FLIR SYSTEMS INC
Form 10-Q
October 27, 2017
UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10-Q

(Mark one)

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

For the quarterly period ended September 30, 2017

OR

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

For the transition period from to

Commission file number 0-21918

FLIR Systems, Inc.
(Exact name of Registrant as specified in its charter)

Oregon	93-0708501
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)
27700 SW Parkway Avenue, Wilsonville, Oregon	97070
(Address of principal executive offices)	(Zip Code)

(503) 498-3547
(Registrant’s telephone number, including area code)

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

Indicate by check mark whether the Registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T during the preceding 12 months (or for such shorter period that the Registrant was required to submit and post such files). Yes x No ¨

Indicate by check mark whether the Registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, a smaller reporting company, or an emerging growth company. See the definition of “large accelerated filer,” “accelerated filer,” “smaller reporting company” and “emerging growth company” in Rule 12b-2 of the Exchange Act. (Check one)

Large accelerated filer	x	Accelerated filer	¨
Non-accelerated filer	¨	Smaller reporting company	¨
		Emerging growth 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

If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the

Exchange Act. Yes ¨ No ¨

As of October 18, 2017, there were 138,574,234 shares of the registrant's common stock, $0.01 par value, outstanding.

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PART I. FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS
FLIR SYSTEMS, INC.
CONSOLIDATED STATEMENTS OF INCOME
(in thousands, except per share amounts)
(Unaudited)

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2017	2016	2017	2016
Revenue	$464,712	$405,228	$1,305,650	$1,187,429
Cost of goods sold	241,821	213,852	684,706	635,041
Gross profit	222,891	191,376	620,944	552,388
Operating expenses:				
Research and development	42,873	33,839	127,902	109,327
Selling, general and administrative	92,932	76,688	280,240	239,623
Total operating expenses	135,805	110,527	408,142	348,950
Earnings from operations	87,086	80,849	212,802	203,438
Interest expense	3,819	5,736	12,744	13,543
Interest income	(488)	(336)	(1,114)	(924)
Other (income) expense, net	(778)	241	(2,465)	138
Earnings before income taxes	84,533	75,208	203,637	190,681
Income tax provision	21,004	16,575	46,124	85,555
Net earnings	$63,529	$58,633	$157,513	$105,126
Net earnings per share:				
Basic	$0.46	$0.43	$1.15	$0.76
Diluted	$0.46	$0.43	$1.13	$0.76
Weighted average shares outstanding:				
Basic	137,849	136,963	137,030	137,438
Diluted	139,419	137,938	138,853	138,594

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

FLIR SYSTEMS, INC.
CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME
(in thousands)
(Unaudited)

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2017	2016	2017	2016
Net earnings	$63,529	$58,633	$157,513	$105,126
Other comprehensive income (loss), net of tax:				
Interest rate swap contracts:				
Fair value adjustment on interest rate swap contracts	—	292	187	(573)
Realized gain reclassified to earnings	(494)	—	(494)	—
Unrealized gain on available-for-sale investments	(3)	—	(4)	—
Foreign currency translation adjustments	19,993	(7,724)	55,788	(9,250)
Total other comprehensive income (loss)	19,496	(7,432)	55,477	(9,823)
Comprehensive income	$83,025	$51,201	$212,990	$95,303

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

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FLIR SYSTEMS, INC.
CONSOLIDATED BALANCE SHEETS
(in thousands, except for par value)
(Unaudited)

	September 30, 2017	December 31, 2016
ASSETS		
Current assets:		
Cash and cash equivalents	$436,961	$361,349
Accounts receivable, net	345,542	352,020
Inventories	413,005	371,371
Prepaid expenses and other current assets	86,570	79,917
Total current assets	1,282,078	1,164,657
Property and equipment, net	270,023	271,785
Deferred income taxes, net	51,179	45,243
Goodwill	930,846	801,406
Intangible assets, net	183,677	168,460
Other assets	48,472	168,155
Total assets	$2,766,275	$2,619,706
LIABILITIES AND SHAREHOLDERS' EQUITY		
Current liabilities:		
Accounts payable	$127,420	$114,225
Deferred revenue	29,015	34,420
Accrued payroll and related liabilities	67,759	52,874
Accrued product warranties	16,193	17,476
Advance payments from customers	19,260	26,019
Accrued expenses	47,528	34,022
Accrued income taxes	46,175	51,017
Other current liabilities	14,588	16,659
Current portion, long-term debt	—	15,000
Total current liabilities	367,938	361,712
Long-term debt	420,369	501,921
Deferred income taxes	14,569	2,331
Accrued income taxes	14,054	9,643
Pension and other long-term liabilities	59,827	65,773
Commitments and contingencies		
Shareholders' equity:		
Preferred stock, $0.01 par value, 10,000 shares authorized; no shares issued at September 30, 2017, and December 31, 2016	—	—
Common stock, $0.01 par value, 500,000 shares authorized, 138,414 and 136,334 shares issued at September 30, 2017, and December 31, 2016, respectively, and additional paid-in capital	72,117	12,139
Retained earnings	1,927,875	1,832,138
Accumulated other comprehensive loss	(110,474)	(165,951)
Total shareholders' equity	1,889,518	1,678,326
Total liabilities and shareholders' equity	$2,766,275	$2,619,706

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

FLIR SYSTEMS, INC.
CONSOLIDATED STATEMENTS OF CASH FLOWS
(in thousands)
(Unaudited)

	Nine Months Ended September 30,	
	2017	2016
CASH PROVIDED BY OPERATING ACTIVITIES:		
Net earnings	$157,513	$105,126
Adjustments to reconcile net earnings to net cash provided by operating activities:		
Depreciation and amortization	53,426	41,857
Deferred income taxes	(2,337)	(200)
Stock-based compensation arrangements	24,745	21,253
Other, net	(28,007)	19,830
Increase (decrease) in cash, net of acquisitions, resulting from changes in:		
Accounts receivable	13,047	19,951
Inventories	(30,589)	20,211
Prepaid expenses	(4,863)	(3,129)
Other assets	20,391	(18,861)
Accounts payable	11,370	(35,507)
Deferred revenue	(5,792)	4,859
Accrued payroll and other liabilities	13,712	(7,839)
Accrued income taxes	(6,647)	53,461
Pension and other long-term liabilities	(6,633)	1,595
Net cash provided by operating activities	209,336	222,607
CASH FLOWS FROM INVESTING ACTIVITIES:		
Additions to property and equipment	(31,861)	(27,682)
Proceeds from sale of assets	2,886	6,986
Business acquisitions, net of cash acquired	—	(42,445)
Net cash used by investing activities	(28,975)	(63,141)
CASH FLOWS FROM FINANCING ACTIVITIES:		
Net proceeds of long-term debt, including current portion	—	524,826
Repayment of long-term debt	(97,500)	(367,435)
Repurchase of common stock	—	(66,057)
Dividends paid	(61,776)	(49,564)
Proceeds from shares issued pursuant to stock-based compensation plans	44,231	7,347
Tax paid for net share exercises and issuance of vested restricted stock units	(9,505)	(5,775)
Other financing activities	(13)	10
Net cash (used) provided by financing activities	(124,563)	43,352
Effect of exchange rate changes on cash	19,814	2,085
Net increase in cash and cash equivalents	75,612	204,903
Cash and cash equivalents, beginning of year	361,349	472,785
Cash and cash equivalents, end of year	$436,961	$677,688

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

FLIR SYSTEMS, INC.
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited)

Note 1. Basis of Presentation

The accompanying consolidated financial statements of FLIR Systems, Inc. and its consolidated subsidiaries (the "Company") are unaudited and have been prepared pursuant to the rules and regulations of the Securities and Exchange Commission. In the opinion of management, these statements have been prepared on the same basis as the audited consolidated financial statements and include all adjustments, consisting of only normal recurring adjustments, necessary for a fair presentation of the Company's consolidated financial position and results of operations for the interim periods. Certain information and footnote disclosures normally included in financial statements prepared in accordance with accounting principles generally accepted in the United States have been condensed or omitted pursuant to such rules and regulations. These consolidated financial statements should be read in conjunction with the Company's audited consolidated financial statements and the notes thereto included in the Company's Annual Report on Form 10-K for the fiscal year ended December 31, 2016.

The accompanying consolidated financial statements include the accounts of FLIR Systems, Inc. and its wholly owned subsidiaries. All significant intercompany accounts and transactions have been eliminated. The results of operations for the interim periods presented are not necessarily indicative of the operating results to be expected for any subsequent interim period or for the year ending December 31, 2017.

Recently Adopted Accounting Pronouncements

Effective January 1, 2017, the Company adopted the Financial Accounting Standards Board ("FASB") Accounting Standards Update 2016-09, "Improvements to Employee Share-Based Payment Accounting" ("ASU 2016-09"). The standard update simplifies several aspects of the accounting for employee share-based payment transactions, including accounting for income taxes, forfeitures, and statutory withholding requirements, as well as classification in the Consolidated Statements of Cash Flows. As a result of the adoption, on a prospective basis, the Company recognized $0.4 million and $4.0 million of excess tax benefits from stock-based compensation as a discrete item in income tax provision for the three and nine months ended September 30, 2017, respectively. Historically, these amounts were recorded as additional paid-in capital. Upon adoption, the Company elected to apply the change retrospectively to the Consolidated Statement of Cash Flows which resulted in a reclassification of excess tax benefits from stock-based compensation of $1.6 million from cash flows from financing activities to cash flows from operating activities for the nine months ended September 30, 2016. Additionally, $5.8 million paid in cash to satisfy withholding requirements for net settlement of restricted stock unit shares vested and stock options exercised has been reclassified from cash flows from operating activities to cash flows from financing activities to conform to the presentation required by the new standard in the Consolidated Statement of Cash Flows for the nine months ended September 30, 2016. ASU 2016-09 also requires excess tax benefits and deficiencies to be excluded from the assumed future proceeds in the calculation of diluted shares. This change resulted in an increase in diluted weighted average shares outstanding of 215,000 shares and 211,000 shares for the three and nine months ended September 30, 2017, respectively. The Company elected not to change its policy on accounting for forfeitures and will continue to estimate a requisite forfeiture rate. Additional amendments to the accounting for income taxes and minimum statutory withholding requirements had no impact on the Company's results of operations.

Reclassifications

The Company made certain reclassifications to the prior years' financial statements and notes to the consolidated financial statements to conform them to the presentation as of and for the three and nine months ended September 30, 2017. These reclassifications had no effect on consolidated financial position, net earnings, shareholders' equity, or net cash flows for any of the periods presented.

FLIR SYSTEMS, INC.
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS—(Continued)
(Unaudited)

Note 2. Stock-based Compensation
Stock Incentive Plans
The Company has a stock-based compensation program that provides equity incentives for employees, consultants and directors. This program includes incentive and non-statutory stock options and non-vested stock awards (referred to as restricted stock unit awards) granted under two plans: the FLIR Systems, Inc. 2002 Stock Incentive Plan (the “2002 Plan”) and the FLIR Systems, Inc. 2011 Stock Incentive Plan (the “2011 Plan”). The Company has discontinued issuing awards out of the 2002 Plan but previously-granted awards under the 2002 Plan remain outstanding.
The Company has granted time-based options, time-based restricted stock unit awards, market-based restricted stock unit awards and performance-based restricted stock unit awards. Options generally expire ten years from the grant date. Time-based options and restricted stock unit awards generally vest over a three-year period. Market-based restricted stock unit awards may be earned based upon the Company's total shareholder return compared to the total shareholder return of the component company at the 60th percentile level in the S&P 500 Index over a three-year period. Performance-based restricted stock unit awards may be earned based upon certain profitability metrics as approved by the compensation committee of the Company's board of directors, including return on invested capital or income from operations over the relevant three-year periods. Shares vested under the performance-based restricted stock unit awards and the market-based restricted stock unit awards must generally be held by the participant for a period of one year from the vest date.
Employee Stock Purchase Plan
The Company has an Employee Stock Purchase Plan (the “ESPP”) which allows employees to purchase shares of the Company’s common stock at 85 percent of the fair market value at the lower of either the date of enrollment or the purchase date. The ESPP provides for six-month offerings commencing on May 1 and November 1 of each year with purchases on April 30 and October 31 of each year. Shares purchased under the ESPP must be held by employees for a period of at least 18 months after the date of purchase.
The following table sets forth the stock-based compensation expense recognized in the Consolidated Statements of Income (in thousands):

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2017	2016	2017	2016
Cost of goods sold	$788	$881	$1,820	$2,351
Research and development	1,329	1,225	3,805	3,639
Selling, general and administrative	7,774	4,766	19,120	15,263
Stock-based compensation expense before income taxes	$9,891	$6,872	$24,745	$21,253

Stock-based compensation expense capitalized in the Consolidated Balance Sheets is as follows (in thousands):

	September 30,	
	2017	2016
Capitalized in inventory	$1,074	$585

As of September 30, 2017, the Company had approximately $45.9 million of total unrecognized stock-based compensation costs, net of estimated forfeitures, to be recognized over a weighted average period of 2.20 years.

FLIR SYSTEMS, INC.
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS—(Continued)
(Unaudited)

Note 3. Net Earnings Per Share
The following table sets forth the reconciliation of the numerator and denominator utilized in the computation of basic and diluted earnings per share (in thousands):

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2017	2016	2017	2016
Numerator for earnings per share:				
Net earnings for basic and diluted earnings per share	$63,529	$58,633	$157,513	$105,126
Denominator for earnings per share:				
Weighted average number of common shares outstanding	137,849	136,963	137,030	137,438
Assumed exercise of stock options and vesting of restricted stock awards, net of shares assumed reacquired under the treasury stock method	1,570	975	1,823	1,156
Diluted shares outstanding	139,419	137,938	138,853	138,594

The effect of stock-based compensation awards for the three and nine months ended September 30, 2017, which in aggregate consisted of 147,000 and 83,000 shares, respectively; and for the three and nine months ended September 30, 2016, which in the aggregate consisted of 322,000 and 317,000 shares, respectively, have been excluded for purposes of diluted earnings per share since the effect of their inclusion would have been anti-dilutive.

Note 4. Fair Value of Financial Instruments
Factors used in determining the fair value of financial assets and liabilities are summarized into three broad categories in accordance with FASB ASC Topic 820, “Fair Value Measurements”:
Level 1 – quoted prices in active markets for identical securities as of the reporting date;
Level 2 – other significant directly or indirectly observable inputs, including quoted prices for similar securities, interest rates, prepayment speeds, credit risk, and observable market prices for identical instruments that are traded in less active markets; and
Level 3 – significant inputs that are generally less observable than objective sources, including our own assumptions in determining fair value.
The factors or methodology used for valuing securities are not necessarily an indication of the risk associated with investing in those securities.
The Company had $60.8 million and $8.3 million of cash equivalents at September 30, 2017 and December 31, 2016, respectively, which were primarily investments in money market funds and overnight deposits. The Company has categorized its cash equivalents as a Level 1 financial asset, measured at fair value based on quoted prices in active markets of identical assets. All cash equivalents are in instruments that are convertible to cash daily. The fair value of the Company’s foreign currency contracts as of September 30, 2017 and December 31, 2016, are disclosed in Note 5, "Derivative Financial Instruments," and are based on Level 2 inputs. The fair value of the Company’s senior unsecured notes as described in Note 13, "Long-Term Debt," is approximately $430.8 million based upon Level 2 inputs at September 30, 2017. At September 30, 2017, the Company had no other borrowings outstanding under the revolving credit facility described in Note 13. The Company does not have any other significant financial assets or liabilities that are measured at fair value.

FLIR SYSTEMS, INC.
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS—(Continued)
(Unaudited)

Note 5. Derivative Financial Instruments
Foreign Currency Exchange Rate Risk

The Company enters into foreign currency forward contracts not formally designated as hedges to manage the consolidated exchange rate risk associated with the remeasurement of non-functional currency denominated monetary assets and liabilities. Changes in fair value of foreign currency forward contracts are recognized in income at the end of each reporting period based on the difference between the contract rate and the spot rate. In general, these gains and losses are offset in the Consolidated Statements of Income by the reciprocal gains and losses from cash settlement of the underlying assets or liabilities which originally gave rise to the exposure. The net amount of the gains and losses related to derivative instruments recorded in other (income) expense, net for the three and nine months ended September 30, 2017 were a net gain of $0.2 million and a net loss of $7.3 million, respectively. The net losses for the three and nine months ended September 30, 2016 were $3.0 million and $4.1 million, respectively.
The table below presents the net notional amounts of the Company's outstanding foreign currency forward contracts by currency (in thousands):

	September 30, 2017	December 31, 2016
European euro	$ 129,730	$ 156,352
Swedish kroner	75,879	48,555
Canadian dollar	46,374	15,645
British pound sterling	24,954	33,862
Brazilian real	10,386	2,747
Australian dollar	1,960	1,653
Japanese yen	898	3,251
Other	896	—
	$ 291,077	$ 262,065

At September 30, 2017, the Company's foreign currency forward contracts, in general, had maturities of three months or less.
The carrying amounts of the foreign exchange contracts included in the Consolidated Balance Sheets are as follows (in thousands):

	September 30, 2017		December 31, 2016	
	Prepaid Expenses and Other Current Assets	Other Current Liabilities	Prepaid Expenses and Other Current Assets	Other Current Liabilities
Foreign exchange contracts	$ 2,269	$ 2,737	$ 2,369	$ 75

Interest Rate Swap Contracts
On May 31, 2016, the Company drew down $105 million under the revolving credit facility as described in Note 11, "Credit Agreement," and repaid the term loan originally issued under the credit agreement dated April 5, 2013. Interest was accrued and paid monthly based on the one-month LIBOR rate. To manage the interest rate risk arising from the variability in monthly interest expense attributable to the original term loan and amounts drawn under the revolver, the Company entered into two amortizing interest rate swaps with an aggregate notional amount of $105 million. The interest rate swaps were designated, and effective, as cash flow hedges.

During the quarter ended September 30, 2017, the Company repaid all amounts outstanding under the revolving credit facility. Concurrently, the Company exited both interest rate swaps which had a combined notional amount at the time of $86.3 million and discontinued the cash flow hedge. The Company reclassified a gain of $0.5 million from accumulated other comprehensive income to interest expense because it was probable that the forecasted variable monthly LIBOR-based interest rate payments would no longer occur.

FLIR SYSTEMS, INC.
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS—(Continued)
(Unaudited)

Note 6. Accounts Receivable

Accounts receivable are net of an allowance for doubtful accounts of $6.1 million and $6.5 million at September 30, 2017 and December 31, 2016, respectively.

Note 7. Inventories

Inventories consist of the following (in thousands):

	September 30, 2017	December 31, 2016
Raw material and subassemblies	$ 223,817	$ 200,640
Work-in-progress	52,287	43,430
Finished goods	136,901	127,301
	$ 413,005	$ 371,371

Note 8. Property and Equipment

Property and equipment are net of accumulated depreciation of $313.6 million and $275.1 million at September 30, 2017 and December 31, 2016, respectively.

Note 9. Goodwill

The carrying value of goodwill and the activity for the nine months ended September 30, 2017 are as follows (in thousands):

Balance, December 31, 2016	$ 801,406
Goodwill from acquisitions	100,022
Currency translation adjustments	29,418
Balance, September 30, 2017	$ 930,846

See Note 17, "Operating Segments and Related Information - Operating Segments," of the Notes to the Consolidated Financial Statements for additional information on the carrying value of goodwill by operating segment at September 30, 2017.

See Note 18, "Business Acquisitions," of the Notes to the Consolidated Financial Statements for additional information on the addition of goodwill from acquisitions.

Note 10. Intangible Assets

Intangible assets are net of accumulated amortization of $100.8 million and $77.8 million at September 30, 2017 and December 31, 2016, respectively.

Note 11. Credit Agreement

On February 8, 2011, the Company entered into a credit agreement with Bank of America, N.A., U.S. Bank National Association, JPMorgan Chase Bank N.A. and other lenders, as amended on April 5, 2013, October 27, 2015 and May 31, 2016 (the "Credit Agreement") which provides for a $500 million revolving line of credit. At September 30, 2017, the Company had no amounts outstanding under its revolving credit facility and had $16.9 million of letters of credit outstanding governed by the facility, which reduces the total available revolving credit under the Credit Agreement to $483.1 million.

FLIR SYSTEMS, INC.
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS—(Continued)
(Unaudited)

Note 12. Accrued Product Warranties
The following table summarizes the Company's warranty liability and activity (in thousands):

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2017	2016	2017	2016
Accrued product warranties, beginning of period	$19,530	$17,492	$20,845	$16,514
Amounts paid for warranty services	(3,790)	(3,624)	(12,781)	(13,221)
Warranty provisions for products sold	3,294	5,099	10,785	15,658
Currency translation adjustments and other	90	1,025	275	1,041
Accrued product warranties, end of period	$19,124	$19,992	$19,124	$19,992
Current accrued product warranties, end of period			$16,193	$16,759
Long-term accrued product warranties, end of period			$2,931	$3,233

Note 13. Long-Term Debt
Long-term debt consists of the following (in thousands):

	September 30,	December 31,
	2017	2016
Unsecured notes	$425,000	$ 425,000
Credit Agreement	—	97,500
Unamortized discounts and issuance costs of unsecured notes	(4,631)	(5,579)
	$420,369	$ 516,921
Current portion, long-term debt	$—	$ 15,000
Long-term debt	$420,369	$ 501,921

In June 2016, the Company issued $425 million aggregate principal amount of its 3.125 percent senior unsecured notes due June 15, 2021 (the "2016 Notes"). The net proceeds from the issuance of the 2016 Notes were approximately $421.0 million, after deducting underwriting discounts and offering expenses, which are being amortized over a period of five years. Interest on the 2016 Notes is payable semiannually in arrears on December 15 and June 15. The proceeds from the 2016 Notes were used to repay the principal amount of the notes issued in August 2011 and outstanding in July 2016 and are being used for general corporate purposes, including working capital and capital expenditure needs, business acquisitions and repurchases of the Company's common stock.
On May 31, 2016, the Company repaid its term loan and drew down $105.0 million under the revolving credit facility. Interest on amounts outstanding under the revolving credit facility accrued at the one-month LIBOR rate plus the applicable margin for the amount outstanding and was paid monthly in arrears. During the quarter ended September 30, 2017, the Company repaid all amounts outstanding under the revolving credit facility.

Note 14. Shareholders' Equity
The following table summarizes the common stock and additional paid-in capital activity during the nine months ended September 30, 2017 (in thousands):

Common stock and additional paid-in capital, December 31, 2016	$12,139
Common stock issued pursuant to stock-based compensation plans, net	34,726
Stock-based compensation	25,252
Common stock and additional paid-in capital, September 30, 2017	$72,117

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FLIR SYSTEMS, INC.
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS—(Continued)
(Unaudited)

Note 14. Shareholders’ Equity - (Continued)
On September 8, 2017, the Company paid a dividend of $0.15 per share on its outstanding common stock to the shareholders of record as of the close of business on August 25, 2017. The total cash payments for dividends during the nine months ended September 30, 2017 were $61.8 million.

Note 15. Contingencies

Raytheon Litigation
FLIR Systems, Inc. and its subsidiary, FLIR Commercial Systems, Inc. (formerly known as Indigo Systems Corporation) (together, the “FLIR Parties”), were named in a lawsuit filed by Raytheon Company (“Raytheon”) on March 2, 2007, in the United States District Court for the Eastern District of Texas. Raytheon's complaint, as amended, asserted claims for tortious interference, patent infringement, trade secret misappropriation, unfair competition, breach of contract, and fraudulent concealment. The FLIR Parties filed an answer to the complaint on September 2, 2008, in which they denied all material allegations. On October 27, 2010, the FLIR Parties and Raytheon entered into a settlement agreement that resolved the patent infringement claims (the "Patent Claims") pursuant to which the FLIR Parties paid $3 million to Raytheon and entitles the FLIR Parties to certain license rights in the patents that were the subject of the Patent Claims. On October 28, 2014, a four-week trial began with respect to Raytheon's remaining claims of misappropriations of trade secrets and claims related to 31 alleged trade secrets. On November 24, 2014, a jury in the United States District Court for the Eastern District of Texas rejected Raytheon’s claims and determined that 27 of the alleged trade secrets were not in fact trade secrets and that neither of the FLIR Parties infringed any of the trade secrets claimed and awarded Raytheon no damages. On March 31, 2016, the United States District Court for the Eastern District of Texas issued a Final Judgment denying Raytheon’s claims and awarding FLIR court costs and denying each of Raytheon’s and FLIR’s Renewed Motions for Judgment as a Matter of Law and denying FLIR’s Amended Rule 54(d) Motion for Attorneys’ Fees and Costs Under the Texas Theft Liability Act.

On April 29, 2016, Raytheon filed a Notice of Appeal to the United States Court of Appeals for the Federal Circuit of the denial by the United States District Court for the Eastern District of Texas of Raytheon’s Renewed Motion for Judgment as a Matter of Law, or in the Alternative, Motion for New Trial. On May 11, 2016, the FLIR Parties filed a Notice of Appeal to the United States Court of Appeals for the Federal Circuit of the Order of the United States District Court for the Eastern District of Texas Denying the FLIR Parties’ Amended Rule 54(d) Motion for Attorneys’ Fees and Costs under the Texas Theft Liability Act, the Order Denying the FLIR Parties’ Renewed Motion For Judgment as a Matter Of Law, and the Final Judgment to the extent it denied the FLIR Parties Attorneys’ Fees and Costs under the Texas Theft Liability Act. The matter remains ongoing and is subject to appeal. The Company is unable to estimate the amount or range of potential loss or recovery, if any, which might result if the final determination of this matter is favorable or unfavorable, but an adverse ruling on the merits of the original claims against the FLIR Parties, while remote, could be material.

Matters Involving the United States Department of State and Department of Commerce
On October 22, 2014, the Company initially contacted the United States Department of State Office of Defense Trade Controls Compliance (“DTCC”), pursuant to International Traffic in Arms Regulation (“ITAR”) § 127.12(c), regarding the unauthorized export of technical data and defense services to dual and third country nationals in at least four facilities of the Company. On April 27, 2015, the Company submitted its initial report to DTCC regarding the details of the issues raised in the October 22, 2014, submission. DTCC subsequently notified the Company that it was considering administrative proceedings under Part 128 of ITAR and requested a tolling agreement, which the Company executed on June 16, 2015 and referenced certain Company disclosures in addition to the submissions made in conjunction with the October 24, 2014 initial notification. On June 6, 2016, the Company executed a subsequent tolling agreement extending the tolling period for matters to be potentially included in an administrative proceeding for an additional 18

months until the end of December 2017. DTCC continues its review of the Company's activities and the Company continues to engage actively with the United States government on these matters.

In May 2017, the Company submitted an initial notification to DTCC regarding potential violations related to certain export classifications obtained through the commodity jurisdiction process. DTCC acknowledged the notification and at the request of DTCC, the Company executed a tolling agreement for this matter, suspending the statute of limitations for a twelve (12) month period.

FLIR SYSTEMS, INC.
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS—(Continued)
(Unaudited)

Note 15. Contingencies - (Continued)

In June 2017, the United States Department of Commerce Bureau of Industry and Security informed the Company of additional export licensing requirements that restrict the Company’s ability to sell 9hz thermal products without a license to customers in China not identified on a list maintained by the United States Department of Commerce. This action was precipitated by concerns of potential diversion of some of the Company's products to prohibited end users and to countries subject to economic and other sanctions implemented by the United States. If the Company is found to have violated applicable rules and regulations with respect to customers and limitations on the end use of the Company’s products, the Company could be subject to substantial fines and penalties, suspension of existing licenses or other authorizations and/or loss or suspension of export privileges.

The Company is unable to reasonably estimate the time it may take to resolve these matters or the amount or range of potential loss, penalty or other government action, if any, that may be incurred in connection with these matters. However, an unfavorable outcome could result in substantial fines and penalties or loss or suspension of export privileges or of particular authorizations that could be material to the Company’s financial position, results of operations or cash flows in and following the period in which such an outcome becomes estimable or known.

SkyWatch Product Quality Matters
In March 2016, the Company learned of potential quality concerns with respect to as many as 312 Level III and Level IV SkyWatch Surveillance Towers sold by FLIR and companies acquired by FLIR from 2002 through 2014. The Company notified customers who purchased the affected SkyWatch Towers of the potential concerns and, as a precautionary measure, also temporarily suspended production of all Level III and Level IV SkyWatch Towers pending the completion of its review and the implementation of any necessary remedial measures. During the quarter ended June 30, 2017, the Company identified the cause of these quality issues and began testing certain remedial solutions to repair the affected SkyWatch Towers. Testing of the remedial solution for certain of the product variations affected was also completed during the quarter ended June 30, 2017. Subsequent to the aforementioned identification and testing, customers who purchased the product configurations for which a remedial solution has been identified and tested were notified of their options to request modifications to their fielded units. While there still remains uncertainty related to estimating the costs associated with a potential remedy and number of units which may require such remedy, the Company currently estimates the range of potential loss to be between $5.6 million and $15 million. As no single amount within the range is a better estimate than any other amount within the range, the Company has recorded a liability of $5.6 million as of September 30, 2017. Factors underlying this estimated range of loss may change from time to time, and actual results may vary significantly from this estimate.

Other Matters
The Company is also subject to other legal and administrative proceedings, investigations, claims and litigation arising in the ordinary course of business not specifically identified above. In these identified matters and others not specifically identified, the Company records a liability with respect to a matter when management believes it is both probable that a liability has been incurred and the Company can reasonably estimate the amount of the loss. The Company believes it has recorded adequate provisions for any probable and estimable losses for matters in existence on the date hereof. The Company reviews these provisions to reflect the impact of negotiations, settlements, rulings, advice of legal counsel and other information and events pertaining to a particular matter. While the outcome of each of these matters is currently not determinable, the Company does not expect that the ultimate resolution of any such matter will individually have a material adverse effect on the Company’s financial position, results of operations or cash flows. The costs to resolve all such matters may in the aggregate have a material adverse effect on the Company’s financial position, results of operations or cash flows.

Note 16. Income Taxes

The provision for income taxes was as follows:

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2017	2016	2017	2016
Income tax provision	$21,004	$16,575	$46,124	$85,555
Effective tax rate	24.8 %	22.0 %	22.6 %	44.9 %

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FLIR SYSTEMS, INC.
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS—(Continued)
(Unaudited)

Note 16. Income Taxes

The effective tax rate for the three and nine months ended September 30, 2017, is lower than the United States Federal tax rate of 35 percent mainly due to the mix of lower foreign jurisdiction tax rates, the effect of federal, foreign and state tax credits, excess tax benefits from stock compensation, and other discrete adjustments.

As of September 30, 2017, the Company had approximately $59.5 million of unrecognized tax benefits, all of which would affect the Company’s effective tax rate if recognized. The Company anticipates approximately $47.0 million of its net unrecognized tax benefits will be recognized within 12 months as the result of settlements or effective settlements with various tax authorities, the closure of certain audits and the lapse of the applicable statute of limitations.

The Company classifies interest and penalties related to unrecognized tax benefits in the income tax provision. As of September 30, 2017, the Company had $2.5 million of accrued interest and penalties related to unrecognized tax benefits that are recorded as current and non-current accrued income taxes on the Consolidated Balance Sheet.

The Company currently has the following tax years open to examination by major taxing jurisdictions:

	Tax Years:
United States Federal	2013 - 2015
State of California	2013 - 2015
State of Massachusetts	2013 - 2015
State of Oregon	2013 - 2015
Sweden	2012 - 2015
United Kingdom	2012 - 2015
Belgium	2011 - 2016

FLIR SYSTEMS, INC.
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS—(Continued)
(Unaudited)

Note 17. Operating Segments and Related Information

Operating Segments

The Company has six reportable operating segments as follows:

Surveillance

The Surveillance segment develops and manufactures enhanced imaging and recognition solutions for a wide variety of military, law enforcement, public safety, and other government customers around the world for the protection of borders, troops, and public welfare. Offerings include airborne, land, maritime, and man-portable multi-spectrum imaging systems, radars, lasers, imaging components, integrated multi-sensor system platforms, and services related to these systems.

Instruments

The Instruments segment develops and manufactures devices that image, measure, and assess thermal energy, gases, and other environmental elements for industrial, commercial, and scientific applications. Products include thermal imaging cameras, gas detection cameras, firefighting cameras, process automation cameras, and environmental test and measurement devices.

Security

The Security segment develops and manufactures cameras, video recording systems, and video management systems for use in commercial, critical infrastructure, and home security applications. Products include thermal and visible-spectrum cameras, digital and networked video recorders, and related software and accessories that enable the efficient and effective safeguarding of assets at all hours of the day and through adverse weather conditions.

OEM & Emerging Markets

The OEM & Emerging Markets segment develops and manufactures thermal and visible-spectrum imaging camera cores and components that are utilized by third parties to create thermal, industrial, and other types of imaging systems. The segment also develops and manufactures intelligent traffic monitoring and signal control systems, imaging payloads for Unmanned Aerial Systems ("UAS"), and thermal imaging solutions for use by consumers in the smartphone and mobile devices markets.

Maritime

The Maritime segment develops and manufactures electronics and imaging instruments for the recreational and commercial maritime market. The segment provides a full suite of networked electronic systems including multi-function helm displays, navigational instruments, autopilots, radars, sonar systems, thermal and visible imaging systems, and communications equipment for boats of all sizes.

Detection

The Detection segment develops and manufactures sensor instruments and integrated platform solutions for the detection, identification, and suppression of chemical, biological, radiological, nuclear, and explosives ("CBRNE") threats for military force protection, homeland security, and commercial applications.

The Company’s chief operating decision maker ("CODM"), its Chief Executive Officer, evaluates each of its segment’s performance and allocates resources based on revenue and segment operating income. Intersegment revenues are recorded at cost and are eliminated in consolidation. The Company and each of its segments employ consistent accounting policies.

The following tables present revenue, operating income, and assets for the six segments. Operating income as reviewed by the CODM is revenue less cost of goods sold and operating expense, excluding general corporate expenses, acquisition related costs, executive transition costs, amortization of purchased intangible assets, amortization of acquisition-related inventory step-up, costs associated with the SkyWatch product remediation, and restructuring charges. Accounts receivable and inventories for operating segments are regularly reviewed by management and are reported below as segment assets. All remaining assets, liabilities, capital expenditures, and depreciation are managed on a Company-wide basis.

FLIR SYSTEMS, INC.
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS—(Continued)
(Unaudited)

Note 17. Operating Segments and Related Information - (Continued)
Operating Segments - (Continued)
Operating segment information is as follows (in thousands):

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2017	2016	2017	2016
Revenue—External Customers:				
Surveillance	$146,805	$136,402	$394,742	$373,993
Instruments	91,429	82,673	255,253	240,160
Security	65,660	56,431	160,447	166,872
OEM & Emerging Markets	87,206	62,719	259,418	167,544
Maritime	42,256	40,586	145,909	147,469
Detection	31,356	26,417	89,881	91,391
	$464,712	$405,228	$1,305,650	$1,187,429
Revenue—Intersegments:				
Surveillance	$10,115	$5,001	$18,203	$13,980
Instruments	929	709	2,916	3,498
Security	2,931	4,267	9,697	10,575
OEM & Emerging Markets	11,456	7,518	29,986	24,528
Maritime	567	656	1,865	2,728
Detection	2	—	3	31
Eliminations	(26,000)	(18,151)	(62,670)	(55,340)
	$—	$—	$—	$—
Segment operating income:				
Surveillance	$44,941	$41,428	$104,313	$103,888
Instruments	29,603	27,578	74,376	67,254
Security	6,486	4,784	8,090	7,025
OEM & Emerging Markets	26,931	20,658	77,628	48,100
Maritime	4,466	3,155	19,060	16,482
Detection	8,883	6,999	24,644	25,556
	$121,310	$104,602	$308,111	$268,305

A reconciliation of the Company's consolidated segment operating income to consolidated earnings before income taxes is as follows (in thousands):

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2017	2016	2017	2016
Consolidated segment operating income	$121,310	$104,602	$308,111	$268,305
Unallocated corporate expenses	(25,492)	(16,514)	(68,733)	(49,186)
Amortization of purchased intangible assets	(7,102)	(4,329)	(20,854)	(12,464)
Amortization of acquisition-related inventory step-up	—	—	(1,992)	—
SkyWatch product quality accrual	(1,088)	(2,000)	(3,088)	(2,000)
Restructuring charges	(542)	(910)	(642)	(1,217)
Consolidated earnings from operations	87,086	80,849	212,802	203,438
Interest and non-operating expense, net	(2,553)	(5,641)	(9,165)	(12,757)
Consolidated earnings before income taxes	$84,533	$75,208	$203,637	$190,681

Unallocated corporate expenses include general corporate expenses, acquisition related costs and executive transition costs.

FLIR SYSTEMS, INC.
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS—(Continued)
(Unaudited)

Note 17. Operating Segments and Related Information - (Continued)
Operating Segments - (Continued)

	September 30, 2017	December 31, 2016
Segment assets (accounts receivable, net and inventories):		
Surveillance	$290,353	$283,324
Instruments	132,642	114,681
Security	95,063	93,174
OEM & Emerging Markets	141,212	144,862
Maritime	65,276	61,494
Detection	34,001	25,856
	$758,547	$723,391

	September 30, 2017	December 31, 2016
Segment goodwill:		
Surveillance	$259,400	$152,383
Instruments	153,677	147,595
Security	111,883	102,983
OEM & Emerging Markets	255,490	252,647
Maritime	102,384	97,860
Detection	48,012	47,938
	$930,846	$801,406

Revenue and Long-Lived Assets by Geographic Area
Information related to revenue by significant geographical location, determined by the end customer, is as follows (in thousands):

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2017	2016	2017	2016
United States	$250,755	$229,350	$696,612	$647,938
Europe	91,529	71,949	265,842	240,656
Asia	56,416	42,639	170,061	133,877
Middle East/Africa	26,437	41,889	86,826	98,231
Canada/Latin America	39,575	19,401	86,309	66,727
	$464,712	$405,228	$1,305,650	$1,187,429

Long-lived assets by significant geographic locations are as follows (in thousands):

	September 30, 2017	December 31, 2016 (as reclassified)
United States	$686,191	$676,007
Europe	485,216	490,089
Canada/Latin America	253,051	235,921
Other foreign	8,560	7,789
	$1,433,018	$1,409,806

FLIR SYSTEMS, INC.
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS—(Continued)
(Unaudited)

Note 17. Operating Segments and Related Information - (Continued)
Operating Segments - (Continued)
Major Customers
Revenue derived from major customers is as follows (in thousands):

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2017	2016	2017	2016
United States government	$117,797	$112,735	$345,856	$298,476

Note 18. Business Acquisitions
Point Grey Research, Inc.
On November 4, 2016, the Company completed the acquisition of the assets of Point Grey Research Inc. (“Point Grey”), a global leader in the development of advanced visible imaging cameras and solutions that are used in industrial automation systems, medical diagnostic equipment, people counting systems, intelligent traffic systems, military and defense products, and advanced mapping systems, for approximately $259.2 million in cash, subject to customary post-closing adjustments. During the third quarter of 2017, the Company finalized the purchase price allocation which had no change to the previously recorded allocation of $39.8 million to identifiable intangible assets and $183.7 million to goodwill. These amounts have been recorded in the Company’s OEM & Emerging Markets segment.
The allocation of the purchase price for Point Grey is as follows (in thousands):

Cash acquired	$ 2,994
Other tangible assets and liabilities, net	35,064
Net deferred taxes	(2,438)
Identifiable intangible assets	39,800
Goodwill	183,741
Total purchase price	$ 259,161

The allocation of the purchase price related to this acquisition is based on management’s judgments after evaluating several factors, including valuation assessments of tangible and intangible assets, and estimates of the fair value of liabilities assumed. The goodwill of $183.7 million represents future economic benefits expected to arise from synergies from combining operations and the ability of Point Grey to provide the Company domain knowledge and distribution channels in adjacent markets.
In connection with the allocation of purchase price to the assets acquired and liabilities assumed, the Company identified certain intangible assets. The following table presents the acquired intangible assets, their estimated fair values, and estimated useful lives (in thousands, except years):

	Estimated Useful Life	Amount
Developed technology	10 years	$23,100
Customer relationships	7 years	13,200
Backlog	1 year	2,300
Non-Competition Agreements	5 years	1,000
Other	n/a	200
		$39,800

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FLIR SYSTEMS, INC.
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS—(Continued)
(Unaudited)

Note 18. Business Acquisitions - (Continued)

Acquisition-date identifiable intangible assets primarily consist of intangibles derived from developed technology, customer relationships, backlog, and non-competition agreements. Developed technology represents the economic advantage of having certain technologies in place that lower manufacturing and operating costs and drive higher margins. Customer relationships represent the relationships Point Grey has established in the OEM and people counting markets as of the date of the acquisition. Backlog represents "pre-sold" business at the date of acquisition, which provides positive earning streams post acquisition that exceed what is required to provide a return on the other assets employed. Non-competition agreements represent the economic benefit of having agreements with certain current and former employees and shareholders of Point Grey that restrict their ability to compete directly with the Company.

The developed technology was valued using the income approach and relief from royalty method. Customer relationships and backlog were valued using the income approach and multi-period excess earnings method. Non-competition agreements were valued using the income approach and the with-and-without method.

Prox Dynamics, AS

On November 30, 2016, the Company acquired 100% of the outstanding stock of Prox Dynamics AS ("Prox Dynamics"), a leading developer and manufacturer of nano-class UASs for military and para-military intelligence, surveillance, and reconnaissance applications, for approximately $134.1 in cash, subject to customary post-close adjustments. At December 31, 2016, the Company reported the net tangible assets of $11.3 million in the respective balance sheet accounts and the excess purchase price of $122.8 million in other long-term assets.

During the three months ended March 31, 2017, the Company performed a preliminary purchase price allocation which resulted in an allocation of $31.4 of identifiable intangible assets and $91.9 million of goodwill in conjunction with the Prox Dynamics acquisition, which has been recorded in the Company's Surveillance business segment. During the three months ended June 30, 2017, the Company finalized the purchase price allocation, resulting in a $7.4 decrease to net deferred taxes, and a corresponding $7.4 increase in goodwill. The goodwill of $99.3 represents future economic benefits expected to arise from synergies from combining operations the ability of Prox Dynamics to provide the Company domain knowledge and distribution channels in adjacent markets.

The allocation of the purchase price for Prox Dynamics is as follows (in thousands):

Cash acquired	$	11,706
Other tangible assets and liabilities, net	(900	)
Net deferred taxes	(7,387	)
Identifiable intangible assets	31,400	
Goodwill	99,269	
Total purchase price	$	134,088

In connection with the allocation of purchase price to the assets acquired and liabilities assumed, the Company identified certain intangible assets. The following table presents the acquired intangible assets, their estimated fair values, and estimated useful lives (in thousands, except years):

	Estimated Useful Life	Amount
Developed technology	8 years	$23,400
Customer relationships	7 years	3,500
Patents	8 years	3,100
Trade name	8 years	1,400
		$31,400

Acquisition-date identifiable intangible assets primarily consist of intangibles derived from developed technology, customer relationships, patents, and trade name. Developed technology and patents represent the economic advantage of having certain technologies in place that lower manufacturing and operating costs and drive higher margins. Customer relationships represents the relationships Prox Dynamics has established in the military and defense ministries of countries throughout the world. Trade name represents the "Black Hornet" name, which is well recognized within the industry and is known as a leading product within the nano-class UAS segment.

FLIR SYSTEMS, INC.
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS—(Continued)
(Unaudited)

Note 18. Business Acquisitions - (Continued)

The developed technology and customer relationships were valued using the income approach and multi-period excess earnings method. Patents and trade name were valued using the income approach and relief from royalty method.

The acquisitions of Point Grey and Prox Dynamics are not significant as defined in Regulation S-X under the Securities Exchange Act of 1934, nor are they significant compared to the Company's overall results of operations. Consequently, no pro forma financial information is provided.

Note 19. Subsequent Events

On October 19, 2017, the Company’s Board of Directors declared a quarterly dividend of $0.15 per share on its common stock, payable on December 8, 2017, to shareholders of record as of the close of business on November 24, 2017. The total cash payment of this dividend will be approximately $20.8 million.

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

Forward-Looking Statements

This Quarterly Report on Form 10-Q (the “Report”), including “Management’s Discussion and Analysis of Financial Condition and Results of Operations” in Part I, Item 2, contains forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995 regarding future events and the future results of FLIR Systems, Inc. and its consolidated subsidiaries (“FLIR” or the “Company”) that are based on management’s current expectations, estimates, projections and assumptions about the Company’s business. Words such as “expects,” “anticipates,” “intends,” “plans,” “believes,” “sees,” “estimates” and variations of such words and similar expressions are intended to identify such forward-looking statements. These statements are not guarantees of future performance and involve risks, uncertainties and assumptions that are difficult to predict. Therefore, actual outcomes and results may differ materially from what is expressed or forecasted in such forward-looking statements due to numerous factors including, but not limited to, those discussed in “Risk Factors” section in Part II, Item 1A of this Report, “Management’s Discussion and Analysis of Financial Condition and Results of Operations” in Part I, Item 2, and elsewhere in this Report as well as those discussed from time to time in the Company’s other Securities and Exchange Commission filings and reports. In addition, such statements could be affected by general industry, economic, and market conditions. Such forward-looking statements speak only as of the date of this Report or, in the case of any document incorporated by reference, the date of that document, and the Company does not undertake any obligation to update any forward-looking statement to reflect events or circumstances after the date of this Report, or for changes made to this document by wire services or Internet service providers. If the Company updates or corrects one or more forward-looking statements, investors and others should not conclude that the Company will make additional updates or corrections with respect to other forward-looking statements.

Consolidated Operating Results

The following discussion of operating results provides an overview of our operations by addressing key elements in our Consolidated Statements of Income. The “Segment Operating Results” section that follows describes the contributions of each of our business segments to our consolidated revenue and earnings from operations. Our six operating segments are: Surveillance, Instruments, Security, OEM & Emerging Markets, Maritime, and Detection. Given the nature of our business, we believe revenue and earnings from operations (including operating margin percentage) are most relevant to an understanding of our performance at a segment level. Additionally, at the segment level we disclose backlog, which represents orders received for products or services for which a sales agreement is in place and delivery is expected within twelve months. See Note 17, "Operating Segments and Related Information," of the Notes to the Consolidated Financial Statements for additional information on the six operating segments.

Revenue. Consolidated revenue for the three months ended September 30, 2017, increased by 14.7 percent year over year, from $405.2 million in the third quarter of 2016 to $464.7 million in the third quarter of 2017. Consolidated revenue for the nine months ended September 30, 2017, increased by 10.0 percent year over year, from $1,187.4 million in the first nine months of 2016 to $1,305.7 million in the first nine months of 2017. Revenue increased in all six of our operating segments for three month period ended September 30, 2017. Increases in revenues for the nine month period in our Surveillance, Instruments, and OEM & Emerging Markets segments were partially offset by declines in revenues in our Security, Maritime, and Detection segments. The growth for the three month period ended September 30, 2017 occurred in all six of our operating segments, supported by the acquisitions of Prox Dynamics and Point Grey. The acquisitions of Armasight, Prox Dynamics, and Point Grey were the primary drivers in revenue growth for the nine month period ended September 30, 2017 compared to the same periods ended September 30, 2016.

The timing of orders, scheduling of backlog, and fluctuations in demand in various regions of the world can give rise to quarter to quarter and year over year fluctuations in the mix of revenue. Consequently, year over year comparisons for any given quarter may not be indicative of comparisons using longer time periods. While we currently expect total annual revenue for 2017 to be higher than 2016 revenue, unexpected changes in economic conditions from key customer markets or other major unanticipated events may cause total revenue, and the mix of revenue between our segments, to vary from quarter to quarter during the year.

International sales accounted for 46.0 percent and 43.4 percent of total revenue for the quarters ended September 30, 2017 and 2016, respectively. The proportion of our international revenue compared to total revenue will fluctuate from quarter to quarter due to normal variation in order activity across various regions as well as specific factors that may affect one region and not another. Overall, we anticipate that revenue from international sales will continue to comprise a significant percentage of total revenue.

Cost of goods sold. Cost of goods sold for the three and nine months periods ended September 30, 2017 were $241.8 million and $684.7 million, respectively compared to cost of goods sold for the three and nine months ended September 30, 2016 of $213.9 million and $635.0 million, respectively. The year over year increase in cost of goods sold is primarily related to higher revenues in 2017.

Gross profit. Gross profit for the quarter ended September 30, 2017, was $222.9 million compared to $191.4 million for the same quarter last year. Gross profit for the nine months ended September 30, 2017 was $620.9 million compared to $552.4 million for the nine month period ended September 30, 2016. Gross margin, defined as gross profit divided by revenue, increased from 47.2 percent in the third quarter of 2016 to 48.0 percent in the third quarter of 2017 and increased from 46.5 percent for the nine months ended September 30, 2016, to 47.6 percent during the nine months ended September 30, 2017. The increase in gross margin for the three and nine month periods was primarily due to the acquisitions and favorable product mix.

Research and development expenses. Research and development expenses for the third quarter of 2017 totaled $42.9 million, compared to $33.8 million in the third quarter of 2016. Research and development expenses in the first nine months of 2017 were $127.9 million compared to $109.3 million for the first nine months of 2016. The increase in research and development expenses year over year for the three and nine month periods was primarily related to the inclusion of companies acquired in the last 12 months. Research and development expenses as a percentage of revenue were 9.2 percent for the three months ended September 30, 2017 and 8.4 percent for the three months ended September 30, 2016. Research and development expenses as a percentage of revenue for the first nine months of 2017 were 9.8 percent compared to 9.2 percent during the first nine months of 2016. We have, and will continue to have, fluctuations in quarterly spending depending on product development needs and overall business spending priorities and believe that annual spending levels are most indicative of our commitment to research and development. Over the past five annual periods through December 31, 2016, our annual research and development expenses have varied between 8.5 percent and 9.9 percent of revenue, and we currently expect these expenses to remain within that range, on an annual basis, for the foreseeable future.

Selling, general, and administrative expenses. Selling, general, and administrative expenses were $92.9 million and $76.7 million for the quarters ended September 30, 2017 and 2016, respectively. Selling, general and administrative expenses were $280.2 million and $239.6 million for the nine months ended September 30, 2017 and 2016, respectively. The increase in selling, general, and administrative expenses year over year for the three and nine month periods was primarily related to the inclusion of selling, general, and administrative expenses of companies acquired in the last 12 months. Selling, general, and administrative expenses as a percentage of revenue were 20.0 percent and 18.9 percent for the quarters ended September 30, 2017 and 2016, respectively. Selling, general and administrative expenses as a percentage of revenue were 21.5 percent and 20.2 percent for the nine month periods ended September 30, 2017 and 2016, respectively. Over the past five annual periods through December 31, 2016, our annual selling, general and administrative expenses have varied between 19.4 percent and 21.7 percent of revenue, and we currently expect these expenses to remain within that range, on an annual basis, for the foreseeable future.

Interest expense. Interest expense for the three months ended September 30, 2017, was $3.8 million, compared to $5.7 million for the same period of 2016. Interest expense for the nine months ended September 30, 2017, was $12.7 million, compared to $13.5 million for the nine months ended September 30, 2016. Interest expense in 2017 was primarily associated with the $425 million aggregate principal amount of our 3.125 percent senior unsecured notes and amounts drawn under our credit facility. During the three month period ended September 30, 2017 we paid off the outstanding amount drawn on our credit facility. Interest expense in 2016 was primarily associated with the $250 million aggregate principal amount of our 3.75 percent senior unsecured notes and our term loan that was drawn upon under our credit agreement.

Income taxes. Our income tax provision of $21.0 million and $46.1 million for the three and nine month periods ended September 30, 2017, represents an effective tax rate of 24.8 percent and 22.6 percent, respectively. Our income tax provision for the three and nine month periods ended September 30, 2016 was $16.6 million and $85.6 million, which represented an effective tax rate of 22.0 percent and 44.9 percent, respectively. The effective tax rate for the three and nine months ended September 30, 2017 is lower than the United States Federal tax rate of 35 percent mainly due to the mix of lower foreign jurisdiction tax rates, the effect of federal, foreign and state tax credits, excess tax benefits for stock compensation, and other discrete adjustments. The first quarter of 2016 included discrete tax charges totaling $39.6 million related to the January 11, 2016, announcement from the European Commission of a decision concluding that certain rules under Belgian tax legislation are deemed to be incompatible with European Union regulations on state aid. As a result of this decision, the European Commission has directed the Belgian Government to recover past taxes from certain entities, reflective of disallowed state aid, which impacts one of the Company's international subsidiaries. The Belgian Government announced they have appealed this decision and filed action for an annulment in the General Court of the European Union, and in July 2016 the Company filed a separate appeal with the General Court of the European Union. In accordance with FASB ASC Topic 740, "Income Taxes," the Company recorded discrete tax expense of $39.6 million during 2016, related to this matter and on January 10, 2017, received tax assessments from the Belgium government for a similar amount, which the Company has classified as current taxes payable on the Consolidated Balance Sheet as of September 30, 2017. The Company has filed a complaint against the Belgian tax assessments, and the result of this complaint, the appeal with the General Court of the European Union, new information received from the Belgian Government, or other future events may cause the income tax provision associated with the decision to be entirely or partially reversed.

Segment Operating Results

The Company is currently organized into six reportable operating segments. See Note 17, "Operating Segments and Related Information," of the Notes to the Consolidated Financial Statements for a description of each segment, including the types of products and services from which each segment derives its revenues. On August 30, 2017, we announced our plans to realign the business operations into three principle business units: Government and Defense, Industrial, and Commercial. The Government and Defense business unit will consist of the current Surveillance and Detection segments, excluding the Outdoor and Tactical Systems (OTS) business; The Industrial business unit will consist of the current Instruments and OEM and Emerging segments, excluding the Intelligent Traffic Systems (ITS) business; and the Commercial business unit will consist of the current Maritime and Security segments, along with the ITS and OTS businesses. With this consolidation, we intend to reduce complexity, realize greater operating synergies, and enhance management focus. We expect to report our financial results in accordance with this new operating structure beginning with the first quarter 2018 operating results. The operating results of our six current reportable operating segments for the three and nine months ended September 30, 2017 are presented below.

Surveillance

Surveillance operating results are as follows (in millions, except percentages):

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2017	2016	2017	2016
Revenue	$146.8	$136.4	$394.7	$374.0
Earnings from operations	44.9	41.4	104.3	103.9
Operating margin	30.6 %	30.4 %	26.4 %	27.8 %
Backlog			395	363

Surveillance revenue for the quarter ended September 30, 2017, increased by 7.6 percent compared to the same period of 2016. Surveillance revenue for the nine months ended September 30, 2017, increased by 5.5 percent compared to the same period of 2016. The increase in revenue for the quarter ended September 30, 2017, compared to the same period of 2016 was driven by increase in sales in Airborne and Weapon Sights markets, and the addition of the Prox Dynamics business, which was acquired in November 2016, partially offset by lower Land market sales. The increase in revenue for the nine months ended September 30, 2017 compared to the same period of 2016 was predominately due to the addition of Armasight, which was acquired in June 2016 , the Prox Dynamics business, and increased Airborne sales. The increase in earnings from operations for the three and nine month periods ended September 30, 2017, compared to the same periods in 2016, was primarily due to higher revenues and favorable product mix, partially offset by increased operating expenses from the acquired businesses. The increased backlog in the Surveillance segment is largely attributed to the $74.7 million contract for land surveillance systems from the United States Army received in September 2017.

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Instruments

Instruments operating results are as follows (in millions, except percentages):

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2017	2016	2017	2016
Revenue	$91.4	$82.7	$255.3	$240.2
Earnings from operations	29.6	27.6	74.4	67.3
Operating margin	32.4 %	33.4 %	29.1 %	28.0 %
Backlog			34	27

Instruments segment revenue for the quarter ended September 30, 2017, increased by 10.6 percent compared to the same period of 2016. Instruments revenue for the nine months ended September 30, 2017, increased by 6.3 percent compared to the same period of 2016. The increase in revenue for the three and nine month periods was predominately attributable to strength in the Premium and Volume Handheld product lines driven by new product launches, supplemented by growth in Optical Gas and Fire products. The revenue growth for the three and nine month periods was partially offset by declines in the test and measurement product lines. The increase in earnings from operations for the three and nine months ended September 30, 2017, compared to the same periods of 2016, was primarily due to the higher revenue base.

Security

Security operating results are as follows (in millions, except percentages):

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2017	2016	2017	2016
Revenue	$65.7	$56.4	$160.4	$166.9
Earnings from operations	6.5	4.8	8.1	7.0
Operating margin	9.9 %	8.5 %	5.0 %	4.2 %
Backlog			24	23

Security segment revenue for the quarter ended September 30, 2017, increased by 16.4 percent compared to the same period of 2016. Security revenue for the nine months ended September 30, 2017, decreased by 3.9 percent compared to the same period of 2016. The increase in revenue for the three month period ended September 30, 2017 was predominately due to growth in the Lorex-branded and other consumer-grade retail sales. The decrease in revenue for the nine month period ended September 30, 2017 compared to the same period ended September 30, 2016 was primarily due to a reduction in sales for consumer-grade security products in retail channels during the first six months of 2017, partially offset by increased consumer-grade sales through our e-commerce channel. The increase in earnings from operations for the three and nine months ended September 30, 2017, compared to the same periods of 2016, was due to cost savings initiatives in 2017.

OEM & Emerging Markets

OEM & Emerging Markets operating results are as follows (in millions, except percentages):

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2017	2016	2017	2016
Revenue	$87.2	$62.7	$259.4	$167.5
Earnings from operations	26.9	20.7	77.6	48.1
Operating margin	30.9 %	32.9 %	29.9 %	28.7 %
Backlog			162	139

OEM & Emerging Markets segment revenue for the quarter ended September 30, 2017, increased by 39.0 percent compared to the same period of 2016. The increase in revenue for the three month period ended September 30, 2017 was primarily related to revenue from the Point Grey business acquired in November 2016, supplemented by growth in our unmanned aerial systems and mobile accessories product lines. OEM & Emerging Markets revenue for the nine months ended September 30, 2017, increased by 54.8 percent compared to the same period of 2016. The increase in revenue for the nine month period was primarily due to the Point Grey acquisition and growth in our cores and traffic product lines. The increase in earnings from operations for the three and nine months ended September 30, 2017, compared to the same periods of 2016, was due to higher revenues. The increase in backlog for the OEM & Emerging Markets segment was primarily attributed to the inclusion of backlog associated with the Point Grey acquisition.

Maritime

Maritime operating results are as follows (in millions, except percentages):

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2017	2016	2017	2016
Revenue	$42.3	$40.6	$145.9	$147.5
Earnings from operations	4.5	3.2	19.1	16.5
Operating margin	10.6 %	7.8 %	13.1 %	11.2 %
Backlog			16	24

Maritime segment revenue for the quarter ended September 30, 2017, increased by 4.1 percent compared to the same period of 2016. The increase was due to sales on the new Axiom line of multi-function displays which began shipping during the second quarter of 2017. Maritime revenue for the nine months ended September 30, 2017, decreased by 1.1 percent. The decrease in revenue for the nine month period of 2017 compared to the same period of the prior year was driven by a decline in Thermal camera sales, partially offset by the increase in multi-function display sales. The increase in operating income for the three and nine month periods ended September 30, 2017 compared to the same periods of 2016 was driven by stronger margins on shipments of new products introduced in 2017.

Detection

Detection operating results are as follows (in millions, except percentages):

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2017	2016	2017	2016
Revenue	$31.4	$26.4	$89.9	$91.4
Earnings from operations	8.9	7.0	24.6	25.6
Operating margin	28.3 %	26.5 %	27.4 %	28.0 %
Backlog			78	68

Detection segment revenue for the quarter ended September 30, 2017, increased by 18.7 percent compared to same period of 2016. The increase for the quarter ended September 30, 2017 compared to the same period of 2016 was due to higher shipments of our CBRNE threat response systems to the United States government customers and higher sales of our ChemBio and Radiation products. Detection revenue for the nine months ended September 30, 2017, decreased by 1.7 percent. The decrease in revenue for the nine month period ending September 30, 2017, compared to the same periods of 2016, was primarily due to lower shipments of our CBRNE threat response systems during the period. These shipments account for a significant portion of Detection revenues, and timing of delivery schedules impacts periodic results. The increase in earnings from operations for the three month period ended September 30, 2017, compared to the same period of 2016 was due to the higher revenues in the quarter, while the decrease for the nine months ended September 30, 2017, compared to the same period of 2016 was due to lower revenues.

Liquidity and Capital Resources

At September 30, 2017, we had a total of $437.0 million in cash and cash equivalents, $136.6 million of which resided in the United States and $300.4 million at our foreign subsidiaries, compared to cash and cash equivalents at December 31, 2016, of $361.3 million, of which $98.3 million resided in the United States and $263.0 million at our foreign subsidiaries. The increase in cash and cash equivalents during the nine months ended September 30, 2017, was primarily due to cash provided from operations of $209.3 million and proceeds of $44.2 million from shares issued under our stock compensation plans, partially offset by the pay down on our revolving credit facility of $97.5 million, capital expenditures of $31.9 million and dividend payments of $61.8 million.

Cash provided by operating activities during the nine months ended September 30, 2017, totaled $209.3 million, which primarily consisted of net earnings, adjusted for depreciation and amortization, stock-based compensation, other non-cash items and changes in working capital.

Cash used for investing activities for the nine months ended September 30, 2017, totaled $29.0 million, which primarily consisted of capital expenditures in the ordinary course of business.

Cash used by financing activities for the nine months ended September 30, 2017, totaled $124.6 million, which primarily consisted of repayment of borrowings under our revolving credit facility and the payment of quarterly dividends, partially offset by proceeds from share issuances pursuant to our stock plans.

On February 8, 2011, we entered into a Credit Agreement (“Credit Agreement”) with Bank of America, N.A., U.S. Bank National Association, JPMorgan Chase Bank N.A. and other Lenders. The Credit Agreement provides for a $200 million, five-year revolving line of credit. On April 5, 2013, the Credit Agreement was amended to extend the maturity of the revolving credit facility from April 8, 2016 to April 5, 2018, in addition to incorporating a $150 million term loan facility maturing April 5, 2019. On May 31, 2016, the Credit Agreement was further amended to increase the borrowing capacity to $500 million and to extend the maturity of the revolving credit facility from April 5, 2018 to May 31, 2021. The amendment also incorporated a revised schedule of fees and interest rate spreads. We have the right, subject to certain conditions, including approval of additional commitments by qualified lenders, to increase the revolving line of credit under the Credit Agreement by an additional $200 million until May 31, 2021. The Credit Agreement allows us and certain designated subsidiaries to borrow in United States dollars, European euros, Swedish kronor, British pound sterling, Japanese yen, Canadian dollars, Australian dollars, and other agreed upon currencies. Interest rates under the Credit Agreement are determined based on the type of borrowing. Interest associated with borrowings can be based on either the prime lending rate of Bank of America, N.A. or the published Eurocurrency rate (i.e. LIBOR). The borrowings have an applicable margin that ranges from 0.125 percent to 2.125 percent depending on the applicable base rate and our consolidated total leverage ratio. Including the respective spreads, the one-month Eurocurrency-based borrowing rate was 2.610 percent per annum and the prime lending-based borrowing rate was 4.625 percent per annum at September 30, 2017. The Credit Agreement requires us to pay a commitment fee on the amount of unused revolving commitments at a rate, based on our total leverage ratio, which ranges from 0.150 percent to 0.300 percent of unused revolving commitments. At September 30, 2017, the commitment fee on the amount of unused revolving credit was 0.175 percent per annum. The Credit Agreement contains two financial covenants that require the maintenance of a total leverage ratio and an interest coverage ratio, with which the Company was in compliance at September 30, 2017. The credit facilities available under the Credit Agreement are unsecured.

On May 31, 2016, the Company drew down $105 million under the revolving credit facility and repaid the term loan originally issued under the credit agreement dated April 5, 2013. Interest was accrued and paid monthly based on the one-month LIBOR rate. To manage the interest rate risk arising from the variability in monthly interest expense attributable to amounts drawn under the revolver, the Company entered into two amortizing interest rate swaps with an aggregate of $105 million. The interest rate swaps were designated, and effective, as cash flow hedges.

During the quarter ended September 30, 2017, the Company repaid all amounts outstanding under the revolving credit facility. Concurrently, the Company exited both interest rate swaps which had a combined notional value at the time of $86.3 million. We had $16.9 million of letters of credit outstanding under the Credit Agreement at September 30, 2017, which reduced the total available revolving credit under the Credit Agreement.

In June 2016, we issued $425 million aggregate principal amount of our 3.125 percent senior unsecured notes due June 15, 2021 (the “Notes”). The net proceeds from the issuance of the Notes were approximately $421.0 million, after deducting underwriting discounts and offering expenses, which are being amortized over a period of five years. Interest on the Notes is payable semiannually in arrears on December 15 and June 15. The proceeds from the Notes were used to repay our 3.75 percent

senior unsecured notes that were due September 1, 2016, and are being used for general corporate purposes, which include working capital and capital expenditure needs, business acquisitions, and repurchases of our common stock.
On February 5, 2015, our Board of Directors authorized the repurchase of up to 15.0 million shares of our outstanding common stock. An aggregate of 6.3 million shares were repurchased under this authorization, which expired on February 5, 2017. On February 8, 2017, our Board of Directors authorized the repurchase of up to 15.0 million shares of our outstanding common stock. This authorization will expire on February 8, 2019. As of September 30, 2017, no shares have been repurchased under the February 8, 2017 authorization.
United States income taxes have not been provided for accumulated earnings of certain subsidiaries outside of the United States as we currently intend to reinvest the earnings in operations and other activities outside the United States indefinitely. Should we subsequently elect to repatriate such foreign earnings, we would need to accrue and pay United States income taxes, thereby reducing the amount of our cash.
We believe that our existing cash combined with the cash we anticipate generating from operating activities, and our available credit facilities and financing available from other sources will be sufficient to meet our cash requirements for the next twelve months. We do not have any significant commitments nor are we aware of any significant events or conditions that are likely to have a material impact on our liquidity or capital resources.

Off-Balance Sheet Arrangements

As of September 30, 2017, we leased our non-owned facilities under operating lease agreements. We also leased certain operating machinery and equipment and office equipment under operating lease agreements. Except for these operating lease agreements, we do not have any off-balance sheet arrangements that have or are likely to have a material current or future effect on our financial condition, revenues or expenses, results of operations, liquidity, capital expenditures, or capital resources.

Recent Accounting Pronouncements
Recently Issued Accounting Pronouncements
In May 2014, the Financial Accounting Standards Board (the "FASB") issued Accounting Standards Update No. 2014-09, "Revenue from Contracts with Customers" ("ASU 2014-09"), which establishes new guidance under which companies will recognize revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the company expects to be entitled in exchange for those goods or services. ASU 2014-09 also provides for additional disclosure requirements. The FASB has recently issued several amendments to the new standard, including clarification on accounting for licenses of intellectual property and identifying performance obligations. The amendments include (i) ASU No. 2016-08, Revenue from Contracts with Customers (Topic 606)-Principal versus Agent Considerations, which was issued in March 2016, and clarifies the implementation guidance for principal versus agent considerations in ASU 2014-09, and (ii) ASU No. 2016-10, Revenue from Contracts with Customers (Topic 606)-Identifying Performance Obligations and Licensing, which was issued in April 2016, and amends the guidance in ASU No. 2014-09 related to identifying performance obligations and accounting for licenses of intellectual property.
The new standard permits adoption either by using (i) a full retrospective approach for all periods presented in the period of adoption or (ii) a modified retrospective approach with the cumulative effect of initially applying the new standard recognized at the date of initial application and providing certain additional disclosures. While ASU 2014-09 was to be effective for annual periods and interim periods beginning after December 15, 2016, on July 9, 2015, the FASB approved the deferral of the effective date to periods beginning on or after December 15, 2017. Accordingly, the Company currently intends to adopt ASU 2014-09 on January 1, 2018. The Company currently plans to adopt using the modified retrospective approach.
The Company has made progress toward completing the evaluation of the potential changes from adopting the new standard on its financial reporting and disclosures. The Company has evaluated the impact of the standard on all of its revenue streams and most of its significant contracts. The Company has completed the assessment of the impact on its business processes, controls and systems. During the third quarter of 2017, the Company completed the design of the changes to our business processes, controls and systems. The Company plans to implement the changes in the fourth quarter of 2017. The Company has also begun quantifying the impact of the adoption of the standard on retained earnings as of January 1, 2017. However, the impact to retained earnings is not known at this time, as it will be dependent on the number, size, and complexity of contracts that have not been substantially completed as of December 31, 2017.
In February 2016, the FASB issued Accounting Standards Update No. 2016-02, “Leases (Topic 842)” (“ASU 2016-02”). The amendments in this update require the identification of arrangements that should be accounted for as leases by lessees. In general, for lease arrangements exceeding a twelve-month term, these arrangements must now be recognized as assets and liabilities on the balance sheet of the lessee. ASU 2016-02 requires the use of the modified retrospective method, which will require adjustment to all comparative periods presented in the consolidated financial statements. ASU 2016-02 is effective for interim and annual reporting periods beginning after December 15, 2018, with early adoption permitted, and the Company currently intends to adopt ASU 2016-02 on January 1, 2019. The Company is assessing the impact ASU 2016-02 will have on its consolidated financial statements and expects that the primary impact upon adoption will be the recognition, on a discounted basis, of its minimum commitments under noncancelable operating leases on its consolidated balance sheets resulting in the recording of right of use assets and lease obligations.
In October 2016, the FASB issued Accounting Standards Update No. 2016-16, “Intra-Entity Transfers of Assets Other Than Inventory” ("ASU 2016-16"). The amendments in this update eliminate the exception of recognizing, at the time of transfer, current and deferred income taxes for intra-entity asset transfers other than inventory. ASU 2016-16 is effective for interim and annual reporting periods beginning after December 15, 2017, and should be applied on a modified retrospective transition basis. The Company is currently planning to adopt ASU 2016-16 on January 1, 2018. The Company has estimated that there will be a remaining deferred tax benefit of $6.5 million recorded in prepaid expenses and other current assets and other assets as of December 31, 2017, which represents the tax benefit that was deferred in accordance with current GAAP. At adoption, the Company will recognize this amount through a cumulative-effect adjustment to retained earnings.

In January 2017, the FASB issued Accounting Standards Update No. 2017-01, "Business Combinations (Topic 805): Clarifying the Definition of a Business" ("ASU 2017-01"). The amendments in this update clarify the definition of a business with the objective of adding guidance to assist entities with evaluating whether transactions should be accounted for as acquisitions (or disposals) of assets or businesses. ASU 2017-01 is effective for interim and annual reporting periods beginning after December 15, 2017. The Company currently intends to adopt ASU 2017-01 on January 1, 2018, and does not expect the adoption of ASU 2017-01 to have a material impact on its consolidated financial statements.

In January 2017, the FASB issued Accounting Standards Updated No. 2017-04, “Intangibles - Goodwill and Other (Topic 350): Simplifying the Test for Goodwill Impairment” (“ASU 2017-04”). The amendments in this update simplify the subsequent measurement of goodwill by removing the second step of the two-step impairment test. The amendment requires an entity to perform its annual, or interim goodwill impairment test by comparing the fair value of a reporting unit with its carrying amount. An impairment charge should be recognized for the amount by which the carrying amount exceeds the reporting unit's fair value; however, the loss recognized should not exceed the total amount of goodwill allocated to that reporting unit. An entity still has the option to perform the qualitative assessment for a reporting unit to determine if the quantitative impairment test is necessary. The amendment should be applied on a prospective basis. ASU 2017-04 is effective for annual or any interim goodwill impairment tests in fiscal years beginning after December 15, 2019. Early adoption is permitted for interim or annual goodwill impairment tests performed on testing dates after January 1, 2017. The amendments in ASU 2017-04 are to be applied on a prospective basis and are not expected to have a material impact on the Company’s consolidated financial statements.

Critical Accounting Policies and Estimates

The Company reaffirms the critical accounting policies and its use of estimates as reported in its Form 10-K for the fiscal year ended December 31, 2016, as described in Note 1, "Nature of Business and Significant Accounting Policies," of the Notes to the Consolidated Financial Statements included in the Form 10-K for the fiscal year ended December 31, 2016.

Contractual Obligations

There were no material changes to the Company's contractual obligations outside the ordinary course of its business during the quarter ended September 30, 2017.

Contingencies

See Note 15, "Contingencies," of the Notes to the Consolidated Financial Statements for a description of an ongoing lawsuit filed by Raytheon Company against FLIR Systems, Inc. and its subsidiary, FLIR Commercial Systems, Inc., the disclosure of certain matters by the Company to the United States Department of State Office of Defense Trade Controls Compliance, communications to the Company from the United States Department of Commerce Bureau of Industry and Security, and the Company's current estimates of the range of potential loss associated with quality concerns identified by the Company regarding certain SkyWatch Surveillance Towers.

ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

As of September 30, 2017, the Company has not experienced any changes in market risk exposure that would materially affect the quantitative and qualitative disclosures about market risk presented in the Company’s Annual Report on Form 10-K for the fiscal year ended December 31, 2016.

ITEM 4. CONTROLS AND PROCEDURES

Evaluation of Disclosure Controls and Procedures

As of September 30, 2017, the Company completed an evaluation, under the supervision and with the participation of the Company’s management, including the Company’s Chief Executive Officer and the Company’s Chief Financial Officer, of the effectiveness of the design and operation of the Company’s disclosure controls and procedures. Based on the evaluation, the Company’s Chief Executive Officer and Chief Financial Officer have concluded that the Company’s disclosure controls and procedures are effective to ensure that information required to be disclosed by the Company in the reports it files or submits under the Securities Exchange Act of 1934, as amended, is recorded, processed, summarized and reported within the time periods specified in Securities and Exchange Commission rules and forms.

Changes in Internal Control Over Financial Reporting

There was no change in the Company’s internal control over financial reporting that occurred during the Company’s fiscal quarter ended September 30, 2017, that has materially affected, or is reasonably likely to materially affect, such internal control over financial reporting.

PART II. OTHER INFORMATION

ITEM 1. LEGAL PROCEEDINGS

The Company is subject to legal proceedings, claims and litigation arising in the ordinary course of its business. See Note 15, "Contingencies" of the Notes to the Consolidated Financial Statements for additional information on the Company's legal proceedings.

ITEM 1A. RISK FACTORS

The following are important factors that could cause actual results or events to differ materially from those contained in any forward-looking statements made by or on behalf of the Company. If we are unable to adequately respond to these risks and uncertainties, our business, financial condition and results of operations could be materially adversely affected. Additionally, we cannot be certain or give any assurance that any actions taken to reduce known risks and uncertainties will be effective.

Risks, Uncertainties and Other Factors Related to Our Business

We depend on the United States government for a material portion of our business and changes in government spending could adversely affect our business

We derive significant revenue from contracts or subcontracts funded by United States government agencies. A significant reduction in the purchase of our products by these agencies or contractors for these agencies would have a material adverse effect on our business. For the fiscal years ended December 31, 2016, 2015 and 2014, approximately 25 percent, 21 percent and 20 percent, respectively, of our revenues were derived directly or indirectly from sales to the United States government and its agencies. The funding of contracts awarded to us depends on the overall United States government budget and appropriations process, which is beyond our control. In addition, at its discretion, the United States government may change its spending priorities and/or terminate, reduce or modify contracts. Substantial uncertainty exists in the spending levels and priorities of the United States government, particularly with respect to military expenditures. Continued and further reductions in military spending could have a material adverse effect on our results from operations.

As a United States government supplier, we are subject to a number of procurement rules and regulations

Government contractors must comply with specific procurement regulations and other requirements and are subject to routine audits and investigations by United States government agencies. In addition, violations of these regulations or other unrelated laws and statutes can lead to debarment and other penalties. If we fail to comply with procurement rules and regulations and other laws and statutes, the results could include: reductions in the value of contracts; contract modifications or termination; the assessment of penalties and fines; and/or suspension or debarment from United States government contracting or subcontracting for a period of time or permanently. An adverse action by the United States government could also result in lost sales to non-governmental customers who might disqualify us as a result of such adverse action. The impairment or loss of our government contracts could have a material adverse effect on our business.

Operating margins may be negatively impacted by reduction in sales or by a change in the mix of products sold

Our expense levels are based, in part, on our expectations regarding future sales and these expenses are largely fixed in the short term. Some expenses, such as those related to research and development activities, would likely be maintained in the event of a sales downturn in order to maintain and enhance the long-term competitiveness of the Company. We maintain inventories of finished goods, components and raw materials at levels we believe are necessary to meet anticipated sales. Accordingly, we may not be able to reduce our costs in a timely manner to compensate for any unexpected shortfall between forecasted and actual sales. Any significant shortfall of sales may result in us carrying higher levels of inventories of finished goods, components and raw materials thereby increasing our risk of inventory obsolescence and corresponding inventory write-downs and write-offs. Our fixed costs, including facilities and information technology costs, compliance and public company costs, and depreciation and amortization related to previous acquisitions and capital expenditures, are significant and are difficult to reduce in the short term.

Our operating margins vary by product and substantial changes in the mix of products sold could also have a negative impact on our operating margins.

We may experience impairment in the value of our tangible and intangible assets

Our industry is subject to rapid changes in technology, which may result in unexpected obsolescence or impairment of our assets. Our intangible assets, including goodwill, represent a significant portion of our total assets. Most of these intangibles are the result of acquisitions in which the purchase price exceeded the value of the tangible assets acquired. We amortize certain of these intangibles over their anticipated useful life and review goodwill and indefinite-lived intangible assets for impairment annually or more frequently if warranted by events. To date we have not experienced any impairment of our intangible assets, but there can be no assurance that we will not experience such impairment in the future. In addition, certain of our tangible assets such as inventory and machinery and equipment may experience impairment in their value as a result of such events as the introduction of new products, changes in technology or changes in customer demand patterns. We depreciate our machinery and equipment at levels we believe are adequate; however, there can be no assurance that there will not be a future impairment that may have a material impact on our business, financial condition and results of operations.

Unfavorable results of legal proceedings could materially adversely affect us

We are subject to various legal proceedings and claims that have arisen out of the ordinary conduct of our business and are not yet resolved, and additional claims may arise in the future. Results of legal proceedings cannot be predicted with certainty. Regardless of merit, litigation may be both time-consuming and disruptive to our operations and could cause significant expense and diversion of management attention. From time to time, we are involved in lawsuits concerning intellectual property, torts, contracts, shareholder litigation, administrative and regulatory proceedings and other matters, as well as governmental inquiries and investigations, the outcomes of which may be significant to our results of operations and may limit our ability to engage in our business activities. In recognition of these considerations, we have and may in the future enter into material settlements to avoid ongoing costs and efforts in defending or pursuing a matter. Should we fail to prevail in certain matters, or should several of these matters be resolved against us in the same reporting period, we may be faced with significant monetary damages or injunctive relief against us that could adversely affect our business, financial condition, operating results and cash flows. While we have insurance related to our business operations, it may not apply to or fully cover liabilities we incur as a result of these lawsuits. We record accruals for liabilities where we believe a loss to be probable and reasonably estimable. However, our actual costs may differ materially from these estimates.

We face risks from international sales and business activities

We market and sell our products worldwide and international sales have accounted for, and are expected to continue to account for, a significant portion of our revenue. For the years ended December 31, 2016, 2015 and 2014, international sales accounted for 46 percent, 47 percent and 49 percent, respectively, of our total revenue. We also manufacture certain products and subassemblies in Europe and we have several contract manufacturing agreements with third parties in Europe and in Asia. Certain of these products, particularly our thermal and infrared products, are subject to substantial government regulation and licensing and end use restrictions throughout the world. Our international business activities are subject to a number of risks, including:

- the imposition of and changes to governmental licensing restrictions and controls impacting our technology and products;
- restrictions and prohibitions on the export of technology and products, including recent changes in regulation prohibiting the sale of certain of our products to certain end users without a license;
- international trade restrictions;
- difficulty in collecting receivables and governmental restrictions with respect to currency;
- inadequate protection of intellectual property;
- labor union activities;
- changes in tariffs and taxes;
- restrictions on repatriation of earnings;
- restriction on the importation and exportation of goods and services;
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risks, costs, impacts and obligations associated with the United States Foreign Corrupt Practices Act ("FCPA"), and other anti-bribery and anti-corruption laws applicable to us, and laws applicable to global trade and United States exports and costs and penalties from violations of such laws and related regulations, including the costs associated with required remedial and other increased compliance activity;

- difficulties in staffing and managing international operations; and
- political and economic instability.

Some of these factors recently have had an adverse impact on our sales and operations and increased the Company's cost of doing business and subjected the business to additional rules, policies and procedures that impacted the operation of the Company. No assurance can be given that these factors will not have a material adverse effect on our future international sales and operations and, consequently, on our business, financial condition and results of operations. Furthermore, compliance with complex foreign and U.S. laws and regulations that apply to our international operations increases our cost of doing business both in the United States and in international jurisdictions. These regulations include import and export laws, anti-competition laws, anti-corruption laws, such as the FCPA and the U.K. Bribery Act, and other local laws prohibiting corrupt payments to governmental officials, data privacy requirements, tax laws, and accounting, internal control and disclosure requirements. For example, on April 8, 2015, the Company and the Securities and Exchange Commission ("SEC") entered into an agreement through entry of an Order Instituting Cease-and-Desist Proceedings Pursuant to Section 21C of the Securities and Exchange Act of 1934, Making Findings, and Imposing a Cease-and-Desist Order (the "SEC Order"). The SEC Order settled charges under the FCPA with respect to incidents of improper travel and gifts involving FLIR's Middle East operation. Pursuant to the SEC Order, the Company is obligated to "cease and desist" from committing any future violations of the Securities Exchange Act of 1934, as amended. Violations of these laws and regulations could result in civil and criminal fines, penalties and sanctions against us, our officers or our employees, prohibitions on the conduct of our business and on our ability to offer our products and services in one or more countries, and could also materially affect our reputation, business and results of operations. In certain foreign jurisdictions, there is a higher risk of fraud or corruption and greater difficulty in maintaining effective internal controls and compliance programs. Further, although we have implemented and continue to implement policies and procedures designed to promote compliance with applicable laws and regulations, there can be no assurance that our employees, contractors or agents will not violate our policies or applicable laws and regulations. In addition, our international contracts may include industrial cooperation agreements requiring specific in-country purchases, investments, manufacturing agreements or other financial obligations, known as offset obligations, and may provide for penalties if we fail to meet such requirements. The impact of these factors is difficult to predict, but one or more of them could have a material adverse effect on our financial position, results of operations, or cash flows.

We face risks from currency fluctuations

Historically, currency fluctuations have affected our operating results. Changes in the value of foreign currencies in which our sales or costs incurred are denominated have in the past caused, and could in the future cause, fluctuations in our operating results. We seek to reduce our exposure to currency fluctuations by denominating, where possible, our international sales in United States dollars, by balancing expenses and revenues in various currencies and by undertaking limited hedging of forecasted currency exposures. With respect to international sales denominated in United States dollars, a decrease in the value of foreign currencies relative to the United States dollar could make our products less price competitive.

We may not be successful in obtaining the necessary export licenses to conduct operations abroad and the United States government may prevent proposed sales to foreign governments and customers

Export licenses and other authorizations are required from United States government agencies under the ITAR, the Export Administration Regulation ("EAR"), the Office of Foreign Assets Control ("OFAC") Regulations, the Trading with the Enemy Act of 1917, the International Emergency Economic Powers Act ("IEEPA"), the Arms Export Control Act of 1976 ("AECA"), and other similar laws and regulations for the sale, use and export of many of our products and related data and services. Thermal and infrared products and technical data have been subject to the ITAR and EAR, historically under United States Munitions List ("USML") Category XII and Commerce Control List ("CCL") Category 6. Recently, the United States Government's export reform effort resulted in the transition of various Company products from the USML to the CCL, shifting the licensing requirements and restrictions for products regulated by the Department of Commerce under the EAR. This transition has increased the licensing requirements and restrictions on some products and reduced the requirements and restrictions on others. We can give no assurance that we will be successful in obtaining the necessary licenses from the United States Department of State or Department of Commerce required to conduct our business as presently or historically conducted.

The United States export licensing environment has been affected by a number of factors, including but not limited to, the aftermath of 9/11, the rise of terrorism and the changing geopolitical environment, heightened tensions with other countries (which shift and evolve over time), and the United States reliance on the tactical advantage of the night-time war fighter. Some of these factors have affected the thermal imaging and infrared technology industry overall while others have impacted the Company directly. In addition, the Company’s 2014 submission to the United States Department of State Office of Defense Trade Controls Compliance (“DTCC”) pursuant to ITAR § 127.12(c), regarding the unauthorized export of technical data and defense services to dual and third country nationals in at least four facilities of the Company, have led to heightened scrutiny of export licenses for products in our markets and in some cases, has resulted in lengthened drafting and review periods for our license applications, including in countries where we have historically made significant sales. Subsequent engagement with the DTCC as part of the Company’s 2014 and related submissions and other communications concerning the Company’s licensing posture overall, highlight DTCC’s focus on the manner in which the Company handles exports of its products, technical data and services subject to the ITAR. In addition, concerns with respect to potential diversion of certain of the Company's products to prohibited end users and countries subject to economic and other sanctions implemented by the United States government has caused the United States Department of Commerce Bureau of Industry and Security to restrict recently the Company’s ability to sell 9hz thermal products without a license to customers in China not identified on a list maintained by the United States Department of Commerce.

Although we have taken actions and continue to take additional actions necessary to implement policies and procedures to promote an improved compliance culture and programs, there is no guarantee that our actions will be effective or that government agencies will not view our actions and programs with heightened scrutiny, including as a result of events outside the Company’s control. As a result, we may receive more restrictive provisos or limitations on new license requests, wholesale denials of our license requests, suspensions or terminations of our existing licenses, or delays in receiving new licenses resulting from requests for follow-up information, due diligence requests or additional limitations on our sale to third parties. We can give no assurance that we will be successful in obtaining necessary licenses required to facilitate our international business. Failures to obtain or delays in obtaining licenses may prevent or limit our ability to market, sell, export, or transfer our products outside the United States and has had and could continue to have a material adverse effect on our business and its operating results.

General economic conditions may adversely affect our business, operating results and financial condition

Our operations and performance depend significantly on worldwide economic conditions and their impact on levels of capital investment and consumer spending. Economic factors that could adversely influence demand for the Company’s products include uncertainty about global economic conditions leading to reduced levels of investment, changes in government spending levels and/or priorities, the size and availability of government budgets, customers’ and suppliers’ access to credit, consumer confidence and other macroeconomic factors affecting government, industrial or consumer spending behavior.

In recent years, our performance has been negatively impacted by reduced spending by United States government agencies, global economic weakness, and the Eurozone crisis. Continuation of the conditions that led to reduced spending and potential further reductions in spending globally by either consumers or government agencies could have a material adverse effect on our business, financial condition and results of operations.

Our primary markets are volatile and unpredictable

Our business depends on the demand for our products and solutions in a variety of commercial, industrial and government markets. In the past, the demand for our products in these markets has fluctuated due to a variety of factors, some of which are beyond our control, including:

- the timing, number and size of orders from, and shipments to, our customers, as well as the relative mix of those orders;
- variations in the volume of orders for a particular product or product line in a particular fiscal quarter;
- the size and timing of new contract awards;
- the timing of the release of government funds for procurement of our products; and
- the timing of orders and shipments within a given fiscal quarter.

Seasonal fluctuations in our operating results are an outcome of:
- the seasonal pattern of contracting by the United States government and certain foreign governments;
- the desire of customers to take delivery of equipment prior to fiscal year ends due to funding considerations; and
- the tendency of commercial enterprises to utilize fully annual capital budgets prior to expiration.

Competition in our markets is intense and our failure to compete effectively could adversely affect our business

Competition in the markets for our products is intense. The speed with which companies can identify new applications for thermal imaging, develop products to meet those needs and supply commercial quantities at low prices to the market are important competitive factors. We believe the principal competitive factors in our markets are product performance, price, customer service and training, product reputation, and effective marketing and sales efforts. Many of our competitors have greater financial, technical, research and development, and marketing resources than we do. All of these factors, as well as the potential for increased competition from new market entrants, require us to continue to invest in, and focus on, research and development and new product innovation. No assurance can be given that we will be able to compete effectively in the future and a failure to do so could have a material adverse effect on our business, financial condition and results of operations.

Our products may suffer from defects or errors leading to substantial product liability, damage or warranty claims

We include complex system designs and components in our products that may contain errors or defects, particularly when we incorporate new technology into our products or release new versions. If any of our products are defective, we might be required to redesign or recall those products or pay substantial damages or warranty claims. Such an event could result in significant expenses including expenses arising from product liability and warranty claims. It also could disrupt sales and affect our reputation and that of our products, which could have a material adverse effect on our business, financial condition and results of operations. As we expand our presence into new markets, we may face increased exposure to product liability claims. We maintain product liability insurance but cannot be certain that it will be sufficient or will continue to be available on acceptable terms.

Risks, Uncertainties and Other Factors Related to Our Technology and Intellectual Property

Our inability to protect our intellectual property and proprietary rights and avoid infringing the rights of others could harm our competitive position and our business

Our ability to compete successfully and achieve future revenue growth depends, in part, on our ability to protect our proprietary technology and operate without infringing the rights of others. To accomplish this, we rely on a combination of patent, trademark, copyright and trade secret laws, confidentiality agreements and contractual provisions to protect our proprietary rights. Many of our proprietary rights are held in confidence as trade secrets and are not covered by patents, making them more difficult to protect. Although we currently hold worldwide patents covering certain aspects of our technologies and products, and we are actively pursuing additional patents, we cannot be certain that we will obtain additional patents or trademarks on our technology, products and trade names. Furthermore, we cannot be certain that our patents or trademarks will not be challenged or circumvented by our competitors or that measures taken by us to protect our proprietary rights will adequately deter their misappropriation or disclosure. Any failure by us to protect our intellectual property could have a material adverse effect on our business, financial condition and results of operations. Moreover, because intellectual property does not necessarily prevent our competitors from entering the markets we serve, there can be no assurance that we will be able to maintain our competitive advantage or that our competitors will not develop capabilities equal or superior to ours.

Litigation over patents and other intellectual property is common in our industry. We have been the subject of patent and other intellectual property litigation in the past and cannot be sure that we will not be subject to such litigation in the future. Similarly, there exists the possibility we will assert claims in litigation to protect our intellectual property. Lawsuits defending or prosecuting intellectual property claims and related legal and administrative proceedings could result in substantial expense to us and significant diversion of effort of our personnel. An adverse determination in a patent suit or in any other proceeding in which we are a party could subject us to significant liabilities, result in the loss of intellectual property rights we claim or impact our competitive position. Additionally, an adverse determination could require us to seek licenses from third parties. If such licenses are not available on commercially reasonable terms or at all, our business, financial condition and results of operations could be adversely affected.

Our future success will depend on our ability to respond to the rapid technological change in the markets in which we compete, our ability to introduce new or enhanced products and enter into new markets

The markets in which we compete are characterized by rapid technological developments and frequent new product introductions, enhancements and modifications. Our ability to develop new products and technologies that anticipate changing customer requirements, reduce costs and otherwise retain or enhance our competitive position in existing and new markets will be an important factor in our future results from operations. We will continue to make substantial capital expenditures and incur significant research and development costs to improve our manufacturing capability, reduce costs, and develop and introduce new products and enhancements. If we fail to develop and introduce new products and technologies in a timely manner, our business, financial condition and results of operations would be adversely affected. In addition, we cannot be certain that our new products and technologies will be successful or that customers will accept any of our new products.

Our business could be negatively impacted by cybersecurity threats and other security threats and technology disruptions

We face certain security threats and technology disruptions, including threats to our information technology infrastructure, attempts to gain access to our or our customers' proprietary or classified information, threats to the physical security of our facilities and employees, threats of terrorism events, and failures of our technology tools and systems. We are subject to laws and rules issued by various agencies concerning safeguarding and maintaining infrastructure and physical security and information confidentiality. Our information technology networks and related systems are critical to the operation of our business and essential to our ability to successfully perform day-to-day operations. We are also involved with information technology systems for certain customers and other third parties, for which we face similar security threats as for our own. In particular, cybersecurity threats-which include, but are not limited to, computer viruses, spyware and malware, attempts to access information, denial of service attacks and other electronic security breaches-are persistent and evolve quickly. Such threats have increased in frequency, scope and potential impact in recent years. Further, a variety of technological tools and systems, including both company-owned information technology and technological services provided by outside parties, support our critical functions. These technologies, as well as our products, are subject to failure and the user's inability to have such technologies properly supported, updated, expanded or integrated into other technologies and may contain open source and third party software which may unbeknownst to us contain defects or viruses that pose unintended risks to our customers. These risks if not effectively mitigated or controlled could materially harm our business or reputation. While we believe that we have implemented appropriate measures and controls, there can be no assurance that such actions will be sufficient to prevent disruptions to critical systems, unauthorized release of confidential information or corruption of data.

We require user names and passwords in order to access our information technology systems. We use encryption and authentication technologies designed to secure the transmission and storage of data and prevent access to our data or accounts. These security measures are subject to third-party security breaches, employee error, malfeasance, faulty password management or other irregularities. For example, third parties may attempt to induce by fraud employees or customers into disclosing user names, passwords or other sensitive information, which may in turn be used to access our information technology systems. These security systems cannot provide absolute security. To the extent we were to experience a breach of our systems and were unable to protect sensitive data, such a breach could materially damage business partner and customer relationships, and curtail or otherwise impact the use of our information technology systems. Moreover, if a security breach of our information technology system affects our computer systems or results in the release of personally identifiable or other sensitive information of customers, business partners, employees and other third parties, our reputation and brand could be materially damaged, use of our products and services could decrease, and we could be exposed to a risk of loss, litigation and potential liability.

Although we have in the past and continue to be subject to cybersecurity threats and other security threats and technology disruptions, to date none has had a material impact on our business, financial condition or results of operations. Nonetheless, in the future, these types of events could disrupt our operations and customer and other third party information technology systems. They also could require significant management attention and resources, negatively impact our reputation among our customers and the public and challenge our eligibility for future work on sensitive or classified systems, which could have a material adverse effect on our business, financial condition and results of operations.

Risks, Uncertainties and Other Factors Related to Our Corporate Structure and Organization

Our future success depends in part on attracting and retaining key senior management and qualified technical, sales and other personnel

Our future success depends in part on the efforts and continued services of our key executives and our ability to attract and retain qualified technical, sales and other personnel. Significant competition exists for such personnel and we cannot assure the retention of our key executives, technical and sales personnel or our ability to attract, integrate and retain other such personnel that may be required in the future. We cannot assure that employees will not leave and subsequently compete against us. If we are unable to attract and retain key personnel, our business, financial condition and results of operations could be adversely affected.

We must successfully manage a complex global organization

As we have grown, the size and scope of our worldwide operations have also increased substantially. We currently design, manufacture and market numerous product lines in locations worldwide. Significant management time and effort is required to manage effectively the increased complexity of the business and our failure to successfully do so could have a material adverse effect on our business, financial condition and results of operations. Our inability to continue to manufacture our products at one or more of our facilities as a result of, for example, a prolonged power outage, earthquake, fire or other natural disaster, or labor or political unrest, could prevent us from supplying products to our customers and could have a material adverse effect on our business, financial condition and results of operations.

We may be unable to integrate successfully recent or future acquisitions into our operations, thereby disrupting our business and harming our financial condition and results of operations

We have made twelve acquisitions of various sizes in the past five years. The integration of businesses, personnel, product lines and technologies can be difficult, time consuming and subject to significant risks. For example, we could lose key personnel from companies that we acquire, incur unanticipated costs, lose major sources of revenue, fail to integrate critical technologies, suffer business disruptions, fail to capture anticipated synergies, fail to establish satisfactory internal controls, or incur unanticipated liabilities. Any of these difficulties could disrupt our ongoing business, distract our management and employees, increase our expenses and decrease our revenue.

We frequently evaluate strategic opportunities available to us and it is likely that we will make additional acquisitions in the future. Such acquisitions may vary in size and complexity. Any future acquisitions are subject to the risks described above. Furthermore, we might assume or incur additional debt or issue additional equity securities to pay for future acquisitions. Additional debt may negatively impact our results and increase our financial risk, and the issuance of any additional equity securities could dilute our then existing shareholders' ownership. No assurance can be given that we will realize anticipated benefits of any future acquisitions, or that any such acquisition or investment will not have a material adverse effect on our business, financial condition and results of operations.

We have indebtedness as a result of the issuance of our 3.125 percent senior unsecured notes (the "Notes") and borrowings against our unsecured credit facility, and we are subject to certain restrictive covenants under our unsecured credit facility and the indenture governing the Notes which may limit our operational and financial flexibility

Our ability to meet our debt service obligations and comply with the financial covenants under our credit facility will be dependent upon our future performance, which will be subject to financial, business and other factors affecting our operations, many of which are beyond our control. Our inability to meet our debt service obligations or comply with the required covenants could result in a default under the credit facility or indenture. In the event of any such default, under the credit facility, the lenders thereunder could elect to declare all outstanding debt, accrued interest and fees under the facility to be due and immediately payable. In the event of any such default under our indenture, either the trustee or the holders of at least 25 percent of the outstanding principal amount of the Notes could declare the principal amount of all of the Notes to be due and payable immediately.

We may not be able to refinance our indebtedness on favorable terms, if at all, which could materially and adversely affect our liquidity and our ongoing results of operations.

Our ability to refinance indebtedness, including the Notes, will depend in part on our operating and financial performance, which, in turn, is subject to prevailing economic conditions and to financial, business, legislative, regulatory and other factors beyond our control. In addition, prevailing interest rates or other factors at the time of refinancing could increase our interest expense. A refinancing of our indebtedness, including the Notes, could also require us to comply with more onerous covenants and further restrict our business operations. Our inability to refinance our indebtedness or to do so upon favorable terms could materially and adversely affect our business, results of operations, financial condition and cash flows, and make us vulnerable to adverse industry and general economic conditions.

Changes in our effective income tax rate may have an adverse effect on our results of operations

We are subject to taxes in the United States and numerous foreign jurisdictions, including Belgium, where a number of our subsidiaries are organized. Due to economic and political conditions, tax rates in various jurisdictions may be subject to significant change. Our future effective tax rate could be affected by changes in the mix of earnings in countries with different statutory tax rates, changes in the valuation of deferred tax assets and liabilities, changes in the enforcement environment, and changes in tax laws or their interpretations, including in the United States and in foreign jurisdictions. For example, in January 2016, the European Commission announced a decision concluding that certain rules under Belgian tax legislation are deemed to be incompatible with European Union regulations on state aid. As a result of this decision, the European Commission has directed the Belgian Government to recover past taxes from certain entities, reflective of disallowed state aid, which impacts one of the Company’s international subsidiaries. The Belgian Government announced they have appealed this decision and filed action for an annulment in the General Count of the European Union, and in July 2016 the Company filed a separate appeal with the General Court of the European Union.   The Company recorded discrete tax expense of $39.6 million during 2016 related to this matter and on January 10, 2017, received tax assessments from the Belgium government for a similar amount. The Company has filed a complaint against the Belgian tax assessments, and the result of this complaint, the appeal with the General Court of the European Union, new information received from the Belgian Government, or other future events may cause the income tax provision associated with the decision to be entirely or partially reversed.

Our future effective tax rate may be adversely affected by a number of additional factors including:

- the jurisdictions in which profits are determined to be earned and taxed;
- the resolution of issues arising from tax audits with various tax authorities;
- changes in the valuation of our deferred tax assets and liabilities;
- adjustments to estimated taxes upon finalization of various tax returns;
- increases in expenses not deductible for tax purposes;
- changes in available tax credits;
- changes in share-based compensation expense;
- changes in tax laws or the interpretation of such tax laws and changes in generally accepted accounting principles;
- changes in foreign tax rates or agreed upon foreign taxable base; and/or
- the repatriation of earnings from outside the United States for which we have not previously provided for United States taxes.

Any significant increase in our future effective tax rates could adversely impact net income for future periods. In addition, the United States Internal Revenue Service (“IRS”) and other tax authorities regularly examine our income tax returns. Our financial condition and results of operations could be adversely impacted if any assessments resulting from the examination of our income tax returns by the IRS or other taxing authorities are not resolved in our favor.

State of Oregon law and our charter documents contain provisions that could discourage or prevent a potential takeover, even if the transaction would benefit our shareholders

Other companies may seek to acquire or merge with us. An acquisition or merger of our Company could result in benefits to our shareholders, including an increase in the value of our common stock. Some provisions of our Articles of Incorporation and Bylaws, including our ability to issue preferred stock without further action by our shareholders, as well as provisions of the State of Oregon law, may discourage, delay or prevent a merger or acquisition that a shareholder may consider favorable.

ITEM 2. UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS
None.

ITEM 3. DEFAULTS UPON SENIOR SECURITIES

None.

ITEM 4. MINE SAFETY DISCLOSURES

Not applicable.

ITEM 5. OTHER INFORMATION
None.

ITEM 6. EXHIBITS

Number	Description
10.1	Separation and Release of Claims Agreement between FLIR Systems, Inc. and Thomas A. Surran effective as of September 30, 2017.(1)
10.2	Executive Officer Severance Plan Agreement between FLIR Systems, Inc. and Thomas A. Surran dated April 24, 2017.(1)
10.3	FLIR Systems, Inc. Executive Officer Severance Plan, effective May 1, 2017.(1)
10.4	Offer Letter (the "Offer Letter") between FLIR Systems, Inc. and Carol P. Lowe dated as of October 16, 2017 (incorporated by reference to Exhibit 10.1 of the Current Report on Form 8-K filed on October 24, 2017).(1)
10.5	Change of Control Agreement between FLIR Systems, Inc. and Carol P. Lowe attached to the Offer Letter as Attachment A (incorporated by reference to Exhibit 10.2 of the Current Report on Form 8-K filed on October 24, 2017).(1)
31.1	Principal Executive Officer Certification Pursuant to Sarbanes-Oxley Act of 2002, Section 302.
31.2	Principal Financial Officer Certification Pursuant to Sarbanes-Oxley Act of 2002, Section 302.
32.1	Certification by the Chief Executive Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
32.2	Certification by the Chief Financial Officer 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

(1) This exhibit constitutes a management contract or compensatory plan or arrangement.

SIGNATURE

Pursuant to the requirements of the Securities Exchange Act of 1934, the Registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

FLIR SYSTEMS, INC.

Date October 27, 2017 /s/ Shane R. Harrison
Shane R. Harrison
Sr. Vice President, Corporate Development & Strategy and Interim Chief Financial Officer
(Duly Authorized and Principal Financial Officer)