HENRY SCHEIN INC
Form 10-Q
October 29, 2010

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

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

For the quarterly period ended September 25, 2010

Or

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

For the transition period from ____________ to ____________
Commission File Number: 0-27078

HENRY SCHEIN, INC.
(Exact name of registrant as specified in its charter)

Delaware	11-3136595
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)

135 Duryea Road
Melville, New York
(Address of principal executive offices)
11747
(Zip Code)

(631) 843-5500
(Registrant’s telephone number, including area code)

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

Yes X 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 X No __

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

Large accelerated filer X	Accelerated filer __
Non-accelerated filer __ (Do not check if a smaller reporting company)	Smaller reporting company __

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

Yes __ No X

As of October 22, 2010, there were 92,273,142 shares of the registrant’s common stock outstanding.

HENRY SCHEIN, INC.
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PART I. FINANCIAL INFORMATION
ITEM 1. CONSOLIDATED FINANCIAL STATEMENTS

HENRY SCHEIN, INC.
CONSOLIDATED BALANCE SHEETS
(in thousands, except share and per share data)

	September 25, 2010 (unaudited)	December 26, 2009
ASSETS		
Current assets:		
Cash and cash equivalents	$203,730	$471,154
Accounts receivable, net of reserves of $54,226 and $51,724	923,026	725,397
Inventories, net	849,541	775,199
Deferred income taxes	40,860	48,001
Prepaid expenses and other	230,617	183,782
Total current assets	2,247,774	2,203,533
Property and equipment, net	254,004	259,576
Goodwill	1,425,651	986,395
Other intangibles, net	413,701	204,445
Investments and other	263,329	182,036
Total assets	$4,604,459	$3,835,985
LIABILITIES AND STOCKHOLDERS' EQUITY		
Current liabilities:		
Accounts payable	$532,274	$521,079
Bank credit lines	201,142	932
Current maturities of long-term debt	25,122	23,560
Accrued expenses:		
Payroll and related	154,103	155,298
Taxes	107,040	86,034
Other	267,966	289,351
Total current liabilities	1,287,647	1,076,254
Long-term debt	383,495	243,373
Deferred income taxes	190,565	100,976
Other liabilities	75,582	75,304
Total liabilities	1,937,289	1,495,907
Redeemable noncontrolling interests	299,101	178,570
Commitments and contingencies		
Stockholders' equity:		
Preferred stock, $.01 par value, 1,000,000 shares authorized, none outstanding	-	-
Common stock, $.01 par value, 240,000,000 shares authorized, 92,366,321 outstanding on September 25, 2010 and 90,630,889 outstanding on December 26, 2009	924	906
Additional paid-in capital	592,646	603,772

Retained earnings	1,722,146	1,492,607
Accumulated other comprehensive income	50,932	64,194
Total Henry Schein, Inc. stockholders' equity	2,366,648	2,161,479
Noncontrolling interest	1,421	29
Total stockholders' equity	2,368,069	2,161,508
Total liabilities, redeemable noncontrolling interests and stockholders' equity	$4,604,459	$3,835,985

See accompanying notes.

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

	Three Months Ended		Nine Months Ended	
	September 25, 2010	September 26, 2009	September 25, 2010	September 26, 2009
Net sales	$ 1,893,511	$ 1,659,433	$ 5,503,222	$ 4,752,255
Cost of sales	1,356,055	1,183,166	3,907,089	3,361,707
Gross profit	537,456	476,267	1,596,133	1,390,548
Operating expenses:				
Selling, general and administrative	400,088	362,382	1,204,715	1,060,062
Restructuring costs	-	-	12,285	4,043
Operating income	137,368	113,885	379,133	326,443
Other income (expense):				
Interest income	3,422	2,387	10,318	7,674
Interest expense	(7,824)	(5,171)	(26,096)	(18,329)
Other, net	29	1,938	388	1,595
Income from continuing operations before taxes, equity in earnings of affiliates and noncontrolling interests	132,995	113,039	363,743	317,383
Income taxes	(42,226)	(15,864)	(115,885)	(83,402)
Equity in earnings of affiliates	3,721	1,200	7,047	3,777
Income from continuing operations	94,490	98,375	254,905	237,758
Income from discontinued operation, net of tax	-	2,373	-	2,715
Net income	94,490	100,748	254,905	240,473
Less: Net income attributable to noncontrolling interests	(6,597)	(4,327)	(22,111)	(15,728)
Net income attributable to Henry Schein, Inc.	$ 87,893	$ 96,421	$ 232,794	$ 224,745
Amounts attributable to Henry Schein, Inc.:				
Income from continuing operations	$ 87,893	$ 94,045	$ 232,794	$ 222,143
Income from discontinued operation, net of tax	-	2,376	-	2,602
Net income	$ 87,893	$ 96,421	$ 232,794	$ 224,745
Earnings per share attributable to Henry Schein, Inc.:				
From continuing operations:				

Basic	$	0.97	$	1.06	$	2.59	$	2.50
Diluted	$	0.94	$	1.03	$	2.50	$	2.45
From discontinued operation:								
Basic	$	-	$	0.03	$	-	$	0.03
Diluted	$	-	$	0.02	$	-	$	0.03
From net income:								
Basic	$	0.97	$	1.09	$	2.59	$	2.53
Diluted	$	0.94	$	1.05	$	2.50	$	2.48
Weighted-average common shares outstanding:								
Basic		90,326		88,796		89,932		88,843
Diluted		93,270		91,513		93,098		90,576

See accompanying notes.

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HENRY SCHEIN, INC.
CONSOLIDATED STATEMENTS OF CHANGES IN STOCKHOLDERS' EQUITY
(In thousands, except share and per share data)

	Common Stock $.01 Par Value Shares	Amount	Additional Paid-in Capital	Retained Earnings	Accumulated Other Comprehensive Income	Noncontrolling Interest	Total Stockholders' Equity
Balance, December 26, 2009	90,630,889	$ 906	$ 603,772	$ 1,492,607	$ 64,194	$ 29	$ 2,161,508
Net income (excluding $21,842 attributable to Redeemable noncontrolling interests)	-	-	-	232,794	-	269	233,063
Foreign currency translation loss (excluding $1,678 attributable to Redeemable noncontrolling interests)	-	-	-	-	(9,929)	-	(9,929)
Unrealized loss from foreign currency hedging activities, net of tax benefit of $1,932	-	-	-	-	(3,857)	-	(3,857)
Unrealized investment gain, net of tax of $411	-	-	-	-	460	-	460
Pension adjustment gain, net of tax benefit of $9	-	-	-	-	64	-	64
Total comprehensive income							219,801
Dividends paid	-	-	-	-	-	(394)	(394)
Other adjustments	-	-	-	-	-	1,517	1,517
Change in fair value of redeemable securities	-	-	(50,750)	-	-	-	(50,750)
Initial noncontrolling interests and adjustments related to business acquisitions	-	-	(22,222)	-	-	-	(22,222)

Shares issued upon conversion of convertible debt senior notes	732,422	7	12,129	-	-	-	12,136
Shares issued to 401(k)	107,662	1	5,720	-	-	-	5,721
Repurchase and retirement of common stock	(86,171)	-	(1,564)	(3,255)	-	-	(4,819)
Stock issued upon exercise of stock options, including tax benefit of $5,141	840,501	8	30,483	-	-	-	30,491
Stock-based compensation expense	201,081	2	19,743	-	-	-	19,745
Shares withheld for payroll taxes	(60,063)	-	(4,260)	-	-	-	(4,260)
Liability for cash settlement stock option awards	-	-	(405)	-	-	-	(405)
Balance, September 25, 2010	92,366,321	$ 924	$ 592,646	$ 1,722,146	$ 50,932	$ 1,421	$ 2,368,069

See accompanying notes.

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

	Nine Months Ended	
	September 25, 2010	September 26, 2009
Cash flows from operating activities:		
Net income	$ 254,905	$ 240,473
Adjustments to reconcile net income to net cash provided by operating activities:		
Gain on sale of discontinued operation, net of tax	-	(2,382)
Depreciation and amortization	75,510	60,930
Amortization of bond discount	4,007	4,473
Stock-based compensation expense	19,745	18,344
Provision for losses on trade and other accounts receivable	2,929	2,754
Benefit from deferred income taxes	(2,068)	(29,633)
Stock issued to 401(k) plan	5,721	5,301
Undistributed earnings of affiliates	(7,047)	(3,777)
Other	5,275	2,535
Changes in operating assets and liabilities, net of acquisitions:		
Accounts receivable	(104,719)	(12,788)
Inventories	5,799	(10,234)
Other current assets	(37,526)	(806)
Accounts payable and accrued expenses	(45,706)	(56,813)
Net cash provided by operating activities	176,825	218,377
Cash flows from investing activities:		
Purchases of fixed assets	(26,926)	(38,417)
Payments for equity investment and business acquisitions, net of cash acquired	(353,305)	(45,458)
Cash received from business divestiture	-	12,716
Purchases of available-for-sale securities	(26,984)	-
Proceeds from sales of available-for-sale securities	5,950	8,730
Proceeds from maturities of available-for-sale securities	26,984	-
Net proceeds from foreign exchange forward contract settlements	-	275
Other	319	(11,258)
Net cash used in investing activities	(373,962)	(73,412)
Cash flows from financing activities:		
Proceeds from (repayments of) bank borrowings	200,195	(3,829)
Proceeds from issuance of long-term debt	100,000	-

Principal payments for long-term debt		(244,699)		(153,452)
Proceeds from issuance of stock upon exercise of stock options		25,350		9,689
Payments for repurchases of common stock		(4,819)		-
Excess tax benefits related to stock-based compensation		7,586		2,821
Distributions to noncontrolling shareholders		(9,739)		(1,858)
Acquisitions of noncontrolling interests in subsidiaries		(149,845)		(52,453)
Other		(269)		(269)
Net cash used in financing activities		(76,240)		(199,351)
Net change in cash and cash equivalents		(273,377)		(54,386)
Effect of exchange rate changes on cash and cash equivalents		5,953		2,423
Cash and cash equivalents, beginning of period		471,154		369,570
Cash and cash equivalents, end of period	$	203,730	$	317,607

See accompanying notes.

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

Note 1. Basis of Presentation

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

Our accompanying unaudited consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States ("U.S. GAAP") for interim financial information and with the instructions to Form 10-Q and Article 10 of Regulation S-X. Accordingly, they do not include all of the information and footnote disclosures required by U.S. GAAP for complete financial statements.

The consolidated financial statements reflect all adjustments considered necessary for a fair presentation of the consolidated results of operations and financial position for the interim periods presented. All such adjustments are of a normal recurring nature. These unaudited interim consolidated financial statements should be read in conjunction with the audited consolidated financial statements and notes to the consolidated financial statements contained in our Annual Report on Form 10-K for the year ended December 26, 2009.

The preparation of financial statements in conformity with U.S. GAAP requires us to make estimates and assumptions that affect the reported amounts of assets and liabilities, and disclosure of contingent assets and liabilities, at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates. The results of operations for the nine months ended September 25, 2010 are not necessarily indicative of the results to be expected for any other interim period or for the year ending December 25, 2010.

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

Note 2. Segment Data

We conduct our business through two reportable segments: healthcare distribution and technology. These segments offer different products and services to the same customer base. The healthcare distribution reportable segment aggregates our dental, medical, animal health and international operating segments. This segment consists of consumable products, small equipment, laboratory products, large dental and medical equipment, equipment repair services, branded and generic pharmaceuticals, vaccines, surgical products, diagnostic tests, infection-control products and vitamins.

Our dental group serves office-based dental practitioners, schools and other institutions in the combined United States and Canadian dental market. Our medical group serves office-based medical practitioners, surgical centers, other alternate-care settings and other institutions throughout the United States. Our animal health group serves animal health practices and clinics throughout the United States. Our international group serves dental, medical and animal health practitioners in 21 countries outside of North America.

Our technology group provides software, technology and other value-added services to healthcare practitioners, primarily in the United States, Canada, the United Kingdom, Australia and New Zealand. Our value-added practice solutions include practice management software systems for dental and medical practitioners and animal health clinics. Our technology group offerings also include financial services on a non-recourse basis, e-services and continuing education services for practitioners.

The following tables present information about our reportable segments:

	Three Months Ended		Nine Months Ended	
	September 25, 2010	September 26, 2009	September 25, 2010	September 26, 2009
Net Sales:				
Healthcare distribution (1):				
Dental (2)	$665,940	$622,065	$1,958,149	$1,838,240
Medical (3)	391,863	347,917	962,743	907,061
Animal health (4)	225,210	62,700	666,590	181,814
International (5)	561,353	583,540	1,773,241	1,699,053
Total healthcare distribution	1,844,366	1,616,222	5,360,723	4,626,168
Technology (6)	49,145	43,211	142,499	126,087
Total	$1,893,511	$1,659,433	$5,503,222	$4,752,255

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

(2) Consists of products sold in the United States and Canada.

(3) Consists of products sold in the United States' medical market.

(4) Consists of products sold in the United States' animal health market.

(5) Consists of products sold in the dental, medical and animal health markets, primarily in Europe.

(6) Consists of practice management software and other value-added products and services, which are distributed primarily to healthcare providers in the United States, Canada, the United Kingdom, Australia and New Zealand.

	Three Months Ended		Nine Months Ended	
	September 25, 2010	September 26, 2009	September 25, 2010	September 26, 2009
Operating Income:				
Healthcare distribution	$121,012	$98,250	$330,984	$280,618
Technology	16,356	15,635	48,149	45,825
Total	$137,368	$113,885	$379,133	$326,443

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

Note 3. Stock-Based Compensation

Our accompanying unaudited consolidated statements of income reflect share-based pretax compensation expense of $6.7 million ($4.6 million after-tax) and $19.7 million ($13.5 million after-tax) for the three and nine months ended September 25, 2010, respectively, and $6.0 million ($4.1 million after-tax) and $18.3 million ($12.4 million after-tax) for the three and nine months ended September 26, 2009, respectively.

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

Stock-based awards are provided to certain employees and non-employee directors under the terms of our 1994 Stock Incentive Plan, as amended, and our 1996 Non-Employee Director Stock Incentive Plan, as amended (together, the “Plans”). The Plans are administered by the Compensation Committee of the Board of Directors. Prior to March 2009, awards under the Plans principally included a combination of at-the-money stock options and restricted stock (including restricted stock units). In March 2009 and March 2010, equity-based awards were granted solely in the form of restricted stock and restricted stock units, with the exception of stock options for certain pre-existing contractual obligations.

Grants of restricted stock are common stock awards granted to recipients with specified vesting provisions. We issue restricted stock that vests solely based on the recipient’s continued service over time (four-year cliff vesting) and restricted stock that vests based on our achieving specified performance measurements and the recipient’s continued service over time (three-year cliff vesting).

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

The Plans provide for adjustments to the performance-based restricted stock targets for significant events such as acquisitions, divestitures, new business ventures and share repurchases. Over the performance period, the number of shares of common stock that will ultimately vest and be issued and the related compensation expense is adjusted upward or downward based upon our estimation of achieving such performance targets. The ultimate number of shares delivered to recipients and the related compensation cost recognized as an expense will be based on our actual performance metrics as defined under the Plans.

Restricted stock units are unit awards that we grant to certain employees that entitle the recipient to shares of common stock upon vesting. We grant restricted stock units with the same time-based and performance-based vesting that we use for restricted stock. The fair value of restricted stock units is determined on the date of grant, based on our closing stock price.

Total unrecognized compensation cost related to non-vested awards as of September 25, 2010 was $58.9 million, which is expected to be recognized over a weighted-average period of approximately 2.2 years.

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

Note 3. Stock-Based Compensation (Continued)

The following weighted-average assumptions were used in determining the fair values of stock options using the Black-Scholes valuation model:

	2010	2009
Expected dividend yield	0%	0%
Expected stock price volatility	20%	28%
Risk-free interest rate	2.37%	1.88%
Expected life of options (years)	4.5	4.5

The following table summarizes stock option activity under the Plans during the nine months ended September 25, 2010:

	Shares	Weighted Average Exercise Price	Weighted Average Remaining Contractual Life in Years	Aggregate Intrinsic Value
Outstanding at beginning of period	6,294,742	$ 40.66		
Granted	10,000	56.03		
Exercised	(840,501)	30.21		
Forfeited	(41,867)	49.60		
Outstanding at end of period	5,422,374	$ 42.24	4.9	$ 84,441
Options exercisable at end of period	4,656,508	$ 39.83	4.5	$ 82,751

The following tables summarize the status of our non-vested restricted stock/units for the nine months ended September 25, 2010:

	Time-Based Restricted Stock/Units		
	Shares/Units	Weighted Average Grant Date Fair Value	Aggregate Intrinsic Value
Outstanding at beginning of period	597,605	$ 25,662	
Granted	222,250	12,458	
Vested	(86,999)	(4,118)	
Forfeited	(12,764)	(565)	
Outstanding at end of period	720,092	$ 33,437	$ 41,283

	Performance-Based Restricted Stock/Units		
	Shares/Units	Weighted Average	Aggregate Intrinsic

		Grant Date Fair Value	Value
Outstanding at beginning of period	1,009,962	$ 22,271	
Granted	339,631	20,319	
Vested	(129,123)	(6,622)	
Forfeited	(10,853)	(469)	
Outstanding at end of period	1,209,617	$ 35,499	$ 69,347

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

Note 4. Business Acquisitions and Other Transactions

Acquisitions

Effective December 31, 2009, we acquired a majority interest in Butler Animal Health Holding Company, LLC ("Butler Holding"), the holding company of Butler Animal Health Supply, LLC ("BAHS"), a distributor of companion animal health supplies to veterinarians. BAHS further complements our domestic and international animal health operations and accordingly has been included in our Animal health business unit, which is reported as part of Healthcare distribution. We contributed certain assets and liabilities with a net book value of approximately $86.0 million related to our United States animal health business to BAHS and paid approximately $42.0 million in cash to acquire 50.1% of the equity interests in Butler Holding indirectly through W.A. Butler Company, a holding company that is partially owned by Oak Hill Capital Partners ("OHCP"). As part of a recapitalization at closing, BAHS combined with our animal health business to form Butler Schein Animal Health ("BSAH"), while incurring approximately $127.0 million in incremental debt used primarily to finance Butler Holding stock redemptions. As a result, BSAH had $320.0 million of debt at closing, $37.5 million of which was provided by Henry Schein, Inc. and is eliminated in the accompanying consolidated financial statements. Total consideration for the acquisition of BAHS, including $96.1 million of value for noncontrolling interests, was $351.1 million and was allocated as follows:

Net assets of BAHS at fair value:	
Current assets	$164,789
Intangible assets:	
Trade name (useful life 3 years)	10,000
Customer relationships (useful life 12 years)	140,000
Non-compete agreements (useful life 2 years)	2,600
Goodwill	270,714
Other assets	14,138
Current liabilities	(62,770)
Bank indebtedness	(200,100)
Deferred income tax liabilities	(74,271)
Net book value of our assets and liabilities contributed	86,048
Total allocation of consideration	$351,148

The goodwill recognized is primarily attributable to expected synergies and the assembled workforce of BAHS. The goodwill is not expected to be tax deductible for income tax purposes. As a result of our contributed business being under the control of Henry Schein before and after the transaction, the assets and liabilities of this business remain at their original historical accounting basis in the accompanying consolidated financial statements.

The debt incurred as part of the acquisition of BAHS is repayable in 23 quarterly installments of $0.8 million through September 30, 2015, and a final installment of $301.6 million on December 31, 2015. Interest on the BAHS debt is charged at LIBOR plus a margin of 3.5% with a LIBOR floor of 2% for a current effective rate of 5.5% as of September 25, 2010. The debt agreement contains provisions which, under certain circumstances, require BAHS to make prepayments of the loan commitment based on excess cash flows of BAHS as defined in the debt agreement. The debt agreement also contains provisions that require BAHS to hedge risks related to potential rising interest rates. As a result, BAHS entered into a series of interest rate caps protecting against LIBOR interest rates rising above 3.0% through March 30, 2012.

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

Note 4. Business Acquisitions and Other Transactions (Continued)

In connection with the acquisition of a majority interest in BAHS, we entered into (i) a Put Rights Agreement with OHCP and Butler Holding (the "Oak Hill Put Rights Agreement"), and (ii) a Put Rights Agreement with Burns Veterinary Supply, Inc. ("Burns") and Butler Holding (the "Burns Put Rights Agreement" and together with the Oak Hill Put Rights Agreement, the "Put Rights Agreements"), which provide each of OHCP and Burns with certain rights to require us to purchase their respective direct and indirect ownership interests in Butler Holding at fair value based on third-party valuations ("Put Rights"). Pursuant to the Oak Hill Put Rights Agreement, OHCP can exercise its Put Rights from and after the earlier of (a) December 31, 2010, and (b) a change of control of Henry Schein, Inc. Except in connection with a change of control of us prior to the first anniversary of the closing (in which case there will not be any maximum), our maximum annual payment to OHCP under the Oak Hill Put Rights Agreement will not exceed $125.0 million for the first year during which OHCP can exercise its rights, $137.5 million for the second year and $150.0 million for the third year and for each year thereafter. Pursuant to the Burns Put Rights Agreement, Burns can exercise its Put Rights from and after December 31, 2014, at which time Burns will be permitted to sell to us up to 20% of its closing date ownership interest in Butler Holding each year. If OHCP still holds ownership interests in Butler Holding at the time the Burns Put Rights begin, then the put amounts payable by us to OHCP and Burns in any year will not exceed $150.0 million in the aggregate. As a result of the Put Right Agreements, the noncontrolling interest in BAHS has been reflected as part of Redeemable noncontrolling interests in the accompanying consolidated balance sheet.

In addition to the BAHS acquisition, we completed certain other acquisitions during the nine months ended September 25, 2010. The operating results of all acquisitions are reflected in our financial statements from their respective acquisition dates. All acquisitions individually and in the aggregate had an immaterial impact on our reported operating results. Total acquisition costs incurred in the three and nine months ended September 25, 2010 were immaterial to our financial results.

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

Note 5. Earnings Per Share

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

On September 3, 2010, we redeemed all of our 3% convertible contingent notes originally due in 2034 (the "Convertible Notes") for approximately $240 million in cash and issued 732,422 shares of our common stock. The effect of assumed conversion of our Convertible Notes, as it relates to the impact on diluted earnings per share, is included through September 3, 2010 for the three and nine months ended September 25, 2010. Beginning with the fourth quarter of 2010 and future periods, our diluted earnings per share will no longer be impacted by the assumed conversion of our Convertible Notes.

For the three and nine months ended September 25, 2010 and the three months ended September 26, 2009, diluted earnings per share includes the effect of common shares issuable upon conversion of our Convertible Notes. During the period, the debt was convertible at a premium as a result of the conditions of the debt. As a result, the amount in excess of the principal was settled in common shares and is reflected in our calculation of diluted earnings per share.

For the nine months ended September 26, 2009, our Convertible Notes were not convertible at a premium and thus the impact of an assumed conversion was not applicable.

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

	Three Months Ended		Nine Months Ended	
	September 25, 2010	September 26, 2009	September 25, 2010	September 26, 2009
Basic	90,325,655	88,796,152	89,932,232	88,843,067
Effect of dilutive securities:				
Stock options, restricted stock and restricted units	2,212,513	2,241,503	2,265,323	1,732,922
Effect of assumed conversion of convertible debt	731,384	475,081	900,289	-
Diluted	93,269,552	91,512,736	93,097,844	90,575,989

Weighted-average options to purchase 1,008,173 shares of common stock at exercise prices ranging from $54.81 to $62.05 per share and 1,971,851 shares of common stock at exercise prices ranging from $51.10 to $62.05 per share that were outstanding during the three months ended September 25, 2010 and September 26, 2009, respectively, were excluded from the computation of diluted earnings per share. Weighted-average options to purchase 993,924 shares of common stock at exercise prices ranging from $56.21 to $62.05 per share and 2,741,364 shares of common stock at exercise prices ranging from $45.85 to $62.05 per share that were outstanding during the nine months ended September 25, 2010 and September 26, 2009, respectively, were excluded from the computation of diluted earnings per share. In each of these periods, such options' exercise prices exceeded the average market price of our common stock, thereby causing the effect of such options to be anti-dilutive.

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Note 6. Comprehensive Income

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

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

	September 25, 2010	December 26, 2009
Attributable to Redeemable noncontrolling interests:		
Foreign currency translation adjustment	$(261)	$1,417
Attributable to Henry Schein, Inc.:		
Foreign currency translation adjustment	$44,800	$54,729
Unrealized gain from foreign currency hedging activities	10,680	14,537
Unrealized investment loss	(861)	(1,321)
Pension adjustment loss	(3,687)	(3,751)
Accumulated other comprehensive income	$50,932	$64,194
Total Accumulated other comprehensive income	$50,671	$65,611

The following table summarizes other comprehensive income attributable to our Redeemable noncontrolling interests, net of applicable taxes as follows:

	Three Months Ended		Nine Months Ended	
	September 25, 2010	September 26, 2009	September 25, 2010	September 26, 2009
Foreign currency translation adjustment	$6,018	$2,530	$(1,678)	$3,704

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

	Three Months Ended		Nine Months Ended	
	September 25, 2010	September 26, 2009	September 25, 2010	September 26, 2009
Comprehensive income attributable to Henry Schein, Inc.	$142,674	$122,765	$219,532	$266,887
Comprehensive income attributable to noncontrolling interests	236	16	269	42
Comprehensive income attributable to				

Redeemable noncontrolling interests	12,379	6,841	20,164	19,390
Comprehensive income	$155,289	$129,622	$239,965	$286,319

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Note 7. Fair Value Measurements

ASC Topic 820 "Fair Value Measurements and Disclosures" ("ASC Topic 820") establishes a framework for measuring fair value in generally accepted accounting principles and expands disclosures about fair value measurements. ASC Topic 820 applies under other previously issued accounting pronouncements that require or permit fair value measurements but does not require any new fair value measurements.

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

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

- Level 1— Unadjusted quoted prices in active markets for identical assets or liabilities that are accessible at the measurement date.

- Level 2— Inputs other than quoted prices included within Level 1 that are observable for the asset or liability, either directly or indirectly. Level 2 inputs include quoted prices for similar assets or liabilities in active markets; quoted prices for identical or similar assets or liabilities in markets that are not active; inputs other than quoted prices that are observable for the asset or liability; and inputs that are derived principally from or corroborated by observable market data by correlation or other means.

- Level 3— Inputs that are unobservable for the asset or liability.

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

Cash equivalents and trade receivables

Due to the short-term maturity of such investments, the carrying amounts are a reasonable estimate of fair value.

Long-term investments and notes receivable

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

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Note 7. Fair Value Measurements (Continued)

Available-for-sale securities

As of September 25, 2010, we have approximately $15.1 million ($13.9 million net of temporary impairments) invested in auction-rate securities ("ARS"), which are included as part of Investments and other within our consolidated balance sheets. ARS are publicly issued securities that represent long-term investments, typically 10-30 years, in which interest rates had reset periodically (typically every 7, 28 or 35 days) through a "dutch auction" process. Approximately $13.1 million ($11.9 million net of temporary impairments) of our ARS are backed by student loans that are backed by the federal government and the remaining $2.0 million are invested in closed-end municipal bond funds. Our ARS portfolio is comprised of investments that are rated AAA by major independent rating agencies. Since the middle of February 2008, ARS auctions have failed to settle due to an excess number of sellers compared to buyers. The failure of these auctions has resulted in our inability to liquidate our ARS in the near term. We are currently not aware of any defaults or financial conditions that would negatively affect the issuers' ability to continue to pay interest and principal on our ARS. We continue to earn and receive interest at contractually agreed upon rates.

During 2010, we have received approximately $0.4 million and $5.6 million of redemptions, at par, for our closed-end municipal bond funds and our student loan portfolios, respectively.

As of September 25, 2010, we have continued to classify our closed-end municipal bond funds, as well as our student loan portfolios, as Level 3 within the fair value hierarchy due to the lack of observable inputs and the absence of significant refinancing activity.

Based upon the information currently available and the use of a discounted cash flow model in accordance with applicable authoritative guidance, our previously recorded cumulative temporary impairment at December 26, 2009 of $2.2 million related to our closed-end municipal bond funds and our student loan portfolios was decreased to $1.2 million during the nine months ended September 25, 2010. The decrease in the temporary impairment was due to the level of redemptions and changes in interest rates during the quarter. The temporary impairment has been recorded as part of Accumulated other comprehensive income within the equity section of our consolidated balance sheet.

Money market fund

As of September 25, 2010, we had approximately $0.2 million, $0 net of reserves, invested in the Reserve Primary Fund. This money market fund included in its holdings commercial paper of Lehman Brothers. As a result of the Chapter 11 bankruptcy of Lehman Brothers Holdings, Inc., the net asset value of the fund decreased below $1.00. During the nine months ended September 25, 2010, we received approximately $1.8 million of distributions from the Reserve Primary Fund. We do not expect to receive any additional redemptions from the Reserve Primary Fund. As of September 25, 2010, the value of our holdings in this fund are included within Prepaid expenses and other in our consolidated balance sheets and as Level 3 within the fair value hierarchy, due to the lack of observable inputs and the absence of trading activity.

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Note 7. Fair Value Measurements (Continued)

Accounts payable and accrued expenses

Financial liabilities with carrying values approximating fair value include accounts payable and other accrued liabilities. The carrying value of these financial instruments approximates fair value due to their short maturities or variable interest rates that approximate current market rates.

Debt

On September 3, 2010, we paid approximately $240 million in cash and issued 732,422 shares of our common stock in connection with the redemption of our $240.0 million of Convertible Notes, which were issued in 2004.

On August 10, 2010, we entered into new $400 million private placement facilities with two insurance companies. These facilities are available through August 2013 on an uncommitted basis. The facilities allow us to issue senior promissory notes to the lenders at a fixed rate based on an agreed upon spread over applicable treasury notes at the time of issuance. The term of each possible issuance will be selected by us and can range from five to 15 years (with an average life no longer than 12 years). The proceeds of any issuances under the facilities will be used for general corporate purposes, including working capital and capital expenditures, to refinance existing indebtedness and/or to fund potential acquisitions. As of September 25, 2010 we have an outstanding balance under the facilities of $100 million at 3.79%, which is due on September 2, 2020.

The fair value of our debt is estimated based on quoted market prices for our traded debt and on market prices of similar issues for our private debt. The fair value of our debt as of September 25, 2010 and December 26, 2009 was estimated at $609.8 million and $307.5 million.

Derivative contracts

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

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

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Note 7. Fair Value Measurements (Continued)

Redeemable noncontrolling interests

Some minority shareholders in certain of our subsidiaries have the right, at certain times, to require us to acquire their ownership interest in those entities at fair value based on third-party valuations. The noncontrolling interests subject to put options are adjusted to their estimated redemption amounts each reporting period with a corresponding adjustment to Additional paid-in capital. Future reductions in the carrying amounts are subject to a "floor" amount that is equal to the fair value of the redeemable noncontrolling interests at the time they were originally recorded. The recorded value of the redeemable noncontrolling interests cannot go below the floor level. These adjustments will not impact the calculation of earnings per share. The details of the changes in Redeemable noncontrolling interests are shown in Note 12.

The following table presents our assets and liabilities that are measured and recognized at fair value on a recurring basis classified under the appropriate level of the fair value hierarchy as of September 25, 2010 and December 26, 2009:

	September 25, 2010			
	Level 1	Level 2	Level 3	Total
Assets:				
Available-for-sale securities	$-	$-	$13,917	$13,917
Money market fund	-	-	-	-
Derivative contracts	-	3,631	-	3,631
Total assets	$-	$3,631	$13,917	$17,548
Liabilities:				
Derivative contracts	$-	$3,603	$-	$3,603
Total liabilities	$-	$3,603	$-	$3,603
Redeemable noncontrolling interests	$-	$-	$299,101	$299,101

	December 26, 2009			
	Level 1	Level 2	Level 3	Total
Assets:				
Available-for-sale securities	$-	$-	$18,848	$18,848
Money market fund	-	-	1,746	1,746
Derivative contracts	-	6,177	-	6,177
Total assets	$-	$6,177	$20,594	$26,771
Liabilities:				
Derivative contracts	$-	$3,829	$-	$3,829

Total liabilities	$-	$3,829	$-	$3,829
Redeemable noncontrolling interests	$-	$-	$178,570	$178,570

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Note 7. Fair Value Measurements (Continued)

As of September 25, 2010, we have estimated the value of our closed-end municipal bond fund ARS portfolio and our student loan backed ARS portfolio based upon a discounted cash flow model. The assumptions used in our valuation model include estimates for interest rates, timing and amount of cash flows and expected holding periods for the ARS portfolio. As a result of these analyses, our previously recorded cumulative temporary impairment at December 26, 2009 of $2.2 million was decreased by $1.0 million to $1.2 million during the nine months ended September 25, 2010.

We estimated the value of our holdings within the Reserve Primary Fund based upon the net asset value of the fund as of September 16, 2008, subsequent to the declaration of bankruptcy by Lehman Brothers Holdings, Inc. During the nine months ended September 25, 2010, we received approximately $1.8 million of distributions from The Reserve Primary Fund, leaving a remaining balance of approximately $0.2 million, $0 net of reserves, as of September 25, 2010. The following table presents a reconciliation of our assets and liabilities measured at fair value on a recurring basis using unobservable inputs (Level 3):

	Level 3 (1)
Balance, December 27, 2008	$266,581
Change in redeemable noncontrolling interests	(54,465)
Redemptions at par	(13,227)
Gains and (losses):	
Reported in earnings - Reserve Primary Fund reduction	500
Reported in accumulated other comprehensive income	(225)
Balance, December 26, 2009	$199,164
Change in redeemable noncontrolling interests	120,531
Redemptions at par	(7,731)
Gains:	
Reported in earnings - Reserve Primary Fund reduction	35
Reported in accumulated other comprehensive income	1,019
Balance, September 25, 2010	$313,018

(1) Level 3 amounts consist of closed-end municipal bond funds, student loan backed auction-rate securities, money market fund and redeemable noncontrolling interests. See Note 12 for the components of the changes in Redeemable noncontrolling interests.

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Note 8. Income Taxes

For the nine months ended September 25, 2010, our effective tax rate from continuing operations was 31.9% compared to 26.3% for the prior year period. The difference in our effective tax rates is primarily related to a reduction in the valuation allowance on foreign deferred tax assets during the third quarter of 2009. Absent the effects of the reversal of a portion of the valuation allowance on certain foreign deferred tax assets in the third quarter of 2009, our effective tax rate for the nine months ended September 26, 2009 would have been 32.9%. The difference between our effective tax rates and the federal statutory tax rates for both periods primarily relates to state and foreign income taxes.

The total amount of unrecognized tax benefits as of September 25, 2010 was approximately $24.4 million, all of which would affect the effective tax rate if recognized. It is expected that the amount of unrecognized tax benefits will change in the next 12 months. However, we do not expect the change to have a material impact on our consolidated financial statements.

The total amounts of interest and penalties resulting from unrecognized tax benefits were approximately $4.8 million and $0, respectively, for the nine months ended September 25, 2010. It is expected that the amount of interest will change in the next twelve months. However, we do not expect the change to have a material impact on our consolidated financial statements.

The tax years subject to examination by major tax jurisdictions include the years 2006 and forward by the U.S. Internal Revenue Service, the years 1997 and forward for certain states and the years 1998 and forward for certain foreign jurisdictions.

Note 9. Supplemental Cash Flow Information

Cash paid for interest and income taxes was:

	Nine Months Ended	
	September 25, 2010	September 26, 2009
Interest	$19,233	$20,892
Income taxes	93,800	114,176

During the nine months ended September 25, 2010, we had a $5.8 million non-cash net unrealized loss related to hedging activities. During the nine months ended September 26, 2009, we had a $15.4 million non-cash net unrealized gain related to hedging activities.

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Note 10. Plans of Restructuring

On November 5, 2008, we announced certain actions to reduce operating costs. These actions included the elimination of approximately 430 positions from our operations and the closing of several smaller facilities.

During the first quarter of 2010, we completed an additional restructuring in order to further reduce operating expenses. This restructuring included headcount reductions of 184 positions, as well as the closing of a number of smaller locations.

For the nine months ended September 25, 2010, we recorded restructuring costs of approximately $12.3 million (approximately $8.3 million after taxes) consisting of employee severance pay and benefits, facility closing costs, representing primarily lease termination and asset write-off costs, and outside professional and consulting fees directly related to the restructuring plan. The costs associated with the restructuring are included in a separate line item, “Restructuring costs” within our consolidated statements of income.

The following table shows the amounts expensed and paid for restructuring costs that were incurred during the nine months ended September 25, 2010 and the remaining accrued balance of restructuring costs as of September 25, 2010, which is included in Accrued expenses: Other and Other liabilities within our consolidated balance sheet:

	Balance at December 26, 2009	Provision	Payments and Other Adjustments	Balance at September 25, 2010
Severance costs (1)	$2,165	$8,800	$ 6,584	$4,381
Facility closing costs (2)	2,030	3,355	1,967	3,418
Other professional and consulting costs	102	130	158	74
Total	$4,297	$12,285	$ 8,709	$7,873

(1) Represents salaries and related benefits for employees separated from the Company.

(2) Represents costs associated with the closing of certain smaller facilities (primarily lease termination costs) and property and equipment write-offs.

We expect that the majority of these costs will be paid in 2010.

The following table shows, by reportable segment, the restructuring costs incurred during our 2010 fiscal year and the remaining accrued balance of restructuring costs as of September 25, 2010:

	Balance at December 26, 2009	Provision	Payments and Other Adjustments	Balance at September 25, 2010
Healthcare distribution	$ 4,225	$ 12,063	$ 8,486	$ 7,802
Technology	72	222	223	71

Total	$ 4,297	$ 12,285	$ 8,709	$ 7,873

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Note 11. Derivatives and Hedging Activities

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

Fluctuations in the value of certain foreign currencies as compared to the U.S. dollar may positively or negatively affect our revenues, gross margins, operating expenses and retained earnings, all of which are expressed in U.S. dollars. Where we deem it prudent, we engage in hedging programs using primarily foreign currency forward and swap contracts aimed at limiting the impact of foreign currency exchange rate fluctuations on earnings. We purchase short-term (i.e., 12 months or less) foreign currency forward and swap contracts to protect against currency exchange risks associated with intercompany loans due from our international subsidiaries and the payment of merchandise purchases to our foreign suppliers. We do not hedge the translation of foreign currency profits into U.S. dollars, as we regard this as an accounting exposure, not an economic exposure.

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Note 11. Derivatives and Hedging Activities (Continued)

The following tables present the fair value of our derivative instruments:

	Asset Derivatives September 25, 2010		Liability Derivatives September 25, 2010	
	Balance Sheet Location	Fair Value	Balance Sheet Location	Fair Value
Derivatives designated as hedging instruments:				
Interest rate contracts	Prepaid expenses and other	$ 3	Accrued expenses other	