

SIRONA DENTAL SYSTEMS, INC.

Form 10-Q

May 05, 2010

[Table of Contents](#)

**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 March 31, 2010

or

**Transition Report pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934**  
For the transition period from \_\_\_\_\_ to \_\_\_\_\_

Commission file number 000-22673

**Sirona Dental Systems, Inc.**

(Exact name of registrant as specified in charter)

Delaware

11-3374812

Edgar Filing: SIRONA DENTAL SYSTEMS, INC. - Form 10-Q

(State or other jurisdiction of incorporation or organization) (I.R.S. Employer Identification No.)  
30-30 47<sup>th</sup> Avenue, Suite 500, Long Island City, New York 11101  
(Address of principal executive offices) (Zip Code)  
Registrant's telephone number, including area code: (718) 482-2011

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.

Yes  No

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

Yes  No

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

Large accelerated filer  Accelerated filer  Non-accelerated filer

Smaller reporting company

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

Yes  No

As of May 3, 2010, the number of shares outstanding of the Registrant's Common Stock, par value \$.01 per share, was 55,241,197.

**Table of Contents**

**SIRONA DENTAL SYSTEMS, INC.**

**FORM 10-Q**

**FOR THE THREE MONTHS ENDED MARCH 31, 2010**

**Index**

	<b>Page</b>
<b>Part I. <u>Financial Information (Unaudited)</u></b>	<b>3</b>
Item 1. <u>Financial Statements</u>	3
<u>Condensed Consolidated Balance Sheets as of March 31, 2010 and September 30, 2009</u>	3
<u>Condensed Consolidated Income Statements for the three and six months ended March 31, 2010 and 2009</u>	4
<u>Condensed Consolidated Statements of Cash Flows for the six months ended March 31, 2010 and 2009</u>	5
<u>Notes to the Condensed Consolidated Financial Statements</u>	7
Item 2. <u>Management's Discussion and Analysis of Financial Condition and Results of Operations</u>	20
Item 3. <u>Quantitative and Qualitative Disclosures About Market Risk</u>	34
Item 4. <u>Controls and Procedures</u>	34
<b>Part II. <u>Other Information</u></b>	<b>35</b>
Item 1. <u>Legal Proceedings</u>	35
Item 1A. <u>Risk Factors</u>	35
Item 2. <u>Unregistered Sales of Equity Securities and Use of Proceeds</u>	35
Item 3. <u>Defaults upon Senior Securities</u>	35
Item 4. <u>(Removed and Reserved)</u>	35
Item 5. <u>Other Information</u>	35
Item 6. <u>Exhibits</u>	36
<u>Signatures</u>	37
<u>Certifications</u>	

**Table of Contents****PART I FINANCIAL INFORMATION (UNAUDITED)****ITEM 1. FINANCIAL STATEMENTS****SIRONA DENTAL SYSTEMS, INC. AND SUBSIDIARIES****CONDENSED CONSOLIDATED BALANCE SHEETS**

(UNAUDITED)

	Financial Statement Notes	March 31, 2010 (unaudited) \$ 000s (except per share amounts)	September 30, 2009
<b>ASSETS</b>			
<b>Current assets</b>			
Cash and cash equivalents		\$ 162,439	\$ 181,098
Restricted cash		721	902
Accounts receivable, net of allowance for doubtful accounts of \$2,201 and \$2,088, respectively		99,700	98,277
Inventories, net	5	73,144	74,525
Deferred tax assets		17,045	16,483
Prepaid expenses and other current assets		16,839	20,239
Income tax receivable		2,578	3,956
<b>Total current assets</b>		<b>372,466</b>	<b>395,480</b>
Property, plant and equipment, net of accumulated depreciation and amortization of \$72,435 and \$70,061, respectively		93,637	102,775
Goodwill	6	648,233	696,355
Investments		1,802	1,739
Intangible assets, net of accumulated amortization of \$335,340 and \$327,183, respectively	6	389,220	447,946
Other non-current assets		1,425	2,837
Deferred tax assets		1,107	943
<b>Total assets</b>		<b>\$ 1,507,890</b>	<b>\$ 1,648,075</b>
<b>LIABILITIES AND SHAREHOLDERS EQUITY</b>			
<b>Current liabilities</b>			
Trade accounts payable		\$ 39,798	\$ 38,463
Short-term debt and current portion of long-term debt	7	2,988	4,688
Income taxes payable		7,821	5,191
Deferred tax liabilities		1,502	466
Accrued liabilities and deferred income		75,079	95,602
<b>Total current liabilities</b>		<b>127,188</b>	<b>144,410</b>
Long-term debt	8	364,336	470,224
Deferred tax liabilities		139,970	159,659
Other non-current liabilities		12,144	8,699
Pension related provisions	12	46,234	50,328
Deferred income		65,000	70,000

<b>Total liabilities</b>	<b>754,872</b>	<b>903,320</b>
<b>Shareholders' equity</b>		
Preferred stock (\$0.01 par value; 5,000,000 shares authorized; none issued and outstanding)		
Common stock (\$0.01 par value; 95,000,000 shares authorized; 55,241,095 shares issued and 55,213,372 shares outstanding at Mar. 31, 2010 and 54,972,754 shares issued and 54,945,031 shares outstanding at Sept. 30, 2009)	553	550
Additional paid-in capital	645,807	637,264
Treasury stock (27,723 shares at cost)	(284)	(284)
Excess of purchase price over predecessor basis	(49,103)	(49,103)
Retained earnings	140,571	91,857
Accumulated other comprehensive income	13,542	63,154
<b>Total Sirona Dental Systems, Inc. shareholders' equity</b>	<b>751,086</b>	<b>743,438</b>
Noncontrolling interests	1,932	1,317
<b>Total shareholders' equity</b>	<b>753,018</b>	<b>744,755</b>
<b>Total liabilities and shareholders' equity</b>	<b>\$ 1,507,890</b>	<b>\$ 1,648,075</b>

The accompanying notes are an integral part of these financial statements.

**Table of Contents****SIRONA DENTAL SYSTEMS, INC.****AND SUBSIDIARIES****CONDENSED CONSOLIDATED INCOME STATEMENTS**

(UNAUDITED)

	Financial Statement Notes	Three months ended March 31,		Six months ended March 31,	
		2010	2009	2010	2009
		\$ 000s (except per share amounts)		\$ 000s (except per share amounts)	
<b>Revenue</b>		<b>\$ 190,136</b>	<b>\$ 164,822</b>	<b>\$ 404,959</b>	<b>\$ 344,543</b>
Cost of sales		90,803	84,507	193,256	177,227
<b>Gross profit</b>		<b>99,333</b>	<b>80,315</b>	<b>211,703</b>	<b>167,316</b>
Selling, general and administrative expense		60,354	56,048	120,206	113,470
Research and development		11,690	10,043	23,155	21,101
Provision for doubtful accounts and notes receivable		72	221	136	446
Net other operating (income)/loss and restructuring costs	<b>13</b>	(3,408)	270	(5,908)	(3,191)
<b>Operating income</b>		<b>30,625</b>	<b>13,733</b>	<b>74,114</b>	<b>35,490</b>
Loss on foreign currency transactions, net		5,049	7,077	4,416	10,669
(Gain)/loss on derivative instruments	<b>14</b>	(1,712)	(240)	(2,735)	4,727
Interest expense, net		4,141	5,593	9,343	11,657
Other expense		404		784	
<b>Income before taxes</b>		<b>22,743</b>	<b>1,303</b>	<b>62,306</b>	<b>8,437</b>
Income tax provision	<b>9</b>	4,548	364	12,461	2,362
Net income		18,195	939	49,845	6,075
Less: Net income attributable to noncontrolling interests		656	344	1,131	(79)
<b>Net income attributable to Sirona Dental Systems, Inc.</b>		<b>\$ 17,539</b>	<b>\$ 595</b>	<b>\$ 48,714</b>	<b>\$ 6,154</b>
<b>Income per share (attributable to Sirona Dental Systems, Inc. common shareholders):</b>	<b>10</b>				
- Basic		\$ 0.32	\$ 0.01	\$ 0.88	\$ 0.11
- Diluted		\$ 0.31	\$ 0.01	\$ 0.86	\$ 0.11
Weighted average shares basic		55,122,944	54,818,604	55,044,832	54,856,537
Weighted average shares diluted		56,610,111	55,044,094	56,490,563	55,103,133

The accompanying notes are an integral part of these financial statements.



**Table of Contents****SIRONA DENTAL SYSTEMS, INC. AND SUBSIDIARIES****CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS**

(UNAUDITED)

	Six months ended March 31,	
	2010	2009
	\$ 000s	
<b>Cash flows from operating activities</b>		
Net income	\$ 49,845	\$ 6,075
<b>Adjustments to reconcile net income to net cash provided by operating activities</b>		
Depreciation and amortization	42,589	44,572
Loss on disposal of property, plant and equipment	15	80
(Gain)/loss on derivative instruments	(2,735)	4,727
Loss on foreign currency transactions	4,416	10,669
Deferred income taxes	(9,491)	(14,010)
Amortization of debt issuance cost	586	597
Compensation expense from stock options	8,048	7,794
<b>Changes in assets and liabilities</b>		
Accounts receivable	(7,288)	(24,724)
Inventories	(3,601)	(1,776)
Prepaid expenses and other current assets	6,701	(11,834)
Restricted cash	109	(16)
Other non-current assets	26	(664)
Trade accounts payable	3,353	(3,177)
Accrued interest on long-term debt	(1,412)	(4,043)
Accrued liabilities and deferred income	(25,309)	6,371
Other non-current liabilities	4,037	(2,702)
Income taxes receivable	1,506	2,066
Income taxes payable	3,415	1,867
<b>Net cash provided by operating activities</b>	<b>74,810</b>	<b>21,872</b>
<b>Cash flows from investing activities</b>		
Investment in property, plant and equipment	(9,566)	(10,137)
Proceeds from sale of property, plant and equipment	150	283
Purchase of intangible assets		(64)
Purchase of long-term investments	(230)	(63)
Sale of businesses, net of cash sold	1,928	4,985
<b>Net cash used in investing activities</b>	<b>(7,718)</b>	<b>(4,996)</b>

The accompanying notes are an integral part of these financial statements.



**Table of Contents**

	Six months ended March 31,	
	2010	2009
	\$ 000s	
<b>Cash flows from financing activities</b>		
Repayments of short-term and long-term debt	(78,072)	(1,153)
Purchase of treasury stock		(285)
Common shares issued under share based compensation plans	2,973	134
Tax effect of common shares exercised under share based compensation plans	1,181	34
<b>Net cash used in financing activities</b>	<b>(73,918)</b>	<b>(1,270)</b>
Change in cash and cash equivalents	(6,826)	15,606
Effect of exchange rate change on cash and cash equivalents	(11,833)	(7,765)
Cash and cash equivalents at beginning of period	181,098	149,663
<b>Cash and cash equivalents at end of period</b>	<b>\$ 162,439</b>	<b>\$ 157,504</b>
<b>Supplemental information</b>		
Interest paid	\$ 10,381	\$ 13,468
Interest capitalized	242	265
Income taxes paid	18,478	12,064
<b>Sale of businesses, net of cash sold</b>		
Current assets	\$ 2,406	\$ 5,899
Non-current assets	550	291
Current liabilities	(867)	(1,205)
Non-current liabilities	(161)	
	<b>\$ 1,928</b>	<b>\$ 4,985</b>

The accompanying notes are an integral part of these financial statements.

**Table of Contents**

**SIRONA DENTAL SYSTEMS, INC. AND SUBSIDIARIES**

**NOTES TO THE CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**

(UNAUDITED)

**1. General**

**The Company and its Operations**

Sirona Dental Systems, Inc. ( Sirona or the Company ) is the leading manufacturer of high-quality, technologically advanced dental equipment, and is focused on developing, manufacturing and marketing innovative systems and solutions for dentists around the world. We offer a broad range of products across all major segments of the dental technology market including CEREC and our other CAD/CAM systems, digital intra oral and 2D and 3D panoramic imaging systems, treatment centers and instruments. The Company acquired Schick Technologies, Inc. ( Schick ) in 2006, in a transaction accounted for as a reverse acquisition, further expanding our global presence and product offerings and strengthening our research and development capabilities. Sirona has served equipment dealers and dentists worldwide for more than 130 years. The Company's headquarters are located in Long Island City, New York with its primary facility located in Bensheim, Germany, as well as other support, manufacturing, assembling and sales and service facilities located elsewhere in the world.

**Basis of Presentation**

These unaudited interim condensed consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States ( U.S. GAAP ). Preparation of the interim financial statements in conformity with U.S. GAAP requires management to make estimates and assumptions related to the reported amounts of assets and liabilities and the disclosure of contingent assets and liabilities as at the reporting date and the reported amounts of revenues and expenses for the interim period. Actual results could differ from those estimates. Certain information and footnote disclosures normally included in financial statements prepared in accordance with U.S. GAAP have been condensed or omitted pursuant to such rules and regulations. However, the Company believes that the disclosures are adequate to make the information not misleading. The year-end condensed consolidated balance sheet data was derived from the audited consolidated financial statements, but does not include all disclosures required by U.S. GAAP. These consolidated financial statements should be read in conjunction with the Consolidated Financial Statements and the Notes thereto included in the Company's Annual Report on Form 10-K for the fiscal year ended September 30, 2009.

In the opinion of management, all adjustments (consisting of those of a normal recurring nature) considered necessary to present fairly the Company's financial position as of March 31, 2010 and September 30, 2009 and the results of operations and cash flows for the three and six months ended March 31, 2010 and 2009, respectively, as applicable to interim periods have been made. The results of operations for the three or six months ended March 31, 2010 are not necessarily indicative of the operating results for the full fiscal year or future periods.

All amounts are reported in thousands of U.S. Dollars (\$), except per share amounts or as otherwise disclosed.

***Fiscal year***

The Company's fiscal year is October 1 to September 30.

***Principles of consolidation***

The consolidated financial statements include, after eliminating inter-company transactions and balances, the accounts of Sirona Dental Systems, Inc. and its subsidiaries. The Company applies the equity method of accounting for investments in associated companies over which the Company has significant influence but does not have effective control.

---

**Table of Contents**

**2. Recently Issued Accounting Pronouncements**

**Adopted**

*Business Acquisitions*

On October 1, 2009, the Company adopted the new accounting guidance for business combinations (SFAS No. 141 (Revised), *Business Combinations* (SFAS 141R) (FASB Codification ASC 805, *Business Combinations*)). This guidance establishes principles and requirements for the reporting entity in a business combination, including recognition and measurement in the financial statements of the identifiable assets acquired, the liabilities assumed, goodwill, and any noncontrolling interest in the acquiree, as well as disclosure requirements to enable financial statement users to evaluate the nature and financial effects of the business combination. Additionally, it provides guidance for identifying a business combination, measuring the acquisition date, and defining the measurement period for adjusting provisional amounts recorded. The implementation of this standard did not have a material impact on the Company's interim condensed consolidated financial statements.

*Noncontrolling Interests*

On October 1, 2009, the Company adopted the new accounting guidance for reporting a noncontrolling interest ( NCI ) in a subsidiary (SFAS No. 160, *Noncontrolling Interests in Consolidated Financial Statements – an amendment of ARB No. 51*, ( SFAS 160 ) (FASB Codification ASC 810, *Consolidation*), which amends Accounting Research Bulletin No. 51, *Consolidated Financial Statements* ( ARB No. 51 )). This new guidance defines a noncontrolling interest, establishes a single method of accounting for changes in a parent's ownership interest not resulting in deconsolidation, accounting for deconsolidation, and expands the disclosures of NCI's in consolidated financial statements. As a result, the Company reported NCI as a separate component of Stockholders' Equity in the Condensed Consolidated Balance Sheet. Additionally, the Company reported the portion of net income attributed to the Company and NCI separately in the Condensed Consolidated Income Statements. The portion of comprehensive income attributed to the Company and NCI are reported separately in a Note to the consolidated financial statements. All related disclosures have been adjusted accordingly. Prior year amounts associated with NCI in the financial statements and accompanying footnotes have been adjusted retrospectively to conform to the adoption.

*Intangible Assets*

On October 1, 2009, the Company adopted the new accounting guidance for determination of the useful lives of intangible assets (FASB Staff Position ( FSP ) No. 142-3, *Determination of the Useful Lives of Intangible Assets*, ( FSP 142-3 ) (FASB Codification ASC 350, *Intangibles Goodwill and Other*)). This new guidance amends the factors that should be considered in developing renewal or extension assumptions used to determine the useful life of an intangible asset as well as the period of expected cash flows used to measure the fair value of intangible assets in business combinations. The implementation of this new guidance did not have a material impact on the Company's interim condensed consolidated financial statements.

*Fair Value Measurement*

On October 1, 2009, the Company adopted FAS 157, *Fair Value Measurements* (FASB Codification ASC 820, *Fair Value Measurements and Disclosures*) for non-recurring fair value measurements of non-financial assets and liabilities. The implementation of this new guidance did not have a material impact on the Company's interim condensed consolidated financial statements.

**Table of Contents****Not yet adopted**

In October 2009, the FASB issued ASU 2009-13, *Multiple-Deliverable Revenue Arrangements – a consensus of the FASB Emerging Issues Task Force*, which amends the criteria for separating consideration in multiple-deliverable arrangements, establishes a selling price hierarchy for determining the selling price of a deliverable, replaces the term *fair value* in the revenue allocation with *selling price* to clarify that the allocation of revenue is based on entity-specific assumptions rather than assumptions of a marketplace participant, replaces the *residual method* of allocation with the *relative selling-price method*, and requires that arrangement consideration be allocated at the inception of the arrangement to all deliverables applying this method, including proportional allocation of any discounts to each deliverable. In addition, this new guidance will require that a vendor determine its best estimate of selling price in a manner that is consistent with that used to determine the selling price of a deliverable on a standalone basis and expands the required disclosures to provide information about the significant judgments made and changes to those judgments and about how the application of the relative selling-price method affects the timing or amount of revenue recognition. ASU 2009-13 is effective prospectively for revenue arrangements entered into or materially modified in fiscal years beginning on or after June 15, 2010, which corresponds to the Company's fiscal year beginning October 1, 2010. The Company is evaluating the potential impact of adoption.

In October 2009, the FASB issued ASU 2009-14, *Certain Revenue Arrangements that Include Software Elements – a consensus of the FASB Emerging Issues Task Force*, which changes the accounting model for revenue arrangements that include both tangible products and software elements. This new guidance removes from the scope of the software revenue recognition guidance in ASC 985-605, *Software Revenue Recognition*, those tangible products containing software components and nonsoftware components that function together to deliver the tangible product's essential functionality. In addition, this guidance requires that hardware components of a tangible product containing software components always be excluded from the software revenue recognition guidance as well as provides further guidance on determining which software, if any, relating to the tangible product also would be excluded from the scope of software revenue recognition guidance. The guidance further identifies specific factors in determining whether the tangible product contains software that works together with the nonsoftware components of the tangible product to deliver the tangible product's essential functions. Guidance is also provided on how a vendor should allocate arrangement consideration to deliverables in an arrangement containing both tangible products and software. The disclosures mandated in ASU 2009-13 are also required by this new guidance. ASU 2009-14 is effective prospectively for revenue arrangements entered into or materially modified in fiscal years beginning on or after June 15, 2010, which corresponds to the Company's fiscal year beginning October 1, 2010. The Company is evaluating the potential impact of adoption.

**3. Employee Share-Based Compensation**

Stock compensation expense for the Company's stock option plans amounted to \$4,109 and \$8,048 for the three and six months ended March 31, 2010, respectively, and \$3,959 and \$7,794 for the three and six months ended March 31, 2009, respectively. The fiscal 2010 expenses include the impact of previous stock options, restricted stock, and the restricted stock unit (RSU) grants.

On December 8, 2009, the Company granted 188,000 RSU's under the Equity Incentive Plan (the 2006 Plan). The RSU's vest over a period of four years (one third each at December 8, 2011, 2012 and 2013). The value of each RSU is determined by the closing price as of the date of grant of \$34.45. The 2006 Plan provides for granting in total up to 4,550,000 stock options, incentive stock, and RSU's to employees, directors, and consultants and received stockholder approval at the Company's Annual Meeting of Stockholders held on February 27, 2007, and was amended on February 25, 2009. As of March 31, 2010, 1,646,358 shares were available for future grant under the 2006 Plan.

**Table of Contents****4. Comprehensive Income/(Loss) and Change in Equity**

	Changes in Equity attributable to Sirona Dental Systems, Inc.		Changes in Equity attributable to Noncontrolling Interests		Total Change in Equity for the Period	
	Three months ended March 31	Six months ended March 31	Three months ended March 31	Six months ended March 31	Three months ended March 31	Six months ended March 31
<b>As of March 31, 2010</b>						
Comprehensive Income/(Loss):						
Net Income	\$ 17,539	\$ 48,714	\$ 656	\$ 1,131	\$ 18,195	\$ 49,845
Other Comprehensive Income/(Loss)						
Cumulative translation adjustments	(38,668)	(49,448)	(26)	(18)	(38,694)	(49,466)
Unrecognized elements of pension cost, net of tax	(77)	(164)			(77)	(164)
<b>Total Other Comprehensive Loss</b>	<b>(38,745)</b>	<b>(49,612)</b>	<b>(26)</b>	<b>(18)</b>	<b>(38,771)</b>	<b>(49,630)</b>
<b>Total Comprehensive Income/(Loss)</b>	<b>(21,206)</b>	<b>(898)</b>	<b>630</b>	<b>1,113</b>	<b>(20,576)</b>	<b>215</b>
Transactions with shareholders:						
Stock-based compensation activities	3,573	9,364			3,573	9,364
Purchase of shares from noncontrolling interest	(818)	(818)	(498)	(498)	(1,316)	(1,316)
<b>Total transactions with shareholders</b>	<b>2,755</b>	<b>8,546</b>	<b>(498)</b>	<b>(498)</b>	<b>2,257</b>	<b>8,048</b>
<b>Total Change in Equity for the period</b>	<b>\$ (18,451)</b>	<b>\$ 7,648</b>	<b>\$ 132</b>	<b>\$ 615</b>	<b>\$ (18,319)</b>	<b>\$ 8,263</b>

	Changes in Equity attributable to Sirona Dental Systems, Inc.		Changes in Equity attributable to Noncontrolling Interests		Total Change in Equity for the Period	
	Three months ended March 31	Six months ended March 31	Three months ended March 31	Six months ended March 31	Three months ended March 31	Six months ended March 31
<b>As of March 31, 2009</b>						
Comprehensive Income/(Loss):						
Net Income	\$ 595	\$ 6,154	\$ 344	\$ (79)	\$ 939	\$ 6,075
Other Comprehensive Income/(Loss)						
Cumulative translation adjustments	(23,287)	(36,821)	(1)	(42)	(23,288)	(36,863)
Unrecognized elements of pension cost, net of tax	117	235			117	235
<b>Total Other Comprehensive Loss</b>	<b>(23,170)</b>	<b>(36,586)</b>	<b>(1)</b>	<b>(42)</b>	<b>(23,171)</b>	<b>(36,628)</b>
<b>Total Comprehensive Income/(Loss)</b>	<b>(22,575)</b>	<b>(30,432)</b>	<b>343</b>	<b>(121)</b>	<b>(22,232)</b>	<b>(30,553)</b>
Transactions with shareholders:						
Stock-based compensation activities	4,128	7,962			4,128	7,962

Edgar Filing: SIRONA DENTAL SYSTEMS, INC. - Form 10-Q

Purchase of treasury stock	(20)	(284)			(20)	(284)
Purchase of shares from noncontrolling interest						
Total transactions with shareholders	4,108	7,678			4,108	7,678
Total Change in Equity for the period	\$ (18,467)	\$ (22,754)	\$ 343	\$ (121)	\$ (18,124)	\$ (22,875)

**5. Inventories, Net**

	March 31, 2010	September 30, 2009
	\$ 000s	
Finished goods	\$ 43,187	\$ 41,594
Work in progress	13,098	14,086
Raw materials	28,572	31,167
	<b>84,857</b>	<b>86,847</b>
Inventory reserve	(11,713)	(12,322)
	<b>\$ 73,144</b>	<b>\$ 74,525</b>

**Table of Contents****6. Intangible Assets and Goodwill**

	Gross	Accumulated amortization \$ 000s	Net
<b>As of March 31, 2010</b>			
Patents & licenses	\$ 140,936	\$ 59,748	\$ 81,188
Trademarks	130,512	378	130,134
Technologies and dealer relationships	452,865	275,214	177,651
Prepayments for intangible assets	247		247
	724,560	335,340	389,220
Goodwill	648,233		648,233
<b>Total intangible assets</b>	<b>\$ 1,372,793</b>	<b>\$ 335,340</b>	<b>\$ 1,037,453</b>

	Gross	Accumulated amortization \$ 000s	Net
<b>As of September 30, 2009</b>			
Patents & licenses	\$ 153,814	\$ 59,322	\$ 94,492
Trademarks	139,743	328	139,415
Technologies and dealer relationships	481,325	267,533	213,792
Prepayments for intangible assets	247		247
	775,129	327,183	447,946
Goodwill	696,355		696,355
<b>Total intangible assets</b>	<b>\$ 1,471,484</b>	<b>\$ 327,183</b>	<b>\$ 1,144,301</b>

The change in the book value of goodwill and of intangible assets from September 30, 2009 to March 31, 2010 mainly results from foreign currency fluctuations, with an impact of \$47,066 on goodwill and \$50,569 on intangible assets for the first half of fiscal 2010. Goodwill has also been reduced by (i) \$400 as a result of the sale of a subsidiary and (ii) \$656 as a result of tax benefits received subsequent to the acquisition of Schick for options that were vested and included in the determination of purchase price at the time of that acquisition.

**Table of Contents****7. Short-Term Debt and Current Portion of Long-Term Debt**

The components of short-term debt are as follows:

	March 31, 2010	September 30, 2009
	\$ 000s	
Accrued interest on long-term debt		2,781
Other short-term debt	2,988	1,907
	<b>\$ 2,988</b>	<b>\$ 4,688</b>

**8. Long-Term Debt**

The components of long-term debt are as follows:

	March 31, 2010	September 30, 2009
	\$ 000s	
Senior term loan, Tranche A1, variable rate repayable in November 2011	105,000	127,986
Senior term loan, Tranche A2, variable rate repayable in November 2011	259,336	343,872
Other debt		1,147
	<b>364,336</b>	<b>473,005</b>
Less current portion		2,781
	<b>\$ 364,336</b>	<b>\$ 470,224</b>

**Senior Term Loans**

On November 22, 2006, Sirona Dental Systems, Inc. entered into a Senior Facilities Agreement (the "Senior Facilities Agreement") as original guarantor, with all significant subsidiaries of Sirona as original borrowers and original guarantors. Initial borrowings under the Senior Facilities Agreement plus excess cash were used to retire the outstanding borrowings under the Company's previous credit facilities.

The Senior Facilities Agreement includes: (1) a term loan A1 in an aggregate principal amount of \$150 million (the "tranche A1 term loan") available to Sirona's subsidiary, Schick NY, as borrower; (2) a term loan A2 in an aggregate principal amount of Euro 275 million (the "tranche A2 term loan") available to Sirona's subsidiary, Sirona Dental Services GmbH, as borrower; and (3) a \$150 million revolving credit facility available to Sirona Dental Systems GmbH, Schick NY and Sirona Dental Services GmbH, as initial borrowers. The revolving credit facility is available for borrowing in Euro, U.S. Dollars, Yen or any other freely available currency agreed to by the facility agent. The facilities are made available on an unsecured basis. Subject to certain limitations, each European guarantor guarantees the performance of each European borrower, except itself, and each U.S. guarantor guarantees the performance of each U.S. borrower, except itself. There are no cross-border guarantees since all guarantees are by entities that have the same functional currency as the currency in which the respective guaranteed borrowing is denominated.



## **Table of Contents**

Each of the senior term loans are to be repaid in three annual installments beginning on November 24, 2009 and ending on November 24, 2011. Of the amounts borrowed under the term loan facilities, 15% was due on November 24, 2009, 15% was due on November 24, 2010 and 70% is due on November 24, 2011. The senior debt repayment tranche originally scheduled for November 24, 2009 was prepaid on May 11, 2009 in the amount of \$78.6 million, and the senior debt repayment tranche originally scheduled for November 24, 2010 was prepaid on March 31, 2010 in the amount of \$78.1 million. At the Company's current Debt Cover Ratio, the facilities bear interest of Euribor, for Euro-denominated loans, and Libor for the other loans, plus a margin of 45 basis points for both.

The Senior Facilities Agreement contains a margin ratchet. Pursuant to this provision, which applies from November 24, 2007 onwards, the applicable margin will vary between 90 basis points and 45 basis points per annum according to the Company's leverage multiple (i.e. the ratio of consolidated total net debt to consolidated adjusted EBITDA as defined in the Senior Facilities Agreement). Interest rate swaps were established for 66.6% of the interest until March 2010. These swaps expired on March 31, 2010 and were not renewed. The interest rate swaps fixed the LIBOR or EURIBOR element of interest payable on 66.7% of the principal amount of the loans for defined twelve and thirteen month interest periods over the lifetime of the swaps, respectively. The defined interest rates fixed for each twelve or thirteen month interest period ranged from 3.50% to 5.24%. Settlement of the swaps was required on a quarterly basis.

The Senior Facilities Agreement contains restrictive covenants that limit Sirona's ability to make loans, make investments (including in joint ventures), incur additional indebtedness, make acquisitions or pay dividends, subject to agreed-upon exceptions. The Company has agreed to certain financial debt covenants in relation to the financing. The covenants stipulate that the Company must maintain certain ratios in respect of interest payments and defined earnings measures. If the Company breaches any of the covenants, the loans will become repayable on demand.

Debt issuance costs of \$5.6 million were incurred in relation to the financing in November 2006 and were capitalized as deferred charges and are amortized using the effective interest method over the term of the loan.

## **9. Income Taxes**

For the first half of fiscal year 2010, an estimated effective tax rate of 20% has been applied, compared to an estimated effective tax rate of 28% for the first half of fiscal year 2009 and an effective tax rate for fiscal year 2009 of 14.7%. The estimated effective tax rate is primarily driven by the expected distribution of profits across different countries. Factors such as variances between the expected and actual distribution of profits for the remainder of the year could result in a deviation of the actual from the estimated tax rate.

With limited exception, the Company and its subsidiaries are no longer subject to U.S. federal, state and local or non-U.S. income tax examinations by taxing authorities for tax returns filed with respect to periods prior to fiscal 2005.

**Table of Contents****10. Income per Share**

The computation of basic and diluted income per share is as follows:

	Three months ended March 31,		Six months ended March 31,	
	2010	2009	2010	2009
	\$ 000s (except per share amounts)		\$ 000s (except per share amounts)	
Net income attributable to Sirona Dental Systems, Inc. common shareholders	\$ 17,539	\$ 595	\$ 48,714	\$ 6,154
Weighted average shares outstanding basic	55,122,944	54,818,604	55,044,832	54,856,537
Dilutive effect of stock options	1,487,167	225,490	1,445,731	246,596
Weighted average shares outstanding diluted	56,610,111	55,044,094	56,490,563	55,103,133
Income per share				
Basic	\$ 0.32	\$ 0.01	\$ 0.88	\$ 0.11
Diluted	\$ 0.31	\$ 0.01	\$ 0.86	\$ 0.11

Stock options to acquire 80,250 and 1,231,950 shares of Sirona's common stock that were granted in connection with the Company's stock option plans were not included in the computation of diluted earnings per share for the three and six months ended March 31, 2010 and 2009, respectively, because the options' underlying exercise prices were greater than the average market price of Sirona's common stock for the respective period.

**11. Product Warranty**

The following table provides the changes in the product warranty accrual for the three and six months ended March 31, 2010 and 2009:

	Three months ended March 31,		Six months ended March 31,	
	2010	2009	2010	2009
	\$ 000s		\$ 000s	
Balance at beginning of the period	\$ 12,083	\$ 12,381	\$ 11,506	\$ 12,176
Accruals for warranties issued during the period	4,828	4,934	11,549	10,276
Warranty settlements made during the period	(4,570)	(4,986)	(10,512)	(9,832)
Translation adjustment	(715)	(523)	(917)	(814)
Balance at the end of the period	\$ 11,626	\$ 11,806	\$ 11,626	\$ 11,806

**Table of Contents****12. Pension Plans**

Components of net periodic benefit costs are as follows:

	Three months ended March 31,		Six months ended March 31,	
	2010	2009	2010	2009
	\$ 000s		\$ 000s	
Service cost, net	\$ 65	\$ 70	\$ 135	\$ 140
Interest cost	635	634	1,312	1,273
Amortization of actuarial gains	(112)	(117)	(233)	(235)
Net periodic benefit cost	\$ 588	\$ 587	\$ 1,214	\$ 1,178

**13. Net Other Operating Income**

Net other operating income for the three and six months ended March 31, 2010 was \$3.4 million and \$5.9 million, respectively, compared to net other operating income/(loss) of \$(0.3) million and \$3.2 million, respectively, for the three and six months ended March 31, 2009. In both periods, net other operating income included \$2.5 million (three months) and \$5.0 million (six months), respectively, of income resulting from the amortization of the deferred income relating to the Patterson exclusivity payment. In the three and six months ended March 31, 2010, net other operating income included a gain from the sale of a subsidiary in Italy of \$0.9 million. In the three and six months ended March 31, 2009, net other operating income included a gain from the sale of a sales and service subsidiary in Spain of \$1.0 million. In the three and six months ended March 31, 2009, net other operating income included restructuring costs of \$2.8 million.

**Restructuring Costs**

In fiscal year 2009, we incurred restructuring costs of \$8.2 million included in net other operating income for certain actions to reduce operating costs and thereby to improve the efficiency of our organization.

As of September 30, 2009, we had accrued restructuring costs in the amount of \$4.2 million. No further restructuring costs were incurred for the three and six months ended March 31, 2010. The development of restructuring costs in the current fiscal year is presented in the following table:

	Accrual at October 1, 2009	Restructuring Costs	Payments \$ 000s	Currency translation adjustment	Accrual at March 31, 2010
Severance costs	\$ 3,660	\$	\$ 1,887	\$ (222)	\$ 1,551
Consulting costs	581		585	4	
Total	\$ 4,241	\$	\$ 2,472	\$ (218)	\$ 1,551

The residual amount of \$1.6 million is expected to be paid in fiscal year 2010.

**Table of Contents****14. Derivative Instruments and Hedging Strategies**

Our operations are exposed to market risks from changes in foreign currency exchange rates and interest rates. In the normal course of business, these risks are managed through a variety of strategies, including the use of derivatives.

**Interest Rate Risk**

The Company is exposed to interest rate risk associated with fluctuations in the interest rates on its variable interest rate debt. In order to manage this risk, the Company entered into interest rate swap agreements that convert the debt's variable interest rate to a fixed interest rate. While these swap agreements were considered to be economic hedges, they are not designated as hedging instruments under ASC 815.

Interest rate swaps were established for 66.6% of the interest until March 2010. These swaps expired on March 31, 2010 and were not renewed. The interest rate swaps fixed the LIBOR or EURIBOR element of interest payable on 66.7% of the principal amount of the loans for defined twelve and thirteen month interest periods over the lifetime of the swaps, respectively. The defined interest rates fixed for each twelve or thirteen month interest period ranged from 3.50% to 5.24%. Settlement of the swaps was required on a quarterly basis.

**Foreign Currency Exposure**

Although the U.S. Dollar is Sirona's reporting currency, its functional currency varies depending on the country of operation. During the periods under review, particularly the U.S. Dollar/Euro exchange rate fluctuated significantly, thereby impacting Sirona's financial results.

In order to manage foreign currency exposures, the Company enters into foreign exchange forward contracts (USD, AUD, and JPY). As with its interest rate swap instruments, the Company enters into forward contracts that are considered to be economic hedges, which are not considered hedging instruments under ASC 815.

As of March 31, 2010, these contracts had notional amounts totaling \$72.7 million. These agreements are relatively short-term (generally six months).

The fair value carrying amount of the Company's derivative instruments at March 31, 2010 is described in Note 15 Fair Value Measurements.

The location and amount of gains and losses from the fair value changes of derivative instruments reported in our condensed consolidated income statement were as follows:

	Location of (Gain)/Loss Recognized in Income on Derivative	For the three months ended		For the six months ended	
		March 31, 2010	March 31, 2009	March 31, 2010	March 31, 2009
Derivatives Not Designated as Hedging Instruments		Amount of (Gain)/Loss Recognized in Income on Derivative	Amount of (Gain)/Loss Recognized in Income on Derivative	Amount of (Gain)/Loss Recognized in Income on Derivative	Amount of (Gain)/Loss Recognized in Income on Derivative
Interest rate swap contracts	(Gain)/Loss on derivative instruments	\$ (2,937)	\$ 507	\$ (6,364)	\$ 8,566
Foreign exchange contracts	(Gain)/Loss on derivative instruments	1,225	(747)	3,629	(3,839)
Total		\$ (1,712)	\$ (240)	\$ (2,735)	\$ 4,727

**15. Fair Value Measurements and Financial Instruments**

On October 1, 2008, the Company adopted the provisions of ASC 820, Fair Value Measurements and Disclosures, for assets and liabilities that are recognized or disclosed at fair value in the financial statements on a recurring basis. ASC 820 defines fair value as the price that would be

## Edgar Filing: SIRONA DENTAL SYSTEMS, INC. - Form 10-Q

received from selling an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. When determining the fair value measurements for assets and liabilities that are required to be recorded or disclosed at fair value, the Company considers the principal or most advantageous market in which it would transact and the market-based risk measurements or assumptions that market participants would use in pricing the asset or liability, such as inherent risk, transfer restrictions, and the credit risk of the Company and counterparties to the arrangement.

ASC 820 establishes a fair value hierarchy that prioritizes the inputs to valuation techniques used to measure fair value into three levels. A financial instrument's categorization within the fair value hierarchy is based upon the lowest

**Table of Contents**

level of input that is available and significant to the fair value measurement. ASC 820 establishes and prioritizes the following three levels of inputs that may be used to measure fair value:

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

Level 2 - Observable inputs other than quoted prices in active markets for identical assets and liabilities, quoted prices for identical or similar assets or liabilities in inactive markets, or other inputs that are observable or can be corroborated by observable market data for substantially the full term of the assets or liabilities.

Level 3 - Inputs that are generally unobservable and typically reflect management's estimates of assumptions that market participants would use in pricing the asset or liability.

**Assets/Liabilities Measured at Fair Value on a Recurring Basis**

The following table presents the Company's assets and liabilities related to foreign exchange contracts measured at fair value on a recurring basis as of March 31, 2010:

	Quoted Prices in Active Markets for Identical Instruments (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Total
	\$ 000s			
<b>Assets</b>				
Derivative Assets	\$	\$ 125	\$	\$ 125
<b>Liabilities</b>				
Derivative Liabilities	\$	\$ (2,201)	\$	\$ (2,201)
<b>Total</b>	\$	\$ (2,076)	\$	

In the Company's March 31, 2010 Consolidated Balance Sheet, derivative assets and derivative liabilities are classified as prepaid expenses and other current assets and accrued liabilities and deferred income, respectively.

The Company did not elect the fair value option for any eligible financial instruments.

**Fair value of financial instruments**

Financial instruments consist of cash, cash equivalents, accounts receivable, accounts payable, and foreign currency forward contracts. The carrying amounts of cash, cash equivalents, accounts receivable and accounts payable approximate their respective fair values because of the short-term nature of these items. The fair value of foreign currency forward contracts is estimated by obtaining quotes from financial institutions.

**16. Segment Reporting**

The following tables reflect the results of the Company's reportable segments under the Company's management reporting system. The segment performance measure used to monitor segment performance is gross profit (Segment Performance Measure) excluding the impact of the acquisition of control of the Sirona business by Sirona Holdings Luxco S.C.A. (Luxco), a Luxembourg-based holding entity owned by funds managed by Madison Dearborn Partners (MDP), Beecken Petty O'Keefe and management of Sirona, through a leveraged buyout transaction on June 30, 2005 (the MDP Transaction) and the acquisition of Schick (the Exchange) in 2006. This measure is considered by management to better reflect the performance of each segment as it eliminates the need to allocate centrally incurred costs and significant purchase accounting impacts that the Company does not believe are representative of the performance of the segments. Furthermore, the Company monitors performance geographically by region. As the Company manages its business on both a product and a geographical basis, U.S. GAAP requires segmental disclosure based on product information.



**Table of Contents**

	Three months ended March 31,		Six months ended March 31,	
	2010	2009	2010	2009
	\$ 000s		\$ 000s	
<b>Revenue external</b>				
Dental CAD/CAM Systems	\$ 66,306	\$ 62,340	\$ 140,122	\$ 116,023
Imaging Systems	59,535	49,451	130,516	114,435
Treatment Centers	39,857	33,050	83,708	72,127
Instruments	24,196	19,823	50,253	41,727
<b>Total</b>	<b>\$ 189,894</b>	<b>164,664</b>	<b>404,599</b>	<b>344,312</b>
Electronic Center and corporate	242	158	360	231
<b>Total</b>	<b>\$ 190,136</b>	<b>\$ 164,822</b>	<b>\$ 404,959</b>	<b>\$ 344,543</b>
<b>Revenue internal</b>				
Dental CAD/CAM Systems	\$	\$	\$	\$
Imaging Systems	11	5	15	27
Treatment Centers	8	4	16	15
Instruments	2,485	2,133	4,843	4,367
Intercompany elimination	(2,504)	(2,142)	(4,874)	(4,409)
<b>Total</b>	<b>\$</b>			
Electronic Center and corporate	5,294	4,418	10,431	9,790
Intercompany elimination	(5,294)	(4,418)	(10,431)	(9,790)
<b>Total</b>	<b>\$</b>	<b>\$</b>	<b>\$</b>	<b>\$</b>
<b>Revenue total</b>				
Dental CAD/CAM Systems	\$ 66,306	\$ 62,340	\$ 140,122	\$ 116,023
Imaging Systems	59,546	49,456	130,531	114,462
Treatment Centers	39,865	33,054	83,724	72,142
Instruments	26,681	21,956	55,096	46,094
<b>Total</b>	<b>\$ 192,398</b>	<b>166,806</b>	<b>409,473</b>	<b>348,721</b>
Electronic Center and corporate	5,536	4,576	10,791	10,021
<b>Total</b>	<b>\$ 197,934</b>	<b>\$ 171,382</b>	<b>\$ 420,264</b>	<b>\$ 358,742</b>
<b>Segment performance measure</b>				
Dental CAD/CAM Systems	\$ 47,498	\$ 43,414	\$ 98,434	\$ 80,961
Imaging Systems	35,878	29,160	79,176	68,012
Treatment Centers	16,516	12,311	34,676	27,034
Instruments	11,114	8,947	23,423	18,927
<b>Total</b>	<b>\$ 111,006</b>	<b>93,832</b>	<b>235,709</b>	<b>194,934</b>
Electronic Center and corporate	2,760	(959)	5,186	1,136
<b>Total</b>	<b>\$ 113,766</b>	<b>\$ 92,873</b>	<b>\$ 240,895</b>	<b>\$ 196,070</b>



Edgar Filing: SIRONA DENTAL SYSTEMS, INC. - Form 10-Q

<b>Depreciation and amortization expense</b>				
Dental CAD/CAM Systems	\$ 1,403	\$ 1,151	\$ 2,814	\$ 2,128
Imaging Systems	1,257	1,152	2,635	2,324
Treatment Centers	1,608	1,386	3,327	2,819
Instruments	802	503	1,708	1,268
<b>Total</b>	<b>\$ 5,070</b>	<b>4,192</b>	<b>10,484</b>	<b>8,539</b>
Electronic Center and corporate	936	599	1,167	861
<b>Total</b>	<b>\$ 6,006</b>	<b>\$ 4,791</b>	<b>\$ 11,651</b>	<b>\$ 9,400</b>

**Table of Contents****Reconciliation of the results of the segment performance measure to the consolidated statements of operations**

The following table and discussion provide a reconciliation of the total results of operations of the Company's business segments under management reporting to the consolidated financial statements. The differences shown between management reporting and U.S. GAAP for the three and six month periods ended March 31, 2010 and 2009 are mainly due to the impact of purchase accounting. Purchase accounting effects are not included in gross profit as the Company does not believe these to be representative of the performance of each segment.

Inter-segment transactions are based on amounts which management believes are approximate to the amounts of transactions with unrelated third parties.

	Three months		Six months	
	ended March 31,		ended March 31,	
	2010	2009	2010	2009
	\$ 000s		\$ 000s	
<b>Revenue</b>				
Total segments (external)	\$ 189,894	\$ 164,664	\$ 404,599	\$ 344,312
Electronic center and corporate	242	158	360	231
Consolidated revenue	<b>190,136</b>	<b>164,822</b>	<b>404,959</b>	<b>344,543</b>
<b>Depreciation and amortization</b>				
Total segments	5,070	4,192	10,484	8,539
Differences management reporting vs. US GAAP, electronic center and corporate	15,740	18,445	32,105	36,074
Consolidated depreciation and amortization	<b>20,810</b>	<b>22,637</b>	<b>42,589</b>	<b>44,613</b>
<b>Segment performance measure</b>				
Total segments	111,006	93,832	235,709	194,934
Differences management reporting vs. US GAAP, electronic center and corporate	(11,673)	(13,517)	(24,006)	(27,618)
Consolidated gross profit	<b>99,333</b>	<b>80,315</b>	<b>211,703</b>	<b>167,316</b>
Selling, general and administrative expense	60,354	56,048	120,206	113,470
Research and development	11,690	10,043	23,155	21,101
Provision for doubtful accounts and notes receivable	72	221	136	446
Net other operating income	(3,408)	270	(5,908)	(3,191)
(Gain)/loss on foreign currency transactions, net	5,049	7,077	4,416	10,669
(Gain)/loss on derivative instruments	(1,712)	(240)	(2,735)	4,727
Interest expense, net	4,141	5,593	9,343	11,657
Other expense	404		784	
<b>Income before taxes</b>	<b>\$ 22,743</b>	<b>\$ 1,303</b>	<b>\$ 62,306</b>	<b>\$ 8,437</b>

**17. Related parties****Sirona Holdings S.C.A. Luxembourg ( Luxco )**

The Company and Luxco, a significant owner of the Company, are parties to an advisory services agreement that was automatically renewed for a one-year term on October 1, 2009. Under the agreement, which became effective October 1, 2005, Sirona pays an annual fee to Luxco of 325 (approximately \$438), and Luxco provides to Sirona certain advisory services regarding the structure, terms and condition of debt offerings by Sirona, financing sources and options, business development and other services. In addition, pursuant to an agreement between Luxco and MDP IV Offshore GP, LP, MDP IV Offshore GP, LP provides these services to the Company in exchange for a fee from Luxco of 324.6.

## Edgar Filing: SIRONA DENTAL SYSTEMS, INC. - Form 10-Q

In December 2009, Luxco sold 7,100,000 shares pursuant to an underwritten follow-on public offering. The Company incurred \$0.4 million of costs pursuant to the terms of a registration rights agreement.

In February 2010, Luxco sold 7,000,000 shares pursuant to an underwritten follow-on public offering. The Company incurred \$0.4 million of costs pursuant to the terms of a registration rights agreement.

---

**Table of Contents**

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

Management's Discussion and Analysis of Financial Condition and Results of Operations (MD&A) should be read in conjunction with the Condensed Consolidated Financial Statements included elsewhere in this Report and the MD&A included in our Annual Report on Form 10-K for the fiscal year ended September 30, 2009. Actual results and the timing of certain events may differ significantly from those projected in such forward-looking statements due to a number of factors, including those set forth in Results of Operations in this Item and elsewhere in this Report. All amounts are reported in thousands of U.S. Dollars (\$), except as otherwise disclosed.

This report contains forward-looking statements that involve risk and uncertainties. All statements, other than statements of historical facts, included in this report regarding the Company, its financial position, products, business strategy and plans and objectives of management of the Company for future operations, are forward-looking statements. When used in this report, words such as anticipate, believe, estimate, expect, intend, objectives, plans and similar expressions, or the negatives thereof or variations thereon or comparable terminology as they relate to the Company, its products or its management, identify forward-looking statements. Such forward-looking statements are based on the beliefs of the Company's management, as well as assumptions made by and information currently available to the Company's management. Actual results could differ materially from those contemplated by the forward-looking statements as a result of various factors, including, but not limited to, those contained in the Risk Factors set forth in Part I, Item 1A of our Annual Report on Form 10-K for the fiscal year ended September 30, 2009. All forward looking statements speak only as of the date of this report and are expressly qualified in their entirety by the cautionary statements included in this report. We undertake no obligation to update or revise forward-looking statements which may be made to reflect events or circumstances that arise after the date made or to reflect the occurrence of unanticipated events other than required by law.

**Overview**

Sirona Dental Systems Inc. ( Sirona or the Company ) is the leading manufacturer of high-quality, technologically advanced dental equipment, and is focused on developing, manufacturing and marketing innovative systems and solutions for dentists around the world. The Company is uniquely positioned to benefit from several trends in the global dental industry, such as technological innovation, increased use of CAD/CAM systems in restorative dentistry, the shift to digital imaging, favorable demographic trends and growing patient focus on dental health and cosmetic appearance. The Company has its headquarters in Long Island City, New York and its largest facility in Bensheim, Germany.

Sirona has a long tradition of innovation in the dental industry. The Company introduced the first dental electric drill 130 years ago, the first dental X-ray unit 100 years ago, the first dental computer-aided design/computer-aided manufacturing ( CAD/CAM ) system 24 years ago, and numerous other significant innovations in dentistry. Sirona continues to make significant investments in research and development, and its track record of innovative and profitable new products continues today with numerous recent product launches including: the inEOS Blue (launched in January 2010), the Galileos and CEREC combination (launched in September 2009), the CEREC AC unit (launched in January 2009), the Galileos Compact 3D imaging system (launched in July 2008), the TENEO treatment center (launched in July 2008) and the CAD/CAM milling unit MC XL (launched in fiscal year 2007).

Sirona manages its business on both a product and geographic basis and has four segments: Dental CAD/CAM Systems, Imaging Systems, Treatment Centers, and Instruments. Sirona has the broadest product portfolio in the industry, and is capable of fully outfitting and integrating a dental practice. Products from each category are marketed in all geographical sales regions.

The Company's business has grown substantially over the past five years, driven by numerous high-tech product introductions, a continued expansion of its global sales and service infrastructure, strong relationships with key distribution partners, namely Patterson and Henry Schein, and an international dealer network. Patterson and Henry Schein accounted for 31% and 17%, respectively, of Sirona's global revenues for the six month period ended March 31, 2010.

The U.S. market is the largest individual market for Sirona, followed by Germany. Between fiscal 2004 and 2009, the Company increased U.S. revenues from \$88.2 million to \$221.2 million, driven by innovative products, particularly in the CAD/CAM and imaging segments, and the Schick acquisition. Patterson made a payment of \$100 million to Sirona in July 2005 in exchange for the exclusive distribution rights for CAD/CAM products in the U.S. and Canada until 2017 (the Patterson exclusivity payment ). The amount received was recorded as deferred income and is being

---

## **Table of Contents**

recognized on a straight-line basis that commenced at the beginning of the extension of the exclusivity period in fiscal 2008.

In addition to strong U.S. market growth, Sirona has pursued expansion in non-U.S. and non-German markets. Between fiscal 2004 and 2009, the Company increased revenues in non-U.S. and non-German markets from \$190.9 million to \$344.8 million. To support this growth, Sirona expanded its local presence and distribution channels by establishing sales and service locations in Japan, Australia, China, Italy, France, and the UK. The expansion helped to increase market share but also contributed to higher SG&A expenses. Due to the international nature of the Company's business, movements in global foreign exchange rates have a significant effect on financial results.

The weak global economy in 2009 resulted in a challenging environment for selling dental technology, which impacted Sirona's revenues. In fiscal year 2009, U.S. revenues were flat and international revenues decreased 8.2% (up 1.8% on a constant currency basis). During the year, the Company introduced breakthrough advancements in dental care, led by the CEREC AC. In the context of the weak global economy, the Company implemented a near-term cost savings and deferral plan for 2009 and separately undertook certain targeted actions to reduce operating costs and to increase efficiency on a longer term basis. We finished the year with a robust fourth quarter with constant currency revenue growth of 8.4%, driven by our innovative high-tech product line.

The positive trends from the fourth quarter of fiscal year 2009 continued into the first half of fiscal 2010. This development was driven by our recent innovative product launches and our technologically advanced product portfolio. Our net income benefited from robust sales growth, margin expansion, expense management initiatives, and deleveraging. Our targeted cost saving actions are on plan, and we expect to begin reinvesting a part of these cost savings as we move through the second half of the year. Cash flow from operations was strong, mainly driven by operating income.

### **Significant Factors that Affect Sirona's Results of Operations**

#### ***The MDP Transaction and the Exchange***

The assets and liabilities acquired in the MDP Transaction and the Exchange were partially stepped up to fair value, and a related deferred tax liability was recorded. The excess of the total purchase price over the fair value of the net assets acquired, including IPR&D, which were expensed at the date of closing of the MDP Transaction and the Exchange, was allocated to goodwill and is subject to periodic impairment testing.

Sirona's cost of goods sold, research and development, selling, general and administrative expense and operating results have been and will continue to be materially affected by depreciation and amortization costs resulting from the step-up to fair value of Sirona's assets and liabilities.

#### ***Fluctuations in U.S. Dollar/Euro Exchange Rate***

Although the U.S. Dollar is Sirona's reporting currency, its functional currency varies depending on the country of operation. For the six months ended March 31, 2010, approximately 45% of Sirona's revenue and approximately 71% of its expenses were denominated in Euros. During the periods under review, the U.S. Dollar/Euro exchange rate has fluctuated significantly, thereby impacting Sirona's financial results. Between October 1, 2008 and March 31, 2010, the U.S. Dollar/Euro exchange rates used to calculate items included in Sirona's financial statements varied from a low of 1.2439 to a high of 1.5121 and as of March 31, 2010 and September 30, 2009 were 1.3472 and 1.4662, respectively. Although Sirona does not apply hedge accounting, Sirona has entered into foreign exchange forward contracts to manage foreign currency exposure. As of March 31, 2010, these contracts had notional amounts totaling \$72.7 million. As these agreements are relatively short-term (generally six months), continued fluctuation in the U.S. Dollar/Euro exchange rate could materially affect Sirona's results of operations.

Certain revenue information under "Results of Operations" below is presented on a constant currency basis. This information is a non-GAAP financial measure. Sirona supplementally presents revenue on a constant currency basis because it believes this information facilitates a comparison of Sirona's operating results from period to period without regard to changes resulting solely from fluctuations in currency rates. Sirona calculates constant currency revenue growth by comparing current period revenues to prior period revenues with both periods converted at the U.S. Dollar/Euro average foreign exchange rate for each month of the current period. The average monthly exchange rate for the six months ended March 31, 2010 was \$1.43 and varied from \$1.48102 to \$1.35825. For the three and six months

## **Table of Contents**

ended March 31, 2009, an average quarterly foreign exchange rate converting Euro-denominated revenues into U.S. Dollars of \$1.30799 and \$1.31347, respectively, was applied.

Loans made to Sirona under the Senior Facilities Agreement entered into November 22, 2006 are denominated in the functional currency of the respective borrowers. See *Liquidity and Capital Resources* for a discussion of our Senior Facilities Agreement. However, intra-group loans are denominated in the functional currency of only one of the parties to the loan agreements. Where intra-group loans are of a long-term investment nature, the potential non-cash fluctuations in exchange rates are reflected within other comprehensive income. These fluctuations may be significant in any period due to changes in the exchange rates between the Euro and the U.S. Dollar.

### ***Fluctuations in Quarterly Operating Results***

Sirona's quarterly operating results have varied in the past and are likely to vary in the future. These variations result from a number of factors, many of which are substantially outside its control, including:

the timing of new product introductions by us and our competitors;

the timing of industry tradeshows;

changes in relationships with distributors;

developments in government reimbursement policies;

changes in product mix;

our ability to supply products to meet customer demand;

fluctuations in manufacturing costs;

income tax incentives;

currency fluctuations; and

general economic conditions, as well as those specific to the healthcare industry and related industries.

Due to the variations which Sirona has experienced in its quarterly operating results, it does not believe that period-to-period comparisons of results of operations of Sirona are necessarily meaningful or reliable as indicators of current and future performance.

### ***Effective Tax Rate***

Sirona's effective tax rate may vary significantly from period to period. Various factors may have a favorable or unfavorable impact on our effective tax rate. These factors may include, but are not limited to, the actual distribution of profits across the different jurisdictions, tax planning initiatives, changes in local tax rates, as well as the timing and deductibility of expenses for tax purposes.



## **Table of Contents**

### **Results of Operations**

#### ***Three Months Ended March 31, 2010 Compared to Three Months Ended March 31, 2009***

##### ***Revenue***

Revenue for the three months ended March 31, 2010 was \$190.1 million, an increase of \$25.3 million, or 15.4%, compared with the three months ended March 31, 2009. On a constant currency basis, adjusting for the fluctuations in the U.S. Dollar/Euro exchange rate, total revenue increased by 11.0%. By segment, Instruments increased 22.0% (up 15.1% on a constant currency basis), Treatment Centers increased 20.7% (up 13.9% on a constant currency basis), Imaging Systems increased 20.4% (up 16.6% on a constant currency basis), and CAD/CAM increased 6.3% (up 3.4% on a constant currency basis).

We were able to grow revenues in all segments due to the demand for our innovative products, and we continue to benefit from our global sales and service infrastructure. Our products enable dental professionals to improve their clinical results and to increase the profitability of their practices. Our new innovative products, including CEREC AC, Galileos, and Teneo, continued to show strong demand.

Revenue in the United States for the three months ended March 31, 2010 increased by 7.7% compared to the prior year period, driven by the Imaging segment.

Revenue outside the United States increased by 19.2%. On a constant currency basis, adjusting for the fluctuations in the U.S. Dollar/Euro exchange rate, these revenues increased by 12.5%. Revenue growth was particularly driven by Germany, Australia, France, China, and The Netherlands.

##### ***Cost of Sales***

Cost of sales for the three months ended March 31, 2010 was \$90.8 million, an increase of \$6.3 million, or 7.4%, as compared with the three months ended March 31, 2009. The increase was due to higher sales. Gross profit as a percentage of revenue was 52.2% compared to 48.7% in the prior year. Cost of sales included amortization and depreciation expense resulting from the step-up to fair values of tangible and intangible assets of \$14.2 million as well as non-cash option expense of \$0.03 million for the three months ended March 31, 2010, compared to amortization and depreciation expense resulting from the step-up to fair values of tangible and intangible assets of \$16.1 million as well as non-cash option expense of \$0.1 million for the three months ended March 31, 2009. Excluding these amounts, costs of sales as a percentage of revenue was 40.2% for the three months ended March 31, 2010 compared with 41.5% for the three months ended March 31, 2009 and therefore gross profit as a percentage of revenue was 59.8% compared to 58.5%. The expansion of gross profit margin was driven by product and regional mix across all segments.



---

**Table of Contents*****Selling, General and Administrative***

SG&A expense for the three months ended March 31, 2010 was \$60.4 million, an increase of \$4.3 million, or 7.7%, as compared with the three months ended March 31, 2009. SG&A expense included amortization and depreciation resulting from the step-up to fair values of tangible and intangible assets of \$0.8 million, as well as non-cash option expense in the amount of \$4.0 million for the three months ended March 31, 2010, compared with \$1.0 million and \$3.8 million, respectively, for the three months ended March 31, 2009. Excluding these amounts, as a percentage of revenue, SG&A expense decreased to 29.2% for the three months ended March 31, 2010 as compared with 31.1% for the three months ended March 31, 2009. The development of SG&A expenses is mainly driven by higher sales.

***Research and Development***

R&D expense for the three months ended March 31, 2010 was \$11.7 million, an increase of \$1.6 million, or 16.4%, as compared with the three months ended March 31, 2009. The increase is mainly driven by the timing of projects. R&D expense included non-cash stock option expense in the amount of \$0.1 million and \$0.1 million, respectively, for the three months ended March 31, 2010 and March 31, 2009. Excluding these amounts, as a percentage of revenue, R&D expense was 6.1% for the three months ended March 31, 2010, compared with 6.0% for the three months ended March 31, 2009.

***Net other operating (income)/loss and restructuring costs***

Net other operating income for the three months ended March 31, 2010 was \$3.4 million, compared to a net other operating loss of \$0.3 million for the three months ended March 31, 2009. In both periods net other operating (income)/loss included \$2.5 million income resulting from the amortization of the deferred income relating to the Patterson exclusivity payment. In the three months ended March 31, 2010, net other operating income included a gain from the sale of a subsidiary in Italy of \$0.9 million. In the three months ended March 31, 2009, net other operating income included a gain from the sale of a sales and services subsidiary in Spain of \$1.0 million.

In December 2008 we announced certain actions to reduce operating costs and thereby to improve the efficiency of our organization. These actions predominantly relate to overhead functions in Germany including increased automation of our processes, the optimization of the supply chain as well as increased efficiency in our administrative functions.

For the three months period ended March 31, 2010, we did not incur any additional restructuring costs. For the three months period ended March 31, 2009, we incurred restructuring costs of \$ 2.8 million (\$2.0 million after taxes), consisting of employee severance pay and benefits and outside consulting fees directly related to the restructuring plan.

***Loss on Foreign Currency Transactions***

Loss on foreign currency transactions for the three months ended March 31, 2010 amounted to \$5.0 million compared to a loss of \$7.1 million for the three months ended March 31, 2009. For the three months ended March 31, 2010, the loss included an unrealized non-cash foreign currency loss of \$5.1 million on the U.S. Dollar denominated deferred income, resulting from the currency revaluation adjustment of the Patterson exclusivity payment and a \$4.4 million loss due to the currency revaluation of U.S. Dollar denominated short-term intra-group loans. For the three months ended March 31, 2009, the loss included an unrealized non-cash foreign currency loss of \$4.0 million on the U.S. Dollar denominated deferred income resulting from the currency revaluation adjustment of the Patterson exclusivity payment and a \$2.5 million loss due to the currency revaluation of U.S. Dollar denominated short-term intra-group loans.

***Gain on Derivative Instruments***

Gain on derivative instruments for the three months ended March 31, 2010 amounted to \$1.7 million compared to a gain of \$0.2 million for the three months ended March 31, 2009. For the three months ended March 31, 2010, the gain included a non-cash gain of \$2.9 million on interest swaps, as well as a non-cash loss on foreign currency hedges of \$1.2 million. The gain for the three months ended March 31, 2009 included an unrealized non-cash loss of \$0.5 million on interest swaps, as well as a non-cash gain on foreign currency hedges of \$0.7 million.

## **Table of Contents**

### ***Interest Expense***

Net interest expense for the three months ended March 31, 2010 was \$4.1 million, compared to \$5.6 million for the three months ended March 31, 2009. This decrease resulted from lower interest rates and lower overall debt levels.

### ***Other Expense***

Professional fees of \$0.4 million, related to the February 2010 follow-on public offering, were incurred in the second quarter of fiscal year 2010.

### ***Income Tax Provision***

The income tax provision for the three months ended March 31, 2010 was \$4.5 million, compared to \$0.4 million for the three months ended March 31, 2009. For the second quarter of fiscal year 2010, an estimated effective tax rate of 20% has been applied, compared to an estimated effective tax rate of 28% for the second quarter of fiscal 2009, and an effective tax rate of 14.7% in fiscal 2009. The estimated effective tax rate is primarily driven by the expected distribution of profits across different countries.

### ***Net Income***

Sirona's net income for the three months ended March 31, 2010 was \$17.5 million, an increase of \$16.9 million, as compared with the three months ended March 31, 2009. Second quarter 2010 net income included amortization and depreciation expense resulting from the step-up to fair values of intangible and tangible assets related to past business combinations (i.e. the Exchange and the MDP transaction - deal related amortization and depreciation) of \$15.1 million (\$12.1 million net of tax), unrealized, non-cash foreign currency losses on the deferred income from the Patterson exclusivity payment of \$5.1 million (\$4.1 million net of tax) and losses on short-term intra-group loans of \$4.4 million (\$3.5 million net of tax).

Sirona's net income for the three month period ended March 31, 2009 included deal related amortization and depreciation of \$17.3 million (\$12.5 million net of tax), currency revaluation losses on the deferred income from the Patterson exclusivity payment of \$4.0 million (\$2.9 million net of tax) and revaluation losses on short-term intra-group loans of \$2.5 million (\$1.8 million net of tax).

Option expense was \$4.1 million (\$3.3 million net of tax) in the second quarter of 2010, compared to \$4.0 million (\$2.9 million net of tax) in the prior year period.

---

**Table of Contents**

***Six Months Ended March 31, 2010 Compared to Six Months Ended March 31, 2009***

***Revenue***

Revenue for the six months ended March 31, 2010 was \$405.0 million, an increase of \$60.4 million, or 17.5%, as compared with the six months ended March 31, 2009. On a constant currency basis, adjusting for the fluctuations in the U.S. Dollar/Euro exchange rate, total revenue increased by 10.9%. By segment, CAD/CAM Systems increased 20.8% (up 15.5% on a constant currency basis), Instruments increased 20.4% (up 10.6% on a constant currency basis), Treatment Centers increased 16.1% (up 6.6% on a constant currency basis), and Imaging Systems increased 14.1% (up 9.2% on a constant currency basis).

We were able to grow revenues in all segments due to the demand for our innovative product offering, and we continue to benefit from our global sales and service infrastructure. Our products enable dental professionals to improve their clinical results and to increase the profitability of their practices. Our new innovative products, including CEREC AC, Galileos, and Teneo, continued to show strong demand.

Revenue in the United States for the six months ended March 31, 2010 increased by 10% compared to the same period of the prior year.

Revenue outside the United States increased by 21.4%. On a constant currency basis, adjusting for the fluctuations in the U.S. Dollar/Euro exchange rate, revenue increased by 11.3%. Revenue growth was particularly driven by Germany and Asia Pacific.

***Cost of Sales***

Cost of sales for the six months ended March 31, 2010 was \$193.3 million, an increase of \$16.0 million, or 9.0%, as compared with the six months ended March 31, 2009. The increase in cost of sales is due to higher sales. Cost of sales included amortization and depreciation expense resulting from the step-up to fair values of tangible and intangible assets of \$29.2 million as well as non-cash option expense of \$0.1 million for the six months ended March 31, 2010, compared to amortization and depreciation expense resulting from the step-up to fair values of tangible and intangible assets of \$32.3 million and non-cash option expense of \$0.2 million for the six months ended March 31, 2009. Excluding these amounts, costs of sales as a percentage of revenue decreased to 40.5% for the six months ended March 31, 2010 compared with 42.1% for the six months ended March 31, 2009 and gross profit as a percentage of revenue increased by 1.6 percentage points to 59.5% from 57.9%. The positive development of the gross profit margin was mainly due to product mix across all segments.

***Selling, General and Administrative***

For the six months ended March 31, 2010, SG&A expense was \$120.2 million, an increase of \$6.7 million, or 5.9%, as compared with the six months ended March 31, 2009. SG&A expense included amortization and depreciation resulting from the step-up to fair values of tangible and intangible assets of \$1.7 million as well as non-cash option expense in the amount of \$7.9 million for the six months ended March 31, 2010, compared with \$2.0 million and \$7.4 million, respectively, for the six months ended March 31, 2009. Excluding these amounts, as a percentage of revenue, SG&A expense decreased to 27.3% for the six months ended March 31, 2010 as compared with 30.2% for the six months ended March 31, 2009. The increase in SG&A is mainly driven by variations in the U.S. Dollar/Euro exchange rate as most of the expenses were denominated in Euro, whereas the decrease as a percentage of sales is mainly due to higher sales and cost savings.

***Research and Development***

R&D expense for the six months ended March 31, 2010 was \$23.2 million, an increase of \$2.1 million, or 9.7%, as compared with the six months ended March 31, 2009. R&D expense included non-cash stock option expense in the amount of \$0.1 million and \$0.3 million, respectively, for the six months ended March 31, 2010 and March 31, 2009.

Excluding these amounts, R&D expense was 5.7% of revenues for the six months ended March 31, 2010, compared with 6.0% for the six months ended March 31, 2009. The increase was primarily due to variations in the U.S. Dollar/Euro exchange rates as most of the expenses were denominated in Euro as well as the project timing.

## **Table of Contents**

### ***Net other operating (income)/loss and restructuring costs***

Net other operating income for the six months ended March 31, 2010 was \$5.9 million, compared to \$3.2 million for the six months ended March 31, 2009. In both periods net other operating income included \$5.0 million resulting from the amortization of the deferred income relating to the Patterson exclusivity payment. In the six months ended March 31, 2010 net other operating income also included a gain from the sale of a subsidiary in Italy of \$0.9 million. In the six months ended March 31, 2009 net other operating income also included a gain from the sale of a sales and service subsidiary in Spain of \$1.0 million and restructuring costs of \$2.8 million (\$2.0 million after taxes), consisting of employee severance pay and benefits and outside consulting fees directly related to the restructuring plan.

In December 2008 we announced certain actions to reduce operating costs and thereby improve the efficiency of our organization. These actions predominantly relate to overhead functions in Germany, including increased automation of our processes, the optimization of the supply chain, as well as increased efficiency in our administrative functions.

For the six month period ended March 31, 2010, we did not incur any restructuring costs.

### ***Loss on Foreign Currency Transactions***

Loss on foreign currency transactions for the six months ended March 31, 2010 amounted to \$4.4 million compared to a loss of \$10.7 million for the six months ended March 31, 2009. For the six months ended March 31, 2010 the loss included an unrealized non-cash foreign currency loss of \$6.5 million on the U.S. Dollar denominated deferred income, resulting from the translation adjustment of the Patterson exclusivity payment, as well as a non-cash foreign currency loss on U.S. Dollar denominated short-term intra-group loans to European entities of \$5.7 million. For the six months ended March 31, 2009 the loss included an unrealized non-cash foreign currency loss of \$6.3 million on the U.S. Dollar denominated deferred income resulting from the translation adjustment of the Patterson exclusivity payment, as well as a non-cash foreign currency loss on U.S. Dollar denominated short-term intra-group loans of \$3.9 million.

### ***(Gain)/Loss on Derivative Instruments***

Gain on derivative instruments for the six months ended March 31, 2010 amounted to \$2.7 million compared to a loss of \$4.7 million for the six months ended March 31, 2009. For the six months ended March 31, 2010, the gain included a non-cash gain of \$6.3 million on interest swaps, as well as a non-cash loss on foreign currency hedges of \$3.6 million. The loss for the six months ended March 31, 2009, included an unrealized non-cash loss of \$8.5 million on interest swaps, as well as a non-cash gain on foreign currency hedges of \$3.8 million.

### ***Interest Expense***

Net interest expense for the six months ended March 31, 2010 was \$9.3 million, compared to \$11.7 million for the six months ended March 31, 2009. This decrease resulted from lower interest rates and lower overall debt levels.

### ***Other Expense***

Professional fees of \$0.8 million, related to the December 2009 and February 2010 follow-on public offerings (professional fees of \$0.4 million and \$0.4 million, respectively), were incurred in the six months ended March 31, 2010. No other expense was incurred for the six months ended March 31, 2009.

**Table of Contents**

***Income Tax Provision***

The income tax provision for the six months ended March 31, 2010 was \$12.5 million, compared to \$2.4 million for the six months ended March 31, 2009. For fiscal year 2010, an estimated effective tax rate of 20% has been applied compared to an estimated effective tax rate of 28% for fiscal year 2009, and an actual effective tax rate of 14.7% for fiscal year 2009. The 2010 effective tax rate is expected to be higher than 2009, due to a variety of factors including the estimated distribution of profits across the different countries.

***Net Income***

Sirona's net income for the six months ended March 31, 2010 was \$48.7 million, an increase of \$42.5 million, as compared with the six months ended March 31, 2009. Net income included amortization and depreciation expense resulting from the step-up to fair values of intangible and tangible assets related to the Exchange and the MDP Transaction (deal related amortization and depreciation) of \$31.1 million (\$24.9 million net of tax), unrealized, non-cash foreign currency losses on the deferred income from the Patterson exclusivity payment of \$6.5 million (\$5.2 million net of tax) and losses on short-term intra-group loans of \$5.7 million (\$4.6 million net of tax).

Sirona's net income for the six month period ended March 31, 2009 included amortization and depreciation expense resulting from the step-up to fair values of intangible and tangible assets related to the Exchange and the MDP Transaction (deal related amortization and depreciation) of \$34.5 million (\$24.8 million net of tax), unrealized, non-cash foreign currency losses on the deferred income from the Patterson exclusivity payment of \$6.3 million (\$4.6 million net of tax) and losses on short-term intra-group loans of \$3.9 million (\$2.8 million net of tax).

Option expense was \$8.0 million (\$6.4 million net of tax) in the first two quarters of 2010, compared to \$7.8 million (\$5.6 million net of tax) in the prior year period.

**Table of Contents****Liquidity and Capital Resources**

Historically, Sirona's principal uses of cash, apart from operating requirements, including research and development expenses, have been for interest payments, debt repayment and acquisitions. Operating capital expenditures are approximately equal to operating depreciation (excluding any effects from the increased amortization and depreciation expense resulting from the step-up to fair values of Sirona's and Schick's assets and liabilities required under purchase accounting). Sirona's management believes that Sirona's working capital is sufficient for its present requirements.

The Senior Facilities Agreement contains restrictive covenants that limit Sirona's ability to make loans, make investments (including in joint ventures), incur additional indebtedness, make acquisitions or pay dividends, subject to agreed exceptions. The Company has agreed to certain financial debt covenants in relation to the financing. The covenants stipulate that the Company must maintain certain ratios in respect of interest payments and defined earnings measures. If the Company breaches any of the covenants, the loans will become repayable on demand.

The financial covenants require that the Company maintain a debt coverage ratio (Debt Cover Ratio) of consolidated total net debt to consolidated adjusted EBITDA (Consolidated Adjusted EBITDA) of no more than 2.50 to 1, and a cash interest coverage ratio (Cash Interest Cover Ratio) of consolidated adjusted EBITDA to cash interest costs of 4.00 to 1 or greater. The Company is required to test its ratios as of September 30 and March 31. As calculated in accordance with the Senior Facilities Agreement, the following table presents the Company's actual Debt Cover Ratio and Cash Interest Cover Ratio, and their respective components, for required testing periods in fiscal year 2010 and 2009:

	LTM March 31 2010	Year Ended September 30 2009 \$ 000s	LTM March 31 2009
Consolidated Total Net Debt	\$ 205.2	\$ 294.2	\$ 362.9
Cash Interest Costs	\$ 11.1	\$ 18.8	\$ 27.7
Consolidated Adjusted EBITDA	\$ 248.1	\$ 200.5	\$ 179.9
Debt Cover Ratio	0.83	1.47	2.02
<i>as set by covenants (less than or equal to)</i>	<i>2.50</i>	<i>2.50</i>	<i>2.75</i>
Cash Interest Cover Ratio	22.39	10.69	6.49
<i>as set by covenants (greater than or equal to)</i>	<i>4.00</i>	<i>4.00</i>	<i>4.00</i>

**Table of Contents***Cash Flows*

	Six months ended	
	March 31, 2010	March 31, 2009
	\$ 000s	
Net cash provided by operating activities	\$ 74,810	\$ 21,872
Net cash used in investing activities	(7,718)	(4,996)
Net cash used in financing activities	(73,918)	(1,270)
 (Decrease)/ increase in cash during the period (before exchange rate effects)	 \$ (6,826)	 \$ 15,606

*Net Cash Provided by Operating Activities*

Net cash provided by operating activities represents net cash from operations, returns on investments, and payments for interest and taxation.

Net cash provided by operating activities was \$74.8 million for the six months ended March 31, 2010, compared to \$21.9 million for the six months ended March 31, 2009. The primary contributing factor to the increase in cash provided by operating activities was an increase in operating income, as well as an improvement in working capital.

---

## **Table of Contents**

### ***Net Cash Used in Investing Activities***

For the six months ended March 31, 2010, net cash used in investing activities represents cash used in capital expenditures in the course of normal operating activities, partly offset by proceeds from the sale of a subsidiary in Italy. The investing cash outflow for the six months ended March 31, 2009, resulted from capital expenditures in the course of normal operating activities, partly offset by proceeds from the sale of a subsidiary in Spain.

### ***Net Cash Used in Financing Activities***

Net cash used in financing activities was \$73.9 million for the six months ended March 31, 2010, compared to net cash used in financing activities of \$1.3 million for the six months ended March 31, 2009. Net cash used in financing activities in the six months ended March 31, 2010 primarily relates to the early repayment of senior debt that was originally due in November 2010 eight months ahead of schedule, partly offset by proceeds and tax-related benefits of stock options exercised in the first half of the fiscal year. Net cash used in financing activities in the six months ended March 31, 2009, related to the repayment of a bank loan in China and the purchase of treasury shares under the stock repurchase program.

Sirona's management believes that Sirona's operating cash flows and available cash (including restricted cash), together with its long-term borrowings, will be sufficient to fund its working capital needs, research and development expenses, anticipated capital expenditure and debt service requirements for the foreseeable future.

### ***Capital Resources***

#### ***Senior Facilities Agreement***

On November 22, 2006, Sirona Dental Systems, Inc. entered into a senior facilities agreement (the "Senior Facilities Agreement") as original guarantor, with Schick Technologies, Inc., a New York company and wholly owned subsidiary of Sirona ("Schick NY"), as original borrower and original guarantor, with Sirona Dental Systems GmbH, as original borrower and original guarantor, with Sirona Dental Services GmbH, as original borrower and original guarantor and with Sirona Dental Systems LLC, Sirona Holding GmbH (subsequently merged with Sirona Dental Services GmbH) and Sirona Immobilien GmbH as original guarantors. Initial borrowings under the Senior Facilities Agreement plus excess cash were used to retire the outstanding borrowings under the Company's previous credit facilities.

The Senior Facilities Agreement includes: (1) a term loan A1 in an aggregate principal amount of \$150 million (the "tranche A1 term loan") available to Sirona's subsidiary, Schick NY, as borrower; (2) a term loan A2 in an aggregate principal amount of Euro 275 million (the "tranche A2 term loan") available to Sirona's subsidiary, Sirona Dental Services GmbH, as borrower; and (3) a \$150 million revolving credit facility available to Sirona Dental Systems GmbH, Schick NY and Sirona Dental Services GmbH, as initial borrowers. The revolving credit facility is available for borrowing in Euro, U.S. Dollars, Yen or any other freely available currency agreed to by the facility agent. The facilities are made available on an unsecured basis. Subject to certain limitations, each European guarantor guarantees the performance of each European borrower, except itself, and each U.S. guarantor guarantees the performance of each U.S. borrower, except itself. There are no cross-border guarantees since all guarantees are by entities that have the same functional currency as the currency in which the respective guaranteed borrowing is denominated.

Each of the senior term loans has a five year maturity and is to be repaid in three annual installments beginning on November 24, 2009 and ending on November 24, 2011. Of the amounts borrowed under the term loan facilities, 15% was due on November 24, 2009, 15% was due on November 24, 2010 and 70% is due on November 24, 2011. The senior debt repayment tranche originally scheduled for November 24, 2009 was prepaid on May 11, 2009 in the amount of \$78.6 million, and the senior debt repayment tranche originally scheduled for November 24, 2010 was prepaid on March 31, 2010 in the amount of \$78.1 million. At the Company's current Debt Cover Ratio, the facilities bear interest of Euribor, for Euro-denominated loans, and Libor for the other loans, plus a margin of 45 basis points for both.

The Senior Facilities Agreement contains a margin ratchet. Pursuant to this provision, which applies from November 24, 2007 onwards, the applicable margin will vary between 90 basis points and 45 basis points per annum according to the Company's leverage multiple (i.e. the ratio of consolidated total net debt to consolidated adjusted EBITDA as defined in the Senior Facilities Agreement). Interest rate swaps were established for 66.6% of the interest until March 2010. These swaps expired on March 31, 2010 and were not renewed. The interest rate swaps fixed the LIBOR or EURIBOR element of interest payable on 66.7% of the principal amount of the loans for defined twelve and





**Table of Contents**

thirteen month interest periods over the lifetime of the swaps, respectively. The defined interest rates fixed for each twelve or thirteen month interest period ranged from 3.50% to 5.24%. Settlement of the swaps was required on a quarterly basis.

The Senior Facilities Agreement contains restrictive covenants that limit Sirona's ability to make loans, make investments (including in joint ventures), incur additional indebtedness, make acquisitions or pay dividends, subject to agreed exceptions. The Company has agreed to certain financial debt covenants in relation to the financing. The covenants stipulate that the Company must maintain certain ratios in respect of interest payments and defined earnings measures. If the Company breaches any of the covenants, the loans will become repayable on demand.

Debt issuance costs of \$5.6 million were incurred in relation to the new financing and were capitalized as deferred charges.

**Other Financial Data**

	Three months ended March 31,		Six months ended March 31,	
	2010	2009	2010	2009
	\$ 000s		\$ 000s	
Net income attributable to Sirona Dental Systems, Inc.	\$ 17,539	\$ 595	\$ 48,714	\$ 6,154
Net interest expense	4,141	5,593	9,343	11,657
Provision for income taxes	4,548	364	12,461	2,362
Depreciation	5,307	4,792	10,929	9,400
Amortization	15,503	17,600	31,660	35,213
 EBITDA	 \$ 47,038	 \$ 28,944	 \$ 113,107	 \$ 64,786

EBITDA is a non-GAAP financial measure that is reconciled to net income, its most directly comparable U.S. GAAP measure, in the accompanying financial tables. EBITDA is defined as net earnings before interest, taxes, depreciation, and amortization. Sirona's management utilizes EBITDA as an operating performance measure in conjunction with U.S. GAAP measures, such as net income and gross margin calculated in conformity with U.S. GAAP. EBITDA should not be considered in isolation or as a substitute for net income prepared in accordance with U.S. GAAP. There are material limitations associated with making the adjustments to Sirona's earnings to calculate EBITDA and using this non-GAAP financial measure. For instance, EBITDA does not include:

interest expense, and because Sirona has borrowed money in order to finance its operations, interest expense is a necessary element of its costs and ability to generate revenue;

depreciation and amortization expense, and because Sirona uses capital and intangible assets, depreciation and amortization expense is a necessary element of its costs and ability to generate revenue; and

tax expense, and because the payment of taxes is part of Sirona's operations, tax expense is a necessary element of costs and impacts Sirona's ability to operate.

In addition, other companies may define EBITDA differently. EBITDA, as well as the other information in this filing, should be read in conjunction with Sirona's consolidated financial statements and footnotes.

In addition to EBITDA, the accompanying financial tables also set forth certain supplementary information that Sirona believes is useful for investors in evaluating Sirona's underlying operations. This supplemental information includes gains/losses recorded in the periods presented which relate to the early extinguishment of debt, share based compensation, revaluation of U.S. Dollar denominated exclusivity payment and borrowings where the functional currency is Euro, and the Exchange. Sirona's management believes that these items are either nonrecurring or noncash in nature, and should be considered by investors in assessing Sirona's financial condition, operating performance and underlying strength.



**Table of Contents**

Sirona's management uses EBITDA together with this supplemental information as an integral part of its reporting and planning processes and as one of the primary measures to, among other things:

- (i) monitor and evaluate the performance of Sirona's business operations;
- (ii) facilitate management's internal comparisons of the historical operating performance of Sirona's business operations;
- (iii) facilitate management's external comparisons of the results of its overall business to the historical operating performance of other companies that may have different capital structures and debt levels;
- (iv) analyze and evaluate financial and strategic planning decisions regarding future operating investments; and
- (v) plan for and prepare future annual operating budgets and determine appropriate levels of operating investments.

Sirona's management believes that EBITDA and the supplemental information provided is useful to investors as it provides them with disclosures of Sirona's operating results on the same basis as that used by Sirona's management.

**Supplemental Information**

	<b>Three months ended March 31, 2010      2009 \$ 000s</b>		<b>Six months ended March 31, 2010      2009 \$ 000s</b>	
Share-based compensation	\$ 4,109	\$ 3,959	\$ 8,048	\$ 7,794
Unrealized, non-cash loss on revaluation of the carrying value of the \$-denominated exclusivity fee	5,099	4,034	6,451	6,325
Unrealized, non-cash loss on revaluation of the carrying value of short-term intra-group loans	4,404	2,510	5,671	3,912
	\$ 13,612	\$ 10,503	\$ 20,170	\$ 18,031

**Recently Issued Accounting Pronouncements**

See Note 2 to the unaudited condensed consolidated financial statements for discussion of recently issued accounting pronouncements that have not yet been adopted.

**Table of Contents**

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

There have been no material changes to the Company's market risk since September 30, 2009.

**ITEM 4. CONTROLS AND PROCEDURES**

**Evaluation of Disclosure Controls and Procedures**

Our management, with the participation of our chief executive officer and chief financial officer, evaluated the effectiveness of our disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934), as of March 31, 2010. Based upon this evaluation, our chief executive officer and chief financial officer concluded that, as of March 31, 2010, the Company's disclosure controls and procedures were effective. Our disclosure controls and procedures are designed to ensure that information relating to the Company, including our consolidated subsidiaries, that is required to be disclosed in the reports we file or submit under the Securities Exchange Act of 1934 is (i) recorded, processed, summarized and reported within the time periods specified in Commission's rules and forms and (ii) accumulated and communicated to our management, including our principal executive and principal financial officers, as appropriate to allow timely decisions regarding required disclosure.

**Changes in Internal Control over Financial Reporting**

No change in our internal control over financial reporting (as defined in rules 13a-15(f) and 15d-15(f) under the Securities Exchange Act of 1934) occurred during the quarter ended March 31, 2010 that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

**Table of Contents****PART II.****ITEM 1. LEGAL PROCEEDINGS**

There are currently no material legal proceedings pending.

**ITEM 1A. RISK FACTORS**

There are no material changes from risk factors as previously disclosed by the Company in Part I, Item IA of its 2009 Annual Report on Form 10-K.

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

None.

**ITEM 3. DEFAULTS UPON SENIOR SECURITIES**

None.

**ITEM 4. (REMOVED AND RESERVED)****ITEM 5. OTHER INFORMATION**

(a) The Company held its 2009 Annual Meeting of Stockholders (the Annual Meeting ) on February 25, 2010. The following matter concerning the election of Directors was voted upon at the Annual Meeting with the accompanying results:

Election of Directors:

	Number of Votes For	Number of Votes Withheld
Simone Blank	33,440,833	13,951,576
(New term expires in 2012)		
Timothy D. Sheehan	43,661,608	3,730,801
(New term expires in 2012)		
Timothy P. Sullivan	34,712,147	12,680,262
(New term expires in 2012)		

The terms of the other Directors of the Company continued after the meeting, as follows: William K. Hood, Harry M. Jansen Kraemer, Jr. and Jeffrey T. Slovin serve in the class whose term expires at the Annual Meeting of Stockholders for the fiscal year ending in 2010 and Nicholas W. Alexos, David K. Beecken, Jost Fischer and Arthur D. Kowaloff serve in the class whose term expires at the Annual Meeting of Stockholders for the fiscal year ending in 2011. Upon the expiration of the term of a class of Directors, the members of such class will be elected for

Edgar Filing: SIRONA DENTAL SYSTEMS, INC. - Form 10-Q

three-year terms at the Annual Meeting of Stockholders at which such expiration occurs.

The following additional matter was voted upon at the Annual Meeting held on February 25, 2010 with the following results:

**Table of Contents**

1. Ratification of the selection of KPMG AG, Wirtschaftsprüfungsgesellschaft, Frankfurt, Germany as the Company's independent auditor for the fiscal year ending September 30, 2010:

Number of votes for:	51,601,603
Number of votes against:	122,159
Number of abstentions:	8,006

(b) Appointment of New Director

On April 29, 2010, the Board unanimously voted to increase the size of the Board to eleven (11) members. On that date, the Board unanimously voted to appoint Thomas Jetter to the Company's Board of Directors to serve in such capacity until his successor is duly elected and qualified or until his earlier death, resignation or removal. There is no arrangement or understanding between Mr. Jetter and any other person, pursuant to which Mr. Jetter is to be appointed as a director. Mr. Jetter is not a party to any transactions that would require disclosure under Item 404(a) of Regulation S-K. In connection with his appointment, Mr. Jetter will be paid an annual retainer of \$35,000.

- (c) We entered into an Amendment to the Distributorship Agreement (the Amendment), dated as of May 5, 2010, between Schick and Patterson Companies, Inc. (Patterson). The Amendment amends a distributorship agreement (Distributorship Agreement) entered into with Patterson Dental Company (now Patterson), dated as of April 6, 2000 and as amended July 1, 2005 and February 26, 2007. The Distributorship Agreement provides for Patterson to be the exclusive distributor of Schick's CDR digital dental products throughout North America. Pursuant to the Amendment, Schick and Patterson have agreed to extend the term of the Distributorship Agreement to December 31, 2012. The Amendment also addresses issues relating to product return policy, termination, annual minimum purchase quotas and preferred vendor designation.

A copy of the Amendment is filed herewith as Exhibit 10.1.

**ITEM 6. EXHIBITS**

The following Exhibits are included in this report:

Exhibit No.	Item Title
10.1*#	Amendment to Distributorship Agreement, dated May 5, 2010, by and between Schick Technologies, Inc. and Patterson Companies, Inc.
31.1	Certification of Principal Executive Officer, pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
31.2	Certification of Principal Financial Officer, pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
32.1	Section 1350 Certification of Chief Executive Officer.
32.2	Section 1350 Certification of Chief Financial Officer.

\* Filed herewith

# A request for confidentiality has been filed for certain portions of the indicated document. Confidential portions have been omitted and filed separately with the Securities and Exchange Commission as required by Rule 24b-2 promulgated under the Securities Exchange Act of 1934.



**Table of Contents**

**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.

Date: May 5, 2010

Sirona Dental Systems, Inc.

By: /s/ Simone Blank  
Simone Blank, Executive Vice President and Chief  
Financial Officer

(Principal Financial and Accounting Officer) (Duly  
authorized signatory)