STERICYCLE INC
Form 10-Q/A
August 09, 2016

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q/A

(Amendment No. 1)

x QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the quarterly period ended March 31, 2016 or

o TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the transition period from to

Commission File Number 1-37556

Stericycle, Inc.

(Exact name of registrant as specified in its charter)

Delaware	36-3640402
(State or other jurisdiction of incorporation or organization)	(IRS Employer Identification Number)

28161 North Keith Drive

Lake Forest, Illinois 60045

(Address of principal executive offices, including zip code)

(847) 367-5910

(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 reports), and (2) has been subject to such filing requirements for the past 90 days. YES x NO o

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). YES x NO o

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

Large accelerated filer	x	Accelerated filer	o
Non-accelerated filer	o	Smaller reporting company	o

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

On April 29, 2016 there were 84,912,603 shares of the Registrant's Common Stock outstanding.

EXPLANATORY NOTE

Stericycle, Inc. (the "Company," "we" or "our") is filing this amended Quarterly Report on Form 10-Q/A because the Audit Committee of our Board of Directors has determined that the consolidated financial statements for the quarters ended March 31, 2015, June 30, 2015 and September 30, 2015, originally included in the Company's Quarterly Reports on Form 10-Q for each of the respective quarterly periods, should no longer be relied upon due to errors in the timing of recognition of certain loss reserves. This Form 10-Q/A is being filed to present the amended and restated financial information for the first fiscal quarter of 2015 and, accordingly, to restate our analysis of the first quarter of 2016 when compared to the first quarter of 2015, as presented in the Company's Form 10-Q for the first quarter of 2016 filed on May 9, 2016 (the "Original Form 10-Q"), and to disclose additional information regarding the Company's internal control over financial reporting and disclosure controls and procedures related to these errors.

The errors in timing of recognition of certain loss reserves relate to the Company's settlement of two previously disclosed litigation matters: first, a class action complaint filed in the Circuit Court of Cook County, Illinois captioned Sawyer v. Stericycle, Inc., et al., Case No. 2015 CH 07190 (the "TCPA Action"), alleging that from 2010 to 2014, the Company violated the Telephone Consumer Protection Act of 1991, as amended by the Junk Fax Prevention Act of 2005; and second, a qui tam action filed in the U.S. District Court for the Northern District of Illinois captioned United States of America ex rel. Jennifer D. Perez v. Stericycle, Inc., Case No. 1:08-cv-2390 (the "Qui Tam Action"), alleging that from January 1, 2003 to June 30, 2014, the Company improperly increased its service price to certain government customers without their consent or contractual authorization, in violation of the False Claims Act and similar state statutes.

The identified accounting errors related to the timing of recognition of loss reserves between quarterly periods and had no effect on the Company's audited annual results for the fiscal year ended December 31, 2015.

We originally recorded $45.0 million in accrued liabilities related to the TCPA Action in the second quarter of 2015; we are now of the view that this amount should have been recorded in the first quarter of 2015. In addition, we originally recorded $28.5 million in accrued liabilities related to the Qui Tam Action in the third quarter of 2015; we are now of the view that this amount also should have been recorded in the first quarter of 2015.

The impact of the restatement is as follows:

- the estimated loss contingency for the first quarter of fiscal 2015 was understated by $73.5 million, resulting in an overstatement of net income of $46.5 million for the three month period ended March 31, 2015;
- the estimated loss contingency for the second quarter of fiscal 2015 was overstated by $45.0 million, resulting in an understatement of net income of $27.4 million for the three month period ended June 30, 2015. For the six month period ended June 30, 2015, the estimated loss contingency was understated by $28.5 million, resulting in an overstatement of net income of $19.1 million for the six month period ended June 30, 2015; and
- the estimated loss contingency for the third quarter of fiscal 2015 was overstated by $28.5 million, resulting in an understatement of net income of $17.2 million for the three month period ended September 30, 2015.

Accordingly, we are filing this Form 10-Q/A to correct the errors presented in the comparative financial information included in the Original Form 10-Q for the three months ended March 31, 2015.

The errors, including the specific line items on each of the Company's financial statements that have been restated, are described in greater detail in Note A1 contained in this Form 10-Q/A. We have made necessary conforming changes in Management's Discussion and Analysis of Financial Condition and Results of Operations in this Form 10-Q/A resulting from this adjustment.

The Company's controls related to the accounting for loss contingencies were inadequate to ensure that loss reserves were recorded timely in the appropriate period. We are revising the COSO Component – Risk Assessment material weakness described in Item 4 of Part I, Controls and Procedures, to also encompass the accounting for loss contingencies.

For the convenience of the reader, this report on Form 10-Q/A sets forth the Original Form 10-Q in its entirety. The following sections of the Original Form 10-Q have been restated:

1) Item 1 of Part I, Financial Statements;
2) Item 2 of Part I, Management's Discussion and Analysis of Financial Condition and Results of Operations;
3) Item 4 of Part I, Controls and Procedures; and
4) Item 6 of Part II, Exhibits.

Specifically, the following sections within Item 1 of Part I have been restated or added:

1) Condensed Consolidated Statements of Income;
2) Condensed Consolidated Statements of Comprehensive Income;
3) Condensed Consolidated Statements of Cash Flows;
4) Note A1 – Restatement;
5) Note 5 – Income Taxes;
6) Note 8 – Earnings per Common Share; and
7) Note 12 – Geographic Information.

The Company has also included the signature page, the certifications of our Chief Executive Officer and Chief Financial Officer in Exhibits 31.3, 31.4, and 32.1, and financial statements formatted in Extensible Business Reporting Language (XBRL) in Exhibits 101.

Except as described above, no other amendments have been made to the Original Form 10-Q. The Company has not updated the disclosures contained herein to reflect events that have occurred since the date of the Original Form 10-Q. Accordingly, this amended quarterly report on Form 10-Q/A should be read in conjunction with the Company’s other filings made with the SEC subsequent to the filing of the Original Form 10-Q.

Stericycle, Inc.

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PART I. – FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS

STERICYCLE, INC. AND SUBSIDIARIES

CONDENSED CONSOLIDATED BALANCE SHEETS

(Unaudited)

In thousands, except share and per share data

	March 31, 2016	December 31, 2015
ASSETS		
Current Assets:		
Cash and cash equivalents	$45,655	$ 55,634
Short-term investments	64	69
Accounts receivable, less allowance for doubtful accounts of $22,964 in 2016 and $22,329 in 2015	622,709	614,494
Prepaid expenses	46,198	46,740
Other current assets	42,732	44,891
Total Current Assets	757,358	761,828
Property, plant and equipment, less accumulated depreciation of $453,753 in 2016 and $426,019 in 2015	677,525	665,602
Goodwill	3,790,016	3,758,177
Intangible assets, less accumulated amortization of $170,507 in 2016 and $151,025 in 2015	1,840,844	1,842,561
Other assets	46,801	49,282
Total Assets	$7,112,544	$ 7,077,450
LIABILITIES AND EQUITY		
Current Liabilities:		
Current portion of long-term debt	$114,066	$ 161,409
Accounts payable	133,779	149,202
Accrued liabilities	218,933	197,329
Deferred revenues	17,543	16,989
Other current liabilities	68,192	62,420
Total Current Liabilities	552,513	587,349
Long-term debt, net of current portion	3,038,083	3,052,639
Deferred income taxes	617,011	608,272
Other liabilities	86,448	81,352
Equity:		
Preferred stock (par value $0.01 per share, 1,000,000 shares authorized), Mandatory Convertible Preferred Stock, Series A, 770,000 issued and outstanding in 2016 and 2015	8	8
Common stock (par value $0.01 per share, 120,000,000 shares authorized, 84,829,822 issued and outstanding in 2016 and 84,852,584 issued and outstanding in 2015)	848	849
Additional paid-in capital	1,172,962	1,143,020
Accumulated other comprehensive loss	(265,018)	(282,631)

Retained earnings	1,897,636	1,868,645
Total Stericycle, Inc.’s Equity	2,806,436	2,729,891
Noncontrolling interest	12,053	17,947
Total Equity	2,818,489	2,747,838
Total Liabilities and Equity	$7,112,544	$ 7,077,450

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

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STERICYCLE, INC. AND SUBSIDIARIES

CONDENSED CONSOLIDATED STATEMENTS OF INCOME

(Unaudited)

In thousands, except share and per share data

	Three Months Ended March 31, 2016	2015 (Restated)
Revenues	$874,181	$663,319
Costs and Expenses:		
Cost of revenues (exclusive of depreciation shown below)	482,356	367,340
Depreciation - cost of revenues	22,641	14,648
Selling, general and administrative expenses (exclusive of depreciation and amortization shown below)	202,488	214,863
Depreciation – selling, general and administrative expenses	7,499	4,118
Amortization	18,274	8,797
Total Costs and Expenses	733,258	609,766
Income from Operations	140,923	53,553
Other Income (Expense):		
Interest income	21	35
Interest expense	(24,062)	(18,633)
Other expense, net	(1,251)	(598)
Total Other Expense	(25,292)	(19,196)
Income Before Income Taxes	115,631	34,357
Income tax expense	38,036	5,065
Net Income	77,595	29,292
Less: net income attributable to noncontrolling interests	809	352
Net Income Attributable to Stericycle, Inc.	76,786	28,940
Less: mandatory convertible preferred stock dividend	10,106	—
Net Income Attributable to Stericycle, Inc. Common Shareholders	$66,680	$28,940
Earnings Per Common Share Attributable to Stericycle, Inc. Common Shareholders:		
Basic	$0.79	$0.34
Diluted	$0.78	$0.34
Weighted Average Number of Common Shares Outstanding:		
Basic	84,705,000	85,037,823
Diluted	85,845,501	86,357,006

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

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STERICYCLE, INC. AND SUBSIDIARIES

CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME

(Unaudited)

In thousands

	Three Months Ended March 31, 2016	2015 (Restated)
Net Income	$77,595	$ 29,292
Other Comprehensive Income/ (Loss):		
Foreign currency translation adjustments	17,164	(64,501)
Amortization of cash flow hedge into income, net of tax (($172) and ($54), for the three months ended March 31, 2016 and 2015, respectively)	269	90
Change in fair value of cash flow hedge, net of tax (($89) and $2,381 for the three months ended March 31, 2016 and 2015, respectively)	242	(4,424)
Total Other Comprehensive Income/ (Loss)	17,675	(68,835)
Comprehensive Income/ (Loss)	95,270	(39,543)
Less: comprehensive income/ (loss) attributable to noncontrolling interests	871	(468)
Comprehensive Income/ (Loss) Attributable to Stericycle, Inc. Common Shareholders	$94,399	$ (39,075)

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

STERICYCLE, INC. AND SUBSIDIARIES

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

(Unaudited)

In thousands	Three Months Ended March 31, 2016	2015
		(Restated)
OPERATING ACTIVITIES:		
Net income	$77,595	$29,292
Adjustments to reconcile net income to net cash provided by operating activities:		
Stock compensation expense	6,105	5,487
Excess tax benefit of stock options exercised	—	(8,222)
Depreciation	30,140	18,766
Amortization	18,274	8,797
Deferred income taxes	6,932	(29,939)
Other, net	(2,644)	5,313
Changes in operating assets and liabilities, net of effect of acquisitions:		
Accounts receivable	(3,918)	(14,491)
Accounts payable	(15,203)	5,443
Accrued liabilities	21,151	109,424
Deferred revenues	487	(628)
Other assets and liabilities	18,030	3,312
Net cash provided by operating activities	156,949	132,554
INVESTING ACTIVITIES:		
Payments for acquisitions, net of cash acquired	(24,884)	(34,210)
Proceeds from investments	7	257
Proceeds from sale of property and equipment	766	—
Capital expenditures	(34,185)	(21,356)
Net cash used in investing activities	(58,296)	(55,309)
FINANCING ACTIVITIES:		
Repayments of long-term debt and other obligations	(6,879)	(9,780)
Proceeds from foreign bank debt	15,607	4,851
Repayments of foreign bank debt	(18,721)	(38,252)
Proceeds from term loan	—	250,000
Repayment of term loan	(171,000)	—
Proceeds from senior credit facility	457,959	394,097
Repayments of senior credit facility	(353,520)	(670,254)
Payments of capital lease obligations	(1,381)	(988)
Payment of cash flow hedge	—	(8,833)
Purchases and cancellations of treasury stock	(37,693)	(11,516)
Proceeds from issuance of common stock	22,310	27,452
Dividends paid on mandatory convertible preferred stock	(10,106)	—

Excess tax benefit of stock options exercised	—	8,222
Payments to noncontrolling interests	(4,997)	(2,603)
Net cash used in financing activities	(108,421)	(57,604)
Effect of exchange rate changes on cash and cash equivalents	(211)	(3,594)
Net (decrease)/ increase in cash and cash equivalents	(9,979)	16,047
Cash and cash equivalents at beginning of period	55,634	22,236
Cash and cash equivalents at end of period	$45,655	$38,283
NON-CASH INVESTING ACTIVITIES:		
Issuances of obligations for acquisitions	$13,013	$21,543

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

STERICYCLE, INC. AND SUBSIDIARIES

CONDENSED CONSOLIDATED STATEMENTS OF CHANGES IN EQUITY

Three Months Ended March 31, 2016 and Year Ended December 31, 2015

(Unaudited)

In thousands

	Stericycle, Inc. Equity								
	Preferred Stock		Common Stock						
	Shares	Amount	Shares	Amount	Additional Paid-In Capital	Retained Earnings	Accumulated Other Comprehensive Income (Loss)	Noncontrolling Interest	Total Equity
Balance at January 1, 2015	—	$ —	84,884	$ 849	$ 289,211	$ 1,743,371	$ (138,419)	$ 22,173	$ 1,917,185
Net income						267,046		967	268,013
Currency translation adjustment							(140,809)	161	(140,648)
Change in qualifying cash flow hedge, net of tax							(3,403)		(3,403)
Issuance of common stock for exercise of options, restricted stock units and employee stock purchases			973	10	68,630				68,640
Issuance of mandatory convertible preferred stock	770	8			746,892				746,900
Purchase and cancellation of treasury stock			(1,004)	(10)		(131,666)			(131,676)
Preferred stock dividend						(10,106)			(10,106)
Stock compensation expense					21,750				21,750
Excess tax benefit of stock options					16,897				16,897

exercised									
Reduction to noncontrolling interests due to additional ownership					(360)			(5,354)	(5,714)
Balance at December 31, 2015	770	8	84,853	849	1,143,020	1,868,645	(282,631)	17,947	2,747,838
Net income						76,786		809	77,595
Currency translation adjustment							17,102	62	17,164
Change in qualifying cash flow hedge, net of tax							511		511
Issuance of common stock for exercise of options, restricted stock units and employee stock purchases			305	3	22,870				22,873
Purchase and cancellation of treasury stock			(328)	(4)		(37,689)			(37,693)
Preferred stock dividend						(10,106)			(10,106)
Stock compensation expense					6,105				6,105
Reduction to noncontrolling interests due to additional ownership					967			(6,765)	(5,798)
Balance at March 31, 2016	770	$ 8	84,830	$ 848	$ 1,172,962	$ 1,897,636	$ (265,018)	$ 12,053	$ 2,818,489

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

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STERICYCLE, INC. AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited)

Unless the context requires otherwise, "we," "us" or "our" refers to Stericycle, Inc. and its subsidiaries on a consolidated basis.

NOTE A1 — RESTATEMENT

The unaudited quarterly financial data for the quarter ended March 31, 2015 has been restated for errors related to the timing of recognition of loss reserves between quarterly periods associated with the Company's previously disclosed settlement of the TCPA Action and Qui Tam Action. The Company determined that the estimated loss contingency for the first quarter of fiscal 2015 was understated by $73.5 million, resulting in an overstatement of net income of $46.5 million for the three month period ended March 31, 2015.

The Company's Condensed Consolidated Statements of Income; Condensed Consolidated Statements of Comprehensive Income; Condensed Consolidated Statements of Cash Flows; Note 5 - Income Taxes; Note 8 - Earnings Per Common Share; and Note 12 - Geographic Information; included in this Form 10-Q/A have been restated to correct the misstatements described above.

The following are previously reported and restated balances of affected line items in the Condensed Consolidated Statement of Income and Condensed Consolidated Statement of Comprehensive Income, and the Condensed Consolidated Statement of Cash Flows for the three months ended March 31, 2015 (Unaudited).

Condensed Consolidated Statement of Income

	Three Months Ended March 31, 2015		
	As Reported	Adjustment	Restated
Selling, general and administrative expenses (exclusive of depreciation and amortization)	$141,363	$ 73,500	$214,863
Total costs and expenses	536,266	73,500	609,766
Income from operations	127,053	(73,500)	53,553
Income before income taxes	107,857	(73,500)	34,357
Income tax expense	32,047	(26,982)	5,065
Net income	75,810	(46,518)	29,292
Net income attributable to Stericycle, Inc.	75,458	(46,518)	28,940
EPS – basic	0.89	(0.55)	0.34
EPS – diluted	0.87	(0.53)	0.34

Condensed Consolidated Statement of Comprehensive Income

	Three Months Ended March 31, 2015		
		Adjustment	Restated

	As Reported		
Net income	$75,810	$ (46,518)	$29,292
Comprehensive income/ (loss)	6,975	(46,518)	(39,543)
Comprehensive income/ (loss)attributable to Stericycle, Inc.	7,443	(46,518)	(39,075)
Condensed Consolidated Statement of Cash Flows	Three Months Ended March 31, 2015		
	As Reported	Adjustment	Restated
Net income	$75,810	$ (46,518)	$29,292
Deferred income taxes	(2,957)	(26,982)	(29,939)
Accrued liabilities	35,924	73,500	109,424

The restatement had no impact on net cash used in or provided by operating, investing and financing activities and there was no change to the reported net increase in cash and cash equivalents.

NOTE 1 – BASIS OF PRESENTATION

The accompanying condensed consolidated financial statements have been prepared pursuant to the rules and regulations of the Securities and Exchange Commission. Certain information and footnote disclosures normally included in annual consolidated financial statements prepared in accordance with generally accepted accounting principles have been condensed or omitted pursuant to such rules and regulations. However, the Company believes the disclosures included in the accompanying condensed consolidated financial statements are adequate to make the information presented not misleading. In our opinion, all adjustments necessary for a fair presentation for the periods presented have been reflected and are of a normal recurring nature. These condensed consolidated financial statements should be read in conjunction with the Stericycle, Inc. and Subsidiaries Consolidated Financial Statements and notes thereto for the year ended December 31, 2015, as filed with our Annual Report on Form 10-K for the year ended December 31, 2015. The results of operations for the three months ended March 31, 2016 are not necessarily indicative of the results that may be achieved for the entire year ending December 31, 2016.

There were no material changes in the Company's significant accounting policies since the filing of its 2015 Form 10-K. As discussed in the 2015 Form 10-K, the preparation of the consolidated financial statements in conformity with accounting principles generally accepted in the United States requires management to make certain estimates and assumptions that affect the amount of reported assets and liabilities and disclosure of contingent assets and liabilities at the date of the consolidated financial statements and revenues and expenses during the periods reported. Actual results may differ from those estimates.

We have evaluated subsequent events through the date of filing this quarterly report on Form 10-Q. No events have occurred that would require adjustment to or disclosure in the condensed consolidated financial statements.

NOTE 2 – ACQUISITIONS

The following table summarizes the locations of our acquisitions for the three months ended March 31, 2016

Acquisition Locations	2016
United States	5
Romania	1
Spain	1
Total	7

During the quarter ended March 31, 2016, we completed seven acquisitions. Domestically, we acquired 100% of the stock of one regulated waste business and selected assets of four secure information destruction businesses. Internationally, we acquired selected assets of one regulated waste business in Romania and one in Spain.

The following table summarizes the aggregate purchase price paid for acquisitions and other adjustments of consideration to be paid for acquisitions during the three months ended March 31:

In thousands

	Three Months Ended March 31,	
	2016	2015
Cash	$24,884	$34,210
Promissory notes	11,595	7,618
Deferred consideration	1,361	624
Contingent consideration	57	13,301
Total purchase price	$37,897	$55,753

During the three months ended March 31, 2016, we recognized a net increase in goodwill of $25.5 million, excluding the effect of foreign currency translation (see Note 9 – Goodwill and Other Intangible Assets). A net increase of $23.7 million was assigned to our United States reportable segment, and a net increase of $1.8 million was assigned to our International reportable segment. Approximately $20.7 million of the goodwill recognized during the three months ended March 31, 2016 will be deductible for income taxes.

During the three months ended March 31, 2016, we recognized a net increase in intangible assets from acquisitions of $8.4 million, excluding the effect of foreign currency translation. The changes include $7.7 million in the estimated fair value of acquired customer relationships with amortizable lives of 10 to 40 years and $0.7 million in covenant not-to-compete with an amortizable life of 5 years.

The purchase prices for these acquisitions in excess of acquired tangible and identifiable intangible assets have been primarily allocated to goodwill, and are preliminary, pending completion of certain intangible asset valuations and finalization of the opening balance sheet. The following table summarizes the preliminary purchase price allocation for current period acquisitions and other adjustments to purchase price allocations during the three months ended March 31:

In thousands

	Three Months Ended March 31,	
	2016	2015
Fixed assets	$3,345	$(1,477)
Intangibles	8,436	19,791
Goodwill	25,519	41,190
Accounts receivable	1,715	4,217
Net other assets/ (liabilities)	133	59
Current liabilities	(201)	(4,650)
Net deferred tax liabilities	(1,050)	(3,377)
Total purchase price allocation	$37,897	$55,753

During the three months ended March 31, 2016 and 2015, the Company incurred $3.0 million and $3.3 million, respectively, of acquisition related expenses. These expenses are included with “Selling, general and administrative expenses” (“SG&A”) on our Condensed Consolidated Statements of Income. The results of operations of these acquired businesses have been included in the Condensed Consolidated Statements of Income from the date of the acquisition.

NOTE 3 – NEW ACCOUNTING STANDARDS

Accounting Standards Recently Adopted

Compensation - Stock Compensation

On January 1, 2016, the Company adopted the guidance in Accounting Standards Update ("ASU") No. 2016-09, “Compensation - Stock Compensation (Topic 718) - Improvements to Employee Share-Based Payment Accounting.” Under this ASU, entities are permitted to make an accounting policy election to either estimate forfeitures on share-based payment awards, as previously required, or to recognize forfeitures as they occur. The Company has elected to recognize forfeitures as they occur and the impact of that change in accounting policy has been evaluated and determined to be insignificant and resulted in no cumulative-effect change to the Company’s retained earnings. Additionally, ASU 2016-09 requires that all income tax effects related to settlements of share-based payment awards be reported in earnings as an increase or decrease to income tax expense (benefit), net. Previously, income tax benefits at settlement of an award were reported as an increase (or decrease) to additional paid-in capital to the extent that those benefits were greater than (or less than) the income tax benefits reported in earnings during the award's vesting period. The requirement to report those income tax effects in earnings has been applied on a prospective basis to settlements occurring on or after January 1, 2016 and the impact of applying that guidance was $2.9 million to the condensed consolidated financial statements for the period ended March 31, 2016. ASU 2016-09 also requires that all income tax-related cash flows resulting from share-based payments be reported as operating activities in the statement of cash flows. Previously, income tax benefits at settlement of an award were reported as a reduction to operating cash flows and an increase to financing cash flows to the extent that those benefits exceeded the income tax benefits reported in earnings during the award's vesting period. The Company has elected to apply that change in cash flow classification on a prospective basis, leaving previously reported net cash provided by operating activities and net cash used in financing activities in the accompanying Condensed Consolidated Statement of Cash Flows for the period ended March 31, 2015 unchanged. The remaining provisions of ASU 2016-09 did not have a material impact on the accompanying condensed consolidated financial statements.

Accounting Standards Issued But Not Yet Adopted

Revenue From Contracts With Customers

In May 2014, the FASB issued ASU No. 2014-09, "Revenue from Contracts with Customers" (Topic 606), guidance to provide a single and comprehensive revenue recognition model for all contracts with customers. The revenue guidance contains principles that an entity will apply to determine the measurement of revenue and timing of when it is recognized. The underlying principle is that an entity will recognize revenue to depict the transfer of goods or services to customers at an amount that the entity expects to be entitled to in exchange for those goods or services. The amended authoritative guidance associated with revenue recognition is effective for the Company on January 1, 2018. The amended guidance may be applied retrospectively for all periods presented or retrospectively with the cumulative effect of initially applying the amended guidance recognized at the date of initial application. We are in the process of assessing the provisions of the new revenue recognition standard and have not determined whether the adoption will have a material impact on our consolidated financial statements.

Leases

In February 2016, the FASB issued ASU No. 2016-02, “Leases” (Topic 842). This ASU will require lessees to record a right-of-use asset and lease liability on the balance sheet for all leases with terms of more than 12 months. Recognition, measurement and presentation of expenses will depend on classification as a finance or operating lease. This ASU also requires certain quantitative and qualitative disclosures. Accounting guidance for lessors is largely unchanged. The amendments should be applied on a modified retrospective basis. ASU 2016-02 is effective for us beginning January 1, 2019. We are beginning to evaluate the impact that the adoption of ASU 2016-02 will have on our consolidated financial statements and related disclosures.

NOTE 4 – FAIR VALUE MEASUREMENTS

Fair value is defined as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. The fair value hierarchy distinguishes between (1) market participant assumptions developed based on market data obtained from independent sources (observable inputs) and (2) an entity's own assumptions about market participant assumptions developed based on the best information available in the circumstances (unobservable inputs). The fair value hierarchy consists of three broad levels, which gives the highest priority to unadjusted quoted prices in active markets for identical assets or liabilities (Level 1) and the lowest priority to unobservable inputs (Level 3). The three levels of the fair value hierarchy are described below:

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

Level 2 – Observable inputs other than quoted prices in active markets for identical assets and liabilities, quoted prices for identical or similar assets or liabilities in inactive markets, or other inputs that are observable or can be corroborated by observable market data for substantially the full term of the assets or liabilities.

Level 3 – Inputs that are generally unobservable and typically reflect management's judgment about the assumptions that market participants would use in pricing the asset or liability.

Financial assets and liabilities are classified in their entirety based on the lowest level of input that is significant to the fair value measurement. Our assessment of the significance of a particular input to the fair value measurement requires judgment, and may affect the valuation of assets and liabilities and their placement within the fair value hierarchy levels. The impact of our creditworthiness has been considered in the fair value measurements noted below. In addition, the fair value measurement of a liability must reflect the nonperformance risk of an entity. There were no movements of items between fair value hierarchies.

In thousands

	Total as of March 31, 2016	Fair Value Measurements Using Level 1 Inputs	Level 2 Inputs	Level 3 Inputs
Assets:				
Cash and cash equivalents	$ 45,655	$45,655	$ —	$—
Short-term investments	64	$64	—	—
Derivative financial instruments	954	—	954	—
Total assets	$ 46,673	$45,719	$ 954	$—
Liabilities:				
Contingent consideration	$ 22,967	$—	$ —	$22,967
Total liabilities	$ 22,967	$—	$ —	$22,967

In thousands

	Total as of December 31, 2015	Fair Value Measurements Using Level 1 Inputs	Level 2 Inputs	Level 3 Inputs
Assets:				
Cash and cash equivalents	$ 55,634	$55,634	$—	$—
Short-term investments	69	69	—	—
Derivative financial instruments	1,207	—	1,207	—
Total assets	$ 56,910	$55,703	$1,207	$—
Liabilities:				
Contingent consideration	$ 25,390	$—	$—	$25,390
Total liabilities	$ 25,390	$—	$—	$25,390

For our derivative financial instruments we use a market approach valuation technique based on observable market transactions of spot and forward rates.

We recorded a $1.0 million asset related to the fair value of the U.S. dollar-Canadian dollar foreign currency swap which was classified as other assets at March 31, 2016. The objective of the swap is to offset the foreign exchange risk to the U.S. dollar equivalent cash outflows for our Canadian subsidiary.

We had contingent consideration liabilities recorded using Level 3 inputs in the amount of $23.0 million, of which $6.9 million was classified as current liabilities at March 31, 2016. Contingent consideration liabilities were $25.4 million at December 31, 2015. Contingent consideration represents amounts expected to be paid as part of acquisition consideration only if certain future events occur. These events are usually targets for revenues or earnings related to the business acquired. We arrive at the fair value of contingent consideration by applying a weighted probability of potential outcomes to the maximum possible payout. The calculation of these potential outcomes is dependent on both past financial performance and management assumptions about future performance. If the financial performance measures were all fully met, our maximum liability would be $40.2 million at March 31, 2016. Contingent consideration liabilities are reassessed each quarter and are reflected in the Condensed Consolidated Balance Sheets as part of “Other current liabilities” and “Other liabilities”. Changes to contingent consideration are reflected in the table below:

In thousands	
Contingent consideration at January 1, 2016	$25,390
Increases due to acquisitions	57
Decrease due to payments	(1,000)
Changes due to foreign currency fluctuations	1,164
Changes in fair value reflected in Selling, general, and administrative expenses	(2,644)
Contingent consideration at March 31, 2016	$22,967

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Fair Value of Debt: At March 31, 2016, the fair value of the Company's debt obligations was estimated, using Level 2 inputs, at $3.13 billion compare to a carrying amount of $3.15 billion. At December 31, 2015, the fair value of the Company's debt obligations was estimated, using Level 2 inputs, at $3.22 billion compared to a carrying amount of $3.21 billion. The fair values were estimated using an income approach by applying market interest rates for comparable instruments. The Company has no current plans to retire a significant amount of its debt prior to maturity.

NOTE 5 – INCOME TAXES

We file income tax returns in the U.S, in various states and in certain foreign jurisdictions.

The Company has recorded accruals to cover certain unrecognized tax positions. Such unrecognized tax positions relate to additional taxes that the Company may be required to pay in various tax jurisdictions. During the course of examinations by various taxing authorities, proposed adjustments may be asserted. The Company evaluates such items on a case-by-case basis and adjusts the accrual for unrecognized tax positions as deemed necessary. During the quarter ended March 31, 2016, we had no material changes to our accruals related to previous or current uncertain tax positions. The effective tax rates for the quarters ended March 31, 2016 and 2015 were approximately 32.9% and 14.7%, respectively. The effective tax rate for the quarter ended March 31, 2015 reflects the recognition of certain deferred tax benefits and a $73.5 million accrual for loss contingencies recorded during the period.

NOTE 6 – STOCK BASED COMPENSATION

At March 31, 2016, we had the following active stock option and stock purchase plans:

- the 2014 Incentive Stock Plan, which our stockholders approved in May 2014;
- the 2011 Incentive Stock Plan, which our stockholders approved in May 2011;
- the 2008 Incentive Stock Plan, which our stockholders approved in May 2008;
- the 2005 Incentive Stock Plan, which our stockholders approved in April 2005;
- the 2000 Non-statutory Stock Option Plan, which expired in February 2010;
- the Employee Stock Purchase Plan ("ESPP"), which our stockholders approved in May 2001.

Stock-Based Compensation Expense:

The following table presents the total stock-based compensation expense resulting from stock option awards, restricted stock units ("RSUs"), and the ESPP included in the Condensed Consolidated Statements of Income:

In thousands

	Three Months Ended March 31,	
	2016	2015

Cost of revenues – stock option plan	$15	$23
Selling, general and administrative – stock option plan	4,752	4,729
Selling, general and administrative – RSUs	559	346
Selling, general and administrative – ESPP	779	389
Total pre-tax expense	$6,105	