TE Connectivity Ltd.
Form 10-Q
July 26, 2017

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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

(Mark One)

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

For the Quarterly Period Ended June 30, 2017

Or

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

001-33260
(Commission File Number)

TE CONNECTIVITY LTD.

(Exact name of registrant as specified in its charter)

Switzerland	**98-0518048**
(Jurisdiction of Incorporation)	(I.R.S. Employer Identification No.)

Rheinstrasse 20
CH-8200 Schaffhausen, Switzerland
(Address of principal executive offices)

+41 (0)52 633 66 61
(Registrant's telephone number)

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 ý No o

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 (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes ý No o

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

Large accelerated filer ý	Accelerated filer o	Non-accelerated filer o (Do not check if a smaller reporting company)	Smaller reporting company o Emerging growth company o

If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the Exchange Act. Yes o No o

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

The number of common shares outstanding as of July 21, 2017 was 353,384,098.

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PART I. FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS

TE CONNECTIVITY LTD.

CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS

(UNAUDITED)

	For the Quarters Ended		For the Nine Months Ended	
	June 30, 2017	June 24, 2016	June 30, 2017	June 24, 2016
	(in millions, except per share data)			
Net sales	$ 3,367	$ 3,121	$ 9,657	$ 8,906
Cost of sales	2,229	2,099	6,346	5,977
Gross margin	1,138	1,022	3,311	2,929
Selling, general, and administrative expenses	412	367	1,196	1,074
Research, development, and engineering expenses	170	161	490	479
Acquisition and integration costs	1	11	5	19
Restructuring and other charges (credits), net	19	31	125	(28)
Operating income	536	452	1,495	1,385
Interest income	3	2	14	12
Interest expense	(32)	(31)	(95)	(93)
Other expense, net	(4)	(651)	(6)	(631)
Income (loss) from continuing operations before income taxes	503	(228)	1,408	673
Income tax (expense) benefit	(71)	1,019	(164)	831
Income from continuing operations	432	791	1,244	1,504
Income from discontinued operations, net of income taxes	3	48	5	68
Net income	$ 435	$ 839	$ 1,249	$ 1,572
Basic earnings per share:				
Income from continuing operations	$ 1.22	$ 2.22	$ 3.50	$ 4.08
Income from discontinued operations	0.01	0.13	0.01	0.18
Net income	1.23	2.35	3.52	4.26
Diluted earnings per share:				
Income from continuing operations	$ 1.21	$ 2.19	$ 3.47	$ 4.03
Income from discontinued operations	0.01	0.13	0.01	0.18
Net income	1.22	2.32	3.48	4.21
Dividends paid per common share	$ 0.40	$ 0.37	$ 1.14	$ 1.03
Weighted-average number of shares outstanding:				
Basic	355	357	355	369

Diluted	358	361	359	373

See Notes to Condensed Consolidated Financial Statements.

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TE CONNECTIVITY LTD.

CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME

(UNAUDITED)

	For the Quarters Ended		For the Nine Months Ended	
	June 30, 2017	June 24, 2016	June 30, 2017	June 24, 2016
	(in millions)			
Net income.	$ 435	$ 839	$ 1,249	$ 1,572
Other comprehensive income (loss):				
Currency translation	77	8	(25)	(84)
Adjustments to unrecognized pension and postretirement benefit costs, net of income taxes	13	12	38	26
Gains (losses) on cash flow hedges, net of income taxes	(12)	54	23	56
Other comprehensive income (loss)	78	74	36	(2)
Comprehensive income.	$ 513	$ 913	$ 1,285	$ 1,570

See Notes to Condensed Consolidated Financial Statements.

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TE CONNECTIVITY LTD.

CONDENSED CONSOLIDATED BALANCE SHEETS

(UNAUDITED)

	June 30, 2017	September 30, 2016
	(in millions, except share data)	
Assets		
Current assets:		
Cash and cash equivalents	$ 755	$ 647
Accounts receivable, net of allowance for doubtful accounts of $20 and $17, respectively	2,271	2,046
Inventories	1,787	1,596
Prepaid expenses and other current assets	541	486
Total current assets	5,354	4,775
Property, plant, and equipment, net	3,165	3,052
Goodwill	5,516	5,492
Intangible assets, net	1,790	1,879
Deferred income taxes	2,287	2,111
Other assets	408	299
Total Assets	$ 18,520	$ 17,608
Liabilities and Shareholders' Equity		
Current liabilities:		
Short-term debt	$ 878	$ 331
Accounts payable	1,309	1,090
Accrued and other current liabilities	1,623	1,437
Deferred revenue	62	208
Total current liabilities	3,872	3,066
Long-term debt	3,113	3,739
Long-term pension and postretirement liabilities	1,494	1,502
Deferred income taxes	197	207
Income taxes	283	247
Other liabilities	420	362
Total Liabilities	9,379	9,123
Commitments and contingencies (Note 9)		
Shareholders' equity:		
Common shares, CHF 0.57 par value, 357,069,981 shares authorized and issued, and 382,835,381 shares authorized and issued, respectively	157	168
Contributed surplus		1,801
Accumulated earnings	9,747	8,682
Treasury shares, at cost, 3,380,507 and 27,554,005 shares, respectively	(257)	(1,624)
Accumulated other comprehensive loss	(506)	(542)
Total Shareholders' Equity	9,141	8,485

Total Liabilities and Shareholders' Equity	$	18,520	$	17,608

See Notes to Condensed Consolidated Financial Statements.

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TE CONNECTIVITY LTD.

CONDENSED CONSOLIDATED STATEMENTS OF SHAREHOLDERS' EQUITY

(UNAUDITED)

	Common Shares		Treasury Shares		Contributed Surplus	Accumulated Earnings	Accumulated Other Comprehensive Loss	Total Shareholders' Equity
	Shares	Amount	Shares	Amount				
					(in millions)			
Balance at September 30, 2016	383	$ 168	(28)	$ (1,624)	$ 1,801	$ 8,682	$ (542)	$ 8,485
Adoption of ASU No. 2016-09						165		165
Net income						1,249		1,249
Other comprehensive income							36	36
Share-based compensation expense					73			73
Dividends approved					(566)			(566)
Exercise of share options			3	86				86
Restricted share award vestings and other activity			1	155	(156)			(1)
Repurchase of common shares			(5)	(386)				(386)
Cancellation of treasury shares	(26)	(11)	26	1,512	(1,152)	(349)		
Balance at June 30, 2017	357	$ 157	(3)	$ (257)	$	$ 9,747	$ (506)	$ 9,141

	Common Shares		Treasury Shares		Contributed Surplus	Accumulated Earnings	Accumulated Other Comprehensive Loss	Total Shareholders' Equity
Balance at September 25, 2015	414	$ 182	(20)	$ (1,256)	$ 4,359	$ 6,673	$ (373)	$ 9,585
Net income						1,572		1,572
Other comprehensive loss							(2)	(2)
Share-based compensation expense					67			67
Dividends approved					(514)			(514)
Exercise of share options			2	77				77
Restricted share award vestings and other activity			2	128	(134)			(6)
Repurchase of common shares			(41)	(2,514)				(2,514)
Cancellation of treasury shares	(31)	(14)	31	2,006	(1,992)			
Balance at June 24, 2016	383	$ 168	(26)	$ (1,559)	$ 1,786	$ 8,245	$ (375)	$ 8,265

See Notes to Condensed Consolidated Financial Statements.

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TE CONNECTIVITY LTD.

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

(UNAUDITED)

	For the Nine Months Ended June 30, 2017	June 24, 2016
	(in millions)	
Cash Flows From Operating Activities:		
Net income	$ 1,249	$ 1,572
Income from discontinued operations, net of income taxes	(5)	(68)
Income from continuing operations	1,244	1,504
Adjustments to reconcile income from continuing operations to net cash provided by operating activities:		
Depreciation and amortization	469	438
Deferred income taxes	(146)	162
Provision for losses on accounts receivable and inventories	15	27
Tax sharing expense	6	632
Share-based compensation expense	73	66
Gain on divestiture		(143)
Other	17	84
Changes in assets and liabilities, net of the effects of acquisitions and divestitures:		
Accounts receivable, net	(260)	15
Inventories	(195)	(2)
Prepaid expenses and other current assets	(6)	302
Accounts payable	217	(4)
Accrued and other current liabilities	56	(68)
Deferred revenue	(150)	(22)
Income taxes	54	(1,735)
Other	55	6
Net cash provided by continuing operating activities	1,449	1,262
Net cash provided by (used in) discontinued operating activities	(1)	1
Net cash provided by operating activities	1,448	1,263
Cash Flows From Investing Activities:		
Capital expenditures	(452)	(420)
Proceeds from sale of property, plant, and equipment	12	3
Acquisition of businesses, net of cash acquired	(77)	(994)
Proceeds from divestiture of business, net of cash retained by sold business	4	326
Other	(25)	28
Net cash used in investing activities	(538)	(1,057)
Cash Flows From Financing Activities:		
Net increase (decrease) in commercial paper	(162)	300
Proceeds from issuance of debt	89	350
Repayment of debt		(500)
Proceeds from exercise of share options	86	77
Repurchase of common shares	(376)	(2,657)
Payment of common share dividends to shareholders	(405)	(377)

Other	(24)	(29)
Net cash used in continuing financing activities	(792)	(2,836)
Net cash provided by (used in) discontinued financing activities	1	(1)
Net cash used in financing activities	(791)	(2,837)
Effect of currency translation on cash	(11)	(4)
Net increase (decrease) in cash and cash equivalents	108	(2,635)
Cash and cash equivalents at beginning of period	647	3,329
Cash and cash equivalents at end of period	$ 755	$ 694

See Notes to Condensed Consolidated Financial Statements.

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TE CONNECTIVITY LTD.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

1. Basis of Presentation and Accounting Pronouncements

Basis of Presentation

The unaudited Condensed Consolidated Financial Statements of TE Connectivity Ltd. ("TE Connectivity" or the "Company," which may be referred to as "we," "us," or "our") have been prepared in United States ("U.S.") dollars, in accordance with accounting principles generally accepted in the U.S. ("GAAP") and the instructions to Form 10-Q under the Securities Exchange Act of 1934, as amended. In management's opinion, the unaudited Condensed Consolidated Financial Statements contain all normal recurring adjustments necessary for a fair presentation of interim results. The results of operations reported for interim periods are not necessarily indicative of the results of operations for the entire fiscal year or any subsequent interim period.

The year-end balance sheet data was derived from audited financial statements, but does not include all of the information and disclosures required by GAAP. These financial statements should be read in conjunction with our audited Consolidated Financial Statements contained in our Annual Report on Form 10-K for the fiscal year ended September 30, 2016.

Unless otherwise indicated, references in the Condensed Consolidated Financial Statements to fiscal 2017 and fiscal 2016 are to our fiscal years ending September 29, 2017 and ended September 30, 2016, respectively.

Recently Issued Accounting Pronouncement

In May 2014, the Financial Accounting Standards Board ("FASB") issued Accounting Standards Update ("ASU") No. 2014-09 which created new Accounting Standards Codification ("ASC") topic 606, *Revenue from Contracts with Customers*. This guidance supersedes ASC 605, *Revenue Recognition*, and introduces a single, comprehensive, five-step revenue recognition model. ASC 606 also enhances disclosures related to revenue recognition. ASC 606, as amended, is effective for us in the first quarter of fiscal 2019 and allows for either a full retrospective or a modified retrospective approach at adoption. We are continuing to assess the impact of adopting ASC 606 and intend to use a modified retrospective approach. Based on the initial evaluation of our current contracts and revenue streams, we do not expect that adoption will have a material impact on our results of operations or financial position. We believe we are following an appropriate timeline to allow for the proper recognition, reporting, and disclosure of revenue upon adoption of ASC 606 at the beginning of fiscal 2019.

Recently Adopted Accounting Pronouncement

In March 2016, the FASB issued ASU No. 2016-09, an update to ASC 718, *Compensation Stock Compensation*, to simplify various aspects of accounting for share-based payments to employees. We elected to early adopt this update in the first quarter of fiscal 2017. The provisions of the update addressing the accounting for excess tax benefits and deficiencies were adopted using a modified retrospective transition approach, with a cumulative-effect adjustment to beginning accumulated earnings and a corresponding increase in deferred tax assets of $165 million. The provision of the update addressing the presentation on the statement of cash flows of employee taxes paid via the withholding of shares was applied retrospectively and did not have a material impact on our Condensed Consolidated Financial Statements. Adoption of other provisions, which were applied prospectively, also did not have a material impact on our Condensed Consolidated Financial Statements.

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TE CONNECTIVITY LTD.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED) (Continued)

2. Restructuring and Other Charges (Credits), Net

Net restructuring and other charges (credits) consisted of the following:

	For the Quarters Ended		For the Nine Months Ended	
	June 30, 2017	June 24, 2016	June 30, 2017	June 24, 2016
	(in millions)			
Restructuring charges, net	$ 19	$ 25	$ 124	$ 86
(Gain) loss on divestiture		3		(143)
Other charges		3	1	29
	$ 19	$ 31	$ 125	$ (28)

Restructuring Charges, Net

Net restructuring charges by segment were as follows:

	For the Quarters Ended		For the Nine Months Ended	
	June 30, 2017	June 24, 2016	June 30, 2017	June 24, 2016
	(in millions)			
Transportation Solutions	$ 3	$ 20	$ 60	$ 39
Industrial Solutions	14	1	53	24
Communications Solutions	2	4	11	23
Restructuring charges, net	$ 19	$ 25	$ 124	$ 86

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TE CONNECTIVITY LTD.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED) (Continued)

2. Restructuring and Other Charges (Credits), Net (Continued)

Activity in our restructuring reserves during the nine months ended June 30, 2017 is summarized as follows:

	Balance at September 30, 2016	Charges	Changes in Estimates	Cash Payments	Non-Cash Items	Currency Translation	Balance at June 30, 2017
				(in millions)			
Fiscal 2017 Actions:							
Employee severance	$	$ 104	$ (1)	$ (21)	$	$ 3	$ 85
Facility and other exit costs		2		(1)			1
Property, plant, and equipment		14			(14)		
Total		120	(1)	(22)	(14)	3	86
Fiscal 2016 Actions:							
Employee severance	54	8	(1)	(24)			37
Facility and other exit costs		2		(2)			
Total	54	10	(1)	(26)			37
Pre-Fiscal 2016 Actions:							
Employee severance	25		(4)	(6)			15
Facility and other exit costs	12			(3)			9
Total	37		(4)	(9)			24
Total Activity	$ 91	$ 130	$ (6)	$ (57)	$ (14)	$ 3	$ 147

Fiscal 2017 Actions

During fiscal 2017, we initiated a restructuring program associated with footprint consolidation related to recent acquisitions and structural improvements impacting all segments. In connection with this program, during the nine months ended June 30, 2017, we recorded net restructuring charges of $119 million. We expect to complete all restructuring actions commenced during the nine months ended June 30, 2017 by the end of fiscal 2018 and to incur total charges of approximately $130 million with remaining charges primarily related to employee severance.

The following table summarizes expected, incurred, and remaining charges for the fiscal 2017 program by segment:

	Total Expected Charges	Cumulative Charges Incurred	Remaining Expected Charges
		(in millions)	
Transportation Solutions	$ 63	$ 59	$ 4

Industrial Solutions	57	52	5
Communications Solutions	10	8	2
Total	$ 130	$ 119	$ 11

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TE CONNECTIVITY LTD.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED) (Continued)

2. Restructuring and Other Charges (Credits), Net (Continued)

Fiscal 2016 Actions

During fiscal 2016, we initiated a restructuring program associated with headcount reductions impacting all segments and product line closures in the Communications Solutions segment. In connection with this program, during the nine months ended June 30, 2017 and June 24, 2016, we recorded net restructuring charges of $9 million and $87 million, respectively. We expect to complete all restructuring actions commenced during fiscal 2016 by the end of fiscal 2019 and to incur total charges of approximately $165 million with remaining charges related primarily to employee severance.

The following table summarizes expected, incurred, and remaining charges for the fiscal 2016 program by segment:

	Total Expected Charges	Cumulative Charges Incurred	Remaining Expected Charges
		(in millions)	
Transportation Solutions	$ 43	$ 40	$ 3
Industrial Solutions	30	29	1
Communications Solutions	92	70	22
Total	$ 165	$ 139	$ 26

Pre-Fiscal 2016 Actions

Prior to fiscal 2016, we initiated a restructuring program associated with headcount reductions and product line closures, primarily impacting the Communications Solutions and Industrial Solutions segments. During the nine months ended June 30, 2017 and June 24, 2016, we recorded net restructuring credits of $4 million and $1 million, respectively, related to pre-fiscal 2016 actions. We do not expect to incur any additional charges related to pre-fiscal 2016 actions.

Total Restructuring Reserves

Restructuring reserves included on the Condensed Consolidated Balance Sheets were as follows:

	June 30, 2017	September 30, 2016
	(in millions)	
Accrued and other current liabilities	$ 127	$ 64
Other liabilities	20	27
Restructuring reserves	$ 147	$ 91

Gain on Divestiture

During the quarter ended March 25, 2016, we sold our Circuit Protection Devices ("CPD") business for net cash proceeds of $326 million, subject to working capital adjustments. We recognized a pre-tax gain of $143 million on the transaction during the nine months ended June 24, 2016. The CPD business was reported in our Communications Solutions segment.

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TE CONNECTIVITY LTD.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED) (Continued)

2. Restructuring and Other Charges (Credits), Net (Continued)

Other Charges

During the nine months ended June 24, 2016, we incurred charges of $15 million related to the write-off of certain investments and costs of $14 million associated with the divestiture of certain businesses.

3. Discontinued Operations

Income from discontinued operations for the quarter ended June 24, 2016 included pre-tax credits of $30 million recorded in connection with the settlement of the Com-Net case related to our former Wireless Systems business which was sold in fiscal 2009.

During fiscal 2015, we sold our Broadband Network Solutions ("BNS") business and recognized a pre-tax gain of $1.1 billion on the transaction. During the nine months ended June 24, 2016, we recognized an additional pre-tax gain of $21 million on the divestiture, related primarily to pension and net working capital adjustments.

The Wireless Systems and BNS businesses met the discontinued operations criteria and were reported as such in all periods presented on the Condensed Consolidated Financial Statements. Prior to reclassification to discontinued operations, the Wireless Systems and BNS businesses were included in the former Wireless Systems and Network Solutions segments, respectively.

4. Acquisitions

During the quarter ended June 30, 2017, we acquired MicroGroup, a manufacturer of specialized metal tubing for medical devices, for a cash purchase price of $77 million, net of cash acquired. This business will be reported as part of our Industrial Solutions segment.

During the nine months ended June 24, 2016, we acquired three businesses, including the Creganna Medical group. The following unaudited pro forma financial information reflects our consolidated results of operations had the fiscal 2016 acquisitions occurred at the beginning of fiscal 2015:

	Pro Forma for the Quarter Ended June 24, 2016	Pro Forma for the Nine Months Ended June 24, 2016
	(in millions, except per share data)	
Net sales	$ 3,128	$ 9,065
Net income	839	1,584
Diluted earnings per share	$ 2.32	$ 4.25

The pro forma adjustments, which were not significant, included interest expense based on pro forma changes in our combined capital structure, charges related to acquired customer order backlog, charges related to the amortization of the fair value of acquired intangible assets, charges related to the fair value adjustment to acquisition-date inventories, and acquisition and other costs, and the related tax effects.

Pro forma results do not include any anticipated synergies or other anticipated benefits of these acquisitions. Accordingly, the unaudited pro forma financial information is not necessarily indicative of

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TE CONNECTIVITY LTD.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED) (Continued)

4. Acquisitions (Continued)

either future results of operations or results that might have been achieved had the fiscal 2016 acquisitions occurred at the beginning of fiscal 2015.

5. Inventories

Inventories consisted of the following:

	June 30, 2017	September 30, 2016
	(in millions)	
Raw materials	$ 281	$ 241
Work in progress	563	504
Finished goods	791	669
Inventoried costs on long-term contracts	152	182
Inventories	$ 1,787	$ 1,596

6. Goodwill

The changes in the carrying amount of goodwill by segment were as follows:

	Transportation Solutions	Industrial Solutions	Communications Solutions	Total
		(in millions)		
September 30, 2016[(1)]	$ 1,903	$ 3,005	$ 584	$ 5,492
Currency translation and other[(2)]	6	15	3	24
June 30, 2017[(1)]	$ 1,909	$ 3,020	$ 587	$ 5,516

(1) At June 30, 2017 and September 30, 2016, accumulated impairment losses for the Transportation Solutions, Industrial Solutions, and Communications Solutions segments were $2,191 million, $669 million, and $1,514 million, respectively.

(2) Includes $50 million of goodwill recognized in connection with the acquisition of MicroGroup and a reduction of goodwill of $33 million associated with adjustments made to the purchase price allocation of certain fiscal 2016 acquisitions primarily within the Industrial Solutions segment.

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TE CONNECTIVITY LTD.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED) (Continued)

7. Intangible Assets, Net

Intangible assets consisted of the following:

	June 30, 2017			September 30, 2016		
	Gross Carrying Amount	Accumulated Amortization	Net Carrying Amount	Gross Carrying Amount	Accumulated Amortization	Net Carrying Amount
	(in millions)					
Customer relationships	$ 1,363	$ (276)	$ 1,087	$ 1,332	$ (212)	$ 1,120
Intellectual property	1,233	(551)	682	1,300	(563)	737
Other	36	(15)	21	36	(14)	22
Total	$ 2,632	$ (842)	$ 1,790	$ 2,668	$ (789)	$ 1,879

Intangible asset amortization expense was $43 million and $40 million for the quarters ended June 30, 2017 and June 24, 2016, respectively, and $126 million and $108 million for the nine months ended June 30, 2017 and June 24, 2016, respectively.

The aggregate amortization expense on intangible assets is expected to be as follows:

	(in millions)
Remainder of fiscal 2017	$ 44
Fiscal 2018	176
Fiscal 2019	174
Fiscal 2020	166
Fiscal 2021	163
Fiscal 2022	162
Thereafter	905
Total	$ 1,790

8. Debt

During the nine months ended June 30, 2017, we reclassified $708 million of 6.55% senior notes due 2017 from long-term debt to short-term debt on the Condensed Consolidated Balance Sheet.

As of June 30, 2017, Tyco Electronics Group S.A. ("TEGSA"), our 100%-owned subsidiary, had $168 million of commercial paper outstanding at a weighted-average interest rate of 1.40%. TEGSA had $330 million of commercial paper outstanding at a weighted-average interest rate of 0.69% at September 30, 2016.

The fair value of our debt, based on indicative valuations, was approximately $4,242 million and $4,424 million at June 30, 2017 and September 30, 2016, respectively.

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TE CONNECTIVITY LTD.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED) (Continued)

9. Commitments and Contingencies

Legal Proceedings

In the normal course of business, we are subject to various legal proceedings and claims, including patent infringement claims, product liability matters, employment disputes, disputes on agreements, other commercial disputes, environmental matters, antitrust claims, and tax matters, including non-income tax matters such as value added tax, sales and use tax, real estate tax, and transfer tax. Although it is not feasible to predict the outcome of these proceedings, based upon our experience, current information, and applicable law, we do not expect that the outcome of these proceedings, either individually or in the aggregate, will have a material effect on our results of operations, financial position, or cash flows.

Environmental Matters

We are involved in various stages of investigation and cleanup related to environmental remediation matters at a number of sites. The ultimate cost of site cleanup is difficult to predict given the uncertainties regarding the extent of the required cleanup, the interpretation of applicable laws and regulations, and alternative cleanup methods. As of June 30, 2017, we concluded that it was probable that we would incur remedial costs in the range of $16 million to $43 million, and that the best estimate within this range was $19 million. We believe that any potential payment of such estimated amounts will not have a material adverse effect on our results of operations, financial position, or cash flows.

Guarantees

In disposing of assets or businesses, we often provide representations, warranties, and/or indemnities to cover various risks including unknown damage to assets, environmental risks involved in the sale of real estate, liability for investigation and remediation of environmental contamination at waste disposal sites and manufacturing facilities, and unidentified tax liabilities and legal fees related to periods prior to disposition. We do not expect that these uncertainties will have a material adverse effect on our results of operations, financial position, or cash flows.

At June 30, 2017, we had outstanding letters of credit, letters of guarantee, and surety bonds of $285 million.

In the normal course of business, we are liable for contract completion and product performance. In the opinion of management, such obligations will not materially affect our results of operations, financial position, or cash flows.

We generally record estimated product warranty costs when contract revenues are recognized under the percentage-of-completion method for construction related contracts; other warranty reserves are not significant. The estimation is based primarily on historical experience and actual warranty claims. Amounts accrued for warranty claims were $52 million and $48 million at June 30, 2017 and September 30, 2016, respectively.

Tax Sharing Agreement

As previously reported, under a Tax Sharing Agreement, we, Tyco International plc ("Tyco International"), and Covidien plc ("Covidien") share 31%, 27%, and 42%, respectively, of income tax

TE CONNECTIVITY LTD.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED) (Continued)

9. Commitments and Contingencies (Continued)

liabilities that arise from adjustments made by tax authorities to the collective income tax returns for certain of our, Tyco International's, and Covidien's income tax liabilities for periods prior to and including June 29, 2007. Pursuant to the Tax Sharing Agreement, we entered into certain guarantee commitments and indemnifications with Tyco International and Covidien. We have substantially settled all U.S. federal income tax matters with the Internal Revenue Service ("IRS") for periods covered under the Tax Sharing Agreement. Certain shared U.S. state and non-U.S. income tax matters remain open. We do not expect these matters will have a material effect on our results of operations, financial position, or cash flows.

10. Financial Instruments

We hedge our net investment in certain foreign operations using intercompany non-derivative financial instruments denominated in the same currencies. The aggregate notional value of these hedges was $3,762 million and $3,480 million at June 30, 2017 and September 30, 2016, respectively. The impacts of our hedging program were as follows:

	For the Quarters Ended		For the Nine Months Ended	
	June 30, 2017	June 24, 2016	June 30, 2017	June 24, 2016
	(in millions)			
Foreign exchange gains (losses)	$ (129)	$ 5	$ 15	$ 6

These foreign exchange gains and losses were recorded as currency translation, a component of accumulated other comprehensive loss, offsetting foreign exchange losses and gains attributable to the translation of the net investment.

11. Retirement Plans

The net periodic pension benefit cost for all U.S. and non-U.S. defined benefit pension plans was as follows:

	U.S. Plans For the Quarters Ended		Non-U.S. Plans For the Quarters Ended	
	June 30, 2017	June 24, 2016	June 30, 2017	June 24, 2016
	(in millions)			
Service cost	$ 3	$ 3	$ 13	$ 11
Interest cost	11	12	9	13
Expected return on plan assets	(13)	(15)	(18)	(17)
Amortization of net actuarial loss	10	10	11	9
Amortization of prior service credit			(2)	(1)
Net periodic pension benefit cost	$ 11	$ 10	$ 13	$ 15

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TE CONNECTIVITY LTD.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED) (Continued)

11. Retirement Plans (Continued)

	U.S. Plans For the Nine Months Ended		Non-U.S. Plans For the Nine Months Ended	
	June 30, 2017	June 24, 2016	June 30, 2017	June 24, 2016
	(in millions)			
Service cost	$ 9	$ 7	$ 39	$ 35
Interest cost	33	37	27	40
Expected return on plan assets	(40)	(44)	(53)	(52)
Amortization of net actuarial loss	30	30	32	27
Amortization of prior service credit			(5)	(4)
Net periodic pension benefit cost	$ 32	$ 30	$ 40	$ 46

During the nine months ended June 30, 2017, we contributed $30 million to our non-U.S. pension plans.

12. Income Taxes

During the quarter and nine months ended June 30, 2017, we recorded income tax expense of $71 million and $164 million, respectively. The income tax expense for the quarter and nine months ended June 30, 2017 included a $14 million income tax benefit associated with pre-separation tax matters. The income tax expense for the nine months ended June 30, 2017 also included a $52 million income tax benefit associated with the tax impacts of certain intercompany transactions and the corresponding reduction in the valuation allowance for U.S. tax loss carryforwards, as well as a $24 million income tax benefit resulting from lapses of statutes of limitations in the U.S. and certain non-U.S. jurisdictions.

During the quarter and nine months ended June 24, 2016, we recorded an income tax benefit of $1,019 million and $831 million, respectively. These income tax benefits included a $1,135 million income tax benefit related to the effective settlement of pre-separation tax matters for the years 1997 through 2000 which resolved all aspects of a disputed debt matter with the IRS through the year 2007, partially offset by a $91 million increase to the valuation allowance for deferred tax assets primarily related to certain U.S. federal and state tax loss and credit carryforwards. Based on our forecast of taxable income for certain U.S. tax reporting groups, U.S. tax loss and credit carryforwards finalized as a result of settlement of the disputed debt matter with the IRS, and certain tax planning actions and strategies, we believed it was more likely than not that a portion of our deferred tax assets would not be realized. Additionally, the income tax benefits recorded during the quarter and nine months ended June 24, 2016 included an $83 million net income tax benefit related to tax settlements in certain other tax jurisdictions, partially offset by an income tax charge related to certain legal entity restructurings.

During the nine months ended June 24, 2016, we made a payment to the IRS of $443 million for tax deficiencies associated with the disputed debt matter discussed above. Concurrent with remitting this payment, we received net reimbursements of $303 million from Tyco International and Covidien pursuant to indemnifications for pre-separation U.S. tax matters.

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TE CONNECTIVITY LTD.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED) (Continued)

12. Income Taxes (Continued)

We record accrued interest and penalties related to uncertain tax positions as part of income tax expense. As of June 30, 2017 and September 30, 2016, we had $57 million and $54 million, respectively, of accrued interest and penalties related to uncertain tax positions on the Condensed Consolidated Balance Sheets, recorded primarily in income taxes. During the nine months ended June 30, 2017, we recognized income tax benefits of $7 million related to interest and penalties on the Condensed Consolidated Statement of Operations.

Although it is difficult to predict the timing or results of our worldwide examinations, we estimate that approximately $50 million of unrecognized income tax benefits, excluding the impact relating to accrued interest and penalties, could be resolved within the next twelve months.

We are not aware of any other matters that would result in significant changes to the amount of unrecognized income tax benefits reflected on the Condensed Consolidated Balance Sheet as of June 30, 2017.

13. Other Expense, Net

During the quarters and nine months ended June 30, 2017 and June 24, 2016, we recorded net other expense primarily pursuant to the Tax Sharing Agreement with Tyco International and Covidien. Net other expense of $651 million and $631 million, recorded during the quarter and nine months ended June 24, 2016, respectively, included $604 million related to the effective settlement of pre-separation tax matters for the years 1997 through 2000 which resolved all aspects of a disputed debt matter with the IRS through the year 2007 and $46 million related to a tax settlement in another jurisdiction. See Notes 9 and 12 for further information regarding the Tax Sharing Agreement and the settlement with the IRS, respectively.

14. Earnings Per Share

The weighted-average number of shares outstanding used in the computations of basic and diluted earnings per share were as follows:

	For the Quarters Ended		For the Nine Months Ended	
	June 30, 2017	June 24, 2016	June 30, 2017	June 24, 2016
	(in millions)			
Basic	355	357	355	369
Dilutive impact of share-based compensation arrangements	3	4	4	4
Diluted	358	361	359	373

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TE CONNECTIVITY LTD.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED) (Continued)

14. Earnings Per Share (Continued)

The following share options were not included in the computation of diluted earnings per share because the instruments' underlying exercise prices were greater than the average market prices of our common shares and inclusion would be antidilutive.

	For the Quarters Ended		For the Nine Months Ended	
	June 30, 2017	June 24, 2016	June 30, 2017	June 24, 2016
	(in millions)			
Antidilutive share options		3	1	3

15. Equity

Common Shares Held in Treasury

In March 2017, our shareholders approved the cancellation of 26 million shares purchased under our share repurchase program during the period from December 11, 2015 to September 30, 2016. The capital reduction by cancellation of these shares was subject to a notice period and filing with the commercial register in Switzerland and became effective in May 2017.

Contributed Surplus

During the nine months ended June 30, 2017, cumulative equity transactions, including dividend activity and treasury share cancellations, have reduced our contributed surplus balance to zero with residual activity recorded against accumulated earnings as reflected on the Condensed Consolidated Statement of Shareholders' Equity. To the extent that the contributed surplus balance continues to be zero, the impact of future transactions that normally would have been recorded as a reduction of contributed surplus will be recorded in accumulated earnings.

As previously disclosed, contributed surplus established for Swiss tax and statutory purposes, which we can distribute free from withholding tax and is updated annually, was CHF 7,878 million (equivalent to $6,992 million) at September 30, 2016 and is not impacted by our GAAP treatment.

Dividends

In March 2017, our shareholders approved a dividend payment to shareholders of $1.60 (equivalent to CHF 1.62) per share, payable in four equal quarterly installments beginning in the third quarter of fiscal 2017 through the second quarter of fiscal 2018. We paid the first installment of the dividend at a rate of $0.40 per share in the quarter ended June 30, 2017.

Upon shareholders' approval of a dividend payment, we record a liability with a corresponding charge to shareholders' equity. At June 30, 2017 and September 30, 2016, the unpaid portion of the dividends recorded in accrued and other current liabilities on the Condensed Consolidated Balance Sheets totaled $424 million and $263 million, respectively.

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TE CONNECTIVITY LTD.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED) (Continued)

15. Equity (Continued)

Share Repurchase Program

Common shares repurchased under the share repurchase program were as follows:

	For the Nine Months Ended June 30, 2017	For the Nine Months Ended June 24, 2016
	(in millions)	
Number of common shares repurchased	5	41
Repurchase value	$ 386	$ 2,514

At June 30, 2017, we had $716 million of availability remaining under our share repurchase authorization.

16. Share Plans

Share-based compensation expense, which was included in selling, general, and administrative expenses on the Condensed Consolidated Statements of Operations, was as follows:

	For the Quarters Ended June 30, 2017	For the Quarters Ended June 24, 2016	For the Nine Months Ended June 30, 2017	For the Nine Months Ended June 24, 2016
	(in millions)			
Share-based compensation expense	$ 26	$ 23	$ 73	$ 66

As of June 30, 2017, there was $154 million of unrecognized compensation expense related to share-based awards, which is expected to be recognized over a weighted-average period of 2.0 years.

During the quarter ended December 30, 2016, we granted the following share-based awards as part of our annual incentive plan grant:

	Shares	Weighted-Average Grant-Date Fair Value
	(in millions)	
Share options	2.1	$ 12.79
Restricted share awards	0.7	66.74
Performance share awards	0.3	66.74

In March 2017, our shareholders approved an increase of 10 million shares in the number of shares available for awards under the TE Connectivity Ltd. 2007 Stock and Incentive Plan, amended and restated as of March 8, 2017 (the "2017 Plan"). As of June 30, 2017, we had 23 million shares available for issuance under our stock and incentive plans, of which the 2017 Plan was the primary plan.

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TE CONNECTIVITY LTD.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED) (Continued)

16. Share Plans (Continued)

Share-Based Compensation Assumptions

The weighted-average assumptions we used in the Black-Scholes-Merton option pricing model for the options granted as part of our annual incentive plan grant were as follows:

Expected share price volatility	24%
Risk free interest rate	1.9%
Expected annual dividend per share	$ 1.48
Expected life of options (in years)	5.6

17. Segment Data

Net sales by segment were as follows:

	For the Quarters Ended		For the Nine Months Ended	
	June 30, 2017	June 24, 2016	June 30, 2017	June 24, 2016
	(in millions)			
Transportation Solutions	$ 1,765	$ 1,652	$ 5,195	$ 4,767
Industrial Solutions	905	849	2,553	2,296
Communications Solutions	697	620	1,909	1,843
Total[(1)]	$ 3,367	$ 3,121	$ 9,657	$ 8,906

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(1) Intersegment sales were not material and were recorded at selling prices that approximated market prices.

Operating income by segment was as follows:

	For the Quarters Ended		For the Nine Months Ended	
	June 30, 2017	June 24, 2016	June 30, 2017	June 24, 2016
	(in millions)			
Transportation Solutions	$ 328	$ 297	$ 971	$ 847
Industrial Solutions	98	95	251	224
Communications Solutions	110	60	273	314(1)
Total	$ 536	$ 452	$ 1,495	$ 1,385

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(1)

Includes pre-tax gain of $143 million on the sale of our CPD business during the nine months ended June 24, 2016.

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TE CONNECTIVITY LTD.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED) (Continued)

18. Tyco Electronics Group S.A.

Tyco Electronics Group S.A. ("TEGSA"), a Luxembourg company and our 100%-owned subsidiary, is a holding company that owns, directly or indirectly, all of our operating subsidiaries. TEGSA is the obligor under our senior notes, commercial paper, and five-year unsecured senior revolving credit facility, which are fully and unconditionally guaranteed by its parent, TE Connectivity Ltd. The following tables present condensed consolidating financial information for TE Connectivity Ltd., TEGSA, and all other subsidiaries that are not providing a guarantee of debt but which represent assets of TEGSA, using the equity method of accounting.

Condensed Consolidating Statement of Operations (UNAUDITED)
For the Quarter Ended June 30, 2017

	TE Connectivity Ltd.	TEGSA	Other Subsidiaries	Consolidating Adjustments	Total
			(in millions)		
Net sales	$	$	$ 3,367	$	$ 3,367
Cost of sales			2,229		2,229
Gross margin			1,138		1,138
Selling, general, and administrative expenses, net	68	18	326		412
Research, development, and engineering expenses			170		170
Acquisition and integration costs			1		1
Restructuring and other charges, net			19		19
Operating income (loss)	(68)	(18)	622		536
Interest income			3		3
Interest expense		(32)			(32)
Other expense, net			(4)		(4)
Equity in net income of subsidiaries	507	530		(1,037)	
Equity in net income of subsidiaries of discontinued operations	3	4		(7)	
Intercompany interest income (expense), net	(7)	27	(20)		
Income from continuing operations before income taxes	435	511	601	(1,044)	503
Income tax expense			(71)		(71)
Income from continuing operations	435	511	530	(1,044)	432
Income (loss) from discontinued operations, net of income taxes		(1)	4		3
Net income	435	510	534	(1,044)	435
Other comprehensive income	78	78	83	(161)	78
Comprehensive income	$ 513	$ 588	$ 617	$ (1,205)	$ 513

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TE CONNECTIVITY LTD.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED) (Continued)

18. Tyco Electronics Group S.A. (Continued)

Condensed Consolidating Statement of Operations (UNAUDITED)
For the Quarter Ended June 24, 2016

	TE Connectivity Ltd.	TEGSA	Other Subsidiaries	Consolidating Adjustments	Total
			(in millions)		
Net sales	$	$	$ 3,121	$	$ 3,121
Cost of sales			2,099		2,099
Gross margin			1,022		1,022
Selling, general, and administrative expenses, net	50	(2)	319		367
Research, development, and engineering expenses			161		161
Acquisition and integration costs	1		10		11
Restructuring and other charges (credits), net	2	(1)	30		31
Operating income (loss)	(53)	3	502		452
Interest income			2		2
Interest expense		(31)			(31)
Other expense, net			(651)		(651)
Equity in net income of subsidiaries	852	847		(1,699)	
Equity in net income of subsidiaries of discontinued operations	47	47		(94)	
Intercompany interest income (expense), net	(8)	33	(25)		
Income (loss) from continuing operations before income taxes	838	899	(172)	(1,793)	(228)
Income tax benefit			1,019		1,019
Income from continuing operations	838	899	847	(1,793)	791
Income from discontinued operations, net of income taxes	1		47		48
Net income	839	899	894	(1,793)	839
Other comprehensive income	74	74	33	(107)	74
Comprehensive income	$ 913	$ 973	$ 927	$ (1,900)	$ 913

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TE CONNECTIVITY LTD.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED) (Continued)

18. Tyco Electronics Group S.A. (Continued)

Condensed Consolidating Statement of Operations (UNAUDITED)
For the Nine Months Ended June 30, 2017

	TE Connectivity Ltd.	TEGSA	Other Subsidiaries	Consolidating Adjustments	Total
			(in millions)		
Net sales	$	$	$ 9,657	$	$ 9,657
Cost of sales			6,346		6,346
Gross margin			3,311		3,311
Selling, general, and administrative expenses, net	144	(52)	1,104		1,196
Research, development, and engineering expenses			490		490
Acquisition and integration costs			5		5
Restructuring and other charges, net			125		125
Operating income (loss)	(144)	52	1,587		1,495
Interest income			14		14
Interest expense		(95)			(95)
Other expense, net			(6)		(6)
Equity in net income of subsidiaries	1,409	1,369		(2,778)	
Equity in net income of subsidiaries of discontinued operations	5	18		(23)	
Intercompany interest income (expense), net	(21)	83	(62)		
Income from continuing operations before income taxes	1,249	1,427	1,533	(2,801)	1,408
Income tax expense			(164)		(164)
Income from continuing operations	1,249	1,427	1,369	(2,801)	1,244
Income (loss) from discontinued operations, net of income taxes[(1)]		(13)	18		5
Net income	1,249	1,414	1,387	(2,801)	1,249
Other comprehensive income	36	36	14	(50)	36
Comprehensive income	$ 1,285	$ 1,450	$ 1,401	$ (2,851)	$ 1,285

(1) Includes the internal allocation of gains and losses associated with the divestiture of our BNS business.

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TE CONNECTIVITY LTD.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED) (Continued)

18. Tyco Electronics Group S.A. (Continued)

Condensed Consolidating Statement of Operations (UNAUDITED)
For the Nine Months Ended June 24, 2016

	TE Connectivity Ltd.	TEGSA	Other Subsidiaries	Consolidating Adjustments	Total
			(in millions)		
Net sales	$	$	$ 8,906	$	$ 8,906
Cost of sales			5,977		5,977
Gross margin			2,929		2,929
Selling, general, and administrative expenses, net	135	35	904		1,074
Research, development, and engineering expenses			479		479
Acquisition and integration costs	1		18		19
Restructuring and other charges (credits), net	2	(1)	(29)		(28)
Operating income (loss)	(138)	(34)	1,557		1,385
Interest income			12		12
Interest expense		(92)	(1)		(93)
Other expense, net			(631)		(631)
Equity in net income of subsidiaries	1,658	1,724		(3,382)	
Equity in net income of subsidiaries of discontinued operations	67	183		(250)	
Intercompany interest income (expense), net	(16)	60	(44)		
Income from continuing operations before income taxes	1,571	1,841	893	(3,632)	673
Income tax benefit			831		831
Income from continuing operations	1,571	1,841	1,724	(3,632)	1,504
Income (loss) from discontinued operations, net of income taxes[(1)]	1	(116)	183		