VARIAN MEDICAL SYSTEMS INC
Form 10-Q
August 05, 2014

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

x QUARTERLY REPORT PURSUANT TO SECTION 13 or 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the quarterly period ended June 27, 2014

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 1-7598

VARIAN MEDICAL SYSTEMS, INC.

(Exact name of registrant as specified in its charter)

Delaware	94-2359345
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification Number)
3100 Hansen Way, Palo Alto, California	94304-1030
(Address of principal executive offices)	(Zip Code)

(650) 493-4000

(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 (§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 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 definitions of "large accelerated filer," "accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act. (Check one):

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

Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date: 103,201,351 shares of common stock, par value $1 per share, outstanding as of July 25, 2014.

VARIAN MEDICAL SYSTEMS, INC.

FORM 10-Q for the Quarter Ended June 27, 2014

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PART I

FINANCIAL INFORMATION

Item 1. Financial Statements

VARIAN MEDICAL SYSTEMS, INC. AND SUBSIDIARIES

CONDENSED CONSOLIDATED STATEMENTS OF EARNINGS

(Unaudited)

	Three Months Ended		Nine Months Ended	
(In thousands, except per share amounts)	June 27, 2014	June 28, 2013	June 27, 2014	June 28, 2013
Revenues:				
Product	$505,648	$503,640	$1,529,024	$1,518,116
Service	242,037	222,571	708,669	654,851
Total revenues	747,685	726,211	2,237,693	2,172,967
Cost of revenues:				
Product	314,874	316,584	957,920	958,954
Service	109,084	99,162	318,157	292,822
Total cost of revenues	423,958	415,746	1,276,077	1,251,776
Gross margin	323,727	310,465	961,616	921,191
Operating expenses:				
Research and development	56,988	53,335	175,668	151,355
Selling, general and administrative	124,235	102,398	348,776	321,910
Litigation settlement	-	-	25,130	-
Total operating expenses	181,223	155,733	549,574	473,265
Operating earnings	142,504	154,732	412,042	447,926
Interest income	3,045	1,915	7,768	5,159
Interest expense	(1,787)	(874)	(5,535)	(2,766)
Earnings before taxes	143,762	155,773	414,275	450,319
Taxes on earnings	36,672	42,942	116,437	129,417
Net earnings	$107,090	$112,831	$297,838	$320,902
Net earnings per share - basic	$1.03	$1.04	$2.85	$2.95
Net earnings per share - diluted	$1.02	$1.03	$2.81	$2.90
Shares used in the calculation of net earnings per share:				
Weighted average shares outstanding - basic	103,644	108,158	104,585	108,741
Weighted average shares outstanding - diluted	104,869	109,760	105,910	110,496

See accompanying notes to the condensed consolidated financial statements.

VARIAN MEDICAL SYSTEMS, INC. AND SUBSIDIARIES

CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE EARNINGS

(Unaudited)

	Three Months Ended		Nine Months Ended	
(In thousands)	June 27, 2014	June 28, 2013	June 27, 2014	June 28, 2013
Net earnings	$107,090	$112,831	$297,838	$320,902
Other comprehensive earnings (loss), net of tax:				
Defined benefit pension and post-retirement benefit plans:				
Amortization of prior service cost included in net periodic benefit cost, net of tax expense of ($6) and ($18) for the three and nine months ended June 27, 2014 respectively, and ($4) and ($14) for the corresponding periods of fiscal 2013, respectively	38	36	113	109
Amortization of net actuarial loss included in net periodic benefit cost, net of tax expense of ($102) and ($303) for the three and nine months ended June 27, 2014, respectively, and ($132) and ($397) for the corresponding periods of fiscal 2013, respectively	433	564	1,303	1,691
	471	600	1,416	1,800
Unrealized gain on derivatives:				
Increase (decrease) in unrealized gain (loss), net of tax benefit (expense) of ($37) and ($816) for the three and nine months ended June 27, 2014, respectively, and $96 and ($768) for the corresponding periods of fiscal 2013, respectively	62	(161)	1,361	1,278
Reclassification adjustments, net of tax benefit (expense) of ($90) and $389 for the three and nine months ended June 27, 2014, respectively, and $751 and $1,112 for the corresponding periods of fiscal 2013, respectively	149	(1,249)	(649)	(1,850)
	211	(1,410)	712	(572)
Currency translation adjustment	(1,742)	1,890	(752)	1,998
Other comprehensive earnings (loss)	(1,060)	1,080	1,376	3,226
Comprehensive earnings	$106,030	$113,911	$299,214	$324,128

See accompanying notes to the condensed consolidated financial statements.

VARIAN MEDICAL SYSTEMS, INC. AND SUBSIDIARIES

CONDENSED CONSOLIDATED BALANCE SHEETS

(Unaudited)

(In thousands, except par values)	June 27, 2014	September 27, 2013 (1)
Assets		
Current assets:		
Cash and cash equivalents	$925,987	$1,117,861
Short-term investment	60,777	62,700
Accounts receivable, net of allowance for doubtful accounts of $18,740 at June 27, 2014 and $14,735 at September 27, 2013	747,346	698,254
Inventories	586,071	535,223
Prepaid expenses and other current assets	183,019	168,495
Deferred tax assets	121,556	122,250
Total current assets	2,624,756	2,704,783
Property, plant and equipment, net	328,646	315,331
Goodwill	236,130	225,335
Other assets	285,343	223,025
Total assets	$3,474,875	$3,468,474
Liabilities and Stockholders' Equity		
Current liabilities:		
Accounts payable	$173,359	$194,272
Accrued expenses	315,325	320,884
Product warranty	48,562	39,050
Deferred revenues	418,267	389,479
Advance payments from customers	174,843	160,644
Short-term debt	29,582	-
Current maturities of long-term debt	50,000	56,250
Total current liabilities	1,209,938	1,160,579
Long-term debt	400,000	450,000
Other long-term liabilities	150,024	144,048
Total liabilities	1,759,962	1,754,627
Commitments and contingencies (Note 9)		
Stockholders' equity:		
Preferred stock of $1 par value: 1,000 shares authorized; none issued and outstanding	-	-
Common stock of $1 par value: 189,000 shares authorized; 103,140 and 106,491 shares issued and outstanding at June 27, 2014 and at September 27, 2013, respectively	103,140	106,491
Capital in excess of par value	661,140	637,084
Retained earnings	989,328	1,010,343
Accumulated other comprehensive loss	(38,695)	(40,071)
Total stockholders' equity	1,714,913	1,713,847
Total liabilities and stockholders' equity	$3,474,875	$3,468,474

(1) The condensed consolidated balance sheet as of September 27, 2013 was derived from audited financial statements as of that date, but does not include all disclosures required by accounting principles generally accepted in the United States of America.

See accompanying notes to the condensed consolidated financial statements.

VARIAN MEDICAL SYSTEMS, INC. AND SUBSIDIARIES

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

(Unaudited)

	Nine Months Ended	
(In thousands)	June 27, 2014	June 28, 2013
Cash flows from operating activities:		
Net earnings	$297,838	$320,902
Adjustments to reconcile net earnings to net cash provided by operating activities:		
Share-based compensation expense	30,054	33,915
Tax benefits from exercises of share-based payment awards	9,882	10,407
Excess tax benefits from share-based compensation	(9,850)	(9,570)
Depreciation	42,717	44,614
Amortization of intangible assets	3,259	3,295
Impairment of a privately-held equity investment	7,725	-
Deferred taxes	(4,689)	5,130
Provision for doubtful accounts receivable	5,662	4,814
Income from equity investment in affiliate	(99)	(2,459)
Other, net	(1,651)	(908)
Changes in assets and liabilities, net of effect of acquisition:		
Accounts receivable	(67,947)	18,663
Inventories	(49,060)	(80,398)
Prepaid expenses and other assets	(22,147)	(22,637)
Accounts payable	(14,020)	(261)
Accrued expenses and other liabilities	(14,768)	(78,035)
Deferred revenues and advance payments from customers	42,683	52,784
Net cash provided by operating activities	255,589	300,256
Cash flows from investing activities:		
Purchases of property, plant and equipment	(63,229)	(56,688)
Investment in available-for-sale corporate debt securities	(40,692)	(7,554)
Sale of a portion of investment in available-for-sale corporate debt security	38,075	-
Acquisitions of businesses, net of cash acquired	(15,500)	-
Notes receivable	(5,500)	(10,000)
Net amounts paid to deferred compensation plan trust account	-	(15)
Other	642	(129)
Net cash used in investing activities	(86,204)	(74,386)
Cash flows from financing activities:		
Repurchases of common stock	(417,245)	(289,099)
Proceeds from issuance of common stock to employees	84,107	104,464
Excess tax benefits from share-based compensation	9,850	9,570
Employees' taxes withheld and paid for restricted stock and restricted stock units	(8,664)	(9,526)
Net borrowings under credit facility agreements	29,553	14,935
Repayments under term loan facility and other bank borrowings	(56,250)	-
Other	(616)	(935)
Net cash used in financing activities	(359,265)	(170,591)
Effects of exchange rate changes on cash and cash equivalents	(1,994)	5,718

Net increase/(decrease) in cash and cash equivalents	(191,874)	60,997
Cash and cash equivalents at beginning of period	1,117,861	704,570
Cash and cash equivalents at end of period	$925,987	$765,567

See accompanying notes to the condensed consolidated financial statements.

VARIAN MEDICAL SYSTEMS, INC. AND SUBSIDIARIES

NOTES TO THE CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited)

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Description of Business

Varian Medical Systems, Inc. ("VMS") and subsidiaries (collectively, the "Company") designs, manufactures, sells and services hardware and software products for treating cancer with radiotherapy, stereotactic radiosurgery, stereotactic body radiotherapy, and brachytherapy. The Company also designs, manufactures, sells and services X-ray imaging components for use in a range of applications, including radiographic or fluoroscopic imaging, mammography, specific procedures, computed tomography and industrial applications. In addition, the Company designs, manufactures, sells and services linear accelerators, image processing software and image detection products for security and inspection purposes. The Company also develops, designs, manufactures, sells and services proton therapy products and systems for cancer treatment.

Basis of Presentation

The condensed consolidated financial statements have been prepared by the Company pursuant to the rules and regulations of the Securities and Exchange Commission ("SEC"). Certain information and note disclosures normally included in annual financial statements prepared in accordance with accounting principles generally accepted in the United States ("GAAP") have been condensed or omitted pursuant to such rules and regulations. These condensed consolidated financial statements and the accompanying notes are unaudited and should be read in conjunction with the consolidated financial statements and the notes thereto included in the Company's Annual Report on Form 10-K for the year ended September 27, 2013 (the "2013 Annual Report"). In the opinion of management, the condensed consolidated financial statements herein include adjustments (consisting only of normal recurring adjustments) necessary for a fair statement of the Company's financial position as of June 27, 2014 and September 27, 2013, results of operations and statements of comprehensive earnings for the three and nine months ended June 27, 2014 and June 28, 2013, and cash flows for the nine months ended June 27, 2014 and June 28, 2013. The results of operations for the three and nine months ended June 27, 2014 are not necessarily indicative of the operating results to be expected for the full fiscal year or any future period.

Segment Reporting

During the second quarter of fiscal year 2014, the Company changed its organizational structure resulting in a change in operating and reportable segments. The Company's operations are grouped into two reportable operating segments: Oncology Systems and Imaging Components. The Company's Ginzton Technology Center ("GTC") and Varian Particle Therapy ("VPT") businesses are reflected in the "Other" category because these operating segments do not meet the criteria of a reportable operating segment. Refer to Note 18, "Segment Information."

Reclassifications

Certain items in the condensed consolidated statements of earnings have been reclassified to conform to the current period's presentation. These reclassifications had no impact on previously reported total revenues, total cost of revenues and net earnings.

Fiscal Year

The fiscal years of the Company as reported are the 52- or 53- week periods ending on the Friday nearest September 30. Fiscal year 2014 is the 52-week period ending September 26, 2014, and fiscal year 2013 was the 52-week period that ended on September 27, 2013. The fiscal quarters ended June 27, 2014 and June 28, 2013 were both 13-week periods.

Principles of Consolidation

The condensed consolidated financial statements include those of VMS and its subsidiaries. Intercompany balances, transactions and stock holdings have been eliminated in consolidation.

Use of Estimates

The preparation of financial statements in conformity with GAAP requires management 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 these estimates.

VARIAN MEDICAL SYSTEMS, INC. AND SUBSIDIARIES

NOTES TO THE CONDENSED CONSOLIDATED FINANCIAL STATEMENTS – (CONTINUED)

(Unaudited)

Recent Accounting Pronouncements

In June 2014, the Financial Accounting Standards Board ("FASB") issued an amendment to its accounting guidance related to stock-based compensation. The amendment requires that a performance target that could be achieved after the requisite service period be treated as a performance condition that affects vesting, rather than a condition that affects the grant-date fair value. The new guidance will be effective in the Company's fiscal year beginning 2017. Early adoption is permitted. The amendment can be applied on a prospective basis to all share-based payments granted or modified on or after the effective date. Entities will also be provided an option to apply the guidance on a modified retrospective basis to existing awards. The Company is evaluating the impact of adopting this guidance to its consolidated financial statements.

In May 2014, the FASB issued an amendment to its accounting guidance related to revenue recognition. The amendment sets forth a single, comprehensive revenue recognition model for all contracts with customers to improve comparability. The amendment requires revenue recognition to depict the transfer of goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. The new guidance will be effective in the Company's fiscal year beginning 2018. Early application is not permitted. The amendments can be applied either retrospectively to each prior reporting period presented or retrospectively with the cumulative effect of initially applying the update recognized at the date of the initial application along with additional disclosures. The Company is evaluating the impact of adopting this guidance to its consolidated financial statements.

2. BALANCE SHEET COMPONENTS:

(In millions)	June 27, 2014	September 27, 2013
Available-for-sale Securities:		
Corporate debt securities:		
Amortized cost	$69.4	$ 62.7
Unrealized gain (loss)	-	-
Fair value	$69.4	$ 62.7

The available-for-sale securities represent loans to California Proton Treatment Center, LLC ("CPTC"). As of June 27, 2014, of the total amount of $69.4 million of the available-for-sale securities, $60.8 million is included in "Short-term investment" and $8.6 million is included in "Other assets" on the condensed consolidated balance sheet. As of September 27, 2013, the entire amount of available-for-sale securities was included in "Short-term investment" on the condensed

consolidated balance sheet. Refer to Note 16, “CPTC Loans” for additional discussion.

(In millions)	June 27, 2014	September 27, 2013
Inventories:		
Raw materials and parts	$300.9	$ 276.6
Work-in-process	115.6	91.6
Finished goods	169.6	167.0
Total inventories	$586.1	$ 535.2

(In millions)	June 27, 2014	September 27, 2013
Other long-term liabilities:		
Long-term income taxes payable	$50.8	$ 41.9
Other	99.2	102.1
Total other long-term liabilities	$150.0	$ 144.0

VARIAN MEDICAL SYSTEMS, INC. AND SUBSIDIARIES

NOTES TO THE CONDENSED CONSOLIDATED FINANCIAL STATEMENTS – (CONTINUED)

(Unaudited)

3. FAIR VALUE

Fair value is defined as the exchange price that would be received for an asset or paid to transfer a liability (an exit price) in the principal or most advantageous market for the asset or liability in an orderly transaction between market participants at the measurement date. There is a three-level fair value hierarchy that prioritizes the inputs used to measure fair value. This hierarchy requires entities to maximize the use of observable inputs and minimize the use of unobservable inputs. The three levels of inputs used to measure fair value are as follows:

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

Level 2 — Observable inputs other than quoted prices included in Level 1, such as quoted prices for similar assets and liabilities in active markets; quoted prices for identical or similar assets and liabilities in markets that are not active; or other inputs that are observable or can be corroborated by observable market data.

Level 3 — Unobservable inputs that are supported by little or no market activity and that are significant to the fair value of the assets or liabilities.

Assets/Liabilities Measured at Fair Value on a Recurring Basis

In the tables below, the Company has segregated all assets and liabilities that are measured at fair value on a recurring basis into the most appropriate level within the fair value hierarchy based on the inputs used to determine the fair value at the measurement date.

	Fair Value Measurement Using			
Type of Instruments (In millions)	Quoted Prices in Active Markets for Identical Instruments (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Total Balance
Assets at June 27, 2014:				
Available-for-sale corporate debt securities	$-	$ -	$ 69.4	$ 69.4
Derivative assets	-	0.1	-	0.1
Total assets measured at fair value	$-	$ 0.1	$ 69.4	$ 69.5
Liabilities at June 27, 2014:				

Contingent consideration	$-	$ -	$ (4.2)	$ (4.2)
Total liabilities measured at fair value	$-	$ -	$ (4.2)	$ (4.2)
Assets at September 27, 2013:				
Money market funds	$ 50.0	$ -	$ -	$ 50.0
Available-for-sale corporate debt security	-	-	62.7	62.7
Option to purchase a privately-held company	-	-	1.4	1.4
Total assets measured at fair value	$ 50.0	$ -	$ 64.1	$ 114.1
Liabilities at September 27, 2013:				
Derivative liabilities	$-	$ (1.1)	$ -	$ (1.1)
Contingent consideration	-	-	(2.5)	(2.5)
Total liabilities measured at fair value	$-	$ (1.1)	$ (2.5)	$ (3.6)

Money market funds are included under cash and cash equivalents, available-for-sale corporate debt securities are included under short-term investment and other assets, derivative assets are included under prepaid expenses and other current assets, option to purchase a company is included under other assets, derivative liabilities are included under accrued liabilities and contingent consideration is included under accrued liabilities and other-long term liabilities on the condensed consolidated balance sheets.

The Company obtains valuations of Level 1 money market funds from quotes for transactions in active exchange markets involving identical assets.

VARIAN MEDICAL SYSTEMS, INC. AND SUBSIDIARIES

NOTES TO THE CONDENSED CONSOLIDATED FINANCIAL STATEMENTS – (CONTINUED)

(Unaudited)

The Company's valuation of its Level 2 instruments includes valuations obtained from quoted prices for identical assets in markets that are not active. In addition, the Company has elected to use the income approach to value its derivative instruments using standard valuation techniques and Level 2 inputs, such as currency spot rates, forward points and credit default swap spreads. The Company's derivative instruments are short-term in nature, typically one month to thirteen months in duration.

The Company measures the fair value of its Level 3 contingent consideration liabilities based on the income approach by using a Monte Carlo simulation model with key assumptions that include estimated sales units or revenues of the acquired business during the earn-out period, volatility, and estimated discount rates corresponding to the periods of expected payments. If the estimated sales units or revenues were to increase or decrease during the respective earn-out period, the fair value of the contingent consideration would increase or decrease, respectively. If the volatility were to increase or decrease, the fair value of contingent consideration would decrease or increase, respectively. If the estimated discount rates used were to increase or decrease, the fair value of the contingent consideration would decrease or increase, respectively.

The fair value of the Company's Level 3 available-for-sale corporate debt securities is based on the income approach by using the discounted cash flow model with key assumptions that include discount rates corresponding to the terms and risks associated with the loan to CPTC. If the estimated discount rates used were to increase or decrease, the fair value of the debt securities would decrease or increase, respectively. However, the Company does not increase the fair value above its par value as ORIX Capital Markets, LLC ("ORIX"), the loan agent, has the option to purchase this loan from the Company under the original terms and conditions at par value.

As of September 27, 2013, the Company had an option to purchase the remaining equity interest of Augmenix, Inc. ("Augmenix"), a privately-held company. The option to purchase the remaining equity interest of Augmenix is classified as a Level 3 asset and its fair value is based on the income approach using key assumptions that include projected operating results of the company and an estimated discount rate corresponding to the period of expected payment.

The following table presents the reconciliation for all assets and liabilities measured and recorded at fair value on a recurring basis using significant unobservable inputs (Level 3):

(In millions)	Available-For-Sale Corporate Debt Securities	Contingent Consideration	Option to Purchase a Privately - Held Company
Balance at September 27, 2013	$ 62.7	$ (2.5)	$ 1.4
Additions [1]	44.8	(2.9)	-
Sale of a portion of available-for-sale corporate debt securities[2]	(38.1)	-	-
Settlements [3]	-	0.6	-
Change in fair value recognized in earnings	-	0.6	(1.4)

Balance at June 27, 2014	$ 69.4	$ (4.2)	$ -

1. Amounts reported under Available-For-Sale Corporate Debt Securities include accrued interest.
2. Refer to Note 16 “CPTC Loans”
3. Amounts reported under “Contingent Consideration” represent cash payments to settle contingent consideration liabilities.

There were no transfers of assets or liabilities between fair value measurement levels during either the three and nine months ended June 27, 2014, or the three and nine months ended June 28, 2013. Transfers between fair value measurement levels are recognized at the end of the reporting period.

VARIAN MEDICAL SYSTEMS, INC. AND SUBSIDIARIES

NOTES TO THE CONDENSED CONSOLIDATED FINANCIAL STATEMENTS – (CONTINUED)

(Unaudited)

Assets Measured at Fair Value on a Nonrecurring Basis

For the three and nine months ended June 27, 2014, the Company recognized a $7.7 million charge relating to the impairment of a portion of our privately-held investment in Augmenix. The impairment charge of $7.7 million included a $1.4 million write-off of the option to purchase the remaining equity interest of Augmenix, upon its expiry. This option was previously measured at fair value on a recurring basis.

For the three and nine months ended June 27, 2014, the Company's assets that were measured at fair value on a nonrecurring basis are summarized below:

(In millions)	Net Carrying Value as of June 27, 2014	Total Losses for the three and nine months ended
Equity investment in Augmenix	$ 7.3	$ 6.3

The fair value measurement of the impaired privately held investment was classified as Level 3 because significant unobservable inputs were used in the valuation due to the absence of quoted market prices and inherent lack of liquidity. Significant unobservable inputs, which included financial condition and recent financing activities of the investees, reflected the assumptions market participants would use in pricing these assets. The impairment charge, representing the difference between the net book value and the fair value of the investment as a result of the evaluation, was recorded to Selling, general and administrative expenses.

Fair Value of Other Financial Instruments

The fair values of certain of the Company's financial instruments, including bank deposits and certificate of deposits included in cash and cash equivalents, accounts receivable, net of allowance for doubtful accounts, note receivables, accounts payable, and short-term debt approximate their carrying amounts due to their short maturities.

As of both June 27, 2014 and September 27, 2013, the fair value of current maturities of long-term debt approximated its carrying value of $50.0 million and $56.3 million, respectively, due to its short-term maturity. The fair value of the long-term debt payable in installments through fiscal year 2018 approximated its carrying value of $400.0 million and $450.0 million, at June 27, 2014 and September 27, 2013, respectively, because it is carried at a market observable interest rate that resets periodically and is categorized as level 2 in the fair value hierarchy.

4. Financing Receivables and Allowance for Credit Losses

A financing receivable represents a financing arrangement with a contractual right to receive money, on demand or on fixed or determinable dates, and that is recognized as an asset on the Company's Condensed Consolidated Balance Sheets.

The Company's financing receivables, consisting of its accounts receivable with contractual maturities of more than one year, and the related allowance for doubtful accounts are presented in the following table:

(In millions)	June 27, 2014	September 27, 2013
Accounts receivable with contractual maturities of more than one year:		
Gross amount	$41.3	$ 28.0
Allowance for doubtful accounts	(3.0)	(3.0)
Net amount	$38.3	$ 25.0
Amount past due	$3.5	$ 3.1

During the three and nine months ended June 27, 2014, the Company sold without recourse $8.3 million and $11.3 million, respectively, of accounts receivable with contractual maturities of more than one year. During the three months ended June 28, 2013, no accounts receivable with contractual maturities of more than one year were sold. During the nine months ended June 28, 2013, the Company sold without recourse $1.1 million of accounts receivable with contractual maturities of more than one year.

VARIAN MEDICAL SYSTEMS, INC. AND SUBSIDIARIES

NOTES TO THE CONDENSED CONSOLIDATED FINANCIAL STATEMENTS – (CONTINUED)

(Unaudited)

5. GOODWILL AND INTANGIBLE ASSETS

The following table reflects the activity of goodwill by reportable operating segment:

(In millions)	Oncology Systems	Imaging Components	Other	Total
Balance at September 27, 2013	$ 132.0	$ 33.2	$60.1	$225.3
Acquisition of businesses	10.4	-	-	10.4
Foreign currency translation adjustments	-	-	0.4	0.4
Balance at June 27, 2014	$ 142.4	$ 33.2	$60.5	$236.1

The following table reflects the gross carrying amount and accumulated amortization of the Company's intangible assets included in "Other assets" in the Condensed Consolidated Balance Sheets as follows:

(In millions)	June 27, 2014	September 27, 2013
Intangible Assets:		
Acquired existing technology	$46.6	$ 36.6
Patents, licenses and other	27.9	29.0
Customer contracts and supplier relationship	11.9	10.9
Accumulated amortization	(54.7)	(53.1)
Net carrying amount	$31.7	$ 23.4

Amortization expense for intangible assets was $1.4 million and $1.1 million for the three months ended June 27, 2014 and June 28, 2013, respectively, and $3.3 million for both the nine months ended June 27, 2014, and June 28, 2013. The Company estimates amortization expense for the remaining three months of fiscal year 2014, fiscal year 2015, fiscal year 2016, fiscal year 2017, fiscal year 2018, fiscal year 2019 and thereafter, will be as follows (in millions): $2.2, $7.1, $6.3, $3.7, $3.6, $3.5, and $5.3, respectively.

6. RELATED PARTY TRANSACTIONS

VMS has a 40% ownership interest in dpiX Holding LLC (“dpiX Holding”), a two-member consortium which has a 100% ownership interest in dpiX LLC (“dpiX”), a supplier of amorphous silicon based thin-film transistor arrays (“flat panels”) for the Company’s Imaging Components’ digital image detectors and for its Oncology Systems’ On-Board Imager®, and PortalVision™ imaging products. In accordance with the dpiX Holding agreement, net profits or losses are allocated to the members in accordance with their ownership interests.

The equity investment in dpiX Holding is accounted for under the equity method of accounting. When VMS recognizes its share of net profits or losses of dpiX Holding, profits or losses in inventory purchased from dpiX are eliminated until realized by VMS. VMS recorded income of $0.7 million and $3.0 million in the three months ended June 27, 2014 and June 28, 2013, respectively, on the equity investment in dpiX Holding. VMS recorded income of $0.1 million $2.5 million in the nine months ended June 27, 2014 and June 28, 2013, respectively, on the equity investment in dpiX Holding. Income and loss on the equity investment in dpiX Holding is included in “Selling, general and administrative” expenses in the Condensed Consolidated Statements of Earnings. The carrying value of the equity investment in dpiX Holding, which is included in “Other assets” in the Condensed Consolidated Balance Sheets, was $48.4 million at June 27, 2014 and $49.7 million at September 27, 2013.

The Company purchased glass transistor arrays from dpiX totaling $5.7 million and $6.5 million, respectively, in the three months ended June 27, 2014 and June 28, 2013. The Company purchased glass transistor arrays from dpiX totaling $14.9 million and $22.6 million, respectively, in the nine months ended June 27, 2014 and June 28, 2013. The purchases of glass transistor arrays are included as a component of “Inventories” in the Condensed Consolidated Balance Sheets or “Cost of revenues - product” in the Condensed Consolidated Statements of Earnings.

VARIAN MEDICAL SYSTEMS, INC. AND SUBSIDIARIES

NOTES TO THE CONDENSED CONSOLIDATED FINANCIAL STATEMENTS – (CONTINUED)

(Unaudited)

In October 2013, VMS entered into an amended agreement with dpiX and other parties that, among other things, provides the Company with the right to 50% of dpiX's total manufacturing capacity produced after January 1, 2014. The amended agreement requires the Company to pay for 50% of the fixed costs (as defined in the amended agreement), as determined at the beginning of each calendar year. As of June 27, 2014, the Company had fixed cost commitments of $4.3 million related to this amended agreement, for the remaining three months of fiscal year 2014. The fixed cost commitment for future years will be determined based on forecasted dpiX sales and approved by the dpiX board of directors at the beginning of each calendar year. The amended agreement will continue unless the ownership structure of dpiX changes (as defined in the amended agreement).

The Company has determined that dpiX is a variable interest entity because at-risk equity holders, as a group, lack the characteristics of a controlling financial interest. Majority votes are required to direct the manufacturing activities, legal operations and other activities that most significantly affect dpiX's economic performance. The Company does not have majority voting rights and no power to direct the activities of dpiX and therefore is not the primary beneficiary of dpiX.

7. BORROWINGS

On August 27, 2013, VMS entered into a Credit Agreement (as amended to date) with certain lenders and Bank of America, N.A. ("BofA") as administrative agent. The Credit Agreement provides for (i) a five-year term loan facility in an aggregate principal amount of up to $500 million (the "2013 Term Loan Facility") and (ii) a five-year revolving credit facility in an aggregate principal amount of up to $300 million (the "2013 Revolving Credit Facility" and, collectively with the 2013 Term Loan Facility, the "2013 Credit Facility"). The 2013 Revolving Credit Facility also includes a $50 million sub-facility for the issuance of letters of credit and permits swing line loans of up to $25 million. Under the 2013 Credit Agreement, the Company has the right to make (i) up to two requests to increase the aggregate commitments under the Term Loan Facility by an aggregate amount for all such requests of up to $100 million and (ii) up to three requests to increase the aggregate commitments under the Revolving Credit Facility by an aggregate amount for all such requests of up to $200 million, provided that, in each case, the Lenders are willing to provide such new or increased commitments and certain other conditions are met. The 2013 Credit Facility contains provisions that limit the Company's ability to pay cash dividends. The proceeds of the Credit Facility may be used for working capital, capital expenditures, permitted Company share repurchases, permitted acquisitions and other lawful corporate purposes.

Borrowings under the 2013 Term Loan Facility accrue interest either (i) based on a Eurodollar Rate, as defined in the Credit Agreement (the "Eurodollar Rate"), plus a margin of 1.00% to 1.25% based on a leverage ratio involving funded indebtedness and EBITDA or (ii) based upon a base rate of (a) the federal funds rate plus 0.50%, (b) BofA's announced prime rate, or (c) the Eurodollar Rate plus 1.00%, whichever is highest, plus a margin of 0.00% to 0.25% based on the same leverage Ratio, depending upon instructions from the Company. Borrowings under the 2013 Revolving Credit Facility accrue interest either (i) based on the Eurodollar Rate plus a margin of 1.25% to 1.50% based on a leverage ratio involving funded indebtedness and EBITDA or (ii) based upon a base rate of (a) the federal funds rate plus 0.50%, (b) BofA's announced prime rate, or (c) the Eurodollar Rate plus 1.00%, whichever is highest, plus a margin of 0.25% to 0.50% based on the same leverage ratio, depending upon instructions from the Company.

At June 27, 2014, borrowings under the 2013 Term Loan Facility totaled $450.0 million with a weighted average interest rate of 1.28%. At September 27, 2013, borrowings under the 2013 Term Loan Facility totaled $500.0 million with a weighted average interest rate of 1.31%. At June 27, 2014 and September 27, 2013, there were no amounts outstanding on the 2013 Revolving Credit Facility.

Subject to certain limitations on the amount secured, a pledge of stock issued by certain of our present and future subsidiaries that are deemed to be material under the terms of the 2013 Credit Facility serve as security for the 2013 Credit Facility. These stock pledges also serve as security for all hedging or treasury management obligations entered into by the Company with a Lender. As of June 27, 2014, VMS had pledged 65% of the voting shares that it holds in Varian Medical Systems Nederland Holdings B.V., a wholly owned subsidiary. The 2013 Credit Agreement provides that certain material domestic subsidiaries must guarantee the 2013 Credit Facility, subject to certain limitations on the amount secured. As of June 27, 2014, the 2013 Credit Facility was not guaranteed by any VMS subsidiary.

The Credit Agreement contains affirmative and negative covenants applicable to the Company and its subsidiaries that are typical for credit facilities of this type, and that are subject to materiality and other qualifications, carve-outs, baskets and exceptions. The Company has also agreed to maintain certain financial covenants including (i) a maximum consolidated leverage ratio, involving funded indebtedness and EBITDA (earnings before interest, tax and depreciation and amortization), and (ii) a minimum cash flow coverage ratio. The Company was in compliance with all covenants under the Credit Agreement for all periods within these condensed consolidated financial statements in which it was in existence.

VARIAN MEDICAL SYSTEMS, INC. AND SUBSIDIARIES

NOTES TO THE CONDENSED CONSOLIDATED FINANCIAL STATEMENTS – (CONTINUED)

(Unaudited)

Prior to the 2013 Credit Facility, VMS had a credit agreement (the "2012 Credit Facility") with certain lenders and BofA as administrative agent which provided for a revolving credit facility that enabled the Company to borrow and have outstanding at any given time a maximum of $300 million. On August 27, 2013, VMS replaced the 2012 Credit Facility with the 2013 Revolving Credit Facility, terminating the 2012 Credit Facility agreement entered into as of April 27, 2012 and repaying in full the approximately $148 million then-outstanding principal balance, plus accrued interest and fees.

VMS's Japanese subsidiary ("VMS KK") has an unsecured uncommitted credit agreement with Sumitomo that enables VMS KK to borrow and have outstanding at any given time a maximum of 3 billion Japanese yen (the "Sumitomo Credit Facility"). In March 2014, the Sumitomo Credit Facility was extended and will expire in March 2015. Borrowings under the Sumitomo Credit Facility accrue interest based on the basic loan rate announced by the Bank of Japan plus a margin of 0.5% per annum. As of June 27, 2014, 3 billion Japanese yen or $29.6 million was outstanding under the Sumitomo Credit Facility. In July 2014, VMS KK repaid the entire balance of the amount outstanding under the Sumitomo Credit Facility. There was no outstanding amount under the Sumitomo Credit Facility as of September 27, 2013.

In April 2014, the Company paid the outstanding balance of $6.3 million for the principal amount and accrued interest of its unsecured term loan.

8. DERIVATIVE INSTRUMENTS AND HEDGING ACTIVITIES

The Company measures all derivatives at fair value on the Condensed Consolidated Balance Sheets. The accounting for gains or losses resulting from changes in the fair value of those derivatives depends upon the use of the derivative and whether it qualifies for hedge accounting. Changes in the fair value of derivatives that do not qualify for hedge accounting treatment must be recognized in earnings, together with elements excluded from effectiveness testing and the ineffective portion of a particular hedge.

The fair values of derivative instruments reported on the Company's Condensed Consolidated Balance Sheets were as follows:

	Asset Derivatives			Liability Derivatives		
(In millions)	Balance Sheet Location	June 27, 2014 Fair Value	September 27, 2013 Fair Value	Balance Sheet Location	June 27, 2014 Fair Value	September 27, 2013 Fair Value
Derivatives designated as hedging instruments:						
		$ -	$ -		$ -	$ 1.1

Foreign exchange forward contracts	Prepaid expenses and other current assets			Accrued liabilities			
Derivatives not designated as hedging instruments:							
Foreign exchange forward contracts	Prepaid expenses and other current assets	0.1	-	Accrued liabilities	-	-	
Total derivatives		$ 0.1	$ -		$ -	$ 1.1	

See Note 3, “Fair Value” regarding valuation of the Company’s derivative instruments. Also see Note 1, “Summary of Significant Accounting Policies” in the Consolidated Financial Statements in the Company’s 2013 Annual Report regarding credit risk associated with the Company’s derivative instruments.

Offsetting of Derivatives

The Company presents its derivative assets and derivative liabilities on a gross basis in the Condensed Consolidated Balance Sheets. However, under agreements containing provisions on netting with certain counterparties of foreign exchange contracts, subject to applicable requirements, the Company is allowed to net-settle transactions on the same date in the same currency, with a single net amount payable by one party to the other. As of June 27, 2014 and September 27, 2013, there were no potential effects of rights of setoff associated with derivative instruments. The Company is neither required to pledge nor entitled to receive cash collateral related to these derivative transactions.

VARIAN MEDICAL SYSTEMS, INC. AND SUBSIDIARIES

NOTES TO THE CONDENSED CONSOLIDATED FINANCIAL STATEMENTS – (CONTINUED)

(Unaudited)

Cash Flow Hedging Activities

The Company has many transactions denominated in foreign currencies and addresses certain of those financial exposures through a risk management program that includes the use of derivative financial instruments. The Company sells products throughout the world, often in the currency of the customer's country, and may hedge certain of the larger foreign currency transactions when they are either not denominated in the relevant subsidiary's functional currency or the U.S. Dollar. These foreign currency sales transactions are hedged using foreign currency forward contracts. The Company may use other derivative instruments in the future. The Company enters into foreign currency forward contracts primarily to reduce the effects of fluctuating foreign currency exchange rates. The Company does not enter into foreign currency forward contracts for speculative or trading purposes. Foreign currency forward contracts may be entered into several times a quarter and range from one to thirteen months. As of June 27, 2014, the foreign currency forward contracts ranged from one to thirteen months in maturity.

The Company designates and accounts for certain of its hedges of forecasted foreign currency revenues as cash flow hedges. The Company's designated cash flow hedges de-designate when the anticipated revenues associated with the transactions are recognized and the effective portion in "Accumulated other comprehensive loss" in the Condensed Consolidated Balance Sheets is reclassified to "Revenues" in the Condensed Consolidated Statements of Earnings. Subsequent changes in fair value of the derivative instrument are recorded in "Selling, general and administrative expenses" in the Condensed Consolidated Statements of Earnings to offset changes in fair value of the resulting non-functional currency receivables. For derivative instruments that are designated and qualify as cash flow hedges, the Company formally documents for each derivative instrument at the hedge's inception the relationship between the hedging instrument (foreign currency forward contract) and hedged item (forecasted foreign currency revenues), the nature of the risk being hedged, and its risk management objective and strategy for undertaking the hedge. The Company records the effective portion of the gain or loss on the derivative instrument that are designated and qualify as cash flow hedges in "Accumulated other comprehensive loss" in the Condensed Consolidated Balance Sheets and reclassifies these amounts into "Revenues" in the Condensed Consolidated Statements of Earnings in the period during which the hedged transaction is recognized in earnings. The Company assesses hedge effectiveness both at the onset of the hedge and on an ongoing basis using regression analysis. The Company measures hedge ineffectiveness by comparing the cumulative change in the fair value of the effective component of the hedge contract with the cumulative change in the fair value of the hedged item. The Company recognizes any over performance of the derivative as ineffectiveness in "Revenues," and amounts excluded from the assessment of effectiveness in "Cost of revenues" in the Condensed Consolidated Statements of Earnings. During the three and nine months ended June 27, 2014, the Company did not discontinue any cash flow hedges. At the inception of the hedge, the Company assesses whether the likelihood of meeting the forecasted cash flow is highly probable. As of June 27, 2014, all forecasted cash flows were still probable to occur. As of June 27, 2014, the net unrealized gain on derivative instruments, before tax, included in "Accumulated other comprehensive loss" and expected to be reclassified to earnings over the next 12 months was immaterial.

The Company had the following outstanding foreign currency forward contracts that were designated as cash flow hedges:

(In millions)	At June 27, 2014 Notional Value Sold
Euro	$ 13.7
Totals	$ 13.7

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VARIAN MEDICAL SYSTEMS, INC. AND SUBSIDIARIES

NOTES TO THE CONDENSED CONSOLIDATED FINANCIAL STATEMENTS – (CONTINUED)

(Unaudited)

The following table presents the amounts, before tax, recognized in "Accumulated other comprehensive loss" in the Condensed Consolidated Balance Sheets and in the Condensed Consolidated Statements of Earnings that are related to the effective portion of the foreign currency forward contracts designated as cash flow hedges:

	Gain (Loss) Recognized in Other Comprehensive Income (Effective Portion)				Location of Gain (Loss) Reclassified from Accumulated Other Comprehensive Income into Net Earnings	Gain (Loss) Reclassified from Accumulated Other Comprehensive Income into Net Earnings (Effective Portion)			
	Three Months Ended		Nine Months Ended			Three Months Ended		Nine Months Ended	
(In millions)	June 27, 2014	June 28, 2013	June 27, 2014	June 28, 2013		June 27, 2014	June 28, 2013	June 27, 2014	June 28, 2013
Foreign currency forward contracts	$0.1	$(0.3)	$2.2	$2.0	Revenues	$(0.3)	$2.0	$1.0	$3.0

Balance Sheet Hedging Activities

The Company also hedges balance sheet exposures from its various subsidiaries and business units where the U.S. Dollar is the functional currency. The Company enters into foreign currency forward contracts to minimize the short-term impact of foreign currency fluctuations on monetary assets and liabilities denominated in currencies other than the U.S. Dollar functional currency. The foreign currency forward contracts are short term in nature, typically with a maturity of approximately one month, and are based on the net forecasted balance sheet exposure. These hedges of foreign currency denominated assets and liabilities do not qualify for hedge accounting treatment and are not designated as hedging instruments. For derivative instruments not designated as hedging instruments, changes in their fair values are recognized in "Selling, general and administrative expenses" in the Condensed Consolidated Statements of Earnings. Changes in the values of these hedging instruments are offset by changes in the values of foreign currency denominated assets and liabilities. Variations from the forecasted foreign currency assets or liabilities, coupled with a significant currency rate movement, may result in a material gain or loss if the hedges are not effectively offsetting the change in value of the foreign currency asset or liability. Other than foreign exchange hedging activities, the Company has no other free-standing or embedded derivative instruments.

The Company had the following outstanding foreign currency forward contracts that were either (i) entered into to hedge balance sheet exposures from its various foreign subsidiaries and business units or (ii) originally designated as cash flow hedges (primarily in Euro and Japanese yen) and were subsequently de-designated when the forecasted revenues were recognized:

	At June 27, 2014	
(In millions)	Notional Value Sold	Notional Value Purchased
Australian dollar	$14.9	$ -
British pound	4.2	-
Canadian dollar	-	10.3
Euro	170.3	-
Japanese yen	101.9	-
Hungarian Forint	2.0	
Indian Rupee	2.3	-
New Zealand dollar	3.4	-
Norwegian krone	6.9	-
Swedish krona	7.8	-
Swiss franc	-	52.1
Totals	$313.7	$ 62.4

VARIAN MEDICAL SYSTEMS, INC. AND SUBSIDIARIES

NOTES TO THE CONDENSED CONSOLIDATED FINANCIAL STATEMENTS – (CONTINUED)

(Unaudited)

The following table presents the gains (losses) recognized in the Condensed Consolidated Statements of Earnings related to the foreign currency forward exchange contracts that are not designated as hedging instruments:

Location of Gain (Loss) Recognized in Income on Derivative	Amount of Gain (Loss) Recognized in Net Earnings on Derivative Three Months Ended		Amount of Gain Recognized in Net Earnings on Derivative Nine Months Ended	
(In millions)	June 27, 2014	June 28, 2013	June 27, 2014	June 28, 2013
Selling, general and administrative expenses	$(1.1)	$3.4	$0.4	$15.7

The gains (losses) on these derivative instruments were significantly offset by the gains (losses) resulting from the remeasurement of monetary assets and liabilities denominated in currencies other than the U.S. Dollar functional currency.

Contingent Features

Certain of the Company’s derivative instruments are subject to master agreements which contain provisions that require the Company, in the event of a default, to settle the outstanding contracts in net liability positions by making settlement payments in cash or by setting off amounts owed to the counterparty against any credit support or collateral held by the counterparty. The counterparty’s right of set-off is not limited to the derivative instruments and applies to other rights held by the counterparty. These events of default, which are defined by the existing agreements, are primarily related to the Company’s failure to pay the counterparty under the derivative instruments, voluntary or involuntary bankruptcy, the Company’s default on its borrowings, and deterioration of creditworthiness of the surviving entity if the Company merges or transfers its assets or liabilities to another entity. As of June 27, 2014 and September 27, 2013, the Company did not have significant outstanding derivative instruments with credit-risk-related contingent features that were in a net liability position.

9. COMMITMENTS AND CONTINGENCIES

Product Warranty

The following table reflects the changes in the Company's accrued product warranty:

	Nine Months Ended	
(In millions)	June 27, 2014	June 28, 2013
Accrued product warranty, at beginning of period	$53.2	$52.8
Charged to cost of revenues	38.8	38.9
Actual product warranty expenditures	(41.5)	(41.0)
Accrued product warranty, at end of period	$50.5	$50.7

Long-term accrued product warranty costs of $1.9 and $14.1 million are included under "Other long-term liabilities" in the Condensed Consolidated Balance Sheets as of June 27, 2014 and September 27, 2013, respectively.

Other Commitments

In September 2011, the Company, through its Swiss subsidiary, participated in a $165.3 million loan ("Tranche A loan") for CPTC, under which the subsidiary committed to loan up to $115.3 million to finance the construction and start-up operations of a proton therapy center. On June 10, 2014 the Company, through its Swiss subsidiary, entered into a series of agreements pursuant to which JPMorgan Chase Bank, N.A. ("J.P. Morgan") assumed $45.0 million of the Company's original maximum commitment of $115.3 million, reducing the Company's maximum commitment under the Tranche A loan to $70.3 million. Through these agreements, the Company's Swiss subsidiary also increased its individual loan commitment by another $10.0 million ("Tranche B loan"). As of June 27, 2014, the Company's outstanding commitment under the Tranche A loan was $9.5 million and under the Tranche B loan was $1.4 million. See Note 16, "CPTC Loans" for additional discussion.

VARIAN MEDICAL SYSTEMS, INC. AND SUBSIDIARIES

NOTES TO THE CONDENSED CONSOLIDATED FINANCIAL STATEMENTS – (CONTINUED)

(Unaudited)

In April 2012, VMS entered into a strategic global partnership with Siemens AG ("Siemens") through which the Company committed to make certain payments, including up to $10 million in fixed fees and $20 million in license fees, in the event certain product development milestones are achieved. As of June 27, 2014, the outstanding fixed fees and license fees commitment for the Siemens agreement was $6.5 million and $19.5 million, respectively. See Note 17 "Strategic Arrangement" for additional discussion.

In October 2013, VMS entered into an amended agreement with dpiX and other parties that, among other things, provides the Company with the right to 50% of dpiX's total manufacturing capacity produced after January 1, 2014. The amended agreement requires the Company to pay for 50% of the fixed costs (as defined in the amended agreement), as determined at the beginning of each calendar year. As of June 27, 2014, the Company had a fixed cost commitment of $4.3 million related to this amended agreement, for the remaining three months of fiscal year 2014. The fixed cost commitment for future years will be determined based on forecasted dpiX sales and approved by the dpiX board of directors at the beginning of each calendar year. The amended agreement will continue unless the ownership structure of dpiX changes (as defined in the amended agreement). See Note 6 "Related Party Transactions" for additional discussion.

Environmental Remediation Liabilities

The Company's operations and facilities, past and present, are subject to environmental laws, including laws that regulate the handling, storage, transport and disposal of hazardous substances. Certain of those laws impose cleanup liabilities under certain circumstances. In connection with those laws and certain of the Company's past and present operations and facilities, the Company oversees various environmental cleanup projects and also reimburses certain third parties for cleanup activities. Those include facilities sold as part of the Company's electron devices business in 1995 and thin film systems business in 1997. In addition, the U.S. Environmental Protection Agency ("EPA") or third parties have named the Company as a potentially responsible party under the amended Comprehensive Environmental Response Compensation and Liability Act of 1980 ("CERCLA"), at sites to which the Company or the facilities of the sold businesses were alleged to have shipped waste for recycling or disposal (the "CERCLA sites"). In connection with the CERCLA sites, the Company to date has been required to pay only modest amounts as its contributions to cleanup efforts. Under the agreement that governs the spin-offs of Varian, Inc., which was acquired by Agilent Technologies Inc. (the successor entity hereinafter referred to as "VI"), and Varian Semiconductor Equipment Associates, Inc., which was acquired by Applied Materials, Inc. (the successor entity hereinafter referred to as "VSEA"), VI and VSEA are each obligated to indemnify the Company for one-third of the environmental cleanup costs associated with corporate, discontinued or sold operations prior to the spin-offs (after adjusting for any insurance proceeds or tax benefits received by the Company), as well as fully indemnify the Company for other liabilities arising from the operations of the business transferred to it as part of the spin-offs.

The Company spent $0.3 million (net of amounts borne by VI and VSEA) in both the three months ended June 27, 2014 and June 28, 2013, respectively, on environmental cleanup costs, third-party claim costs, project management costs and legal costs. The Company spent $0.8 million (net of amounts borne by VI and VSEA) in both the nine months ended June 27, 2014 and June 28, 2013, respectively, on such costs.

Inherent uncertainties make it difficult to estimate the likelihood of the cost of future cleanup, third-party claims, project management and legal services for the CERCLA sites and one of the Company's past facilities. Nonetheless, as

of June 27, 2014, the Company estimated that, net of VI's and VSEA's indemnification obligations, future costs associated with the CERCLA sites and this facility would range in total from $1.7 million to $9.9 million. The time frames over which these cleanup project costs are estimated vary, ranging from one year up to thirty years as of June 27, 2014. Management believes that no amount in that range is more probable of being incurred than any other amount and therefore accrued $1.7 million for these cleanup projects as of June 27, 2014. The accrued amount has not been discounted to present value due to the uncertainties that make it difficult to develop a single best estimate.

The Company believes it has gained sufficient knowledge to better estimate the scope and cost of monitoring, cleanup and management activities for its other past and present facilities. This, in part, is based on agreements with other parties and also cleanup plans approved by or completed in accordance with the requirements of the governmental agencies having jurisdiction. As of June 27, 2014, the Company estimated that the Company's future exposure, net of VI's and VSEA's indemnification obligations, for the costs at these facilities, and reimbursements of third-party's claims for these facilities, ranged in total from $6.3 million to $36.7 million. The time frames over which these costs are estimated to be incurred vary, ranging from one year to thirty years as of June 27, 2014. As to each of these facilities, management determined that a particular amount within the range of estimated costs was a better estimate than any other amount within the range, and that the amount and timing of these future costs were reliably determinable. The best estimate within that range was $11.8 million at June 27, 2014. Accordingly, the Company has accrued $9.3 million for these costs, which represents the best estimate discounted at 4%, net of inflation. This accrual is in addition to the $1.7 million described in the preceding paragraph.

VARIAN MEDICAL SYSTEMS, INC. AND SUBSIDIARIES

NOTES TO THE CONDENSED CONSOLIDATED FINANCIAL STATEMENTS – (CONTINUED)

(Unaudited)

These amounts are only estimates of anticipated future costs. The amounts the Company will actually spend may be greater or less than these estimates, even as the Company believes the degree of uncertainty will narrow as cleanup activities progress. While the Company believes its reserve is adequate, as the scope of the Company's obligations becomes more clearly defined, the Company may modify the reserve, and charge or credit future earnings accordingly. Nevertheless, based on information currently known to management, and assuming VI and VSEA satisfy their indemnification obligations, management believes the costs of these environmental-related matters are not reasonably likely to have a material adverse effect on the consolidated financial statements of the Company in any one fiscal year.

The Company evaluates its liability for investigation and cleanup costs in light of the obligations and apparent financial strength of potentially responsible parties and insurance companies with respect to which the Company believes it has rights to indemnity or reimbursement. The Company has asserted claims for recovery of environmental investigation and cleanup costs already incurred, and to be incurred in the future against various insurance companies and other third parties. The Company receives certain cash payments in the form of settlements and judgments from defendants, insurers and other third parties from time to time. The Company has also reached an agreement with an insurance company under which that insurer has agreed to pay a portion of the Company's past and future environmental-related expenditures. Receivables, net of VI's and VSEA's portion, from that insurer amounted to $2.5 million at June 27, 2014 and $2.4 million at September 27, 2013. The current and noncurrent receivables portion from that insurer is included in "Prepaid expenses and other current assets" and "Other assets," and the payable portion to that insurer is included "Other long-term liabilities" in the Condensed Consolidated Balance Sheets. The Company believes that this receivable is recoverable because it is based on a binding, written settlement agreement with what appears to be a financially viable insurance company, and the insurance company has paid the Company's claims in the past.

The availability of the indemnities of VI and VSEA will depend upon the future financial strength of VI and VSEA. Given the long-term nature of some of the liabilities, VI and VSEA may be unable to fund the indemnities in the future. It is also possible that a court would disregard this contractual allocation among the parties and require the Company to assume responsibility for obligations allocated to another party, particularly if the other party were to refuse or was unable to pay any of its allocated share. The agreement governing the spin-offs generally provides that if a court prohibits a company from satisfying its shared indemnification obligations, the indemnification obligations will be shared equally by the two other companies.

Other Matters

From time to time, the Company is a party to or otherwise involved in legal proceedings, claims and government inspections or investigations and other legal matters, both inside and outside the United States, arising in the ordinary course of its business or otherwise. These matters included a patent infringement lawsuit initiated on April 13, 2007 by the University of Pittsburgh of the Commonwealth System of Higher Education (the "University of Pittsburgh") regarding the Company's Real-time Position Management™ ("RPM") technology. The lawsuit was dismissed and re-filed on June 16, 2008 in the Northern District of California. The case was subsequently transferred to the United States District Court for the Western District of Pennsylvania ("trial court"). On or about December 21, 2011, the trial court entered a summary judgment order in the case finding that the Company's RPM technology was covered by some of the claims of the subject patent. Subsequently, in early 2012, in the proceedings at the trial court on the remaining issues in litigation, it was found (i) that the Company willfully infringed the subject patent, (ii) that the Company is

liable for approximately $40 million in actual damages and (iii) that the subject patent was valid. The trial court had ordered the Company to pay a total of approximately $102 million, comprised of approximately $80 million in enhanced damages (a doubling of the damages amount), pre-judgment interest to the damage award of approximately $13 million and approximately $9 million in attorneys' fees. The trial court also ordered the Company to pay ongoing royalties at the rates found by the jury for sales after the date of judgment. The Company appealed the findings against it. In January 2014, the Company entered into a settlement agreement with the University of Pittsburgh that was dependent upon the appellate ruling. In April 2014, the appellate court issued an opinion affirming the trial court judgment in part and reversing it in part. Based on the opinion and the terms of the settlement agreement, the Company paid $35.6 million in full settlement of the lawsuit to the University of Pittsburgh in the third fiscal quarter of 2014. Prior to the beginning of the second quarter of fiscal year 2014, the Company had accrued in aggregate approximately $5 million for the low end of the range of the probable settlement value for this matter. In the second quarter of fiscal year 2014 the Company accrued an additional $25.1 million of the $35.6 million for all damages and interest related to the case and in the third quarter of fiscal year 2014 recorded the remaining amount of approximately $5.5 million for future royalties as prepaid royalties. The amount of prepaid royalties is being amortized over the remaining life of the patent of approximately two and a half years.

VARIAN MEDICAL SYSTEMS, INC. AND SUBSIDIARIES

NOTES TO THE CONDENSED CONSOLIDATED FINANCIAL STATEMENTS – (CONTINUED)

(Unaudited)

The Company accrues amounts, to the extent they can be reasonably estimated, that it believes are adequate to address any liabilities related to legal proceedings and other loss contingencies that the Company believes will result in a probable loss (including, among other things, probable settlement value). However, such matters are subject to many uncertainties and outcomes are not predictable with assurance. The Company is unable to estimate a range of reasonably possible losses with respect to all other matters. There can be no assurances as to whether the Company will become subject to significant additional claims and liabilities with respect to ongoing or future proceedings. If actual liabilities significantly exceed the estimates made, the Company's consolidated financial position, results of operations or cash flows could be materially adversely affected.

Restructuring Charges

As part of the Company's plan to enhance operational performance through productivity initiatives, the Company offered an enhanced retirement program to its qualified employees during the first quarter of fiscal year 2013. The Company incurred insignificant restructuring charges during the three months ended June 28, 2013 and incurred $6.7 million of restructuring charges during nine months ended June 28, 2013. No restructuring charges were incurred during the three and nine months ended June 27, 2014 in relation to this or any other restructuring program.

10. RETIREMENT PLANS

The Company's net defined benefit and post-retirement benefit costs were composed of the following:

	Three Months Ended		Nine Months Ended	
(In thousands)	June 27, 2014	June 28, 2013	June 27, 2014	June 28, 2013
Defined Benefit Plans				
Service cost	$1,028	$1,169	$3,077	$3,598
Interest cost	1,545	1,276	4,591	3,891
Expected return on plan assets	(1,977)	(1,388)	(5,869)	(4,235)
Amortization of prior service cost	43	41	128	121
Recognized actuarial loss	539	682	1,616	2,045
Net periodic benefit cost	$1,178	$1,780	$3,543	$5,420
Post-Retirement Benefit Plans				
Interest cost	$43	$40	$129	120
Amortization of prior service cost	1	1	3	3
Recognized actuarial (gain) / loss	(3)	15	(9)	45

Net periodic benefit cost	$41	$56	$123	$168

The Company made contributions to the defined benefit plans of $5.7 million during the nine months ended June 27, 2014. The Company currently expects total contributions to the defined benefit plans for fiscal year 2014 will be approximately $7.3 million. The Company made contributions to the post-retirement benefit plans of $0.4 million during the nine months ended June 27, 2014. The Company currently expects total contributions to the post-retirement benefit plans for fiscal year 2014 will be approximately $0.5 million.

11. INCOME TAXES

The Company’s effective tax rate was 25.5% for the three months ended June 27, 2014, compared to 27.6% for the same period of fiscal year 2013. The decrease in the Company’s effective tax rate during the three months ended June 27, 2014 compared to the year ago period was primarily due to a larger net benefit for discrete items in the current period, which is primarily related to the release of certain liabilities for uncertain tax positions due to the expiration of the statutes of limitation in various jurisdictions. The Company’s effective tax rate was 28.1% for the nine months ended June 27, 2014, compared to 28.7% for the same period of fiscal year 2013. The decrease in the Company’s effective tax rate during the nine months ended June 27, 2014 compared to the year ago period was primarily due to a favorable shift in the mix of geographic earnings.

The Company’s effective income tax rate differs from the U.S. federal statutory rate primarily because the Company’s foreign earnings are taxed at rates that are, on average, lower than the U.S. federal rate, and because the Company’s domestic earnings are subject to state income taxes.

VARIAN MEDICAL SYSTEMS, INC. AND SUBSIDIARIES

NOTES TO THE CONDENSED CONSOLIDATED FINANCIAL STATEMENTS – (CONTINUED)

(Unaudited)

The total amount of unrecognized tax benefits did not materially change during the nine months ended June 27, 2014; however, the amount of unrecognized tax benefits has increased as a result of positions taken during the current and prior years, and has decreased as the result of the expiration of the statutes of limitation and audit settlements in various jurisdictions.

12. STOCKHOLDERS' EQUITY

Stock Repurchase Program

In August 2012, the VMS Board of Directors authorized the repurchase of 8,000,000 shares of VMS common stock from September 29, 2012 through December 31, 2013. The Company repurchased a total of 2,000,000 shares of VMS common stock during the three months ended December 27, 2013 and thereafter no shares of VMS common stock remained available for repurchase under this repurchase authorization. All shares that were repurchased have been retired.

In November 2013, the VMS Board of Directors authorized the repurchase of an additional 6,000,000 shares of VMS common stock from December 30, 2013 through December 31, 2014. Stock repurchases under the November 2013 authorization may be made in open market purchases, in privately negotiated transactions (including accelerated share repurchase programs) or under Rule 10b5-1 share repurchase plans, and may be made from time to time in one or more blocks. The Company has repurchased a total of 1,250,000, and 5,250,000 of VMS common stock during the three and nine months ended June 27, 2014, respectively. The 5,250,000 shares repurchased during the nine months ended fiscal year 2014 included 2,000,000 shares repurchased under the August 2012 repurchase program. All shares that were repurchased have been retired. As of June 27, 2014, 2,750,000 shares of VMS common stock remained available for repurchase under this repurchase authorization.

Other Comprehensive Earnings

The changes in accumulated other comprehensive earnings (loss) by component and related tax effects are summarized as follows (in thousands):

	Net Unrealized Gains (Losses) Defined benefit pension and	Net Unrealized Gains (Losses) Cash Flow	Cumulative Translation	Accumulated Other Comprehensive

	post-retirement benefit plans	Hedging Instruments	Adjustment and Other	Earnings (Loss)
Balance at September 27, 2013	$ (40,081)	$ (691)	$ 701	$ (40,071)
Other comprehensive earnings before reclassifications	-	2,177	(752)	1,425
Amounts reclassified out of other comprehensive earnings	1,737	(1,038)	-	699
Tax expense	(321)	(427)	-	(748)
Balance at June 27, 2014	$ (38,665)	$ 21	$ (51)	$ (38,695)

	Net Unrealized Gains (Losses) Defined benefit pension and post-retirement benefit plans	Net Unrealized Gains (Losses) Cash Flow Hedging Instruments	Cumulative Translation Adjustment and Other	Accumulated Other Comprehensive Earnings (Loss)
Balance at September 28, 2012	$ (48,623)	$ 531	$ (8,529)	$ (56,621)
Other comprehensive earnings before reclassifications	-	2,046	1,998	4,044
Amounts reclassified out of other comprehensive earnings	2,211	(2,962)	-	(751)
Tax benefit / (expense)	(411)	344	-	(67)
Balance at June 28, 2013	$ (46,823)	$ (41)	$ (6,531)	$ (53,395)

VARIAN MEDICAL SYSTEMS, INC. AND SUBSIDIARIES

NOTES TO THE CONDENSED CONSOLIDATED FINANCIAL STATEMENTS – (CONTINUED)

(Unaudited)

The amounts reclassified out of other comprehensive earnings into the Condensed Consolidated Statements of Earnings, with line item location, during each period were as follows (in thousands):

	Three Months Ended		Nine Months Ended		
	June 27, 2014	June 28, 2013	June 27, 2014	June 28, 2013	
Comprehensive Earnings Components	Income (Loss) Before Taxes		Income (Loss) Before Taxes		Line Item in Statements of Earnings
Unrealized gains and (losses) on defined benefit pension and post-retirement benefit plans	$(579)	$(736)	$(1,737)	$(2,211)	Cost of Revenues & Operating Expenses
Unrealized gains and (losses) on cash flow hedging instruments	(239)	2,000	1,038	2,962	Revenues
Total amounts reclassified out of other comprehensive earnings	$(818)	$1,264	$(699)	$751	

13. EMPLOYEE STOCK PLANS

The table below summarizes the net share-based compensation expense recognized for employee stock awards and for the option component of the employee stock purchase plan shares:

	Three Months Ended		Nine Months Ended	
(In thousands)	June 27, 2014	June 28, 2013	June 27, 2014	June 28, 2013
Cost of revenues - Product	$950	$1,058	$2,374	$3,443
Cost of revenues - Service	1,330	1,069	3,392	2,530
Research and development	1,771	1,515	4,392	4,741
Selling, general and administrative	7,363	6,882	19,896	23,201
Total share-based compensation expense	11,414	10,524	30,054	33,915
Tax effects	(3,564)	(3,181)	(9,301)	(10,359)
Net share-based compensation expense	$7,850	$7,343	$20,753	$23,556

During the nine months ended June 27, 2014, the Company granted performance units to certain employees under the Third Amended 2005 Plan. The number of shares of VMS common stock ultimately issued under the performance units at the end of a three-year performance period will depend on the Company's business performance during the three-year period against specified performance targets set by the Compensation and Management Development Committee of the Board of Directors at the beginning of the period. Subject to certain exceptions, any unvested performance unit awards are forfeited at the time of termination.

The fair value of options granted was estimated at the date of grant using the Black-Scholes model with the following weighted average assumptions:

	Three Months Ended		Nine Months Ended	
	June 27, 2014	June 28, 2013	June 27, 2014	June 28, 2013
Employee Stock Option Plans				
Expected term (in years)	-	4.77	4.13	4.76
Risk-free interest rate	-	0.7 %	1.2 %	0.6 %
Expected volatility	-	29.6 %	24.6 %	32.2 %
Expected dividend	-	0.0 %	0.0 %	0.0 %
Weighted average fair value at grant date	$-	$18.21	$18.23	$19.73

VARIAN MEDICAL SYSTEMS, INC. AND SUBSIDIARIES

NOTES TO THE CONDENSED CONSOLIDATED FINANCIAL STATEMENTS – (CONTINUED)

(Unaudited)

The option component of employee stock purchase plan shares was estimated at the date of grant using the Black-Scholes model with the following weighted average assumptions:

	Three Months Ended		Nine Months Ended	
	June 27, 2014	June 28, 2013	June 27, 2014	June 28, 2013
Employee Stock Purchase Plan				
Expected term (in years)	0.50	0.50	0.50	0.50
Risk-free interest rate	0.1 %	0.1 %	0.1 %	0.1 %
Expected volatility	11.1 %	13.6 %	12.8 %	16.5 %
Expected dividend	0.0 %	0.0 %	0.0 %	0.0 %
Weighted average fair value at grant date	$14.42	$12.21	$14.20	$12.95

A summary of share-based awards available for grant is as follows:

(In thousands)	Shares Available for Grant
Balance at September 27, 2013	9,925
Granted	(1,923)
Cancelled or expired	151
Balance at June 27, 2014	8,153

Awards other than stock options set forth in the table were counted against the shares available for grant limit of the Third Amended 2005 Plan as 2.5 shares for every one share awarded before February 9, 2012 and were counted against the shares available for grant limit as 2.6 shares for every one awarded on or after February 9, 2012. In addition, the shares available for grant limit was further adjusted to reflect a maximum payout of 1.5 shares that could be issued for each performance unit granted.

Activity under the Company’s employee stock plans is presented below:

	Options Outstanding	
		Weighted-

(In thousands, except per share amounts)	Number of Shares	Weighted Average Exercise Price	Average Remaining Contractual Term (in years)	Aggregate Intrinsic Value (1)
Balance at September 27, 2013	4,485	$ 53.02		
Granted	619	83.49		
Cancelled or expired	(36)	71.03		
Exercised	(1,421)	48.39		
Balance at June 27, 2014	3,647	$ 59.84	3.4	$ 87,565
Exercisable at June 27, 2014	2,688	$ 53.64	2.4	$ 81,202

(1) The aggregate intrinsic value represents the total pre-tax intrinsic value of options, which is computed based on the difference between the exercise price and VMS's closing common stock price of $83.85 as of June 27, 2014, the last trading date of the third quarter of fiscal year 2014, and which would have been received by the option holders had all option holders exercised and sold their options as of that date.

As of June 27, 2014, there was $13.4 million of total unrecognized compensation expense related to outstanding stock options. This unrecognized compensation expense is expected to be recognized over a weighted average period of 1.8 years.

VARIAN MEDICAL SYSTEMS, INC. AND SUBSIDIARIES

NOTES TO THE CONDENSED CONSOLIDATED FINANCIAL STATEMENTS – (CONTINUED)

(Unaudited)

The activity for restricted stock, restricted stock units, deferred stock units and performance units is summarized as follows:

(In thousands, except per share amounts)	Shares	Weighted Average Grant-Date Fair Value
Balance at September 27, 2013	1,035	$ 64.36
Granted	467	82.50
Vested	(331)	63.40
Cancelled or expired	(38)	70.40
Balance at June 27, 2014	1,133	$ 72.10

Share-based compensation expense for restricted common stock, restricted stock units and deferred stock units is measured at the stock's fair value on the date of grant and is amortized over each award's respective service period. The Company values performance units using the Monte Carlo simulation model on the date of grant with assumptions that includes the historical volatilities of shares of VMS common stock, as well as the shares of common stock of peer companies. In addition, the Company estimates the probability that certain performance conditions that affect the vesting of performance units will be achieved, and recognizes expense only for those awards expected to vest.

As of June 27, 2014, unrecognized compensation expense totaling $45.9 million was related to awards of restricted stock, restricted stock units, deferred stock units and performance units. This unrecognized compensation expense is expected to be recognized over a weighted average period of 1.9 years.

14. EARNINGS PER SHARE

Basic net earnings per share is computed by dividing net earnings by the weighted average number of shares of VMS common stock outstanding for the period. Diluted net earnings per share is computed by dividing net earnings by the sum of the weighted average number of common shares outstanding and dilutive common shares under the treasury stock method.

The following table sets forth the computation of net basic and diluted earnings per share:

	Three Months Ended		Nine Months Ended	
	June 27,	June 28,	June 27,	June 28,

(In thousands, except per share amounts)	2014	2013	2014	2013
Net earnings	$107,090	$112,831	$297,838	$320,902
Weighted average shares outstanding - basic	103,644	108,158	104,585	108,741
Dilutive effect of potential common shares	1,225	1,602	1,325	1,755
Weighted average shares outstanding - diluted	104,869	109,760	105,910	110,496
Net earnings per share - basic	$1.03	$1.04	$2.85	$2.95
Net earnings per share - diluted	$1.02	$1.03	$2.81	$2.90
Anti-dilutive employee shared based awards, excluded	657	737	720	739

The Company excludes potentially dilutive common shares (consisting of shares underlying stock options and the employee stock purchase plan) from the computation of diluted weighted average shares outstanding if the per share value, either the exercise price of the awards or the sum of (a) the exercise price of the awards and (b) the amount of the compensation cost attributed to future services and not yet recognized and (c) the amount of tax benefit or shortfall that would be recorded in additional paid-in capital when the award becomes deductible, is greater than the average market price of the shares, because the inclusion of the shares underlying these stock awards would be antidilutive to earnings per share.

VARIAN MEDICAL SYSTEMS, INC. AND SUBSIDIARIES

NOTES TO THE CONDENSED CONSOLIDATED FINANCIAL STATEMENTS – (CONTINUED)

(Unaudited)

15. BUSINESS COMBINATIONS

In April 2014, the Company closed the acquisition of certain assets of Velocity Medical Solutions LLC (“Velocity”), a privately-held Atlanta-based developer of specialized software for cancer clinics. The Velocity software aggregates unstructured treatment and imaging data from diverse systems to give a more comprehensive view of a patient's diagnostic imaging and treatment history and help clinicians make more informed treatment decisions. The acquired assets of Velocity were integrated into the Company’s Oncology Systems business and will increase the Company’s current product offerings. The acquisition was accounted for as a business combination. The total purchase price of the acquisition of $19.9 million consisted of $17.0 million in cash (of which $2.6 million was held back) and $2.9 million of earn-out consideration at fair value. Of the purchase price, $10.6 million was preliminarily allocated to amortizable intangible assets, $9.8 million goodwill, and $(0.5) million to net assumed liabilities. If any additional information becomes available, we may revise our preliminary purchase price allocation. Goodwill represents the excess of the purchase price over the fair value of the net tangible and intangible assets acquired and in this case is deductible for income tax purposes. The amortization period for the intangible assets acquired through the acquisition was as follows: 6 years for Developed Technology, 7 years for Customer Relationships and 6 years for Trade Name. The goodwill recognized, which was assigned to the Company’s Oncology Systems reporting unit, is primarily attributable to expected synergies resulting from the acquisition. The Company also completed an insignificant acquisition during the first quarter of fiscal year 2014.

The business combination transactions during the first nine months of fiscal year 2014 were not significant, and therefore pro forma disclosures have not been presented.

VARIAN MEDICAL SYSTEMS, INC. AND SUBSIDIARIES

NOTES TO THE CONDENSED CONSOLIDATED FINANCIAL STATEMENTS – (CONTINUED)

(Unaudited)

16. CPTC LOANS

In April 2010, the Company signed an $88 million agreement to supply a proton therapy system to CPTC, a variable interest entity that was established to finance and operate the Scripps Proton Therapy Center in San Diego, California. The Company began recognizing revenues under this contract in the fourth quarter of fiscal year 2011. In June 2011, the Company signed a ten-year, approximately $60 million agreement with CPTC to service the proton therapy system which commenced in the quarter ended December 27, 2013. In addition, in September 2011, ORIX and the Company, through its Swiss subsidiary, committed to loan up to $165.3 million ("Tranche A loan") to CPTC to fund the development, construction and initial operations of the Scripps Proton Therapy Center. ORIX is the loan agent for this facility and, along with CPTC and Scripps, has budgetary approval authority for the Scripps Proton Therapy Center. The Company's maximum loan commitment under the Tranche A loan was $115.3 million, reflecting the Company's pro rata share of 69.75% of the obligation to fund the initial distribution and subsequent advances. In June 2014, the Company, through its Swiss subsidiary, entered into a series of agreements pursuant to which JPMorgan Chase Bank, N.A. ("J.P. Morgan") assumed $45 million of the Company's original maximum commitment of $115.3 million, reducing the Company's maximum commitment under the Tranche A loan to $70.3 million. Pursuant to these agreements, J.P. Morgan purchased $38.1 million of the Company's outstanding Tranche A loan at par value and is obligated to fund up to an additional $6.9 million of the remaining Tranche A loan commitment. Through these agreements, the Company's Swiss subsidiary also increased its individual loan commitment by $10 million ("Tranche B loan") and as a result, the Company's maximum loan commitment under the Tranche A and Tranche B loans (collectively, referred to as the "CPTC Loans") is $80.3 million reflecting the Company's pro rata share of 45.8% of the total obligation to fund CPTC of $175.3 million.

As of June 27, 2014, the Company had loaned $60.8 million of its $70.3 million commitment under the Tranche A loan. The Company intends to sell all or a portion of its participation in its Tranche A loan before the maturity date. Upon the sale of all or a portion of the Tranche A loan, the Company will not be required to make further loan advances for the portion of the loan that is sold. As of June 27, 2014 the Company had loaned $8.6 million of its $10.0 million commitment under the Tranche B loan. The amounts loaned under the Tranche A and Tranche B loans include accrued interest. The CPTC loans are accounted for as available-for-sale securities and recorded at fair value. The Tranche A loan is classified as a short-term investment and included in current assets and the Tranche B loan is included in other assets on the Company's Condensed Consolidated Balance Sheets. The Tranche B loan is subordinated to the Tranche A loan in the event of default, but otherwise has the same terms as the Tranche A loan. The Company's subsidiary is not obligated to fund any additional amounts to CPTC beyond the $80.3 million under the CPTC Loans.

Pursuant to the agreements entered into in June 2014, the CPTC Loans mature in September 2017 and bear interest at the London Interbank Offer Rate ("LIBOR") plus 7.00% per annum with a minimum interest rate of 9.00% per annum. Interest only payments on the CPTC Loans are due monthly in arrears until January 1, 2015, at which time monthly payments based on amortization of the principal balance over a 15-year period at the above mentioned interest rate become due and payable. The Company, as one of the lenders, is entitled to certain fees, including a commitment fee of 1.5% of the Tranche A loan commitment amount and an exit fee of 1% of the amount of CPTC Loans principal paid, whether as a result of prepayment or maturity. The CPTC Loans are collateralized by all of the assets of the Scripps Proton Therapy Center. In connection with the agreements entered into in June 2014, the Company's subsidiary share of the gross revenues of the Scripps Proton Therapy Center for 35 years was reduced from 4% to

2.5%. Additionally, as a result of J.P. Morgan's assumption of a portion of the Company's maximum loan commitment, the Company's subsidiary's share of 2.5% of gross revenues is further proportionately split between the Company's subsidiary and J.P. Morgan based on their maximum amount of CPTC Loans commitment. The Company's subsidiary's right of revenue sharing may further be reduced upon the sale of a portion of the Company's loan and will be reduced to an amount not to exceed 1% of the gross revenues of the Scripps Proton Therapy Center upon repayment of the first $71 million of the Company's loan amount.

The Company has determined that CPTC is a variable interest entity and that the Company holds a significant variable interest of CPTC through its subsidiary's participation in the loan facility and its agreements to supply and service the proton therapy equipment. The Company has concluded that it is not the primary beneficiary of CPTC. The Company has no voting rights, has no approval authority or veto rights for CPTC's budget, and does not have the power to direct patient recruitment, clinical operations and management of the Scripps Proton Therapy Center, which the Company believes are the matters that most significantly affect CPTC's economic performance.

As of June 27, 2014, in addition to the $60.8 million of the Tranche A loan and $8.6 million of the Tranche B loan to CPTC, the Company had recorded $30.5 million in accounts receivable from CPTC, which includes unbilled accounts receivable. As of September 27, 2013, the outstanding Tranche A loan balance to CPTC was $62.7 million and the accounts receivable balance from CPTC was $48.4 million, which includes unbilled accounts receivable. The Company's exposure to loss as a result of its involvement with CPTC was limited to the carrying amounts of these assets on its Condensed Consolidated Balance Sheets.

VARIAN MEDICAL SYSTEMS, INC. AND SUBSIDIARIES

NOTES TO THE CONDENSED CONSOLIDATED FINANCIAL STATEMENTS – (CONTINUED)

(Unaudited)

17. STRATEGIC ARRANGEMENT

In April 2012, VMS entered into a strategic global alliance with Siemens through which, among other things, the Company and Siemens are working on developing interfaces to enable the Company's ARIA® oncology information system software to connect with Siemens linear accelerators and imaging systems. Under the agreement establishing this collaboration, the Company committed to make certain payments, including up to $10.0 million in fixed fees and $20.0 million in license fees, in the event certain product development milestones are achieved. The Company will also pay for additional licenses beyond the minimum quantities set forth in the agreement. As of June 27, 2014, the outstanding fixed fees and license fees commitment under the Siemens agreement was $6.5 million and $19.5 million, respectively.

In addition, pursuant to this agreement, the Company represents Siemens diagnostic imaging products to radiation oncology clinics in most international markets and in North America, and Siemens, in turn, represents the Company's equipment and software products for radiotherapy and radiosurgery within its offerings to its healthcare customers in agreed upon countries. The Company receives commissions from Siemens for sales agency activities provided to Siemens and makes commission payments to Siemens for sales agency activities provided to the Company as part of this agreement. This agreement also provides a framework for both companies to explore opportunities to co-develop new imaging and treatment solutions in the future.

18. SEGMENT INFORMATION

During the second quarter of fiscal year 2014, the Company changed its organizational structure resulting in a change in operating and reportable segments. The Company's operations are grouped into two reportable operating segments: Oncology Systems and Imaging Components. The Imaging Components segment includes the Company's X-ray imaging tubes and flat panel products (previously reported as "X-Ray Products" segment), as well as our security and inspection products (previously reported as "Security and Inspection Products" under the "Other" category). The Company's GTC and VPT businesses are reflected in the "Other" category because these operating segments do not meet the criteria of a reportable operating segment. The operating segments were determined based on how the Company's Chief Executive Officer, its Chief Operating Decision Maker ("CODM"), views and evaluates the Company's operations. The CODM allocates resources to and evaluates the financial performance of each operating segment primarily based on operating earnings. There was no change to the reporting units as a result of the change in operating segments.

Description of Segments

The Oncology Systems segment designs, manufactures, sells and services hardware and software products for treating cancer with radiotherapy, stereotactic radiotherapy, stereotactic body radiotherapy, stereotactic radiosurgery and brachytherapy. Products include linear accelerators, brachytherapy afterloaders, treatment simulation and verification equipment and accessories; as well as information management, treatment planning and image processing software. Oncology Systems' products enable radiation oncology departments in hospitals and clinics to perform conventional radiotherapy treatments and offer advanced treatments such as fixed field intensity-modulated radiation therapy ("IMRT"), image-guided radiation therapy ("IGRT"), volumetric modulated arc therapy and stereotactic radiotherapy, as

well as to treat patients using brachytherapy techniques, which involve temporarily implanting radioactive sources. The Company's Oncology Systems products are also used by neurosurgeons to perform stereotactic radiosurgery. Oncology Systems' customers worldwide include university research and community hospitals, private and governmental institutions, healthcare agencies, physicians' offices and cancer care clinics.

The Imaging Components segment designs, manufactures, sells and services X-ray imaging components for use in a range of applications, including radiographic or fluoroscopic imaging, mammography, special procedures, computed tomography and industrial applications. The Company's X-ray imaging components are sold to large imaging system OEM customers that incorporate them into their medical diagnostic, dental, veterinary and industrial imaging systems. The Company sells X-ray tubes and flat panel digital image detectors for filmless X-ray imaging (commonly referred to as "flat panel detectors" or "digital image detectors") to small OEM customers, independent service companies and directly to end-users for replacement purposes. The Imaging Components segment also designs, manufactures, sells and services Linatron® X-ray accelerators, imaging processing software and image detection products (including IntellX™) for security and inspection purposes, such as cargo screening at ports and borders and nondestructive examination in a variety of applications. The Company generally sells security and inspection products to OEM customers who incorporate its products into their inspection systems, which are then sold to customs and other government agencies, as well as to commercial private parties in the casting, power, aerospace, chemical, petro-chemical and automotive industries for nondestructive product examination purposes.

The Company has two other businesses, VPT and GTC, which are reported together under the "Other" category.

VARIAN MEDICAL SYSTEMS, INC. AND SUBSIDIARIES

NOTES TO THE CONDENSED CONSOLIDATED FINANCIAL STATEMENTS – (CONTINUED)

(Unaudited)

The VPT business develops, designs, manufactures, sells and services products and systems for delivering proton therapy, a form of external beam radiotherapy using proton beams for the treatment of cancer.

GTC develops technologies that enhance the Company's current businesses or may lead to new business areas, including technology to improve radiation therapy and X-ray imaging, as well as other technology for a variety of applications, including security and cargo screening.

The following table summarizes selected operating results information for each reportable segment:

	Three Months Ended		Nine Months Ended	
(In millions)	June 27, 2014	June 28, 2013	June 27, 2014	June 28, 2013
Revenues				
Oncology Systems	$578.2	$561.3	$1,722.7	$1,667.4
Imaging Components	161.8	158.2	492.0	474.6
Total reportable segments	$740.0	$719.5	$2,214.7	$2,142.0
Other	7.7	6.7	23.0	31.0
Total company	$747.7	$726.2	$2,237.7	$2,173.0
Operating Earnings (Loss)				
Oncology Systems	$123.5	$129.5	$369.3	$381.0
Imaging Components	41.7	40.2	124.6	118.9
Total reportable segments	$165.2	$169.7	$493.9	$499.9
Other	(12.2)	(11.9)	(40.9)	(35.7)
Corporate	(10.5)	(3.1)	(41.0)	(16.3)
Total company	$142.5	$154.7	$412.0	$447.9

Prior period numbers have been recast to conform to the current period's presentation.

19. SUBSEQUENT EVENT

In July 2014, the Company closed the acquisition of certain assets and liabilities of Transpire, Inc., a privately-held developer of software solutions for accurately and rapidly predicting the macroscopic behavior of radiation. The transaction will be accounted for as a business combination. The total purchase consideration for the acquisition is $16 million in cash, excluding potential earn-out consideration of up to $4 million, which will be paid over the next three years if certain performance targets are achieved. The Company is currently evaluating the purchase price allocation

for this transaction.

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

To the Board of Directors and

Stockholders of Varian Medical Systems, Inc.:

We have reviewed the accompanying condensed consolidated balance sheet of Varian Medical Systems Inc. and its subsidiaries as of June 27, 2014, and the related condensed consolidated statement of earnings and of comprehensive earnings for the three-month and nine-month periods ended June 27, 2014 and June 28, 2013 and the condensed consolidated statement of cash flows for the nine-month periods ended June 27, 2014 and June 28, 2013. These interim financial statements are the responsibility of the Company's management.

We conducted our review in accordance with the standards of the Public Company Accounting Oversight Board (United States). A review of interim financial information consists principally of applying analytical procedures and making inquiries of persons responsible for financial and accounting matters. It is substantially less in scope than an audit conducted in accordance with the standards of the Public Company Accounting Oversight Board (United States), the objective of which is the expression of an opinion regarding the financial statements taken as a whole. Accordingly, we do not express such an opinion.

Based on our review, we are not aware of any material modifications that should be made to the accompanying condensed consolidated interim financial statements for them to be in conformity with accounting principles generally accepted in the United States of America.

We previously audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the consolidated balance sheet as of September 27, 2013 and the related consolidated statements of earnings and of comprehensive earnings, of stockholders' equity, and of cash flows for the year then ended (not presented herein), and in our report dated November 26, 2013, we expressed an unqualified opinion on those consolidated financial statements. In our opinion, the information set forth in the accompanying condensed consolidated balance sheet as of September 27, 2013, is fairly stated in all material respects in relation to the consolidated balance sheet from which it has been derived.

/s/ PRICEWATERHOUSECOOPERS LLP

PricewaterhouseCoopers LLP

San Jose, California

August 5, 2014

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Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations

Forward-Looking Statements

This Quarterly Report on Form 10-Q contains "forward-looking" statements within the meaning of the Private Securities Litigation Reform Act of 1995, which provides a "safe harbor" for statements about future events, products and future financial performance that are based on the beliefs of, estimates made by, and information currently available to the management of Varian Medical Systems, Inc. ("VMS") and its subsidiaries (collectively "we," "our" or the "Company"). The outcome of the events described in these forward-looking statements is subject to risks and uncertainties. Actual results and the outcome or timing of certain events may differ significantly from those projected in these forward-looking statements or management's current expectations due to the factors cited in this "Management's Discussion and Analysis of Financial Condition and Results of Operations" ("MD&A"), the Risk Factors listed under Part II, Item 1A of this Quarterly Report on Form 10-Q, and other factors described from time to time in our other filings with the Securities and Exchange Commission ("SEC"), or other reasons. For this purpose, statements concerning: industry or market segment outlook; market acceptance of or transition to new products or technology such as fixed field intensity-modulated radiation therapy ("IMRT"), image-guided radiation therapy ("IGRT"), stereotactic radiosurgery, volumetric modulated arc therapy, brachytherapy, software, treatment techniques, proton therapy and advanced X-ray tube and panel products; growth drivers; future orders, revenues, backlog, earnings or other financial results; and any statements using the terms "believe," "expect," "anticipate," "can," "should," "would," "could," "estimate," "n "intended," "potential," and "possible" or similar statements are forward-looking statements that involve risks and uncertainties that could cause our actual results and the outcome and timing of certain events to differ materially from those projected or management's current expectations. By making forward-looking statements, we have not assumed any obligation to, and you should not expect us to, update or revise those statements because of new information, future events or otherwise.

Overview

During the second quarter of fiscal year 2014, we changed our organizational structure resulting in a change in operating and reportable segments. Our operations are grouped into two reportable operating segments: Oncology Systems and Imaging Components. The Imaging Components segment includes our X-ray imaging tubes and flat panel products (previously reported as "X-Ray Products" segment), as well as our security and inspection products (previously reported as "Security and Inspection Products" under the "Other" category). Our Ginzton Technology Center ("GTC") and Varian Particle Therapy ("VPT") businesses are reflected in the "Other" category because these operating segments do not meet the criteria of a reportable operating segment. The operating segments were determined based on how our Chief Executive Officer, who is our Chief Operating Decision Maker ("CODM"), views and evaluates our operations. The CODM allocates resources to and evaluates the financial performance of each operating segment primarily based on operating earnings. Prior period numbers have been recast to conform to the current period's presentation.

In the third quarter of fiscal year 2014, revenues increased 3% and gross margin increased 0.5 percentage points, compared to the year-ago quarter. Net earnings per diluted share decreased 1% in the third quarter of fiscal year 2014, compared to the year-ago quarter. Net earnings decreased 5% in the third quarter of fiscal year 2014, compared to the year-ago quarter. During the third quarter of fiscal year 2014, operating expenses included a charge of approximately $8 million relating to impairment of a portion of our privately-held equity investment in Augmenix, Inc. ("Augmenix"). Gross orders for Oncology Systems decreased 1% and Imaging Components increased 12% in the third quarter of fiscal year 2014, compared to the year-ago quarter. We recorded gross orders of $57 million in the "Other" category during the third quarter of fiscal year 2014. Our backlog at June 27, 2014 was 4% higher than at the end of the third quarter of fiscal year 2013.

In order to assist with the assessment of how our underlying businesses performed, we compare the percentage change in revenues and gross orders from one period to another, excluding the effect of foreign currency fluctuations (i.e., using constant currency exchange rates). To present this information on a constant currency basis, we convert current period revenues and gross orders in currencies other than U.S. Dollars into U.S. Dollars using the comparable prior period's average exchange rate. The U.S. Dollar strengthened against the Japanese Yen and weakened against the Euro in the third quarter of fiscal year 2014, compared to the prior-year quarter. In the third quarter of fiscal year 2014, our total revenues increased 2% in constant currency and gross orders for Oncology Systems decreased 2% in constant currency, each compared to the prior-year quarter.

Oncology Systems. Our largest business segment is Oncology Systems, which designs, manufactures, sells and services hardware and software products for treating cancer with conventional radiotherapy (including IMRT, IGRT and volumetric modulated arc therapy), stereotactic body radiotherapy, stereotactic radiotherapy, stereotactic radiosurgery and brachytherapy.

Our primary goal in the Oncology Systems business is to promote the adoption of more advanced and effective cancer treatments. In our view, the fundamental market forces that drive long-term growth in our Oncology Systems business are the rise in cancer cases; technology advances and product developments that are leading to improvements in patient care; customer demand for the more advanced and effective cancer treatments that we enable; competitive conditions among hospitals and clinics to offer such advanced treatments; continued improvement in safety and cost efficiency in delivering radiation therapy; and underserved medical needs outside of the United States. Over the last few years, we have seen a greater percentage of Oncology Systems gross orders and revenues coming from emerging markets within our international region, which typically demand lower-priced products compared to developed markets. Reimbursement rates in the United States have generally supported a favorable return on investment for the purchase of new radiotherapy equipment. While we believe that improved product functionality, greater cost-effectiveness and prospects for better clinical outcomes with new capabilities such as IMRT, IGRT and volumetric modulated arc therapy tend to drive demand for radiotherapy products, large changes in reimbursement rates or reimbursement structure can affect customer demand and cause market shifts. We do not know what impact the Patient Protection and Affordable Care Act (the “Affordable Care Act”) in the United States will have on long-term growth or demand for our products and services. We believe, however, that growth of the radiation oncology market in the United States is being impacted as customers’ decision-making processes are complicated by the uncertainties surrounding the Affordable Care Act and reimbursement rates for radiotherapy and radiosurgery, and that this uncertainty will likely continue into the next fiscal year and result in a high degree of variability of gross orders and revenue from quarter-to-quarter. We also believe that the Affordable Care Act is causing healthcare providers to re-evaluate their business models and we are seeing increased consolidation of hospitals and clinics and more integration of systems and equipment across multi-site healthcare networks, which is impacting transaction size, timing and purchasing processes, and also contributing to the increased business variability. We continued to see signs that the Affordable Care Act is causing decision-makers at treatment centers to sharpen their focus on both clinical efficacy and cost efficiency. In accordance with the Affordable Care Act, in the second quarter of fiscal year 2013, we began to incur the 2.3% excise tax on sales of medical devices (including our Oncology Systems products) in the United States, which has had and may continue to have a negative impact on our gross margin and/or may lead our customers to reduce their orders for our products. In the radiation oncology markets outside of North America, we expect the market growth of our European region (which includes Europe, Russia, the Middle East, India and Africa) will be mixed, with stronger market growth in Eastern Europe, India, and Africa, offset by lower market growth in Southern Europe which is facing severe economic challenges. Our outlook for Asia and the Rest of World remains healthy. In the third quarter of fiscal year 2014, within Asia, we experienced a sharp decline in orders from Japan, which was partially offset by continued growth in orders in China and other countries in Asia, compared to the year-ago period. Overall, we believe the longer-term global radiation oncology market can grow, on average, in the mid-single-digit range.

In the third quarter of fiscal year 2014, Oncology Systems North American gross orders were flat and international gross orders decreased 2%, compared to the year-ago quarter. On a constant currency basis, Oncology Systems international gross orders decreased 4% in the third quarter of fiscal year 2014, compared to the year-ago quarter.

In the third quarter of fiscal year 2014, Oncology Systems revenues increased 3% and gross margin increased by 0.4 percentage points compared to the year-ago quarter.

In the third quarter of fiscal year 2014, we acquired certain assets of Velocity Medical Solutions, LLC (“Velocity”), a privately-held Atlanta-based developer of specialized software for cancer clinics, for a cash consideration of $17 million plus potential contingent consideration upon achievement of certain milestones. The Velocity software aggregates unstructured treatment and imaging data from diverse systems to give a more comprehensive view of a patient's diagnostic imaging and treatment history and help clinicians make more informed treatment decisions.

Imaging Components. Our Imaging Components segment designs, manufactures, sells and services X-ray imaging components for use in a range of applications, including radiographic or fluoroscopic imaging, mammography, specific procedures, computed tomography and industrial applications. We continue to view the long-term fundamental growth driver for this business to be the ongoing success of key X-ray imaging original equipment manufacturers ("OEMs") that incorporate our X-ray tube products and flat panel detectors into their medical diagnostic, dental, veterinary and industrial imaging systems. Our Imaging Components segment also designs, manufactures, sells and services security and inspection products, which include Linatron® x-ray accelerators, imaging processing software and image detection products (including IntellX™) for cargo screening at ports and borders and for non-destructive examination and testing in a variety of applications. Orders and revenues for our security and inspection products have been and may continue to be unpredictable as governmental agencies may place large orders with us or our OEM customers in a short time period, and then may not place any orders for a long time period thereafter.

In the third quarter of fiscal year 2014, Imaging Components revenues increased 2% and gross orders increased 12%, compared to the year-ago quarter. Imaging Components gross margin for the third quarter of fiscal year 2014 increased by 1.2 percentage points compared to the third quarter of fiscal year 2013.

Our success in Imaging Components depends upon our ability to anticipate changes in our markets, the direction of technological innovation and the demands of our customers. We continue to introduce new products which we believe will help contribute to the growth of Imaging Components. In addition, changes in access to diagnostic radiology or the reimbursement rates associated with diagnostic radiology as a result of the Affordable Care Act and similar state proposals, or otherwise, could affect demand for our products in our Imaging Components business.

Other. The "Other" category is comprised of VPT and the operations of the GTC.

VPT develops, designs, manufactures, sells and services products and systems for delivering proton therapy, another form of external beam radiotherapy using proton beams, for the treatment of cancer. Although proton therapy has been in clinical use for more than four decades, it has not been widely deployed due to high capital cost. Our current focus is commercializing our ProBeam™ proton therapy system and bringing our expertise in traditional radiation therapy to proton therapy to improve its clinical utility and to reduce its cost of treatment per patient. Orders and revenues for our VPT products have been and may continue to be subject to significant variability due to the size of each individual transaction, and the timing of each transaction may be impacted by numerous factors, including items outside of our control such as customer project financing.

In the second quarter of fiscal year 2014, we received U.S. Food and Drug Administration ("FDA") 510(k) clearance for our updated ProBeam™ proton therapy system.

GTC, our scientific research facility, develops technologies that enhance our current businesses or may lead to new business areas, including technology to improve radiation therapy and X-ray imaging, as well as other technology for a variety of applications, including security and cargo screening. GTC is also actively engaged in searching for chemical or biological agents that work synergistically with radiation to improve treatment outcomes.

Revenues in our "Other" category increased $1.0 million in the third quarter of fiscal year 2014, compared to the year-ago quarter. Gross orders in our "Other" category increased $56.2 million and $115.2 million, respectively, in the third quarter and first nine months of fiscal year 2014, compared to the respective year-ago periods.

This discussion and analysis of our financial condition and results of operations is based upon and should be read in conjunction with the Condensed Consolidated Financial Statements and the notes included elsewhere in this Quarterly Report on Form 10-Q and the Consolidated Financial Statements and the Notes to the Consolidated Financial Statements and the related Management's Discussion and Analysis of Financial Condition and Results of Operations in our Annual Report on Form 10-K for the fiscal year ended September 27, 2013 (the "2013 Annual Report"), as well as the Risk Factors contained in Part II, Item 1A of this Quarterly Report on Form 10-Q, and other information provided from time to time in our other filings with the SEC.

Critical Accounting Estimates

The preparation of our financial statements and related disclosures in conformity with accounting principles generally accepted in the United States ("GAAP") requires us to make estimates and assumptions that affect the reported amounts of assets, liabilities, revenues and expenses. These estimates and assumptions are based on historical experience and on various other factors that we believe are reasonable under the circumstances. We periodically review our accounting policies, estimates and assumptions and make adjustments when facts and circumstances dictate. In addition to the accounting policies that are more fully described in the Notes to the Consolidated Financial Statements included in our 2013 Annual Report, we consider the critical accounting policies described below to be affected by critical accounting estimates. Our critical accounting policies that are affected by accounting estimates include revenue recognition, share-based compensation expense, valuation of allowance for doubtful accounts, valuation of inventories, assessment of recoverability of goodwill and intangible assets, valuation of warranty obligations,

assessment of loss contingencies, valuation of defined benefit pension and post-retirement benefit plans, valuation of derivative instruments and taxes on earnings. Such accounting policies require us to use judgments, often as a result of the need to make estimates and assumptions regarding matters that are inherently uncertain, and actual results could differ materially from these estimates. For a discussion of how these estimates and other factors may affect our business, see Part II, Item 1A, “Risk Factors.”

Revenue Recognition

Our revenues are derived primarily from the sale of hardware and software products, and services. The Company recognizes its revenues net of any value added or sales tax and net of sales discounts.

We frequently enter into sales arrangements with customers that contain multiple elements or deliverables such as hardware, software and services. Judgments as to the allocation of consideration from an arrangement to the multiple elements of the arrangement, and the appropriate timing of revenue recognition are critical with respect to these arrangements to ensure compliance with GAAP.

The allocation of consideration in a multiple element arrangement is affected by the determination of whether any software deliverables that function together with other hardware components to deliver the hardware products' essential functionality are considered as non-software products for purpose of revenue recognition. The allocation of consideration to each non-software deliverable is based on the assumptions we use to establish its selling price, which are based on vendor-specific objective evidence ("VSOE") of selling price, if it exists, otherwise, third-party evidence of selling price, if it exists, and if not on estimated selling prices. In addition, the allocation of consideration to each software deliverable in a multiple element arrangement is affected by our judgment as to whether VSOE of its fair value exists in these arrangements.

Changes to the elements in an arrangement and the amounts allocated to each element could affect the timing and amount of revenue recognition. Revenue recognition also depends on the timing of shipment, the readiness of customers' facilities for installation or is subject to customer acceptance. If shipments or installations are not made on scheduled timelines or if the products are not accepted by the customer in a timely manner, our reported revenues may differ materially from expectations.

Service revenues include revenues from hardware service contracts, software service agreements, bundled support arrangements, paid services and trainings, and parts that are sold by the service department.

In addition, revenues related to certain highly customized image detection systems, proton therapy systems and proton therapy system commissioning contracts are recognized in accordance with contract accounting. We recognize contract revenues under the percentage-of-completion method which are based on contract costs incurred to date compared with total estimated contract costs. Changes in estimates of total contract revenue, total contract cost or the extent of progress towards completion are recognized in the period in which the changes in estimates are identified. Estimated losses on contracts are recognized in the period in which the loss is identified. In circumstances in which the final outcome of a contract cannot be precisely estimated but a loss on the contract is not expected, we recognize revenues under the percentage-of-completion method based on a zero profit margin until more precise estimates can be made. If and when we can make more precise estimates, revenues and costs of revenues are adjusted in the same period. Because the percentage-of-completion method involves considerable use of estimates in determining revenues, costs and profits and in assigning the dollar amounts to relevant accounting periods, and because the estimates must be periodically reviewed and appropriately adjusted, if our estimates prove to be inaccurate or circumstances change over time, we may be forced to adjust revenues or even record a contract loss in later periods.

Share-based Compensation Expense

We value our stock options granted and the option component of the shares of VMS common stock purchased under the employee stock purchase plan using the Black-Scholes option-pricing model. We value our performance units using the Monte Carlo simulation model. The determination of fair value of share-based payment awards on the date of grant under both the Black-Scholes option-pricing model and the Monte Carlo simulation model is affected by VMS's stock price, as well as the input of other subjective assumptions, including the expected terms of share-based awards and the expected price volatilities of shares of VMS common stock and peer companies that are used to assess certain performance targets over the expected term of the awards, and the dividend yield of VMS.

The expected term of our stock options is based on the observed and expected time to post-vesting exercise and post-vesting cancellations of stock options by our employees. We determine the expected term of stock options based on the demographic grouping of employees and retirement eligibility. We use a combination of historical and implied volatility, or blended volatility, in deriving the expected volatility assumption for our stock options. Blended volatility represents the weighted average of implied volatility and historical volatility. Implied volatility is derived based on traded options on VMS common stock. Implied volatility is weighted in the calculation of blended volatility based on the ratio of the term of the exchange-traded options to the expected terms of the employee stock options. Historical volatility represents the remainder of the weighting. Our decision to incorporate implied volatility was based on our assessment that implied volatility of publicly traded options on VMS common stock is reflective of market conditions and is generally reflective of both historical volatility and expectations of how future volatility will differ from historical volatility. In determining the extent of use of implied volatility, we considered: (i) the volume of market activity of traded options; (ii) the ability to reasonably match the input variables of traded options to those of stock options granted by us, including the date of grant; (iii) the similarity of the exercise prices; and (iv) the length of term of traded options. After considering the above factors, we determined that we could not rely exclusively on implied volatility based on the fact that the term of VMS exchange-traded options is less than one year and that it is different from the expected terms of the stock options we grant. Therefore, we believe a combination of the historical volatility over the expected terms of the stock options we grant and the implied volatility of exchange-traded options best reflects the expected volatility of VMS common stock. In determining the grant date fair value of our performance units, historical volatilities of shares of VMS common stock, as well as the shares of common stock of peer companies, were used to assess certain performance targets. The risk-free interest rate assumption is based upon observed interest rates appropriate for the term of our stock awards. The dividend yield assumption is based on our history and expectation of no dividend payouts. If factors change and we employ different assumptions in future periods, the compensation expense that we record may differ significantly from what we have recorded in the current period. In addition, we are required to estimate the expected forfeiture rate, as well as the probability that certain performance conditions that affect the vesting of performance units will be achieved, and recognize expense only for those awards expected to vest. If the actual forfeiture rate and/or the actual number of performance units that vest based on achievement of performance conditions are materially different from our estimates, the share-based compensation expense could be significantly different from what we have recorded in the current period.

Allowance for Doubtful Accounts

We evaluate the creditworthiness of our customers prior to authorizing shipment for all major sale transactions. Except for government tenders, group purchases and orders with letters of credit in Oncology Systems and for our security and inspection products, and orders for our X-ray tubes and X-ray panel products, our payment terms usually require payment of a small portion of the total amount due when the customer signs the purchase order, a significant amount upon transfer of risk of loss to the customer and the remaining amount upon completion of the installation. On a quarterly basis, we evaluate aged items in the accounts receivable aging report and provide an allowance in an amount we deem adequate for doubtful accounts. If our evaluation of our customers' financial conditions does not reflect our future ability to collect outstanding receivables, additional provisions may be needed and our operating results could be negatively affected.

Inventories

Our inventories include high technology parts and components that are highly specialized in nature and that are subject to rapid technological obsolescence. We have programs to minimize the required inventories on hand and we regularly review inventory quantities on hand and on order and adjust for excess and obsolete inventory based primarily on historical usage rates and our estimates of product demand and production. Actual demand may differ from our estimates, in which case we may have understated or overstated the provision required for obsolete and excess inventory, which would have an impact on our operating results.

Goodwill and Intangible Assets

Goodwill is initially recorded when the purchase price paid for a business acquisition exceeds the estimated fair value of the net identified tangible and intangible assets acquired. The majority of businesses that we have acquired have not had significant identified tangible assets and, as a result, we have typically allocated a significant portion of the purchase price to intangible assets and goodwill. Our future operating performance will be impacted by the future amortization of these acquired intangible assets and potential impairment charges related to these intangibles or to goodwill if indicators of impairment exist. The allocation of the purchase price from business acquisitions to goodwill and intangible assets could have a significant impact on our future operating results. In addition, the allocation of the purchase price of the acquired businesses to goodwill and intangible assets requires us to make significant estimates and assumptions, including estimates of future cash flows expected to be generated by the acquired assets and the appropriate discount rate for those cash flows. Should conditions differ from management’s estimates at the time of the acquisition, material write-downs of intangible assets and/or goodwill may be required, which would adversely affect our operating results.

We evaluate goodwill for impairment at least annually or whenever an event occurs or circumstances change that would more likely than not reduce the fair value of a reporting unit below its carrying amount. If we determine that a quantitative analysis is necessary, the impairment test for goodwill is a two-step process. Step one consists of a comparison of the fair value of a reporting unit against its carrying amount, including the goodwill allocated to each reporting unit. We determine the fair value of our reporting units based on a combination of income and market approaches. The income approach is based on the present value of estimated future cash flows of the reporting units and the market approach is based on a market multiple calculated for each business unit based on market data of other companies engaged in similar business. If the carrying amount of the reporting unit is in excess of its fair value, step two requires the comparison of the implied fair value of the reporting unit's goodwill against the carrying amount of the reporting unit's goodwill. Any excess of the carrying value of the reporting unit's goodwill over the implied fair value of the reporting unit's goodwill is recorded as an impairment loss. The impairment test for intangible assets with indefinite useful lives, if any, consists of a comparison of fair value to carrying value, with any excess of carrying value over fair value being recorded as an impairment loss.

Based on the most recent annual goodwill impairment testing that we performed in fiscal year 2013 for each of our four reporting units with goodwill, (i) Oncology Systems, (ii) X-ray tubes and panel products (formerly "X-Ray Products"), (iii) Security and inspection products, and (iv) VPT, the fair value of each such reporting unit was substantially in excess of its carrying value. However, significant changes in our projections about our operating results or other factors could cause us to make interim assessments of impairments in any quarter that could result in some or all of the goodwill being impaired. For our VPT business in particular, which had $60.5 million in goodwill as of June 27, 2014, our estimates as to future operating results include certain assumptions about factors that cannot be predicted with certainty, including future market conditions, revenue growth rates, and operating margins.

We will continue to make assessments of impairment on an annual basis or more frequently if indicators of potential impairment arise.

Warranty Obligations

We warrant most of our products for a specific period of time, usually 12 months from installation, against material defects. We provide for the estimated future costs of warranty obligations in cost of revenues when the related revenues are recognized. The accrued warranty costs represent our best estimate at the time of sale of the total costs that we will incur to repair or replace product parts that fail while still under warranty. The amount of accrued estimated warranty costs obligation for established products is primarily based on historical experience as to product failures adjusted for current information on repair costs. For new products, estimates will include historical experience of similar products, as well as reasonable allowance for start-up expenses. Actual warranty costs could differ from the estimated amounts. On a quarterly basis, we review the accrued balances of our warranty obligations and update the historical warranty cost trends, if required. If we were required to accrue additional warranty costs in the future, it would have a negative effect on our operating results.

Loss Contingencies

From time to time, we are a party to or otherwise involved in legal proceedings, claims and government inspections or investigations or other legal matters, both inside and outside the United States, arising in the ordinary course of our business or otherwise. We accrue amounts, to the extent they can be reasonably estimated, that we believe are adequate to address any liabilities related to legal proceedings and other loss contingencies that we believe will result in a probable loss. Such matters are subject to many uncertainties, outcomes are not predictable with assurance, and actual liabilities could significantly exceed out estimates of potential liabilities. For example, in the University of Pittsburgh patent infringement case, as of December 27, 2013 we were subject to a court judgment that could have resulted in the Company incurring up to approximately $102 million in damages, including prejudgment interest, plus

an ongoing royalty for sales after the date of judgment. While we appealed the findings against us, this appeal was subject to uncertainties. As of December 27, 2013, we had accrued an aggregate of approximately $5 million for the low end of the range of the probable settlement value for the University of Pittsburgh matter. In January 2014, we entered into a settlement agreement with the University of Pittsburgh that was dependent upon the appellate ruling, which was issued in April 2014. Based on the appellate court opinion and the terms of the settlement agreement, we paid approximately $35.6 million in full settlement of the lawsuit to the University of Pittsburgh in the third fiscal quarter of 2014, $25.1 million of which was accrued in the second quarter of fiscal year 2014 and the remaining $5.5 million of which was recorded in the third quarter of fiscal year 2014 as prepaid royalties and is being amortized over the remaining life of the patent of approximately two and half years.

In addition, we are subject to a variety of environmental laws around the world. Those laws regulate multiple aspects of our operations, including the handling, storage, transport and disposal of hazardous substances. They impose costs on our operations. In connection with our past and present operations and facilities, we record environmental remediation liabilities when we conclude that environmental assessments or remediation efforts are probable and we believe we can reasonably estimate the costs of those efforts. Our accrued environmental costs represent our best estimate of the total costs of assessments and remediation and the time period over which we expect to incur those costs. We review these accrued balances quarterly. If we were required to increase or decrease the accrued environmental costs in the future, it would adversely or favorably impact our operating results.

Defined Benefit Pension and Post-Retirement Benefit Plans

We sponsor five defined benefit pension plans in Germany (where we have two defined benefit pension plans), Japan, Switzerland and the United Kingdom covering employees who meet the applicable eligibility requirements in these countries. Although we do not have any defined benefit pension plans in the United States, we sponsor a post-retirement benefit plan that provides healthcare benefits to certain eligible retirees. Several statistical and other factors that attempt to anticipate future events are used in calculating the expenses and liabilities related to those plans for which the benefits are actuarially determined, such as our defined benefit pension and post-retirement benefit plans. These factors include assumptions about the discount rate, expected return on plan assets, rate of future compensation increases and rate of healthcare cost increases, all of which we determine within certain guidelines. In addition, we also use assumptions, such as withdrawal and mortality rates, to calculate the expenses and liabilities. The actuarial assumptions we use are long-term assumptions and may differ materially from actual experience particularly in the short term due to changing market and economic conditions and changing participant demographics. These differences may have a significant impact on the amount of defined benefit pension and post-retirement benefit plan expenses we record.

The expected rates of return on the various defined benefit pension plans' assets are based on the asset allocation of each plan and the long-term projected return on those assets. The discount rate enables us to state expected future cash flows at a present value on the measurement date. The discount rates used for defined benefit plans in all countries are based primarily on the yields of a universe of high quality corporate bonds in each applicable country or the spot rate of high quality AA-rated corporate bonds, with durations corresponding to the expected durations of the benefit obligations. A change in the discount rate will cause the present value of benefit obligations to change in the opposite direction.

Valuation of Derivative Instruments

We use foreign currency forward contracts to reduce the effects of currency rate fluctuations on sales transactions denominated in foreign currencies and on assets and liabilities denominated in foreign currencies. These foreign currency forward contracts are derivative instruments and are measured at fair value. There are three levels of inputs that may be used to measure fair value (see Note 3, "Fair Value" of the Notes to the Condensed Consolidated Financial Statements). Each level of input has different levels of subjectivity and difficulty involved in determining fair value. The fair value of foreign currency forward contracts are calculated primarily using Level 2 inputs, which include currency spot and forward rates, interest rate and credit or non-performance risk. The spot rate for each currency is the same spot rate used for all balance sheet translations at the measurement date and sourced from our major trading banks. The forward point values for each currency and the London Interbank Offered Rate ("LIBOR") to discount assets and liabilities are interpolated from commonly quoted broker services. One year credit default swap spreads of the counterparty at the measurement date are used to adjust derivative assets, all of which mature in 13 months or less, for non-performance risk. We are required to adjust derivative liabilities to reflect the potential non-performance risk to lenders based on our incremental borrowing rate. Each contract is individually adjusted using the counterparty credit default swap rates (for net assets) or our borrowing rate (for net liabilities). The use of Level 2 inputs in determining fair values requires certain management judgment and subjectivity. Changes to these Level 2 inputs could have a material impact on the valuation of our derivative instruments, as well as on our result of operations. There were no transfers of assets or liabilities between fair value measurement levels during the first nine months of fiscal years 2014 and 2013.

Taxes on Earnings

We are subject to taxes on earnings in both the United States and numerous foreign jurisdictions. As a global taxpayer, significant judgments and estimates are required in evaluating our tax positions and determining our provision for

taxes on earnings.

The accounting for uncertainty in income taxes requires a two-step approach to recognizing, derecognizing and measuring uncertain tax positions. The first step is to evaluate the tax position for recognition by determining whether the weight of available evidence indicates that it is more likely than not that, based on the technical merits, the position will be sustained on audit, including resolution of related appeals or litigation processes, if any. The second step is to measure the tax benefit as the largest amount that is more than 50% likely of being realized upon settlement. Recognition, derecognition and measurement are based on management's best judgment given the facts, circumstances and information available at the end of the accounting period. A tax benefit should be recognized in the first period in which it meets the more likely than not recognition threshold, and conversely, a tax benefit previously recognized should be derecognized in the first period in which new information results in a change in judgment in which the position fails to meet the recognition threshold. A benefit not previously recognized would be recognized when the tax position is effectively settled through examination, negotiation or litigation with tax authorities, or when the statute of limitations for the relevant taxing authority to examine and challenge the position has expired. Our policy is to include interest and penalties related to unrecognized tax benefits within the provision for taxes on earnings.

Generally, the carrying value of our net deferred tax assets assumes that we will be able to generate sufficient future taxable earnings in the applicable tax jurisdictions to utilize these deferred tax assets. Should we conclude it is more likely than not that we will be unable to recover our net deferred tax assets in these tax jurisdictions, we would increase our valuation allowance and our tax provision would increase in the period in which we make such a determination.

Our foreign earnings are generally taxed at rates lower than U.S. rates. Our effective tax rate is impacted by existing tax laws in both the United States and in the respective countries in which our foreign subsidiaries do business. In addition, a decrease in the percentage of our total earnings from our foreign countries, or a change in the mix of foreign countries among particular tax jurisdictions could increase or decrease our effective tax rate. Our current effective tax rate does not assume U.S. taxes on certain undistributed profits of certain foreign subsidiaries. These earnings could become subject to incremental foreign withholding or U.S. federal and state taxes should they either be deemed or actually remitted to the United States.

Results of Operations

Fiscal Year

Our fiscal year is the 52- or 53-week period ending on the Friday nearest September 30. Fiscal year 2014 is a 52-week period ending September 26, 2014, and fiscal year 2013 was a 52-week period ended September 27, 2013. The fiscal quarters ended June 27, 2014 and June 28, 2013 were both 13-week periods.

Discussion of Results of Operations for the Third Quarter and First Nine Months of Fiscal year 2014 Compared to the Third Quarter and First Nine Months of Fiscal year 2013

Total Revenues

Revenues by sales classification	Three Months Ended			Nine Months Ended		
(Dollars in millions)	June 27, 2014	June 28, 2013	Percent Change	June 27, 2014	June 28, 2013	Percent Change
Product	$505.6	$503.6	0 %	$1,529.0	$1,518.1	1 %
Service [1]	242.1	222.6	9 %	708.7	654.9	8 %
Total Revenues	$747.7	$726.2	3 %	$2,237.7	$2,173.0	3 %
Product as a percentage of total revenues	68 %	69 %		68 %	70 %	
Service as a percentage of total revenues	32 %	31 %		32 %	30 %	

Revenues by region

North America	$358.1	$309.5	16 %	$943.7	$914.0	3 %
Europe	219.1	223.6	(2 %)	668.3	657.2	2 %
Asia	146.0	159.5	(9 %)	543.2	509.5	7 %
Rest of World	24.5	33.6	(27 %)	82.5	92.3	(11 %)
Total International [2]	389.6	416.7	(7 %)	1,294.0	1,259.0	3 %
Total	$747.7	$726.2	3 %	$2,237.7	$2,173.0	3 %

North America as a percentage of total revenues	48	%	43	%	42	%	42	%
International as a percentage of total revenues	52	%	57	%	58	%	58	%

(1) Service revenues include revenues from parts sold by the service department.
(2) We consider international revenues to be revenues outside of North America.

Total revenues increased in the third quarter of fiscal year 2014, compared to the year-ago period due to an increase in revenues in Oncology Systems and to a lesser extent increases in revenues in Imaging Components and the “Other” category.

Total revenues increased in the first nine months of fiscal year 2014, compared to the year-ago period due to increases in revenues in Oncology Systems and Imaging Components, partially offset by a decrease in revenues in the “Other” category.

A small increase in product revenues from Imaging Components was almost fully offset by a small decrease in product revenues from Oncology Systems during the third quarter of fiscal year 2014, compared to the year-ago period.

Product revenues increased slightly in the first nine months of fiscal year 2014, compared to the year-ago period, due to an increase in revenues in Imaging Components and to a lesser extent an increase in revenues in Oncology Systems, partially offset by a decrease in revenues in the “Other” category.

Service revenues increased in the third quarter and the first nine months of fiscal year 2014, compared to the respective year-ago periods, primarily due to an increase in service revenues from Oncology Systems, and to a lesser extent, increases in Imaging Components and the “Other” category.

North American revenues increased in the third quarter of fiscal year 2014, compared to the year-ago period, primarily due to increases in revenues in Oncology Systems and Imaging Components. North American revenues increased in the first nine months of fiscal year 2014, compared to the year-ago period, primarily due to an increase in revenues in Oncology Systems, slightly offset by decreases in revenues from Imaging Components and the “Other” category.

International revenues decreased in the third quarter of fiscal year 2014, compared to the year-ago period, due to a decrease in revenues from Oncology Systems, and a slight decrease in revenues from Imaging Components, partially offset by a slight increase in revenues from the “Other” category. International revenues increased in the first nine months of fiscal year 2014, compared to the respective year-ago period, primarily due to increases in revenues in Oncology Systems and Imaging Components, partially offset by a decrease in revenues in the “Other” category.

The U.S. Dollar was weaker against the Euro and stronger against the Japanese Yen in the third quarter and the first nine months of fiscal year 2014, compared to the respective year-ago periods. On a constant currency basis, international revenues decreased 8% during the third quarter and increased 4% during the first nine months of fiscal year 2014, compared to the respective year-ago periods.

Oncology Systems Revenues

Revenues by sales classification	Three Months Ended			Nine Months Ended		
(Dollars in millions)	June 27, 2014	June 28, 2013	Percent Change	June 27, 2014	June 28, 2013	Percent Change
Product	$343.7	$345.2	0 %	$1,035.1	$1,028.9	1 %
Service	234.5	216.1	9 %	687.6	638.5	8 %
Total Oncology Systems revenues	$578.2	$561.3	3 %	$1,722.7	$1,667.4	3 %
Product as a percentage of Oncology Systems revenues	59 %	62 %		60 %	62 %	
Service as a percentage of Oncology Systems revenues	41 %	38 %		40 %	38 %	
Oncology Systems revenues as a percentage of total revenues	77 %	77 %		77 %	77 %	

Oncology Systems product revenues were flat in the third quarter and increased slightly in the first nine months of fiscal year 2014, compared to the respective year-ago periods. The increase in revenues from hardware products was offset by a decrease in revenues from certain software licenses during the third quarter of fiscal year 2014, compared to the year-ago period. The slight increase in product revenues in the first nine months of fiscal year 2014 was primarily due to an increase in revenues from high energy linear accelerators, partially offset by a decrease in revenues from certain software licenses, compared to the year-ago period. Revenues from TrueBeam as a percentage of revenues from hardware products increased during the third quarter and first nine months of fiscal year 2014, compared to the respective year-ago periods. Oncology Systems service revenues increased in the third quarter and the first nine months of fiscal year 2014, compared to the respective year-ago periods, primarily due to increased customer adoption of service contracts as the warranty period on our TrueBeam systems expire and by an increased number of customers as the installed base of our products continues to grow.

Revenues by region	Three Months Ended			Nine Months Ended		
(Dollars in millions)	June 27, 2014	June 28, 2013	Percent Change	June 27, 2014	June 28, 2013	Percent Change
North America	$309.0	$264.4	17 %	$796.9	$763.7	4 %
Europe	163.8	169.2	(3 %)	511.2	502.2	2 %
Asia	82.4	95.4	(14 %)	336.8	313.6	7 %
Rest of World	23.0	32.3	(29 %)	77.8	87.9	(12 %)
Total International	269.2	296.9	(9 %)	925.8	903.7	2 %
Total Oncology Systems revenues	$578.2	$561.3	3 %	$1,722.7	$1,667.4	3 %
North America as a percentage of Oncology Systems revenues	53 %	47 %		46 %	46 %	
International as a percentage of Oncology Systems revenues	47 %	53 %		54 %	54 %	

North American Oncology Systems revenues increased in the third quarter of fiscal year 2014 and first nine months of fiscal year 2014, compared to the respective year-ago periods, due to increases in revenues from hardware products, services, and software licenses.

International Oncology Systems revenues decreased in the third quarter of fiscal year 2014, compared to the year-ago period, due to decreases in revenues from Asia, the Rest of World region, and Europe. The decrease in revenues in Asia in the third quarter of fiscal year 2014, compared to the year-ago period, was due to decreases in revenues from certain hardware products including high energy linear accelerators, and software licenses, partially offset by increases in revenues in services and low energy linear accelerators. The decrease in revenues in the Rest of World region in the third quarter of fiscal year 2014, compared to the year-ago period, was primarily due to a decrease in revenues from hardware products, partially offset by an increase in revenues from services. The decrease in revenues in Europe in the third quarter of fiscal year 2014, compared to the year-ago period, was due to decreases in revenues from hardware products and software licenses, partially offset by an increase in revenues from services. Within revenues from hardware products, revenues from high energy linear accelerators in Europe increased during the third quarter of the fiscal year 2014, compared to the year-ago period.

International Oncology Systems revenues increased in the first nine months of fiscal year 2014, compared to the year-ago period, due to an increase in revenues from Asia and to a lesser extent an increase in revenues from Europe, partially offset by a decrease in revenues from the Rest of World region. The increase in revenues from Asia in the first nine months of fiscal year 2014, compared to the year-ago period, was primarily due to increases in revenues from hardware products and services. The increase in revenues from Europe in the first nine months of fiscal year 2014, compared to the year-ago period was primarily due to an increase in revenues from services and high energy linear accelerators, partially offset by decreases in revenues from other hardware products and certain software licenses. The decrease in revenues from the Rest of World region in the first nine months of fiscal year 2014, compared to the year-ago period, was primarily due to decreases in revenues from hardware products.

The U.S. Dollar was weaker against the Euro and stronger against the Japanese Yen in the third quarter and the first nine months of fiscal year 2014, compared to the respective year-ago periods. The combined impact of the currency exchange rates had a positive impact on the revenues of Oncology Systems during the third quarter and a negative impact on the revenues of Oncology Systems during the first nine months of the fiscal year 2014.

Varying cycles of higher and lower revenues between the North American and international regions are impacted by regional influences, which recently have included government economic stimulus programs, the recession and the pace of economic recovery, the European sovereign debt crisis, uncertainty created by healthcare reform (such as the excise tax on the sale of most medical devices, Medicare reimbursement rates and consolidation of free standing clinics in the United States), and different technology adoption cycles that are consistent with the gross order patterns. See further discussion of orders under “Gross Orders.”

Imaging Components Revenues

Revenues by sales classification	Three Months Ended			Nine Months Ended		
(Dollars in millions)	June 27, 2014	June 28, 2013	Percent Change	June 27, 2014	June 28, 2013	Percent Change
Product	$155.3	$151.8	2 %	$474.5	$459.3	3 %
Service	6.5	6.4	1 %	17.5	15.3	15 %
Total Imaging Components revenues	$161.8	$158.2	2 %	$492.0	$474.6	4 %
Product as a percentage of Imaging Components revenues	96 %	96 %		96 %	97 %	
Service as a percentage of Imaging Components revenues	4 %	4 %		4 %	3 %	
Imaging Components revenues as a percentage of total revenues	22 %	22 %		22 %	22 %	

Imaging Components revenues increased in the third quarter and the first nine months of fiscal year 2014, compared to the respective year-ago periods, due to an increase in revenues from products and to a lesser extent an increase in revenues from services. Imaging Components product revenues increased in the third quarter of fiscal year 2014, compared to the year-ago period, primarily due to an increase in revenues from X-ray flat panel products and security and inspection products, partially offset by a decrease in revenues from X-ray tube products, as customers delayed purchases due to longer tube life resulting from improvements in our X-ray tubes. Imaging Components product revenues increased in the first nine months of fiscal year 2014, compared to the year-ago period, primarily due to an increase in revenues from X-ray flat panel products, partially offset by a decrease in revenues from security and

inspection products and to a lesser extent a decrease in revenues from X-ray tube products.

Revenues by region	Three Months Ended			Nine Months Ended		
(Dollars in millions)	June 27, 2014	June 28, 2013	Percent Change	June 27, 2014	June 28, 2013	Percent Change
North America	$46.7	$42.5	10 %	$140.5	$141.7	(1 %)
Europe	50.1	50.4	0 %	140.4	132.7	6 %
Asia	63.6	64.1	(1 %)	206.4	195.9	5 %
Rest of World	1.4	1.2	17 %	4.7	4.3	9 %
Total International	115.1	115.7	(1 %)	351.5	332.9	6 %
Total Imaging Components Revenues	$161.8	$158.2	2 %	$492.0	$474.6	4 %
North America as a percentage of Imaging Components revenues	29 %	27 %		29 %	30 %	
International as a percentage of Imaging Components revenues	71 %	73 %		71 %	70 %	

Imaging Components revenues increased in the third quarter of fiscal year 2014, compared to the year-ago period, primarily due to an increase in revenues in North America. North American Imaging Components revenues increased in the third quarter of fiscal year 2014, compared to the year-ago period, due to increases in X-ray flat panel products and security and inspection products. In Asia, the decrease in revenues from X-ray tube products was almost completely offset by an increase in revenues from X-ray flat panel products in the third quarter of fiscal year 2014, compared to the year-ago period. Imaging Components revenues in Europe and the rest of world region were relatively flat in the third quarter of fiscal year 2014, compared to the year-ago period.

Imaging Components revenues increased in the first nine months of fiscal year 2014, compared to the year-ago period, due to increases in revenues from Asia and Europe, partially offset by a decrease in revenues from North America. Imaging Components revenues increased in Asia during the first nine months of fiscal year 2014, compared to the year-ago period, primarily due to an increase in revenues from X-ray flat panel products and to a lesser extent an increase in security and inspection products, partially offset by a decrease in revenues from X-ray tube products. Imaging Components revenues increased in Europe in the first nine months of fiscal year 2014, compared to the year-ago period, primarily due an increase in revenues from X-ray tube products and to a lesser extent an increase in X-ray flat panel products, partially offset by a decrease in revenues from security and inspection products. Imaging Components revenues decreased in North America in the first nine months of fiscal year 2014, compared to the year-ago period, primarily due to a decrease in revenues from security and inspection products, partially offset by an increase in revenues in X-ray flat panel products.

The difference in currency exchange rates between the U.S. Dollar and foreign currencies in the third quarter and the first nine months of fiscal year 2014, compared to the respective year-ago periods, did not have a material impact on Imaging Components international revenues because sales transactions in Imaging Components are primarily denominated in U.S. Dollars.

Other Revenues

Revenues by sales classification	Three Months Ended			Nine Months Ended		
(Dollars in millions)	June 27, 2014	June 28, 2013	Percent Change	June 27, 2014	June 28, 2013	Percent Change
Product	$6.6	$6.6	0 %	$19.4	$29.9	(35 %)
Service	1.1	0.1	n/m	3.6	1.1	225 %
Total Other revenues	$7.7	$6.7	15 %	$23.0	$31.0	(26 %)
Other revenues as a percentage of total revenues	1 %	1 %		1 %	1 %	

n/m = not meaningful

Revenues in our “Other” category, which is comprised of VPT and GTC, increased slightly in the third quarter of fiscal year 2014, compared to the year-ago period primarily due to an increase in VPT service revenues. Revenues from the “Other” category decreased in the first nine months of fiscal year 2014, compared to the year-ago, period primarily due to a decrease in VPT product revenues, partially offset by an increase in VPT service revenues. VPT product revenues decreased in the first nine months of fiscal year 2014, compared to the year-ago period, primarily due to the timing of commencement of revenue recognition relating to two proton therapy projects in the first nine months of fiscal year 2013. The increase in the service revenues in the “Other” category during the first nine months of fiscal year 2014, compared to the year-ago period, was primarily due to commencement of services for Scripps Proton Therapy Center in the first three months of fiscal year 2014.

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Gross Margin

(Dollars in millions)	Three Months Ended June 27, 2014	June 28, 2013	Percent Change	Nine Months Ended June 27, 2014	June 28, 2013	Percent Change
Dollars by segment						
Oncology Systems	$255.0	$245.4	4 %	$756.2	$724.5	4 %
Imaging Components	68.3	64.8	5 %	205.1	196.4	4 %
Other	0.4	0.3	17 %	0.3	0.3	-
Gross margin	$323.7	$310.5	4 %	$961.6	$921.2	4 %
Percentage by segment						
Oncology Systems	44.1 %	43.7 %		43.9 %	43.5 %	
Imaging Components	42.2 %	41.0 %		41.7 %	41.4 %	
Total Company	43.3 %	42.8 %		43.0 %	42.4 %	

Gross margin percentage increased in the third quarter and the first nine months of fiscal year 2014 compared to the year-ago periods due to increases in Imaging Components and Oncology Systems gross margin percentages.

The dollar amount of Oncology Systems gross margin increased in the third quarter and the first nine months of fiscal year 2014, as compared to the respective year-ago periods, due to an increase in service volume, and to a lesser extent, an increase in product volume in the first nine months ended of fiscal year 2014, as compared to the year-ago period.

Oncology Systems products gross margin percentage for the third quarter of fiscal year 2014, remained flat at 36.2% compared to the year-ago period. Oncology Systems service gross margin was 55.7% for the third quarter of fiscal year 2014, compared to 55.8% for the year-ago period. Oncology Systems product gross margin percentage for the first nine months of fiscal year 2014, was 36.3% compared to 35.8% for the year-ago period. The increase in Oncology Systems products gross margin for the first nine months of fiscal year 2014, as compared to the year-ago period was due to improved quality costs. Oncology Systems service gross margin percentage for the first nine months of fiscal year 2014, was 55.3% compared to 55.8% for the year-ago period. The decrease in the Oncology Systems service gross margin was primarily due to an unfavorable geographic mix.

We believe the shift of Oncology Systems revenues towards international markets will generally continue and may negatively impact Oncology Systems gross margins.

Imaging Components gross margin percentage increased for the third quarter and first nine months of fiscal year 2014, compared to the respective year-ago periods, primarily due to increases in gross margin percentages in X-ray tube products, partially offset by decreases in gross margin percentages from X-ray flat panel products and security and inspection products. The increases in gross margin percentages in X-ray tube products during the third quarter and first nine months of fiscal year 2014 were primarily due to improved quality costs. The decreases in gross margin percentages in X-ray flat panel products during the third quarter and first nine months of fiscal year 2014 were primarily due to increased pricing pressures. The decreases in gross margin percentages in our security and inspection products during the third quarter and first nine months of fiscal year 2014, compared to the respective year-ago periods were due to customer pricing pressures and an unfavorable product mix.

Research and Development

	Three Months Ended			Nine Months Ended		
(Dollars in millions)	June 27, 2014	June 28, 2013	Percent Change	June 27, 2014	June 28, 2013	Percent Change
Research and development	$57.0	$53.4	7 %	$175.7	$151.4	16 %
As a percentage of total revenues	8 %	7 %		8 %	7 %	

The $3.6 million increase in research and development expenses in the third quarter of fiscal year 2014, compared to the year-ago period, was due to increases in expenses of $3.4 million in Oncology Systems and $0.9 million in Imaging Components, partially offset by a decrease in expenses of $0.6 million in the "Other" category. The $3.4 million increase in expenses in Oncology Systems was due to expenses relating to new product development projects and the enhancement of existing products and an unfavorable currency impact when foreign-currency-denominated research and development expenses for Oncology Systems were translated into U.S. Dollars. The $0.9 million increase in expenses in Imaging Components was due to new product development projects and enhancement of existing X-ray tube and flat panel products, partially offset by a decrease in expenses in security and inspection products. The $0.6 million decrease in expenses in the "Other" category was due to completion of certain research and development projects, partially offset by an unfavorable currency impact when foreign-currency-denominated research and development expenses for VPT were translated into U.S. Dollars.

The $24.3 million increase in research and development expenses in the first nine months of fiscal year 2014, compared to the year-ago period was due to an increase in expenses of $17.5 million in Oncology Systems, $4.5 million in the "Other" category, and $2.3 million in Imaging Components. The $17.5 million increase in expenses in Oncology Systems was due to expenses relating to new product development projects and enhancement of existing products, and an unfavorable currency impact when foreign-currency-denominated research and development expenses for Oncology Systems were translated into U.S. Dollars. The $4.5 million increase in the "Other" category was due to expenses relating to new product development projects, a net increase in costs associated with increased headcount to support our growing engineering activities in VPT, and an unfavorable currency impact when foreign-currency-denominated research and development expenses for VPT were translated into U.S. Dollars, partially offset by a decrease in expenses due to completion of certain research and development projects. The $2.3 million increase in expenses in Imaging Components was due to new product development projects and enhancement of existing X-ray tube and flat panel products, partially offset by a decrease in research and development expenses relating to security and inspection products.

Selling, General and Administrative, and Litigation Settlement

	Three Months Ended			Nine Months Ended		
(Dollars in millions)	June 27, 2014	June 28, 2013	Percent Change	June 27, 2014	June 28, 2013	Percent Change
Selling, general and administrative	$124.2	$102.4	21 %	$348.8	$321.9	8 %
Litigation settlement	$-	$-	-	$25.1	$-	-
Selling, General and Administrative as a percentage of total revenues	17 %	14 %		16 %	15 %	
Litigation Settlement as a percentage of total revenues	-	-		1 %	-	

The $21.8 million increase in selling, general and administrative expenses for the third quarter of fiscal year 2014, compared to the year-ago period was primarily attributable to: a $11.3 million net increase in employee-related costs (including share-based compensation) due to an increase in headcount to support our growing business activities; a $7.7 million impairment charge of a portion of our privately-held equity investment in Augmenix (including a $1.4 million write-off of the option to purchase the remaining equity interest of Augmenix, upon its expiry); a $2.3 million decrease in gain recognized on our equity investment in dpiX Holding LLC; a $2.6 million increase in fees primarily due to the timing of certain international commission arrangements; and a $1.6 million unfavorable currency impact when foreign-currency-denominated selling, general and administrative expenses were translated into U.S. Dollars. These increases were partially offset by a $2.5 million decrease in legal expenses and a $0.7 million decrease in bad debt expense.

The $26.9 million increase in selling, general and administrative expenses for the first nine months of fiscal year 2014, compared to the year-ago period was primarily attributable to: a $21.7 million net increase in employee-related costs (excluding share-based compensation) due to an increase in headcount to support our growing business activities; a $7.7 million impairment charge of a portion of our privately-held equity investment in Augmenix (including a $1.4 million write-off of the option to purchase the remaining equity interest of Augmenix, upon its expiry); a $2.7 million unfavorable currency impact when foreign-currency-denominated selling, general and administrative expenses were translated into U.S. Dollars; a $2.9 million increase in software and hardware maintenance expense; and a $2.4 million decrease in gain recognized on our equity investment in dpiX Holding LLC. These increases were partially offset by a $6.7 million decrease in employee-related restructuring costs due to the enhanced retirement program offered to employees in the first half of fiscal year 2013; a $3.3 million decrease in share-based compensation expense due to timing of the grants awarded; and a $1.5 million decrease in legal expenses.

In the second quarter of fiscal year 2014, we recorded a litigation settlement charge of $25.1 million as a result of settlement of patent litigation with University of Pittsburgh (see Note 9 “Commitments and Contingencies” in our Notes to the Condensed Consolidated Financial Statements for additional information).

Interest Income (Expense), Net

	Three Months Ended			Nine Months Ended		
(Dollars in millions)	June 27, 2014	June 28, 2013	Percent Change	June 27, 2014	June 28, 2013	Percent Change
Interest income, net	$1.2	$1.0	21 %	$2.2	$2.4	(7 %)

Interest income, net of interest expense, increased in the third quarter of fiscal year 2014, compared to the year-ago period primarily due higher interest income generated from our loan to California Proton Treatment Center, LLC ("CPTC"), partially offset by a higher interest expense associated with increased borrowings from our credit facilities. Interest income, net of interest expense, decreased in the first nine months of fiscal year 2014, compared to the year-ago period primarily due to a higher interest expense associated with increased borrowings from our credit facilities, partially offset by higher interest income generated from our loan to CPTC.

Taxes on Earnings

	Three Months Ended			Nine Months Ended		
	June 27, 2014	June 28, 2013	Percent Change	June 27, 2014	June 28, 2013	Percent Change
Effective tax rate	25.5%	27.6%	(2.1 %)	28.1%	28.7%	(0.6 %)

The decrease in our effective tax rate in the third quarter of fiscal year 2014, compared to the year-ago period, was primarily due to a larger net benefit for discrete items in the current period, which is primarily related to the release of certain liabilities for uncertain tax positions due to the expiration of the statutes of limitation in various jurisdictions. The decrease in our effective tax rate in the first nine months of fiscal year 2014, compared to the year-ago period, was primarily due to favorable shift in the mix of geographic earnings.

Our effective tax rate is impacted by the percentage of our total earnings that come from our international region, the mix of particular tax jurisdictions within our international region, changes in the valuation of our deferred tax assets or liabilities, and changes in tax laws or interpretations of those laws. We also expect that our effective tax rate may experience increased fluctuation from period to period. See Note 13, "Taxes on Earnings" of the Notes to the Consolidated Financial Statements in our 2013 Annual Report.

Net Earnings Per Diluted Share

	Three Months Ended			Nine Months Ended		
	June 27, 2014	June 28, 2013	Percent Change	June 27, 2014	June 28, 2013	Percent Change
Net earnings per diluted share	$1.02	$1.03	(1 %)	$2.81	$2.90	(3 %)

The decreases in earnings per diluted share in the third quarter and the first nine months of fiscal year 2014, compared to the respective year-ago periods, were due to increases in operating expenses, partially offset by increases in revenues, gross margin, a decrease in the effective tax rate, and a reduction in the number of diluted shares of common

stock outstanding due to stock repurchases.

Gross Orders

Total Gross Orders (by segment and region)	Three Months Ended			Nine Months Ended		
(Dollars in millions)	June 27, 2014	June 28, 2013	Percent Change	June 27, 2014	June 28, 2013	Percent Change
Oncology Systems:						
North America	$285.8	$285.3	0 %	$800.3	$763.6	5 %
Total International	334.6	341.9	(2 %)	966.4	949.3	2 %
Total Oncology Systems	$620.4	$627.2	(1 %)	$1,766.7	$1,712.9	3 %
Imaging Components:						
North America	$51.9	$45.9	13 %	$135.1	$122.7	10 %
Total International	110.4	98.7	12 %	353.6	344.2	3 %
Total Imaging Components	$162.3	$144.6	12 %	$488.7	$466.9	5 %
Other:	$57.5	$1.3	n/m	$117.9	$2.7	n/m
Total Gross Orders:	$840.2	$773.1	9 %	$2,373.3	$2,182.5	9 %

n/m = not meaningful

Beginning in the fourth quarter of fiscal 2013, we changed the presentation of reported orders from net orders to gross orders.

Gross orders are defined as the sum of new orders recorded during the period adjusted for any revisions to existing orders during the period. New orders are recorded for the total contractual amount, excluding certain pass-through items, once a written agreement for the delivery of goods or provision of services is in place and, for businesses other than VPT, when shipment of the product (or in the case of certain highly customized security and inspection products, construction of the product) is expected to occur within two years, so long as any contingencies are deemed perfunctory. However, we will not record security and inspection products orders from governmental agencies with bid protest provisions until the expiration of the bid protest period. For our VPT business, we record orders when construction of the related proton therapy treatment center is reasonably expected to start within two years, but only if any contingencies are either deemed perfunctory or if the existence and nature of material contingencies is disclosed. However, we will not record VPT orders if there are major financing contingencies or customer board approval contingencies pending. We perform a quarterly review to verify that outstanding orders remain valid.

Oncology Systems gross orders within our Europe, Asia and the Rest of World regions were marginally impacted by currency exchange rates in the third quarter and first nine months of fiscal year 2014, compared to the respective year-ago periods. Oncology Systems gross orders decreased 2% on a constant currency basis in the third quarter of fiscal year 2014 and increased 3% on a constant currency basis in the first nine months of fiscal year 2014, as compared to the respective year-ago periods.

North American Oncology Systems gross orders were flat in the third quarter of fiscal year 2014, compared to the year-ago period. The increase in gross orders from services was offset by a decrease in gross orders from hardware products and software licenses during the third quarter of fiscal year 2014, compared to the year-ago quarter. The increase in North American Oncology Systems gross orders during the first nine months of fiscal year 2014, compared to the year-ago period, was due to increases in gross orders from services and software licenses partially offset by a decrease in gross orders from hardware products.

International Oncology Systems gross orders decreased in the third quarter of fiscal year 2014, compared to the year-ago period, due to a decrease in orders in the Rest of World region and Asia, partially offset by an increase in gross orders in Europe. The decrease in gross orders in the Rest of World region and Asia during the third quarter of fiscal year 2014, compared to the year-ago period, was primarily due to a decrease in gross orders from hardware products. The increase in gross orders in Europe during the third quarter of fiscal year 2014, compared to the year-ago period, was due to an increase in orders from software licenses and services, partially offset by a decrease in orders from hardware products. On a constant currency basis, international Oncology Systems gross orders decreased 4% in the third quarter of fiscal year 2014, compared to the year-ago period.

International Oncology Systems gross orders increased in the first nine months of fiscal year 2014, compared to the year-ago period, due to increases in gross orders in Rest of World region and Europe, partially offset by a decrease in gross orders in Asia. The increase in gross orders in the Rest of World region in the first nine months of fiscal year 2014, compared to the year-ago period was from increases in orders from hardware products, services and software products. The increase in gross orders from Europe in the first nine months of fiscal year 2014, compared to the year-ago period, was due to an increase in orders from services and software licenses, partially offset by a decrease in orders from hardware products. The decrease in gross orders in Asia in the first nine months of fiscal year 2014, compared to the year-ago period, was primarily due to decreases in gross orders from hardware products and software licenses, partially offset by an increase in orders from services. On a constant currency basis, international Oncology Systems gross orders increased 2% in the first nine months of fiscal year 2014, compared to the year-ago period.

The trailing 12 months growth in gross orders for Oncology Systems at the end of the third quarter of fiscal year 2014 and at the end of each of the previous three fiscal quarters were: a 3% total increase, with a 1% increase in North America and a 5% increase for the international region, as of June 27, 2014; a 5% total increase, with a 0.7% increase in North America and a 9% increase for the international region, as of March 28, 2014; a 3% total increase, with a 0.4% increase in North America and a 5% increase for the international region, as of December 27, 2013; and a 2% total increase, with a 2% decrease in North America and a 6% increase for the international region, as of September 27, 2013. Consistent with the historical pattern, we expect that Oncology Systems gross orders will continue to experience regional fluctuations, even with an overall shift of orders towards international regions and emerging markets. In addition, the availability of government programs that stimulate the purchase of healthcare products could affect the demand for our products from period to period, and could therefore make it difficult to compare our financial results.

Imaging Components gross orders increased in the third quarter and first nine months of fiscal year 2014, compared to the respective year-ago periods, due to increases in North American and International gross orders. North American gross orders increased in the third quarter of fiscal year 2014, compared to the year-ago period, due to increases in gross orders from X-ray tube and X-ray flat panel products. North American gross orders increased in the first nine months of fiscal year 2014, compared to the year-ago period, due to increases in gross orders from X-ray flat panel products and security and inspection products, partially offset by a decrease in gross orders in X-ray tube products.

International gross orders for Imaging Components increased in the third quarter of fiscal year 2014, compared to the year-ago period due to an increase in gross orders in Asia partially offset by a decrease in gross orders in Europe, and to a lesser extent a decrease in gross orders in the Rest of World region. Gross orders in Asia increased in the third quarter of fiscal year 2014, compared to the year-ago period primarily due to an increase in gross orders from X-ray flat panel products. Gross orders in Europe decreased in the third quarter of fiscal year 2014, compared to the year-ago period due to a decrease in gross orders from security and inspection products, partially offset by increases in gross orders from X-ray tube and X-ray flat panel products. Gross orders in the Rest of World region decreased in the third quarter of fiscal year 2014, compared to the year-ago period, primarily due to a decrease in gross orders from security and inspection products. International gross orders increased in the first nine months of fiscal 2014, compared to the year-ago period, due to increases in gross orders from Europe and Asia, partially offset by a decrease in orders from the Rest of World region. Gross orders in Europe increased in the first nine months of fiscal year 2014, compared to the year-ago period, due to increases in X-ray flat panel and X-ray tube products partially offset by a decrease in gross orders from security and inspection products. Gross orders in Asia increased in the first nine months of fiscal year 2014, compared to the year-ago period, due to an increase in X-ray flat panel products partially offset by a decrease in gross orders in X-ray tube products and to a lesser extent a decrease in gross orders in security and inspection products.

The increases in gross orders in the “Other” category in the third quarter and the first nine months of fiscal year 2014, compared to the respective year-ago periods, were due to an increase in orders from VPT.

Orders in any period may not be directly correlated to the level of revenues in any particular future quarter or period since the timing of revenue recognition will vary significantly based on the delivery requirements of individual orders, acceptance schedules and the readiness of individual customer sites for installation of our products. Moreover, certain types of orders, such as orders for software or newly introduced products in our Oncology Systems segment, typically take more time from order to completion of installation and acceptance than hardware or older products. Orders and revenues for our security and inspection products in our Imaging Components segment have been and may continue to be unpredictable as governmental agencies may place large orders with us or with our OEM customers over a short period of time and then may not place any orders for a long time period thereafter. Because an order for a proton therapy system can be relatively large, an order in one fiscal period will cause gross orders in our VPT business to vary significantly, making comparisons between fiscal periods more difficult. Furthermore, bid awards, primarily in our VPT business, may be subject to challenge by third parties, which can make these orders more unpredictable than other products.

Net Orders

The below table for net orders is provided for comparison purposes only. Net orders are defined as gross orders less backlog adjustments.

Total Net Orders (by segment and region)	Three Months Ended			Nine Months Ended		
(Dollars in millions)	June 27, 2014	June 28, 2013	Percent Change	June 27, 2014	June 28, 2013	Percent Change
Oncology Systems:						
North America	$267.4	$252.1	6 %	$719.7	$693.4	4 %
Total International	324.3	329.9	(2 %)	920.7	920.6	0 %
Total Oncology Systems	$591.7	$582.0	2 %	$1,640.4	$1,614.0	2 %
Imaging Components:						
North America	$51.9	$45.9	13 %	$133.9	$122.7	9 %
Total International	109.5	97.2	13 %	346.8	342.0	1 %
Total Imaging Components	$161.4	$143.1	13 %	$480.7	$464.7	3 %
Other:	$57.4	$1.4	n/m %	$117.0	$2.8	n/m %
Total Net Orders:	$810.5	$726.5	12 %	$2,238.1	$2,081.5	8 %

n/m = not meaningful

Backlog

Backlog is the accumulation of all gross orders for which revenues have not been recognized and are still considered valid. Backlog also includes a small portion of billed service contracts that are included in deferred revenue. Our backlog at June 27, 2014 was $2.9 billion, which was an increase of 4% over the backlog at June 28, 2013. Our Oncology Systems backlog at June 27, 2014 was 1% higher than the backlog at June 28, 2013, which reflected a 12% increase for the international region and a 10% decrease for North America.

We perform a quarterly review to verify that outstanding orders in the backlog remain valid. Aged orders that are not expected to be converted to revenues are deemed dormant and are reflected as a reduction in the backlog amounts and net orders in the period identified. Backlog adjustments are comprised of dormancies, cancellations, foreign currency exchange rate and other adjustments. In the third quarter of fiscal years 2014 and 2013, our backlog adjustments were $29.7 million and $46.6 million, respectively. In the first nine months of fiscal years 2014 and 2013, our backlog adjustments were $135.2 million and $101.0 million, respectively.

Liquidity and Capital Resources

Liquidity is the measurement of our ability to meet potential cash requirements, including ongoing commitments to repay borrowings, acquire businesses or make other investments or loans, repurchase shares of VMS common stock, and fund continuing operations and capital expenditures. Our sources of cash have included operations, borrowings, stock option exercises, employee stock purchases and interest income. Our cash usage is actively managed on a daily basis to ensure the maintenance of sufficient funds to meet our needs.

Cash and Cash Equivalents

The following table summarizes our cash and cash equivalents:

(In millions)	June 27, 2014	September 27, 2013	Increase/(Decrease)
Cash and cash equivalents	$926.0	$ 1,117.9	$ (191.9)

The decrease in cash and cash equivalents in the first nine months of fiscal year 2014 was primarily due to $417.2 million of cash used for the repurchase of shares of VMS common stock, $63.2 million used for purchases of property, plant, and equipment, $56.3 million used for repayments under our term loan facility and other borrowings, $40.7 million used to fund a portion of our loan commitment to CPTC for financing the construction and initial operation period of the Scripps Proton Therapy Center, $15.5 million for the acquisition of businesses, and $5.5 million for notes receivable. These decreases were partially offset by $255.6 million of cash provided by operating activities, $84.1 million of cash provided by stock option exercises, $38.1 million received from the sale of a portion of our loan to CPTC, and $29.6 million in borrowings under our credit facilities.

At June 27, 2014, we had approximately $101.7 million, or 11%, of total cash and cash equivalents in the United States. Approximately $824.3 million, or 89%, of total cash and cash equivalents was held abroad and could be subject to additional taxation if it were repatriated to the United States. As of June 27, 2014, most of our cash and cash equivalents that were held abroad were in U.S. Dollars and were primarily held as bank deposits. We have used our credit facilities to meet our cash needs from time to time and expect to continue to do so in the future. Borrowings under our credit facilities may be used for working capital, capital expenditures, permitted VMS stock repurchases, acquisitions and other lawful corporate purposes.

Cash Flows

	Nine Months Ended	
(In millions)	June 27, 2014	June 28, 2013
Net cash flow provided by (used in):		
Operating activities	$255.6	$300.3
Investing activities	(86.2)	(74.4)
Financing activities	(359.3)	(170.6)
Effects of exchange rate changes on cash and cash equivalents	(2.0)	5.7
Net increase / (decrease) in cash and cash equivalents	$(191.9)	$61.0

Our primary cash inflows and outflows for the first nine months of fiscal year 2014, as compared to the first nine months of fiscal year 2013, were as follows:

In the first nine months of fiscal year 2014, we generated net cash from operating activities of $255.6 million, compared to $300.3 million in the first nine months of fiscal year 2013. The $44.7 million decrease in net cash from operating activities in the first nine months of fiscal year 2014 compared to the year-ago period was primarily driven by decreases of $23.1 million in net earnings, $15.4 million in net change from operating assets and liabilities (working capital items), and $6.2 million from non-cash items.

The major contributors to the net change in working capital items in the first nine months of fiscal year 2014 were accounts receivable, inventories, deferred revenues and advance payments from customers, prepaid expenses and other assets, accrued expenses and other liabilities, and accounts payable:

Accounts receivable increased $67.9 million due to higher revenues and longer payment cycles.

Inventories increased $49.1 million due to anticipated customer demand for products in VPT, Oncology Systems, and Imaging Components.

Deferred revenues and advance payments from customers increased $42.7 million due to receipt of down payments for Oncology Systems and VPT orders for which revenues have not been recognized.

Prepaid expenses and other assets increased $22.1 million primarily due to an increase in prepayments for items such as state and local taxes, insurance, and license fees.

Accrued expenses and other liabilities decreased $14.8 million due to timing of tax payments and other expenses.

Accounts payable decreased $14.0 million primarily due to the timing of payments.

We expect that cash provided by operating activities will fluctuate in future periods as a result of a number of factors, including fluctuations in our operating results, timing of product shipments and customer acceptance, accounts receivable collections, inventory management, and the timing and amount of tax and other payments. For additional discussion, please refer to the “Risk Factors” in Item 1A.

In the first nine months of fiscal year 2014, we used $86.2 million for investing activities compared to $74.4 million used in the first nine months of fiscal year 2013. In the first nine months of fiscal year 2014, we used $63.2 million for purchases of property, plant and equipment, $40.7 million to fund a portion of our loan commitment to CPTC, $15.5 million for acquisitions of businesses and $5.5 million for notes receivable, partially offset by $38.1 million received from the sale of a portion of our loan to CPTC. In the first nine months of fiscal year 2013, we used $56.7 million for purchases of property, plant and equipment, $10.0 million for note receivable, and $7.6 million to fund a portion of our loan commitment to CPTC.

In the first nine months of fiscal year 2014, we used $359.3 million for financing activities compared to $170.6 million used in the first nine months of fiscal year 2013. In the first nine months of fiscal year 2014, we used $417.3 million for the repurchase of VMS common stock, $56.3 million for repayments under our term loan facility and other borrowings, and $8.7 million to satisfy employee tax withholding requirements for employees who tendered shares of VMS common stock upon vesting of restricted common stock and restricted stock units. These uses were partially offset by $84.1 million of proceeds from employee stock option exercises and employee stock purchases, $29.6 million in borrowings under credit facilities and $9.9 million in excess tax benefits from share-based compensation. During the first nine months of fiscal 2013, we used $289.1 million for the repurchase of VMS common stock, and $9.5 million to satisfy employee tax withholding requirements for employees who tendered shares of VMS common stock upon vesting of restricted common stock and restricted stock units. These uses were partially offset by $104.5 million of proceeds from employee stock option exercises and employee stock purchases, $14.9 million of net borrowings under our credit facilities, and $9.6 million in excess tax benefits from share-based compensation.
We expect our capital expenditures, which typically represent construction and/or purchases of facilities, manufacturing equipment, office equipment and furniture and fixtures, as well as capitalized costs related to the implementation of software applications, will be approximately 2.4% of revenues in fiscal year 2014.

As further described under “Contractual Obligations” below, we have loaned $69.4 million (including accrued interest) to CPTC as of June 27, 2014. We expect CPTC to continue to draw down on the loans. As of June 27, 2014, our remaining outstanding commitment to loan CPTC is up to $10.9 million to fund the construction and initial operation period of the Scripps Proton Therapy Center.

On August 27, 2013, we entered into the Credit Agreement with certain lenders and Bank of America, N.A. (“BofA”) as administrative agent. The Credit Agreement provides for (i) a five year term loan facility in an aggregate principal amount of up to $500 million (the “2013 Term Loan Facility”) and (ii) a five-year revolving credit facility in an aggregate principal amount of up to $300 million (the “2013 Revolving Credit Facility” and, collectively with the 2013 Term Loan Facility, the “2013 Credit Facility”). The 2013 Revolving Credit Facility also includes a $50 million sub-facility for the issuance of letters of credit and permits swing line loans of up to $25 million. Under the 2013 Credit Agreement, we have the right to make (i) up to two requests to increase the aggregate commitments under the Term Loan Facility by an aggregate amount for all such requests of up to $100 million and (ii) up to three requests to increase the aggregate commitments under the Revolving Credit Facility by an aggregate amount for all such requests of up to $200 million, provided that, in each case, the Lenders are willing to provide such new or increased commitments and certain other conditions are met. We may prepay, reduce or terminate the commitments without penalty. The 2013 Credit Facility contains provisions that limit our ability to pay cash dividends. The proceeds of the 2013 Credit Facility may be used for working capital, capital expenditures, permitted Company share repurchases, permitted acquisitions and other lawful corporate purposes.

Borrowings under the 2013 Term Loan Facility accrue interest either (i) based on a Eurodollar Rate, as defined in the Credit Agreement (the “Eurodollar Rate”), plus a margin of 1.00% to 1.25% based on a leverage ratio involving funded indebtedness and EBITDA or (ii) based upon a base rate of (a) the federal funds rate plus 0.50%, (b) BofA’s announced prime rate, or (c) the Eurodollar Rate plus 1.00%, whichever is highest, plus a margin of 0.00% to 0.25% based on the same leverage Ratio, depending upon instructions from us. Borrowings under the 2013 Revolving Credit Facility accrue interest either (i) based on the Eurodollar Rate plus a margin of 1.25% to 1.50% based on a leverage ratio involving funded indebtedness and EBITDA or (ii) based upon a base rate of (a) the federal funds rate plus 0.50%, (b) BofA’s announced prime rate, or (c) the Eurodollar Rate plus 1.00%, whichever is highest, plus a margin of 0.25% to 0.50% based on the same leverage ratio, depending upon instructions from us. At June 27, 2014, borrowings under the 2013 Term Loan Facility totaled $450.0 million with a weighted average interest rate of 1.28%. At June 27, 2014, there was no amount outstanding under the 2013 Revolving Credit Facility.

The Credit Agreement contains affirmative and negative covenants applicable to us and its subsidiaries that are typical for credit facilities of this type, and that are subject to materiality and other qualifications, carve-outs, baskets and exceptions. We have also agreed to maintain certain financial covenants including (i) a maximum consolidated leverage ratio, involving funded indebtedness and EBITDA (earnings before interest, tax and depreciation and amortization), and (ii) a minimum cash flow coverage ratio. We were in compliance with all covenants under the Credit Agreement during the first nine months of fiscal year 2014.

In addition, our Japanese subsidiary ("VMS KK") has an unsecured uncommitted credit agreement with Sumitomo Mitsui Banking Corporation that enables VMS KK to borrow and have outstanding at any given time a maximum of 3 billion Japanese yen (the "Sumitomo Credit Facility"). In March 2014, the Sumitomo Credit Facility was extended to March 2015. Borrowings under the Sumitomo Credit Facility accrue interest based on the basic loan rate announced by the Bank of Japan plus a margin of 0.5% per annum. As of June 27, 2014, $29.6 million was outstanding under the Sumitomo Credit Facility. In July 2014, VMS KK repaid the entire balance of the amount outstanding under the Sumitomo Credit Facility. There was no outstanding amount under the Sumitomo Credit Facility as of September 27, 2013.

In April 2014, we paid the outstanding balance of $6.3 million for the principal amount and accrued interest of our unsecured term loan.

See Note 7 “Borrowings” of the Condensed Consolidated Financial Statements for a discussion regarding the 2013 Term Loan Facility, 2013 Credit Facility and the Sumitomo Credit Facility.

Our liquidity is affected by many factors, some of which result from the normal ongoing operations of our business and some of which arise from uncertainties and conditions in the United States and global economies. Although our cash requirements will fluctuate as a result of the shifting influences of these factors, we believe that existing cash and cash equivalents and cash to be generated from operations and current or future credit facilities will be sufficient to satisfy anticipated commitments for capital expenditures and other cash requirements for at least the next 12 months and into the foreseeable future. We currently anticipate that we will continue to utilize our available liquidity and cash flows from operations, as well as borrowed funds, to make strategic acquisitions, invest in the growth of our business, invest in advancing our systems and processes, repurchase VMS common stock and fund our loan commitment to CPTC.

Total debt as a percentage of total capital decreased to 21.9% at June 27, 2014 from 22.8% at September 27, 2013 primarily due to the repayment of some of our borrowings under our 2013 Term Loan Facility. The ratio of current assets to current liabilities decreased to 2.17 to 1 at June 27, 2014 from 2.33 to 1 at September 27, 2013.

Days Sales Outstanding

Trade accounts receivable days sales outstanding (“DSO”) was 95 days at June 27, 2014 compared to 84 days at June 28, 2013. Excluding VPT, DSO was 87 days at June 27, 2014 compared to 76 days at June 28, 2013. Our accounts receivable and DSO are impacted by a number of factors, primarily including: the timing of product shipments, collections performance, payment terms, the mix of revenues from different regions, and the effects of continued economic instability. As of June 27, 2014, approximately 5% of our accounts receivable balance was related to customer contracts with remaining terms of more than one year.

Stock Repurchase Program

In November 2013, the VMS Board of Directors authorized the repurchase of an additional 6,000,000 shares of VMS common stock from December 30, 2013 through December 31, 2014. Stock repurchases under the November 2013 authorization may be made in open market purchases, in privately negotiated transactions (including accelerated share repurchase programs) or under Rule 10b5-1 share repurchase plans, and may be made from time to time in one or more blocks. Shares will be retired upon repurchase.

We repurchased a total of 5,250,000 shares of VMS common stock during the first nine months of fiscal year 2014, of which 1,250,000 shares were repurchased in the three months ended June 27, 2014. 3,250,000 of the shares repurchased in the first nine months of fiscal year 2014 were repurchased under the November 2013 authorization. During the first nine months of fiscal 2013, we repurchased a total of 4,150,000 shares of VMS common stock, of which 1,250,000 shares were repurchased in the three months ended June 28, 2013. As of June 27, 2014, 2,750,000 shares of VMS common stock remained available for repurchase under the November 2013 authorization.

Contractual Obligations

Long-term income taxes payable includes the liability for uncertain tax positions (including interest and penalties) and may also include other long-term tax liabilities. As of June 27, 2014, our liability for uncertain tax positions was $50.8 million, of which we do not anticipate making any payments in the next 12 months. We are unable to reliably estimate

the timing of the future payments related to uncertain tax positions; we believe that existing cash and cash equivalents and cash to be generated from operations and current or future credit facilities will be sufficient to satisfy any payment obligations that may arise related to our liability for uncertain tax positions.

As further described in Note 16, “CPTC Loans” of the Notes to the Condensed Consolidated Financial Statements, we participated, through our Swiss subsidiary, in a $165.3 million loan (“Tranche A loan”) to CPTC, under which we committed to loan up to $115.3 million, to finance the construction and start-up operations of the Scripps Proton Therapy Center. On June 10, 2014 our Swiss subsidiary entered into a series of agreements pursuant to which JPMorgan Chase Bank, N.A. (“J.P. Morgan”) assumed $45.0 million of our original maximum commitment of $115.3 million reducing our maximum commitment under the Tranche A loan to $70.3 million. Through these agreements, our Swiss subsidiary also increased its individual loan commitment by another $10.0 million (“Tranche B loan”). As of June 27, 2014, we had loaned $69.4 million under the Tranche A and Tranche B loans (collectively, referred to as “CPTC Loans”). We expect CPTC to continue to draw down on the loans during the construction and initial operation period. The amounts loaned under the CPTC Loans include accrued interest. As of June 27, 2014, our remaining outstanding commitment under the CPTC Loans was $10.9 million. We expect to use our cash abroad to meet funding requirements under this loan facility. We intend to sell all or a portion of our Tranche A loan before the maturity date of September 2017. We will not be required to make further loan advances for the portion of the Tranche A loan that is sold.

In April 2012, VMS entered into a strategic global partnership with Siemens AG (“Siemens”) through which, among other things, we and Siemens will collaborate to develop interfaces that will enable our ARIA oncology information system software to connect with Siemens linear accelerators and imaging systems. Under the agreement establishing this collaboration, we committed to make certain payments, including up to $10 million in fixed fees and $20 million in license fees, in the event that certain product development milestones are achieved. We will also pay for additional licenses beyond minimum quantities set forth in the agreement. We expect that these interfaces will be commercialized as part of our ARIA oncology information system offering to customers. As of June 27, 2014, the outstanding fixed fees and license fees commitment under the Siemens agreement was $6.5 million and $19.5 million, respectively.

In October 2013, VMS entered into an amended agreement with dpiX LLC (“dpiX”), and other parties that, among other things, provides us with the right to 50% of dpiX’s total manufacturing capacity produced after January 1, 2014. The amended agreement requires us to pay for 50% of the fixed costs (as defined in the amended agreement), as determined at the beginning of each calendar year. As of June 27, 2014, we had fixed cost commitments of $4.3 million related to this amended agreement for the remaining three months of fiscal year 2014. The fixed cost commitment for future years will be determined based on forecasted dpiX sales and approved by the board of directors of dpiX at the beginning of each calendar year. The amended agreement will continue unless the ownership structure of dpiX changes (as defined in the amended agreement).

Except for the change in the outstanding balance under our term loan facility and the other items discussed above, there has been no significant change to the other contractual obligations we reported in our 2013 Annual Report.

Subsequent Event

In July 2014, we closed the acquisition of certain assets and liabilities of Transpire, Inc., a privately-held developer of software solutions for accurately and rapidly predicting the macroscopic behavior of radiation. The transaction will be accounted for as a business combination. The total purchase consideration for the acquisition is $16 million in cash, excluding potential earn-out consideration of up to $4 million, which will be paid over the next three years if certain performance targets are achieved. We are currently evaluating the purchase price allocation for this transaction.

Contingencies

Environmental Remediation Liabilities

For a discussion of environmental remediation liabilities, see Note 9, “Commitments and Contingencies—Environmental Remediation Liabilities” of the Notes to the Condensed Consolidated Financial Statements, which discussion is incorporated herein by reference.

Other Matters

From time to time, we are a party to or otherwise involved in legal proceedings, claims and government inspections or investigations and other legal matters both inside and outside the United States, arising in the ordinary course of our business or otherwise. Such matters are subject to many uncertainties and outcomes are not predictable with assurance. See Note 9, “Commitments and Contingencies—Other Matters” of the Notes to the Condensed Consolidated Financial Statements, which discussion is incorporated herein by reference.

Off-Balance Sheet Arrangements

In conjunction with the sale of our products in the ordinary course of business, we provide standard indemnification of business partners and customers for losses suffered or incurred for property damages, death and injury and for patent, copyright or any other intellectual property infringement claims by any third parties with respect to our products. The terms of these indemnification arrangements are generally perpetual. Except for losses related to property damages, the maximum potential amount of future payments we could be required to make under these arrangements is unlimited. As of June 27 2014, we have not incurred any significant costs since the spin-offs to defend lawsuits or settle claims related to these indemnification arrangements. As a result, we believe the estimated fair value of these arrangements is minimal.

We have entered into indemnification agreements with our directors and officers and certain of our employees that serve as officers or directors of our foreign subsidiaries that may require us to indemnify our directors and officers and those certain employees against liabilities that may arise by reason of their status or service as directors or officers, and to advance their expenses incurred as a result of any legal proceeding against them as to which they could be indemnified.

Recent Accounting Pronouncements

In June 2014, the Financial Accounting Standards Board ("FASB") issued an amendment to its accounting guidance related to stock-based compensation. The amendment requires that a performance target that could be achieved after the requisite service period be treated as a performance condition that affects vesting, rather than a condition that affects the grant-date fair value. The new guidance will be effective in our fiscal year beginning 2017. Early adoption is permitted. The amendment can be applied on a prospective basis to all share-based payments granted or modified on or after the effective date. Entities will also be provided an option to apply the guidance on a modified retrospective basis to existing awards. We are evaluating the impact of adopting this guidance to our consolidated financial statements.

In May 2014, FASB issued an amendment to its accounting guidance related to revenue recognition. The amendment sets forth a single, comprehensive revenue recognition model for all contracts with customers to improve comparability. The amendment requires revenue recognition to depict the transfer of goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. The new guidance will be effective in our fiscal year beginning 2018. Early application is not permitted. The amendments can be applied either retrospectively to each prior reporting period presented or retrospectively with the cumulative effect of initially applying the update recognized at the date of the initial application along with additional disclosures. We are evaluating the impact of adopting this guidance to our consolidated financial statements.

Item 3. Quantitative and Qualitative Disclosures About Market Risk

We are exposed to three primary types of market risks: credit risk, foreign currency exchange rate risk and interest rate risk.

Credit Risk and Counterparty Risk

We are exposed to credit loss in the event of nonperformance by counterparties on the foreign currency forward contracts used in hedging activities. These counterparties are large international and regional financial institutions and to date, no such counterparty has failed to meet its financial obligation to us under such contracts. We are also exposed to credit loss in the event of default by CPTC, the obligor under the loan facility in which we are participating to finance the construction and start-up of the Scripps Proton Therapy Center. In addition, cash and cash equivalents

held with financial institutions may exceed the Federal Deposit Insurance Corporation insurance limits or similar limits in foreign jurisdictions. We also may need to rely on the credit facility described below under “Interest Rate Risk.” Our access to our cash and cash equivalents or ability to borrow could be reduced if one or more financial institutions with which we have deposits or from which we borrow should fail or otherwise be adversely impacted by conditions in the financial or credit markets. Conditions such as those we experienced as a result of the economic downturn of 2008 and accompanying contraction in the credit markets heighten these risks. Concerns over continued economic instability, including the sovereign debt and banking crises in Europe, could make it more difficult for us to collect outstanding receivables and could adversely impact our liquidity.

Foreign Currency Exchange Rate Risk

As a global entity, we are exposed to movements in foreign currency exchange rates. These exposures may change over time as business practices evolve. Adverse foreign currency rate movements could have a material negative impact on our financial results. Our primary exposures related to foreign currency denominated sales and purchases are in Europe, Asia, Australia and Canada.

We have many transactions denominated in foreign currencies and address certain of those financial exposures through a risk management program that includes the use of derivative financial instruments. We sell products throughout the world, often in the currency of the customer's country, and may hedge certain of these larger foreign currency transactions when they are not transacted in the subsidiaries' functional currency or in U.S. Dollars. The foreign currency sales transactions that fit our risk management policy criteria are hedged with forward contracts. We may use other derivative instruments in the future. We enter into foreign currency forward contracts primarily to reduce the effects of fluctuating foreign currency exchange rates. We do not enter into forward contracts for speculative or trading purposes. The forward contracts range from one to thirteen months in maturity.

We also hedge the balance sheet exposures from our various foreign subsidiaries and business units. We enter into foreign currency forward contracts to minimize the short-term impact of currency fluctuations on assets and liabilities denominated in currencies other than the U.S. dollar functional currency.

The notional values of our sold and purchased foreign currency forward contracts outstanding as of June 27, 2014 were $327.4 million and $62.4 million, respectively. The notional amounts of forward contracts are not a measure of our exposure. The fair value of forward contracts generally reflects the estimated amounts that we would receive or pay to terminate the contracts at the reporting date, thereby taking into account and approximating the current unrealized and realized gains or losses of the open contracts. A move in foreign currency exchange rates would change the fair value of the contracts, and the fair value of the underlying exposures hedged by the contracts would change in a similar offsetting manner.

Interest Rate Risk

Our market risk exposure to changes in interest rates depends primarily on our investment portfolio and short-term borrowings. Our investment portfolio consisted of cash and cash equivalents and available-for-sale securities as of June 27, 2014. The principal amount of cash and cash equivalents at June 27, 2014 totaled $926 million with a weighted average interest rate of 0.22%.

The 2013 Credit Facility, which includes the 2013 Revolving Credit Facility and the 2013 Term Loan Facility, allows us to borrow up to a maximum amount of $300 million under the 2013 Revolving Credit Facility and $500 million under the 2013 Term Loan Facility. We secured a portion of the 2013 Credit Facility with a pledge of 65% of the voting shares that we hold in Varian Medical Systems Nederland B.V., a wholly-owned subsidiary.

Borrowings under the 2013 Term Loan Facility accrue interest either (i) based on a Eurodollar Rate, plus a margin of 1.00% to 1.25% based on a leverage ratio involving funded indebtedness and EBITDA or (ii) based upon a base rate of (a) the federal funds rate plus 0.50%, (b) BofA's announced prime rate, or (c) the Eurodollar Rate plus 1.00%, whichever is highest, plus a margin of up to 0.25% based on the same leverage ratio, depending upon instructions from the Company. Borrowings under the 2013 Revolving Credit Facility accrue interest either (i) based on the Eurodollar Rate plus a margin of 1.25% to 1.50% based on a leverage ratio involving funded indebtedness and EBITDA or (ii) based upon a base rate of (a) the federal funds rate plus 0.50%, (b) BofA's announced prime rate, or (c) the Eurodollar Rate plus 1.00%, whichever is highest, plus a margin of 0.25% to 0.50% based on the same leverage ratio, depending upon instructions from VMS.

In addition, the Sumitomo Credit Facility allows us to borrow up to a maximum amount of 3 billion Japanese Yen. Borrowings under the Sumitomo Credit Facility accrue interest based on the basic loan rate announced by the Bank of Japan plus a margin of 0.5% per annum. As of June 27, 2014, we have borrowed $29.6 million under the Sumitomo Credit Facility which is included in short-term debt on the Condensed Consolidated Balance Sheets. In July 2014, we repaid the entire balance of the amount outstanding under the Sumitomo Credit Facility.

We are affected by market risk exposure primarily through the effect of changes in interest rates on amounts payable under our revolving credit facility and term loan facility. As of June 27, 2014, there was no amount outstanding under our revolving credit facility. As of June 27, 2014, borrowings under the 2013 Term Loan Facility totaled $450.0 million with a weighted average interest rate of 1.28%. If the amount outstanding under our 2013 Term Loan Facility remained at this level for an entire year and interest rates increased or decreased by 1%, our annual interest expense would increase or decrease, respectively, by approximately $5 million. See Note 7 “Borrowings” of the Condensed Consolidated Financial Statements for a discussion regarding the 2013 Term Loan Facility.

To date, we have not used derivative financial instruments to hedge the interest rate of our investment portfolio, short-term borrowings or long-term debt, but may consider the use of derivative instruments in the future.

The estimated fair value of our long-term debt at June 27, 2014, approximates its carrying value because the term loan is carried at a market observable interest rate that resets periodically.

At June 27, 2014, loans of an aggregate amount of $69.4 million (including accrued interest) to CPTC bear interest at LIBOR plus 7.00% per annum with a minimum interest rate of 9.00% per annum. The CPTC loans are classified as available-for-sale securities and carried at fair value.

The fair value of our CPTC loans was $69.4 million at June 27, 2014, which was estimated based on the income approach by using the discounted cash flow model with key assumptions that include discount rates corresponding to the terms and risks associated with the loan to CPTC. In addition we do not increase the fair value above its par value as ORIX Capital Markets LLC ("ORIX"), the loan agent, has the option to purchase this loan from us under the original terms and conditions at par value.

Although payments under certain of our operating leases for our facilities are tied to market indices, these operating leases do not expose us to material interest rate risk.

Item 4. Controls and Procedures

(a) Disclosure controls and procedures. Based on the evaluation of our disclosure controls and procedures (as defined in the Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934, as amended (the "Exchange Act")) required by Exchange Act Rules 13a-15(b) or 15d-15(b), our principal executive officer and principal financial officer have concluded that as of the end of the period covered by this report, our disclosure controls and procedures were effective to ensure that information we are required to disclose in reports that we file or submit under the Exchange Act is recorded, processed, summarized and reported within the time periods specified in Securities and Exchange Commission rules and forms, and include controls and procedures designed to ensure that information required to be disclosed by us in such reports is accumulated and communicated to our management, including the principal executive officer and principal financial officer, as appropriate to allow timely decisions regarding required disclosure.

(b) Changes in internal control over financial reporting. There were no changes in our internal control over financial reporting that occurred during the third quarter of fiscal year 2014 that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

PART II

OTHER INFORMATION

Item 1. Legal Proceedings

We are subject to various legal proceedings and claims that are discussed in Note 9, “Commitments and Contingencies” to the Condensed Consolidated Financial Statements, which discussion is incorporated by reference into this item.

Item 1A. Risk Factors

The following risk factors and other information included in this Quarterly Report on Form 10-Q and in our 2013 Annual Report should be carefully considered. Although the risk factors described below are the ones management deems significant, additional risks and uncertainties not presently known to us or that we presently deem less significant may also impair our business operations. If any of the following risks actually occur, our business, operating results, and financial condition could be adversely affected.

IF OUR PRODUCTS AND PRODUCT LINES FAIL TO CONTINUE TO MEET CUSTOMER DEMANDS, OUR PRODUCTS MAY BECOME LESS USEFUL OR OBSOLETE AND OUR OPERATING RESULTS WILL SUFFER

We believe that IMRT, including volumetric modulated arc therapy, and IGRT have become accepted standards for treatment in the radiation oncology market. Demand for our IMRT and IGRT products have been the drivers for our gross orders and revenues in Oncology Systems and, because of the significance of Oncology Systems, in our business in general. We have introduced products such as TrueBeam, a line of linear accelerators for radiotherapy and radiosurgery, and UNIQUE, a less complex, low-energy linear accelerator for the more price sensitive emerging markets, to meet the evolving needs of our IMRT and IGRT customers. We believe TrueBeam is a valuable tool for clinicians in the fight against cancer and will stimulate faster replacement of older systems in our installed base. We also believe that our RapidArc products for volumetric modulated arc therapy are a significant advance in IMRT treatments and can help drive longer term demand for our linear accelerators and IMRT- and IGRT-related products. Orders for these products and products lines have contributed greatly to our orders and revenue growth and are keys to our future success. If our customers do not purchase these products or if future studies call into question the effectiveness of these or our other IMRT or IGRT products (including other volumetric modulated arc therapy products) or show negative side effects, or if other more effective technologies are introduced, our gross orders, revenues and financial results could suffer. As more institutions buy or upgrade to achieve IMRT and IGRT capabilities, the market for these products (including volumetric modulated arc therapy products) may become saturated. Alternatively, the marketplace may conclude that functions and features of our products should no longer be an element of a generally accepted diagnostic or treatment regimen. If this occurs, the market for our products may be adversely affected and they may become less useful or obsolete.

Our Imaging Components business sells products primarily to a small number of imaging system OEM customers who use our products in their medical diagnostic, security and industrial imaging systems. To succeed, we must provide products that meet customer demands for product quality, superior technology and product performance at a competitive cost. If we are unable to continue to innovate our Imaging Components and anticipate our customers’ demands in the areas of cost, quality, technology and performance, then our customers may purchase from other imaging component manufacturers (including the in-house operations of some of these customers), which would negatively impact this business.

In our Oncology Systems and Imaging Components businesses, as well as in our other product lines, we may be unable to accurately anticipate changes in our markets and the direction of technological innovation and demands of our customers. Our competitors may develop products or processes that are superior to, or more cost efficient than, what we can then offer. If this occurs, the market for our products may be adversely affected and our products may become less useful or obsolete. Any development adversely affecting the markets for our products would force us to reduce production volumes or to discontinue manufacturing one or more of our products or product lines and would reduce our revenues and earnings.

OUR SUCCESS DEPENDS ON THE SUCCESSFUL DEVELOPMENT, INTRODUCTION AND COMMERCIALIZATION OF NEW GENERATIONS OF PRODUCTS AND ENHANCEMENTS TO OR SIMPLIFICATIONS OF EXISTING PRODUCT LINES

Rapid change and technological innovation characterize the markets in which we operate. Our Oncology Systems products often have long development and government approval cycles, so we must anticipate changes in the marketplace, in technology and in customer demands. Our success depends on the successful development, introduction and commercialization of new generations of products, treatment systems and enhancements to and/or simplification of existing product lines. Our Oncology Systems products, including products such as EDGE™ and TrueBeam, are technologically complex and must keep pace with, if not be superior to, the products of our competitors. Our Imaging Components business must also continually improve products at competitive costs. We are investing in long-term growth initiatives, such as development of our VPT business, and expect that we will need to invest more to develop and commercialize new products and technology for this business. Accordingly, our products may require significant planning, design, development and testing, as well as significant capital commitments, involvement of senior management and other investments on our part. In addition, because of the large footprint and high price of many proton therapy systems, including ours, there is increasing demand for development of a smaller, more compact proton therapy system. Other companies currently offer smaller, less expensive proton therapy systems, and our ability to compete with these companies may depend on our ability to timely develop new technologies to reduce the size and price of our system or provide additional features and functionality that our competitors do not.

We may need to spend more time and money than we expect to develop and introduce new products or enhancements and, even if we succeed, they may not be sufficiently profitable that we are able to recover all or a meaningful part of our investment. Once introduced, new products may adversely impact orders and sales of our existing products, or make them less desirable or even obsolete, and could adversely impact our revenues and operating results. In addition, certain costs, including installation and warranty, associated with new products may be proportionately greater than other products, and may therefore adversely affect our gross and operating margins. If we are unable to lower these costs over time, our operating results could be adversely affected. Compliance with regulations, competitive alternatives, and shifting market preferences may also impact our success with new products or enhancements.

Our ability to successfully develop and introduce new products and product enhancements and simplifications, and the revenues and costs associated with these efforts, are affected by our ability to:

properly identify customer needs;
prove the feasibility of new products;
limit the time required from proof of feasibility to routine production;
timely and efficiently comply with internal quality assurance systems and processes;
limit the timing and cost of regulatory approvals;
accurately predict and control costs associated with inventory overruns caused by phase-in of new products and phase-out of old products;
price our products competitively and profitably;
manufacture, deliver and install our products in sufficient volumes on time, and accurately predict and control costs associated with manufacturing, installation, warranty and maintenance of the products;
appropriately manage our supply chain;
manage customer acceptance and payment for products;
manage customer demands for retrofits of both new and old products; and
anticipate and compete successfully with competitors.

Furthermore, we cannot be sure that we will be able to successfully develop, manufacture or introduce new products, treatment systems or enhancements, the roll-out of which involves compliance with complex quality assurance

processes, including the Quality System Regulation ("QSR") of the FDA. Failure to complete these processes timely and efficiently could result in delays that could affect our ability to attract and retain customers, or could cause customers to delay or cancel orders, causing our revenues and operating results to suffer.

New products generally take longer to install than well-established products. Because a portion of a product's revenue is generally tied to installation and acceptance of the product, our recognition of revenue associated with new products may be deferred longer than expected. In addition, even if we succeed in our product introductions, potential customers may not decide to upgrade their equipment, or customers may delay delivery of some of our more sophisticated products because of the longer preparation and renovation of treatment rooms required. As a result, our revenues and other financial results could be adversely affected.

MORE THAN HALF OF OUR REVENUES ARE INTERNATIONAL, AND ECONOMIC, POLITICAL AND OTHER RISKS ASSOCIATED WITH INTERNATIONAL SALES AND OPERATIONS COULD ADVERSELY AFFECT OUR SALES OR MAKE THEM LESS PREDICTABLE

We conduct business globally. Our international revenues accounted for approximately 52% and 57% of revenues from continuing operations during the third quarter of fiscal year 2014 and 2013, respectively, and approximately 57%, 56% and 55% during fiscal years 2013, 2012 and 2011, respectively. As a result, we must provide significant service and support globally. We intend to continue to expand our presence in international markets and expect to expend significant resources in doing so. We cannot be sure, however, that we will be able to meet our sales, service and support objectives or obligations in these international markets, or recover our investments. For example, we have aligned our resources to support sales and marketing efforts in emerging markets. Our future results could be harmed by a variety of factors, including:

currency fluctuations;
the lower sales prices and gross margins usually associated with sales of our products in the international region, in particular emerging markets;
the longer payment cycles associated with many foreign customers;
difficulties in interpreting or enforcing agreements and collecting receivables through many foreign country's legal systems;
changes in the political, regulatory, safety or economic conditions in a country or region;
the imposition by foreign countries of additional taxes, tariffs or other restrictions on foreign trade;
the longer period in the international region from placement of any order to revenue recognition;
any inability to obtain export licenses and other required export or import licenses or approvals;
failure to comply with export laws and requirements, which may result in civil or criminal penalties and restrictions on our ability to export our products, particularly our industrial linear accelerator products;
failure to obtain proper business licenses or other documentation, or to otherwise comply with local laws and requirements regarding marketing, sales, service or any other business we conduct in a foreign jurisdiction, which may result in civil or criminal penalties and restrictions on our ability to conduct business in that jurisdiction; and
the possibility that it may be more difficult to protect our intellectual property in foreign countries.

Although our orders and sales fluctuate from period to period, in recent years our international region has represented a larger share of our business. The more we depend on sales in the international region, the more vulnerable we become to these factors.

As of June 27, 2014, 89% of our cash and cash equivalents were held abroad. If these funds were repatriated to the United States, they could be subject to additional taxation and our overall tax rate and our results of operations could suffer.

Our effective tax rate is impacted by tax laws in both the United States and in the countries in which our international subsidiaries do business. Earnings from our international region are generally taxed at rates lower than U.S. rates. A change in the percentage of our total earnings from the international region, or a change in the mix of particular tax jurisdictions within the international region could cause our effective tax rate to increase or decrease. Also, we are not currently taxed in the United States on certain undistributed earnings of certain foreign subsidiaries. These earnings

could become subject to incremental foreign withholding or U.S. federal and state taxes should they either be deemed or actually remitted to the United States, in which case our financial results would be adversely affected. In addition, there have been proposals that would significantly change U.S. taxation of U.S.-based multinational corporations. Although we cannot predict whether or in what form Congress would enact any such proposals, legislation of this type could negatively impact our effective tax rate and adversely affect our financial results.

OUR RESULTS HAVE BEEN AND MAY CONTINUE TO BE AFFECTED BY CONTINUING WORLDWIDE ECONOMIC INSTABILITY

Since fiscal year 2008, the global economy has been impacted by a number of economic factors, including the sequential effects of the subprime lending crisis; the credit market crisis; collateral effects on the finance and banking industries; volatile currency exchange rates and energy costs; concerns over the downgrade of the sovereign debt of the United States and several European countries; continued sovereign debt and banking system uncertainties in Europe and other foreign countries and concerns regarding recession in Europe and the directions of the Chinese and United States economies. In many markets, these conditions have shrunk capital equipment budgets, slowed decision-making, made financing for large equipment purchases more expensive and more time consuming to obtain, and made it difficult for our customers and our vendors to accurately forecast and plan future business activities and reduced their confidence. This, in turn, has caused our customers to freeze, delay or dramatically reduce purchases and capital project expenditures. Project delays may continue, particularly as they relate to large scale or government projects, which may be affected by austerity measures. Alternatively, in the past, some countries have adopted and may in the future adopt government stimulus programs to revitalize their economies and improve healthcare and medical services. The availability of stimulus programs in the future could positively affect our results in one period and adversely affect our results in other periods, making it difficult for investors to compare our financial results between fiscal periods. Weak economic recovery may also disrupt supply if vendors consolidate or go out of business. As with our customers and vendors, these economic conditions make it more difficult for us to accurately forecast and plan our future business activities. Continued economic uncertainty may also affect our service business, as customers' constrained budgets may result in pricing pressure, extended warranty provisions and even cancellation of service contracts.

In addition, concerns over continued economic instability, including the sovereign debt and banking crises in Europe, could make it more difficult for us to collect outstanding receivables. Historically, our business has felt the effects of market trends later than other sectors in the healthcare industry, such as diagnostic radiology, and we may experience the effects of any economic recovery later than others in the healthcare industry. A continued weak or deteriorating healthcare market would inevitably adversely affect our business, financial conditions and results of operations.

WE FACE SIGNIFICANT COSTS IN ORDER TO COMPLY WITH LAWS AND REGULATIONS APPLICABLE TO THE MANUFACTURE AND DISTRIBUTION OF OUR PRODUCTS, AND FAILURE OR DELAYS IN OBTAINING REGULATORY CLEARANCES OR APPROVALS, OR FAILURE TO COMPLY WITH APPLICABLE LAWS AND REGULATIONS COULD PREVENT US FROM DISTRIBUTING OUR PRODUCTS, REQUIRE US TO RECALL OUR PRODUCTS AND RESULT IN SIGNIFICANT PENALTIES

Our products and those of OEMs that incorporate our products are subject to extensive and rigorous government regulation in the United States. Compliance with these laws and regulations is expensive and time-consuming, and failure to comply with these laws and regulations could adversely affect our business. Furthermore, public media reports on misadministrations of radiotherapy in patients and focus on the role of the FDA in regulating medical devices has led to increased scrutiny of medical device companies and an increased likelihood of enforcement actions.

U.S. laws governing marketing a medical device. In the United States, as a manufacturer and seller of medical devices and devices emitting radiation or utilizing radioactive by-product material, we and some of our suppliers and distributors are subject to extensive regulation by federal governmental authorities, such as the FDA, the Nuclear Regulatory Commission ("NRC") and state and local regulatory agencies, such as the State of California, to ensure the devices are safe and effective and comply with laws governing products which emit, produce or control radiation. These regulations govern, among other things, the design, development, testing, manufacturing, packaging, labeling, distribution, import/export, sale and marketing and disposal of our products.

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Unless an exception applies, the FDA requires that the manufacturer of a new medical device or a new indication for use of, or other significant change in, existing currently marketed medical device obtain either 510(k) pre-market notification clearance or pre-market approval ("PMA") before it can market or sell those products in the United States. Modifications or enhancements to a product that could significantly affect its safety or effectiveness, or that would constitute a major change in the intended use of the device, technology, materials, labeling, packaging, or manufacturing process also require a new 510(k) clearance. Although manufacturers make the initial determination whether a change to a cleared device requires a new 510(k) clearance, we cannot assure you that the FDA will agree with our decisions not to seek additional approvals or clearances for particular modifications to our products or that we will be successful in obtaining new 510(k) clearances for modifications. Obtaining clearances or approvals is time-consuming, expensive and uncertain, and the PMA process is more complex than the 510(k) clearance process. We may not be able to obtain the necessary clearances or approvals or may be unduly delayed in doing so, which could harm our business. Furthermore, even if we are granted regulatory clearances or approvals, they may include significant limitations on the indicated uses of the product, which may limit the market for the product. If we were unable to obtain required FDA clearance or approval for a product or unduly delayed in doing so, or the uses of that product were limited, our business could suffer. In the past, our devices have generally been subject to 510(k) clearance or exempt from 510(k) clearance. However, there are some in the regulatory field who believe that certain medical devices should be required to use the PMA approval process. If we were required to use the PMA process for future products or product modifications, it could delay or prevent release of the proposed products or modifications, which could harm our business.

Further, as we enter new businesses or pursue new business opportunities, such as radiosurgery and opportunities that require clinical trials, we may become subject to additional laws, rules and regulations, including FDA rules and regulations that are applicable to the clinical trial process and protection of study subjects. Becoming familiar with and implementing the infrastructure necessary to comply with these laws, rules and regulations is costly. In addition, failure to comply with these laws, rules and regulations could delay the introduction of new products and could adversely affect our business.

Quality systems. Our manufacturing operations for medical devices, and those of our third-party manufacturers, are required to comply with the FDA's QSR, as well as other federal and state regulations for medical devices and radiation emitting products. The FDA makes announced and unannounced periodic and on-going inspections of medical device manufacturers to determine compliance with QSR and in connection with these inspections issues reports, known as Form FDA 483 reports when the FDA believes the manufacturer has failed to comply with applicable regulations and/or procedures. If observations from the FDA issued on Form FDA 483 reports are not addressed and/or corrective action taken in a timely manner and to the FDA's satisfaction, the FDA may issue a Warning Letter and/or proceed directly to other forms of enforcement action. Similarly, if a Warning Letter were issued, prompt corrective action to come into compliance would be required. Failure to respond timely to Form FDA 483 observations, a Warning Letter or other notice of noncompliance and to promptly come into compliance could result in the FDA bringing enforcement action against us, which could include the total shutdown of our production facilities, denial of importation rights to the U.S. for products manufactured in overseas locations, adverse publicity and criminal and civil fines. The expense and costs of any corrective actions that we may take, which may include products recalls, correction and removal of products from customer sites and/or changes to our product manufacturing and quality systems, could adversely impact our financial results and may also divert management resources, attention and time. Additionally, if a Warning Letter were issued, customers could delay purchasing decisions or cancel orders, and we could face increased pressure from our competitors who could use the Warning Letter against us in competitive sales situations, either of which could adversely affect our reputation, business and stock price.

In addition, we are required to timely file various reports with the FDA, including reports required by the medical device reporting regulations ("MDRs"), that require that we report to regulatory authorities if our devices may have caused or contributed to a death or serious injury or malfunctioned in a way that would likely cause or contribute to a

death or serious injury if the malfunction were to recur. If these reports are not filed timely, regulators may impose sanctions and sales of our products may suffer, and we may be subject to product liability or regulatory enforcement actions, all of which could harm our business.

If we initiate a correction or removal of a device to reduce a risk to health posed by the device, we would be required to submit a publicly available Correction and Removal report to the FDA and in many cases, similar reports to other regulatory agencies. This report could be classified by the FDA as a device recall which could lead to increased scrutiny by the FDA, other international regulatory agencies and our customers regarding the quality and safety of our devices. Furthermore, the submission of these reports have been and could be used by competitors against us in competitive situations and cause customers to delay purchase decisions, cancel orders or adversely affect our reputation.

Our medical devices utilizing radioactive material are subject to the NRC clearance and approval requirements, and the manufacture and sale of these products are subject to extensive federal and state regulation that varies from state to state and among regions. Our manufacture, distribution, installation and service (and decommissioning and removal) of medical devices utilizing radioactive material or emitting radiation also requires us to obtain a number of licenses and certifications for these devices and materials. Service of these products must also be in accordance with a specific radioactive materials license. Obtaining licenses and certifications may be time consuming, expensive and uncertain. In addition, we are subject to a variety of environmental laws regulating our manufacturing operations and the handling, storage, transport and disposal of hazardous materials, and which impose liability for the cleanup of any contamination from these materials. In particular, the handling and disposal of radioactive materials resulting from the manufacture, use or disposal of our products may impose significant costs and requirements. Disposal sites for the lawful disposal of materials generated by the manufacture, use or decommissioning of our products may no longer accept these materials in the future, or may accept them on unfavorable terms.

The FDA and the FTC also regulate advertising and promotion of our products to ensure that the claims we make are consistent with our regulatory clearances, that there are adequate and reasonable scientific data to substantiate the claims and that our promotional labeling and advertising is neither false nor misleading in any respect. If the FDA or FTC determines that any of our advertising or promotional claims are misleading, not substantiated or not permissible, we may be subject to enforcement actions, including Warning Letters, and may be required to revise our promotional claims and make other corrections or restitutions.

If we or any of our suppliers, distributors, agents or customers fail to comply with FDA, FTC and other applicable U.S. regulatory requirements or are perceived to potentially have failed to comply, we may face:

adverse publicity affecting both us and our customers;
increased pressures from our competitors;
investigations by governmental authorities or Warning Letters;
fines, injunctions, and civil penalties;
partial suspensions or total shutdown of production facilities, or the imposition of operating restrictions;
increased difficulty in obtaining required FDA clearances or approvals;
losses of clearances or approvals already granted;
seizures or recalls of our products or those of our customers;
delays in purchasing decisions by customers or cancellation of existing orders;
the inability to sell our products;
difficulty in obtaining product liability or operating insurance at a reasonable cost, or at all; and
civil fines and criminal prosecutions.

Other applicable U.S. regulations. As a participant in the healthcare industry, we are also subject to extensive laws and regulations protecting the privacy and integrity of patient medical information that we receive, including the HIPAA, “fraud and abuse” laws and regulations, including physician self-referral prohibitions, and false claims laws. From time to time, these laws and regulations may be revised or interpreted in ways that could make it more difficult for our customers to conduct their businesses, such as recent proposed revisions to the laws prohibiting physician self-referrals, and such revisions could have an adverse effect on the demand for our products, and therefore our business and results of operations. We also must comply with numerous federal, state and local laws of more general applicability relating to such matters as safe working conditions, manufacturing practices and fire hazard control.

The laws and regulations and their enforcement are constantly undergoing change, and we cannot predict what effect, if any, changes to these laws and regulations may have on our business. For example, HIPAA was amended by the HITECH Act, enacted as part of the American Recovery and Reinvestment Act of 2009. The HITECH Act significantly increases the civil money penalties for violations of patient privacy rights protected under HIPAA. Furthermore, business associates who have access to patient health information provided by hospitals and healthcare

providers are now directly subject to HIPAA, including the new enforcement scheme and inspection requirements. Moreover, there has been a trend in recent years toward more stringent regulation and enforcement of requirements applicable to medical device manufacturers who receive or have access to patient health information.

Government regulation also may cause considerable delay or even prevent the marketing and full commercialization of future products or services that we may develop, and/or may impose costly requirements on our business. Insurance coverage is not commercially available for violations of law, including the fines, penalties or investigatory costs that may flow to us as the consequence of regulatory violations; consequently, we do not have insurance that would cover this type of liability.

COMPLIANCE WITH FOREIGN LAWS AND REGULATIONS APPLICABLE TO THE MANUFACTURE AND DISTRIBUTION OF OUR PRODUCTS MAY BE COSTLY, AND FAILURE TO COMPLY MAY RESULT IN SIGNIFICANT PENALTIES

Regulatory requirements affecting our operations and sales outside the United States vary from country to country, often differing significantly from those in the United States. In general, outside the United States, our products are regulated as medical devices by foreign governmental agencies similar to the FDA.

Marketing a medical device internationally. In order for us to market our products internationally, we must obtain clearances or approvals for products and product modifications. These processes (including for example in the European Union ("EU"), the European Economic Area ("EEA"), Switzerland, China, Japan and Canada) can be time consuming, expensive and uncertain, which can delay our ability to market products in those countries. Delays in receipt of or failure to receive regulatory approvals, the inclusion of significant limitations on the indicated uses of a product, the loss of previously obtained approvals or failure to comply with existing or future regulatory requirements could restrict or prevent us from doing business in a country or subject us to a variety of enforcement actions and civil or criminal penalties, which would adversely affect our business.

Within the EEA, we must affix a CE mark, a European marking of conformity that indicates that a product meets the essential requirements of the Medical Device Directive. This conformity to the Medical Device Directive is done through self-declaration and is verified by an independent certification body, called a "Notified Body." Once the CE mark is affixed, the Notified Body will regularly audit us to ensure that we remain in compliance with the applicable European laws and Medical Device Directive. By affixing the CE mark marking to our product, we are certifying that our products comply with the laws and regulations required by the EEA countries, thereby allowing the free movement of our products within these countries and others that accept CE mark standards. If we cannot support our performance claims and demonstrate compliance with the applicable European laws and Medical Device Directive, we would lose our right to affix the CE mark to our products, which would prevent us from selling our products within the EU/EEA/Switzerland territory and in other countries that recognize the CE mark. Significant revisions to some of the applicable regulations governing requirements for medical devices in the EU/EEA/Switzerland went into effect in March 2010. These revisions have introduced additional uncertainty into the marketing authorization process for medical devices in Europe. Until medical device manufacturers and European regulatory agencies, including Notified Bodies and "Competent Authorities," (governmental agencies to whom the legislator has delegated the capacity to enforce the Medical Devices Directive) have greater experience with interpreting and applying the revised regulations, we may be subject to risks associated with additional testing, modification, certification or amendment of our existing market authorizations, or we may be required to modify products already installed at our customers' facilities in order to comply with the official interpretations of these revised regulations.

In addition, we are required to timely file various reports with international regulatory authorities, including reports required by international adverse event reporting regulations, that require that we report to regulatory authorities if our devices may have caused or contributed to a death or serious injury or malfunctioned in a way that would likely cause or contribute to a death or serious injury if the malfunction were to recur. If these reports are not timely filed, regulators may impose sanctions, including temporarily suspend our market authorizations or CE mark, and sales of our products may suffer, and we may be subject to product liability or regulatory enforcement actions, all of which could harm our business.

Further, as we enter new businesses or pursue new business opportunities internationally, such as opportunities that require clinical trials, we may become subject to additional laws, rules and regulations. Becoming familiar with and implementing the infrastructure necessary to comply with these laws, rules and regulations is costly. In addition, failure to comply with these laws, rules and regulations could delay the introduction of new products and could adversely affect our business.

Manufacturing and selling a device internationally. We are also subject to laws and regulations that apply to manufacturers of radiation emitting devices and products utilizing radioactive materials, as well as laws and regulations of general applicability relating to matters such as environmental protection, safe working conditions, manufacturing practices and other matters. These are often comparable to, if not more stringent than, the equivalent regulations in the United States. Sales overseas are also affected by regulation of matters such as product standards, packaging, labeling, environmental and product recycling requirements, import and export restrictions, tariffs, duties and taxes.

In some countries, we rely on our foreign distributors and agents to assist us in complying with foreign regulatory requirements, and we cannot be sure that they will always do so. If we or any of our suppliers, distributors, agents or customers fail to comply with applicable international regulatory requirements or are perceived to potentially have failed to comply, we may face:

adverse publicity affecting both us and our customers;
investigations by governmental authorities;
fines, injunctions, civil penalties and criminal prosecutions;

increased difficulty in obtaining required approvals in foreign countries;
losses of clearances or approvals already granted;
seizures or recalls of our products or those of our customers;
delays in purchasing decisions by customers or cancellation of existing orders; and
the inability to sell our products in or to import our products into such countries.

Other applicable international regulations. We are subject to laws and regulations in foreign countries covering data privacy and other protection of health and employee information. Particularly within the EU/EEA/Switzerland area, data protection legislation is comprehensive and complex and there has been a recent trend toward more stringent enforcement of requirements regarding protection and confidentiality of personal data. Data protection authorities from the different member states of the EU may interpret the legislation differently, which adds to this complexity, and data protection is a dynamic field where guidance is often revised. Fully understanding and implementing this legislation could be quite costly and timely, which could adversely affect our business. Additionally, in some instances, in order to fulfill the requirements of applicable U.S. laws, we may be faced with deciding whether to comply with EU/EEA/Switzerland data protection rules. Failure or partial failure to comply with data protection rules and regulations across the EU/EEA/Switzerland area could result in substantial monetary fines. New data protection legislation that will entail substantial changes to the current legal framework, some stricter than before, some less strict, is expected to be enacted by the EU Commission in 2014.

We are also subject to international “fraud and abuse” laws and regulations, as well as false claims and misleading advertisement laws. From time to time, these laws and regulations may be revised or interpreted in ways that could make it more difficult for our customers to conduct their businesses, which could have an adverse effect on the demand for our products, and therefore our business and results of operations. The laws and regulations and their enforcement are constantly undergoing change, and we cannot predict what effect, if any, changes to these laws and regulations may have on our business.

THE AFFORDABLE CARE ACT INCLUDES PROVISIONS THAT MAY ADVERSELY AFFECT OUR BUSINESS AND RESULTS OF OPERATIONS, INCLUDING AN EXCISE TAX ON THE SALES OF MOST MEDICAL DEVICES

On March 23, 2010, President Obama signed into law the Affordable Care Act. While we are continuing to evaluate the Affordable Care Act, it could adversely impact the demand for our products and services, and therefore our financial position and results of operations, possibly materially.

Specifically, one of the components of the law is a 2.3% excise tax on sales of most medical devices, which include our Oncology Systems and VPT products, which started January 1, 2013. The Congressional Budget Office estimates that the total cost to the medical device industry could exceed $30 billion over ten years. This tax has had and may continue to have a negative impact on our gross margin and/or may lead our customers to reduce their orders for our products.

In addition, discussions relating to the Affordable Care Act have included the possibility for bundled reimbursement payments and accountable care organizations (“ACOs”). ACOs and bundled payment programs were established by the Affordable Care Act to reward integrated, efficient care and allow providers to share in any savings they achieve through the coordination of care and meeting certain mandated quality standards. ACOs and the bundled payment programs have primarily focused on primary care. However, some customers appear to be developing new partnerships across clinical specialties to prepare for the possibility of operating in an ACO environment and bundled reimbursement payments. These and other elements of the Affordable Care Act, including comparative effectiveness research, an independent payment advisory board, payment system reforms (including shared savings pilots) and the reporting of certain payments by us to healthcare professionals and hospitals (the “Physician Payment Sunshine Act”), could meaningfully change the way healthcare is developed and delivered, and may materially impact numerous

aspects of our business, including the demand and availability of our products, the reimbursement available for our products from governmental and third-party payors, and reduced medical procedure volumes. We believe that growth of the radiation oncology market, which includes both traditional radiation therapy as well as proton therapy, in the United States is being adversely impacted as customers' decision-making processes are complicated by the uncertainties surrounding the implementation of the Affordable Care Act and reimbursement rates for radiotherapy and radiosurgery, and that this uncertainty will likely continue into the next fiscal year and result in a high degree of variability of gross orders and revenue from quarter-to-quarter.

Various healthcare reform proposals have also emerged at the state level, and we are unable to predict which, if any of these proposals will be enacted. We are also unable to predict what effect ongoing uncertainty surrounding federal and state health reform proposals will have on our customer's purchasing decisions. However, an expansion in government's role in the U.S. healthcare industry may adversely affect our business, possibly materially.

CHANGES TO RADIATION ONCOLOGY AND OTHER REIMBURSEMENTS AND CHANGES IN INSURANCE DEDUCTIBLES AND ADMINISTRATION MAY AFFECT DEMAND FOR OUR PRODUCTS

Sales of our healthcare products indirectly depend on whether adequate reimbursement is available to our customers from a variety of sources, such as government healthcare insurance programs, including the Medicare and Medicaid programs; private insurance plans; health maintenance organizations; and preferred provider organizations. In general, employers and third-party payors in the United States have become increasingly cost-conscious, with higher deductibles imposed or encouraged in many medical plans. The imposition of higher deductibles tends to restrain individuals from seeking the same level of medical treatments as they might seek if the costs they bear are lower, particularly in the medical diagnostic portion of our business. Third party payors have also increased utilization controls related to the use of our products by healthcare providers.

Furthermore, there is no uniform policy on reimbursement among third-party payors, and we cannot be sure that third-party payors will reimburse our customers for procedures using our products that will enable us to achieve or maintain adequate sales and price levels for our products. Without adequate support from third-party payors, the market for our products may be limited.

Once Medicare has made a decision to provide reimbursement for a given treatment, these reimbursement rates are generally reviewed and adjusted by Medicare annually. Private third-party payors, although independent from Medicare, sometimes use portions of Medicare reimbursement policies and payment amounts in making their own reimbursement decisions. As a result, decisions by CMS to reimburse for a treatment, or changes to Medicare's reimbursement policies or reductions in payment amounts with respect to a treatment sometimes extend to third-party payor reimbursement policies and amounts for that treatment. We have seen our customers' decision-making process complicated by the uncertainty surrounding Medicare reimbursement rates for radiotherapy and radiosurgery in the United States. From time to time, CMS and third party payors may review and modify the factors upon which they rely to determine appropriate levels of reimbursement for cancer treatments. For example, CMS and third-party payors have begun to focus on the comparative effectiveness of radiation therapy versus other methods of cancer treatment, including surgery, and could modify reimbursement rates based on the results of comparative effectiveness studies. In addition, discussions relating to the Affordable Care Act have included the possibility for bundled reimbursement payments and ACOs. Any significant cuts in reimbursement rates or changes in reimbursement methodology or administration for radiotherapy, radiosurgery, proton therapy or brachytherapy, or concerns or proposals regarding further cuts or changes in methodology or administration, could further increase uncertainty, influence our customers' decisions, reduce demand for our products, cause customers to cancel orders and have a material adverse effect on our revenues and stock price.

Foreign governments also have their own healthcare reimbursement systems and we cannot be sure that adequate reimbursement will be made available with respect to our products under any foreign reimbursement system.

OUR RESULTS MAY BE IMPACTED BY CHANGES IN FOREIGN CURRENCY EXCHANGE RATES

Because our business is global and payments are generally made in local currency, fluctuations in foreign currency exchange rates can impact our results by affecting product demand, or our revenues and expenses, and/or the profitability in U.S. Dollars of products and services that we provide in foreign markets.

While we use hedging strategies to help offset the effect of fluctuations in foreign currency exchange rates, the protection these strategies provide is affected by the timing of transactions, and the effectiveness of the hedges, the number of transactions that are hedged and forecast volatility. If our hedging strategies do not offset these fluctuations, our revenues, margins and other operating results may be harmed. In addition, movement in foreign currency exchange rates could impact our financial results positively or negatively in one period and not another,

making it more difficult to compare our financial results from period to period.

In addition, long-term movements in foreign currency exchange rates can also affect the competitiveness of our products in the local currencies of our international customers. Even though our international sales are mostly in local currencies, our cost structure is weighted towards the U.S. Dollar. The volatility of the U.S. Dollar that we have experienced over the last several years has affected the competitiveness of our pricing against our foreign competitors, some of which may have cost structures based in other currencies, either helping or hindering our international order and revenue growth, thereby affecting our overall financial performance and results. Changes in monetary or other policies here and abroad, including as a result of economic instability or concerns about the downgrade and levels of sovereign debt, or in reaction thereto, would also likely affect foreign currency exchange rates. Furthermore, in the event that one or more European countries were to replace the Euro with another currency, our sales into these countries, or into Europe generally, would likely be adversely affected until such time as stable exchange rates are established.

WE ARE SUBJECT TO FEDERAL, STATE AND FOREIGN LAWS GOVERNING OUR BUSINESS PRACTICES WHICH, IF VIOLATED, COULD RESULT IN SUBSTANTIAL PENALTIES. ADDITIONALLY, CHALLENGES TO OR INVESTIGATION INTO OUR PRACTICES COULD CAUSE ADVERSE PUBLICITY AND BE COSTLY TO RESPOND TO AND THUS COULD HARM OUR BUSINESS

Laws and ethical rules governing interactions with healthcare providers. The Medicare and Medicaid "anti-kickback" laws, and similar state laws, prohibit payments or other remuneration that is intended to induce hospitals, physicians or others either to refer patients or to purchase, lease or order, or arrange for or recommend the purchase, lease or order of healthcare products or services for which payment may be made under federal and state healthcare programs, such as Medicare and Medicaid. These laws affect our sales, marketing and other promotional activities by limiting the kinds of financial arrangements we may have with hospitals, physicians or other potential purchasers of our products. They particularly impact how we structure our sales offerings, including discount practices, customer support, education and training programs, physician consulting, research grants and other service arrangements. These laws are broadly written, and it is often difficult to determine precisely how these laws will be applied to specific circumstances.

Federal and state "false claims" laws generally prohibit knowingly presenting, or causing to be presented, claims for payment from Medicare, Medicaid or other government payors that are false or fraudulent, or for items or services that were not provided as claimed. Although we do not submit claims directly to payors, manufacturers can be, and have been, held liable under these laws if they are deemed to "cause" the submission of false or fraudulent claims by providing inaccurate billing or coding information to customers, or through certain other activities, including promoting products for uses not approved or cleared by the FDA, which is called off-label promotion. Violating "anti-kickback" and "false claims" laws can result in civil and criminal penalties, which can be substantial, and potential mandatory or discretionary exclusion from healthcare programs for noncompliance. Even an unsuccessful challenge or investigation into our practices could cause adverse publicity, and be costly to defend, and thus could harm our business and results of operations. Additionally, several recently enacted state and federal laws, including the laws in Massachusetts and Vermont, and the federal Physician Payment Sunshine Act, now require, among other things, extensive tracking and maintenance of databases regarding the disclosure of equity ownership and payments to physicians, healthcare providers and hospitals. These laws require us to implement the necessary and costly infrastructure to track and report certain payments to healthcare providers. Failure to comply with these new tracking and reporting laws could subject us to significant civil monetary penalties.

We are subject to similar laws in foreign countries where we conduct business. For example, within the EU, the control of unlawful marketing activities is a matter of national law in each of the member states. The member states of the EU closely monitor perceived unlawful marketing activity by companies. We could face civil, criminal and administrative sanctions if any member state determines that we have breached our obligations under its national laws. Industry associations also closely monitor the activities of member companies. If these organizations or authorities name us as having breached our obligations under their regulations, rules or standards, our reputation would suffer and our business and financial condition could be adversely affected.

Anti-corruption laws and regulations. We are also subject to the U.S. Foreign Corrupt Practices Act and anti-corruption laws, and similar laws in foreign countries, such as the U.K. Bribery Act of 2010, which became effective on July 1, 2011, and the Law "On the Fundamentals of Health Protection in the Russian Federation," with a significant anti-corruption intent and effective since January 2012. In general, there is a worldwide trend to strengthen anticorruption laws and their enforcement, and the healthcare industry and medical equipment manufacturers have been particular targets of these investigation and enforcement efforts. Any violation of these laws by us or our agents or distributors could create a substantial liability for us, subject our officers and directors to personal liability and also cause a loss of reputation in the market. Transparency International's 2012 Corruption Perceptions Index measured the degree to which public sector corruption is perceived to exist in 174 countries around the world, and found that nearly

three quarters of the countries in the index, including many that we consider to be high growth areas for our products, such as China, India, Russia and Brazil, scored below 50, on a scale from 100 (very clean) to 0 (highly corrupt). We currently operate in many countries where the public sector is perceived as being more or highly corrupt. Our strategic business plans include expanding our business in regions and countries that are rated as higher risk for corruption activity by Transparency International. Becoming familiar with and implementing the infrastructure necessary to comply with laws, rules and regulations applicable to new business activities and mitigate and protect against corruption risks could be quite costly. In addition, failure by us or our agents or distributors to comply with these laws, rules and regulations could delay our expansion into high-growth markets and could adversely affect our business. This notwithstanding, we will inevitably do more business, directly and potentially indirectly in countries, where the public sector is perceived to be more or highly corrupt and be engaging in business in more countries perceived to be more or highly corrupt. Increased business in higher risk countries could subject us and our officers and directors to increased scrutiny and increased liability. In addition, we have conducted, and in the future expect to conduct internal investigations or face audits or investigations by one or more domestic or foreign government agencies, which could be costly and time-consuming, and could divert our management and key personnel from our business operations. An adverse outcome under any such investigation or audit could subject us to fines or criminal or other penalties, which could adversely affect our business and financial results.

Competition laws. Due to our competitive position in many jurisdictions, compliance with competition laws is of increased importance to us. Regulatory authorities under whose laws we operate may have enforcement powers that can subject us to sanctions, and can impose changes or conditions in the way we conduct our business. In addition, an increasing number of jurisdictions also provide private rights of action for competitors or consumers to seek damages asserting claims of anti-competitive conduct. Increased government scrutiny of our actions or enforcement or private rights of action could adversely affect our business or damage our reputation. In addition, we have conducted, and in the future expect to conduct, internal investigations or face audits or investigations by one or more domestic or foreign government agencies, which could be costly and time-consuming, and could divert our management and key personnel from our business operations. An adverse outcome under any such investigation or audit could subject us to fines or criminal or other penalties, which could adversely affect our business and financial results.

PRODUCT DEFECTS OR MISUSE MAY RESULT IN MATERIAL PRODUCT LIABILITY OR PROFESSIONAL ERRORS AND OMISSIONS CLAIMS, LITIGATION, INVESTIGATION BY REGULATORY AUTHORITIES OR PRODUCT RECALLS THAT COULD HARM FUTURE REVENUES AND REQUIRE US TO PAY MATERIAL UNINSURED CLAIMS

Our business exposes us to potential product liability claims that are inherent in the manufacture, sale, installation, servicing and support of medical devices and other devices that deliver radiation. Because our products are involved in the intentional delivery of radiation to the human body and other situations where people may come in contact with radiation (for example, when our SIP products are being used to scan cargo), the collection and storage of patient treatment data for medical analysis and treatment delivery, the planning of radiation treatment and diagnostic imaging of the human body, and the diagnosing of medical problems, the possibility for significant injury and/or death exists to the intended or unintended recipient of the delivery. Our medical products operate within our customers' facilities and network systems, and under quality assurance procedures established by the facility that ultimately result in the delivery of radiation to patients. Human and other errors or accidents may arise from the operation of our products in complex environments, particularly with products from other vendors, where interoperability or data sharing protocol may not be optimized even though the equipment or system operates according to specifications. As a result, we may face substantial liability to patients, our customers and others for damages resulting from the faulty, or allegedly faulty, design, manufacture, installation, servicing, support, testing or interoperability of our products with other products, or their misuse or failure. In addition, third party service providers could fail to adequately perform their obligations, which could subject us to further liability. We may also be subject to claims for property damages or economic loss related to or resulting from any errors or defects in our products, or the installation, servicing and support of our products. Any accident or mistreatment could subject us to legal costs, litigation, adverse publicity and damage to our reputation, whether or not our products or services were a factor. In connection with our products that collect and store patient treatment data, we may be liable for the loss or misuse of such private data, if those products fail or are otherwise defective.

Product liability actions are subject to significant uncertainty and may be expensive, time-consuming, and disruptive to our operations. For these and other reasons, we may choose to settle product liability claims against us, regardless of their actual merit. If a product liability action were finally determined against us, it could result in significant damages, including the possibility of punitive damages and our consolidated financial position, results of operations or cash flows could be materially adversely affected. Adverse publicity regarding any accidents or mistreatments, even ones that do not involve our products, could cause patients to be less receptive to radiotherapy or radiosurgery treatments, to question the efficacy of radiation therapy and radiosurgery and to seek other methods of treatment. Adverse publicity could also result in additional regulation of radiation therapy, radiosurgery, medical devices or the healthcare industry in general, and adversely affect our ability to promote, manufacture and sell our products. Both adverse publicity and increased regulatory activities could negatively impact our business and results of operations.

In addition, if a product we design or manufacture were defective (whether due to design, labeling or manufacturing defects, improper use of the product or other reasons), we may be required to correct or recall the product and notify regulatory authorities. The adverse publicity resulting from a correction or recall could damage our reputation and cause customers to review and potentially terminate their relationships with us. A product correction or recall could consume management time and have an adverse financial impact on our business, including incurring substantial costs, losing revenues and accruing losses under GAAP.

We maintain limited product liability insurance coverage and currently self-insure professional liability/errors and omissions liability. Our product liability insurance policies are expensive and have high deductible amounts and self-insured retentions. Our insurance coverage may also prove to be inadequate, and future policies may not be available on acceptable terms or in sufficient amounts, if at all. If a material claim is successfully brought against us relating to a self-insured liability or a liability that is in excess of our insurance coverage, or for which insurance coverage is denied or limited, we could have to pay substantial damages, which could have a material adverse effect on our financial position and results of operation.

WE COMPETE IN HIGHLY COMPETITIVE MARKETS, AND WE MAY LOSE MARKET SHARE TO COMPANIES WITH GREATER RESOURCES OR THE ABILITY TO DEVELOP MORE EFFECTIVE TECHNOLOGIES, OR WE COULD BE FORCED TO REDUCE OUR PRICES

Rapidly evolving technology, intense competition and pricing pressure characterize the markets for radiation therapy equipment and software. New competitors may enter our markets, and we have encountered new competitors as we have entered new markets such as radiosurgery, volumetric modulated arc therapy and proton therapy. Some of these competitors may have greater financial, marketing and other resources than we have. To compete successfully, we must provide technically superior, clinically proven products that deliver more precise, cost-effective, high quality clinical outcomes, in a complete package of products and services, and do so ahead of our competitors. As our Oncology Systems products are generally sold on a basis of total value to the customer, our business may suffer when purchase decisions are based solely upon price, which can happen if hospitals and clinics give purchasing decision authority to group purchasing organizations. The shift in the proportion of sales within our international region towards emerging market countries, which typically have purchased less complex, lower-priced products compared to more developed countries and which usually have stiffer price competition, could also adversely impact our results of operations. New competitors may also delay customer purchasing decisions as customers evaluate the products of these competitors along with ours, potentially extending our sales cycle and adversely affecting our gross orders.

In Imaging Components, we often compete with companies that have greater financial, marketing and other resources than we have. Some of the major diagnostic imaging systems companies, which are the primary OEM customers for our X-ray components, also manufacture X-ray components, including X-ray tubes, for use in their own imaging systems products. We must compete with these in-house manufacturing operations for business from their affiliated companies. In addition, we compete against other stand-alone, independent X-ray tube manufacturers who compete with us for both the OEM business of major diagnostic imaging equipment manufacturers and the independent servicing business for X-ray tubes. The market for flat panel detectors is also very competitive. As a result, we must have an advantage in one or more significant areas, which may include lower product cost, better product quality and/or superior technology and/or performance.

With our security and inspection products, we compete with other OEM suppliers, primarily outside of the United States. The market for our X-ray tube and panel products used for nondestructive testing in industrial applications is small and highly fragmented.

The market for proton therapy products is still developing and is characterized by rapidly evolving technology and pricing pressure. Our ability to compete successfully depends, in part, on our ability to lower our product costs, develop and provide technically superior, clinically proven products that deliver more precise, cost-effective, high quality clinical outcomes, including integration of technologies such as our On-Board Imager (“OBI”) for IGRT and our motion management technologies.

In each of our business segments, existing competitors’ actions and new entrants may adversely affect our ability to compete. These competitors could develop technologies and products that are more effective than those we currently use or produce or that could render our products obsolete or noncompetitive. In addition, the timing of our competitors’ introduction of products into the market could affect the market acceptance and market share of our products. Some competitors offer specialized products that provide, or may be perceived by customers to provide, a marketing advantage over our mainstream cancer treatment products. Also, some of our competitors may not be subject to the same standards, regulatory and/or other legal requirements that we are, and therefore, they could have a competitive advantage in developing, manufacturing and marketing products and services. Any inability to develop, gain regulatory approval for and supply commercial quantities of competitive products to the market as quickly and effectively as our competitors could limit market acceptance of our products and reduce our sales. In addition, some of our smaller competitors could be acquired by larger companies that have greater financial strength, which could

enable them to compete more aggressively. Our competitors could also acquire some of our suppliers or distributors, which could disrupt these supply or distribution arrangements and result in less predictable and reduced revenues in our businesses. Any of these competitive factors could negatively affect our pricing, sales, revenues, market share and gross margins and our ability to maintain or increase our operating margins.

OPEN ARCHITECTURE IS BECOMING INCREASINGLY IMPORTANT, AND SALES OF OUR PRODUCTS COULD FALL IF WE FAIL TO ACHIEVE THIS

As radiation oncology treatment becomes more complex, our customers are increasingly focusing on ease-of-use and interconnectivity. Our equipment and software are highly sophisticated and require a high level of training and education to use them competently and safely—requirements made even more important because they work together within integrated environments. We have directed substantial product development efforts into (i) increasing the interconnectivity of our products for more seamless operation within a system, (ii) making our software products easier to use and (iii) reducing setup and treatment times to increase patient throughput. We have emphasized an "open systems" approach that allows customers to "mix and match" our individual products, incorporate products from other manufacturers, share information with other systems or products and use the equipment for offering various methods of radiation and chemotherapy treatment. We have done this based on our belief that such interconnectivity will increase the acceptance and adoption of IMRT, IGRT and volumetric modulated arc therapy and will stimulate demand for our products. There are competitive "closed-ended" dedicated-use systems, however, that place simplicity of use ahead of flexibility. If we have misjudged the importance to our customers of maintaining an "open systems" approach, or if we are unsuccessful in our efforts to increase interconnectivity, enhance ease-of-use and reduce setup and treatment times, our revenues could suffer.

Obtaining and maintaining interoperability and compatibility can be costly and time-consuming. While we try to use standard published protocols for communication with widely used oncology products manufactured by other companies, if we cannot do this, we may need to develop individual interfaces so that our products communicate correctly with the other company products. When other companies modify the design or functionality of their products, this may affect their compatibility with our products. In addition, when we improve our products, customers may be reluctant to adopt our new technology due to potential interoperability issues. For example, a clinic may be unwilling to implement one of our new technologies because its third-party software does not yet communicate correctly with our new product. Our ability to obtain compatibility with products of other companies may depend on our ability to obtain adequate information from them regarding their products. In many cases, these third parties are our competitors and may schedule their product changes and delay their release of relevant information to place us at a competitive disadvantage. When we modify our products to make them interoperable or compatible with third-party products, we may be required to obtain additional regulatory clearances. This process is costly and could delay our ability to release our products for commercial use. It is also possible that, despite our best efforts, we may not be able to make our products interoperable or compatible with widely used third-party products or may only be able to do so at a prohibitive expense, making our products less attractive or more costly to our customers.

PROTECTING OUR INTELLECTUAL PROPERTY CAN BE COSTLY AND WE MAY NOT BE ABLE TO MAINTAIN LICENSED RIGHTS, AND IN EITHER CASE OUR COMPETITIVE POSITION WOULD BE HARMED IF WE ARE NOT ABLE TO DO SO

We file applications as appropriate for patents covering new products and manufacturing processes. We cannot be sure, however, that our current patents, the claims allowed under our current patents, or patents for technologies licensed to us will be sufficiently broad to protect our technology position against competitors. Issued patents owned by, or licensed to, us may be challenged, invalidated or circumvented, or the rights granted under the patents may not provide us with competitive advantages. We also cannot be sure that patents will be issued from any of our pending or future patent applications. Asserting our patent rights against others in litigation or other legal proceedings is costly and diverts managerial resources. An unfavorable outcome in any such litigation or proceeding could harm us. In addition, we may not be able to detect patent infringement by others or may lose our competitive position in the market before we are able to do so.

We also rely on a combination of copyright, trade secret and other laws, and contractual restrictions on disclosure, copying and transferring title (including confidentiality agreements with vendors, strategic partners, co-developers, employees, consultants and other third parties), to protect our proprietary and other confidential rights. These protections may prove inadequate, since agreements may still be breached and we may not have adequate remedies for a breach, and our trade secrets may otherwise become known to or be independently developed by others. In the event that our proprietary or confidential information is misappropriated, our business and financial results could be adversely impacted. We have trademarks, both registered and unregistered, that are maintained and enforced to provide customer recognition for our products in the marketplace, but unauthorized third parties may still use them. We also have agreements with third parties that license to us certain patented or proprietary technologies. In some cases products with substantial revenues may depend on these license rights. If we were to lose the rights to license these technologies, or our costs to license these technologies were to materially increase, our business would suffer.

THIRD PARTIES MAY CLAIM WE ARE INFRINGING THEIR INTELLECTUAL PROPERTY, AND WE COULD SUFFER SIGNIFICANT LITIGATION OR LICENSING EXPENSES OR BE PREVENTED FROM SELLING OUR PRODUCTS

There is a substantial amount of litigation over patent and other intellectual property rights in the industries in which we compete. Our competitors, like companies in many high technology businesses, continually review other companies' activities for possible conflicts with their own intellectual property rights. In addition, non-practicing entities may review our activities for conflicts with their patent rights. Determining whether a product infringes a third party's intellectual property rights involves complex legal and factual issues, and the outcome of this type of litigation is often uncertain. Third parties may claim that we are infringing their intellectual property rights. We may not be aware of intellectual property rights of others that relate to our products, services or technologies. From time to time, we have received notices from third parties asserting infringement and we have been subject to lawsuits alleging infringement of third-party patent or other intellectual property rights. For example, we recently settled a patent infringement lawsuit relating to our Real-time Position Management™ technology initiated in 2007 by the University of Pittsburgh. Any dispute regarding patents or other intellectual property could be costly and time-consuming, and could divert our management and key personnel from our business operations. We may not prevail in a dispute. We do not maintain insurance for intellectual property infringement, so costs of defense, whether or not we are successful in defending an infringement claim, will be borne by us and could be significant. If we are unsuccessful in defending or appealing an infringement claim, we may be subject to significant damages and our consolidated financial position, results of operations or cash flows could be materially adversely affected. If actual liabilities significantly exceed our estimates regarding potential liabilities, our consolidated financial position, results of operations or cash flows could be materially adversely affected. We may also be subject to injunctions against development and sale of our products, the effect of which could be to materially reduce our revenues. Furthermore, even if a third party rights holder is willing to license its rights to us, the amounts we might be required to pay under the associated royalty or license agreement could be significant.

UNFAVORABLE RESULTS OF LEGAL PROCEEDINGS COULD MATERIALLY ADVERSELY AFFECT OUR FINANCIAL RESULTS

From time to time, we are a party to or otherwise involved in legal proceedings, claims and government inspections or investigations and other legal matters, both inside and outside the United States, arising in the ordinary course of our business or otherwise. We are currently involved in various legal proceedings and claims, including product liability and intellectual property claims, that have not yet been fully resolved and additional claims may arise in the future. Legal proceedings are often lengthy, taking place over a period of years with interim motions or judgments subject to multiple levels of review (such as appeals or rehearings) before the outcome is final. Litigation is subject to significant uncertainty and may be expensive, time-consuming, and disruptive to our operations. For these and other reasons, we may choose to settle legal proceedings and claims, regardless of their actual merit.

If a legal proceeding were finally resolved against us, it could result in significant compensatory damages, and in certain circumstances punitive or trebled damages, disgorgement of revenue or profits, remedial corporate measures or injunctive relief imposed on us. If our existing insurance does not cover the amount or types of damages awarded, or if other resolution or actions taken as a result of the legal proceeding were to restrain our ability to market one or more of our material products or services, our consolidated financial position, results of operations or cash flows could be materially adversely affected. In addition, legal proceedings, and any adverse resolution thereof, can result in adverse publicity and damage to our reputation, which could adversely impact our business.

THE LOSS OF A SUPPLIER OR ANY INABILITY TO OBTAIN SUPPLIES OF IMPORTANT COMPONENTS COULD RESTRICT OUR ABILITY TO MANUFACTURE PRODUCTS, CAUSE DELAYS IN OUR ABILITY TO DELIVER PRODUCTS, OR SIGNIFICANTLY INCREASE OUR COSTS

We obtain some of the components included in our products from a limited group of suppliers or from a single source supplier, such as the radioactive sources for high dose afterloaders, klystrons for linear accelerators; transistor arrays and cesium iodide coatings for flat panel detectors, and specialized integrated circuits, X-ray tube targets, housings, glassframes and various other components; and radiofrequency components, magnets and gantry hardware for proton therapy systems. If we lose any of these suppliers, if their operations were substantially interrupted, or if any of them failed to meet performance or quality specifications, we may be required to obtain and qualify one or more replacement suppliers. This may then also require us to redesign or modify our products to incorporate new parts and/or further require us to obtain clearance, qualification or certification of these products by the FDA or obtain other applicable regulatory approvals in other countries. Events like these could significantly increase costs for the affected product and likely cause material delays in delivery of that and other related products. Although we have insurance to protect against business interruption loss, this insurance coverage may not be adequate or continue to remain available on acceptable terms, if at all. Furthermore, some of our single-source suppliers provide components for some of our rapidly growing product lines. Manufacturing capacity limitations of any of our suppliers or other inability of these suppliers to meet increasing demand could adversely affect us, resulting in curtailed growth opportunities for our affected product lines. Shortage of, and greater demand for, components and subassemblies could also increase manufacturing costs if the supply/demand imbalance increases the price of the components and subassemblies. Disruptions or loss of any of our limited- or sole-sourced components or subassemblies or the capacity limitations of the suppliers for these components or subassemblies, including the ones referenced above, could adversely affect our business and financial results and could damage our customer relationships.

A SHORTAGE OR CHANGE IN SOURCE OF RAW MATERIALS COULD RESTRICT OUR ABILITY TO MANUFACTURE PRODUCTS, CAUSE DELAYS, OR SIGNIFICANTLY INCREASE OUR COST OF GOODS

We rely upon the supplies of certain raw materials such as tungsten, lead, iridium and copper for Oncology Systems and SIP; copper, lead, tungsten, rhenium, molybdenum zirconium, and various high grades of steel alloy for X-ray tubes, and high-grade steel, high-grade copper and iron for VPT. Worldwide demand, availability and pricing of these raw materials have been volatile, and we expect that availability and pricing will continue to fluctuate in the future. If supplies are restricted or become unavailable or if prices increase, this could constrain our manufacturing of affected products, reduce our profit margins or otherwise adversely affect our business.

Pursuant to the Dodd-Frank Wall Street Reform and Consumer Protection Act, the SEC has promulgated rules regarding disclosure of the presence in a company’s products of certain metals, known as “conflict minerals,” which are metals mined from the Democratic Republic of the Congo and adjoining countries, as well as procedures regarding a manufacturer’s efforts to identify the sourcing of those minerals from this region. Complying with these rules requires investigative efforts, which has and will continue to cause us to incur associated costs, and could adversely affect the sourcing, supply, and pricing of materials used in our products, or result in process or manufacturing modifications, all of which could adversely affect our results of operations.

CONSOLIDATION AMONG OUR ONCOLOGY SYSTEMS CUSTOMERS COULD ADVERSELY AFFECT OUR SALES OF ONCOLOGY PRODUCTS

We have seen and may continue to see some consolidation among our customers in our Oncology Systems business, as hospitals and clinics combine through mergers and acquisitions, and as they join group purchasing organizations or affiliated enterprises. In addition, we have seen and may continue to see integration of equipment and information systems among hospitals as they consolidate their networks. As customers consolidate and/or integrate, the volume of

product sales to these customers might decrease. Alternatively, order size may increase, as what were previously more than one customer combine orders as one entity, or as groups of organizations combine their purchases. As a result, as orders increase in size and require more customer approvals, the purchasing cycle for our Oncology Systems products could lengthen. Both increased order size and extended purchasing cycles could cause our gross orders to be more volatile and less predictable. In addition, some customers appear to be developing new partnerships across clinical specialties to prepare for the possibility of operating in an ACO environment and the possibility of bundled reimbursement payments. Group purchasing organizations often focus on pricing as the determinant in making purchase decisions. A reduction in gross orders could affect the level of future revenues, which would adversely affect our operating results, financial condition, and the price of VMS common stock.

WE SELL OUR IMAGING COMPONENTS TO A LIMITED NUMBER OF OEM CUSTOMERS, MANY OF WHICH ARE ALSO OUR COMPETITORS, AND A REDUCTION IN BUSINESS OR INABILITY TO PROPERLY FORECAST SALES BY ONE OR MORE OF THESE CUSTOMERS COULD REDUCE OUR SALES

We sell our X-ray tube products to a limited number of OEM customers, many of which are also our competitors with in-house X-ray tube manufacturing operations. If these customers manufacture a greater percentage of their components in-house or otherwise lower external sourcing costs, we could experience reduction in purchasing volume by, or loss of, one or more of these customers. Such a reduction or loss could have a material adverse effect on our Imaging Components business. In addition, economic uncertainties over the past few years and, in Japan, the power outages, facility closures and other effects of the 2011 tsunami, have made it difficult for our OEM customers to accurately forecast and plan future business activities. Such economic uncertainties and natural disasters, as well as other factors, have previously impacted our Imaging Components business with inventory reduction efforts and slowdowns in sales at some of these customers. Similar inventory adjustments and slowdowns in sales could occur in the future. Our agreements for imaging components may contain purchasing estimates that are based on our customers' historical purchasing patterns, and actual purchasing volumes under the agreements may vary significantly from these estimates.

ORDERS FOR OUR SECURITY AND INSPECTION PRODUCTS COULD BE UNPREDICTABLE

Our Imaging Components business designs, manufactures, sells and services Linatron X-ray accelerators, imaging processing software and image detection products for security and inspection, such as cargo screening at ports and borders and nondestructive examination for a variety of applications, as well as industrial applications. We generally sell security and inspection products to OEMs who incorporate our products into their inspection systems, which are then sold to customs and other government agencies, as well as to commercial organizations in the casting, power, aerospace, chemical, petro-chemical and automotive industries. We believe growth in our security and inspection products will be driven by security cargo screening and border protection needs, as well as by the needs of customs agencies to verify shipments for assessing duties and taxes. Orders for our security and inspection products have been and may continue to be unpredictable as governmental agencies may place large orders with us or our OEM customers in a short time period, and then may not place any orders for a long time period thereafter. Because it is difficult to predict our OEM customer delivery, the actual timing of sales and revenue recognition varies significantly.

In addition, demand for our security and inspection products is heavily influenced by U.S. and foreign governmental policies on national and homeland security, border protection and customs revenue activities, which depend upon government budgets and appropriations that are subject to economic conditions, as well as political changes. We have seen customers freeze or dramatically reduce purchases and capital project expenditures, delay projects, or act cautiously as governments around the world wrestle with spending priorities. As economic growth remains sluggish in various jurisdictions and appears to be deteriorating in others, and as concerns about levels of government employment and government debt continue, we expect that these effects will also continue. Furthermore, bid awards in this business may be subject to challenge by third parties, as we have previously encountered with a large government project. These factors make the timing of orders, sales and revenues in this business more unpredictable and could cause volatility in our revenues and earnings, and therefore the price of VMS common stock.

IF WE ARE UNABLE TO PROVIDE THE SIGNIFICANT EDUCATION AND TRAINING REQUIRED FOR THE HEALTHCARE MARKET TO ACCEPT OUR PRODUCTS, OUR BUSINESS WILL SUFFER

In order to achieve market acceptance for our radiation therapy products, we often need to educate physicians about the use of new treatment procedures such as IMRT, IGRT, volumetric modulated arc therapy, stereotactic radiotherapy, stereotactic radiosurgery, stereotactic body radiation therapy or proton therapy, overcome physician objections to some of the effects of the product or its related treatment regimen, convince healthcare payors that the

benefits of the product and its related treatment process outweigh its costs and help train qualified physicists in the skilled use of the product. For example, the complex and dynamic nature of IMRT and IGRT requires significant education of hospital personnel and physicians regarding the benefits of and practices associated with IMRT and IGRT. Further, the complexity and high cost of proton therapy requires similar significant education, as well as education regarding construction and facility requirements. We have devoted and will continue to devote significant resources on marketing and educational efforts to create awareness of IMRT, IGRT, volumetric modulated arc therapy, stereotactic radiotherapy, stereotactic radiosurgery, stereotactic body radiation therapy and proton therapy generally, to encourage the acceptance and adoption of our products for these technologies and to promote the safe and effective use of our products in compliance with their operating procedures. Future products may not gain adequate market acceptance among physicians, patients and healthcare payors, even if we spend significant time and expense on their education.

OUR BUSINESS MAY SUFFER IF WE ARE NOT ABLE TO HIRE AND RETAIN QUALIFIED PERSONNEL

Our future success depends, to a great degree, on our ability to retain, attract, expand, integrate and train our management team and other key personnel, such as qualified engineering, service, sales, marketing and other staff. We compete for key personnel with other medical equipment and software manufacturers and technology companies, as well as universities and research institutions. Because this competition is intense, compensation-related costs could increase significantly if the supply of qualified personnel decreases or demand increases. If we are unable to hire and train qualified personnel, we may not be able to maintain or expand our business. Additionally, if we are unable to retain key personnel, we may not be able to replace them readily or on terms that are reasonable, which also could hurt our business.

IF WE ARE NOT ABLE TO MATCH OUR MANUFACTURING CAPACITY WITH DEMAND FOR OUR PRODUCTS, OUR FINANCIAL RESULTS MAY SUFFER

Many of our products have a long production cycle, and we need to anticipate demand for our products in order to ensure adequate manufacturing or testing capacity. If we are unable to anticipate demand and our manufacturing or testing capacity does not keep pace with product demand, we will not be able to fulfill orders in a timely manner, which may negatively impact our financial results and overall business. Conversely, if demand for our products decreases, the fixed costs associated with excess manufacturing capacity may harm our financial results.

WE MAY NOT REALIZE EXPECTED BENEFITS FROM ACQUISITIONS OF OR INVESTMENTS IN NEW BUSINESSES, PRODUCTS, OR TECHNOLOGIES, WHICH COULD HARM OUR BUSINESS

We need to grow our businesses in response to changing technologies, customer demands and competitive pressures. In some circumstances, we may decide to grow our business through the acquisition of complementary businesses, products or technologies rather than through internal development. For example, in the third quarter of fiscal year 2014 we acquired certain assets of Velocity Medical Solutions, LLC, a privately-held Atlanta-based developer of specialized software for cancer clinics. Identifying suitable acquisition candidates can be difficult, time-consuming and costly, and we may not be able to identify suitable candidates or successfully complete identified acquisitions. In addition, completing an acquisition can divert our management and key personnel from our current business operations, which could harm our business and affect our financial results. Even if we complete an acquisition, we may not be able to successfully integrate newly acquired organizations, products, technologies or employees into our operations, or may not fully realize some of the expected synergies.

Integrating an acquisition can also be expensive and time-consuming, and may strain our resources. It may cost us more to commercialize new products than we originally anticipated, as we experienced with our proton therapy systems, or cause us to increase our expenses related to research and development, either of which could impact our results of operations. In many instances, integrating a new business will also involve implementing or improving internal controls appropriate for a public company at a business that lacks them. In addition, we may be unable to retain the employees of acquired companies, or the acquired company’s customers, suppliers, distributors or other partners for a variety of reasons, including the fact that these entities may be our competitors or may have close relationships with our competitors.

Further, we may find that we need to restructure or divest acquired businesses, or assets of those businesses. Even if we do so, an acquisition may not produce the full efficiencies, growth or benefits we expected. If we decide to sell assets or a business, as we did in fiscal year 2008 with the scientific research instruments business that we acquired as part of our acquisition of ACCEL GmbH, it may be difficult to identify buyers or alternative exit strategies on acceptable terms, in a timely manner, or at all, which could delay the accomplishment of our strategic objectives. We may be required to dispose of a business at a lower price or on less advantageous terms, or to recognize greater losses,

than we had anticipated.

We account for our acquisitions under the purchase method of accounting. Under this method, we allocate the total purchase price to the acquired businesses' tangible assets and liabilities, identifiable intangible assets and in-process research and development costs based on their fair values as of the date of the acquisition, and record the excess of the purchase price over those fair values as goodwill. If we fail to achieve the anticipated growth from an acquisition, or if we decide to sell assets or a business, we may be required to recognize an impairment loss on the write down of our assets and goodwill, which could adversely affect our financial results. In addition, acquisitions can result in potentially dilutive issuances of equity securities or the incurrence of debt, contingent liabilities or expenses, or other charges, any of which could harm our business and affect our financial results.

Additionally, we have investments in privately held companies that are subject to risk of loss of investment capital. These investments are inherently risky, in some instances because the markets for the technologies or products these companies have under development may never materialize. If these companies do not succeed, we could lose some or all of our investment in these companies. For example, in the third quarter of fiscal year 2014, we recorded a charge relating to the impairment of a portion of a privately-held equity investment when we became aware of certain indicators of impairment.

WE MAY FACE ADDITIONAL RISKS FROM THE ACQUISITION OR DEVELOPMENT OF NEW LINES OF BUSINESS

From time to time, we may acquire or develop new lines of business, such as proton therapy. There are substantial risks and uncertainties associated with new lines of business, particularly in instances where the markets are not fully developed. Risks include developing knowledge of and experience in the new business, recruiting market professionals, increasing research and development expenditures, and developing and capitalizing on new relationships with experienced market participants. This may mean significant investment and involvement of our senior management to acquire or develop, then integrate, the business into our operations. Timelines for integration of new businesses may not be achieved and price and profitability targets may not prove feasible, as new products can carry lower gross margins than existing products. External factors, such as compliance with regulations, competitive alternatives, and shifting market preferences, may also impact whether implementation of a new business will be successful. Failure to manage these risks could have a material adverse effect on our business, results of operations and financial condition.

WE WORK WITH DISTRIBUTORS FOR SALES IN SOME TERRITORIES, AND LOSING THEM COULD HARM OUR REVENUES IN THAT TERRITORY

We have strategic relationships with a number of key distributors, including Siemens AG, for sales and service of our products. If these strategic relationships end and are not replaced, our revenues from product sales in these territories and/or ability to service our products in the territories serviced by these distributors could be adversely affected.

FLUCTUATIONS IN OUR OPERATING RESULTS, INCLUDING QUARTERLY GROSS ORDERS, REVENUES, AND MARGINS, MAY CAUSE OUR STOCK PRICE TO BE VOLATILE, WHICH COULD CAUSE LOSSES FOR OUR STOCKHOLDERS

We have experienced and expect in the future to experience fluctuations in our operating results, including gross orders, revenues and margins, from period to period. Drivers of orders include the introduction and timing of announcement of new products or product enhancements by us and our competitors, as well as changes or anticipated changes in third party reimbursement amounts or policies applicable to treatments using our products. The availability of economic stimulus packages or other government funding, or reductions thereof, may also affect timing of customer purchases. Many of our products require significant capital expenditures by our customers. Accordingly, individual product orders can be quite large in dollar amounts, which can extend the customer purchasing cycle. We have experienced this with our IGRT products, and it is especially true with our proton therapy products because of the high cost of the proton therapy equipment and the complexity of project financing. In addition, the budgeting cycles of hospitals and clinics for capital equipment purchases are frequently fixed well in advance. Economic uncertainty also tends to extend the purchasing cycle as potential customers more closely scrutinize and prioritize their capital spending budgets, and analyze appropriate financing alternatives. In addition, some of our more sophisticated equipment, such as IGRT and proton therapy products, requires greater site preparation and longer construction cycles, which can delay customer decision cycles and the placement of orders even further. When orders are placed, installation is accomplished and the revenues recognized affect our quarterly results.

Once orders are received and booked into backlog, factors that may affect whether these orders become revenue (or are cancelled or deemed dormant and reflected as a reduction in the net order amounts) and the timing of revenue include:

- delay in shipment due, for example, to an unanticipated construction delay at a customer location where our products are to be installed, cancellations or reschedulings by customers, extreme weather conditions, natural disasters, port strikes or other labor actions;

- a challenge to a bid award for one or more of our products;
- delay in the installation and/or acceptance of a product;
- failure to satisfy contingencies associated with an order;
- the method of accounting used to recognize revenue;
- a change in a customer's financial condition or ability to obtain financing; or
- timing of necessary regulatory approvals or authorizations.

Our quarterly operating results, including our margins, may also be affected by a number of other factors, including:

- changes in our or our competitors' pricing or discount levels;
- changes in foreign currency exchange rates;
- changes in the relative portion of our revenues represented by our various products, including the relative mix between higher margin and lower margin products;

- changes in the relative portion of our revenues represented by our international region as a whole, by regions within the overall region, as well as by individual countries (notably those in emerging markets);
- fluctuation in our effective tax rate, which may or may not be known to us in advance;
- changes to our organizational structure, which may result in restructuring or other charges;
- disruptions in the supply or changes in the costs of raw materials, labor, product components or transportation services;
- disruptions in our operations, including our ability to manufacture products, caused by events such as earthquakes, fires, floods, terrorist attacks or the outbreak of epidemic diseases;
- the impact of changing levels of sales on sole purchasers of certain of our imaging components;
- the unfavorable outcome of any litigation or administrative proceeding or inquiry, as well as ongoing costs associated with legal proceedings; and
- accounting changes and adoption of new accounting pronouncements.

Because many of our operating expenses are based on anticipated capacity levels and a high percentage of these expenses are fixed for the short term, a small variation in the timing of revenue recognition can cause significant variations in operating results from quarter to quarter. Our overall gross margin may also be impacted by the gross margin of our proton therapy products, which are presently below the gross margins for our traditional radiotherapy products and particularly prior to completion because the associated revenues are being accounted for in accordance with the zero profit, percentage-of-completion method. If our gross margins fall below the expectation of securities analysts and investors, the trading price of VMS common stock would almost certainly decline.

We report on a quarterly and annual basis our gross orders and backlog. It is important to understand that, unlike revenues, gross orders and backlog are not governed by GAAP, and are not within the scope of the audit conducted by our independent registered public accounting firm; therefore, investors should not interpret our gross orders or backlog in such a manner. Also, for the reasons set forth above, our gross orders and backlog cannot necessarily be relied upon as accurate predictors of future revenues. Order cancellation or delays in customer purchase decisions or delivery dates will reduce our backlog and future revenues, and we cannot predict if or when orders will mature into revenues. Particularly high levels of cancellations in one period will make it difficult to compare our operating results. Our gross orders, backlog, revenues and net earnings in one or more future periods may fall below the expectations of securities analysts and investors. In that event, the trading price of VMS common stock would almost certainly decline.

THE FINANCIAL RESULTS OF OUR VARIAN PARTICLE THERAPY BUSINESS MAY FLUCTUATE AND BE UNPREDICTABLE

The development of our VPT business enables us to offer products for delivering image-guided, intensity-modulated proton therapy for the treatment of cancer. Our success in this area will depend upon the wide-spread awareness, acceptance and adoption by the oncology market of proton therapy systems for the treatment of cancer. However, this technology has not been widely adopted and future developments may not be adopted as quickly as others.

Since proton therapy projects are generally large, highly customized and more complex than projects in our Oncology Systems radiotherapy business, planning for these projects takes more of our time and uses more of our resources. Many of the components used in proton therapy equipment require long lead times, which may require an increase in our inventory levels. This may cause fluctuations in the operating results of VPT that may make it difficult to predict our results and to compare our results from period to period. The construction of a proton therapy facility requires significant capital investment and may involve complex project financing. Consequently, this business is vulnerable to deterioration in general economic and market conditions. The worldwide economic downturn resulted in a contraction in credit markets. This has made and may continue to make it more difficult for potential customers of this business to find appropriate financing for large proton therapy projects, which could cause them to delay or cancel their projects, or request that we participate in financing arrangements (such as we did for the Scripps Proton Therapy Center) or

make payment concessions in their agreements with us, which could impact our operating results. Challenges or delays in obtaining financing or commencing treatment could also impact the viability of one or more of our customers as a going concern. Changes in reimbursement rates for proton therapy treatments, or uncertainty regarding these reimbursement rates, such as we experienced in 2012 with the reductions to reimbursement rates for hospital based proton therapy centers in the United States by CMS, can affect growth or demand for our VPT products and services.

We compete for many proton therapy system sales through tenders, where parties compete on price and other factors. Many companies sell their products at a lower price than we do. If we are unable to lower our prices or our customers are not willing to pay for additional features and functionality that we may provide, there is a risk we will lose sales, and if we lower our prices to gain business, our margins and other financial results may suffer. Further, the award of certain proton therapy system orders may be subject to challenge by third parties, which can make these orders more unpredictable than orders for other products. Because an order for a proton therapy system can be relatively large and complex, the sales and customer decision cycles for proton therapy projects may take several years, and an order in one fiscal period (or the cancellation of an order as a result of bid challenge or otherwise) will cause our gross orders to vary significantly, making comparisons between fiscal periods more difficult. We expect that a limited number of customers will account for a substantial portion of VPT's business for the foreseeable future. In instances where one customer undertakes multiple proton center projects, an adverse event with respect to one project could cause an adverse event with respect to the other projects, which could adversely impact our operating results.

Our estimates as to future operating results include certain assumptions about the results of VPT's business. If we are incorrect in our assumptions, our financial results could be materially and adversely affected. It is possible that VPT could perform significantly below our expectations due to a number of factors that cannot be predicted with certainty, including future market conditions, revenue growth rates, and operating margins. These factors could adversely impact VPT's ability to meet its projected results, which could cause a portion or all of the goodwill of VPT to become impaired. As of June 27, 2014, the goodwill of VPT was $60.5 million. If we determine that VPT's goodwill becomes impaired, we would be required to record a charge that could have a material adverse effect on our results of operations in such period.

OUR VPT BUSINESS MAY SUBJECT US TO INCREASED RISK AND POTENTIAL LIABILITY

VPT's business may subject us to increased risk and potential liability. For example, because proton therapy projects are large in scale and require detailed project planning, failure to deliver or delays in delivering on our commitments could result in greater than expected liabilities, as we could be required to indemnify business partners and customers for losses suffered or incurred if we are unable to deliver our products in accordance with the terms of customer contracts. Additionally, customers have in the past requested and may in the future request that the systems vendor, as the primary technology provider, provide guarantees for and suffer penalties in relation to the overall construction project, as well as in some situations participate in or provide project financing for the project. Since the cost of each proton therapy center project will often exceed $100 million, the amount of potential liability and potential for financial loss would likely be higher than the levels historically assumed by us for our traditional radiation therapy business and may also exceed the project's value. Insurance covering these contingencies may be unobtainable or expensive. If we cannot reasonably mitigate or eliminate these contingencies or risks, our ability to competitively bid upon proton center projects will be negatively impacted or we may be required to assume material amounts of potential liability, all of which may have adverse consequences to us. In addition, we have encountered and may encounter additional challenges in the commercialization of the proton therapy products, which may increase our research and development costs and delay the introduction of our products. These and other unanticipated events could adversely affect our business and make our results of operations unpredictable.

DISRUPTION OF CRITICAL INFORMATION SYSTEMS OR MATERIAL BREACHES IN THE SECURITY OF OUR SYSTEMS MAY ADVERSELY AFFECT OUR BUSINESS AND CUSTOMER RELATIONS

Information technology helps us operate efficiently, interface with and support our customers, maintain financial accuracy and efficiency, and produce our financial statements. There is an increasing threat of information security attacks that pose risk to companies, including Varian. If we do not allocate and effectively manage the resources necessary to build and sustain the proper technology infrastructure, we could be subject to, among other things, transaction errors, processing inefficiencies, the loss of customers, business disruptions, or the loss of or damage to

intellectual property through a security breach. If our data management systems do not effectively collect, secure, store, process and report relevant data for the operation of our business, whether due to equipment malfunction or constraints, software deficiencies, or human error, our ability to effectively plan, forecast and execute our business plan and comply with applicable laws and regulations will be impaired, perhaps materially. Any such impairment could materially and adversely affect our financial condition, results of operations, cash flows and the timeliness with which we report our operating results internally and externally.

Moreover, we manufacture and sell products that allow our customers to store confidential information about their patients. While we have implemented security measures to protect our systems from unauthorized access, these measures do not secure our customers' equipment or any information stored in our customers' systems or at their locations. A breach of network security and systems or other events that cause the loss or public disclosure of, or access by third parties to, our customers' stored information could have serious negative consequences for our business, including possible fines, penalties and damages, reduced demand for our solutions, an unwillingness of our customers to use our solutions, harm to our reputation and brand, and time-consuming and expensive litigation, any of which could have an adverse effect on our financial results.

WE HAVE ENTERED INTO A CREDIT FACILITY AGREEMENT THAT RESTRICTS CERTAIN ACTIVITIES, AND FAILURE TO COMPLY WITH THIS AGREEMENT MAY HAVE AN ADVERSE EFFECT ON OUR BUSINESS, LIQUIDITY AND FINANCIAL POSITION

We maintain a credit facility with debt outstanding that contains restrictive financial covenants, including financial covenants that require us to comply with specified financial ratios. We may have to curtail some of our operations to comply with these covenants. In addition, our revolving credit facility contains other affirmative and negative covenants that could restrict our operating and financing activities. These provisions limit our ability to, among other things, incur future indebtedness, contingent obligations or liens, guarantee indebtedness, make certain investments and capital expenditures, sell stock or assets and pay dividends, and consummate certain mergers or acquisitions. Because of the restrictions on our ability to create or assume liens, we may find it difficult to secure additional indebtedness if required. Furthermore, if we fail to comply with the credit facility requirements, we may be in default. Upon an event of default, if the credit agreement is not amended or the event of default is not waived, the lender could declare all amounts outstanding, together with accrued interest, to be immediately due and payable. If this happens, we may not be able to make those payments or borrow sufficient funds from alternative sources to make those payments. Even if we were to obtain additional financing, that financing may be on unfavorable terms.

CHANGES IN INTERPRETATION OR APPLICATION OF GENERALLY ACCEPTED ACCOUNTING PRINCIPLES MAY ADVERSELY AFFECT OUR OPERATING RESULTS

We prepare our financial statements to conform to GAAP. These principles are subject to interpretation by the Financial Accounting Standards Board (“FASB”), American Institute of Certified Public Accountants, the SEC and various other regulatory or accounting bodies. A change in interpretations of, or our application of, these principles can have a significant effect on our reported results and may even affect our reporting of transactions completed before a change is announced. In addition, when we are required to adopt new accounting standards, our methods of accounting for certain items may change, which could cause our results of operations to fluctuate from period to period and make it more difficult to compare our financial results to prior periods.

As our operations evolve over time, we may introduce new products or new technologies that require us to apply different accounting principles, including ones regarding revenue recognition, than we have applied in past periods. Currently, we recognize revenues for our proton therapy systems and proton therapy commissioning contracts and for certain highly customized image detection systems in our SIP business under contract accounting rules, which affects the timing of revenue recognition. We could be required to apply contract accounting rules to other businesses in the future. Under contract accounting rules, the use of the percentage-of-completion method involves considerable use of estimates in determining revenues, costs and profits and in assigning dollar amounts to relevant accounting periods, estimates which must be periodically reviewed and appropriately adjusted. For example, revenues recognized under the percentage-of-completion method are based on contract costs incurred to date compared with total estimated contract costs. In circumstances in which the final outcome of a contract cannot be precisely estimated but a loss on the contract is not expected, we recognize revenues under the percentage-of-completion method based on a zero profit margin until more precise estimates can be made. Recognizing revenues using the percentage-of-completion method based on a zero profit margin, as we had done with the revenues associated with the Scripps Proton Therapy Center in the earlier stages of the project lowers our gross margins and makes it more difficult to compare our financial results from quarter to quarter. In addition, if we were to recognize revenues for our proton therapy systems and services under either the completed contract method or outside of contract accounting rules altogether, we would defer revenue until a contract is completed or substantially completed. This may cause our results of operations to fluctuate from period to period.

If our estimates prove to be inaccurate or circumstances change over time, we would be required to adjust revenues or even record a contract loss in later periods, and our financial results could suffer. In addition, if a loss is expected on a

contract under the percentage-of-completion method, the estimated loss would be charged to cost of sales in the period the loss is identified. The application of different types of accounting principles and related potential changes may make it more difficult to compare our financial results from quarter to quarter, and the trading price of VMS common stock could suffer or become more volatile as a result.

AS A STRATEGY TO ASSIST OUR SALES EFFORTS, WE MAY PARTICIPATE IN PROJECT FINANCING OR OFFER EXTENDED PAYMENT TERMS, WHICH MAY ADVERSELY AFFECT OUR FINANCIAL RESULTS

We have provided financing for the construction and start-up operations of the Scripps Proton Therapy Center, and we may provide or be requested to provide financing to other potential VPT customers in the future. Providing such financing could adversely affect our financial results, since we cannot provide assurance that a center will be completed on time or within budget, that the center can or will generate sufficient patient volumes and revenues to support scheduled loan payments or to provide incremental revenue to us, or that the borrower will have the financial means to pay off any financing at maturity. In addition, in connection with our financing of the Scripps Proton Therapy Center, we cannot provide any assurance that any portion of our loan commitment can be syndicated to third parties, or that the loan facility can be successfully refinanced upon the maturity of the loan, which has a maximum term of six years. If a borrower does not have the financial means to pay off its debts, and if we cannot recover the amounts due us from the sale of any collateral, we may be required to write off all, or a portion of the loan, which would adversely affect our financial results.

In addition, in some circumstances we offer longer or extended payment terms for qualified customers in our other businesses. Many of the areas where we offer such longer or extended payment terms have under-developed legal systems for securing debt and enforcing collection of debt. As of June 27, 2014, customer contracts with remaining terms of more than one year amounted to approximately five percent of our accounts receivable balance. While we qualify customers to whom we offer longer or extended payment terms, their financial positions may change adversely over the longer time period given for payment. Concerns over continued economic instability could also make it more difficult for us to collect outstanding receivables. This may result in an increase in payment defaults and uncollectible accounts, or could cause us to increase our bad debt expense, which would adversely affect our net earnings. In addition, longer or extended payment terms could impact the timing of our revenue recognition, and they have in the past and may in the future result in an increase in our days sales outstanding.

ENVIRONMENTAL LAWS IMPOSE COMPLIANCE COSTS ON OUR BUSINESS AND CAN ALSO RESULT IN LIABILITY

We are subject to environmental laws around the world. These laws regulate many aspects of our operations, including our handling, storage, transport and disposal of hazardous materials. They can also impose cleanup liabilities, including with respect to discontinued operations. As a consequence, we can incur significant environmental costs and liabilities, some recurring and others not recurring. Although we follow procedures intended to comply with existing environmental laws, we, like other businesses, can never completely eliminate the risk of contamination or injury from certain materials that we use in our business and, therefore, the prospect of resulting claims and damage payments. We may also be assessed fines or penalties for failure to comply with environmental laws and regulations. Although insurance has provided coverage for portions of cleanup costs resulting from historical occurrences, we maintain only limited insurance coverage for costs or claims that might result from any future contamination.

Future changes in environmental laws could also increase our costs of doing business, perhaps significantly. Several countries, including some in the EU, now require medical equipment manufacturers to bear certain disposal costs of products at the end of the product’s useful life, increasing our costs. The EU has also adopted a directive that may lead to restrictions on the use of certain hazardous substances in some of our products sold there. This directive, along with another that requires material disclosure information to be provided upon request, could increase our operating costs. All of these costs, and any future violations or liabilities under environmental laws or regulations, could have a material adverse effect on our business.

OUR OPERATIONS ARE VULNERABLE TO INTERRUPTION OR LOSS DUE TO NATURAL OR OTHER DISASTERS, POWER LOSS, STRIKES AND OTHER EVENTS BEYOND OUR CONTROL

We conduct a significant portion of our activities, including manufacturing, administration and data processing at facilities located in the State of California and other seismically active areas that have experienced major earthquakes and other natural disasters. We carry limited earthquake insurance that may not be adequate or continue to be available at commercially reasonable rates and terms. A major earthquake or other disaster (such as a major fire, hurricane, flood, tsunami, volcanic eruption or terrorist attack) affecting our facilities, or those of our suppliers, could significantly disrupt our operations, and delay or prevent product manufacture and shipment during the time required to repair, rebuild or replace our or our suppliers' damaged manufacturing facilities; these delays could be lengthy and costly. If any of our customers' facilities are adversely affected by a disaster, shipments of our products could be delayed. Additionally, customers may delay purchases of our products until operations return to normal. Even if we are able to quickly respond to a disaster, the ongoing effects of the disaster could create some uncertainty in the operations of our businesses, such as occurred following the March 2011 tsunami in Japan. In addition, our facilities may be subject to a shortage of available electrical power and other energy supplies. Any shortages may increase our costs for power and energy supplies or could result in blackouts, which could disrupt the operations of our affected facilities and harm our business. Further, our products are typically shipped from a limited number of ports, and any disaster, strike or other event blocking shipment from these ports could delay or prevent shipments and harm our business. In addition, concerns about terrorism, the effects of a terrorist attack, political turmoil or an outbreak of epidemic diseases, such as the swine flu, could have a negative effect on our business operations, those of our suppliers and customers, and the ability to travel, resulting in adverse consequences on our revenues and financial performance.

WE WORK IN INTERNATIONAL LOCATIONS WHERE THERE ARE HIGH SECURITY RISKS, WHICH COULD RESULT IN HARM TO OUR EMPLOYEES OR CONTRACTORS OR CAUSE US TO INCUR SUBSTANTIAL COSTS

We work in some international locations where there are high security risks, which could result in harm to our employees and contractors or substantial costs. Some of our services are performed in or adjacent to high-risk locations, such as Iraq, Libya, and Mexico, where the country or location and surrounding area is suffering from political, social, or economic issues; war or civil unrest, or has a high level of criminal or terrorist activity. In those locations where we have employees or operations, we may incur substantial costs to maintain the safety of our personnel. Despite these precautions, the safety of our personnel in these locations may continue to be at risk, and we may in the future suffer the loss of employees and contractors, which could harm our business and operating results.

Item 2. Unregistered Sales of Equity Securities and Use of Proceeds

(a) Not applicable
(b) Not applicable
(c) The following table provides information with respect to the shares of common stock repurchased by us during the third quarter of fiscal year 2014.

Period	Total Number of Shares Purchased	Average Price Paid Per Share	Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs	Maximum Number of Shares that May Yet Be Purchased Under the Plans or Programs [1]
March 29, 2014 – April 25, 2014	252,752	$ 83.09	252,752	3,747,248
April 26, 2014 – May 23, 2014	497,248	$ 80.35	497,248	3,250,000
May 24, 2014 – June 27, 2014	500,000	$ 83.54	500,000	2,750,000
Total	1,250,000	$ 82.18	1,250,000	

(1) In November 2013, the VMS Board of Directors authorized the repurchase of an additional 6,000,000 shares of VMS common stock from December 30, 2013 through December 31, 2014. Stock repurchases under the November 2013 authorization may be made in open market purchases, in privately negotiated transactions (including accelerated share repurchase programs) or under Rule 10b5-1 share repurchase plans, and may be made from time to time in one or more blocks. Shares will be retired upon repurchase. As of June 27, 2014, 2,750,000 shares of VMS common stock remained available for repurchase under this repurchase authorization.

The preceding table excludes 2,290 shares of VMS common stock that were tendered to VMS in satisfaction of tax withholding obligations upon the vesting of restricted stock units granted under the Company’s employee stock plans.

Item 3. Defaults Upon Senior Securities

None.

Item 4. Mine Safety Disclosures

Not applicable.

Item 5. Other Information

None.

Item 6. Exhibits

(a) Exhibits required to be filed by Item 601 of Regulation S-K:
The exhibits listed in the accompanying index to exhibits are filed or incorporated by reference as part of this Form 10-Q.

SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, the Registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

VARIAN MEDICAL SYSTEMS, INC.
(Registrant)

Dated: August 5, 2014 By: /s/ ELISHA W. FINNEY
Elisha W. Finney
Executive Vice President, Finance and
Chief Financial Officer
(Duly Authorized Officer and
Principal Financial Officer)

INDEX TO EXHIBITS

Exhibit No.	Description
15.1	Letter Regarding Unaudited Interim Financial Information.
31.1	Chief Executive Officer Certification Pursuant to Rule 13a-14(a) of the Securities Exchange Act.
31.2	Chief Financial Officer Certification Pursuant to Rule 13a-14(a) of the Securities Exchange Act.
32.1	Certification pursuant to 18 U.S.C. Section 1350 as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
32.2	Certification pursuant to 18 U.S.C. Section 1350 as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
101.INS†	XBRL Instance Document
101.SCH†	XBRL Taxonomy Extension Schema Document
101.CAL†	XBRL Taxonomy Extension Calculation Linkbase Document
101.DEF†	XBRL Taxonomy Extension Definition Linkbase Document
101.LAB†	XBRL Taxonomy Extension Label Linkbase Document
101.PRE†	XBRL Taxonomy Extension Presentation Linkbase Document

†Attached as Exhibit 101 to this Quarterly Report on Form 10-Q are the following formatted in XBRL (eXtensible Business Reporting Language): (i) Condensed Consolidated Statements of Earnings for the three and nine months ended June 27, 2014 and June 28, 2013; (ii) Condensed Consolidated Statements of Comprehensive Earnings for the three and nine months ended June 27, 2014 and June 28, 2013; (iii) Condensed Consolidated Balance Sheets at June 27, 2014 and September 27, 2013; (iv) Condensed Consolidated Statements of Cash Flows for the nine months ended June 27, 2014 and June 28, 2013; and (v) Notes to Condensed Consolidated Financial Statements for the three and nine months ended June 27, 2014 and June 28, 2013.