

SIRONA DENTAL SYSTEMS, INC.

Form 10-Q

August 05, 2011

[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
or

For the quarterly period ended June 30, 2011

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)

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

Delaware
(State or other jurisdiction of
incorporation or organization)

11-3374812
(I.R.S. Employer
Identification No.)

30 30 4th Avenue, Suite 500,
Long Island City, New York
(Address of principal executive offices)

11101
(Zip Code)

(718) 482-2011

Registrant's telephone number, including area code:

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

Indicate by check mark whether the registrant has submitted electronically 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 August 3, 2011, the number of shares outstanding of the Registrant's Common Stock, par value \$.01 per share, was 56,207,781.

Table of Contents

SIRONA DENTAL SYSTEMS, INC.

FORM 10-Q

FOR THE THREE MONTHS ENDED JUNE 30, 2011

Index

	Page	
Part I.	<u>Financial Information (Unaudited)</u>	3
Item 1.	<u>Financial Statements</u>	3
	<u>Condensed Consolidated Balance Sheets as of June 30, 2011 and September 30, 2010</u>	3
	<u>Condensed Consolidated Income Statements for the three and nine months ended June 30, 2011 and 2010</u>	5
	<u>Condensed Consolidated Statements of Cash Flows for the nine months ended June 30, 2011 and 2010</u>	6
	<u>Notes to the Condensed Consolidated Financial Statements</u>	8
Item 2.	<u>Management's Discussion and Analysis of Financial Condition and Results of Operations</u>	24
Item 3.	<u>Quantitative and Qualitative Disclosures About Market Risk</u>	35
Item 4.	<u>Controls and Procedures</u>	35
Part II.	<u>Other Information</u>	36
Item 1.	<u>Legal Proceedings</u>	36
Item 1A.	<u>Risk Factors</u>	36
Item 2.	<u>Unregistered Sales of Equity Securities and Use of Proceeds</u>	36
Item 3.	<u>Defaults upon Senior Securities</u>	36
Item 4.	<u>(Removed and Reserved)</u>	36
Item 5.	<u>Other Information</u>	36
Item 6.	<u>Exhibits</u>	36
	<u>Signatures</u>	37
	Certifications	

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	June 30, 2011 (unaudited) \$ 000s (except per share amounts)	September 30, 2010
ASSETS			
Current assets			
Cash and cash equivalents		\$ 331,203	\$ 251,767
Restricted cash			703
Accounts receivable, net of allowance for doubtful accounts of \$1,615 and \$1,681, respectively		116,476	82,952
Inventories, net	6	93,926	74,027
Deferred tax assets	10	22,213	20,570
Prepaid expenses and other current assets		15,009	24,139
Income tax receivable	10	9,065	3,533
Total current assets		587,892	457,691
Property, plant and equipment, net of accumulated depreciation and amortization of \$113,944 and \$90,713, respectively		127,287	102,686
Goodwill	7	694,551	656,465
Investments		2,419	2,317
Restricted cash		724	
Intangible assets, net of accumulated amortization of \$421,401 and \$371,303, respectively	7	378,110	362,722
Other non-current assets		2,986	2,229
Deferred tax assets	10	4,758	8,827
Total assets		\$ 1,798,727	\$ 1,592,937
LIABILITIES AND SHAREHOLDERS EQUITY			
Current liabilities			
Trade accounts payable		\$ 46,280	\$ 42,737
Short-term debt and current portion of long-term debt	8	389,268	2,935
Income taxes payable	10	7,795	7,748
Deferred tax liabilities	10	964	1,456
Accrued liabilities and deferred income		95,135	105,209
Total current liabilities		539,442	160,085
Long-term debt	9		367,801
Deferred tax liabilities	10	149,403	138,190
Other non-current liabilities		16,776	6,556

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

Table of Contents

Pension related provisions	13	57,070	52,672
Deferred income		52,500	60,000
Total liabilities		815,191	785,304
Shareholders equity			
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; 56,235,504 shares issued and 56,207,781 shares outstanding at Jun. 30, 2011, and 55,333,304 shares issued and 55,305,581 shares outstanding at Sept. 30, 2010)		562	553
Additional paid-in capital		677,649	652,698
Treasury stock (27,723 shares at cost)		(284)	(284)
Excess of purchase price over predecessor basis		(49,103)	(49,103)
Retained earnings		289,881	181,846
Accumulated other comprehensive income	5	61,266	19,701
Total Sirona Dental Systems, Inc. shareholders equity		979,971	805,411
Noncontrolling interests		3,565	2,222
Total shareholders equity		983,536	807,633
Total liabilities and shareholders equity		\$ 1,798,727	\$ 1,592,937

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

Table of Contents

SIRONA DENTAL SYSTEMS, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF INCOME

(UNAUDITED)

	Financial Statement Notes	Three months ended June 30,		Nine months ended June 30,	
		2011 \$ 000s (except per share amounts)	2010 \$ 000s (except per share amounts)	2011 \$ 000s (except per share amounts)	2010 \$ 000s (except per share amounts)
Revenue		\$ 244,686	\$ 182,418	\$ 695,069	\$ 587,377
Cost of sales		117,854	88,243	322,134	281,499
Gross profit		126,832	94,175	372,935	305,878
Selling, general and administrative expense		68,540	54,994	202,444	175,200
Research and development		14,390	11,648	42,045	34,803
Provision for doubtful accounts and notes receivable		13	47	34	183
Net other operating income	14	(2,500)	(3,254)	(7,500)	(9,162)
Operating income		46,389	30,740	135,912	104,854
(Gain)/Loss on foreign currency transactions, net		(3,435)	6,003	(8,532)	10,419
Loss/(gain) on derivative instruments	15	1,081	2,598	1,162	(137)
Interest expense, net		984	857	2,863	10,200
Other expense/(income)		383	(9)	(140)	775
Income before taxes		47,376	21,291	140,559	83,597
Income tax provision	10	10,423	4,258	30,923	16,719
Net income		36,953	17,033	109,636	66,878
Less: Net income attributable to noncontrolling interests		622	456	1,601	1,587
Net income attributable to Sirona Dental Systems, Inc.		\$ 36,331	\$ 16,577	\$ 108,035	\$ 65,291
Income per share (attributable to Sirona Dental Systems, Inc. common shareholders):	11				
- Basic		\$ 0.65	\$ 0.30	\$ 1.94	\$ 1.18
- Diluted		\$ 0.63	\$ 0.29	\$ 1.89	\$ 1.15
Weighted average shares basic		55,992,911	55,227,417	55,619,151	55,105,687
Weighted average shares diluted		57,577,513	56,739,364	57,246,485	56,587,308

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)

	Nine months ended June 30,	
	2011	2010
	\$ 000s	
Cash flows from operating activities		
Net income	\$ 109,636	\$ 66,878
Adjustments to reconcile net income to net cash provided by operating activities		
Depreciation and amortization	59,839	62,272
Loss on disposal of property, plant and equipment		37
Loss/(gain) on derivative instruments	1,162	(137)
(Gain)/loss on foreign currency transactions	(8,532)	10,419
Deferred income taxes	(9,143)	(16,169)
Amortization of debt issuance cost	895	760
Share-based compensation expense	7,241	11,828
Changes in assets and liabilities		
Accounts receivable	(27,953)	(4,524)
Inventories	(13,801)	(5,948)
Prepaid expenses and other current assets	10,042	9
Restricted cash	20	134
Other non-current assets	(243)	26
Trade accounts payable	1,171	5,045
Accrued interest on long-term debt		(476)
Accrued liabilities and deferred income	(19,478)	(1,137)
Other non-current liabilities	712	(500)
Income taxes receivable	(5,518)	2,675
Income taxes payable	(604)	4,804
Net cash provided by operating activities	105,446	135,996
Cash flows from investing activities		
Investment in property, plant and equipment	(37,097)	(16,651)
Proceeds from sale of property, plant and equipment		408
Purchase of intangible assets	(247)	(216)
Purchase of long-term investments	(95)	(359)
Acquisition of business, net of cash acquired	(20,840)	
Sale of business, net of cash sold		1,928
Net cash used in investing activities	(58,279)	(14,890)

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)

	Nine months ended June 30,	
	2011	2010
	\$ 000s	
Cash flows from financing activities		
Repayments of short-term and long-term debt		(78,072)
Purchase of shares from noncontrolling interest		(1,315)
Dividend distributions to noncontrolling interest	(487)	
Common shares issued under share based compensation plans	10,365	3,433
Tax effect of common shares exercised under share based compensation plans	8,283	1,382
Net cash provided by/(used in) financing activities	18,161	(74,572)
Change in cash and cash equivalents	65,328	46,534
Effect of exchange rate change on cash and cash equivalents	14,108	(27,474)
Cash and cash equivalents at beginning of period	251,767	181,098
Cash and cash equivalents at end of period	\$ 331,203	\$ 200,158
Supplemental information		
Interest paid	\$ 3,114	\$ 10,971
Interest capitalized	376	396
Income taxes paid	37,291	26,635
Acquisition of business		
Current assets	\$ 201	\$
Non-current assets	47,277	
Current liabilities	(269)	
Non-current liabilities	(16,156)	
	\$ 31,053	\$
Cash paid	(20,898)	
	\$ 10,155	\$
Sale of business, net of cash sold		
Current assets	\$	\$ 2,406
Non-current assets		550
Current liabilities		(867)
Non-current liabilities		(161)
	\$	\$ 1,928

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, the Company, we, us, and our refer to Sirona Dental Systems, Inc. and its consolidated subsidiaries and their predecessors) 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 (the Exchange), 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 around the globe.

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, 2010.

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 June 30, 2011, and the results of operations and cash flows for the nine months ended June 30, 2011 and 2010, respectively, as applicable to interim periods have been made. The results of operations for the nine months ended June 30, 2011 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

SIRONA DENTAL SYSTEMS, INC AND SUBSIDIARIES

NOTES TO THE CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(UNAUDITED)

Business acquisitions

The Company acquires businesses as well as partial interests in businesses. Acquired businesses are accounted for using the acquisition method of accounting which requires that all assets and liabilities are recorded at their respective fair values. Any excess of the purchase price over estimated fair values of net assets is recorded as goodwill. The assumptions made in determining fair value assigned to acquired assets and liabilities as well as asset lives can materially impact the results of operations.

The Company obtains information during due diligence and through other sources to arrive at respective fair values. Examples of factors and information that the Company uses to determine the fair values include: tangible and intangible asset evaluations and appraisals; evaluations of existing contingencies and liabilities; product line integration information; and information systems compatibilities. If the initial accounting for an acquisition is incomplete by the end of the quarter in which the acquisition occurred, the Company will record a provisional estimate in the financial statements. The provisional estimate will be finalized as soon as information becomes available but no later than one year from the acquisition date.

2. Recently Issued Accounting Pronouncements

Adopted

Revenue Recognition

In October 2009, the Financial Accounting Standards Board (FASB) issued new accounting guidance for multiple-deliverable revenue arrangements (ASU 2009-13, *Multiple-Deliverable Revenue Arrangements a consensus of the FASB Emerging Issues Task Force*). This new guidance 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 October 2009, the FASB also issued new accounting guidance for revenue arrangements that include both tangible products and software elements (ASU 2009-14, *Certain Revenue Arrangements that Include Software Elements a consensus of the FASB Emerging Issues Task Force*). 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 non-software 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 Company adopted these standards at the beginning of its first quarter of fiscal year 2011 for applicable arrangements that were entered into or materially modified on or after October 1, 2010. Implementation of these standards did not have a material impact on the Company s condensed consolidated financial statements in the period under report and is not expected to significantly affect the timing and pattern of revenue recognition in future periods.

The Company s main revenue stream results from the delivery of dental equipment. The Company also enters into revenue arrangements that consist of multiple deliverables of its product and service offerings. Additionally, certain products, primarily in our CAD/CAM and Imaging segments, may contain embedded software that functions together with the product to deliver the product s essential functionality.

Revenue, net of related discounts and allowances, is recognized when products or equipment have been shipped, when persuasive evidence of the arrangement exists, the price is fixed or determinable, collectability is reasonably assured, title and risk of loss has passed to customers based

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

on the shipping terms, no significant obligations remain, and allowances for discounts, returns, and customer incentives can be reliably estimated. The Company offers discounts to its distributors if certain conditions are met. Discounts and allowances are primarily based on the volume of products purchased or targeted to be purchased by the individual customer or distributor. Discounts are deducted from revenue at the time of sale or when the discount is offered, whichever is later. The Company estimates volume discounts based on the individual customer's historical and estimated future product purchases. Returns of products, excluding warranty related returns, are infrequent and insignificant. Amounts received from customers in advance of product shipment are classified as deferred income until the revenue can be recognized in accordance with the Company's revenue recognition policy.

Table of Contents

SIRONA DENTAL SYSTEMS, INC AND SUBSIDIARIES

NOTES TO THE CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(UNAUDITED)

Services: Service revenue is generally recognized ratably over the contract term as the specified services are performed. Amounts received from customers in advance of rendering of services are classified as deferred income until the revenue can be recognized upon rendering of those services.

Extended Warranties: The Company offers its customers an option to purchase extended warranties on certain products. The Company recognizes revenue on these extended warranty contracts ratably over the life of the contract. The costs associated with these extended warranty contracts are recognized when incurred.

Multiple-Element Arrangements (MEAs): Arrangements with customers may include multiple deliverables, including any combination of equipment, services, and extended warranties. The deliverables included in the Company's MEAs are separated into more than one unit of accounting when (i) the delivered equipment has value to the customer on a stand-alone basis, and (ii) delivery of the undelivered service element(s) is probable and substantially in the control of the Company. Based on the new accounting guidance adopted October 1, 2010, arrangement consideration is then allocated to each unit, delivered or undelivered, based on the relative selling price (RSP) of each unit of accounting based first on vendor-specific objective evidence (VSOE) if it exists and then based on estimated selling price (ESP).

VSOE In most instances, products are sold separately in stand-alone arrangements. Services are also sold separately through renewals of contracts with varying periods. The Company determines VSOE based on its pricing and discounting practices for the specific product or service when sold separately, considering geographical, customer, and other economic or marketing variables, as well as renewal rates or stand-alone prices for the service element(s).

ESP The estimated selling price represents the price at which the Company would sell a product or service if it were sold on a stand-alone basis. When VSOE does not exist for all elements, the Company determines ESP for the arrangement element based on sales, cost and margin analysis, as well as other inputs based on its pricing practices. Adjustments for other market and Company-specific factors are made as deemed necessary in determining ESP.

After separating the elements into their specific units of accounting, total arrangement consideration is allocated to each unit of accounting according to the nature of the revenue as described above and application of the RSP method. Total recognized revenue is limited to the amount not contingent upon future transactions.

Not Yet Adopted

In May 2011, the FASB issued ASU 2011-04, *Fair Value Measurement (Topic 820): Amendments to Achieve Common Fair Value Measurement and Disclosure Requirements in U.S. GAAP and IFRSs*, which clarifies certain principles or requirements for measuring fair value, including measuring the fair value of financial instruments that are managed within a portfolio and the application of premiums and discounts in a fair value measurement. In addition, ASU 2011-04 requires expanded fair value measurement disclosures including: (1) for Level 3 fair value measurements, qualitative information about unobservable inputs used, valuation processes applied, and the sensitivity of those measurements to changes in observable inputs; (2) for an entity's use of a nonfinancial asset in a manner other than its highest and best use, the reason for the difference; and (3) for items not measured at fair value but for which fair value disclosure is required, the hierarchical level in which the fair values were determined. ASU 2011-04 is effective for fiscal years, and interim periods within those years, beginning after December 15, 2011, which corresponds to the Company's fiscal quarter beginning January 1, 2012, with early adoption not permitted for public entities. The Company is evaluating the potential impact of adoption.

In June 2011, the FASB issued ASU 2011-05, *Presentation of Comprehensive Income*, which requires that all non-owner changes in shareholders' equity be presented either (1) in a single continuous statement of comprehensive income or (2) in two separate but consecutive statements. ASU 2011-05 is effective for public entities for fiscal years, and interim periods within those years, beginning after December 15, 2011, which corresponds to the Company's fiscal year beginning October 1, 2012, with early adoption permitted. The Company is evaluating the potential impact of adoption.

3. Business Acquisitions

On May 16, 2011, the Company acquired 100% of the outstanding shares of capital stock of a development stage technology company. The results of its operations have been included in the consolidated financial statements since this date. The results were not material to the consolidated financial statements.

Table of Contents

SIRONA DENTAL SYSTEMS, INC AND SUBSIDIARIES

NOTES TO THE CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(UNAUDITED)

The fair value of total consideration transferred for this acquisition totaled \$31.1 million, consisting of cash of \$20.9 million and contingent consideration arrangements. The contingent consideration arrangements require the Company to pay the former owners additional amounts contingent upon revenue and product development milestones. These contingent arrangements provide for payments ranging from \$0 up to a total of \$28.0 million (undiscounted) and vary over a period of up to six years, ending in fiscal year 2017. The fair value at acquisition date was \$10.2 million and will be remeasured through settlement, with changes in fair value recorded in income (see Note 16). As a result of the acquisition, the Company primarily acquired in-process research and development assets. The determination of the fair value of the intangible assets is based on preliminary estimates.

4. Employee Share-Based Compensation

Stock compensation expense under the Company's stock option plans amounted to \$2,762 and \$7,241 for the three and nine months ended June 30, 2011, respectively, and \$3,780 and \$11,828 for the three and nine months ended June 30, 2010, respectively. These expenses include the effect of previous stock options, restricted stock unit (RSU) grants, and performance-based stock unit (PSU) grants.

On June 14, 2011, the Company granted 24,000 RSU's under its 2006 Equity Incentive Plan (2006 Plan). The RSU grants vest over a period of three years (one third each during fiscal years 2012, through 2014). The value of each RSU grant is determined by the closing price at the date of grant of \$52.06.

On April 1, 2011, the Company granted 1,000 RSU's under the 2006 Plan. The RSU grant vests over a period of four years (one third each during fiscal years 2013 through 2015). The value of the RSU grant is determined by the closing price at the date of grant of \$50.47.

On November 22, 2010, the Company granted 232,700 RSU's and 12,800 PSU's under the 2006 Plan. The RSU grants vest over a period of four years (one third each during fiscal years 2013 through 2015). The PSU's were granted to three executive officers of the Company and vest three years from the date of grant provided the Company achieves earnings targets specified in the grant. The value of each RSU and PSU grant is determined by the closing price at the date of grant of \$36.78.

On December 8, 2009, the Company granted 188,000 RSU's under the 2006 Plan. The RSU grants 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 at 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 June 30, 2011, 1,384,330 shares were available for future grant under the 2006 Plan.

Table of Contents**SIRONA DENTAL SYSTEMS, INC AND SUBSIDIARIES****NOTES TO THE CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**

(UNAUDITED)

5. Comprehensive Income/(Loss) and Change in Equity

	Three months ended June 30, Changes in Equity attributable to			Nine months ended June 30, Changes in Equity attributable to		
	Sirona Dental Systems, Inc.	Noncontrolling Interests \$ 000s	Total Change in Equity for the Period	Sirona Dental Systems, Inc.	Noncontrolling Interests \$ 000s	Total Change in Equity for the Period
As of June 30, 2011						
Comprehensive Income:						
Net Income	\$ 36,331	\$ 622	\$ 36,953	\$ 108,035	\$ 1,601	\$ 109,636
Other Comprehensive Income						
Cumulative translation adjustments	13,658	87	13,745	41,687	229	41,916
Unrecognized elements of pension cost, net of tax	(42)		(42)	(122)		(122)
Total Other Comprehensive Income	13,616	87	13,703	41,565	229	41,794
Total Comprehensive Income	49,947	709	50,656	149,600	1,830	151,430
Transactions with shareholders:						
Stock-based compensation activities	12,348		12,348	24,960		24,960
Dividend distribution to noncontrolling interest					(487)	(487)
Total transactions with shareholders	12,348		12,348	24,960	(487)	24,473
Total Change in Equity for the period	\$ 62,295	\$ 709	\$ 63,004	\$ 174,560	\$ 1,343	\$ 175,903

	Three months ended June 30, Changes in Equity attributable to			Nine months ended June 30, Changes in Equity attributable to		
	Sirona Dental Systems, Inc.	Noncontrolling Interests \$ 000s	Total Change in Equity for the Period	Sirona Dental Systems, Inc.	Noncontrolling Interests \$ 000s	Total Change in Equity for the Period
As of June 30, 2010						
Comprehensive Income/(Loss):						
Net Income	\$ 16,577	\$ 456	\$ 17,033	\$ 65,291	1,587	\$ 66,878
Other Comprehensive Income/(Loss)						
Cumulative translation adjustments	(50,807)	(161)	(50,968)	(100,255)	(179)	(100,434)
Unrecognized elements of pension cost, net of tax	(173)		(173)	(337)		(337)
Total Other Comprehensive Loss	(50,980)	(161)	(51,141)	(100,592)	(179)	(100,771)

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

Total Comprehensive Income/(Loss)	(34,403)	295	(34,108)	(35,301)	1,408	(33,893)
Transactions with shareholders:						
Stock-based compensation activities	4,413		4,413	13,777		13,777
Purchase of shares from noncontrolling interest	(79)	(124)	(203)	(897)	(622)	(1,519)
Total transactions with shareholders	4,334	(124)	4,210	12,880	(622)	12,258
Total Change in Equity for the period	\$ (30,069)	\$ 171	\$ (29,898)	\$ (22,421)	786	\$ (21,635)

Table of Contents**SIRONA DENTAL SYSTEMS, INC AND SUBSIDIARIES****NOTES TO THE CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**

(UNAUDITED)

6. Inventories, net

	June 30, 2011	September 30, 2010
	\$ 000s	
Finished goods	\$ 59,553	\$ 51,102
Work in progress	17,347	12,646
Raw materials	34,087	23,342
	110,987	87,090
Inventory reserve	(17,061)	(13,063)
	\$ 93,926	\$ 74,027

7. Intangible Assets and Goodwill

	Gross	Accumulated amortization \$ 000s	Net
As of June 30, 2011			
Patents & Licenses	\$ 150,088	\$ 76,320	\$ 73,768
Trademarks	138,308	503	137,805
Technologies and dealer relationships	470,733	344,578	126,155
In-process research & development	40,382		40,382
	799,511	421,401	378,110
Goodwill	694,551		694,551
Total intangible assets	\$ 1,494,062	\$ 421,401	\$ 1,072,661
As of September 30, 2010			
Patents & Licenses	\$ 150,706	\$ 71,965	\$ 78,741
Trademarks	131,908	428	131,480
Technologies and dealer relationships	451,333	298,910	152,423
Prepayments for intangible assets	78		78
	734,025	371,303	362,722
Goodwill	656,465		656,465

Total intangible assets	\$ 1,390,490	\$ 371,303	\$ 1,019,187
--------------------------------	--------------	------------	--------------

The change in the value of goodwill and of intangible assets from September 30, 2010 to June 30, 2011 is mainly attributable to (i) the acquisition of a development stage technology company, which resulted in in-process research and development of \$40,382 and \$6,761 of goodwill based on preliminary estimates, (ii) foreign currency fluctuations, with an increase of \$32,671 in goodwill and \$15,438 in intangible assets, and (iii) a reduction in goodwill by \$1,347 as a result of tax benefits received subsequent to the Exchange for options that were vested and included in the determination of purchase price at the time of that acquisition.

Table of Contents**SIRONA DENTAL SYSTEMS, INC AND SUBSIDIARIES****NOTES TO THE CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**

(UNAUDITED)

8. Short-Term Debt and Current Portion of Long-Term Debt

The components of short-term debt are as follows:

	000000000 June 30, 2011	000000000 September 30, 2010
	\$ 000s	
Senior Term Loans (Tranches A1/A2, variable rate repayable in November 2011)	\$ 383,682	\$
Accrued interest on long-term debt		319
Other short-term debt	5,586	2,616
	\$ 389,268	\$ 2,935

9. Long-Term Debt

The components of long-term debt are as follows:

	000000000 June 30, 2011	000000000 September 30, 2010
	\$ 000s	
Bank loans:		
Senior term loan, Tranche A1, variable rate repayable in November 2011	\$	\$ 105,063
Senior term loan, Tranche A2, variable rate repayable in November 2011		263,057
		368,120
Less current portion		319
	\$	\$ 367,801

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 Schick Technologies, Inc., a New York company and wholly-owned subsidiary of Sirona ("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

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

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 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

Table of Contents

SIRONA DENTAL SYSTEMS, INC AND SUBSIDIARIES

NOTES TO THE CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(UNAUDITED)

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.

10. Income Taxes

For the first nine months of fiscal year 2011, an estimated effective tax rate of 22% has been applied, compared to an estimated effective tax rate of 20% for the first nine months of fiscal year 2010 and an effective tax rate for fiscal year 2010 of 20.6%.

The Company's effective tax rate may vary significantly from period to period, and can be influenced by many factors. These factors include, but are not limited to, changes in the mix of earnings in countries with differing statutory tax rates (including as a result of business acquisitions and dispositions), changes in the valuation of deferred tax assets and liabilities, the results of audits and examinations of previously filed tax returns, tax planning initiatives, tax characteristics of income, as well as the timing and deductibility of expenses for tax purposes. The Company's effective tax rate differs from the United States federal statutory rate of 35% primarily as a result of lower effective tax rates on certain earnings outside of the United States. The distribution of lower-taxed foreign earnings to the U.S. would generally increase the Company's effective 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 year 2005.

Table of Contents**SIRONA DENTAL SYSTEMS, INC AND SUBSIDIARIES****NOTES TO THE CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**

(UNAUDITED)

11. Income per Share

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

	Three months ended June 30,		Nine months ended June 30,	
	2011	2010	2011	2010
	\$ 000s (except for share amounts)		\$ 000s (except for share amounts)	
Net income attributable to Sirona Dental Systems, Inc. common shareholders	\$ 36,331	\$ 16,577	\$ 108,035	\$ 65,291
Weighted average shares outstanding basic	55,992,911	55,227,417	55,619,151	55,105,687
Dilutive effect of stock-based compensation	1,584,602	1,511,947	1,627,334	1,481,621
Weighted average shares outstanding diluted	57,577,513	56,739,364	57,246,485	56,587,308
Net income per share				
Basic	\$ 0.65	\$ 0.30	\$ 1.94	\$ 1.18
Diluted	\$ 0.63	\$ 0.29	\$ 1.89	\$ 1.15

Stock options to acquire 86,500 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 months ended June 30, 2010 because the options' underlying exercise prices were greater than the average market price of Sirona's common stock for the period. There were no out of the money options for the three and nine months ended June 30, 2011.

12. Product warranty

The following table provides the changes in the product warranty accrual for the three months ended June 30, 2011 and 2010:

	Three months ended June 30,		Nine months ended June 30,	
	2011	2010	2011	2010
	\$ 000s		\$ 000s	
Balance at beginning of the period	\$ 8,554	\$ 11,626	\$ 8,972	\$ 11,506
Accruals for warranties issued during the period	5,740	2,674	14,772	14,073
Warranty settlements made during the period	(4,985)	(3,635)	(14,711)	(14,081)
Translation adjustment	149	(1,078)	425	(1,911)
Balance at end of the period	\$ 9,458	\$ 9,587	\$ 9,458	\$ 9,587

Table of Contents**SIRONA DENTAL SYSTEMS, INC AND SUBSIDIARIES****NOTES TO THE CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**

(UNAUDITED)

13. Pension Plans

Components of net periodic benefit costs are as follows:

	Three months ended June 30,		Nine months ended June 30,	
	2011	2010	2011	2010
	\$ 000s		\$ 000s	
Service cost, net	\$ 68	\$ 60	\$ 197	\$ 195
Interest cost	640	585	1,853	1,897
Amortization of actuarial gains	(42)	(104)	(122)	(337)
Net periodic benefit cost	\$ 666	\$ 541	\$ 1,928	\$ 1,755

14. Net Other Operating Income

Net other operating income for the three and nine months ended June 30, 2011 was \$2.5 million and \$7.5 million, respectively, compared to \$3.3 million and \$9.2 million, respectively, for the three and nine months ended June 30, 2010. In both periods, net other operating income included \$2.5 million (three months) and \$7.5 million (nine months) of income resulting from the amortization of the deferred income relating to the Patterson exclusivity payment. In the three and nine months ended June 30, 2010, net other operating income included a gain of \$0.8 million from the release of the remaining accrued restructuring costs. In the nine months ended June 30, 2010, net other operating income included a gain from the sale of a subsidiary in Italy of \$0.9 million.

15. 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, 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.

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

As of June 30, 2011, these contracts had notional amounts totaling \$39.6 million. These agreements are relatively short-term (generally six months).

The fair value carrying amount of the Company's derivative instruments at June 30, 2011 is described in Note 16 Fair Value Measurements.

Table of Contents**SIRONA DENTAL SYSTEMS, INC AND SUBSIDIARIES****NOTES TO THE CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**

(UNAUDITED)

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

Derivatives Not Designated as Hedging Instruments	Location of (Gain)/Loss Recognized in Income on Derivative	For the three months ended June 30,		For the nine months ended June 30,	
		2011	2010	2011	2010
		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
		\$ 000s		\$ 000s	
Interest rate swap contracts	Gain on derivative instruments, net	\$	\$	\$	(6,364)
Foreign exchange contracts	Loss on derivative instruments, net	1,081	2,598	1,162	6,227
Total		\$ 1,081	\$ 2,598	\$ 1,162	(137)

16. Fair Value Measurements

The Company applies 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 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 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.

Table of Contents**SIRONA DENTAL SYSTEMS, INC AND SUBSIDIARIES****NOTES TO THE CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**

(UNAUDITED)

Assets/Liabilities Measured at Fair Value on a Recurring Basis

The following table presents the Company's assets and liabilities measured at fair value on a recurring basis as of June 30, 2011 and September 30, 2010:

	000000000	000000000	000000000 June 30, 2011	000000000	000000000
	Quoted Prices in Active Markets for Identical Instruments (Level 1)	Significant Other Observable Inputs (Level 2) Interest	Significant Other Observable Inputs (Level 2) Foreign Exchange \$ 000s	Significant Unobservable Inputs (Level 3)	Total
Assets					
Cash Equivalents (money market funds)	\$ 210,099	\$	\$	\$	\$ 210,099
Derivative Assets			616		616
Liabilities					
Derivative Liabilities	\$	\$	\$ (219)	\$	\$ (219)
Business Acquisition-related liabilities				(10,300)	(10,300)
Total	\$ 210,099	\$	\$ 397	\$ (10,300)	\$ 200,196

	September 30, 2010				
	Quoted Prices in Active Markets for Identical Instruments (Level 1)	Significant Other Observable Inputs (Level 2) Interest	Significant Other Observable Inputs (Level 2) Foreign Exchange \$ 000s	Significant Unobservable Inputs (Level 3)	Total
Assets					
Cash Equivalents (money market funds)	\$ 141,981	\$	\$	\$	\$ 141,981
Derivative Assets			2,015		2,015
Liabilities					
Derivative Liabilities	\$	\$	\$ (563)	\$	\$ (563)
Total	\$ 141,981	\$	\$ 1,452	\$	\$ 143,433

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

In the Company's June 30, 2011 and September 30, 2010 Condensed Consolidated Balance Sheet, derivative assets and derivative liabilities are classified as prepaid expenses and other current assets and accrued liabilities and deferred income, respectively.

Table of Contents**SIRONA DENTAL SYSTEMS, INC AND SUBSIDIARIES****NOTES TO THE CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**

(UNAUDITED)

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

Fair value of financial instruments

Financial instruments consist of cash, cash equivalents, accounts receivable, accounts payable, foreign currency forward contracts, and certain liabilities related to business acquisitions primarily resulting from earn-out features. The carrying amounts of cash, cash equivalents, accounts receivable and accounts payable approximate their respective fair values because of the short maturity and nature of these items. The fair value of the foreign currency forward contracts is estimated by obtaining quotes from financial institutions. The fair values of the acquisition-related liabilities are based on discounted valuations of commercial assumptions made by Company management of stipulations governed in the underlying purchase agreements.

17. 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 Exchange. 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.

	Three months ended June 30,		Nine months ended June 30,	
	2011	2010	2011	2010
	\$ 000s		\$ 000s	
Revenue External				
Dental CAD/CAM Systems	\$ 83,209	\$ 63,298	\$ 243,593	\$ 203,420
Imaging Systems	85,014	61,771	233,564	192,287
Treatment Centers	48,166	35,027	139,128	118,735
Instruments	28,002	22,191	77,969	72,444
Total	244,391	182,287	694,254	586,886
Electronic center and corporate	295	131	815	491
Total	\$ 244,686	\$ 182,418	\$ 695,069	\$ 587,377
Revenue Internal				
Dental CAD/CAM Systems	\$	\$	\$	\$
Imaging Systems	1	10	9	25
Treatment Centers	2	6	19	22
Instruments	2,747	2,452	7,963	7,295
Intercompany elimination	(2,750)	(2,468)	(7,991)	(7,342)

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

Total				
Electronic center and corporate	6,461	4,367	18,690	14,798
Intercompany elimination	(6,461)	(4,367)	(18,690)	(14,798)
Total	\$	\$	\$	\$

Table of Contents**SIRONA DENTAL SYSTEMS, INC AND SUBSIDIARIES****NOTES TO THE CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**

(UNAUDITED)

Revenue Total				
Dental CAD/CAM Systems	\$ 83,209	\$ 63,298	\$ 243,593	\$ 203,420
Imaging Systems	85,015	61,781	233,573	192,312
Treatment Centers	48,168	35,033	139,147	118,757
Instruments	30,750	24,643	85,933	79,739
Total	247,142	184,755	702,246	594,228
Electronic center and corporate	6,755	4,498	19,504	15,289
Total	\$ 253,897	\$ 189,253	\$ 721,750	\$ 609,517
Segment performance measure				
Dental CAD/CAM Systems	\$ 56,075	\$ 44,920	\$ 170,270	\$ 143,354
Imaging Systems	49,553	37,307	138,040	116,483
Treatment Centers	18,788	14,349	57,261	49,025
Instruments	13,258	9,753	37,981	33,176
Total	137,674	106,329	403,552	342,038
Electronic center and corporate	2,102	1,271	7,199	6,457
Total	\$ 139,776	\$ 107,600	\$ 410,751	\$ 348,495
Depreciation and amortization expense				
Dental CAD/CAM Systems	\$ 2,113	\$ 1,440	\$ 5,847	\$ 4,254
Imaging Systems	1,623	1,293	4,494	3,928
Treatment Centers	1,916	1,464	5,118	4,791
Instruments	920	704	2,490	2,412
Total	6,572	4,901	17,949	15,385
Electronic center and corporate	255	272	823	1,439
Total	\$ 6,827	\$ 5,173	\$ 18,772	\$ 16,824

Table of Contents**SIRONA DENTAL SYSTEMS, INC AND SUBSIDIARIES****NOTES TO THE CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**

(UNAUDITED)

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 nine months ended June 30, 2011 and 2010 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 ended June 30,		Nine months ended June 30,	
	2011	2010	2011	2010
	\$ 000s		\$ 000s	
Revenue				
Total segments (external)	\$ 244,391	\$ 182,287	\$ 694,254	\$ 586,886
Electronic center and corporate	295	131	815	491
Consolidated revenue	244,686	182,418	695,069	587,377
Depreciation and amortization				
Total segments	6,572	4,901	17,949	15,385
Differences management reporting vs. US GAAP, electronic center and corporate	14,310	14,807	41,890	46,887
Consolidated depreciation and amortization	20,882	19,708	59,839	62,272
Segment performance measure				
Total segments	137,674	106,329	403,552	342,038
Differences management reporting vs. US GAAP, electronic center and corporate	(10,842)	(12,154)	(30,617)	(36,160)
Consolidated gross profit	126,832	94,175	372,935	305,878
Selling, general and administrative expense	68,540	54,994	202,444	175,200
Research and development	14,390	11,648	42,045	34,803
Provision for doubtful accounts and notes receivable	13	47	34	183
Net other operating income	(2,500)	(3,254)	(7,500)	(9,162)
Foreign currency transaction (gain)/loss, net	(3,435)	6,003	(8,532)	10,419
Loss/(Gain) on derivative instruments	1,081	2,598	1,162	(137)
Interest expense, net	984	857	2,863	10,200
Other expense/(income)	383	(9)	(140)	775
Income before taxes	\$ 47,376	\$ 21,291	\$ 140,559	\$ 83,597

Table of Contents

SIRONA DENTAL SYSTEMS, INC AND SUBSIDIARIES

NOTES TO THE CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(UNAUDITED)

18. Related parties

Sirona Holdings S.C.A. Luxembourg (Luxco)

On July 30, 2010, the Company and Luxco, a significant shareholder of the Company, elected not to renew the advisory services agreement between them that terminated on October 1, 2010. Under the agreement, which became effective October 1, 2005, the Company paid an annual fee to Luxco of 325 (approximately \$444 for fiscal year 2010), and Luxco provided to the Company certain advisory services regarding the structure, terms and condition of debt offerings by the Company, financing sources and options, business development and other services.

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.

In March 2011, Luxco sold 4,500,000 shares pursuant to an underwritten follow-on public offering. The Company incurred \$0.3 million of costs pursuant to the terms of a registration rights agreement.

In May 2011, Luxco sold 9,747,480 shares pursuant to an underwritten follow-on public offering. The Company incurred \$0.2 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, 2010. 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, 2010. 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, the Company, we, us, and our refer to Sirona Dental Systems, Inc. and its consolidated subsidiaries and predecessors) 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 approximately 130 years ago, the first dental X-ray unit approximately 100 years ago, the first dental computer-aided design/computer-aided manufacturing (CAD/CAM) system 25 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 product launches including: the SINIUS treatment center (launched in March 2011), the Orthophos XG3D (launched in October 2010), 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 28% and 19%, respectively, of Sirona's global revenues for the nine months ended June 30, 2011.

The U.S. market is the largest individual market for Sirona, followed by Germany. Between fiscal years 2004 and 2010, the Company increased U.S. revenues from \$88.2 million to \$239.5 million, driven by innovative products, particularly in the CAD/CAM and Imaging segments and the Exchange. 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 recognized on a straight-line basis that commenced at the beginning of the extension of the exclusivity period in fiscal year 2008.

Table of Contents

In addition to strong U.S. market growth, Sirona has pursued expansion in non-U.S. and non-German markets. Between fiscal years 2004 and 2010, the Company increased revenues in non-U.S. and non-German markets from \$190.9 million to \$382.4 million. To support this growth, Sirona expanded its local presence and distribution channels by establishing sales and service locations e.g. in Japan, Australia, China, Korea, Brazil, 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 revenue and financial performance. While the global economy improved in 2010, it did not fully recover and we continued to experience economic headwinds in fiscal year 2010. Despite these headwinds, Sirona increased revenues by 7.9% constant currency in fiscal year 2010, with strong growth in our Imaging segment driven by our Galileos 3D imaging system. In fiscal year 2010, our net income benefited from this revenue growth, but also from margin expansion, expense management initiatives, and debt reduction. Our targeted cost-saving actions were on plan, and we started reinvesting some of these cost savings in the second half of fiscal year 2010.

The positive trends from fiscal year 2010 strengthened during the first nine months of fiscal year 2011. This development is driven by robust demand for our technologically advanced product portfolio, a successful biennial International Dental Show (IDS) in Cologne at the end of March 2011, and our continued investment in our global sales and service infrastructure. Revenues were particularly strong in international markets during the first nine months of fiscal year 2011, up 29.5% on a constant currency basis. Our net income benefited from strong sales growth, margin expansion, and debt reduction.

Significant Factors that Affect Sirona's Results of Operations

The MDP Transaction and the Exchange

On June 30, 2005, Sirona Holdings Luxco S.C.A. (Luxco), a Luxembourg-based holding entity owned by funds managed by Madison Dearborn Partners, Beecken Petty O'Keefe, management and employees of Sirona, obtained control over the Sirona business. The transaction was effected by using new legal entities, Sirona Holding GmbH (formerly Blitz 05-118 GmbH) and its wholly owned subsidiary Sirona Dental Services GmbH, to acquire 100% of the interest in Sirona Dental Systems Beteiligungs- und Verwaltungen GmbH, the former parent of the Sirona business through a leveraged buy-out transaction (the MDP Transaction).

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 result 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 currencies vary depending on the country of operation. For the nine months ended June 30, 2011, approximately 52% of Sirona's revenue and approximately 71% of its expenses were in Euro. During the periods under review, the U.S. Dollar/Euro exchange rate has fluctuated significantly, thereby impacting Sirona's financial results. Between October 1, 2009 and June 30, 2011, the U.S. Dollar/Euro exchange rate used to calculate items included in Sirona's financial statements varied from a low of \$1.1919 to a high of \$1.5121. Although Sirona does not apply hedge accounting, Sirona has entered into foreign exchange forward contracts to manage foreign currency exposure. As of June 30, 2011, these contracts had notional amounts totaling \$39.6 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 above and 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

Table of Contents

foreign exchange rate for each month of the current period. The average exchange rate for the three months ended June 30, 2011, was \$1.43894 and varied from \$1.44395 to \$1.43446. The average exchange rate for the nine months ended June 30, 2011, was \$1.38876 and varied from \$1.44395 to \$1.32171. For the three and nine months ended June 30, 2010, an average quarterly exchange rate converting Euro denominated revenues into U.S. Dollars of \$1.27606 and \$1.37990, respectively, was applied.

Loans made to Sirona under the Senior Facilities Agreement entered into on 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;

timing of industry tradeshows, particularly the International Dental Show;

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;

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 future performance.

Effective Tax Rate

The Company's effective tax rate may vary significantly from period to period, and can be influenced by many factors. These factors include, but are not limited to, changes in the mix of earnings in countries with differing statutory tax rates (including as a result of business acquisitions and

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

dispositions), changes in the valuation of deferred tax assets and liabilities, the results of audits and examinations of previously filed tax returns, tax planning initiatives, tax characteristics of income, as well as the timing and deductibility of expenses for tax purposes. The Company's effective tax rate differs from the United States federal statutory rate of 35% primarily as a result of lower effective tax rates on certain earnings outside of the United States. The distribution of lower-taxed foreign earnings to the U.S. would generally increase the Company's effective tax rate.

Table of Contents

Results of Operations

Three Months Ended June 30, 2011 Compared to Three Months Ended June 30, 2010

Revenue

Revenue for the three months ended June 30, 2011 was \$244.7 million, an increase of \$62.3 million, or 34.1%, as compared with the three months ended June 30, 2010. On a constant currency basis, adjusting for the fluctuations in the U.S. Dollar/Euro exchange rate, total revenue increased by 24.0%. By segment, Imaging Systems increased 37.6% (up 29.6% on a constant currency basis), Treatment Centers increased 37.6% (up 22.1% on a constant currency basis), CAD/CAM Systems increased 31.5% (up 23.8% on a constant currency basis), and Instruments increased 26.0% (up 12.3% on a constant currency basis).

We were able to grow our revenues due to solid demand for our innovative products, and we continue to benefit from our increased global sales and service infrastructure. Our products enable dental professionals to improve their clinical results and to increase the profitability of their practices. Our presence at the IDS at the end of March 2011 demonstrated our innovative strength and the breadth of our products.

Imaging Systems revenues showed a strong increase driven by robust demand, particularly for our Orthophos product line. Growth was strong in all major markets. CAD/CAM Systems revenues benefited from robust growth in many international markets, led by Germany. Treatment Center revenue was driven by volume projects in the economy product line in non European international markets and a strong demand in Germany after the IDS. Instrument revenues benefited from robust demand particularly in Europe, with good unit sales growth, leading to gross profit margin improvement.

Revenue in the U.S. for the three months ended June 30, 2011 was up 11.8% compared to the prior year period. Revenue growth was particularly strong in the Imaging Systems segment. Revenue outside the U.S. increased by 45.6%. On a constant currency basis, adjusting for the fluctuations in the U.S. Dollar/Euro exchange rate, these revenues increased by 29.5%. Revenue growth was particularly strong in Germany, Asia-Pacific, and the Middle East.

Revenue growth on a constant currency basis was mainly volume driven.

Cost of Sales

Cost of sales for the three months ended June 30, 2011 was \$117.9 million, an increase of \$29.6 million, or 33.6%, as compared with the three months ended June 30, 2010. Gross profit as a percentage of revenue was 51.8% compared to 51.6% in the prior year period. Cost of sales included amortization and depreciation expense resulting from the step-up to fair values of tangible and intangible assets of \$12.9 million as well as non-cash share-based compensation expense of \$0.03 million for the three months ended June 30, 2011 compared to amortization and depreciation expense resulting from the step-up to fair values of tangible and intangible assets of \$13.4 million and non-cash share-based compensation expense of \$0.03 million for the three months ended June 30, 2010. Excluding these amounts, cost of sales as a percentage of revenue was 42.9% for the three months ended June 30, 2011 compared with 41.0% for the three months ended June 30, 2010, and therefore gross profit as a percentage of revenue was 57.1%, compared to 59.0% in the prior year period. The decrease in the gross profit margin was mainly due to product and regional mix as well as fluctuations in the U.S. Dollar/Euro exchange rate.

Selling, General and Administrative

For the three months ended June 30, 2011, SG&A expense was \$68.5 million, an increase of \$13.5 million, or 24.6%, as compared with the three months ended June 30, 2010. The increase in SG&A expense is mainly driven by increased revenues, as well as investments in sales and service infrastructure in international markets. SG&A expense included amortization and depreciation resulting from the step-up to fair values of tangible and intangible assets of \$0.7 million as well as non-cash share-based compensation expense in the amount of \$2.7 million for the three months ended June 30, 2011, compared with \$0.8 million and \$3.7 million, respectively, for the three months ended June 30, 2010. Excluding these amounts, as a percentage of revenue, SG&A expense decreased to 26.6% for the three months ended June 30, 2011, as compared with 27.7% for the three months ended June 30, 2010.

Research and Development

R&D expense for the three months ended June 30, 2011, was \$14.4 million, an increase of \$2.7 million, or 23.5%, as compared with the three months ended June 30, 2010. The increase of R&D expense was primarily driven by the timing of new product launches.

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

R&D expense included non-cash share-based compensation expense in the amount of \$0.04 million for the three months ended June 30, 2011, compared with \$0.05 million for the three months ended June 30, 2010. Excluding this amount, as a percentage of revenue, R&D expense decreased to 5.9% for the three months ended June 30, 2011, compared to 6.4% for the three months ended June 30, 2010.

Table of Contents***Net Other Operating Income***

Net other operating income for the three months ended June 30, 2011 and 2010 was \$2.5 million and \$3.3 million, respectively. In both periods, net other operating income included \$2.5 million of income resulting from the amortization of the deferred income relating to the Patterson exclusivity payment. In the three months ended June 30, 2010, net other operating income included \$0.8 million of income from the release of accrued restructuring costs.

(Gain)/Loss on Foreign Currency Transactions

Gain on foreign currency transactions for the three months ended June 30, 2011 amounted to \$3.4 million compared to a loss of \$6.0 million for the three months ended June 30, 2010. For the three months ended June 30, 2011, the gain included an unrealized non-cash foreign currency gain of \$1.2 million on the U.S. Dollar denominated deferred income from the translation adjustment of Patterson's exclusivity payment and an unrealized non-cash foreign currency gain on the short term intra-group loans to our Austrian entity of \$1.6 million. Excluding these amounts, foreign currency transactions for the three months ended June 30, 2011 resulted in a gain of \$0.6 million.

The loss for the three months ended June 30, 2010 included an unrealized non-cash foreign currency loss of \$6.7 million on the U.S. Dollar denominated deferred income from the translation adjustment of Patterson's exclusivity payment, as well as a non-cash unrealized foreign currency loss on the short term intra-group loans to our Austrian entity of \$5.8 million. Excluding these amounts, foreign currency transactions for the three months ended June 30, 2010 resulted in a gain of \$6.5 million.

Loss on Derivative Instruments

The loss on derivative instruments for the three months ended June 30, 2011, amounted to \$1.1 million compared to a loss of \$2.6 million for the three months ended June 30, 2010. For the three months ended June 30, 2011 and 2010, the loss represented a non-cash loss on foreign currency hedges of \$1.1 million and \$2.6 million, respectively.

Interest Expense

Net interest expense for the three months ended June 30, 2011, was \$1.0 million, compared to \$0.9 million for the three months ended June 30, 2010.

Income Tax Provision

For the three months ended June 30, 2011 and 2010, Sirona recorded a profit before income taxes of \$47.4 million and \$21.3 million, respectively. The estimated effective tax rate applied for these periods was 22% and 20%, respectively, compared to an actual effective tax rate of 20.6% in fiscal year 2010. The income tax provision for the three months ended June 30, 2011 and 2010, was \$10.4 million and \$4.3 million, respectively. The estimated effective tax rate is primarily driven by the expected mix of earnings across different countries.

Net Income

Net income for the three months ended June 30, 2011 was \$37.0 million, an increase of \$19.9 million, as compared with the three months ended June 30, 2010. Major influencing factors on net income were the increase in revenues and lower amortization, partially offset by the increase in operating expenses and a higher estimated effective tax rate. Net income for the three months ended June 30, 2011 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 \$13.7 million (\$10.7 million net of tax), unrealized, non-cash foreign currency gain on the deferred income from the Patterson exclusivity payment of \$1.2 million (\$0.9 million net of tax), and gain on the revaluation of short-term intra-group loans of \$1.6 million (\$1.2 million net of tax).

Sirona's net income for the three months ended June 30, 2010 included deal related amortization and depreciation of assets acquired in past business combinations of \$14.2 million (\$11.4 million net of tax), currency revaluation losses on the Patterson exclusivity payment of \$6.7 million (\$5.4 million after tax), a loss on the revaluation of short-term intra-group loans of \$5.8 million (\$4.6 million net of tax), and a gain of \$0.8 million (\$0.6 million net of tax) from the release of the remaining accrued restructuring costs.

Share-based compensation expense was \$2.8 million (\$2.2 million net of tax) in the third quarter of 2011 compared to \$3.8 million (\$3.0 million net of tax) in the prior year period.

Table of Contents

Nine Months Ended June 30, 2011 Compared to Nine Months Ended June 30, 2010

Revenue

Revenue for the nine months ended June 30, 2011 was \$695.1 million, an increase of \$107.7 million, or 18.3%, as compared with the nine months ended June 30, 2010. On a constant currency basis, adjusting for the fluctuations in the U.S. Dollar/Euro exchange rate, total revenue increased by 17.8%. By segment, Imaging Systems increased 21.5% (up 21.1% on a constant currency basis), CAD/CAM Systems increased 19.7% (up 19.3% on a constant currency basis), Treatment Centers increased 17.2% (up 16.4% on a constant currency basis), and Instruments increased 7.6% (up 7.0% on a constant currency basis).

We were able to grow our revenues in all segments due to solid 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.

The increase in Imaging Systems revenues showed in all regions and was driven by strong interest in our 2D and 3D panoramic systems. CAD/CAM Systems revenues were particularly strong in Europe and benefited from a trade-up program in Germany. Treatment Center revenues growth was particularly driven by non European international markets. Instrument revenues were up, benefiting from high-volume projects in several international markets.

Revenue in the U.S. for the nine months ended June 30, 2011 was up 5.1% compared to the prior year period. Revenue outside the U.S. increased by 24.7%. On a constant currency basis, adjusting for the fluctuations in the U.S. Dollar/Euro exchange rate, these revenues increased by 23.9%. Revenue growth was particularly strong in Europe, led by Germany, as well as in the Asia-Pacific market.

Revenue growth on a constant currency basis was mainly volume driven.

Cost of Sales

Cost of sales for the nine months ended June 30, 2011 was \$322.1 million, an increase of \$40.6 million, or 14.4%, as compared with the nine months ended June 30, 2010. Gross profit as a percentage of revenue was 53.7% compared to 52.1% in the prior year period. Cost of sales included amortization and depreciation expense resulting from the step-up to fair values of tangible and intangible assets of \$37.8 million as well as non-cash share-based compensation expense of \$0.1 million for the nine months ended June 30, 2011 compared to amortization and depreciation expense resulting from the step-up to fair values of tangible and intangible assets of \$42.6 million and non-cash share-based compensation expense of \$0.1 million for the nine months ended June 30, 2010. Excluding these amounts, cost of sales as a percentage of revenue was 40.9% for the nine months ended June 30, 2011 compared with 40.7% for the nine months ended June 30, 2010, and therefore gross profit as a percentage of revenue was 59.1% compared to 59.3% in the prior year period. The slight decrease in the gross profit margin was mainly due to product and regional mix.

Selling, General and Administrative

For the nine months ended June 30, 2011, SG&A expense was \$202.4 million, an increase of \$27.2 million, or 15.6%, as compared with the nine months ended June 30, 2010. The increase in the absolute SG&A expense is mainly driven by increased revenues, investments in sales and service infrastructure in international markets, and expenses related to the IDS. SG&A expense included amortization and depreciation resulting from the step-up to fair values of tangible and intangible assets of \$2.2 million as well as non-cash share-based compensation expense in the amount of \$7.0 million for the nine months ended June 30, 2011, compared with \$2.5 million and \$11.6 million, respectively, for the nine months ended June 30, 2010. Excluding these amounts, as a percentage of revenue, SG&A expense increased to 27.8% for the nine months ended June 30, 2011, as compared with 27.4% for the nine months ended June 30, 2010.

Research and Development

R&D expense for the nine months ended June 30, 2011, was \$42.0 million, an increase of \$7.2 million, or 20.8%, as compared with the nine months ended June 30, 2010. The increase of R&D expense was primarily driven by the timing of new product launches.

R&D expense included non-cash share-based compensation expense in the amount of \$0.1 million for the nine months ended June 30, 2011, compared with \$0.1 million for the nine months ended June 30, 2010. Excluding this amount, as a percentage of revenue, R&D expense increased to 6.0% for the nine months ended June 30, 2011, compared to 5.9% for the nine months ended June 30, 2010.

Table of Contents***Net Other Operating Income***

Net other operating income for the nine months ended June 30, 2011 and 2010 was \$7.5 million and \$9.2 million, respectively. In both periods, net other operating income included \$7.5 million of income resulting from the amortization of the deferred income relating to the Patterson exclusivity payment. For the three and nine months ended June 30, 2010, net other operating income included a gain from the sale of a subsidiary in Italy of \$0.9 million as well as a \$0.8 million gain from the release of the accrued restructuring expenses.

(Gain)/Loss on Foreign Currency Transactions

Gain on foreign currency transactions for the nine months ended June 30, 2011 amounted to \$8.5 million compared to a loss of \$10.4 million for the nine months ended June 30, 2010. For the nine months ended June 30, 2011, the gain included an unrealized non-cash foreign currency gain of \$3.7 million on the U.S. Dollar denominated deferred income from the translation adjustment of Patterson's exclusivity payment and an unrealized non-cash foreign currency gain on the short term intra-group loans to our Austrian entity of \$4.6 million. Excluding these amounts, foreign currency transactions for the nine months ended June 30, 2011 resulted in a gain of \$0.2 million.

The loss for the nine months ended June 30, 2010 included an unrealized non-cash foreign currency loss of \$13.2 million on the U.S. Dollar denominated deferred income from the translation adjustment of Patterson's exclusivity payment, as well as a non-cash unrealized foreign currency loss on the short term intra-group loans to our Austrian entity of \$11.5 million. Excluding these amounts, foreign currency transactions for the nine months ended June 30, 2010 resulted in a gain of \$14.3 million.

Loss/(Gain) on Derivative Instruments

The loss on derivative instruments for the nine months ended June 30, 2011, amounted to \$1.2 million compared to a gain of \$0.1 million for the nine months ended June 30, 2010. For the nine months ended June 30, 2011, the loss included an unrealized non-cash loss on foreign currency hedges of \$1.2 million. The gain for the nine months ended June 30, 2010, included an unrealized non-cash gain of \$6.4 million on interest swaps, as well as a non-cash loss on foreign currency hedges of \$6.3 million.

Interest Expense

Net interest expense for the nine months ended June 30, 2011, was \$2.9 million, compared to \$10.2 million for the nine months ended June 30, 2010. This decrease resulted from lower interest rates and lower overall debt levels.

Income Tax Provision

For the nine months ended June 30, 2011 and 2010, Sirona recorded a profit before income taxes of \$140.6 million and \$83.6 million, respectively. The estimated effective tax rate applied for these periods was 22% and 20%, respectively, compared to an actual effective tax rate of 20.6% in fiscal year 2010. The income tax provision for the nine months ended June 30, 2011 and 2010, was \$30.9 and \$16.7 million, respectively. The estimated effective tax rate is primarily driven by the expected mix of earnings across different countries.

Net Income

Net income for the nine months ended June 30, 2011 was \$109.6 million, an increase of \$42.8 million, as compared with the nine months ended June 30, 2010. Major influencing factors on net income were the increase in revenues, lower interest and debt levels, and the lower amortization of assets acquired in past business combinations, partially offset by the increase in operating expenses and a higher estimated effective tax rate. Net income for the nine months ended June 30, 2011 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 \$40.0 million (\$31.2 million net of tax), unrealized, non-cash foreign currency gain on the deferred income from the Patterson exclusivity payment of \$3.7 million (\$2.9 million net of tax), and gain on the revaluation of short-term intra-group loans of \$4.6 million (\$3.6 million net of tax).

Sirona's net income for the nine months ended June 30, 2010 included deal related amortization and depreciation of assets acquired in past business combinations of \$45.1 million (\$36.1 million net of tax), currency revaluation losses on the Patterson exclusivity payment of \$13.2 million (\$10.6 million after tax), a gain on interest swaps of \$6.3 million (\$5.0 million net of tax), a loss on the revaluation of short-term intra-group loans of \$11.5 million (\$9.2 million net of tax), a gain of \$0.8 million (\$0.6 million net of tax) from the release of the remaining accrued restructuring costs, and a gain from the sale of a subsidiary in Italy of \$0.9 million (\$0.7 million net of tax).

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

Share-based compensation expense was \$7.2 million (\$5.6 million net of tax) in the first nine months of fiscal year 2011 compared to \$11.8 million (\$9.4 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 believes that its operating cash flows and available cash (including restricted cash) will be sufficient to fund its working capital needs, research and development expenses, and anticipated capital expenditures for the foreseeable future. The Company anticipates using its current cash balance of \$331.2 million as of June 30, 2011, plus its expected operating cash flows and access to capital markets, to comply with its repayment obligations for the final senior debt tranche due in November 2011.

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 be 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 of March 31, 2011, the most recent period for which these ratios were calculated, the Company was in compliance with both ratios. For further information regarding the calculation of these ratios as of March 31, 2011, please see our Form 10-Q for the fiscal quarter ended March 31, 2011 under the caption Management's Discussion and Analysis of Financial Condition and Results of Operations Liquidity and Capital Resources.

Cash Flows

	Nine months ended June 30,	
	2011	2010
	\$ 000s	
Net cash provided by operating activities	\$ 105,446	\$ 135,996
Net cash used in investing activities	(58,279)	(14,890)
Net cash provided by/(used in) financing activities	18,161	(74,572)
Increase in cash during the period	\$ 65,328	\$ 46,534

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 \$105.4 million for the nine months ended June 30, 2011 compared to \$136.0 million for the nine months ended June 30, 2010. The primary contributing factor to the decrease in cash provided by operating cash flows in the nine months ended June 30, 2011 was an increase in accounts receivable and inventories, driven by the overall increase in revenues, which was strongest at the end of the quarter, as well as the expansion of our global sales and service infrastructure, resulting in higher working capital requirements.

Net Cash Used in Investing Activities

Net cash used in investing activities represents cash used for capital expenditures in the normal course of operating activities, financial investments, acquisitions and long-lived asset disposals. The primary contributors to the investing cash outflow in the nine months ended June 30, 2011 were the construction of the Center of Innovation in Bensheim, Germany, acquisition of a development stage entity, and capital expenditures in the course of normal operating activities. For the nine months ended June 30, 2010, net cash used in investing activities represented capital expenditures in the course of normal operating activities, partly offset by proceeds from the sale of a subsidiary in Italy.

Net Cash Provided by / (Used in) Financing Activities

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

Net cash provided by financing activities was \$18.2 million for the nine months ended June 30, 2011, compared to net cash used in financing activities of \$74.6 million for the nine months ended June 30, 2010. Net cash provided by financing activities in the nine months ended June 30, 2011 results from proceeds and tax-related benefits from exercises of options previously granted in the Company's stock-based compensation activities. Net cash used in financing activities in the nine months ended June 30, 2010 primarily relates to the early repayment of senior debt that was originally due in November 2010 eight months ahead of schedule and the purchase of additional shares from a noncontrolling interest, partly offset by proceeds and tax-related benefits of exercises of options previously granted in the Company's stock-based compensation activities.

Table of Contents

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 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.

Table of Contents**Other Financial Data**

	Three months ended June 30,		Nine months ended June 30,	
	2011	2010	2011	2010
	\$ 000s		\$ 000s	
Net income attributable to Sirona Dental Systems, Inc.	\$ 36,331	\$ 16,577	\$ 108,035	\$ 65,291
Net interest expense	984	857	2,863	10,200
Provision for income taxes	10,423	4,258	30,923	16,719
Depreciation	6,827	5,162	18,772	16,091
Amortization	14,055	14,521	41,067	46,181
EBITDA	\$ 68,620	\$ 41,375	\$ 201,660	\$ 154,482

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 the U.S. Dollar-denominated exclusivity payment and borrowings where the functional currency is the Euro, and the Exchange. Sirona's management believes that these items are either nonrecurring or non-cash in nature, and should be considered by investors in assessing Sirona's financial condition, operating performance and underlying strength.

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.

Table of Contents

Sirona 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

	Three months ended June 30,		Nine months ended June 30,	
	2011	2010	2011	2010
	\$ 000s		\$ 000s	
Share-based compensation	\$ 2,762	\$ 3,780	\$ 7,241	\$ 11,828
Unrealized, non-cash (gain)/loss on revaluation of the carrying value of the \$-denominated exclusivity fee	(1,248)	6,740	(3,718)	13,191
Unrealized, non-cash (gain)/loss on revaluation of the carrying value of short-term intra-group loans	(1,618)	5,835	(4,619)	11,506
	\$ (104)	\$ 16,355	\$ (1,096)	\$ 36,525

Recent Accounting Pronouncements Not Yet Adopted

Please see Note 2 to the unaudited condensed consolidated financial statements for any discussions 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 as reported under Part II, Item 7A in its Annual Report on Form 10-K for the fiscal year ended September 30, 2010.

ITEM 4. CONTROLS AND PROCEDURES

Evaluation of Disclosure Controls and Procedures

Our management, with the participation of our chief executive officer (principal executive officer) and chief financial officer (principal 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 June 30, 2011. Based upon this evaluation, our chief executive officer and chief financial officer concluded that, as of June 30, 2011, the Company's disclosure controls and procedures are 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 recorded, processed, summarized and reported within the time periods specified in Commission's rules and forms, and is accumulated and communicated to our management, including our principal executive officer and our principal financial officer, 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 Exchange Act) occurred during the quarter ended June 30, 2011, 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 1A of its Annual Report on Form 10-K for the fiscal year ended September 30, 2010 and in Part II, Item 1A of its Quarterly Report on Form 10-Q for the fiscal quarter ended March 31, 2011.

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

On August 4, 2011, certain existing shareholders in Sirona Holdings Luxco S.C.A. (Luxco), a former significant shareholder of the Registrant, informed the Registrant that they intended to make a one-time cash payment to the chief executive officer and chief financial officer of the Registrant in connection with their Luxco participation. These payments are expected to be made in the fourth quarter 2011 and will total \$6.625 million. The Registrant is required to record a non-cash compensation charge in that period as a result of such payment.

ITEM 6. EXHIBITS

The following Exhibits are included in this report:

Exhibit No.	Item Title
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.
101.INS	XBRL Instance Document
101.SCH	XBRL Taxonomy Extension Schema Document

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

101.CAL	XBRL Taxonomy Extension Calculation Linkbase Document
101.DEF	XBRL Taxonomy Extension Definition Linkbase Document
101.LAB	XBRL Extension Labels Linkbase Document
101.PRE	XBRL Taxonomy Extension Presentation Linkbase Document

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.

Sirona Dental Systems, Inc.

Date: August 5, 2011

By: /s/ Simone Blank
Simone Blank, Executive Vice President and
Chief Financial Officer
(Principal Financial and Accounting Officer)
(Duly authorized signatory)