash provided by operating activities .....			\$ 390,754	\$ 307,501
Net cash used in investing activities .....			(146,357)	(320,795)
Net cash provided by (used in) financing activities .....			(318,516)	16,068

## Plan of Restructuring

On July 9, 2018, we committed to an initiative to rationalize our operations and provide expense efficiencies. These actions will allow us to execute on our plan to reduce our cost structure and fund new initiatives that will drive future growth under our 2018 to 2020 strategic plan. This initiative is expected to include the elimination of approximately 2% to 3% of our workforce and the closing of certain facilities. The total 2018 costs associated with the actions to complete this restructuring are expected to be in the range of \$45 million to \$55 million pre-tax, or \$0.22 to \$0.27 per diluted share, consisting of \$40 million to \$45 million in employee severance pay and benefits and \$5 million to \$10 million in facility costs, representing primarily lease termination and other facility closure related costs.

During the three and nine months ended September 29, 2018, we recorded restructuring costs of \$8.9 million and \$27.5 million, respectively, primarily for certain redundancies. The costs associated with these restructuring activities are included in a separate line item, "Restructuring costs" within our consolidated statements of income.



### Three Months Ended September 29, 2018 Compared to Three Months Ended September 30, 2017

#### Net Sales

Net sales for the three months ended September 29, 2018 and September 30, 2017 were as follows (in thousands):

	September 29, 2018	% of Total	September 30, 2017	% of Total	Increase \$	%
Health care distribution (1):						
Dental .....	\$ 1,514,538	46.2%	\$ 1,478,730	46.8%	\$ 35,808	2.4%
Animal health .....	899,295	27.4	882,580	27.9	16,715	1.9
Medical .....	721,942	22.0	690,761	21.9	31,181	4.5
Total health care distribution .....	3,135,775	95.6	3,052,071	96.6	83,704	2.7
Technology and value-added services (2).....	143,903	4.4	109,012	3.4	34,891	32.0
Total .....	\$ 3,279,678	100.0%	\$ 3,161,083	100.0%	\$ 118,595	3.8

(1) Consists of consumable products, small equipment, laboratory products, large equipment, equipment repair services, branded and generic pharmaceuticals, vaccines, surgical products, diagnostic tests, infection-control products and vitamins.

(2) Consists of practice management software and other value-added products, which are distributed primarily to health care providers, and financial services on a non-recourse basis, e-services, continuing education services for practitioners, consulting and other services.

The \$118.6 million, or 3.8%, increase in net sales for the three months ended September 29, 2018 includes an increase of 5.1% local currency growth (3.2% increase in internally generated revenue and 1.9% growth from acquisitions) partially offset by a decrease of 1.3% related to foreign currency exchange.

The \$35.8 million, or 2.4%, increase in dental net sales for the three months ended September 29, 2018 includes an increase of 4.4% in local currency growth (3.5% increase in internally generated revenue and 0.9% growth from acquisitions) partially offset by a decrease of 2.0% related to foreign currency exchange. The 4.4% increase in local currency sales was due to increases in dental consumable merchandise sales growth of 5.1% (4.0% growth from internally generated revenue and 1.1% growth from acquisitions) and dental equipment sales and service revenues of 2.1% (2.0% growth from internally generated revenue and 0.1% growth from acquisitions).

The \$16.7 million, or 1.9%, increase in animal health net sales for the three months ended September 29, 2018 includes an increase of 3.4% local currency growth (1.1% increase in internally generated revenue and 2.3% growth from acquisitions) partially offset by a decrease of 1.5% related to foreign currency exchange. The local currency growth in animal health revenue is affected by the revenue for certain products being recognized on an agency basis in 2018 that had been recognized on a principal basis in the prior year. When excluding the effects of this change, internally generated revenue grew by 4.3%.

The \$31.2 million, or 4.5%, increase in medical net sales for the three months ended September 29, 2018 consists of an increase of 4.4% in internally generated revenue and 0.1% growth from acquisitions.

The \$34.9 million, or 32.0%, increase in technology and value-added services net sales for the three months ended September 29, 2018 includes an increase of 32.6% local currency growth (7.8% increase in internally generated revenue and 24.8% growth from acquisitions) partially offset by a decrease of 0.6% related to foreign currency exchange.



## Gross Profit

Gross profit and gross margin percentages for the three months ended September 29, 2018 and September 30, 2017 were as follows (in thousands):

	September 29, 2018	Gross Margin %	September 30, 2017	Gross Margin %	Increase \$	%
Health care distribution .....	\$ 788,423	25.1%	\$ 765,528	25.1%	\$22,895	3.0%
Technology and value-added services .....	100,137	69.6	70,526	64.7	29,611	42.0
Total .....	\$ 888,560	27.1	\$ 836,054	26.4	\$52,506	6.3

Gross profit increased \$52.5 million, or 6.3%, for the three months ended September 29, 2018, compared to the prior year period. As a result of different practices of categorizing costs associated with distribution networks throughout our industry, our gross margins may not necessarily be comparable to other distribution companies. Additionally, we realize substantially higher gross margin percentages in our technology segment than in our health care distribution segment. These higher gross margins result from being both the developer and seller of software products and services, as well as certain financial services. The software industry typically realizes higher gross margins to recover investments in research and development.

Within our health care distribution segment, gross profit margins may vary from one period to the next. Changes in the mix of products sold as well as changes in our customer mix have been the most significant drivers affecting our gross profit margin. For example, sales of pharmaceutical products are generally at lower gross profit margins than other products. Conversely, sales of our private label products achieve gross profit margins that are higher than average. With respect to customer mix, sales to our large-group customers are typically completed at lower gross margins due to the higher volumes sold as opposed to the gross margin on sales to office-based practitioners who normally purchase lower volumes at greater frequencies.

Health care distribution gross profit increased \$22.9 million, or 3.0%, for the three months ended September 29, 2018 compared to the prior year period. Health care distribution gross profit margin remained consistent at 25.1% for the three months ended September 29, 2018 and September 30, 2017. The overall increase in our health care distribution gross profit is attributable to a \$13.2 million gross profit increase from growth in internally generated revenue and \$10.5 million is attributable to acquisitions. These increases were partially offset by a \$0.8 million decline in gross profit due to lower gross margin rates.

Technology and value-added services gross profit increased \$29.6 million, or 42.0%, for the three months ended September 29, 2018 compared to the prior year period. Technology and value-added services gross profit margin increased to 69.6% for the three months ended September 29, 2018 from 64.7% for the comparable prior year period, primarily due to our Henry Schein One joint venture which closed on July 1, 2018, as well as favorable sales mix. Acquisitions accounted for \$22.0 million of our gross profit increase within our technology and value-added services segment for the three months ended September 29, 2018 compared to the prior year period. The remaining increase of \$7.6 million in our technology and value-added services segment gross profit was attributable to growth of \$5.1 million in internally generated revenue and \$2.5 million related to increases in gross margin rates.



### Selling, General and Administrative

Selling, general and administrative expenses for the three months ended September 29, 2018 and September 30, 2017 were as follows (in thousands):

	September 29, Respective		September 30, Respective		Increase	
	2018	% of Net Sales	2017	% of Net Sales	\$	%
Health care distribution .....	\$ 660,434	21.1%	\$ 583,915	19.1%	\$ 76,519	13.1%
Technology and value-added services .....	62,200	43.2	38,591	35.4	23,609	61.2
Total .....	\$ 722,634	22.0	\$ 622,506	19.7	\$100,128	16.1

Selling, general and administrative expenses (together with litigation settlements, transactions costs related to the Animal Health spin-off and restructuring costs) increased \$100.1 million, or 16.1%, for the three months ended September 29, 2018 from the comparable prior year period. The \$76.5 million increase in selling, general and administrative expenses within our health care distribution segment for the three months ended September 29, 2018 as compared to the prior year period was attributable to \$67.5 million of additional operating costs (including \$38.5 million for a litigation settlement, \$7.3 million of transaction costs related to the Animal Health spin-off and \$7.3 million of restructuring costs), and \$9.0 million of additional costs from acquired companies. The \$23.6 million increase in selling, general and administrative expenses within our technology and value-added services segment for the three months ended September 29, 2018 as compared to the prior year period was attributable to \$21.6 million of additional costs from acquired companies and \$2.0 million of additional operating costs (including \$1.6 million of restructuring costs). As a percentage of net sales, selling, general and administrative expenses increased to 22.0% from 19.7% for the comparable prior year period primarily due to the costs mentioned above.

As a component of total selling, general and administrative expenses, selling expenses increased \$15.7 million, or 4.1% to \$401.4 million, for the three months ended September 29, 2018 from the comparable prior year period. As a percentage of net sales, selling expenses remained consistent at 12.2%.

As a component of total selling, general and administrative expenses, general and administrative expenses increased \$84.4 million, or 35.7% to \$321.2 million, for the three months ended September 29, 2018 from the comparable prior year period primarily due to \$38.5 million for a litigation settlement, \$7.3 million of transaction costs related to the Animal Health spin-off and \$8.9 million of restructuring costs. As a percentage of net sales, general and administrative expenses increased to 9.8% from 7.5% for the comparable prior year period.

### Other Expense, Net

Other expense, net, for the three months ended September 29, 2018 and September 30, 2017 was as follows (in thousands):

	September 29, September 30,		Variance	
	2018	2017	\$	%
Interest income .....	\$ 5,163	\$ 4,793	\$ 370	7.7%
Interest expense .....	(21,045)	(13,428)	(7,617)	(56.7)
Other, net .....	(346)	(194)	(152)	(78.4)
Other expense, net .....	\$ (16,228)	\$ (8,829)	\$ (7,399)	(83.8)

Other expense, net increased \$7.4 million to \$16.2 million for the three months ended September 29, 2018 from the comparable prior year period. Interest expense increased \$7.6 million primarily due to increased borrowings under our bank credit lines and our private placement facilities, as well as higher interest rates.



***Income Taxes***

For the three months ended September 29, 2018, our effective tax rate was 19.6% compared to 29.0% for the prior year period. The difference between our effective tax rate and the federal statutory tax rate for the three months ended September 29, 2018 primarily relates to a provisional transition tax benefit of \$10 million related to the Tax Act, as well as state and foreign income taxes and interest expense. See Note 12 “Income Taxes” in the Notes to the Consolidated Financial Statements. The difference between our effective tax rate and the federal statutory tax rate for the three months ended September 30, 2017 primarily relates to state and foreign income taxes and interest expense.

***Net Income***

Net income decreased \$24.0 million, or 15.9%, for the three months ended September 29, 2018, compared to the prior year period due to the factors noted above.



**Nine Months Ended September 29, 2018 Compared to Nine Months Ended September 30, 2017**

**Net Sales**

Net sales for the nine months ended September 29, 2018 and September 30, 2017 were as follows (in thousands):

	September 29, 2018	% of Total	September 30, 2017	% of Total	Increase \$	%
Health care distribution (1):						
Dental .....	\$ 4,675,212	47.6%	\$ 4,372,055	47.8%	\$303,157	6.9%
Animal health .....	2,805,031	28.5	2,586,850	28.3	218,181	8.4
Medical .....	1,976,367	20.1	1,861,074	20.4	115,293	6.2
Total health care distribution .....	9,456,610	96.2	8,819,979	96.5	636,631	7.2
Technology and value-added services (2).....	370,183	3.8	323,510	3.5	46,673	14.4
Total .....	\$ 9,826,793	100.0%	\$ 9,143,489	100.0%	\$683,304	7.5

(1) Consists of consumable products, small equipment, laboratory products, large equipment, equipment repair services, branded and generic pharmaceuticals, vaccines, surgical products, diagnostic tests, infection-control products and vitamins.

(2) Consists of practice management software and other value-added products, which are distributed primarily to health care providers, and financial services on a non-recourse basis, e-services, continuing education services for practitioners, consulting and other services.

The \$683.3 million, or 7.5%, increase in net sales for the nine months ended September 29, 2018 includes an increase of 5.9% in local currency growth (3.9% increase in internally generated revenue and 2.0% growth from acquisitions) as well as an increase of 1.6% related to foreign currency exchange.

The \$303.2 million, or 6.9%, increase in dental net sales for the nine months ended September 29, 2018 includes an increase of 5.2% in local currency growth (3.6% increase in internally generated revenue and 1.6% growth from acquisitions) as well as an increase of 1.7% related to foreign currency exchange. The 5.2% increase in local currency sales was due to an increase in dental consumable merchandise sales growth of 5.4% (3.4% growth from internally generated revenue and 2.0% growth from acquisitions) and dental equipment sales and service revenues of 4.5%, all of which is attributable to growth from internally generated revenue.

The \$218.2 million, or 8.4%, increase in animal health net sales for the nine months ended September 29, 2018 includes an increase of 6.0% in local currency growth (3.0% internally generated revenue and 3.0% growth from acquisitions) as well as an increase of 2.4% related to foreign currency exchange. The local currency growth in animal health revenue is affected by the revenue for certain products being recognized on an agency basis in 2018 that had been recognized on a principal basis in the prior year. When excluding the effects of this change, internally generated revenue grew by 6.8%.

The \$115.3 million, or 6.2%, increase in medical net sales for the nine months ended September 29, 2018 includes an increase of 6.0% in local currency growth (5.9% increase in internally generated revenue and 0.1% growth from acquisitions) as well as an increase of 0.2% related to foreign currency exchange.

The \$46.7 million, or 14.4%, increase in technology and value-added services net sales for the nine months ended September 29, 2018 includes an increase of 13.5% in local currency growth (4.6% increase in internally generated revenue and 8.9% growth from acquisitions) as well as an increase of 0.9% related to foreign currency exchange.



## Gross Profit

Gross profit and gross margin percentages for the nine months ended September 29, 2018 and September 30, 2017 were as follows (in thousands):

	September 29, 2018	Gross Margin %	September 30, 2017	Gross Margin %	Increase	
	\$	%	\$	%	\$	%
Health care distribution .....	\$ 2,438,300	25.8%	\$ 2,286,863	25.9%	\$151,437	6.6%
Technology and value-added services .....	246,924	66.7	211,284	65.3	35,640	16.9
<b>Total .....</b>	<b>\$ 2,685,224</b>	<b>27.3</b>	<b>\$ 2,498,147</b>	<b>27.3</b>	<b>\$187,077</b>	<b>7.5</b>

For the nine months ended September 29, 2018, gross profit increased \$187.1 million, or 7.5%, from the comparable prior year period. As a result of different practices of categorizing costs associated with distribution networks throughout our industry, our gross margins may not necessarily be comparable to other distribution companies. Additionally, we realize substantially higher gross margin percentages in our technology segment than in our health care distribution segment. These higher gross margins result from being both the developer and seller of software products and services, as well as certain financial services. The software industry typically realizes higher gross margins to recover investments in research and development.

Within our health care distribution segment, gross profit margins may vary from one period to the next. Changes in the mix of products sold as well as changes in our customer mix have been the most significant drivers affecting our gross profit margin. For example, sales of pharmaceutical products are generally at lower gross profit margins than other products. Conversely, sales of our private label products achieve gross profit margins that are higher than average. With respect to customer mix, sales to our large-group customers are typically completed at lower gross margins due to the higher volumes sold as opposed to the gross margin on sales to office-based practitioners who normally purchase lower volumes at greater frequencies.

Health care distribution gross profit increased \$151.4 million, or 6.6%, for the nine months ended September 29, 2018 compared to the prior year period. Health care distribution gross profit margin decreased to 25.8% for the nine months ended September 29, 2018 from 25.9% for the comparable prior year period. The overall increase in our health care distribution gross profit is attributable to a \$126.1 million gross profit increase from growth in internally generated revenue and a \$44.3 million gross profit increase from acquisitions, partially offset by a \$19.0 million decrease due to lower gross margin rates.

Technology and value-added services gross profit increased \$35.6 million, or 16.9%, for the nine months ended September 29, 2018 compared to the prior year period. Technology gross profit margin increased to 66.7% for the nine months ended September 29, 2018 from 65.3% for the comparable prior year period. Acquisitions accounted for \$23.2 million of our gross profit increase within our technology and value-added services segment for the nine months ended September 29, 2018 compared to the prior year period. The remaining increase of \$12.4 million in technology and value-added services segment gross profit was attributable to growth of \$11.5 million in internally generated revenue and \$0.9 million related to higher gross margin rates.



### Selling, General and Administrative

Selling, general and administrative expenses for the nine months ended September 29, 2018 and September 30, 2017 were as follows (in thousands):

	September 29, Respective		September 30, Respective		Increase	
	2018	% of Net Sales	2017	% of Net Sales	\$	%
Health care distribution .....	\$ 1,966,757	20.8%	\$ 1,765,585	20.0%	\$201,172	11.4%
Technology and value-added services .....	145,050	39.2	114,384	35.4	30,666	26.8
<b>Total .....</b>	<b>\$ 2,111,807</b>	<b>21.5</b>	<b>\$ 1,879,969</b>	<b>20.6</b>	<b>\$231,838</b>	<b>12.3</b>

Selling, general and administrative expenses (together with litigation settlements, transactions costs related to the Animal Health spin-off and restructuring costs) increased \$231.8 million, or 12.3%, to \$2,111.8 million for the nine months ended September 29, 2018 from the comparable prior year period. The \$201.2 million increase in selling, general and administrative expenses within our health care distribution segment for the nine months ended September 29, 2018 as compared to the prior year period was attributable to \$164.8 million of additional operating costs (including an increase of \$33.2 million for litigation settlements, \$18.7 million of transaction costs related to the Animal Health spin-off and \$25.6 million of restructuring costs), and \$36.4 million of additional costs from acquired companies. The \$30.6 million increase in selling, general and administrative expenses within our technology and value-added services segment for the nine months ended September 29, 2018 as compared to the prior year period was attributable to \$23.4 million of additional costs from acquired companies and \$7.2 million of additional operating costs (including \$1.9 million of restructuring costs). As a percentage of net sales, selling, general and administrative expenses increased to 21.5% from 20.6% for the comparable prior year period primarily due to the costs mentioned above.

As a component of selling, general and administrative expenses, selling expenses increased \$90.3 million, or 7.9%, to \$1,236.5 million for the nine months ended September 29, 2018 from the comparable prior year period. As a percentage of net sales, selling expenses increased to 12.6% from 12.5% for the comparable prior year period.

As a component of selling, general and administrative expenses, general and administrative expenses increased \$141.5 million, or 19.3%, to \$875.3 million for the nine months ended September 29, 2018 from the comparable prior year period primarily due to an increase of \$33.2 million for litigation settlements, \$18.7 million of transaction costs related to the Animal Health spin-off and \$27.5 million of restructuring costs. As a percentage of net sales, general and administrative expenses increased to 8.9% from 8.0% for the comparable year period.

### Other Expense, Net

Other expense, net, for the nine months ended September 29, 2018 and September 30, 2017 was as follows (in thousands):

	September 29, September 30,		Variance	
	2018	2017	\$	%
Interest income .....	\$ 15,429	\$ 13,204	\$ 2,225	16.9%
Interest expense .....	(56,466)	(37,056)	(19,410)	(52.4)
Other, net .....	(802)	489	(1,291)	(264.0)
<b>Other expense, net .....</b>	<b>\$ (41,839)</b>	<b>\$ (23,363)</b>	<b>\$ (18,476)</b>	<b>(79.1)</b>

Other expense, net increased \$18.5 million to \$41.8 million for the nine months ended September 29, 2018 from the comparable prior year period. Interest income increased \$2.2 million primarily due to increased interest and late fee income. Interest expense increased \$19.4 million primarily due to increased borrowings under our bank credit lines and our private placement facilities, as well as higher interest rates. Other, net decreased by \$1.3 million primarily due to changes in foreign exchange rates.



***Income Taxes***

Our effective tax rate was 23.3% for the nine months ended September 29, 2018 and 26.3% and for the nine months ended September 30, 2017. The difference between our effective tax rate and the federal statutory tax rate for the nine months ended September 29, 2018 primarily relates to a provisional transition tax benefit of \$10 million related to the Tax Act, as well as state and foreign income taxes and interest expense. See Note 12 “Income Taxes” in the Notes to the Consolidated Financial Statements. The difference between our effective tax rate and the federal statutory tax rate for the nine months ended September 30, 2017 primarily relates to the adoption of ASU 2016-09 in the first quarter of 2017, as well as state and foreign income taxes and interest expense.

***Net Income***

Net income decreased \$27.7 million, or 6.1%, for the nine months ended September 29, 2018, compared to the prior year period due to the factors noted above.



## Liquidity and Capital Resources

Our principal capital requirements include funding of acquisitions, purchases of additional noncontrolling interests, repayments of debt principal, the funding of working capital needs, purchases of fixed assets and repurchases of common stock. Working capital requirements generally result from increased sales, special inventory forward buy-in opportunities and payment terms for receivables and payables. Historically, sales have tended to be stronger during the third and fourth quarters and special inventory forward buy-in opportunities have been most prevalent just before the end of the year, and have caused our working capital requirements to be higher from the end of the third quarter to the end of the first quarter of the following year.

We finance our business primarily through cash generated from our operations, revolving credit facilities and debt placements. Our ability to generate sufficient cash flows from operations is dependent on the continued demand of our customers for our products and services, and access to products and services from our suppliers.

Our business requires a substantial investment in working capital, which is susceptible to fluctuations during the year as a result of inventory purchase patterns and seasonal demands. Inventory purchase activity is a function of sales activity, special inventory forward buy-in opportunities and our desired level of inventory. We anticipate future increases in our working capital requirements.

We finance our business to provide adequate funding for at least 12 months. Funding requirements are based on forecasted profitability and working capital needs, which, on occasion, may change. Consequently, we may change our funding structure to reflect any new requirements.

We believe that our cash and cash equivalents, our ability to access private debt markets and public equity markets, and our available funds under existing credit facilities provide us with sufficient liquidity to meet our currently foreseeable short-term and long-term capital needs. We have no off-balance sheet arrangements.

Net cash provided by operating activities was \$390.8 million for the nine months ended September 29, 2018, compared to \$307.5 million for the comparable prior year period. The net change of \$83.3 million was primarily attributable to working capital requirements, partially offset by lower net income.

Net cash used in investing activities was \$146.4 million for the nine months ended September 29, 2018, compared to \$320.8 million for the comparable prior year period. The net change of \$174.4 million was primarily due to reduced payments for equity investments and business acquisitions.

Net cash used in financing activities was \$318.5 million for the nine months ended September 29, 2018, compared to net cash provided by financing activities of \$16.1 million for the comparable prior year period. The net change of \$334.6 million was primarily due to increased acquisitions of noncontrolling interests in subsidiaries, partially offset by increased net borrowings from debt and decreased repurchases of common stock.



The following table summarizes selected measures of liquidity and capital resources (in thousands):

	September 29, December 30,	
	2018	2017
Cash and cash equivalents .....	\$ 119,740	\$ 174,658
Working capital .....	964,167	1,257,045
Debt:		
Bank credit lines .....	\$ 1,144,881	\$ 741,653
Current maturities of long-term debt .....	12,482	16,659
Long-term debt .....	1,000,315	907,756
Total debt .....	<u>\$ 2,157,678</u>	<u>\$ 1,666,068</u>

Our cash and cash equivalents consist of bank balances and investments in money market funds representing overnight investments with a high degree of liquidity.

*Accounts receivable days sales outstanding and inventory turns*

Our accounts receivable days sales outstanding from operations increased to 43.8 days as of September 29, 2018 from 43.2 days as of September 30, 2017. During the nine months ended September 29, 2018, we wrote off approximately \$5.0 million of fully reserved accounts receivable against our trade receivable reserve. Our inventory turns from operations decreased to 4.9 as of September 29, 2018 from 5.3 as of September 30, 2017. Our working capital accounts may be impacted by current and future economic conditions.

*Bank Credit Lines*

On April 18, 2017, we entered into a new \$750 million revolving credit agreement (the "Credit Agreement"). This facility, which matures in April 2022, replaced our \$500 million revolving credit facility, which was scheduled to mature in September 2019. The interest rate is based on the USD LIBOR plus a spread based on our leverage ratio at the end of each financial reporting quarter. On June 29, 2018, we amended the Credit Agreement to, among other things, (i) permit the consummation of the spin-off of our Animal Health business (the "Spin-off"), (ii) provide for swing-line commitments in the amount of \$75 million, and (iii) provide for the designation of subsidiary borrowers under the facility. The Credit Agreement provides, among other things, that we are required to maintain maximum leverage ratios, and contains customary representations, warranties and affirmative covenants. The Credit Agreement also contains customary negative covenants, subject to negotiated exceptions on liens, indebtedness, significant corporate changes (including mergers), dispositions and certain restrictive agreements.

As of September 29, 2018 and December 30, 2017, the borrowings under this revolving credit facility were \$350.0 million and \$320.0 million, respectively. As of September 29, 2018 and December 30, 2017, there were \$11.2 million and \$11.3 million of letters of credit, respectively, provided to third parties under the credit facility.

As of September 29, 2018 and December 30, 2017, we had various other short-term bank credit lines available, of which \$394.9 million and \$421.7 million, respectively, were outstanding. At September 29, 2018 and December 30, 2017, borrowings under all of our credit lines had a weighted average interest rate of 3.06% and 2.27%, respectively.



### Private Placement Facilities

On September 15, 2017, we increased our available private placement facilities with three insurance companies to a total facility amount of \$1 billion, and extended the expiration date to September 15, 2020. These facilities are available on an uncommitted basis at fixed rate economic terms to be agreed upon at the time of issuance, from time to time through September 15, 2020. The facilities allow us to issue senior promissory notes to the lenders at a fixed rate based on an agreed upon spread over applicable treasury notes at the time of issuance. The term of each possible issuance will be selected by us and can range from five to 15 years (with an average life no longer than 12 years). The proceeds of any issuances under the facilities will be used for general corporate purposes, including working capital and capital expenditures, to refinance existing indebtedness and/or to fund potential acquisitions. On June 29, 2018, we amended and restated the above private placement facilities to, among other things, (i) permit the consummation of the Spin-off and (ii) provide for the issuance of notes in Euros, British Pounds and Australian Dollars, in addition to U.S. Dollars. The agreements provide, among other things, that we maintain certain maximum leverage ratios, and contain restrictions relating to subsidiary indebtedness, liens, affiliate transactions, disposal of assets and certain changes in ownership. These facilities contain make-whole provisions in the event that we pay off the facilities prior to the applicable due dates.

The components of our private placement facility borrowings as of September 29, 2018 are presented in the following table (in thousands):

<u>Date of Borrowing</u>	<u>Amount of Borrowing Outstanding</u>	<u>Borrowing Rate</u>	<u>Due Date</u>
September 2, 2010	\$ 100,000	3.79%	September 2, 2020
January 20, 2012	50,000	3.45	January 20, 2024
January 20, 2012 (1)	28,571	3.09	January 20, 2022
December 24, 2012	50,000	3.00	December 24, 2024
June 2, 2014	100,000	3.19	June 2, 2021
June 16, 2017	100,000	3.42	June 16, 2027
September 15, 2017	100,000	3.52	September 15, 2029
January 2, 2018	100,000	3.32	January 2, 2028
Less: Deferred debt issuance costs	(439)		
	<u>\$ 628,132</u>		

(1) Annual repayments of approximately \$7.1 million for this borrowing commenced on January 20, 2016.

### Committed Loan Associated with Animal Health Spin-off

On May 21, 2018, we obtained a \$400 million committed loan which matures on the earlier of (i) March 31, 2019 and (ii) the consummation of the Spin-off. The proceeds of this loan were used, among other things, to fund our purchase of all of the equity interests in Butler Animal Health Holding Company, LLC (“BAHHC”) directly or indirectly owned by Darby Group Companies, Inc. (“Darby”) and certain other sellers pursuant to the terms of that certain Amendment to Put Rights Agreements, dated as of April 20, 2018, by and among us, Darby, BAHHC and the individual sellers party thereto for an aggregate purchase price of \$365 million. As of September 29, 2018, the balance outstanding on this loan was \$400 million and is included within the “Bank credit lines” caption within our consolidated balance sheet. At September 29, 2018, the interest rate on this loan was 3.125%.



### U.S. Trade Accounts Receivable Securitization

We have a facility agreement with a bank, as agent, based on the securitization of our U.S. trade accounts receivable that is structured as an asset-backed securitization program with pricing committed for up to three years. On June 1, 2016, we extended the expiration date of this facility agreement to April 29, 2019 and increased the purchase limit under the facility from \$300 million to \$350 million. On July 6, 2017, we extended the expiration date of this facility agreement to April 29, 2020. The borrowings outstanding under this securitization facility were \$350 million and \$350 million as of September 29, 2018 and December 30, 2017, respectively. At September 29, 2018, the interest rate on borrowings under this facility was based on the asset-backed commercial paper rate of 2.31% plus 0.75%, for a combined rate of 3.06%. At December 30, 2017, the interest rate on borrowings under this facility was based on the asset-backed commercial paper rate of 1.53% plus 0.75%, for a combined rate of 2.28%.

We are required to pay a commitment fee of 30 basis points on the daily balance of the unused portion of the facility if our usage is greater than or equal to 50% of the facility limit or a commitment fee of 35 basis points on the daily balance of the unused portion of the facility if our usage is less than 50% of the facility limit.

Borrowings under this facility are presented as a component of Long-term debt within our consolidated balance sheet.

### Long-term debt

Long-term debt consisted of the following:

	September 29, December 30,	
	2018	2017
Private placement facilities .....	\$ 628,132	\$ 535,295
U.S. trade accounts receivable securitization .....	350,000	350,000
Various collateralized and uncollateralized loans payable with interest in varying installments through 2022 at interest rates ranging from 2.61% to 4.73% at September 29, 2018 and ranging from 2.56% to 12.90% at December 30, 2017 .....	29,719	34,027
Capital lease obligations payable through 2029 with interest rates ranging from 0.07% to 19.79% at September 29, 2018 and ranging from 0.84% to 19.79% at December 30, 2017 .....	4,946	5,093
Total .....	1,012,797	924,415
Less current maturities .....	(12,482)	(16,659)
Total long-term debt .....	\$ 1,000,315	\$ 907,756



### *Acquisitions*

On July 1, 2018, we closed on a joint venture with Internet Brands, a provider of web presence and online marketing software, to create a newly formed entity, Henry Schein One, LLC. The joint venture includes Henry Schein Practice Solutions products and services, as well as Henry Schein's international dental practice management systems and the dental businesses of Internet Brands. We own 74% of the joint venture and Internet Brands owns the remaining 26% minority interest. Beginning with the second anniversary of the effective date of the formation of the joint venture, Henry Schein One will issue a fixed number of additional interests to Internet Brands through the fifth anniversary of the effective date, thereby increasing Internet Brands' ownership by approximately 7.6%. Internet Brands will also be entitled to receive a fixed number of additional interests, in the aggregate up to approximately 1.6% of the joint venture's ownership, if certain operating targets are met by the joint venture in its fourth, fifth and sixth operating years. Senior management from Henry Schein and Internet Brands serve on the board of Henry Schein One. The combined entity, which serves markets globally, had pro-forma 2017 sales of approximately \$400 million, of which approximately \$100 million originated at Internet Brands. As a result of this acquisition, \$412.8 million of initial goodwill resulted which reflects the excess of our purchase price over the fair value of the net assets acquired. The initial goodwill recorded as part of the acquisition primarily reflects the value of future synergies. We allocated all of the goodwill to our Technology and value-added services reporting segment. None of the goodwill recognized is deductible for income tax purposes, and as such, no deferred taxes have been recorded related to goodwill.

Concurrent with the formation of Henry Schein One, LLC, we entered into a separate agreement with Internet Brands whereby (1) beginning July 1, 2023, Internet Brands will have the right to require Henry Schein to purchase all or a portion of Internet Brands ownership interests in Henry Schein One, LLC for fair market value, and (2) beginning July 1, 2028, or earlier if certain events occur, Henry Schein will have the right to require Internet Brands to sell all or a portion of its ownership interests in Henry Schein One, LLC to Henry Schein for fair market value.

### *Planned Divestiture*

On April 23, 2018, we announced that we entered into a definitive agreement with HS Spinco, Inc., a direct, wholly owned subsidiary of Henry Schein ("Spinco"), and Direct Vet Marketing, Inc. (d/b/a Vets First Choice) ("DVM") to create a newly formed company, Vets First Corp. The transaction is intended to be tax-free to Henry Schein stockholders for U.S. tax purposes. As part of this transaction, subject to the terms and conditions set forth in certain definitive agreements, we will contribute the assets and entities comprising our animal health business to Spinco. In exchange for the contribution to Spinco of our animal health business, Spinco will issue to Henry Schein shares of common stock, par value \$0.01 per share, of Spinco (the "Spinco Common Stock"). We will subsequently distribute to our stockholders all of the shares of Spinco Common Stock held by us (the "Distribution"). Immediately after the Distribution, HS Merger Sub, Inc., a wholly owned subsidiary of Spinco, will merge with and into DVM, with DVM surviving the merger as a wholly owned subsidiary of Spinco (with such subsidiary to be renamed Vets First Corp.). Upon consummation of these transactions, on a fully-diluted basis, the stockholders of Henry Schein and, if applicable, certain third parties and minority holders of our animal health subsidiaries that are contributed to Spinco in exchange for their interests in these subsidiaries, are expected to own approximately 63% of the outstanding shares of Spinco Common Stock, and the then former stockholders of DVM are expected to own approximately 37% of the outstanding shares of Spinco Common Stock, subject to certain adjustments. Henry Schein will nominate six individuals to the Vets First Corp. Board of Directors and DVM will nominate five individuals to the Vets First Corp. Board of Directors.

Additionally, we expect to receive a cash dividend between \$1.0 billion and \$1.25 billion on a tax-free basis as part of the transaction. We plan to use the proceeds for general corporate purposes, including share repurchases and repayment of indebtedness.



The transaction has been unanimously approved by our Board of Directors and the Board of Directors of DVM. We are working toward closing the transaction by the end of 2018 or early 2019. The transaction is subject to customary closing conditions, including customary regulatory approvals, the receipt of tax opinions from counsel with respect to the transaction and the effectiveness of a registration statement on Form S-1/S-4 to be filed with the Securities and Exchange Commission in connection with the transaction.

#### Stock Repurchases

From June 21, 2004 through September 29, 2018, we repurchased \$2.8 billion, or 57,192,198 shares, under our common stock repurchase programs, with \$85.9 million available as of September 29, 2018 for future common stock share repurchases.

#### Redeemable Noncontrolling Interests

Some minority stockholders in certain of our subsidiaries have the right, at certain times, to require us to acquire their ownership interest in those entities at fair value. Accounting Standards Codification (“ASC”) Topic 480-10 is applicable for noncontrolling interests where we are or may be required to purchase all or a portion of the outstanding interest in a consolidated subsidiary from the noncontrolling interest holder under the terms of a put option contained in contractual agreements. The components of the change in the Redeemable noncontrolling interests for the nine months ended September 29, 2018 and the year ended December 30, 2017 are presented in the following table:

	<b>September 29, December 30,</b>	
	<b>2018</b>	<b>2017</b>
Balance, beginning of period .....	\$ 832,138	\$ 607,636
Decrease in redeemable noncontrolling interests due to		
redemptions .....	(666,363)	(48,669)
Increase in redeemable noncontrolling interests due to		
business acquisitions.....	10,058	78,939
Net income attributable to redeemable noncontrolling interests .....	17,019	52,203
Dividends declared .....	(16,293)	(28,161)
Effect of foreign currency translation gain (loss) attributable to		
redeemable noncontrolling interests .....	(13,752)	7,461
Change in fair value of redeemable securities .....	119,695	162,729
Balance, end of period .....	<u>\$ 282,502</u>	<u>\$ 832,138</u>

Changes in the estimated redemption amounts of the noncontrolling interests subject to put options are adjusted at each reporting period with a corresponding adjustment to Additional paid-in capital. Future reductions in the carrying amounts are subject to a floor amount that is equal to the fair value of the redeemable noncontrolling interests at the time they were originally recorded. The recorded value of the redeemable noncontrolling interests cannot go below the floor level. These adjustments do not impact the calculation of earnings per share.

Additionally, some prior owners of such acquired subsidiaries are eligible to receive additional purchase price cash consideration if certain financial targets are met. Any adjustments to these accrual amounts are recorded in our consolidated statement of income. For nine months ended September 29, 2018 and September 30, 2017, there were no material adjustments recorded in our consolidated statement of income relating to changes in estimated contingent purchase price liabilities.



## Critical Accounting Policies and Estimates

There have been no material changes in our critical accounting policies and estimates from those disclosed in Item 7 of our Annual Report on Form 10-K for the year ended December 30, 2017 (the "2017 Form 10-K"), except as follows:

### *Revenue Recognition*

On December 31, 2017, we adopted Accounting Standard Update ("ASU") No. 2014-09, "Revenue from Contracts with Customers", ASC 606 ("Topic 606") using the modified retrospective method applied to those contracts which were not completed as of the adoption date. Results for reporting periods beginning after December 30, 2017 are presented under Topic 606, while prior period amounts are not adjusted and continue to be reported under the accounting standards in effect for those periods. Our revenue recognition accounting policies applied prior to adoption of Topic 606 are outlined in the financial statements in the 2017 Form 10-K. The disclosures included herein reflect our accounting policies under Topic 606.

We generate revenue from the sale of dental, animal health and medical consumable products, as well as equipment, software products and services and other sources. Provisions for discounts, rebates to customers, customer returns and other contra revenue adjustments are included in the transaction price at contract inception by estimating the most likely amount based upon historical data and estimates and are provided for in the period in which the related sales are recognized.

Revenue derived from the sale of consumable products is recognized at a point in time when control transfers to the customer. Such sales typically entail high-volume, low-dollar orders shipped using third-party common carriers. We believe that the shipment date is the most appropriate point in time indicating control has transferred to the customer because we have no post-shipment obligations and this is when legal title and risks and rewards of ownership transfer to the customer and the point at which we have an enforceable right to payment.

Revenue derived from the sale of equipment is recognized when control transfers to the customer. This occurs when the equipment is delivered. Such sales typically entail scheduled deliveries of large equipment primarily by equipment service technicians. Some equipment sales require minimal installation, which is typically our product generally carries standard warranty terms provided by the manufacturer, however, in instances where we provide warranty labor services, the warranty costs are accrued in accordance with ASC 460 "Guarantees".

Revenue derived from the sale of software products is recognized when products are shipped to customers or made available electronically. Such software is generally installed by customers and does not require extensive training due to the nature of its design. Revenue derived from post-contract customer support for software, including annual support and/or training, is generally recognized over time using time elapsed as the input method that best depicts the transfer of control to the customer.

Revenue derived from other sources, including freight charges, equipment repairs and financial services, is recognized when the related product revenue is recognized or when the services are provided. We apply the practical expedient to treat shipping and handling activities performed after the customer obtains control as fulfillment activities, rather than a separate performance obligation in the contract.

Sales, value-add and other taxes we collect concurrent with revenue-producing activities are excluded from revenue.

Certain of our revenue is derived from bundled arrangements that include multiple distinct performance obligations which are accounted for separately. When we sell software products together with related services (i.e., training and technical support), we allocate revenue to software using the residual method, using an estimate of the standalone selling price to estimate the fair value of the undelivered elements. There are no cases



where revenue is deferred due to a lack of a standalone selling price. Bundled arrangements that include elements that are not considered software consist primarily of equipment and the related installation service. We allocate revenue for such arrangements based on the relative selling prices of the goods or services. If an observable selling price is not available (i.e., we do not sell the goods or services separately), we use one of the following techniques to estimate the standalone selling price: adjusted market approach; cost-plus approach; or the residual method. There is no specific hierarchy for the use of these methods, but the estimated selling price reflects our best estimate of what the selling prices of each deliverable would be if it were sold regularly on a standalone basis taking into consideration the cost structure of our business, technical skill required, customer location and other market conditions.

#### *Accounts Receivable*

The carrying amount of accounts receivable is reduced by a valuation allowance that reflects our best estimate of the amounts that will not be collected. In addition to reviewing delinquent accounts receivable, we consider many factors in estimating our reserve, including historical data, experience, customer types, credit worthiness and economic trends. From time to time, we adjust our assumptions for anticipated changes in any of these or other factors expected to affect collectability.

#### *Contract Assets*

Contract assets include amounts related to any conditional right to consideration for work completed but not billed as of the reporting date and generally represent amounts owed to us by customers, but not yet billed. Contract assets are transferred to accounts receivable when the right becomes unconditional. Current contract assets are included in Prepaid expenses and other and the non-current contract assets are included in Investments and other within our consolidated balance sheet.

#### *Contract Liabilities*

Contract liabilities are comprised of advance payments and deferred revenue amounts. Contract liabilities are transferred to revenue once the performance obligation has been satisfied. Current contract liabilities are included in Accrued expenses: Other and the non-current contract liabilities are included in Other liabilities within our consolidated balance sheet.

#### *Deferred Commissions*

Sales commissions earned by our sales force that relate to long term arrangements are capitalized as costs to obtain a contract when the costs incurred are incremental and are expected to be recovered. Deferred sales commissions are amortized over the estimated customer relationship period. We apply the practical expedient related to the capitalization of incremental costs of obtaining a contract, and recognize such costs as an expense when incurred if the amortization period of the assets that we would have recognized is one year or less.

#### *Sales Returns*

Sales returns are recognized as a reduction of revenue by the amount of expected returns and are recorded as refund liability within current liabilities. We estimate the amount of revenue expected to be reversed to calculate the sales return liability based on historical data for specific products, adjusted as necessary for new products. The allowance for returns is presented gross as a refund liability and we record an inventory asset (and a corresponding adjustment to cost of sales) for any goods or services that we expect to be returned.



## Accounting Pronouncements Adopted

In May 2014, the Financial Accounting Standards Board (“FASB”) issued Topic 606. We adopted the provisions of this standard as of December 31, 2017, on a modified retrospective basis. We applied the requirements of the new standard only to contracts that were not completed as of the adoption date. We recorded an immaterial adjustment to the opening balance of retained earnings for the adoption of Topic 606. The comparative information has not been restated and continues to be reported under the accounting standards in effect for those periods.

The impact of the new standard on our consolidated statements of income, which we expect to be immaterial on an ongoing basis, is primarily related to software sales and sales commissions and is described as follows:

### *Software Sales*

For software licenses sold together with post contract support (PCS), we previously deferred software revenue if it did not have vendor-specific evidence of fair value of the PCS. Under Topic 606, the concept of vendor-specific objective evidence is eliminated and there are no cases where revenue is deferred due to a lack of standalone selling price. In addition, we previously recognized revenue from term licenses ratably over the contract term. Under Topic 606, such licenses represent a right to use intellectual property and therefore require upfront recognition. Furthermore, certain upfront fees related to service arrangements were previously deferred and recognized over the estimated customer life. Under Topic 606, the period over which we will recognize these fees is reduced, as the upfront fee represents additional contract price which will be allocated to the performance obligations in the contract and recognized as those performance obligations are satisfied, rather than being amortized over the estimated customer life. Based on the aforementioned changes, such software revenue will be recognized sooner than under the previous revenue recognition standard.

### *Sales Commissions*

We previously recognized sales commissions as an expense when incurred. Under Topic 606, we defer such sales commissions as costs to obtain a contract when the costs are incremental and expected to be recovered. Deferred sales commissions are amortized over the estimated customer relationship period. We apply the practical expedient to expense, as incurred, commissions with an expected amortization period of one year or less.

In October 2016, the FASB issued ASU No. 2016-16, “Income Taxes, Intra-Entity Transfers of Assets Other Than Inventory” (“Topic 740”). Topic 740 requires companies to recognize the income tax effects of intercompany sales and transfers of assets other than inventory in the period which the transfer occurs. Previously, companies were required to defer the income tax effects on intercompany transfer of assets until the asset has been sold to an outside party. On December 31, 2017, we adopted the guidance, which is effective for annual periods and related interim periods beginning after December 15, 2017 on a modified retrospective basis. As a result of the adoption of Topic 740, we have recorded an immaterial adjustment to the opening balance of retained earnings and a reduction to prepaid assets.

In May 2017, the FASB issued ASU No. 2017-09, “Compensation-Stock Compensation, Scope of Modification Accounting” (“Topic 718”). Topic 718 provides guidance on determining which changes to the terms and conditions of share-based payment awards require an entity to apply modification accounting. Topic 718 requires modification accounting if the fair value, vesting conditions, or equity or liability classification of the award is not the same immediately before and after a change to the terms and conditions of the award. Topic 718 was adopted on a prospective basis as of December 31, 2017 and did not have a material impact on the consolidated financial statements or disclosures as of September 29, 2018.



## Recently Issued Accounting Standards

In February 2016, the FASB issued ASU No. 2016-02, "Leases" (Topic 842) ("ASU 2016-02"), which will require lessees to recognize assets and liabilities for leases with lease terms of more than 12 months. Consistent with current accounting principles generally accepted in the United States ("U.S. GAAP"), the recognition, measurement, and presentation of expenses and cash flows arising from a lease by a lessee primarily will depend on its classification as a finance or operating lease. However, unlike current U.S. GAAP, which requires only capital leases to be recognized on the balance sheet, the new guidance will require both types of leases to be recognized on the balance sheet. The ASU is effective for interim and annual periods beginning after December 15, 2018, with early adoption permitted. In August 2018, the FASB issued ASU No. 2018-11, "Leases (Topic 842): Targeted Improvements" which permits adoption of the guidance in ASU 2016-02 using either a modified retrospective transition, requiring application at the beginning of the earliest comparative period presented or a transition method whereby companies could continue to apply existing lease guidance during the comparative periods and apply the new lease requirements through a cumulative-effect adjustment in the period of adoption rather than in the earliest period presented without adjusting historical financial statements. We expect to adopt the ASU on December 30, 2018, and we are currently evaluating the effects that the adoption of ASU 2016-02 will have on our consolidated financial statements, but anticipate that the new guidance will significantly impact our consolidated balance sheet given our considerable lease obligations. We are implementing a new lease accounting system and updating our processes in preparation for the adoption of the new standard.

In June 2016, the FASB issued ASU No. 2016-13, "Financial Instruments-Credit Losses (Topic 326): Measurement of Credit Losses on Financial Instruments" which requires the measurement and recognition of expected credit losses for financial assets held at amortized cost. This ASU is effective for interim and annual reporting periods beginning after December 15, 2019, with early adoption permitted for interim and annual reporting periods beginning after December 15, 2018. This ASU is required to be adopted using the modified retrospective basis, with a cumulative-effect adjustment to retained earnings as of the beginning of the first reporting period in which the guidance of this ASU is effective. Based upon the level and makeup of our financial asset portfolio, past loan loss activity and current known activity regarding our outstanding loans, we do not expect that this ASU will have a material impact on our consolidated financial statements.

In January 2017, the FASB issued ASU No. 2017-04, "Intangibles-Goodwill and Other" (Topic 350) ("ASU 2017-04"). ASU 2017-04 eliminates step two from the goodwill impairment test, thereby eliminating the requirement to calculate the implied fair value of a reporting unit. ASU 2017-04 will require us to perform our annual goodwill impairment test by comparing the fair value of our reporting units to the carrying value of those units. If the carrying value exceeds the fair value, we will be required to recognize an impairment charge; however, the impairment charge should not exceed the amount of goodwill allocated to such reporting unit. ASU 2017-04 is required to be implemented on a prospective basis for fiscal years beginning after December 15, 2019. We do not expect that the requirements of ASU 2017-04 will have a material impact on our consolidated financial statements.

In August 2017, the FASB issued ASU No. 2017-12, "Derivatives and Hedging" (Topic 815) ("ASU 2017-12"), which simplifies the requirements for hedge accounting, more closely aligns hedge accounting with risk management activities and increases transparency of the scope and results of hedging activities. This ASU amends the presentation and disclosure requirements and changes how we can assess the effectiveness of our hedging relationships. This ASU will make more financial and nonfinancial hedging strategies eligible for hedge accounting. ASU 2017-12 is required to be implemented for fiscal years beginning after December 15, 2018 and interim periods within those fiscal years. Early adoption of ASU 2017-12 is permitted in any interim period after the issuance of this ASU. We do not expect that the requirements of ASU 2017-12 will have a material impact on our consolidated financial statements.



In February 2018, the FASB issued ASU No. 2018-02, "Treatment of Stranded Tax Effects in Accumulated Other Comprehensive Income Resulting From the Tax Cuts and Jobs Act of 2017 " which allows the reclassification from accumulated comprehensive income to retained earnings the income tax effects resulting from the Tax Act. This ASU is effective for interim and annual reporting periods beginning after December 15, 2018, with early adoption permitted in any interim period after the issuance of this ASU. We do not expect that the requirements of ASU 2018-02 will have a material impact on our consolidated financial statements.

In June 2018, the FASB issued ASU No. 2018-07, "Compensation - Stock Compensation (Topic 718): Improvements to Nonemployee Share-Based Payment Accounting" ("ASU 2018-07"), which expands the scope of Topic 718 to include share-based payment transactions for acquiring goods and services from nonemployees. ASU 2018-07 simplifies the accounting for share-based payments to nonemployees by aligning it with the accounting for share-based payments to employees. ASU 2018-07 is effective for public business entities for fiscal years beginning after December 15, 2018, including interim periods within that fiscal year. Early adoption is permitted. We do not expect that the requirements of ASU-2018-07 will have a material impact on our consolidated financial statements.

In August 2018, the FASB issued ASU No. 2018-15, "Intangibles – Goodwill and Other-Internal-Use Software (Subtopic 350-40): Customer's Accounting for Implementation Costs Incurred in a Cloud Computing Arrangement That Is a Service Contract" ("ASU 2018-15"), which aligns the requirements for capitalizing implementation costs incurred in a hosting arrangement that is a service contract with the requirements for capitalizing implementation costs incurred to develop or obtain internal-use software (and hosting arrangements that include an internal use software license). The accounting for the service element of a hosting arrangement that is a service contract is not affected by the amendments in this ASU. ASU 2018-15 is effective for public business entities for fiscal years beginning after December 15, 2019, including interim periods within those fiscal years. Early adoption is permitted. We do not expect that the requirements of this ASU will have a material impact on our consolidated financial statements.

### **ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK**

There have been no material changes in our exposure to market risk from that disclosed in Item 7A of our Annual Report on Form 10-K for the year ended December 30, 2017.



## ITEM 4. CONTROLS AND PROCEDURES

### *Evaluation of Disclosure Controls and Procedures*

Under the supervision and with the participation of management, including our principal executive officer and principal financial officer, we evaluated the effectiveness of the design and operation of our disclosure controls and procedures as of the end of the period covered by this quarterly report as such term is defined in Rules 13a-15(e) and 15d-15(e) promulgated under the Securities Exchange Act of 1934, as amended (the "Exchange Act"). Based on this evaluation, our management, including our principal executive officer and principal financial officer, concluded that our disclosure controls and procedures were effective as of September 29, 2018 to ensure that all material information required to be disclosed by us in reports that we file or submit under the Exchange Act is accumulated and communicated to them as appropriate to allow timely decisions regarding required disclosure and that all such information is recorded, processed, summarized and reported within the time periods specified in the SEC's rules and forms.

### *Changes in Internal Control over Financial Reporting*

The combination of acquisitions, continued acquisition integrations and systems implementations undertaken during the quarter and carried over from prior quarters, when considered in the aggregate, represents a material change in our internal control over financial reporting.

During the quarter ended September 29, 2018, we completed the acquisition of a technology business and a dental business in North America with approximate aggregate annual revenues of \$122 million. In addition, post-acquisition integration related activities continued for our global dental and animal health businesses acquired during prior quarters, representing aggregate annual revenues of approximately \$253 million. These acquisitions, the majority of which utilize separate information and financial accounting systems, have been included in our consolidated financial statements since their respective dates of acquisition.

Also, during the quarter ended September 29, 2018, post-implementation systems improvement activities continued for a new equipment system implemented during prior quarters for our U.S. dental business equipment centers representing approximate aggregate annual revenues of \$341 million and for the upgrade of an ERP system at an animal health business in Switzerland having approximate aggregate annual revenues of \$49 million.

All acquisition integrations and systems implementations involved necessary and appropriate change-management controls that are considered in our annual assessment of the design and operating effectiveness of our internal control over financial reporting.

### *Limitations of the Effectiveness of Internal Control*

A control system, no matter how well conceived and operated, can provide only reasonable, not absolute, assurance that the objectives of the internal control system are met. Because of the inherent limitations of any internal control system, no evaluation of controls can provide absolute assurance that all control issues, if any, within a company have been detected.



## PART II. OTHER INFORMATION

### ITEM 1. LEGAL PROCEEDINGS

Beginning in January 2016, purported class action complaints were filed against Patterson Companies, Inc. (“Patterson”), Benco Dental Supply Co. (“Benco”) and Henry Schein, Inc. Although there were factual and legal variations among these complaints, each of these complaints alleges, among other things, that defendants conspired to fix prices, allocate customers and foreclose competitors by boycotting manufacturers, state dental associations and others that deal with defendants’ competitors. On February 9, 2016, the U.S. District Court for the Eastern District of New York ordered all of these actions, and all other actions filed thereafter asserting substantially similar claims against defendants, consolidated for pre-trial purposes. On February 26, 2016, a consolidated class action complaint was filed by Arnell Prato, D.D.S., P.L.L.C., d/b/a Down to Earth Dental, Evolution Dental Sciences, LLC, Howard M. May, DDS, P.C., Casey Nelson, D.D.S., Jim Peck, D.D.S., Bernard W. Kurek, D.M.D., Larchmont Dental Associates, P.C., and Keith Schwartz, D.M.D., P.A. (collectively, “putative class representatives”) in the U.S. District Court for the Eastern District of New York, entitled *In re Dental Supplies Antitrust Litigation*, Civil Action No. 1:16-CV-00696-BMC-GRB. In the consolidated class action complaint, putative class representatives allege a nationwide agreement among Henry Schein, Benco, Patterson and non-party Burkhart Dental Supply Company, Inc. (“Burkhart”) not to compete on price. The consolidated class action complaint asserts a single count under Section 1 of the Sherman Act, and seeks equitable relief, compensatory and treble damages, jointly and severally, and reasonable costs and expenses, including attorneys’ fees and expert fees. On February 22, 2018, plaintiffs moved to certify a class that, subject to certain exclusions, includes all private dental practices and laboratories that purchased dental supplies directly from Henry Schein, Patterson, Benco, Burkhart or any combination thereof, during the period beginning January 1, 2009 until March 31, 2016. On September 28, 2018, the parties executed a settlement agreement that proposes a full and final settlement of the lawsuit on a classwide basis, subject to court approval. As a result, we recorded a charge of \$38.5 million in our third quarter 2018 results.

On August 31, 2012, Archer and White Sales, Inc. (“Archer”) filed a complaint against Henry Schein, Inc. as well as Danaher Corporation and its subsidiaries Instrumentarium Dental, Inc., Dental Equipment, LLC, Kavio Dental Technologies, LLC and Dental Imaging Technologies Corporation (collectively, the “Danaher Defendants”) in the U.S. District Court for the Eastern District of Texas, Civil Action No. 2:12-CV-00572-JRG, styled as an antitrust action under Section 1 of the Sherman Act, and the Texas Free Enterprise Antitrust Act. Archer alleges a conspiracy between Henry Schein, an unnamed company and the Danaher Defendants to terminate or limit Archer’s distribution rights. On August 1, 2017, Archer filed an amended complaint, adding Patterson and Benco as defendants, and alleging that Henry Schein, Patterson, Benco and Burkhart conspired to fix prices and refused to compete with each other for sales of dental equipment to dental professionals and agreed to enlist their common suppliers, the Danaher Defendants, to join a price-fixing conspiracy and boycott by reducing the distribution territory of, and eventually terminating, their price-cutting competing distributor Archer. Archer seeks damages in an amount to be proved at trial, to be trebled with interest and costs, including attorneys’ fees, jointly and severally, as well as injunctive relief. On October 30, 2017, Archer filed a second amended complaint, to add additional allegations that it believes support its claims. The named parties and causes of action are the same as the August 1, 2017 amended complaint.

On October 1, 2012, we filed a motion for an order: (i) compelling Archer to arbitrate its claims against us; (2) staying all proceedings pending arbitration; and (3) joining the Danaher Defendants’ motion to arbitrate and stay. On May 28, 2013, the Magistrate Judge granted the motions to arbitrate and stayed proceedings pending arbitration. On June 10, 2013, Archer moved for reconsideration before the District Court judge. On December 7, 2016, the District Court Judge granted Archer’s motion for reconsideration and lifted the stay. Defendants appealed the District Court’s order. On December 21, 2017, the U.S. Court of Appeals for the Fifth Circuit affirmed the District Court’s order denying the motions to compel arbitration. On February 12, 2018, defendants filed an Application for Stay of Proceedings in the District Court in the Supreme Court of the United States, seeking to stay proceedings in the District Court pending a decision on defendants’ forthcoming petition for writ of certiorari. On March 2, 2018, the Supreme Court of the United States granted a stay of proceedings. On June 25, 2018, the Supreme Court of the United States granted defendants’ petition for writ of certiorari, pursuant to which it will review the lower court’s decision affirming the District Court’s decision denying our motion to compel



arbitration. On October 29, 2018, the Supreme Court heard oral argument. The Supreme Court's decision is pending. We intend to defend ourselves vigorously against this action.

On August 17, 2017, IQ Dental Supply, Inc. ("IQ Dental") filed a complaint in the U.S. District Court for the Eastern District of New York, entitled IQ Dental Supply, Inc. v. Henry Schein, Inc., Patterson Companies, Inc. and Benco Dental Supply Company, Case No. 2:17-cv-4834. Plaintiff alleges that it is a distributor of dental supplies and equipment, and sells dental products through an online dental distribution platform operated by SourceOne Dental ("SourceOne"). SourceOne had previously brought an antitrust lawsuit against Henry Schein, Patterson and Benco, which Henry Schein settled in the second quarter of 2017 and which is described in our prior filings with the SEC.

IQ Dental alleges, among other things, that defendants conspired to suppress competition from IQ Dental and SourceOne for the marketing, distribution and sale of dental supplies and equipment in the United States, and that defendants unlawfully agreed with one another to boycott dentists, manufacturers and state dental associations that deal with, or considered dealing with, plaintiff and SourceOne. Plaintiff claims that this alleged conduct constitutes unreasonable restraint of trade in violation of Section 1 of the Sherman Act, New York's Donnelly Act and the New Jersey Antitrust Act, and also makes pendant state law claims for tortious interference with prospective business relations, civil conspiracy and aiding and abetting. Plaintiff seeks injunctive relief, compensatory, treble and punitive damages, jointly and severally, and reasonable costs and expenses, including attorneys' fees and expert fees. On December 21, 2017, the District Court granted the defendants' motion to dismiss. On January 19, 2018, IQ Dental appealed the District Court's order. The U.S. Court of Appeals for the Second Circuit heard oral argument on the appeal on September 13, 2018. The court's decision is pending. We intend to defend ourselves vigorously against this action.

On February 12, 2018, the United States Federal Trade Commission ("FTC") filed a complaint against Benco Dental Supply Co., Henry Schein, Inc. and Patterson Companies, Inc. The FTC alleges, among other things, that defendants violated U.S. antitrust laws by conspiring, and entering into an agreement, to refuse to provide discounts to or otherwise serve buying groups representing dental practitioners. The FTC alleges that defendants conspired in violation of Section 5 of the FTC Act. The complaint seeks equitable relief only and does not seek monetary damages. We deny the allegation that we conspired to refuse to provide discounts to or otherwise serve dental buying groups and intend to defend ourselves vigorously against this action. A hearing before an administrative law judge began on October 16, 2018 and is ongoing. We believe this matter will not have a material adverse effect on our consolidated financial position, liquidity or results of operations.

On March 7, 2018, Joseph Salkowitz, individually and on behalf of all others similarly situated, filed a putative class action complaint for violation of the federal securities laws against Henry Schein, Inc., Stanley M. Bergman and Steven Paladino in the U.S. District Court for the Eastern District of New York, Case No. 1:18-cv-01428. The complaint sought to certify a class consisting of all persons and entities who, subject to certain exclusions, purchased Henry Schein securities from March 7, 2013 through February 12, 2018 (the "Class Period"). The complaint alleged, among other things, that the defendants had made materially false and misleading statements about Henry Schein's business, operations and prospects during the Class Period, including matters relating to the issues in the antitrust class action and the FTC action described above, thereby causing the plaintiff and members of the purported class to pay artificially inflated prices for Henry Schein securities. The complaint sought unspecified monetary damages and a jury trial. Pursuant to the provisions of the Private Securities Litigation Reform Act of 1995 (the "PSLRA"), the court appointed lead plaintiff and lead counsel on June 22, 2018 and recaptioned the putative class action as In re Henry Schein, Inc. Securities Litigation, under the same case number. Lead plaintiff filed a consolidated class action complaint on September 14, 2018. The consolidated class action complaint asserts similar claims against the same defendants (plus Timothy Sullivan) on behalf of the same putative class of purchasers during the Class Period. It alleges that Henry Schein's stock price was inflated during that period because Henry Schein had misleadingly portrayed its dental-distribution business "as successfully producing excellent profits while operating in a highly competitive environment" even though, "in reality, [Henry Schein] had engaged for years in collusive and anticompetitive practices in order to maintain Schein's margins, profits, and market share." The complaint alleges that the stock price started to fall from August 8, 2017, when the company announced below-expected financial performance that allegedly "revealed that Schein's poor results were a product



of abandoning prior attempts to inflate sales volume and margins through anticompetitive collusion,” through February 13, 2018, after the FTC filed a complaint against Benco, Henry Schein and Patterson alleging that they violated U.S. antitrust laws. The complaint alleges violations of Section 10(b) of the Exchange Act and Rule 10b-5 and Section 20(a) of the Exchange Act. We intend to defend ourselves vigorously against this action. Henry Schein has also received a request under 8 Del. C. § 220 to inspect corporate books and records relating to the issues raised in the securities class action and the antitrust matters discussed above.

On May 3, 2018, a class action complaint, Marion Diagnostic Center, LLC, et al. v. Becton, Dickinson, and Co., et al., Case No. 3:18-cv-010509 (S.D. Ill), was filed in the U.S. District Court for the Southern District of Illinois against Becton, Dickinson, and Co. (“Becton”); Premier, Inc. (“Premier”), Vizient, Inc. (“Vizient”), Cardinal Health, Inc. (“Cardinal”), Owens & Minor Inc. (“O&M”), Henry Schein, Inc., and Unnamed Becton Distributor Co-Conspirators. The complaint alleges that the defendants entered into a vertical conspiracy to force healthcare providers into long-term exclusivity contracts that restrain trade in the nationwide markets for conventional and safety syringes and safety IV catheters and inflate the prices of certain Becton products to above-competitive levels. The named plaintiffs seek to represent three separate classes consisting of all healthcare providers that purchased (i) Becton’s conventional syringes, (ii) Becton’s safety syringes, or (iii) Becton’s safety catheters directly from Becton, Premier, Vizient, Cardinal, O&M or Henry Schein on or after May 3, 2014. The complaint asserts a single count under Section 1 of the Sherman Act, and seeks equitable relief, treble damages, reasonable attorneys’ fees and costs and expenses, and pre-judgment and post-judgment interest. On June 15, 2018, an amended complaint was filed asserting the same allegations against the same parties and adding McKesson Medical-Surgical, Inc. as an additional defendant. We intend to defend ourselves vigorously against this action.

On May 29, 2018, an amended complaint was filed in the MultiDistrict Litigation (MDL) proceeding In Re National Prescription Opiate Litigation (MDL No. 2804; Case No. 17-md-2804) in an action entitled The County of Summit, Ohio et al. v. Purdue Pharma, L.P., et al., Civil Action No. 1:18-op-45090-DAP, in the U.S. District Court for the Northern District of Ohio, adding Henry Schein, Inc., Henry Schein Medical Systems, Inc. and others as defendants. Plaintiffs allege that manufacturers of prescription opioid drugs engaged in a false advertising campaign to expand the market for such drugs and their own market share and that the entities in the supply chain (including Henry Schein, Inc. and Henry Schein Medical Systems, Inc.) reaped financial rewards by refusing or otherwise failing to monitor appropriately and restrict the improper distribution of those drugs. Plaintiffs assert the following claims for relief against Henry Schein, Inc. and Henry Schein Medical Systems, Inc.: statutory public nuisance; common law absolute public nuisance; negligence; injury through criminal acts (R.C. 2307.60); unjust enrichment; and civil conspiracy. This case has been designated “Track 1” and is currently set for trial on September 3, 2019. We intend to defend ourselves vigorously against this action.

On July 3, 2018, the City of Barberton, Ohio (and related entities) filed a complaint in the same MDL proceeding (MDL No. 2804; Case No. 17-md-2804) in an action entitled City of Barberton, et al. v. Purdue Pharma, L.P., et al., Civil Action No. 1:18-op-45767-DAP, in the Northern District of Ohio, against Henry Schein, Inc., Henry Schein Medical Systems, Inc. and others, that is similar to The County of Summit complaint. This case has been designated “Track 2” and is currently stayed. On September 20, 2018, Southeast Alaska Regional Health Consortium filed a complaint entitled Southeast Alaska Regional Health Consortium v. Purdue Pharma L.P., et al., Case No. 3:18-cv-00217-TMB, in the U.S. District Court for the District of Alaska, against Henry Schein, Inc., Henry Schein Medical Systems, Inc. and others. That case was transferred to the MDL proceeding referenced above (MDL Civil Action No. 1:17-md-02804; Case No. 1:18-op-46149), designated a “Track 2” case and is currently stayed. On September 20, 2018, Tucson Medical Center filed a complaint entitled Tucson Medical Center v. Purdue Pharma L.P., et al., Case No. C20184213, in the Superior Court of Arizona, County of Pima, against Henry Schein, Inc. and others. On September 27, 2018, Defendants removed that case to the U.S. District Court for the District of Arizona (Case No. 4:18-cv-00481-RCC). On October 8, 2018, Tucson Medical Center voluntarily dismissed the lawsuit pending in the District of Arizona without prejudice. On October 9, 2018, Tucson Medical Center refiled the lawsuit in the Superior Court of Arizona, County of Pima (Case No. C20184991). On October 29, 2018, defendants removed the case to the U.S. District Court for the District of Arizona (Case No. CV-18-00532). Sales of opioids in North America last year were less than 1% of all North American sales. We intend to defend ourselves vigorously against these actions.



On October 9, 2018, a purported class action complaint entitled *Kramer v. Henry Schein, Inc., Patterson Co., Inc., Benco Dental Supply Co., and Unnamed Co-Conspirators*, was filed in the U.S. District Court for the Northern District of California. The complaint alleges that members of the proposed class, comprised of purchasers of dental services from dental practices in California, suffered antitrust injury due to an unlawful boycott, price-fixing or otherwise anticompetitive conspiracy among Henry Schein, Patterson and Benco. The complaint alleges that the alleged conspiracy overcharged California dental practices, orthodontic practices and dental laboratories on their purchase of dental supplies, which in turn passed on some or all of such overcharges to members of the California class purchasing dental services. Subject to certain exclusions, the complaint defines the class as “all persons residing in California purchasing and/or reimbursing for dental services from California dental practices on or after August 31, 2012.” The complaint alleges violations of California antitrust laws, including the Cartwright Act (Cal. Bus. and Prof. Code § 16720) and the Unfair Competition Act (Cal. Bus. and Prof. Code § 17200), and seeks a permanent injunction, actual damages to be determined at trial, trebled, reasonable attorneys’ fees and costs, and pre- and post-judgment interest. We intend to defend ourselves vigorously against this action.

From time to time, we may become a party to other legal proceedings, including, without limitation, product liability claims, employment matters, commercial disputes, governmental inquiries and investigations (which may in some cases involve our entering into settlement arrangements or consent decrees), and other matters arising out of the ordinary course of our business. While the results of any legal proceeding cannot be predicted with certainty, in our opinion none of these other pending matters are currently anticipated to have a material adverse effect on our consolidated financial position, liquidity or results of operations.

As of September 29, 2018, we had accrued our best estimate of potential losses relating to claims that were probable to result in liability and for which we were able to reasonably estimate a loss. This accrued amount, as well as related expenses, was not material to our financial position, results of operations or cash flows. Our method for determining estimated losses considers currently available facts, presently enacted laws and regulations and other factors, including probable recoveries from third parties.



## ITEM 1A. RISK FACTORS

There have been no material changes from the risk factors disclosed in Part 1, Item 1A, of our Annual Report on Form 10-K for the year ended December 30, 2017.

## ITEM 2. UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS

### *Purchases of equity securities by the issuer*

Our share repurchase program, announced on June 21, 2004, originally allowed us to repurchase up to \$100 million of shares of our common stock, which represented approximately 3.5% of the shares outstanding at the commencement of the program. As summarized in the table below, subsequent additional increases totaling \$2.8 billion, authorized by our Board of Directors, to the repurchase program provide for a total of \$2.9 billion of shares of our common stock to be repurchased under this program.

	<b>Date of Authorization</b>	<b>Amount of Additional Repurchases Authorized</b>
	October 31, 2005	\$ 100,000,000
	March 28, 2007	100,000,000
	November 16, 2010	100,000,000
	August 18, 2011	200,000,000
	April 18, 2012	200,000,000
	November 12, 2012	300,000,000
	December 9, 2013	300,000,000
	December 4, 2014	300,000,000
	November 30, 2015	400,000,000
	October 18, 2016	400,000,000
	September 15, 2017	400,000,000

As of September 29, 2018, we had repurchased approximately \$2.8 billion of common stock (57,192,198 shares) under these initiatives, with \$85.9 million available for future common stock share repurchases.

The following table summarizes repurchases of our common stock under our stock repurchase program during the fiscal quarter ended September 29, 2018:

<b>Fiscal Month</b>	<b>Total Number of Shares Purchased (1)</b>	<b>Average Price Paid Per Share</b>	<b>Total Number of Shares Purchased as Part of Our Publicly Announced Program</b>	<b>Maximum Number of Shares that May Yet Be Purchased Under Our Program (2)</b>
07/01/18 through 08/04/18	145,273	\$ 74.01	145,273	1,693,799
08/05/18 through 09/01/18	-	-	-	1,749,401
09/02/18 through 09/29/18	631,655	79.16	631,655	1,010,157
	<u>776,928</u>		<u>776,928</u>	

(1) All repurchases were executed in the open market under our existing publicly announced authorized program.

(2) The maximum number of shares that may yet be purchased under this program is determined at the end of each month based on the closing price of our common stock at that time.



**ITEM 6. EXHIBITS**

Exhibits.

<a href="#"><u>10.1</u></a>	<a href="#"><u>Letter Agreement, dated as of September 14, 2018, by and among Henry Schein, Inc., HS Spincio, Inc., HS Merger Sub, Inc., Direct Vet Marketing, Inc. and Shareholder Representative Services LLC+</u></a>
<a href="#"><u>31.1</u></a>	<a href="#"><u>Certification Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.+</u></a>
<a href="#"><u>31.2</u></a>	<a href="#"><u>Certification Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.+</u></a>
<a href="#"><u>32.1</u></a>	<a href="#"><u>Certification Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.+</u></a>
101.INS	XBRL Instance Document+
101.SCH	XBRL Taxonomy Extension Schema Document+
101.CAL	XBRL Taxonomy Extension Calculation Linkbase Document+
101.DEF	XBRL Taxonomy Definition Linkbase Document+
101.LAB	XBRL Taxonomy Extension Label Linkbase Document+
101.PRE	XBRL Taxonomy Extension Presentation Linkbase Document+

+ Filed herewith.

**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.

Henry Schein, Inc.  
(Registrant)

By: /s/ Steven Paladino  
Steven Paladino  
Executive Vice President and  
Chief Financial Officer  
(Authorized Signatory and Principal Financial  
and Accounting Officer)

Dated: November 6, 2018

September 14, 2018

Direct Vet Marketing, Inc.  
(d/b/a Vets First Choice)  
7 Custom House Street, Suite 2  
Portland, ME 04101  
Attn: General Counsel (voyagerlegal@vetsfirstchoice.com)

With copy to:

Morgan, Lewis & Bockius LLP  
One Federal Street  
Boston, MA 02110-1726  
Attn: Mark Stein (mark.stein@morganlewis.com)

Re: Amendment No. 1 to Contribution and Distribution Agreement and Amendment No. 1 to Merger Agreement

Dear Sir and/or Madame:

Reference is made to (i) that certain Agreement and Plan of Merger, dated as of April 20, 2018 (the "Merger Agreement"), by and among Henry Schein, Inc. ("Henry Schein"), HS Spingo, Inc. ("Spingo"), HS Merger Sub, Inc., Direct Vet Marketing, Inc. ("Voyager"), and Shareholder Representative Services, LLC, solely in its capacity as the Voyager Stockholders' Representative (the "Voyager Stockholders' Representative"), and (ii) that certain Contribution and Distribution Agreement, dated as of April 20, 2018 (the "CDA"), by and among Henry Schein, Spingo, Voyager and, solely for purposes of certain articles thereto, the Voyager Stockholders' Representative. For purposes of this letter agreement (this "Letter"), capitalized terms used but not otherwise defined in this Letter shall have the meaning ascribed to them in the Merger Agreement or in the CDA, as applicable.

This Letter shall amend each of the Merger Agreement and the Contribution and Distribution Agreement in the manner and to the extent set forth below, and shall constitute Amendment No. 1 to the Merger Agreement and Amendment No. 1 to the CDA for such purposes.

In consideration of the premises and mutual agreements and covenants contained herein and other good and valuable consideration, the receipt and sufficiency of which is hereby acknowledged, and intending to be legally bound, the parties to this Letter agree as follows:

- I. To amend the CDA as follows:
  - a. The definition of "Spingo Target Working Capital" in Article I (*Definitions*) Section 1.1 (*General*) is amended and restated to read as follows:
    - i. "Spingo Target Working Capital" means the sum of (1) \$598,000,000 plus (2) the amount payable to Henry Schein pursuant to Section 2.13(a) hereof.
  - b. The definition of "Spingo Closing Date Net Debt" in Article I (*Definitions*) Section 1.1 (*General*) is amended and restated to read as follows:

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“Spinco Closing Date Net Debt” means an amount (which may be negative), in each case, determined as of the Calculation Time and without giving effect to the consummation of the Transactions, equal to (i) the Indebtedness of the Spinco Group, less (ii) an amount equal to the Cash and Cash Equivalents of the Spinco Group; provided, that, as used within the definition of “Spinco Closing Date Net Debt,” (x) Indebtedness shall (1) include all Indebtedness represented by the Spinco Financing and (2) exclude all Indebtedness owed from a member of the Spinco Group to a member of the Harbor Group (any such Indebtedness, “Harbor-Spinco Indebtedness”), to the extent such Harbor-Spinco Indebtedness has been repaid or equitized or the receivable in respect thereof has been transferred to a member of the Spinco Group, in each case prior to the Distribution, and (y) Cash and Cash Equivalents shall (1) include all Cash and Cash Equivalents of the Harbor Group or the Spinco Group used to fund payments of Shared Expenses (as such term is defined in the Merger Agreement) by, or on behalf of, Spinco on or prior to the Calculation Time, and (2) exclude all Cash and Cash Equivalents of the Spinco Group used to pay the Special Dividend, the Additional Special Dividend (if applicable) and the Intercompany Debt Repayment.

- c. The definition of “Spinco Current Liabilities” in Article I (*Definitions*) Section 1.1 (*General*) is amended to read as follows:

“Spinco Current Liabilities” means, without duplication, all current Liabilities (excluding Excluded Liabilities, Income Tax Liabilities and deferred Tax Liabilities, but including current Non-Income Tax Liabilities), deferred rent and any Indebtedness to the extent exclusively relating to or exclusively arising from the conduct of the Spinco Business, determined as of the Calculation Time in accordance with the Applicable Accounting Principles. For the avoidance of doubt, (1) any Indebtedness taken into account for purposes of the calculation of the Spinco Closing Date Net Debt will not be deemed a Spinco Current Liability and (2) any Shared Expenses borne by Spinco shall not be deemed a Spinco Current Liability.
- d. The definition of “Spinco 2017 Balance Sheet” in Article I (*Definitions*) Section 1.1 (*General*) is amended to read as follows:

“Spinco 2017 Balance Sheet” is the unaudited, combined balance sheet of the Spinco Business as of December 30, 2017 included in the Spinco Annual Financial Statements for the fiscal year ended December 30, 2017.”
- e. Henry Schein’s obligation pursuant to Section 2.10 (*Minority Interests*) of the CDA to use reasonable best efforts, prior to the Harbor Contribution, to acquire, or cause the applicable member of the Harbor Group, as the case may be, to acquire, the outstanding Spinco Minority Interest Shares owned by the JV Minority Shareholders is hereby waived by Voyager and Spinco solely with respect to those entities identified by Voyager in writing to Henry Schein prior to the Closing. Except as set forth in the preceding sentence, the treatment of the Spinco Minority Interest Shares, and all other obligations of the Harbor Group and Spinco with respect thereto, shall remain in full force and effect.
- f. Article II of the CDA is amended by adding at the end thereof a new Section 2.13, which shall read in its entirety as follows:

“Section 2.13. Additional Payments.”

“(a) At the Closing, Spinco shall pay to Henry Schein \$1,312,500 minus the ATP Amount, where the ATP Amount is equal to the product of (a) \$1,602 and (b) the number of days from (i) the date the Distribution Agreement by and between Elanco Animal Health (“Elanco”) and Provet NZ Pty Ltd. granting distribution rights for Elanco products in New Zealand and (ii) the Closing Date.

“(b) At the Closing, Spinco shall pay to Henry Schein an amount equal to \$2,175,719 with respect to the restructuring activities described on Schedule A, which as of the date hereof have already occurred and the amount of which has actually been incurred.

“(c) At the Closing, Spinco shall pay to Henry Schein an amount equal to the Other Restructuring Costs actually incurred by Henry Schein. “Other Restructuring Costs” shall mean the amount set forth by Henry Schein on a schedule to be delivered to Voyager no later than December 1, 2018, which amount shall not exceed \$3,500,000.

“(d) Spinco shall make any and all payments to Henry Schein as required pursuant to Subsections (a) through (c) at the Closing by wire transfer of immediately available funds to an account of Henry Schein designated in writing by Henry Schein.”

2. To amend the Merger Agreement as follows:

- a. Section 1.1 of the Merger Agreement is hereby amended by amending and restating the defined term “Indebtedness” as follows:

“Indebtedness” shall mean, with respect to any Person at any date, without duplication: (i) all indebtedness of such Person for borrowed money or Liabilities issued in substitution for or exchange or replacement of indebtedness for borrowed money, including in respect of loans or advances, whether current, short-term or long-term, secured or unsecured, (ii) all Liabilities of such Person evidenced by bonds, debentures, mortgages, notes or other similar instruments or debt securities (including any seller notes, earnout obligations, compensation arrangements, unpaid principal, related expenses, commitment and other fees, reimbursements, indemnities and all other amounts payable in connection therewith), (iii) any commitment by which a Person assures a creditor against loss (including contingent reimbursement obligations with respect to letters of credit and bankers’ acceptances), (iv) all Liabilities under leases or other similar Contracts for real or personal property which have been or must be, in accordance with GAAP, recorded as capital leases, (v) all Liabilities under any sale-leaseback arrangement in accordance with ASC 840-40: Sale-Leaseback Transactions, (vi) all indebtedness (including earnout obligations) related to conditional sales, title retention or similar arrangements, or with respect to any deferred purchase price of equity, assets or services with respect to which a Person is liable, contingently or otherwise, as obligor, guarantor, surety or otherwise, (vii) all deferred compensation obligations that are owed or that are not cancelable by

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unilateral action by such Person and will be owed by the Surviving Corporation or any of its Subsidiaries under agreements or arrangements existing as of the Effective Time, (viii) any Liabilities with respect to any interest rate cap, hedging or swap agreements, foreign currency exchange agreements or similar arrangements (valued at the termination value thereof), (ix) any Liabilities with respect to unfunded pension obligations that are or would become obligations of the Surviving Corporation or any of its Subsidiaries, in each case, other than, with respect to Voyager, those Liabilities specifically related to the Voyager Pension Plans and, with respect to Spingo, the Spingo Group Employees under any Multiemployer Plans, (x) all guarantees, direct or indirect, of such Person in connection with any of the foregoing and any other indebtedness guaranteed in any manner by a Person (including guarantees in the form of an agreement to repurchase or reimburse), but not any items to the extent for which Spingo is entitled to be indemnified pursuant to Section 6.3(b) of the Distribution Agreement and (xi) all accrued and unpaid interest, prepayment premiums or penalties, or breakage fees related to any of the foregoing. Notwithstanding the foregoing, Indebtedness shall not include any (i) Indebtedness or other intercompany obligations between or among (x) the Spingo Entities or (y) the Voyager Entities and (ii) items included in the calculation of (x) Voyager Current Liabilities or (y) for purposes of calculating Spingo Working Capital in the Distribution Agreement, the Spingo Current Liabilities (as defined therein) or (iii) Shared Expenses.

- b. Section 1.1 of the Merger Agreement is hereby amended by amending and restating the defined term “Voyager Closing Date Net Debt” as follows:

“Voyager Closing Date Net Debt” shall mean an amount (which may be positive or negative), in each case, determined as of the Calculation Time and without giving effect to the consummation of the Transactions, equal to (i) the Indebtedness of Voyager and its Subsidiaries, less the sum of (a) an amount equal to the Cash and Cash Equivalents of Voyager and its Subsidiaries, and (b) all Cash and Cash Equivalents of Voyager and its Subsidiaries used by Voyager to pay Voyager Transaction Expenses or Shared Expenses prior to the Calculation Time.

- c. Section 1.1 of the Merger Agreement is hereby amended by amending and restating the defined term “Voyager Transaction Expenses Amount” as follows:

“Voyager Transaction Expenses Amount” means the amount of Transaction Expenses allocated to or to be borne by Voyager or any of its Subsidiaries pursuant to this Agreement or any of the Transaction Agreements in excess of twenty-five million dollars (\$25,000,000), including in such amount the Voyager Stockholders’ Representative Expense Fund Amount.

- d. Section 1.1 of the Merger Agreement is hereby amended by adding the following defined term, which shall be set forth in its proper alphabetic location:

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“Voyager Written Consent’ shall mean the written consent, prepared and delivered in accordance with the requirements of Voyager’s Certificate of Incorporation and bylaws, of each of (i) the holders of at least a majority of the outstanding shares of Voyager Common Stock (calculated on an as-converted basis), and (ii) the holders of at least sixty percent (60%) of the issued and outstanding shares of Voyager Preferred Stock.”

- e. Section 5.2 of the Merger Agreement is hereby amended and restated in its entirety as follows:

“Section 5.2. Authorization and Validity of Agreement. Voyager has all necessary corporate power and authority to execute and deliver this Agreement and each Transaction Agreement to which it is a party, to perform its obligations hereunder and thereunder and, subject to the receipt of the Voyager Stockholder Approval, to consummate the Transactions. The execution, delivery and performance of this Agreement and the Transaction Agreements by Voyager and the consummation by Voyager of the Transactions, have been duly and validly authorized and unanimously approved by the Voyager Board of Directors, and no other corporate or other action on the part of Voyager is necessary to authorize the execution, delivery and performance of this Agreement and the Transaction Agreements or the consummation of the Transactions (other than the Voyager Stockholder Approval). The Voyager Board of Directors has unanimously (i) determined that this Agreement, the Transaction Agreements and the Transactions (including the Merger), taken together, are advisable, fair and in the best interest of Voyager and its stockholders and (ii) approved this Agreement, the Transaction Agreements and the Transactions (including the Merger). In addition, the Voyager Board of Directors has recommended the affirmative vote of the Voyager Stockholders at the Voyager Stockholders Meeting with respect to the Voyager Stockholder Approval. The only approval or consent of the holders of any class or series of capital stock of Voyager or its Subsidiaries necessary to approve and adopt this Agreement and the Transaction Agreements and to approve and adopt the Merger and the Transactions under applicable Law, the Voyager Certificate of Incorporation and the bylaws of Voyager is (a) the affirmative vote of each of (i) the holders of at least a majority of the outstanding shares of Voyager Common Stock (calculated on an as-converted basis), and (ii) the holders of at least sixty percent (60%) of the issued and outstanding shares of Voyager Preferred Stock, at the Voyager Stockholders Meeting or (b) the Voyager Written Consent (the “Voyager Stockholder Approval”). This Agreement and the Transaction Agreements have been or shall be duly and validly executed and delivered by Voyager and, to the extent it is a party thereto, assuming due and valid authorization, execution and delivery hereof and thereof by each of Harbor, Spinceo and Merger Sub, as applicable, each is a valid and binding obligation of Voyager and enforceable against Voyager in accordance with their terms, except to the extent that its enforceability may be subject to applicable bankruptcy, insolvency, reorganization, moratorium or other similar Laws, now or hereinafter in effect, affecting the enforcement of creditors’ rights generally and by general equitable principles.”

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f. Section 6.4(b) of the Merger Agreement is hereby amended by adding the following text immediately after “Voyager Stockholders Meeting” therein:

“or the effective date of the Voyager Written Consent”.

g. Section 6.9(b) of the Merger Agreement is hereby amended by adding the following text immediately after “Voyager Stockholders Meeting” therein:

“or the effective date of the Voyager Written Consent”.

h. Section 6.9(c) of the Merger Agreement is hereby amended and restated in its entirety as follows:

“(c) (i) As promptly as practicable following the date on which the SEC shall clear (whether orally or in writing) the Prospectus and, if required by the SEC as a condition to the mailing of the Prospectus, the Registration Statement shall have been declared effective and no later than five (5) Business Days after such date, Voyager shall duly take all lawful action to (A) duly call, give notice of, convene and hold a meeting of its stockholders (the “Voyager Stockholders Meeting”) to be held as promptly as practicable for the purpose of voting (the “Voyager Stockholder Vote”) upon the Voyager Stockholder Approval or (B) solicit the Voyager Written Consent.

“(ii) In the event that Voyager elects to obtain the Voyager Stockholder Approval by holding the Voyager Stockholder Meeting, Voyager shall deliver, or cause to be delivered, to Voyager’s stockholders (A) a proxy statement with respect to the Voyager Stockholders Meeting that includes a copy of the notice required pursuant to Section 262 of the DGCL informing the Voyager Stockholders that appraisal rights are available for their shares of Voyager Capital Stock pursuant to Section 262 of the DGCL, along with such other information as required by Section 262 of the DGCL and applicable Law, and (B) the Prospectus in definitive form, in each case in connection with the Voyager Stockholders Meeting at the time and in a manner in accordance with applicable Laws, the Voyager Certificate of Incorporation and the bylaws of Voyager, and shall conduct the Voyager Stockholders Meeting and the solicitation of proxies in connection therewith in compliance with applicable Laws, the Voyager Certificate of Incorporation and the bylaws of Voyager. Such proxy statement, including any amendments or supplements thereto, shall be subject to reasonable review and approval by Harbor and Spinco, which approval shall not be unreasonably withheld, conditioned or delayed.

“(iii) In the event that Voyager elects to obtain the Voyager Stockholder Approval by soliciting the Voyager Written Consent, Voyager shall deliver, or cause to be delivered, to Voyager’s Stockholders (A) a copy of the text of the Voyager Written Consent, together with the notice required pursuant to Section 262 of the DGCL informing the Voyager Stockholders that appraisal rights are available for their shares

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of Voyager Capital Stock pursuant to Section 262 of the DGCL, along with such other information as required by Section 262 of the DGCL and applicable Law (which materials shall be subject to reasonable prior review and approval by Harbor and Spinco, such approval not to be unreasonably withheld, conditioned or delayed), and (B) the Prospectus in definitive form, in each case in the manner prescribed by applicable Laws, the Voyager Certificate of Incorporation and the bylaws of Voyager.”

i. Section 7.1(d) of the Merger Agreement is hereby amended and restated in its entirety as follows:

“(d) The Voyager Stockholder Approval shall have been obtained in accordance with applicable Law, the Voyager Certificate of Incorporation, the bylaws of Voyager and Section 6.9(c) hereof.”

j. Section 7.2(c) of the Merger Agreement is hereby amended and restated in its entirety as follows:

“(c) Voyager shall have delivered to Harbor evidence of the Voyager Stockholder Approval pursuant to the Voyager Stockholder Vote or the Voyager Written Consent.”

Other than as expressly set forth herein, all obligations, representations and warranties, covenants, conditions and other provisions in the Merger Agreement and in the CDA remain unchanged and in full force and effect.

This Letter may be executed in one or more counterparts each of which when executed shall be deemed to be an original but all of which taken together shall constitute one and the same agreement. Delivery of an executed counterpart of a signature page to this Letter by facsimile or portable document format (PDF) shall be as effective as delivery of a manually executed counterpart of this Letter.

This Letter and all issues and questions concerning the construction, validity, enforcement and interpretation of this Letter (and all Annexes hereto) shall be governed by, and construed in accordance with, the Laws of the State of Delaware, without giving effect to any choice of law or conflict of law rules or provisions (whether of the State of Delaware or any other jurisdiction) that would cause the application of the Laws of any jurisdiction other than the State of Delaware. In furtherance of the foregoing, the internal Laws of the State of Delaware shall control the interpretation and construction of this Letter (and all Annexes hereto), even though under that jurisdiction’s choice of law or conflict of law analysis, the substantive Law of some other jurisdiction would ordinarily apply.

*[Remainder of page intentionally left blank]*

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If you are in agreement with the foregoing, please sign and return one copy of this Letter, which thereupon will constitute a binding agreement between us with respect to the subject matter hereof as of the date first written above.

Very truly yours,

**HENRY SCHEIN, INC.**

By: /s/ Steven Paladino  
Name: Steven Paladino  
Title: Chief Financial Officer

**HS SPINCO, INC.**

By: /s/ Steven Paladino  
Name: Steven Paladino  
Title: Treasurer and Chief Financial Officer

**HS MERGER SUB, INC.**

By: /s/ Steven Paladino  
Name: Steven Paladino  
Title: Treasurer and Chief Financial Officer

*[Signature Page to Project Voyager Side Letter]*

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Confirmed and agreed to as of the date first above written:

**DIRECT VET MARKETING, INC.**

By: /s/ Benjamin Shaw

Name: Benjamin Shaw

Title: Chief Executive Officer

**SHAREHOLDER REPRESENTATIVE SERVICES, LLC**

as Voyager Stockholders' Representative

By: /s/ Sam Riffe

Name: Sam Riffe

Title: Executive Director

*[Signature Page to Project Voyager Side Letter]*

**CERTIFICATION PURSUANT TO RULE 13a-14(a) OR 15d-14(a) OF THE SECURITIES  
EXCHANGE ACT OF 1934, AS ADOPTED PURSUANT TO SECTION 302 OF THE  
SARBANES-OXLEY ACT OF 2002**

I, Stanley M. Bergman, certify that:

1. I have reviewed this quarterly report on Form 10-Q of Henry Schein, Inc.;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
  - (a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
  - (b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
  - (c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
  - (d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
  - (a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
  - (b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: November 6, 2018

/s/ Stanley M. Bergman

Stanley M. Bergman  
Chairman and Chief Executive Officer

**CERTIFICATION PURSUANT TO RULE 13a-14(a) OR 15d-14(a) OF THE SECURITIES  
EXCHANGE ACT OF 1934, AS ADOPTED PURSUANT TO SECTION 302 OF THE  
SARBANES-OXLEY ACT OF 2002**

I, Steven Paladino, certify that:

1. I have reviewed this quarterly report on Form 10-Q of Henry Schein, Inc.;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
  - (a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
  - (b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
  - (c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
  - (d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
  - (a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
  - (b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: November 6, 2018

/s/ Steven Paladino

Steven Paladino  
Executive Vice President and  
Chief Financial Officer

**CERTIFICATION PURSUANT TO 18 U.S.C. SECTION 1350,  
AS ADOPTED PURSUANT TO SECTION 906 OF THE  
SARBANES-OXLEY ACT OF 2002**

In connection with the quarterly report on Form 10-Q of Henry Schein, Inc. (the "Company") for the period ending September 29, 2018, as filed with the Securities and Exchange Commission on the date hereof (the "Report"), I, Stanley M. Bergman, the Chairman and Chief Executive Officer of the Company, and I, Steven Paladino, Executive Vice President and Chief Financial Officer of the Company, do hereby certify pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, to the best of my knowledge and belief that:

- (1) the Report fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934, as amended; and
- (2) the information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

Dated: November 6, 2018

/s/ Stanley M. Bergman  
Stanley M. Bergman  
Chairman and Chief Executive Officer

Dated: November 6, 2018

/s/ Steven Paladino  
Steven Paladino  
Executive Vice President and  
Chief Financial Officer

This certification accompanies each Report pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 and shall not, except to the extent required by the Sarbanes-Oxley Act of 2002, be deemed filed by the Company for purposes of Section 18 of the Securities Exchange Act of 1934, as amended.

A signed original of this written statement required by Section 906 of the Sarbanes-Oxley Act of 2002 has been provided to the Company and will be retained by the Company and furnished to the Securities and Exchange Commission or its staff upon request.