

**UNITED STATES**  
**SECURITIES AND EXCHANGE COMMISSION**  
Washington, D.C. 20549

**FORM 10-K**

☒ **ANNUAL REPORT PURSUANT TO SECTION 13 or 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**

For the year ended September 27, 2019  
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 001-37860



**VAREX IMAGING CORPORATION**

(Exact name of registrant as specified in its charter)

**Delaware**  
(State or other jurisdiction of  
incorporation or organization)

**81-3434516**  
(I.R.S. Employer  
Identification Number)

**1678 S. Pioneer Road**                      **Salt Lake City**   **Utah**  
(Address of principal executive offices)

**84104**  
(Zip Code)

**(801) 972-5000**  
(Registrant's telephone number, including area code)

**Securities registered pursuant to Section 12(b) of the Act:**

Title of each class	Trading Symbol(s)	Name of each exchange on which registered
Common Stock	VREX	The Nasdaq Global Select Market

**Securities registered pursuant to Section 12(g) of the Act: None**

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. Yes ☐ No ☒

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Exchange Act. Yes ☐ No ☒

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 ☒ No ☐

Indicate by check mark whether the registrant has submitted electronically every Interactive Data File required to be submitted 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 such files). Yes ☒ 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 definitions of "large accelerated filer," "accelerated filer," "smaller reporting company," and "emerging growth

company” in Rule 12b-2 of the Exchange Act.

Large Accelerated filer	<input checked="" type="checkbox"/>	Accelerated filer	<input type="checkbox"/>
Non-Accelerated filer	<input type="checkbox"/>	Smaller reporting company	<input type="checkbox"/>
		Emerging growth company	<input type="checkbox"/>

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. ☐

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

As of March 29, 2019, the last business day of the registrant’s most recently completed second fiscal quarter, the aggregate market value of shares of the registrant’s common stock held by non-affiliates of the registrant (based upon the closing sale price of such shares on the NASDAQ Global Select Market on March 29, 2019) was approximately \$1,160.4 million. Shares of the registrant’s common stock held by the registrant’s executive officers and directors and by each entity that owned 10% or more of the registrant’s outstanding common stock have been excluded in that such persons may be deemed to be affiliates. This determination of affiliate status is not necessarily a conclusive determination for other purposes.

As of November 18, 2019, there were 38,494,349 shares of the registrant’s common stock outstanding.

#### **Documents Incorporated by Reference**

Portions of registrant’s proxy statement relating to registrant’s 2020 annual meeting of stockholders have been incorporated by reference in Part III of this annual report on Form 10-K.

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# VAREX IMAGING CORPORATION

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## Forward-Looking Statements

This Annual Report on Form 10-K (this “Annual Report”), including the section entitled “Management’s Discussion and Analysis of Financial Condition and Results of Operations” (“MD&A”) contains “forward-looking” statements within the meaning of the Private Securities Litigation Reform Act of 1995, which provides a safe harbor for statements about future events, products and financial performance that are based on the beliefs of, estimates made by, and information currently available to the management of Varex Imaging Corporation (“we,” “our,” “us,” the “Company,” “Varex,” or “Varex Imaging”). Actual results and the outcome or timing of certain events described in these forward-looking statements are subject to risk and uncertainties and may differ significantly from those projected in these forward-looking statements. Important factors that could cause our actual results and financial condition to differ significantly from those projections or expectations include, among other things, the following:

- reduction in or loss of business to key customers;
- changes in, or our inability to predict and meet, demand for our products;
- loss of business to, and inability to compete with, competitors;
- changes in macroeconomic and global geopolitical factors, including changes in regulatory regimes, import and export controls and restrictions (such as tariffs) and global or regional economic stability;
- our ability to meet the payment and other requirements of our existing bank debt and other contractual obligations;
- our ability to develop new products and enhance existing products;
- the ability to identify and remediate significant deficiencies and material weaknesses in internal controls;
- disruption at our manufacturing facilities and fluctuations in manufacturing costs;
- changes in our effective tax rate;
- our inability to source components and raw materials of our products
- disruption or breach of our critical information technology systems;
- the results of any product liability or product defect claims, product recalls and other litigation and regulatory investigations;
- risks related to intellectual property;
- our ability to hire and retain qualified personnel;
- the impact of natural and other disasters, power loss, strikes and other events beyond our control; and
- other factors cited in the Risk Factors listed under Part I, Item 1A of this Annual Report, MD&A and other factors described from time to time in our other filings with the U.S. Securities and Exchange Commission (the “SEC”), or other reasons.

Statements concerning industry or market segment outlook; market acceptance of or transition to new products or technology such as advanced X-ray tube and digital flat panel detector products; growth drivers; future orders, revenues, backlog, earnings or other financial results; and any statements using the terms “believe,” “expect,” “anticipate,” “can,” “should,” “would,” “could,” “estimate,” “may,” “intended,” “potential,” and “possible” or similar statements are forward-looking statements.

Any forward-looking statement made in this Annual Report (including in any exhibits or documents incorporated by reference) is based only on information currently available to Varex and its management and speaks only as of the date on which it is made. We have not assumed any obligation to, and you should not expect us to, update or revise those statements because of new information, future events or otherwise.

## PART I

### Item 1. Business

#### Overview

Varex Imaging Corporation is a leading innovator, designer and manufacturer of X-ray imaging components including X-ray tubes, digital detectors, linear accelerators and other image processing solutions, which are key components of X-ray imaging systems. Our components are used in medical imaging as well as in industrial and security imaging applications. Global original equipment manufacturers (“OEM”) incorporate our X-ray imaging components in their systems to detect, diagnose, protect and inspect. As of September 27, 2019, we had approximately 2,000 full-time equivalents employees, located at manufacturing and service center sites in North America, Europe, and Asia. For more information about us, visit [vareximaging.com](http://vareximaging.com).

Founded as a Delaware corporation in July 2016, Varex was established as an independent publicly-traded company in January 2017 as a result of its spin-off from Varian Medical Systems, Inc. (“Varian”). We expanded our business in May 2017, when we acquired the medical imaging business (“Acquired Detector Business”) of PerkinElmer, Inc. (“PKI”) for \$273.3 million. In the transaction, we acquired PerkinElmer Medical Holdings, Inc. and Dexela Limited, together with certain assets of PKI and its direct and indirect subsidiaries relating to digital detectors that serve as components for medical and industrial X-ray imaging systems. In



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April 2019, we acquired Direct Conversion AB, a manufacturer and marketer of linear array digital detectors utilizing direct conversion and photon counting technology.

Our products are sold in three geographic regions: the Americas, EMEA, and APAC. The Americas includes North America (primarily the United States) and Latin America. EMEA includes Europe, Russia, the Middle East, India and Africa. APAC includes Asia and Australia. Revenues by region are based on the known final destination of products sold.

Our success depends, among other things, on our ability to anticipate and respond to changes in our markets, the direction of technological innovation and the demands of our customers. We continue to invest in research and development and employ over 500 engineers. Combining this focus on innovation and product performance with strong long-term customer relationships allows us to partner with our customers to bring industry-leading products to the X-ray imaging market. We continue to work to improve the life and quality of our imaging components and leverage our scale as the largest X-ray imaging component supplier to provide cost-effective solutions for our customers. Demand for our products can also be impacted by geo-political factors, including tariffs on key imported materials used in manufacturing our products and also on X-ray imaging products we sell to customers outside the United States. The escalation of trade conflicts between the United States and China has negatively impacted our business and are expected to continue.

### **Operating Segments and Products**

Our Chief Executive Officer, who is our Chief Operating Decision Maker (“CODM”), evaluates our product groupings and measures our business performance in two reportable operating segments: Medical and Industrial. The segments align our products and service offerings with customer use in medical and industrial markets and are consistent with how the CODM evaluates the business for the allocation of resources. The CODM allocates resources to and evaluates the financial performance of each operating segment primarily based on revenues and gross margin.

#### ***Medical***

In our Medical business segment, we design, manufacture, sell and service X-ray imaging components for use in a range of radiographic or fluoroscopic imaging applications including computed tomography (“CT”), mammography, oncology, cardiac, surgery, dental, and computer-aided detection. We provide a broad range of X-ray imaging components for Medical customers, including X-ray tubes, digital detectors, high voltage connectors, image-processing software and workstations, computer-aided diagnostic software, collimators, automatic exposure control devices, generators, heat exchangers, ionization chambers and buckys.

A significant portion of our revenues come from the sales of high-end X-ray tubes used in CT imaging and high-end dynamic digital detectors used in fluoroscopic and 3D dental imaging applications. These upper-tier imaging components are characterized by increased levels of technological complexity, engineering and intellectual property that typically allow these products to have a higher sales price and gross margin.

The digital detector market continues to mature from initial product introductions that were made approximately 15 years ago. For the past few years, we have experienced price erosion for these products, predominantly in the highly-competitive market for radiographic detectors. We anticipate this trend will continue in the foreseeable future.

Our X-ray imaging components are primarily sold to OEM customers that incorporate our products into their X-ray imaging systems for a variety of medical modalities and industrial applications. To a much lesser extent, we also sell our X-ray imaging components to independent service companies, distributors and directly to end-users for replacement purposes.

In China, the government is broadening the availability of healthcare services throughout the country. As a result, the number of diagnostic X-ray imaging systems, including CT, has grown significantly. We are developing CT tubes and related subsystems for Chinese OEMs as they introduce new CT imaging systems in China. Over the long-term, we anticipate that China-based revenues will increase as a percentage of our revenues. For fiscal year 2019, revenues from X-ray imaging components shipped to China-based OEMs and distributors declined to approximately 8% of total company revenues from 10% in the prior year. This decrease reflects a tariff-related decline in sales of radiographic digital detectors in China as well as lower non-OEM aftermarket sales, which more than offset an increase in sales of CT tubes to OEM customers.

To mitigate the impact of the trade war between the United States and China, we have implemented changes to secure more non-China sources of supply of parts and materials used to manufacture our X-ray imaging products, and in September 2019, we received from the United States Trade Representative a temporary exclusion from Section 301 tariffs on certain parts and components



imported from China into the United States. We continue to expand manufacturing capabilities at our facilities in China, Germany and the Philippines.

## ***Industrial***

In our Industrial business segment, we design, manufacture, sell and service X-ray imaging products for use in a number of markets, including security applications, such as cargo screening at ports and borders and baggage screening at airports, and nondestructive testing and inspection applications used in a number of other markets. Our industrial products include Linatron® X-ray linear accelerators, X-ray tubes, digital detectors and high voltage connectors. In addition, we provide proprietary image-processing and detection software designed to work with these other Varex products to provide package solutions to our Industrial customers.

The security market primarily consists of airport security for carry-on baggage, checked baggage and palletized cargo, as well as cargo security for the screening of trucks, trains and cargo containers at ports and borders. The end customers for border protection systems are typically government agencies, many of which are in oil-based economies and war zones where there has been significant year over year variation in buying patterns.

The non-destructive testing market utilizes X-ray imaging to scan items for inspection of manufacturing defects and product integrity in a wide range of industries including the aerospace, automotive, oil and gas, food packaging, metal castings and 3D printing industries. We provide X-ray sources, digital detectors, high voltage connectors and image processing software to OEM customers, system integrators and manufacturers. In addition, new applications for X-ray sources are being developed, such as sterilization of food and its packaging.

## **Customers**

Our customers are primarily large OEMs. Our top five customers, measured by revenue, are Canon Medical Systems Corporation (“Canon”), General Electric Company, Elekta AB, Varian Medical Systems, Inc. and Hologic, Inc., which collectively accounted for approximately 38% in fiscal year 2019. Our largest customer, Canon, accounted for approximately 17%, 18% and 19% of our total revenues for fiscal years 2019, 2018, and 2017, respectively, while our ten largest customers as a group accounted for approximately 51%, 49% and 48% of our revenue for fiscal years 2019, 2018 and 2017, respectively. The loss of one or more of our top customers would have a material and adverse effect on our business. For more information, see “Risk Factors-Varex sells its products and services to a limited number of OEM customers, many of which are also its competitors, and a reduction in or loss of business of one or more of these customers may materially reduce its sales.”

## **Competition**

The imaging components market is highly competitive. OEMs may choose to develop and manufacture X-ray imaging components in-house or they may choose to out-source to a supplier such as us or other providers of imaging components. Our success depends upon our ability to anticipate changes in our markets, the direction of technological innovation and the demands of our customers. To remain competitive, we must continue to invest in research and development focused on innovation, improve product performance and quality, and reduce the cost of our imaging components. Significant capital investment is required for imaging component manufacturers. We believe we have sufficient manufacturing scale to leverage our high volume to reduce overall costs by spreading fixed costs over more units.

## ***Medical***

We often compete with the in-house X-ray tube manufacturing operations of major diagnostic imaging systems companies, which are the primary OEM customers for our Medical products. To effectively compete with these in-house capabilities, we must have a competitive advantage in one or more significant areas, such as innovative technology and greater product performance, better product quality or lower product price. We sell a significant volume of our X-ray tubes to OEM customers that have in-house X-ray tube production capability. In addition, we compete with some OEM customers, such as Canon, Philips Healthcare and other companies who sell X-ray tubes to smaller OEMs and other manufacturers, such as Industria Applicazioni Elettroniche S.p.A, as well as emerging X-ray tube manufacturers in China. High capital costs and mastery of complex manufacturing processes that drive production yield and product life are significant characteristics of the X-ray tubes business.

The market for digital detectors is also highly competitive. We sell our digital detectors to a number of OEM customers that incorporate our detectors into their medical diagnostic, oncology, 3D dental and veterinary imaging systems. Our amorphous silicon based digital detector technology, our photon counting technology and our complementary metal-oxide-semiconductor technology



competes with other detector technologies, such as amorphous selenium, charge-coupled devices and variations of amorphous silicon scintillators. We believe that our products provide a competitive advantage due to product quality and performance and lower overall product lifecycle costs. In the digital flat panel detector market, we primarily compete against Trixell S.A.S., Canon, Vieworks Co., Ltd., Hamamatsu Corporation, iRay Technology (Shanghai) Limited and Jiangsu CareRay Medical Systems Co., Ltd.

### *Industrial*

In the low-energy market of the Industrial segment, we compete with other OEM suppliers, such as General Electric, Canon, Nuctech Company Limited (“Nuctech”) and Comet AG. While there are other manufacturers of low-energy X-ray tubes and digital detectors for specialized and niche industrial applications, our products are designed for a broad range of applications in inspection, analysis, and testing. In the high-energy market, we compete against technologies from Nuctech, Siemens AG, and Foton Ltd., whose X-ray sources are used in applications that include cargo and container scanning, border security, aerospace applications, castings and pressure vessel inspections.

### **Customer Services and Support**

We generally warranty our products for 12 to 24 months. In certain cases, the warranty also may be specified by usage metrics such as number of scans. We provide technical advice and consultation to major OEM customers from our U.S. offices in Utah, California, Nevada, South Carolina, New York and Illinois; and internationally in the Philippines, China, the Netherlands, Germany, France, Sweden, Switzerland, the United Kingdom, Italy and Japan. Our application specialists and engineers make recommendations to meet the customer’s technical requirements within the customer’s budgetary constraints. We often develop specifications for a unique product that will be designed and manufactured to meet a specific customer’s requirements.

### **Manufacturing and Supplies**

We manufacture our products at facilities located in Salt Lake City, Utah; Santa Clara, California; Las Vegas, Nevada; Liverpool, New York; Franklin Park, Illinois; Dinxperlo and Heerlen, the Netherlands; Walluf and Bremen, Germany; Espoo, Finland and Calamba City, Philippines. These facilities employ state-of-the-art manufacturing techniques and several have been recognized by the press, governments and trade organizations for their commitment to quality improvement. Each of these manufacturing facilities are certified by International Standards Organization (“ISO”) under ISO 9001 (for industrial products) or ISO 13485 (for medical devices). In addition, we have regional service centers in North Charleston, South Carolina; Willich, Germany; and Wuxi, China. The combined medical and industrial manufacturing infrastructure enable us to leverage production scale to achieve productivity and low cost advantage as well as research and development synergies.

Manufacturing processes at our various facilities include machining, fabrication, subassembly, system assembly and final testing. We have invested in various automated and semi-automated equipment for the fabrication and machining of the parts and assemblies that we incorporate into our products. We may, from time to time, invest further in such equipment. Our quality assurance program includes various quality control measures from inspection of raw materials, purchased parts and assemblies through in-line inspection. In some cases, we may outsource the manufacturing of sub-assemblies while still performing system design, final assembly and testing in-house. In such cases, we believe outsourcing enables us to reduce or maintain fixed costs and capital expenditures, while also providing the flexibility to increase production capacity. We purchase material and components from various suppliers that are either standard products or customized to our specifications. Some of the components included in our products may be sourced from a limited group of suppliers or from a single source supplier, such as the wave guides for linear accelerators; transistor arrays and cesium iodide coatings for digital detectors and specialized integrated circuits, X-ray tube targets, housings, bearings and various other components. We require certain raw materials, such as copper, lead, tungsten, iridium, rhenium, molybdenum zirconium, and various high grades of steel alloy for X-ray tubes and industrial products. Worldwide demand, availability and pricing of these raw materials have been volatile, and we expect that availability and pricing will continue to fluctuate in the future.

In the fourth quarter of 2019, we announced the closure of the remainder of our Santa Clara facility and that we would relocate production to other existing facilities. We expect operations at the Santa Clara facility to cease by the end of December 2020 and all activities related to the closure of the facility to be completed by the end of March 2021.

## Research and Development

Innovation and developing products, systems and services based on advanced technology is essential to our ability to compete effectively in the marketplace. We maintain a research and development and engineering staff responsible for product design and engineering.

Research and development are primarily conducted domestically at our facilities in Salt Lake City, Utah; San Jose and Santa Clara, California; Las Vegas, Nevada; Liverpool, New York; and Franklin Park, Illinois and internationally at our facilities in the Netherlands, Sweden and Germany. Our research and development activities are primarily focused on developing and improving imaging component technology. Current X-ray source development areas include smaller footprint linear accelerators, improvements to tube life and tube stability, reductions of tube noise and tube designs that will enable OEMs to continue to reduce dose delivered, and improve image resolution, cost effectively. Research in digital detector imaging technology is aimed at developing new panel technologies with better dose utilization, improved image quality and materials discrimination, lower product costs and new image processing tools for advanced applications.

Industrial products share some of the same base technology competencies and platforms as medical products and our medical and industrial development teams are therefore co-located in Salt Lake City, San Jose, Santa Clara, Dinxperlo, Danderyd and Walluf. One of our competitive advantages is that some of the foundational technologies and software components developed for medical applications may also be applicable in industrial components, and vice versa. In addition to these product development synergies, we are also able to realize sourcing, production, service center, and logistics synergies across the different products and market sectors.

## Product and Other Liabilities

Our business exposes us to potential product liability claims that are inherent in the manufacture, sale, installation, servicing and support of X-ray imaging devices, related software and other devices that contain hazardous material or deliver radiation. Because our products are involved in the intentional delivery of radiation to the human body and other situations where people may come in contact with radiation (for example, when our Industrial products are being used to scan cargo) as well as the detection, planning and treatment of medical problems, the possibility for significant injury or death exists if our products fail to work or are not used properly. We may face substantial liability to patients, our customers and others for damages resulting from the faulty, or allegedly faulty, design, manufacture, installation, servicing, support, testing or interoperability of our products and our customers' products, or their misuse or failure. We may also be subject to claims for property damages or economic loss related to or resulting from any errors or defects in our products, or the installation, servicing and support of our products. Any accident or mistreatment could subject us to legal costs, litigation, adverse publicity and damage to our reputation, whether or not our products or services were a factor. In addition, if a product we design or manufacture were defective (whether due to design, labeling or manufacturing defects, improper use of the product or other reasons), or found to be so by a regulatory authority, we may be required to correct or recall the product and notify other regulatory authorities. We maintain limited product liability, professional liability and omissions liability insurance coverage.

## Government Regulation

### *U.S. Regulations*

*Laws governing marketing a medical device.* In the United States, as a manufacturer and seller of medical devices and devices emitting radiation or utilizing radioactive by-product material, we and some of our suppliers and distributors are subject to extensive regulation by federal governmental authorities, such as the U.S. Food and Drug Administration (the "FDA"), Nuclear Regulatory Commission ("NRC"), and state and local regulatory agencies, to ensure the devices are safe and effective and comply with laws governing products which emit, produce or control radiation. Similar international regulations apply overseas. These regulations, which include the U.S. Food, Drug and Cosmetic Act (the "FDC Act") and regulations promulgated by the FDA, govern, among other things, the design, development, testing, manufacturing, packaging, labeling, distribution, import/export, sale and marketing and disposal of medical devices, post market surveillance and reporting of serious injuries and death, repairs, replacements, recalls and other matters relating to medical devices, radiation emitting devices and devices utilizing radioactive by-product material. State regulations are extensive and vary from state to state. Our X-ray tube products, imaging workstations and flat panel detectors are considered medical devices. Under the FDC Act, each medical device manufacturer must comply with quality system regulations that are strictly enforced by the FDA.

Unless an exception applies, the FDA requires that the manufacturer of a new medical device or a new indication for use of, or other significant change in, existing currently marketed medical device obtain 510(k) pre-market notification clearance before it can

market or sell those products in the United States. The 510(k) clearance process is applicable when the device introduced into commercial distribution is substantially equivalent to a legally marketed device. The obtaining 510(k) clearance generally takes at least six months from the date an application is filed, but could take significantly longer, and generally requires submitting supporting testing data. After a product receives 510(k) clearance, any modifications or enhancements to a product that could significantly affect its safety or effectiveness, or that would constitute a major change in the intended use of the device, technology, materials, labeling, packaging, or manufacturing process, may require a new 510(k) clearance. The FDA requires each manufacturer to make this determination in the first instance, but the FDA can review any such decision. If the FDA disagrees with the manufacturer's decision, it may retroactively require the manufacturer to submit a request for 510(k) pre-market notification clearance and may require the manufacturer to cease marketing and recall the product until 510(k) clearance is obtained. The FDA adopted guidance in September 2019 that we expect will increase the number and frequency of clearances for changes made to legally marketed devices. Most of our products are non-classified or Class I medical devices, which do not require 510(k) clearance.

*Quality systems.* Our manufacturing operations for medical devices, and those of our third-party manufacturers, are required to comply with the FDA's Quality System Regulation ("QSR"), which addresses a company's responsibility for product design, testing, and manufacturing quality assurance, and the maintenance of records and documentation. The QSR requires that each manufacturer establish a quality systems program by which the manufacturer monitors the manufacturing process and maintains records that show compliance with FDA regulations and the manufacturer's written specifications and procedures relating to the devices. QSR compliance is necessary to receive and maintain FDA clearance or approval to market new and existing products. The FDA makes announced and unannounced periodic and ongoing inspections of medical device manufacturers to determine compliance with the QSR. If in connection with these inspections the FDA believes the manufacturer has failed to comply with applicable regulations and/or procedures, it may issue observations that would necessitate prompt corrective action. If FDA inspection observations are not addressed and/or corrective action taken in a timely manner and to the FDA's satisfaction, the FDA may issue a warning letter (which would similarly necessitate prompt corrective action) and/or proceed directly to other forms of enforcement action. Failure to respond timely to FDA inspection observations, a warning letter or other notice of noncompliance and to promptly come into compliance could result in the FDA bringing enforcement action against us, which could include the total shutdown of our production facilities, denial of importation rights to the United States for products manufactured in overseas locations and denial of export rights for U.S. products and criminal and civil fines.

The FDA and the Federal Trade Commission (the "FTC") regulate advertising and promotion of our products to ensure that the claims we make are consistent with our regulatory clearances, that we have adequate and reasonable scientific data to substantiate the claims and that our promotional labeling and advertising is neither false nor misleading. We may not promote or advertise our products for uses not within the scope of our intended use statement in our clearances or approvals or make unsupported safety and effectiveness claims.

It is also important that our products comply with electrical safety and environmental standards, such as those of Underwriters Laboratories ("UL"), the Canadian Standards Association ("CSA"), and the International Electrotechnical Commission ("IEC"). In addition, the manufacture and distribution of medical devices utilizing radioactive material requires a specific radioactive material license. For the United States, manufacture and distribution of these radioactive sources and devices also must be in accordance with a model-specific certificate issued by either the NRC or by an Agreement State. In essentially every country and state, installation and service of these products must be in accordance with a specific radioactive materials license issued by the applicable radiation control agency. Service of these products must be in accordance with a specific radioactive materials license. We are also subject to a variety of additional environmental laws regulating our manufacturing operations and the handling, storage, transport and disposal of hazardous substances, and which impose liability for the cleanup of any contamination from these substances.

*Other applicable U.S. regulations.* As a participant in the healthcare industry, we are also subject to extensive laws and regulations protecting the privacy and integrity of patient medical information that we receive, including the Health Insurance Portability and Accountability Act of 1996 ("HIPAA"), "fraud and abuse" laws and regulations, including physician self-referral prohibitions, and false claims laws. From time to time, these laws and regulations may be revised or interpreted in ways that could make it more difficult for our customers to conduct their businesses, such as recent proposed revisions to the laws prohibiting physician self-referrals, and such revisions could have an adverse effect on the demand for our products, and therefore our business and results of operations. We also must comply with numerous federal, state and local laws of more general applicability relating to such matters as environmental protection, safe working conditions, manufacturing practices, fire hazard control and other matters.

The laws and regulations and their enforcement are constantly undergoing change, and we cannot predict what effect, if any, changes to these laws and regulations may have on our business. For example, national and state laws regulate privacy and may regulate our use of data. Furthermore, HIPAA was amended by the HITECH Act to provide that business associates who have access

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to patient health information provided by hospitals and healthcare providers are now directly subject to HIPAA, including the associated enforcement scheme and inspection requirements.

### *Medicare and Medicaid Reimbursement*

The federal and state governments of the United States establish guidelines and pay reimbursements to hospitals and free-standing clinics for diagnostic examinations and therapeutic procedures under Medicare at the federal level and Medicaid at the state level. Private insurers often establish payment levels and policies based on reimbursement rates and guidelines established by the government.

The federal government and Congress review and adjust rates annually, and from time to time consider various Medicare and other healthcare reform proposals that could significantly affect both private and public reimbursement for healthcare services in hospitals and free-standing clinics. In the past, we have seen demand for our customers' systems (in which our products are incorporated) negatively impacted by the uncertainties surrounding reimbursement rates in the United States. State government reimbursement for services is determined pursuant to each state's Medicaid plan, which is established by state law and regulations, subject to requirements of federal law and regulations.

Various healthcare reform proposals have also emerged at the state level, and we are unable to predict which, if any, of these proposals will be enacted. In addition, it is possible that changes in federal health care law and policy could result in additional proposals and/or changes to health care system legislation which could have a material adverse effect on our business. Uncertainty created by healthcare reform complicates our customers' decision-making process and, therefore, impacts our business, and may continue to do so.

The sale of medical devices, the referral of patients for diagnostic examinations and treatments utilizing such devices, and the submission of claims to third-party payors (including Medicare and Medicaid) seeking reimbursement for such services, are subject to various federal and state laws pertaining to healthcare "fraud and abuse." Anti-kickback laws make it illegal to solicit, induce, offer, receive or pay any remuneration in exchange for the referral of business, including the purchase of medical devices from a particular manufacturer or the referral of patients to a particular supplier of diagnostic services utilizing such devices. False claims laws prohibit anyone from knowingly and willfully presenting, or causing to be presented, claims for payment to third-party payors (including Medicare and Medicaid) that are false or fraudulent, for services not provided as claimed, or for medically unnecessary services. The Office of the Inspector General prosecutes violations of fraud and abuse laws and any violation may result in criminal and/or civil sanctions, including, in some instances, imprisonment and exclusion from participation in federal healthcare programs such as Medicare and Medicaid, which may negatively impact the demand for our products.

### *Foreign Regulations*

Our operations, sales and service of our products outside the United States are subject to regulatory requirements that vary from country to country and may differ significantly from those in the United States. In general, our products are regulated outside the United States as medical devices by foreign governmental agencies similar to the FDA.

*Marketing a medical device internationally.* For us to market our products internationally, we must obtain clearances or approvals for products and product modifications. We are required to affix the CE mark to our products to sell them in member countries of the European Union ("EU"). The CE mark is an international symbol of adherence to certain essential principles of safety and effectiveness, which once affixed enables a product to be sold in member countries of the EEA. The CE mark is also recognized in many countries outside the EU, such as Switzerland and Norway and can assist in the clearance process. To receive permission to affix the CE mark to our medical devices products, we must obtain Quality System certification, *e.g.*, ISO 13485, through an accredited Notified Body and must otherwise have a quality management system that complies with the EU Medical Device Directive to be superseded by the EU MDR-Medical Device Regulations in May 2020. The ISO promulgates standards for certification of quality assurance operations. We are certified as complying with the ISO 9001 for our security and inspection products and ISO 13485 for our medical devices. Several Asian countries, including Japan and China, have adopted regulatory schemes that are comparable, and in some cases more stringent, than the EU scheme. To import medical devices into Japan, the requirements of Japan's New Medical Device Regulation must be met and an approval to sell medical products in Japan, must be obtained. Similarly, a registration certification issued by the National Medical Products Administration and a China Compulsory Certification mark for certain products are required to sell medical devices in China. Obtaining such certifications on our products can be time-consuming and can cause us to delay marketing or sales of certain products in such countries. Similarly, prior to selling a device in Canada, manufacturers of Class II devices must obtain a medical device license in Canada. Additionally, many countries have laws and regulations relating to radiation and radiation safety that apply to our products. In most countries, radiological regulatory agencies require some form of licensing or

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registration by the facility prior to acquisition and operation of an X-ray generating device or a radiation source. The handling, transportation and recycling of radioactive metals and source materials are also highly regulated.

A number of countries, including the members of the EU, have implemented or are implementing regulations that would require manufacturers to dispose, or bear certain disposal costs, of products at the end of a product's useful life and restrict the use of some hazardous substances in certain products sold in those countries.

*Manufacturing and selling a device internationally.* We are subject to laws and regulations outside the United States applicable to manufacturers of radiation-producing devices and products utilizing radioactive materials, and laws and regulations of general applicability relating to matters such as environmental protection, safe working conditions, manufacturing practices and other matters, in each case that are often comparable to, if not more stringent than, regulations in the United States. In addition, our sales of products in foreign countries are subject to regulation of matters such as product standards, packaging requirements, labeling requirements, import restrictions, environmental and product recycling requirements, tariff regulations, duties and tax requirements. In some countries, we rely on our foreign distributors and agents to assist us in complying with foreign regulatory requirements.

*Other applicable international regulations.* In addition to the U.S. laws regarding the privacy and integrity of patient medical information, we are subject to similar laws and regulations in foreign countries covering data privacy and other protection of health and employee information. Particularly within Europe, data protection legislation is comprehensive and complex and there has been a recent trend toward more stringent enforcement of requirements regarding protection and confidentiality of personal data, as well as enactment of stricter legislation. We are also subject to international "fraud and abuse" laws and regulations, as well as false claims and misleading advertisement laws. We also must comply with numerous international laws of more general applicability relating to such matters as environmental protection, safe working conditions, manufacturing practices, fire hazard control and other matters.

On June 23, 2016, the United Kingdom (the "U.K.") held a referendum in which voters approved an exit from the E.U., commonly referred to as "Brexit". Brexit could lead to legal uncertainty and potentially divergent national laws and regulations as the U.K. determines which E.U. laws to replace or replicate. Given the lack of comparable precedent, it is unclear what financial, regulatory and legal implications the withdrawal of the U.K. from the E.U. would have and how such withdrawal would affect us. We currently have UK based Notified Bodies that must be transferred to an EU Member State recognized Notified Body.

### *Anti-Corruption Laws and Regulations*

We are subject to the U.S. Foreign Corrupt Practices Act and anti-corruption laws, and similar laws in foreign countries, such as the U.K. Bribery Act of 2010, which became effective on July 1, 2011, and the law "On the Fundamentals of Health Protection in the Russian Federation," which became effective in January 2012. In general, there is a worldwide trend to strengthen anti-corruption laws and their enforcement, and the healthcare industry and medical equipment manufacturers have been particular targets of these investigation and enforcement efforts. Any violation of these laws by us or our agents or distributors could create a substantial liability for us, subject our officers and directors to personal liability and also cause a loss of reputation in the market.

Transparency International's 2015 Corruption Perceptions Index measured the degree to which public sector corruption is perceived to exist in 168 countries/territories around the world, and found that two-thirds of the countries in the index, including many that we consider to be high-growth areas for our products, such as China and India, scored below 50, on a scale from 100 (very clean) to 0 (highly corrupt). We currently operate in many countries where the public sector is perceived as being more or highly corrupt and our strategic business plans include expanding our business in regions and countries that are rated as higher risk for corruption activity by Transparency International.

Increased business in higher-risk countries could subject us and our officers and directors to increased scrutiny and increased liability. In addition, becoming familiar with and implementing the infrastructure necessary to comply with laws, rules and regulations applicable to new business activities and mitigating and protecting against corruption risks could be quite costly. Failure by us or our agents or distributors to comply with these laws, rules and regulations could delay our expansion into high-growth markets and could materially and adversely affect our business.

### *Competition and Trade Compliance Laws*

We are subject to various competition and trade compliance laws in the jurisdictions where we operate. Regulatory or government authorities where we operate may have enforcement powers that can subject us to sanctions and can impose changes or conditions in the way we conduct our business. For example, local authorities may disagree with how we classify our products, and we may be required to change our classifications, which could increase our operating costs or subject us to increased taxes or fines and



penalties. In addition, an increasing number of jurisdictions also provide private rights of action for competitors or consumers to seek damages asserting claims of anti-competitive conduct. Increased government scrutiny of our actions or enforcement of private rights of action could materially and adversely affect our business or damage our reputation. In addition, we may conduct, or we may be required to conduct, internal investigations or face audits or investigations by one or more domestic or foreign government or regulatory agencies, which could be costly and time-consuming, and could divert our management and key personnel from our business operations. An adverse outcome under any such investigation or audit could subject us to increased costs, fines or criminal or other penalties, which could materially and adversely affect our business and financial results. Furthermore, competition laws may prohibit or increase the cost of future acquisitions that we may desire to undertake.

International sales of certain of our Linatron® X-ray accelerators are subject to U.S. export licenses that are issued at the discretion of the U.S. government. Orders and revenues for our security and inspection products have been and may continue to be unpredictable as governmental agencies may place large orders with us or with our customers over a short period of time and then may not place additional orders until complete deployment and installation of previously ordered products. We have seen domestic and international governments postpone purchasing decisions and delay installations of products for security and inspection systems. Furthermore, tender awards in this business may be subject to challenge by third parties, as we have previously encountered, which can make the conversion of orders to revenues unpredictable for some security and inspection products. The market for border protection systems has slowed significantly and end customers, particularly in oil-based economies and war zones in which we have a significant customer base, are delaying system deployments or tenders and have considered moving to alternative sources.

## **Intellectual Property**

We place considerable importance on obtaining and maintaining patent, copyright and trade secret protection for significant new technologies, products and processes, because of the length of time and expense associated with bringing new products through the development process and to the marketplace.

We generally rely on a combination of patents, copyrights, trademarks, trade secret and other laws, and contractual restrictions on disclosure, copying and transferring title, including confidentiality agreements with vendors, strategic partners, co-developers, employees, consultants and other third parties, to protect our proprietary rights in the developments, improvements and inventions that we have originated and which are incorporated in our products or that fall within our fields of interest. As of September 27, 2019, we own over 290 patents issued in the United States, over 370 patents issued throughout the rest of the world and had approximately another 160 patent applications pending with various patent agencies worldwide. The patents and patents issuing from the pending applications generally expire between 2019 and 2037. We intend to file additional patent applications as appropriate. We have trademarks, both registered and unregistered, that are maintained and enforced to provide customer recognition for our products in the marketplace. We also have agreements with third parties that provide for licensing of patented or proprietary technology, including royalty-bearing licenses and technology cross-licenses. These licenses generally can only be terminated for breach. See “Risk Factors-Protecting our intellectual property can be costly, and we may not be able to maintain licensed rights, and, in either case, our competitive position would be harmed if we are not able to do so.”

In conjunction with the January 2017 separation from Varian, we entered into an Intellectual Property Matters Agreement with Varian, pursuant to which, among other things, we each granted the other licenses to use certain intellectual property.

## **Environmental Matters**

Our operations and facilities, past and present, are subject to environmental laws, including laws that regulate the handling, storage, transport and disposal of hazardous substances. Certain of those laws impose cleanup liabilities under certain circumstances. In connection with those laws and certain of our past and present operations and facilities, we are obligated to indemnify Varian for 20% of the cleanup liabilities related to prior corporate restructuring activities while a division of Varian and fully indemnify Varian for other liabilities arising from the operations of the business transferred to it as part of those activities. Those include facilities sold as part of Varian’s electron devices business in 1995 and thin film systems business in 1997. The U.S. Environmental Protection Agency (“EPA”) or third parties have named Varian as a potentially responsible party under the amended Comprehensive Environmental Response Compensation and Liability Act of 1980 (“CERCLA”), at sites to which Varian or the facilities of the businesses sold in 1995 and 1997 were alleged to have shipped waste for recycling or disposal (the “CERCLA sites”). We anticipate that we will be obligated to reimburse Varian for 20% of the liabilities of Varian related to these CERCLA sites (after adjusting for any insurance proceeds or tax benefits received by Varian). In connection with the CERCLA sites, to date Varian has been required to pay only a small portion of the total cleanup costs and we anticipate that any reimbursement to Varian in the future will not be material. As of September 27, 2019, we had an existing environmental liability of approximately \$0.9 million related to the CERCLA sites.



## **Working Capital**

Our working capital needs and our credit practices are comparable to those of other companies manufacturing and selling similar products in similar markets. We endeavor to carry sufficient levels of inventory to meet the product delivery needs of our customers. We also provide payment terms to customers in the normal course of business. The product warranty obligations contained in our standard terms and conditions typically range from 12 to 24 months, depending on the product.

## **Employees**

As of September 27, 2019, we had approximately 2,000 full-time and part-time employees worldwide. None of our employees based in the United States are unionized or subject to collective bargaining agreements. Employees based in some foreign countries may, from time to time, be represented by works councils or unions or subject to collective bargaining agreements. We currently consider our relations with our employees to be good.

## **Information Available to Investors**

The Securities and Exchange Commission (“SEC”) maintains an internet site, [www.sec.gov](http://www.sec.gov), that contains reports, proxy and information statements, and other information regarding the Company and other issuers that file electronically with the SEC. As soon as reasonably practicable after filing with or furnishing to the SEC, we also make the following reports and information available free of charge on the Investors page of our website [www.vareximaging.com](http://www.vareximaging.com):

- our annual reports on Form 10-K;
- quarterly reports on Form 10-Q;
- current reports on Form 8-K (including any amendments to those reports); and
- proxy statements.

Additionally, our Code of Conduct, Corporate Governance Guidelines and the charters of the Audit Committee, Compensation and Management Development Committee, and Nominating and Corporate Governance Committee are also available on the Investors page of our website. Investors and others should note that we announce material financial and operational information to our investors using our investor relations website (<http://investors.vareximaging.com/>), press releases, SEC filings and public conference calls and webcasts. Please note that information on, or that can be accessed through, our website is not deemed “filed” with the SEC and is not to be incorporated by reference into any of our filings under the Securities Act of 1933, as amended (the “Securities Act”), or the Securities Exchange Act of 1934, as amended (the “Exchange Act”).

## **Executive Officers of the Registrant**

The biographical summaries of our executive officers are as follows:

*Sunny S. Sanyal*, 55, has served as President, Chief Executive Officer, and Director since January 2017. Prior to the separation of Varex from Varian, Sunny served as senior vice president and president of Varian’s Imaging Components business for Varian since February 2014. Prior to joining Varian in 2014, Sunny was chief executive officer of T-System, a privately held company providing information technology solutions and services to hospitals and urgent care facilities. He also served as president of McKesson Provider Technologies, where he led the company to significant market expansion with its clinical software, medical imaging technology, and services solutions. Sunny has held executive positions at GE Healthcare, Accenture, and IDX Systems. He received a Master of Business Administration from Harvard Business School, a Master of Science in industrial engineering from Louisiana State University, and a Bachelor of Engineering in electrical engineering from the University of Bombay.

*Clarence R. Verhoef*, 64, has served as Chief Financial Officer, and Senior Vice President since January 2017. Prior to the separation of Varex from Varian, Clarence served as senior vice president, chief accounting officer and corporate controller for Varian since August 2012. He joined Varian in 2006 and served as the divisional controller of Varian’s Imaging Components business until 2012. Prior to joining Varian, Clarence served in numerous executive management roles, including chief financial officer of Techniscan Medical Systems, and chief financial officer and vice president of marketing for GE OEC Medical Systems. He holds a bachelor’s degree in finance from the University of Utah.

*Kimberley E. Honeysett*, 48, has served as Senior Vice President, General Counsel, and Corporate Secretary since January 2017. Prior to the separation of Varex from Varian, Kim served vice president and assistant general counsel and assistant corporate secretary for Varian, where she advised Varian’s Board of Directors, executive management and corporate functions, including business development, investor relations, human resources, information technology and was responsible for corporate governance,



general compliance matters, litigation and global subsidiary governance. Prior to joining Varian in 2005, Kim served as group director, legal affairs at Siebel Systems, Inc., an enterprise software company, and as an associate with the law firm Brobeck, Phleger & Harrison LLP. Kim holds juris doctor degree from Cornell Law School and a bachelor's degree in communications from the University of California, Los Angeles.

*Brian W. Giambattista*, 60, has served as Senior Vice President, and General Manager - X-ray Detectors since May 2017 and joined Varex after the acquisition of the PerkinElmer Medical Imaging business. He has nearly 30 years of experience in the industry, having held various management and engineering roles at PerkinElmer and General Electric, and received his doctorate degree in physics from the University of Virginia.

*Mark S. Jonaitis*, 58, has served as Senior Vice President and General Manager - X-Ray Sources since 2017. Prior to the separation of Varex from Varian, Mark served in various management positions at Varian, including most recently vice president and general manager, X-ray Tube Products and global manufacturing. Mark joined Varian's predecessor, Varian Associates, in 1983, where he served in various product and engineering positions. Mark received his Bachelor of Science in physics from the University of Utah.

## **Item 1A. Risk Factors**

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

***Varex sells its products and services to a limited number of OEM customers, many of which are also its competitors, and a reduction in or loss of business of one or more of these customers may materially reduce its sales.***

Varex had one customer during fiscal year 2019 that accounted for 17% of its revenue. Varex's ten largest customers as a group accounted for approximately 51%, 49% and 48% of its revenue for fiscal years 2019, 2018 and 2017, respectively.

Varex sells its products to a limited number of OEM customers, many of which are also its competitors with in-house X-ray component manufacturing operations. Although Varex seeks to broaden its customer base, it will continue to depend on sales to a relatively small number of major customers. Because it often takes significant time to replace lost business, it is likely that Varex's operating results would be materially and adversely affected if one or more of its major OEM customers were to cancel, delay, or reduce orders in the future.

Furthermore, Varex generates significant accounts receivables from the sale of its products and the provision of services directly to its major customers. If one or more of these customers were to cancel a product order or service contract (whether in accordance with its terms or otherwise), become insolvent or otherwise be unable or fail to pay for Varex products and services, Varex's operating results and financial condition could be materially and adversely affected.

***Varex may not be able to accurately predict the demand for its products by its customers.***

End-user product demand, economic uncertainties, natural disasters, and other matters beyond Varex's control make it difficult for its customers to accurately forecast and plan future business activities; which makes it difficult for Varex to accurately predict the demand for its products. Because the manufacture of our products requires some lead-time, changes in customer purchasing forecasts have previously impacted Varex's business, resulting in excess inventory and slowdowns in sales. Similar inventory adjustments and slowdowns in sales are likely to occur in the future. Changes to customer forecasts can occur on short notice. Varex's customers also face inherent competitive issues and new product introduction delays which can result in changes in forecasts. The market and regulatory risks faced by Varex's customers also ultimately impact Varex's ability to forecast future business. Varex's agreements for imaging components, such as its three-year pricing agreement with Canon Medical Systems, may contain purchasing estimates that are based on its customers' historical purchasing patterns rather than firm commitments, and actual purchasing volumes under the agreements may vary significantly from these estimates. The variation from forecasted purchasing volume may be due, in part, to the increasing life of X-ray tubes, which can result in reduced demand for replacement X-ray tubes in ways Varex may not be able to accurately forecast. Reductions in purchasing patterns have in the past and may in the future materially and adversely affect Varex's operating results.

***Varex competes in highly competitive markets, and it may lose business to its customers or other companies with greater resources or the ability to develop more effective technologies, or it could be forced to reduce its prices.***

Rapidly-evolving technology, intense competition and pricing pressure characterize the market in which Varex competes. Varex often competes with companies that have greater financial, marketing and other resources than Varex. Some of the major diagnostic imaging systems companies, which are the primary OEM customers for Varex's X-ray components, also manufacture X-ray components, including X-ray tubes, for use in their own imaging systems products. Varex must compete with these in-house manufacturing operations for business. If these customers manufacture a greater percentage of their components in-house or otherwise decrease purchases from external sources, which may occur for a number of reasons, including a strong U.S. Dollar, or a general economic slowdown, Varex could experience reductions in purchasing volume by, or loss of, one or more of these customers. Such a reduction or loss may have a material and adverse effect on its business. In addition, Varex competes against other stand-alone, independent X-ray tube manufacturers for both the OEM business of major diagnostic imaging equipment manufacturers and the independent servicing business for X-ray tubes.

The market for flat panel detectors is also very competitive, and Varex faces intense competition from over a dozen smaller competitors. As a result of these competitive dynamics, to effectively retain the business of its customers and compete with its competitors Varex must have an advantage in one or more significant areas, such as lower product cost, better product quality and/or superior technology and/or performance. Varex has made price concessions to maintain existing customers and attract new customers, and may have to make additional price concessions in the future.

In its industrial segment, Varex competes with other OEM suppliers, primarily outside of the United States. The market for its X-ray tube and flat panel products used for nondestructive testing in industrial applications is small and highly fragmented. Some of Varex's competitors outside the United States may have resources and support from their governments that Varex does not, such as preferences for local manufacturers, and may not be subject to the same trade compliance regulations as Varex. Therefore, Varex's ability to compete in certain high-growth markets may be limited compared to its competitors.

Varex's competitors could develop technologies and products that are more effective than those Varex currently uses or produces or that could render its products obsolete or noncompetitive. In addition, the timing of Varex's competitors' introduction of products into the market could affect the market acceptance and sales of Varex's products. Some competitors offer specialized products that provide, or may be perceived by customers to provide, an advantage over Varex's products. Also, some of Varex's non-U.S. competitors may not be subject to the same standards, regulatory and/or other legal requirements to which Varex is subject and, therefore, they could have a competitive advantage in developing, manufacturing and marketing products and services. Any inability to develop, gain regulatory approval for and supply commercial quantities of competitive products to the market as quickly and effectively as Varex's competitors could limit market acceptance of Varex's products and reduce its sales. Any of these competitive factors could negatively and materially affect Varex's pricing, sales, revenues, market share and gross margins and its ability to maintain or increase its operating margins.

***Changes in import/export regulatory regimes and tariffs could continue to negatively impact our business.***

Tariffs and changes in international trade agreements or trade-related laws and regulations may have an indirect adverse impact on our business. As a component manufacturer, our products are integrated into the systems and products of our OEM customers. If the United States, China or other countries levy tariffs, duties or other additional taxes or restrictions on our customer's products, the demand for such products, and our components included in such products, could decrease, which could have a material adverse effect on our business. Uncertainty over tariffs and trade wars could also cause our customers to delay or cancel orders for our products.

In 2018 and 2019, the United States has imposed tariffs on items imported from China that are incorporated into our products. Tariffs on items imported by us from China and other countries have increased our costs and has increased prices and lowered gross margins on some of our products. These tariffs have had a direct adverse impact on our business and results of operations, and future tariffs could have a more significant impact on our business. China has imposed retaliatory tariffs that impact a number of Varex products including U.S. origin X-ray tubes, heat exchange units, and certain flat panel detectors. The tariffs levied by China have increased our customers' costs for products imported into China, which has caused us to make price concessions on some products and has caused some customers to stop purchasing products from us. We expect that tariffs will continue to have a negative effect on our business and results of operations, including the possibility of continued price concessions or loss of business. Tariffs could limit our ability to compete for increased market share in China, which could cause our long-term prospects in China to suffer. The imposition of additional tariffs by the United States could result in the adoption of additional tariffs by China and other countries,



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as well as further retaliatory actions by any affected country, which could negatively impact the global market for imaging equipment and could have a significant adverse effect on our business.

***Varex's success depends on the successful development, introduction, and commercialization of new generations of products and enhancements to or simplifications of existing product lines.***

Rapid change and technological innovation characterize the markets in which Varex operates, particularly with respect to flat panel technology. Varex's customers use its products in their medical diagnostic, security, and industrial imaging systems, and Varex must continually introduce new products at competitive costs while also improving existing products with higher quality, lower costs, and increased features. To be successful, Varex must anticipate its customers' needs and demands, as well as potential shifts in market preferences. Varex's failure to do so has in the past resulted, and may in the future result, in the loss of customers and an adverse impact to its financial performance. With a relatively strong U.S. Dollar, Varex's ability to meet its customers' pricing expectations is particularly challenging and may result in erosion of product margin and market share.

Varex has in the past spent, and in the future may need to spend, more time and money than it expects to develop, market and introduce new products or enhancements, and, even if Varex succeeds, Varex may not be able to recover all or a meaningful part of its investment. Once introduced, new products may materially and adversely impact sales of Varex's existing products or make them less desirable or even obsolete, which could materially and adversely impact Varex's revenues and operating results. In addition, certain costs, including installation and warranty costs, associated with new products may be proportionately greater than the costs associated with other products and may therefore disproportionately, materially, and adversely affect Varex's gross and operating margins. If Varex is unable to lower these costs over time, Varex's operating results could be materially and adversely affected. Some of the electronic components and integrated circuits used in Varex's flat panel detectors are susceptible to discontinuance and obsolescence risks, which may force Varex to incorporate newer generations of these components, resulting in unplanned additional R&D expenses, delays in the launch of new products, supply disruption, or inventory write downs.

Varex's ability to successfully develop and introduce new products and product enhancements and simplifications, and the revenues and costs associated with these efforts, are affected by Varex's ability to, among other things:

- properly identify customer needs or long-term customer demands;
- prove the feasibility of new products;
- properly manage and control research and development costs;
- limit the time required from proof of feasibility to routine production;
- timely and efficiently comply with internal quality assurance systems and processes;
- limit the timing and cost of regulatory approvals;
- accurately predict and control costs associated with inventory overruns caused by the phase-in of new products and the phase-out of old products;
- price its products competitively and profitably, which can be particularly difficult with a strong U.S. Dollar;
- manufacture, deliver, and install its products in sufficient volumes on time and accurately predict and control costs associated with manufacturing installation, warranty, and maintenance of the products;
- appropriately manage its supply chain;
- manage customer acceptance and payment for products; and
- anticipate, respond to, and compete successfully with competitors.

Furthermore, as discussed in greater detail elsewhere in this "Risk Factors" section, Varex cannot be sure that it will be able to successfully develop, manufacture, or introduce new products or enhancements, the roll-out of which involves compliance with complex quality assurance processes, including the Quality System Regulation of the U.S. Food and Drug Administration ("FDA"). Failure to complete these processes timely and efficiently could result in delays that could affect Varex's ability to attract and retain customers or cause customers to delay or cancel orders, which would materially and adversely affect Varex's revenues and operating results.

***More than half of Varex's revenues are generated from customers located outside the United States, and economic, political, and other risks associated with international sales and operations could materially and adversely affect Varex's sales or make them less predictable.***

Varex conducts business globally. Revenues generated from customers located outside the United States accounted for approximately 65%, 65% and 66% of Varex's total revenues during fiscal years 2019, 2018, and 2017, respectively. As a result,



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Varex must provide significant service and support globally. Varex intends to continue to expand its presence in international markets and expects to expend significant resources in doing so. Varex cannot be sure that it will be able to meet its sales, service, and support objectives or obligations in these international markets or recover its investment in these international markets. Varex's future results could be harmed by a variety of factors, including:

- currency fluctuations, and in particular the strength of the U.S. Dollar (which is our functional and reporting currency) relative to many currencies, which have and may in the future adversely affect Varex's financial results and cause some customers to delay purchasing decisions or move to in-sourcing supply or migrate to lower cost alternatives or ask for additional discounts;
- the longer payment cycles associated with many customers located outside the United States;
- difficulties in interpreting or enforcing agreements and collecting receivables through many foreign countries' legal systems;
- changes in restrictions on trade between the United States and other countries or unstable regional political and economic conditions;
- changes in the political, regulatory, safety or economic conditions in a country or region
- the imposition by governments of additional taxes, tariffs, global economic sanctions programs, or other restrictions on foreign trade such as the tariffs recently put into place by both China and the United States;
- any inability to obtain required export or import licenses or approvals, including the inability to obtain required export licenses during a U.S. government shutdown;
- failure to comply with export laws and requirements, which may result in civil or criminal penalties and restrictions on Varex's ability to export its products, particularly its industrial linear accelerator products;
- risks unique to the Chinese market, including import barriers and preferences for local manufacturers;
- failure to obtain proper business licenses or other documentation or to otherwise comply with local laws and requirements regarding marketing, sales, service, or any other business Varex conducts in a foreign jurisdiction, which may result in civil or criminal penalties and restrictions on its ability to conduct business in that jurisdiction; and
- difficulties in protecting Varex's intellectual property in foreign countries.

Although Varex's sales fluctuate from period to period, in recent years Varex's international operations have represented a larger share of its business. The more Varex depends on international sales, the more vulnerable Varex becomes to these factors.

### ***A change in the percentage of Varex's total earnings from international sales or additional changes in tax laws could increase Varex's effective tax rate.***

Varex's effective tax rate is impacted by tax laws in both the United States and in foreign countries. Earnings from Varex's international subsidiaries are generally taxed at rates that differ from U.S. rates. A change in the percentage of Varex's total earnings from the international subsidiaries, a change in the mix of particular tax jurisdictions between the international subsidiaries, or a change in currency exchange rates could cause Varex's effective tax rate to increase. The Tax Cuts and Jobs Act of 2017 ("U.S. Tax Reform") was signed into law on December 22, 2017. Prior to the enactment of U.S. Tax Reform, Varex was not taxed in the United States on certain undistributed earnings of certain foreign subsidiaries. While U.S. Tax Reform imposed a current tax on cumulative undistributed earnings, these earnings could also become subject to incremental foreign withholding or U.S. state taxes should they be actually remitted to the United States, in which case Varex's financial results could be materially and adversely affected.

The changes included in U.S. Tax Reform are broad, complex, and subject to change and interpretation. Additional statutory changes or interpretive guidance issued by Federal or local authorities could have a material impact on income tax expense, the effective rate, or the value of deferred tax assets and liabilities. In addition, significant judgments and estimates are required to evaluate our tax position and the impact of the new tax law. If these judgments and estimates are incorrect, or if the underlying assumptions are modified by subsequent guidance or are different from what we expect, our tax liability could differ significantly from our current estimates. Changes in the valuation of Varex's deferred tax assets or liabilities, additional changes in tax laws or rates, changes in the interpretation of tax laws in other jurisdictions, or other changes beyond Varex's control could materially and adversely affect its financial position and results of operations.

Varex has entities in certain jurisdictions with cumulative net operating losses for which no income tax benefit can be recorded due to full valuation allowance positions. There could be additional future losses in these and other jurisdictions that would negatively impact Varex's effective tax rate.

***Our secured revolving credit facility and secured term loan credit facility (collectively the “Credit Facility”) restrict certain activities, and failure to comply with the terms of this facility may have an adverse effect on our business, liquidity and financial position.***

Varex is party to a secured revolving credit facility and a secured term loan credit facility, each of which contains restrictive financial covenants, including financial covenants that require Varex to comply with specified financial ratios. If we do not increase our earnings, we are at risk of not being in compliance with certain of our financial covenants, including our consolidated total leverage ratio and our consolidated senior secured leverage ratio. Varex may have to curtail some of its operations to comply with these covenants. In addition, its credit facilities contain other affirmative and negative covenants that could restrict its operating and financing activities. These provisions limit its ability to, among other things, incur future indebtedness, contingent obligations or liens, guarantee indebtedness, make certain investments and capital expenditures, sell stock or assets, pay dividends and consummate certain mergers or acquisitions. Failure to comply with the credit facility requirements, including the requirement to timely deliver financial statements within applicable grace periods, could result in an event of default under our credit facility. Upon an event of default, if the credit facility documents are not amended or the event of default is not waived, the lender could declare all amounts then outstanding, together with accrued interest, to be immediately due and payable. If this happens, Varex may not be able to make those payments or borrow sufficient funds from alternative sources to make those payments. Even if Varex were to obtain additional financing, that financing may be on unfavorable terms.

***Varex has significant debt obligations that could adversely affect its business, profitability and ability to meet its obligations.***

As of September 27, 2019, Varex’s total combined indebtedness, net of deferred loan costs, was approximately \$395.1 million. The borrowings under Varex’s credit facilities bear interest at floating interest rates. As part of its overall risk management practices, Varex entered into financial derivatives, particularly interest rate swaps designed as cash flow hedges, to hedge the floating LIBOR interest rate on \$264.4 million of its debt. As a result, Varex will be exposed to fluctuations in interest rates to the extent of the balance of its borrowings under the LIBOR-based portion of its credit facilities.

Varex's debt could potentially have important consequences to Varex and its investors, including:

- requiring that a portion of Varex’s cash flow from operations be used to make principal and interest payments on this debt, which would reduce cash flow available for other corporate purposes;
- increasing Varex’s vulnerability to shifts in interest rates and to general adverse economic and industry conditions;
- limiting Varex’s flexibility in planning for, or reacting to, changes in its business and the industry; and
- limiting Varex’s ability to borrow additional funds as needed or increasing the costs of any such borrowing.

In addition, Varex’s actual cash requirements in the future may be greater than expected. Varex’s cash flow from operations may not be sufficient to repay all of the outstanding debt as it becomes due, and Varex may not be able to borrow money, sell assets, or otherwise raise funds on acceptable terms, or at all, to refinance Varex’s debt.

***Fulfilling obligations incidental to being a public company place significant demands on Varex’s management, administrative, and operational resources, including accounting and information technology resources.***

As a public company, Varex is subject to the reporting requirements of the Securities Exchange Act of 1934 (the “Exchange Act”), and is required to prepare its financial statements according to the rules and regulations required by the SEC. The Exchange Act requires that Varex file annual, quarterly, and current reports. Varex’s failure to prepare and disclose this information in a timely manner or to otherwise comply with applicable law could subject it to penalties under federal securities laws, cause it to be out of compliance with applicable stock exchange listing requirements, and expose it to lawsuits and restrict its ability to access financing. For example, as a result of the delayed filing of this Annual Report on Form 10-K, we received a notification letter from Nasdaq advising us that we were not in compliance with Nasdaq listing requirements. While with the filing of our Form 10-K we will regain compliance with the Nasdaq listing requirements, if we had failed to regain compliance in a timely manner, it would have negatively impacted Varex.

Varex must, among other things, establish and maintain effective internal controls and procedures for financial reporting and disclosure purposes. Internal control over financial reporting is complex and may be revised over time to adapt to changes in Varex’s business or changes in applicable accounting rules. As described in the following risk factor, Varex has identified material weaknesses in its internal control over financial reporting. Varex cannot assure that its internal control over financial reporting will be effective in the future or that additional material weaknesses will not be discovered with respect to a prior period for which it had previously believed that internal controls were effective.



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Matters impacting Varex's internal controls may cause Varex to be unable to report its financial information on a timely basis or may cause Varex to restate previously-issued financial information, thereby subjecting Varex to adverse regulatory consequences, including sanctions or investigations by the SEC or in respect of violations of applicable stock exchange listing rules. There could also be a negative reaction in the financial markets due to a loss of investor confidence in Varex and the reliability of its financial statements, which could affect Varex's stock price.

***The delayed filing of some of this Annual Report has made Varex currently ineligible to use a registration statement on Form S-3 to register the offer and sale of securities, which could adversely affect its ability to raise future capital or complete acquisitions.***

As a result of the delayed filing of this Annual Report on Form 10-k, Varex will not be eligible to register the offer and sale of our securities using a registration statement on Form S-3 until one year from the date it regained and maintains its status as a current filer. Should Varex wish to register the offer and sale of its securities to the public prior to the time it is eligible to use Form S-3, both the transaction costs and the amount of time required to complete the transaction could increase, making it more difficult to execute any such transaction successfully and potentially harming our financial condition.

***Varex identified material weaknesses in its internal control over financial reporting which, if not remediated appropriately or timely, could result in loss of investor confidence and adversely impact our stock price.***

As further described in Item 9A of this report, at the end of each of fiscal year 2019 and 2018, management determined that Varex's internal control over financial reporting and its disclosure controls and procedures were not effective and that there is a reasonable possibility that a material misstatement of our annual or interim financial statements will not be prevented or detected on a timely basis. Management has identified material weaknesses within our risk assessment process and control environment. Management also identified business process control deficiencies which resulted in material weaknesses in the business processes for revenue, inventory and financial close. These material weaknesses resulted in immaterial audit adjustments and out of period adjustments to the Company's consolidated financial statements. Until remediated, these material weaknesses could result in a material misstatement to the annual or interim consolidated financial statements that would not be prevented or detected on a timely basis. There can be no assurance that the remedial measures being implemented by Varex's management will be successful. If Varex is unable to remediate the material weaknesses, or is otherwise unable to maintain effective internal control over financial reporting or disclosure controls and procedures, Varex's ability to record, process and report financial information accurately, and to prepare financial statements within required time periods, could be adversely affected, which could subject Varex to litigation or investigations requiring management resources and payment of legal and other expenses, including civil penalties, negatively affect investor confidence in our financial statements and adversely impact our stock price.

***Varex may face additional risks from the acquisition or development of new lines of business.***

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

***Varex may be unable to complete future acquisitions or realize expected benefits from acquisitions of or investments in new businesses, products, or technologies, which could harm Varex's business.***

Varex's ability to identify and take advantage of attractive acquisitions or other business development opportunities is an important component in implementing its overall business strategy. Varex must grow its businesses in response to changing technologies, customer demands, and competitive pressures. In some circumstances, Varex may decide to grow its business through the acquisition of complementary businesses, products, or technologies, rather than through internal development; however, there is no guarantee that these acquisitions will be successful or that Varex will realize a return on its investment.

Identifying suitable acquisition candidates can be difficult, time consuming, and costly, and Varex may not be able to identify suitable candidates or successfully complete or finance identified acquisitions, including as a result of failing to obtain regulatory or competition clearances, which could impair Varex's growth and ability to compete. In addition, completing an acquisition can divert



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Varex's management and key personnel from its current business operations, which could harm its business and affect its financial results. Even if Varex completes an acquisition, Varex may not be able to successfully integrate newly-acquired organizations, products, technologies, or employees into its operations or may not fully realize some of the expected synergies.

Integrating an acquisition can also be expensive and time consuming and may strain Varex's resources. It may cost Varex more to commercialize new products than originally anticipated or cause Varex to increase its expenses related to research and development, either of which could materially and adversely impact its results of operations. In many instances, integrating a new business will also involve implementing or improving internal controls appropriate for a public company into a business that lacks them. It is also possible that an acquisition could increase Varex's risk of litigation, as a third party may be more likely to assert a legal claim following an acquisition because of perceived deeper pockets or a perceived greater value of a claim. In addition, Varex may be unable to retain the employees of acquired companies or the acquired company's customers, suppliers, distributors, or other partners for a variety of reasons, including the fact that these entities may be Varex's competitors or may have close relationships with its competitors.

Further, Varex may find that it needs to restructure or divest acquired businesses or assets of those businesses. Even if it does so, an acquisition may not produce the full efficiencies, growth, or benefits that were expected. If Varex decides to sell assets or a business, it may be difficult to identify buyers or alternative exit strategies on acceptable terms, in a timely manner, or at all, which could delay the accomplishment of its strategic objectives. Varex may be required to dispose of a business at a lower price or on less advantageous terms, or to recognize greater losses than it had anticipated.

If Varex acquires a business, it allocates the total purchase price to the acquired business' tangible assets and liabilities, identifiable intangible assets, and liabilities based on their fair values as of the date of the acquisition and records the excess of the purchase price over those values as goodwill. If it fails to achieve the anticipated growth from an acquisition, or if it decides to sell assets or a business, it may be required to recognize an impairment loss on the write down of its assets and goodwill, which could materially and adversely affect its financial results. In addition, acquisitions can result in potentially dilutive issuances of equity securities or the incurrence of debt, contingent liabilities or expenses, or other charges, any of which could harm Varex's business and affect its financial results.

Additionally, Varex participates in joint ventures and has investments in privately-held companies (for example, its 40% ownership in dpiX LLC, its major supplier of its amorphous silicon-based thin film transistor arrays (flat panels used in its digital detectors) that are subject to risk of loss of investment capital. These investments are inherently risky, in some instances because the markets for the technologies or products these companies have under development may never materialize. If these companies do not succeed, Varex could lose some or all of its investment in these companies.

***A disruption at Varex's manufacturing facilities, as well as fluctuating manufacturing costs, could materially and adversely affect its business.***

The majority of Varex's products are manufactured at its facility in Salt Lake City, Utah. Varex's manufacturing operations are subject to potential power failures, the breakdown, failure, or substandard performance of equipment, the improper installation or operation of equipment, and natural or other disasters. Loss or damage to its manufacturing facility due to any of these factors or otherwise could materially and adversely affect Varex's ability to manufacture sufficient quantities of its products or otherwise deliver products to meet customer demand or contractual requirements, which may result in a loss of revenue and other adverse business consequences. Because of the time required to obtain regulatory approval and licensing of a manufacturing facility, Varex may not be available on a timely basis to replace any lost manufacturing capacity. The occurrence of these or any other operational issues at Varex's manufacturing facilities could have a material and adverse effect on Varex's business, financial condition, and results of operations.

Some of Varex's products are manufactured in Wuxi, China; Walluf, Germany; Heerlen and Dinxperlo, the Netherlands; and Calamba City, Philippines, which are subject to similar risks but may also face additional regulatory and political risks, which could impact Varex's ability to manufacture and ship products in a timely manner or at all. Varex manufactures its security products in Las Vegas, Nevada, and certain flat panels in Santa Clara, California, and these operations are also subject to potential power failures, the breakdown, failure, or substandard performance of equipment, the improper installation or operation of equipment, earthquakes, and other disasters, all of which could materially and adversely affect Varex's ability to deliver products to meet customer demand. In addition, Varex's costs associated with manufacturing its products can vary significantly from quarter to quarter, and fluctuations thereof may adversely affect its business, operating results, and/or financial condition.

***Varex's results have been and may continue to be affected by continuing worldwide economic instability, including changes in foreign currency exchange rates and fluctuations in the price of crude oil and other commodities.***

The global economy has been impacted by a number of economic and political factors. In many markets, these conditions have shrunk capital equipment budgets, slowed decision-making and made it difficult for Varex's customers and vendors to accurately forecast and plan future business activities. This, in turn, has caused Varex's customers to be more cautious with, and sometimes freeze, delay, or dramatically reduce purchases and capital project expenditures. Some countries have adopted and may in the future adopt austerity or stimulus programs that could negatively affect Varex's results from period to period. In addition, actions taken by the current U.S. administration and the pending withdrawal of the United Kingdom from the European Union ("EU") may also create global economic uncertainty, which may cause our customers to reduce their spending, which, in turn, could adversely affect our business, financial condition, operating results, and cash flows. An uncertain economic environment may also disrupt supply or affect our service business, as customers' constrained budgets may result in pricing pressure, extended warranty provisions, and even cancellation of service contracts.

In addition, concerns over continued economic instability could make it more difficult for Varex to collect outstanding receivables. A weak or deteriorating healthcare market would inevitably materially and adversely affect Varex's business, financial conditions, and results of operations.

Because Varex's products are generally priced in U.S. Dollars, the strengthening of the U.S. Dollar in the last several years has caused, and could continue to cause, some customers to ask for discounts, delay purchasing decisions, or consider moving to in-sourcing such components or migrating to lower cost alternatives. Further, because Varex's business is global and some payments may be made in local currency, fluctuations in foreign currency exchange rates can impact its results by affecting product demand, revenues and expenses, and/or the profitability in U.S. Dollars of products and services that Varex provides in foreign markets.

Changes in monetary or other policies here and abroad, including as a result of economic and/or political instability or in reaction thereto, would also likely affect foreign currency exchange rates. Furthermore, if one or more European countries were to replace the Euro with another currency, Varex's sales in these countries, or in Europe generally, would likely be materially and adversely affected until stable exchange rates are established.

Additionally, fluctuations in commodities prices could materially and adversely affect Varex's performance. Rising commodities prices will increase Varex's costs and those of Varex's medical OEM customers, which could in turn result in reduced demand for Varex's products. Further, Varex's security product revenues from oil-producing countries, in which Varex has a significant customer base, have in the past suffered as a result of volatility in oil prices and remain sensitive to fluctuations in the future.

***The loss of a supplier or any inability to obtain supplies of important components could restrict Varex's ability to manufacture products, cause delays in its ability to deliver products, or significantly increase its costs.***

Varex obtains from a limited group of suppliers or from sole-source suppliers some of the components included in its products, such as wave guides for industrial linear accelerators, transistor arrays, cesium iodide coatings and specialized integrated circuits for flat panel detectors, X-ray tube targets, housings, glass frames, high-voltage cable, bearings and various other components. For example, Varex's major supplier of its amorphous silicon-based thin film transistor arrays (flat panels) used in its digital image detectors is dpiX LLC. Although Varex holds a 40% ownership interest in dpiX, Varex does not have majority voting rights and does not have the power to direct the activities of dpiX. In addition, Varian is Varex's sole source supplier for a key component in linear accelerators used in Varex's security and inspection products subsystems, which are specially made for Varex. If current suppliers cease producing these components, there can be no assurance that the components will be available from other suppliers on reasonable terms or at all.

If Varex loses any of these limited- or sole-source suppliers, if their operations are substantially interrupted, or if any of them fail to meet performance or quality specifications or delivery deadlines, Varex may be required to obtain and qualify one or more replacement suppliers. Such an event (1) may then also require Varex to redesign or modify its products to incorporate new parts and/or further require Varex to obtain clearance, qualification, or certification of these products, including by the FDA, or obtain other applicable regulatory approvals in other countries, or (2) could significantly increase costs for the affected products and cause material delays in delivery of those and other related products. In addition, manufacturing capacity limitations of any of Varex's suppliers or other inability of these suppliers to meet increasing demand or delivery deadlines could limit growth opportunities for the affected product lines and damage customer relationships. Shortage of, and greater demand for, components and subassemblies could also

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increase manufacturing costs if the supply/demand imbalance increases the price of the components and subassemblies. Any of these events could materially and adversely affect Varex's business and financial results.

***A shortage or change in source of, or increase in price of, raw materials could restrict Varex's ability to manufacture products, cause delays, or significantly increase its cost of goods.***

Varex relies on the supplies of certain raw materials such as tungsten, lead, iridium, and copper for security and inspection products and copper, lead, tungsten, rhenium, molybdenum zirconium, and various high grades of steel alloy for X-ray tubes. Worldwide demand, availability, and pricing of these raw materials have been volatile, and Varex expects that availability and pricing will continue to fluctuate in the future. If supplies are restricted or become unavailable or if prices increase, this could constrain Varex's manufacturing of affected products, reduce its profit margins, or otherwise materially and adversely affect its business.

Varex is required to disclose (1) the presence in a company's products of certain metals known as "conflict minerals," which are metals mined from the Democratic Republic of the Congo and adjoining countries, and (2) procedures regarding a manufacturer's efforts to identify the sourcing of those minerals from this region. Varex's complex supply chain may inhibit Varex's ability to sufficiently verify the origins of the relevant minerals used in its products through the due diligence procedures that it implements, which may harm Varex's reputation. In addition, Varex may encounter challenges in satisfying customers who require that all of the components of Varex products are certified as conflict-free, which could place Varex at a competitive disadvantage if it is unable to do so. Moreover, complying with these rules requires investigative efforts, which has and will continue to cause Varex to incur associated costs and could materially and adversely affect the sourcing, supply, and pricing of materials used in Varex's products or result in process or manufacturing modifications, all of which could materially and adversely affect its results of operations.

***The trading price of Varex's common stock may decline or fluctuate significantly and fluctuations in Varex's operating results, including quarterly revenues, and margins, may cause its stock price to be volatile, which could cause losses for its stockholders.***

In the past year, Varex's stock price has ranged from a low of \$21.57 to a high of \$35.00. Varex cannot guarantee that an active trading market will be sustained for its common stock. Nor can Varex predict the prices at which shares of its common stock may trade. Varex has experienced and expects in the future to experience fluctuations in its operating results, including revenues and margins, from period to period. These fluctuations may cause Varex's stock price to be volatile, which could cause losses for its stockholders.

Varex's quarterly and annual operating results, including its revenues and margins, may be affected by a number of other factors, including:

- the introduction and timing of announcement of new products or product enhancements by Varex and its competitors;
- change in its or its competitors' pricing or discount levels;
- changes in foreign currency exchange rates and other economic uncertainty;
- changes in import/export regulatory regimes including the imposition of tariffs on our products or those of our customers;
- changes in the relative portion of its revenues represented by its various products, including the relative mix between higher margin and lower-margin products;
- the ability to identify and remediate significant deficiencies and material weaknesses in internal controls;
- changes in the relative portion of its revenues represented by its international region as a whole and by regions within the overall region, as well as by individual countries (notably, those in emerging markets);
- fluctuation in its effective tax rate, which may or may not be known to Varex in advance;
- the availability of economic stimulus packages or other government funding, or reductions thereof;
- disruptions in the supply or changes in the costs of raw materials, labor, product components or transportation services;
- changes to its organizational structure, which may result in restructuring or other charges;
- disruptions in its operations, including its ability to manufacture products, caused by events such as earthquakes, fires, floods, terrorist attacks or the outbreak of epidemic diseases;
- the unfavorable outcome of any litigation or administrative proceeding or inquiry, including governmental audits, as well as ongoing costs associated with legal proceedings and governmental audits; and
- accounting changes and adoption of new accounting pronouncements.

Because many of Varex's operating expenses are based on anticipated capacity levels, and a high percentage of these expenses are fixed for the short term, a small variation in the timing of revenue recognition can cause significant variations in operating results from quarter to quarter. If Varex's gross margins fall below the expectation of securities analysts and investors, the trading price of Varex common stock may decline.



***Compliance with foreign laws and regulations applicable to the marketing, manufacture, and distribution of Varex's products may be costly, and failure to comply may result in significant penalties and other harm to Varex's business.***

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

For Varex to market its products internationally, Varex must obtain clearances or approvals for products and product modifications. These processes (including, for example, in the EU, the European Economic Area ("EEA"), Switzerland, Brazil, Australia, China, Japan and Canada) can be time consuming, expensive and uncertain, which can delay Varex's ability to market products in those countries. Delays in the receipt of or failure to receive regulatory approvals, the inclusion of significant limitations on the indicated uses of a product, the loss of previously obtained approvals or failure to comply with existing or future regulatory requirements could restrict or prevent Varex from doing business in a country or subject Varex to a variety of enforcement actions and civil or criminal penalties, which would materially and materially and adversely affect its business. In addition, compliance with changing regulatory schemes, such as what may occur in connection with Brexit, may add additional complexity, cost and delays in marketing or selling Varex's products. The Brexit process has caused legal uncertainty and will likely lead to divergent national laws and regulations. While the full financial, regulatory and legal effects of Brexit are unknown, if the United Kingdom's regulatory scheme is materially different from the current EU regulatory process, Varex's regulatory compliance burden will likely increase.

Within the EU/EEA, Varex must obtain, and in turn affix, a CE mark certification, which is a European marking of conformity that indicates that a product meets the essential requirements of the Medical Device Directive. Compliance with the Medical Device Directive is done through a self-certification process that is then verified by an independent certification body called a "Notified Body," which is an organization empowered by the legislature to conduct this verification. Once the CE mark is affixed, the Notified Body will regularly audit Varex to ensure that it remains in compliance with the applicable European laws and Medical Device Directive. By affixing the CE mark to its product, Varex is certifying that its products comply with the laws and regulations required by the EU/EEA countries, thereby allowing the free movement of its products within these countries and others that accept CE mark standards. If Varex cannot support its performance claims and demonstrate compliance with the applicable European laws and the Medical Device Directive, Varex would lose its right to affix the CE mark to its products, which would prevent Varex from selling its products within the EU/EEA/Switzerland territory and in other countries that recognize the CE mark. In April 2017, the European Commission adopted two new regulations on medical devices. These new regulations impose stricter requirements for placing medical devices in the EU market, as well as for Notified Bodies. These new regulations have resulted in the limited availability of recognized Notified Bodies, which could delay our ability to obtaining CE marks. Varex may be subject to risks associated with additional testing, modification, certification, or amendment of its existing market authorizations, or Varex may be required to modify products already installed at its customers' facilities to comply with the official interpretations of these revised regulations.

Varex is also subject to international laws and regulations of general applicability relating to matters such as environmental protection, safe working conditions, and manufacturing practices, as well as others. These are often comparable to, if not more stringent than, the equivalent regulations in the United States. Sales overseas are also affected by regulation of matters such as product standards, packaging, labeling, environmental and product recycling requirements, import and export restrictions, tariffs, duties, and taxes.

In addition, Varex is required to timely file various reports with international regulatory authorities similar to the reports it is required to timely file with U.S. regulatory authorities, including reports required by international adverse event reporting regulations. If these reports are not timely filed, regulators may impose sanctions, including temporarily suspending Varex's market authorizations or CE mark, and sales of its products may suffer.

Further, as Varex enters new businesses or pursues new business opportunities internationally, or as regulatory schemes change, Varex may become subject to additional laws, rules, and regulations. Becoming familiar with and implementing the infrastructure necessary to comply with these laws, rules, and regulations is costly. Additionally, in some countries, Varex relies or may rely in the future on foreign distributors and agents to assist in complying with foreign regulatory requirements, and Varex cannot be sure that they will always do so. The failure of Varex or its agents to comply with these laws, rules, and regulations could delay the introduction of new products, cause reputational harm, or result in investigations, fines, injunctions, civil penalties, criminal prosecution, or an inability to sell Varex's products in or to import its products into certain countries, which could materially and adversely affect Varex's business.

***Compliance with U.S. laws and regulations applicable to the marketing, manufacture, and distribution of Varex's products may be costly, and failure or delays in obtaining regulatory clearances or approvals or failure to comply with applicable laws and regulations could prevent Varex from distributing its products, require Varex to recall its products, or result in significant penalties or other harm to Varex's business.***

Some of Varex's products and those of OEMs that incorporate Varex's products are subject to extensive and rigorous government regulation in the United States. Compliance with these laws and regulations is expensive and time-consuming, and failure to comply with these laws and regulations could materially and adversely affect Varex's business.

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

In addition, Varex is required to timely file various reports with the FDA, including reports required by the medical device reporting regulations ("MDRs"), that require Varex report to regulatory authorities if its devices may have caused or contributed to a death or serious injury or malfunctioned in a way that would likely cause or contribute to a death or serious injury if the malfunction were to recur. If Varex initiates a correction or removal of a device to reduce a risk to health posed by the device, Varex would be required to submit a publicly-available correction and removal report to the FDA and, in many cases, similar reports to other regulatory agencies. This report could be classified by the FDA as a device recall, which could lead to increased scrutiny by the FDA, other international regulatory agencies, and Varex's customers regarding the quality and safety of Varex's devices. If these MDRs or correction and removal reports are not filed on a timely basis, regulators may impose sanctions, sales of Varex's products may suffer, and Varex may be subject to product liability or regulatory enforcement actions, all of which could harm its business.

Government regulation may also cause significant delays or even prevent the marketing and full commercialization of future products or services that Varex may develop and/or may impose costly requirements on Varex's business. Further, as Varex enters new businesses or pursues new business opportunities, Varex will become subject to additional laws, rules, and regulations, including FDA and foreign rules and regulations. Becoming familiar with and implementing the infrastructure necessary to comply with these laws, rules, and regulations is costly and time consuming. In addition, failure to comply with these laws, rules and regulations could delay the introduction of new products and could materially and adversely affect Varex's business.

If Varex or any of its suppliers, distributors, agents, or customers fail to comply with FDA, Federal Trade Commission, or other applicable U.S. regulatory requirements or are perceived to have failed to comply with regulations, Varex may face:

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



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Varex is also subject to federal and state laws and regulations of general applicability relating to matters such as environmental protection, safe working conditions, manufacturing practices, and other matters. Insurance coverage is not commercially available for violations of law, including the fines, penalties, or investigatory costs that Varex may incur as the consequence of regulatory violations. Consequently, Varex does not have insurance that would cover this type of liability.

***Varex sells certain X-ray tube products as replacements which are subject to medical device certification and product registration laws and regulations, which vary by country and are subject to change, and Varex may be unable to receive registration approval or renewal of existing registrations if it fails to meet regulatory approval requirements or if the approval process becomes commercially infeasible or impractical.***

Varex markets and distributes certain X-ray tubes through distributors and third-party/multi-vendor service organizations that are used as equivalent replacements for specific OEM tubes. Varex is subject to medical device certification and product registration laws, which vary by country and are subject to periodic reviews and changes by regulatory authorities in those countries. For example, to sell X-ray tubes for replacement applications in China, product registrations must be approved by the new National Medical Products Administration (“NMPA”). Varex must comply with the requirements of the NMPA, and Varex may not be able to receive registration approval or renewal of existing registrations if it fails to meet regulatory approval requirements or if the process of gaining approval becomes commercially infeasible or impractical. Certain of these local laws and regulations have the effect of serving as a barrier to trade and can be difficult to navigate predictably.

In addition, certain countries in which Varex products are sold require products to undergo re-registration if the product is altered in any significant way, and it may be determined that the separation of Varex from Varian, including Varex’s new name, will require these products to be re-registered as Varex products, even if they are physically unchanged.

These registration processes can be costly and time consuming, and customers may decide to purchase products from Varex’s competitors that do not have to be involved in a re-registration process. In addition, Varex’s inability to receive or renew product registrations may prevent Varex from marketing and/or distributing those particular products for replacement applications in the specific country.

***Existing and future healthcare reforms, including the Affordable Care Act and changes to reimbursement rates, may indirectly have a material adverse effect on Varex’s business and results of operations.***

Sales of Varex’s products to OEMs in the medical sector indirectly depend on whether adequate reimbursement is available for its customers’ products from a variety of sources, such as government healthcare insurance programs, including U.S. Medicare and Medicaid programs, foreign government programs, private insurance plans, health maintenance organizations, and preferred provider organizations. Without adequate reimbursement, the demand for Varex’s customers’ products, and therefore indirectly Varex’s products, may be limited.

Healthcare reform proposals and medical cost containment measures in the United States and in many foreign countries could limit the use of both Varex’s and its customers’ products, reduce reimbursement available for such use, further tax the sale or use of Varex’s products, and further increase the administrative and financial burden of compliance. These reforms and measures, including the uncertainty in the medical community regarding their nature and effect, could have a material and adverse effect on Varex’s and its customers’ purchasing decisions regarding its products and treatments and could harm Varex’s business, results of operations, financial condition, and prospects. Varex cannot predict the specific healthcare programs and regulations that will be ultimately implemented by local, regional, and national governments globally. However, any changes that lower reimbursements for Varex’s or its customers’ products and/or procedures using these products, including, for example, existing reimbursement incentives to convert from analog to digital X-ray systems, or changes that reduce medical procedure volumes or increase cost containment pressures on Varex or others in the healthcare sector could materially and adversely affect Varex’s business and results of operations.

***Varex is subject to federal, state, and foreign laws governing its business practices which, if violated, could result in substantial penalties. Additionally, challenges to or investigations into Varex’s practices could cause adverse publicity and be costly to respond to and thus could harm its business.***

***Anti-corruption laws and regulations.*** Varex is subject to the U.S. Foreign Corrupt Practices Act and anti-corruption laws, as well as similar laws in foreign countries, such as the U.K. Bribery Act and the Law On the Fundamentals of Health Protection in the Russian Federation. In general, there is a worldwide trend to strengthen anti-corruption laws and their enforcement, and the healthcare industry and medical equipment manufacturers have been particular targets of these investigation and enforcement efforts. Any violation of these laws by Varex or its agents or distributors could create substantial liability for Varex, subject its officers and



directors to personal liability, and cause a loss of reputation in the market. Varex operates in many countries, including India and China, where the public sector is perceived as being corrupt. Varex's strategic business plans include expanding its business in regions and countries that are rated as higher risk for corruption activity by Transparency International e.V., an international non-profit that publishes an annual corruption perception index. Becoming familiar with and implementing the infrastructure necessary to comply with laws, rules, and regulations applicable to new business activities and mitigating and protecting against corruption risks could be costly. Failure by Varex or its agents or distributors to comply with these laws, rules, and regulations could delay its expansion into high-growth markets and could materially and adversely affect its business. Varex will likely do more business, directly and potentially indirectly, in countries where the public sector is perceived to be corrupt. Increased business in higher-risk countries could subject Varex and its officers and directors to increased scrutiny and increased liability from its business operations.

*Competition and trade compliance laws.* Varex is subject to various competition and trade compliance laws in the jurisdictions where it operates. Regulatory authorities in those jurisdictions may have the power to subject Varex to sanctions and impose changes or conditions in the way Varex conducts its business. An increasing number of jurisdictions provide private rights of action for competitors or consumers to assert claims of anti-competitive conduct and seek damages. Increased government scrutiny of Varex's actions or enforcement of private rights of action could materially and adversely affect its business or damage its reputation. Varex may be required to conduct internal investigations or face audits or investigations by one or more domestic or foreign government agencies, which could be costly and time consuming and could divert its management and key personnel from its business operations. An adverse outcome under any such investigation or audit could subject Varex to fines and/or criminal or other penalties, which could materially and adversely affect Varex's business and financial results. Furthermore, competition laws may prohibit or increase the cost of future acquisitions that Varex may desire to undertake.

*Laws and ethical rules governing interactions with healthcare providers.* Varex does not generally sell its products directly to healthcare providers, but may occasionally sell its products to healthcare providers through distributors. The U.S. Medicare and Medicaid "anti-kickback" laws, and similar state laws, prohibit payments or other remuneration that is intended to induce hospitals, physicians, or others either to refer patients or to purchase, lease, or order, or to arrange for or recommend the purchase, lease, or order of healthcare products or services for which payment may be made under federal and state healthcare programs, such as Medicare and Medicaid. These laws affect Varex's sales, marketing, and other promotional activities by limiting the kinds of financial arrangements Varex may have with hospitals, physicians, or other potential purchasers of its products. They particularly impact how Varex structures its sales offerings, including discount practices, customer support, education and training programs, physician consulting, research grants, and other fee-for-service arrangements. These laws are broadly written, and it is often difficult to determine precisely how these laws will be applied to specific circumstances.

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

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

***Warranty claims may materially and adversely affect Varex's business.***

Varex could experience an increase in warranty claims as a result of issues with product quality or product failures as a direct result of Varex's design, manufacturing, or issues in its supply chain. Such an occurrence may damage Varex's market reputation, cause sales to decline, or require repairs or voluntary remedial measures to enhance customer satisfaction, which could materially and adversely impact Varex's financial results. Increased warranty claims on any given product could cause Varex to halt production on that product and significantly impair Varex's liquidity and profitability, and cause reputational harm to Varex. Because some categories of products tend to experience higher numbers of warranty claims than others, a shift in the types of products that Varex's customers purchase could lead to an increase in warranty claims. If actual levels of warranty claims are greater than the level of claims Varex estimates, cost of sales could increase, and Varex's financial condition could be materially and adversely affected. In addition, product quality issues could result in significant follow-on effects for Varex, including, among other things, reputational harm to Varex and its customers, loss of customers, and liability as a result of product quality issues. These outcomes would materially and adversely affect Varex's business and financial condition.

***If Varex is not able to match its manufacturing capacity with demand for its products, its financial results may suffer.***

Many of Varex's products have a long production cycle, and Varex must anticipate demand for its products to ensure adequate manufacturing or testing capacity. If Varex is unable to anticipate demand, and its manufacturing or testing capacity does not keep pace with product demand, Varex will not be able to fulfill orders in a timely manner, which may negatively impact its financial results and overall business. Conversely, if demand for Varex's products decreases, the fixed costs associated with excess manufacturing capacity may harm its financial results, including by decreasing gross margins and increasing research and development costs as a percentage of revenue.

***Delivery schedules for Varex's security, industrial, and inspection products tend to be unpredictable.***

Varex designs, manufactures, sells, and services Linatron® X-ray accelerators, image-processing software, and image detection products for security and inspection, such as cargo screening at ports and borders and nondestructive examination for a variety of applications, as well as industrial applications. Varex generally sells security and inspection products to OEMs who incorporate its products into their inspection systems, which are then sold to customs and other government agencies, as well as to commercial organizations in the casting, power, aerospace, chemical, petro-chemical, and automotive industries. Varex believes growth in its security and inspection products will be driven by security cargo screening and border protection needs, as well as by the needs of customs agencies to verify shipments for assessing duties and taxes. This business is heavily influenced by domestic and international government policies on border and port security, political change, and government budgets. In addition, Varex believes growth in this product line may be driven in part by industrial customers engaged in 3-D printing, which, as a developing market, may be difficult to predict. Orders for Varex's security and inspection products have been and may continue to be unpredictable, as governmental agencies may place large orders with Varex or its OEM customers in a short time period and then may not place any orders for a long time period thereafter. Because it is difficult to predict Varex's OEM customer delivery, the actual timing of sales and revenue recognition varies significantly. The market for border protection systems has slowed significantly, and end customers, particularly in oil-based economies and war zones in which Varex has a significant customer base, are delaying system deployments or tenders and considering moving to alternative sources, resulting in a decline in the demand for security and inspection products.

The demand for Varex's security and inspection products is heavily influenced by U.S. and foreign governmental policies on national and homeland security, border protection, and customs activities, which depend upon government budgets and appropriations that are subject to economic conditions, as well as political changes and oil prices. Varex has seen customers freeze or dramatically reduce purchases and capital project expenditures, delay projects, or act cautiously as governments around the world wrestle with spending priorities. As economic growth remains sluggish in various jurisdictions and appears to be deteriorating in others, and as concerns about levels of government employment and government debt continue, Varex expects that these effects will also continue. Bid awards in this business may be subject to challenge by third parties, as Varex has previously encountered with a large government project. These factors make this business more unpredictable and could cause volatility in Varex's revenues and earnings.

***Varex's international manufacturing operations subject it to volatility and other risks, including high security risks, which could result in harm to its employees and contractors or substantial costs.***

Varex conducts certain manufacturing operations internationally to reduce costs and streamline its manufacturing operations. There are administrative, legal, and governmental risks to operating internationally that could increase operating expenses or hamper the development of these operations. The risks from operating internationally that could increase Varex's operating expenses and



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materially and adversely affect its operating results, financial condition, and ability to deliver its products and grow its business include, among others:

- difficulties in staffing and managing employee relations and foreign operations, particularly in attracting and retaining personnel qualified to design, sell, test, and support its products;
- fluctuations in currency exchange rates;
- difficulties in coordinating its operations globally and in maintaining uniform standards, controls, procedures, and policies across its operations;
- difficulties in enforcing contracts and protecting intellectual property;
- diversion of management attention;
- imposition of burdensome governmental regulations, including changing laws and regulations with respect to collection and maintenance of personally identifiable data;
- regional and country-specific political and economic instability, as discussed in greater detail below; and
- inadequacy of the local infrastructure to support its operations.

Varex's international locations expose it to higher security risks compared to its United States locations, which could result in both harm to its employees and contractors or substantial costs. Some of its services are performed in or adjacent to high-risk locations where the country or location and surrounding area is suffering from political, social, or economic turmoil, war or civil unrest, or has a high level of criminal or terrorist activity. In those locations where Varex has employees or operations, Varex may incur substantial costs to maintain the safety of its personnel. Despite these precautions, the safety of its personnel in these locations may continue to be at risk, and Varex may in the future suffer the loss of employees and contractors, which could harm its business reputation and operating results.

***Varex's competitive position would be harmed if it is not able to maintain its intellectual property rights and protecting Varex's intellectual property can be costly.***

Varex files applications as appropriate for patents covering new products and manufacturing processes. Varex cannot be sure, however, that patents will be issued from any of Varex's pending or future patent applications. Varex also cannot be sure that its current patents, the claims allowed under its current patents, or patents for technologies licensed to Varex will be sufficiently broad to protect its technology position against competitors. Issued patents owned by, or licensed to, Varex may be challenged, invalidated, or circumvented, or the rights granted under the patents may not provide Varex with competitive advantages. Asserting Varex's patent rights against others in litigation or other legal proceedings is costly and diverts managerial resources. For example, during fiscal year 2019, Varex initiated litigation asserting claims of patent infringement against a third party. Varex intends to prosecute its claims vigorously, and Varex has experienced, and will continue to experience, increased legal expenses related to this litigation that could adversely affect its financial results. An adverse finding in this or similar patent infringement litigation could adversely impact Varex's competitive position. In addition, Varex may not be able to detect patent infringement by others or may lose its competitive position in the market before Varex is able to do so.

Varex also relies on a combination of copyright, trade secret, and other laws, and contractual restrictions on disclosure, copying and transferring title (including confidentiality agreements with vendors, strategic partners, co-developers, employees, consultants, and other third parties), to protect its proprietary, and other confidential rights. These protections may prove to be inadequate, since agreements may still be breached, and Varex may not have adequate remedies for a breach. Varex's trade secrets may become known to or be independently developed by others, including as a result of misappropriation by unauthorized access to Varex's technology systems. If Varex's proprietary or confidential information is misappropriated, its business and financial results could be materially and adversely impacted. Varex has trademarks, both registered and unregistered, that are maintained and enforced to provide customer recognition for its products in the marketplace, but unauthorized parties may still use them. Varex also licenses certain patented or proprietary technologies from others. In some cases, products with substantial revenues may depend on these license rights. If Varex were to lose the rights to license these technologies, or its costs to license these technologies were to materially increase, its business would suffer. As Varex expands its manufacturing capabilities outside of the United States, more of Varex's intellectual property may be held in jurisdictions that do not have robust intellectual property protections, which may make it harder for Varex to adequately protect its Intellectual Property.

***Third parties may claim that Varex is infringing upon their intellectual property, and Varex could suffer significant litigation or licensing expenses or be prevented from selling its products.***

There is a substantial amount of litigation over patent and other intellectual property rights in the industries in which Varex competes. Varex's competitors, like companies in many high technology businesses, continually review other companies' activities for



possible conflicts with their own intellectual property rights. In addition, non-practicing entities may review Varex's activities for conflicts with their patent rights. Determining whether a product infringes on a party's intellectual property rights involves complex legal and factual issues, and the outcome of this type of litigation is often uncertain. Parties may claim that Varex is infringing upon their intellectual property rights. Varex may not be aware of intellectual property rights of others that relate to its products, services, or technologies. From time to time, Varex has received notices from parties asserting infringement, and Varex has been subject to lawsuits alleging infringement of patent or other intellectual property rights. Any dispute regarding patents or other intellectual property could be costly and time consuming and could divert Varex's management and key personnel from its business operations. Varex may not prevail in a dispute. Varex does not maintain insurance for intellectual property infringement, so costs of defense, whether or not Varex is successful in defending an infringement claim, will be borne by Varex and could be significant. If Varex is unsuccessful in defending or appealing an infringement claim, Varex may be subject to significant damages, and its combined financial position, results of operations, or cash flows could be materially and adversely affected. Varex may also be subject to injunctions against development and sale of its products, the effect of which could be to materially reduce its revenues. Furthermore, a third party claiming infringement may not be willing to license its rights to Varex, and even if a third-party rights holder is willing to do so, the amounts Varex might be required to pay under the associated royalty or license agreement could be significant. Varex could decide to alter its business strategy or voluntarily cease the allegedly infringing actions rather than face litigation or pay a royalty, which could materially and adversely impact its business and results of operations.

***Product defects or misuse may result in material product liability or professional errors and omissions claims, litigation, investigation by regulatory authorities, or product recalls that could harm Varex's future revenues and require it to pay material uninsured claims.***

Varex's business exposes it to potential product liability claims that are inherent in the manufacture, sale, installation, servicing, and support of components that are used in medical devices and other devices that deliver radiation. Because Varex's products, through incorporation in OEMs' systems, are involved in the intentional delivery of radiation to the human body and other situations where people may come into contact with radiation (for example, when Varex's security and inspection products are being used to scan cargo or in the diagnosis of medical problems), the possibility for significant personal injury or loss of life exists. Although Varex's products are incorporated into OEMs' systems, and thus only perform pursuant to the design and operating systems of OEMs, Varex may also be subject to claims for property damage, personal injury, or economic loss related to or resulting from any errors or defects in its products or the installation, servicing, or support of its products. Any accident or mistreatment could subject Varex to legal costs, litigation, adverse publicity, and damage to its reputation, whether or not its products or services were a factor.

If Varex's X-ray inspection systems fail to detect the presence of bombs, explosives, weapons, contraband, or other threats to personal safety, Varex could be subject to product and other liability claims or negative publicity, which could result in increased costs, reduced sales, and a decline in the market price of Varex's common stock. There are many factors beyond Varex's control that could result in the failure of its products to detect the presence of bombs, explosives, weapons, contraband, or other threats to personal safety, including operator error and misuse of or malfunction of Varex equipment. The failure of Varex's systems to detect the presence of these dangerous materials may lead to personal injury, loss of life, and extensive property damage and may result in potential claims against Varex.

Product liability actions are subject to uncertainty and may be expensive, time consuming, and disruptive to Varex's operations. For these and other reasons, Varex may choose to settle product liability claims against it regardless of their actual merit. A product liability action determined against Varex could result in adverse publicity or significant damages, including the possibility of punitive damages, and Varex's combined financial position, results of operations, or cash flows could be materially and adversely affected.

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

Varex maintains limited product liability insurance coverage. Varex's product liability insurance policies are expensive and have high deductible amounts and self-insured retentions. Varex's insurance coverage may prove to be inadequate, and future policies may not be available on acceptable terms or in sufficient amounts, if at all. If a material claim is not insured or is in excess of Varex's insurance coverage, Varex could have to pay substantial damages, which could have a material and adverse effect on its financial position and/or results of operations.



***Certain of Varex's products are subject to regulations relating to use of radioactive material, compliance with which may be costly, and a failure to comply therewith may materially and adversely affect Varex's business.***

As a manufacturer and seller of medical devices and devices emitting radiation or utilizing radioactive by-product material, Varex and some of its suppliers and distributors are subject to extensive regulation by United States governmental authorities, such as the FDA, the Nuclear Regulatory Commission ("NRC"), and state and local regulatory agencies, which is intended to ensure the devices are safe and effective and comply with laws governing products which emit, produce, or control radiation. These regulations govern, among other things, the design, development, testing, manufacturing, packaging, labeling, distribution, import/export, sale, and marketing and disposal of Varex's products. Varex is also subject to international laws and regulations that apply to manufacturers of radiation-emitting devices and products utilizing radioactive materials. These are often comparable to, if not more stringent than, the equivalent regulations in the United States.

Varex's industrial and medical devices utilizing radioactive material are subject to NRC clearance and approval requirements, and the manufacture and sale of these products are subject to extensive federal and state regulation that varies from state to state and among regions. Varex's manufacture, distribution, installation, service, and removal of industrial devices utilizing radioactive material or emitting radiation also requires Varex to obtain a number of licenses and certifications for these devices and materials. Service of these products must also be in accordance with a specific radioactive materials licenses. Obtaining licenses and certifications may be time consuming, expensive, and uncertain.

The handling and disposal of radioactive materials resulting from the manufacture, use, or disposal of Varex's products may impose significant costs and requirements. Disposal sites for the lawful disposal of materials generated by the manufacture, use, or decommissioning of Varex's products may no longer accept these substances in the future or may accept them on unfavorable terms.

***If Varex is unable to obtain required FDA clearances or approvals for a product or is unduly delayed in doing so, or the uses of that product were limited, Varex's business could suffer.***

Typically, Varex's OEM customers are responsible for obtaining 510(k) pre-market notification clearance on their systems that integrate Varex products. A substantial majority of Varex's products are "Class I" devices that do not require 510(k) clearance, but Varex does produce software that is classified as a Class II device subject to 510(k) clearance. Unless an exception applies, Varex may be required by FDA regulations to obtain a 510(k) pre-market notification clearance in connection with the manufacture of a new medical device or a new indication for use of, or other significant change in, an existing currently marketed medical device before it can market or sell those products in the United States. Modifications or enhancements to a product that could significantly affect its safety or effectiveness, or that would constitute a major change in the intended use of the device, technology, materials, labeling, packaging, or manufacturing process also require a new 510(k) clearance. Although manufacturers make the initial determination whether a change to a cleared device requires a new 510(k) clearance, Varex cannot ensure that the FDA will agree with its decisions not to seek additional approvals or clearances for particular modifications to its products or that Varex will be successful in obtaining new 510(k) clearances for modifications. Obtaining clearances or approvals is time consuming, expensive, and uncertain. Varex may not be able to obtain the necessary clearances or approvals or may be unduly delayed in doing so, which could harm its business. Furthermore, even if Varex is granted regulatory clearances or approvals, they may include significant limitations on the indicated uses of the product, which may limit the market for the product. If Varex is unable to obtain required FDA clearance or approval for a product or is unduly delayed in doing so, or the uses of that product were limited, Varex's business could suffer.

***Disruption of critical information systems or material breaches in the security of Varex's systems may materially and adversely affect its business and customer relations.***

Information technology (including technology from third party providers) helps Varex operate efficiently, interface with and support its customers, maintain financial accuracy and efficiency, and produce its financial statements. In the ordinary course of its business, Varex collects, processes and stores sensitive data, including intellectual property, proprietary business information and that of customers, suppliers and business partners, third parties accessing its website, patient data and personally identifiable information of customers and employees, in Varex's data centers, and on its networks, as well as third party off-site infrastructure. Despite security measures, there is an increasing threat of information security attacks, including from computer viruses or other malicious codes, unauthorized access attempts, and cyber-attacks that pose risks to companies, including Varex. Because the techniques used to obtain unauthorized access, or to sabotage systems, change frequently, have become increasingly sophisticated and generally are not recognized until launched against a target, Varex may be unable to anticipate these techniques or to implement adequate preventative measures, which could result in data leaks or otherwise compromise our confidential or proprietary information and disrupt our operations. If Varex does not allocate and effectively manage the resources necessary to build and sustain the proper technology infrastructure, Varex could be subject to, among other things, transaction errors, processing inefficiencies, the loss of customers,



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business disruptions, or the loss of or damage to intellectual property through a security breach or misappropriation of intellectual property. Such security breaches could expose Varex to a risk of loss of information, litigation, and possible liability to employees, customers, and/or regulatory authorities. If Varex's data management systems do not effectively collect, secure, store, process, and report relevant data for the operation of its business, whether due to equipment malfunction or constraints, software deficiencies, or human error, Varex's ability to effectively plan, forecast, and execute its business plan and comply with applicable laws and regulations will be impaired, perhaps materially. Any such impairment could materially and adversely affect Varex's financial condition, results of operations, cash flows, and the timeliness with which Varex reports its operating results internally and externally.

Varex uses certain cloud-based software. A security breach, whether of Varex's products, of Varex's customers' network security and systems, or of third-party hosting services could disrupt access to Varex's customers' stored information and could lead to the loss of, damage to or public disclosure of Varex's customers' stored information, including patient health information. Such an event could have serious negative consequences, including possible patient injury, regulatory action, fines, penalties and damages, reduced demand for Varex's solutions, an unwillingness of its customers to use its solutions, harm to its reputation and brand, and time-consuming and expensive litigation, any of which could have a material and adverse effect on Varex's financial results.

### ***Unfavorable results of legal proceedings could materially and adversely affect Varex's financial results.***

From time to time, Varex is a party to or otherwise involved in legal proceedings, claims, government inspections, audits or investigations, and other legal matters, both inside and outside the United States, arising in the ordinary course of its business or otherwise. Legal proceedings are often lengthy, taking place over a period of years with interim motions or judgments subject to multiple levels of review (such as appeals or rehearings) before the outcome is final. Litigation and other legal proceedings, claims, government inspections, audits and investigations are subject to significant uncertainty and may be expensive, time consuming, and disruptive to Varex's operations. For these and other reasons, Varex may choose to settle legal proceedings and claims, regardless of their actual merit.

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

### ***Varex's business may suffer if it is not able to hire and retain qualified personnel.***

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

### ***Changes in interpretation or application of generally accepted accounting principles may materially and adversely affect Varex's operating results.***

Varex prepares its financial statements in accordance with GAAP. These principles are subject to interpretation by the FASB, American Institute of Certified Public Accountants, the SEC, and various other regulatory and/or accounting bodies. A change in interpretations of, or its application of, these principles can have a significant effect on Varex's reported results and may even affect its reporting of transactions completed before a change is announced. In addition, when Varex is required to adopt new accounting standards, Varex's methods of accounting for certain items may change, which could cause its results of operations to fluctuate from period to period and make it more difficult to compare its financial results to prior periods.

As its operations evolve over time, Varex may introduce new products and/or new technologies that require Varex to apply different accounting principles, including ones regarding revenue recognition, than Varex has applied in past periods. The application of different types of accounting principles and related potential changes may make it more difficult to compare its financial results from quarter to quarter, and the trading price of Varex common stock could suffer or become more volatile as a result.



***Environmental laws impose compliance costs on Varex's business and may also result in liability.***

Varex is subject to environmental laws around the world. These laws regulate many aspects of its operations, including its handling, storage, transport, and disposal of hazardous substances, such as the chemicals and materials that Varex uses in the course of its manufacturing operations. They can also impose cleanup liabilities, including with respect to discontinued operations. As a consequence, Varex can incur significant environmental costs and liabilities, some recurring and others not recurring. Although it follows procedures intended to comply with existing environmental laws, Varex, like other businesses, may mishandle or inadequately manage hazardous substances used in its manufacturing operations and can never completely eliminate the risk of contamination or injury from certain materials that it uses in its business and, therefore, it cannot completely eliminate the prospect of resulting claims and damage payments. Varex may also be assessed fines and/or other penalties for failure to comply with environmental laws and regulations. Insurance has provided coverage for portions of cleanup costs resulting from historical occurrences, but Varex does not expect to maintain insurance coverage for costs or claims that might result from any future contamination.

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

***Varex's operations are vulnerable to interruption or loss due to natural or other disasters, power loss, strikes, and other events beyond its control.***

Varex conducts some of its activities, including manufacturing, research and development, administration, and data processing at facilities located in areas that have in the past experienced or may in the future experience natural disasters. Varex's insurance coverage for such disasters may not be adequate or continue to be available at commercially-reasonable terms, or at all. A major disaster (such as a major fire, hurricane, earthquake, flood, tsunami, volcanic eruption or terrorist attack) affecting Varex's facilities, or those of its suppliers, could significantly disrupt its operations and delay or prevent product manufacture and shipment during the time required to repair, rebuild, or replace its or its suppliers' damaged manufacturing facilities. These delays could be lengthy and costly. If any of Varex's customers' facilities are adversely affected by a disaster, shipments of its products could be delayed. Additionally, customers may delay purchases of Varex's products until its operations return to normal. For example, following the earthquake and tsunami disasters in Japan in 2011, the operations of Canon Medical Systems, our largest customer, were impacted, and, as a consequence, orders to and product shipment from our business were delayed for several months. Even if Varex's suppliers or customers are able to quickly respond to a disaster, the ongoing effects of the disaster could create some uncertainty in the operations of its business. In addition, Varex's facilities may be subject to a shortage of available electrical power and other energy supplies. Any shortages may increase its costs for power and energy supplies or could result in blackouts, which could disrupt the operations of its affected facilities and harm its business. Further, Varex's products are typically shipped from a limited number of ports, and any disaster, strike, or other event blocking shipment from these ports could delay or prevent shipments and harm its business. In addition, concerns about terrorism, the effects of a terrorist attack, political turmoil, or an outbreak of epidemic diseases could have a negative effect on Varex's business operations, those of its suppliers and customers, and the ability to travel, resulting in adverse consequences on its revenues and financial performance.

***Certain provisions in Varex's Amended and Restated Certificate of Incorporation and Amended and Restated Bylaws, and of Delaware law, may prevent or delay an acquisition of Varex, which could decrease the trading price of Varex's common stock.***

Varex's Amended and Restated Certificate of Incorporation and Amended and Restated Bylaws contain, and Delaware law contains, provisions that are intended to deter coercive takeover practices and inadequate takeover bids by making such practices or bids unacceptably expensive to the bidder and to encourage prospective acquirers to negotiate with Varex's board of directors rather than to attempt a hostile takeover. These provisions include, among others:

- the inability of Varex's stockholders to call a special meeting;
- the inability of Varex's stockholders to act without a meeting of stockholders;
- rules regarding how stockholders may present proposals or nominate directors for election at stockholder meetings;
- the right of Varex's board of directors to issue preferred stock without stockholder approval;

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- the division of Varex's board of directors into three classes of directors, with each class serving a staggered three-year term, and this classified board provision could have the effect of making the replacement of incumbent directors more time-consuming and difficult, until the 2022 annual meeting of stockholders, after which directors will be elected annually;
- a provision that stockholders may only remove directors with cause while the board is classified;
- the ability of Varex's directors, and not stockholders, to fill vacancies on Varex's board of directors; and,
- the requirement that the affirmative vote of stockholders holding at least 66 2/3% of Varex's voting stock is required to amend certain provisions in Varex's Amended and Restated Certificate of Incorporation (relating to the term and removal of its directors, the filling of its board vacancies, the calling of special meetings of stockholders, stockholder action by written consent, the elimination of liability of directors to the extent permitted by Delaware law and indemnification of directors and officers), although this requirement will expire on the completion of the 2021 annual meeting of stockholders, after which Varex's Amended and Restated Certificate of Incorporation may be amended by the affirmative vote of the holders of at least a majority of the outstanding voting stock.

In addition, because Varex did not elect to be exempt from Section 203 of the Delaware General Corporation Law (the "DGCL"), this provision could also delay or prevent a change of control that stockholders may favor. Section 203 provides that, subject to limited exceptions, persons that acquire, or who are affiliated with a person that acquires, more than 15% of the outstanding voting stock of a Delaware corporation (an "interested stockholder") shall not engage in any business combination with that corporation, including by merger, consolidation, or acquisitions of additional shares, for a three-year period following the date on which the person became an interested stockholder, unless: (1) prior to such time, the board of directors of such corporation approved either the business combination or the transaction that resulted in the stockholder becoming an interested stockholder; (2) upon consummation of the transaction that resulted in the stockholder becoming an interested stockholder, the interested stockholder owned at least 85% of the voting stock of such corporation at the time the transaction commenced; or (3) on or subsequent to such time the business combination is approved by the board of directors of such corporation and authorized at a meeting of stockholders by the affirmative vote of at least two-thirds of the outstanding voting stock of such corporation not owned by the interested stockholder.

Varex believes these provisions will protect its stockholders from coercive or otherwise unfair takeover tactics by requiring potential acquirers to negotiate with Varex's board of directors and by providing Varex's board of directors with more time to assess any acquisition proposal. These provisions are not intended to make Varex immune from takeovers. However, these provisions will apply even if the offer may be considered beneficial by some stockholders and could delay or prevent an acquisition that Varex's board of directors determines is not in the best interests of Varex and Varex's stockholders. These provisions may also prevent or discourage attempts to remove and replace incumbent directors.

### ***Potential indemnification liabilities to Varian could materially and adversely affect Varex's business, financial condition, results of operations, and cash flows.***

Varex entered into a Separation and Distribution Agreement when it spun off from Varian. The agreement provides for, among other things, indemnification obligations designed to make Varex financially responsible for any Varex liabilities; the failure of Varex to pay, perform, or otherwise promptly discharge any Varex liabilities or contracts in accordance with their respective terms; any guarantee, indemnification obligation, surety bond or other credit support agreement, arrangement, commitment, or understanding by Varian for the benefit of Varex, unless related to Varian liabilities; any breach by Varex of the Separation and Distribution Agreement or any of the ancillary agreements; any action by Varex in contravention of its Amended and Restated Certificate of Incorporation or Amended and Restated Bylaws; and, any untrue statement or alleged untrue statement of a material fact or omission or alleged omission to state a material fact required to be stated therein or necessary to make the statements therein not misleading, with respect to all information contained in the Registration Statement on Form 10 (as amended or supplemented) or any other disclosure document that describes the separation, the distribution, Varex and its subsidiaries, or the transactions contemplated by the Separation and Distribution Agreement, subject to certain exceptions. If Varex is required to indemnify Varian under the circumstances set forth in the Separation and Distribution Agreement, Varex may be subject to substantial liabilities.

### ***In connection with Varex's spin-off from Varian, Varian has agreed to indemnify Varex for certain liabilities. However, there can be no assurance that the indemnity will be sufficient to insure Varex against the full amount of such liabilities or that Varian's ability to satisfy its indemnification obligation will not be impaired in the future.***

Pursuant to the Separation and Distribution Agreement and certain other agreements with Varian, Varian agreed to indemnify Varex for certain liabilities. However, third parties could also seek to hold Varex responsible for any of the liabilities that Varian retained, and there can be no assurance that the indemnity from Varian will be sufficient to protect Varex against the full amount of such liabilities or that Varian will be able to fully satisfy its indemnification obligations. In addition, Varian's insurers may attempt to deny coverage to Varex for liabilities associated with certain occurrences of indemnified liabilities prior to the separation. Moreover,



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even if Varex ultimately succeeds in recovering from Varian or such insurance providers any amounts for which Varex is held liable, Varex may be temporarily required to bear these losses. Each of these risks could negatively affect Varex's business, financial position, results of operations, and/or cash flows.

***Potential liabilities may arise due to fraudulent transfer considerations, which could materially and adversely affect Varex's financial condition and its results of operations.***

In connection with the spin-off, Varian completed several corporate restructuring transactions, which, along with the separation and distribution, may be subject to federal and state fraudulent conveyance and transfer laws. If, under these laws, a court were to determine that, at the time of the separation and distribution, any entity involved in these restructuring transactions or the separation and distribution:

- was insolvent;
- was rendered insolvent by reason of the separation and distribution;
- had remaining assets constituting unreasonably small capital; or,
- intended to incur, or believed it would incur, debts beyond its ability to pay these debts as they matured,

then the court could void the separation and distribution, in whole or in part, as a fraudulent conveyance or transfer. The court could then require Varex's stockholders to return to Varian some or all of the shares of Varex common stock issued in the distribution or require Varian or Varex, as the case may be, to fund liabilities of the other company for the benefit of creditors. The measure of insolvency will vary depending upon the jurisdiction whose law is being applied. Generally, however, an entity would be considered insolvent if the fair value of its assets was less than the amount of its liabilities or if it incurred debt beyond its ability to repay the debt as it matures.

### **Item 1B. Unresolved Staff Comments**

None.

### **Item 2. Properties**

Our business is primarily located in Salt Lake City, Utah, where we own approximately 37 acres of land and approximately 494,000 square feet of space used for manufacturing, administrative functions and research and development, for both our Medical and Industrial segments. We also own or lease 34 other facilities throughout North America, Europe and Asia (located in 8 states and 17 foreign countries) that comprise over 2 million square feet of manufacturing facilities, warehouses, sales and service, research and development and office space, which are used for our Medical and/or Industrial segments, depending on the location.

In addition to our location in Salt Lake City, Utah, our other primary owned facilities are located in Las Vegas, Nevada and Franklin Park, Illinois. Our Las Vegas, Nevada, facility has approximately 5 acres of land and 94,000 square feet of space used for manufacturing, administrative functions and research and development, for our Industrial segments. Our Franklin Park, Illinois, facility has approximately 3 acres of land and approximately 61,000 square feet of space used for manufacturing, administrative functions and research and development, for both our Medical and Industrial segments.

Primary leased facilities include approximately 144,000 square feet in Laguna, Philippines, approximately 73,000 square feet in Santa Clara, California, approximately 46,000 square feet in Wuxi, China, approximately 47,000 square feet in Dinxperlo, the Netherlands, approximately 34,000 square feet in Bremen, Germany and approximately 34,000 of square feet in Walluf, Germany, all of which are used for manufacturing and administrative functions for our Medical and Industrial segments.

### **Item 3. Legal Proceedings**

From time to time, we are involved in legal proceedings arising in the ordinary course of business or otherwise. We do not believe that any material liability will be imposed as a result of these matters. If actual liabilities significantly exceed the estimates made, our combined financial position, results of operations, comprehensive earnings or cash flows could be materially and adversely affected. Legal expenses relating to legal matters are expensed as incurred. See "Risk Factors- Unfavorable results of legal proceedings could materially and adversely affect Varex's financial results."

**Item 4. Mine Safety Disclosures**

Not applicable.

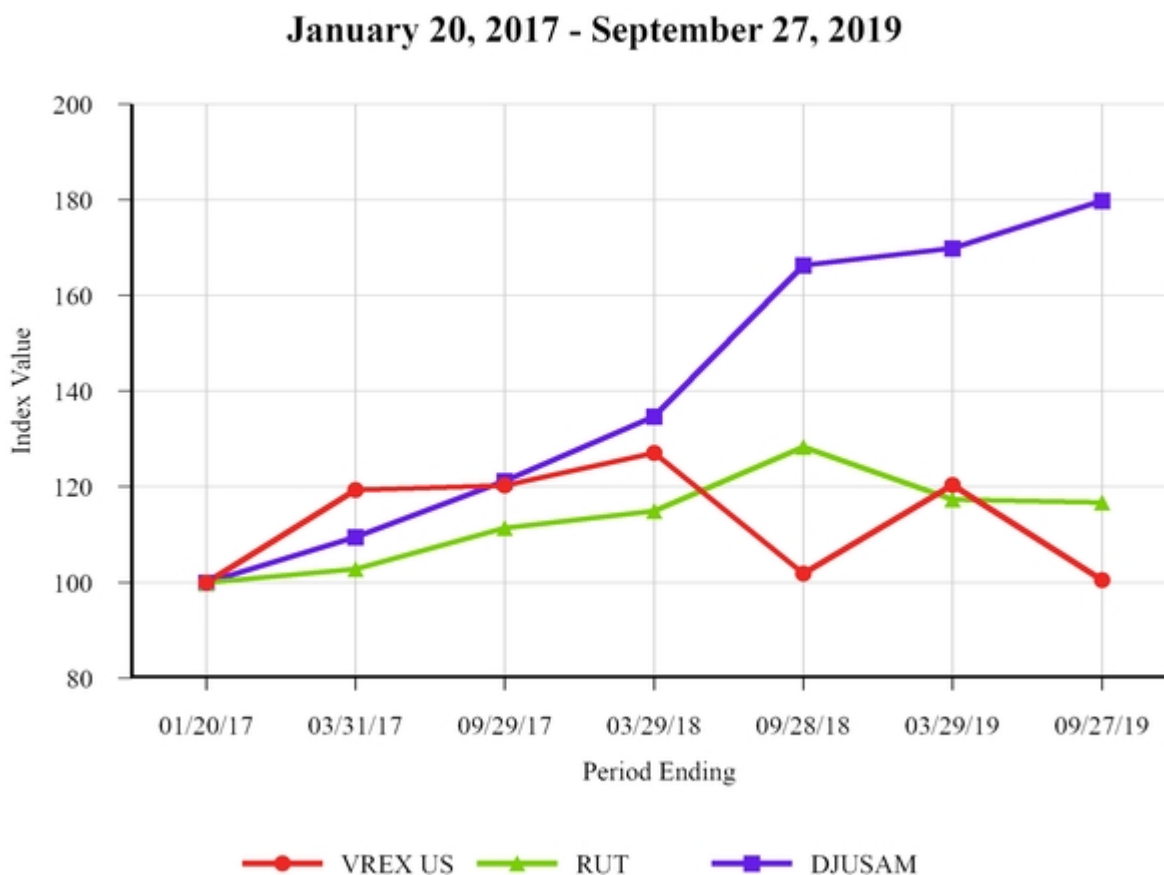
## PART II

### Item 5. Market for the Registrant's Common Equity, Related Stockholder Matters and Issuer Purchases of Equity Securities

Varex's common stock is traded on the NASDAQ Global Select Market (the "NASDAQ") under the symbol "VREX."

Since our inception, we have not paid any cash dividends and have no current plan to pay cash dividends on Varex common stock. As of November 18, 2019, there were 1,662 holders of record of Varex common stock.

This graph shows the total return on VREX common stock since listing on NASDAQ on January 20, 2017, with comparative total returns for the Russell 2000 Index ("RUT") and the Dow Jones Medical Equipment Index ("DJUSAM"). The graph below assumes that \$100.00 was invested on January 20, 2017 in our common stock and the companies listed in the RUT and the DJUSAM, as well as a reinvestment of dividends paid on such investments throughout the period.



### Item 6. Selected Financial Data

In January 2017, we separated from Varian. Prior to the date of separation, the financial statements were prepared on a stand-alone basis and derived from Varian's consolidated financial statements as we operated as part of Varian.

The following data, in so far as it relates to each of the fiscal years from 2015 through 2019, has been derived from annual consolidated financial statements, including the consolidated balance sheets at September 27, 2019 and September 28, 2018 and the related consolidated statements of earnings, of comprehensive earnings, and of cash flows for the fiscal years 2019, 2018 and 2017 and

notes thereto appearing elsewhere herein. In addition, the following financial data should be read in conjunction with our consolidated financial statements and the accompanying notes and the MD&A included elsewhere herein.

**Summary of Operations:**
**(In millions, except per share amounts)**

	Fiscal Years				
	2019	2018	2017 <sup>(1)</sup>	2016	2015
Revenues	\$ 780.6	\$ 773.4	\$ 698.1	\$ 620.1	\$ 632.3
Gross margin	\$ 256.7	\$ 253.9	\$ 253.5	\$ 248.4	\$ 250.6
Earnings before taxes	21.5	25.7	74.8	105.0	127.6
Taxes on earnings	5.7	(2.6)	22.8	36.0	46.8
Net earnings	15.8	28.3	52.0	69.0	80.8
Less: Net earnings attributable to noncontrolling interests	0.3	0.8	0.4	0.5	0.8
Net earnings attributable to Varex	\$ 15.5	\$ 27.5	\$ 51.6	\$ 68.5	\$ 80.0
Net earnings per share attributable to Varex					
Net earnings per share - basic	\$ 0.41	\$ 0.73	\$ 1.37	\$ 1.83	\$ 2.14
Net earnings per share - diluted	\$ 0.40	\$ 0.72	\$ 1.36	\$ 1.82	\$ 2.12
Financial Position at Fiscal Year End:					
Working capital	\$ 263.3	\$ 306.1	\$ 343.5	\$ 282.1	\$ 237.5
Total assets	1,038.9	987.9	1,040.1	622.4	583.6
Total debt (excluding current maturities, net of deferred costs)	364.4	364.8	464	—	—

(1) The summary of operations for fiscal year 2017 includes operating results from the Acquired Detector Business for the period from May 1, 2017 through September 29, 2017.

**Selected Quarterly Financial Data (Unaudited)**

The following table sets forth selected financial data from our unaudited quarterly consolidated statements of earnings for the eight quarters ended fiscal year 2019. The information for each quarter has been derived from unaudited financial statements and in the opinion of management, include all adjustments, consisting only of normal recurring adjustments, necessary for a fair statement of the results for the unaudited interim periods and includes certain reclassifications and rounding differences. The quarterly data should be read together with our consolidated financial statements and related notes appearing elsewhere in this annual report.

	Fiscal Year 2019 <sup>(1)</sup>				
	First Quarter	Second Quarter	Third Quarter	Fourth Quarter	Total Year
<b>(In millions, except per share amounts, unaudited)</b>					
Total revenues	\$ 185.7	\$ 195.8	\$ 196.7	\$ 202.4	\$ 780.6
Gross margin	\$ 60.0	\$ 64.4	\$ 60.7	\$ 71.6	\$ 256.7
Net earnings	\$ 3.0	\$ 5.9	\$ (1.3)	\$ 8.2	\$ 15.8
Net earnings attributable to Varex	\$ 3.0	\$ 5.8	\$ (1.4)	\$ 8.1	\$ 15.5
Net earnings per share - basic	\$ 0.08	\$ 0.15	\$ (0.04)	\$ 0.21	\$ 0.41
Net earnings per share - diluted	\$ 0.08	\$ 0.15	\$ (0.04)	\$ 0.21	\$ 0.40

(1) During fiscal year 2019, the Company identified errors that originated in prior periods and were corrected for as out of period adjustments in the quarters of fiscal year 2019. Management has determined that such errors and out of period adjustments, which primarily related to inventory accounting, revenue recognition and intercompany transactions, were not material to any of the unaudited interim financial statements. The impact of these errors and out of period adjustments on total revenues, gross margin, net earnings and net earnings per diluted share was as follows:

- Q1 2019 - \$(0.6) million, \$(1.1) million, \$0.4 million and \$0.01 per diluted share, respectively;
- Q2 2019 - \$0.1 million, \$0.0 million, \$(1.2) million and \$(0.03) per diluted share respectively;
- Q3 2019 - \$0.0 million, \$(0.9) million, \$(0.6) million and \$(0.02) per diluted share respectively;
- Q4 2019 - \$0.0 million, \$2.2 million, \$1.6 million and \$0.04 per diluted share, respectively.

	Fiscal Year 2018				
	First Quarter	Second Quarter	Third Quarter	Fourth Quarter	Total Year
(In millions, except per share amounts, unaudited)					
Total revenues	\$ 176.2	\$ 201.2	\$ 191.2	\$ 204.8	\$ 773.4
Gross margin	\$ 61.5	\$ 70.1	\$ 63.0	\$ 59.3	\$ 253.9
Net earnings	\$ 11.4	\$ 12.3	\$ 3.9	\$ 0.7	\$ 28.3
Net earnings attributable to Varex	\$ 11.3	\$ 12.2	\$ 3.8	\$ 0.2	\$ 27.5
Net earnings per share - basic	\$ 0.30	\$ 0.32	\$ 0.10	\$ 0.01	\$ 0.73
Net earnings per share - diluted	\$ 0.30	\$ 0.32	\$ 0.10	\$ 0.01	\$ 0.72

## **Item 7. Management’s Discussion and Analysis of Financial Condition and Results of Operations**

### **Basis of Presentation**

We became an independent publicly-traded company in January 2017 following our separation from Varian and subsequent distribution of shares of our common stock to Varian shareholders.

Prior to the spin-off, we operated as a division of Varian. Accordingly, for part of fiscal year 2017, certain shared costs have been allocated to us and are reflected as expenses in the accompanying financial statements. Management considers the allocation methodologies used to be reasonable and appropriate reflections of the related expenses attributable to us for purposes of the carve-out financial statements; however, the expenses reflected in these financial statements may not be indicative of the actual expenses that would have been incurred during the periods presented if we had operated as a separate stand-alone entity. The allocation methods include revenue, headcount, actual usage of services, and others. In addition, the expenses reflected in the financial statements may not be indicative of expenses that will be incurred by us in the future.

### **Our Business**

Varex Imaging Corporation is a leading innovator, designer and manufacturer of X-ray imaging components including X-ray tubes, digital detectors, linear accelerators and other image processing solutions, which are key components of X-ray imaging systems. Our components are used in medical imaging as well as in industrial and security imaging applications. Global original equipment manufacturers (“OEM”) incorporate our X-ray imaging components in their systems to detect, diagnose, protect and inspect. As of September 27, 2019, we had approximately 2,000 full-time equivalents employees, located at manufacturing and service center sites in North America, Europe, and Asia.

Our products are sold in three geographic regions: the Americas, EMEA, and APAC. The Americas includes North America (primarily the United States) and Latin America. EMEA includes Europe, Russia, the Middle East, India and Africa. APAC includes Asia and Australia. Revenues by region are based on the known final destination of products sold.

Our success depends, among other things, on our ability to anticipate and respond to changes in our markets, the direction of technological innovation and the demands of our customers. We continue to invest in research and development and employ over 500 engineers. Combining this focus on innovation and product performance with strong long-term customer relationships allows us to partner with our customers to bring industry-leading products to the X-ray imaging market. We continue to work to improve the life and quality of our imaging components and leverage our scale as the largest X-ray imaging component supplier to provide cost-effective solutions for our customers. Demand for our products can also be impacted by geo-political factors, including tariffs on key imported materials used in manufacturing our products and also on X-ray imaging products we sell to customers outside the United States. The escalation of trade conflicts between the United States and China has negatively impacted our business and are expected to continue.

### **Operating Segments and Products**

Our Chief Executive Officer, who is our Chief Operating Decision Maker (“CODM”), evaluates our product groupings and measures our business performance in two reportable operating segments: Medical and Industrial. The segments align our products and service offerings with customer use in medical and industrial markets and are consistent with how the CODM evaluates the business for the allocation of resources. The CODM allocates resources to and evaluates the financial performance of each operating segment primarily based on revenues and gross margin.

#### ***Medical***

In our Medical business segment, we design, manufacture, sell and service X-ray imaging components for use in a range of radiographic or fluoroscopic imaging applications including, computed tomography (“CT”), mammography, oncology, cardiac, surgery, dental, and computer-aided detection. We provide a broad range of X-ray imaging components for Medical customers, including X-ray tubes, digital detectors, high voltage connectors, image-processing software and workstations, computer-aided diagnostic software, collimators, automatic exposure control devices, generators, heat exchangers, ionization chambers and buckys.

A significant portion of our revenues come from the sales of high-end X-ray tubes used in CT imaging and high-end dynamic digital detectors used in fluoroscopic and 3D dental imaging applications. These upper-tier imaging components are characterized by increased levels of technological complexity, engineering and intellectual property that typically allow these products to have a higher sales price and gross margin.



The digital detector market continues to mature from initial product introductions that were made approximately 15 years ago. For the past few years, we have experienced price erosion for these products, predominantly in the highly-competitive market for radiographic detectors. We anticipate this trend will continue in the foreseeable future.

Our X-ray imaging components are primarily sold to OEM customers that incorporate our products into their X-ray imaging systems for a variety of medical modalities and industrial applications. To a much lesser extent, we also sell our X-ray imaging components to independent service companies, distributors and directly to end-users for replacement purposes.

In China, the government is broadening the availability of healthcare services throughout the country. As a result, the number of diagnostic X-ray imaging systems, including CT, has grown significantly. We are developing CT tubes and related subsystems for Chinese OEMs as they introduce new CT imaging systems in China. Over the long-term, we anticipate that China-based revenues will increase as a percentage of our revenues. For fiscal year 2019, revenues from X-ray imaging components shipped to China-based OEMs and distributors declined to approximately 8% of total company revenues from 10% in the prior year. This decrease reflects a tariff-related decline in sales of radiographic digital detectors in China as well as lower non-OEM aftermarket sales, which more than offset an increase in sales of CT tubes to OEM customers.

We have taken certain actions to help us mitigate the impact of the trade war between the United States and China. We have implemented changes to secure more non-China sources of supply of parts and materials used to manufacture our X-ray imaging products, and in September 2019, we received from the United States Trade Representative a temporary exclusion from Section 301 tariffs on certain parts and components imported from China into the United States. We continue to expand manufacturing capabilities at our facilities in China, Germany and the Philippines.

### ***Industrial***

In our Industrial business segment, we design, manufacture, sell and service X-ray imaging products for use a number of markets, including security applications, such as cargo screening at ports and borders and baggage screening at airports, as well as nondestructive testing and inspection applications used in a number of other markets. Our industrial products include Linatron® X-ray linear accelerators, X-ray tubes, digital detectors and high voltage connectors. In addition, we provide proprietary image-processing and detection software designed to work with these other Varex products to provide package solutions to our Industrial customers.

The security market primarily consists of airport security for carry-on baggage, checked baggage and palletized cargo, as well as cargo security for the screening of trucks, trains and cargo containers at ports and borders. The end customers for border protection systems are typically government agencies, many of which are in oil-based economies and war zones where there has been significant year over year variation in buying patterns.

The non-destructive testing market utilizes X-ray imaging to scan items for inspection of manufacturing defects and product integrity in a wide range of industries including the aerospace, automotive, oil and gas, food packaging, metal castings and 3D printing industries. We provide X-ray sources, digital detectors, high voltage connectors and image processing software to OEM customers, system integrators and manufacturers. In addition, new applications for X-ray sources are being developed, such as sterilization of food and its packaging.

### ***Fiscal Year***

Our fiscal year is the 52- or 53-week period ending on the Friday nearest September 30. Fiscal year 2019 was the 52-week period that ended September 27, 2019, fiscal year 2018 was the 52-week period that ended September 28, 2018, and fiscal year 2017 was the 52-week period ended September 29, 2017. Set forth below is a discussion of our results of operations for fiscal years 2019, 2018 and 2017.

## Discussion of Results of Operations for Fiscal Year 2019 and 2018

### Revenues, net

(In millions)	Fiscal Years		\$ Change	% Change
	2019	2018		
Medical	\$ 596.8	\$ 602.0	\$ (5.2)	(1)%
Industrial	183.8	171.4	12.4	7%
Total revenues, net	<u>\$ 780.6</u>	<u>\$ 773.4</u>	<u>\$ 7.2</u>	<u>1%</u>
<i>Medical as a percentage of total revenues</i>	76%	78%		
<i>Industrial as a percentage of total revenues</i>	24%	22%		

Medical revenues decreased \$5.2 million primarily due to decreased sales of radiographic digital detectors in China and non-OEM aftermarket X-ray tubes, partially offset by increased sales of digital detectors and X-ray tubes for oncology applications, OEM X-ray tubes for CT applications and the addition of revenues from the acquisition of Direct Conversion AB (publ) (“Direct Conversion”).

Industrial revenues increased \$12.4 million due to increased sales of X-ray tubes for airport security, digital detectors for inspection applications and the addition of revenues with the acquisition of Direct Conversion.

### Revenues by Region

(In millions)	Fiscal Years		\$ Change	% Change
	2019	2018		
Americas	\$ 282.6	\$ 275.8	\$ 6.8	2 %
EMEA	269.0	254.5	14.5	6 %
APAC	229.0	243.1	(14.1)	(6)%
Total revenues, net	<u>\$ 780.6</u>	<u>\$ 773.4</u>	<u>\$ 7.2</u>	<u>1 %</u>
<i>Americas as a percentage of total revenues</i>	36%	36%		
<i>EMEA as a percentage of total revenues</i>	34%	33%		
<i>APAC as a percentage of total revenues</i>	29%	31%		

The Americas revenues increased \$6.8 million primarily due to increased sales of X-ray tubes partially offset by lower sales of digital detectors and computer-aided detection software. EMEA revenues increased \$14.5 million primarily due to increased sales of digital detectors, the addition of revenues from the acquisition of Direct Conversion in April of 2019 and higher sales of high voltage cables partially offset by lower sales of X-ray tubes. APAC revenues decreased \$14.1 million primarily due to decreased sales of radiographic digital detectors in China partially offset by the addition of revenues with the acquisition of Direct Conversion.

### Gross Margin

(In millions)	Fiscal Years		\$ Change	% Change
	2019	2018		
Medical	\$ 188.9	\$ 190.5	\$ (1.6)	(1)%
Industrial	67.8	63.4	4.4	7 %
Total gross margin	<u>\$ 256.7</u>	<u>\$ 253.9</u>	<u>\$ 2.8</u>	<u>1 %</u>
<i>Medical gross margin %</i>	31.7%	31.6%		
<i>Industrial gross margin %</i>	36.9%	37.0%		
<i>Total gross margin %</i>	32.9%	32.8%		

Gross margin percentage increased for fiscal year 2019 compared to 2018. The gross margin for fiscal year 2019 included \$9.4 million of restructuring charges and purchase price accounting adjustments and the gross margin for fiscal year 2018 included



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\$7.3 million of restructuring charges. The industrial gross margin percentage decreased primarily due to higher manufacturing costs and unfavorable product mix.

### **Operating Expenses**

(In millions)	Fiscal Years		\$ Change	% Change
	2019	2018		
Research and development	\$ 78.1	\$ 83.0	\$ (4.9)	(6)%
<i>As a percentage of total revenues</i>	<i>10.0%</i>	<i>10.7%</i>		
Selling, general and administrative	\$ 128.1	\$ 123.4	\$ 4.7	4 %
<i>As a percentage of total revenues</i>	<i>16.4%</i>	<i>16.0%</i>		
Impairment of intangible assets	\$ 4.8	\$ 3.0	\$ 1.8	60 %
<i>As a percentage of total revenues</i>	<i>0.6%</i>	<i>0.4%</i>		
Operating expenses	\$ 211.0	\$ 209.4	\$ 1.6	1 %
<i>As a percentage of total revenues</i>	<i>27.0%</i>	<i>27.1%</i>		

### **Research and Development**

Research and development costs for fiscal year 2019 decreased to 10% of revenues due to lower personnel costs and prototype material costs. We are committed to investing in the business to support long-term growth and believe long-term research and development expenses of approximately 8% to 10% of annual revenues is the appropriate range that will allow us to innovate and bring new products to market for our global OEM customers.

### **Selling, General and Administrative**

Selling, general and administrative expenses as a percentage of total revenues increased to 16.4% for fiscal year 2019 from 16.0% for fiscal year 2018 due to higher audit and consulting fees associated with the remediation of internal control deficiencies and increased legal fees for patent litigation. These were offset by reductions in personnel costs and other consulting fees.

### **Impairment of intangible assets**

Impairment of intangible assets increased for fiscal year 2019 to \$4.8 million as compared to \$3.0 million for fiscal year 2018. In connection with the July 2019 announcement of the Santa Clara facility shut down we made the decision to discontinue further efforts on certain in-process research and development intangible assets. As a result, we recorded a corresponding impairment charge of \$4.8 million in fiscal year 2019. See Note 4. *Restructuring* included in the notes to our consolidated financial statements for further information.

### **Interest and Other Income (Expense), Net**

The following table summarizes our interest and other income (expense), net:

(In millions)	Fiscal Years		\$ Change
	2019	2018	
Interest income	\$ 0.1	\$ 0.2	\$ (0.1)
Interest expense	(21.1)	(21.7)	0.6
Other income (expense), net	(3.2)	2.7	(5.9)
Interest and other expenses, net	\$ (24.2)	\$ (18.8)	\$ (5.4)

Interest and other expense, net increased in fiscal year 2019 compared to fiscal year 2018, primarily due to a other expense from equity method investments compared to other income from equity method investments in the prior fiscal year. A new joint venture investment was established in fiscal year 2019.

### **Taxes on Earnings**

	Fiscal Years	
	2019	2018
Effective tax rate	26.5%	(10.1)%



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We had an income tax expense of \$5.7 million and an income tax benefit of \$2.6 million, for effective rates of 26.5% and (10.1)%, for fiscal years 2019 and 2018, respectively.

On December 22, 2017, the Tax Cuts and Jobs Act of 2017 (U.S. Tax Reform) was enacted in the U.S. which significantly revised the U.S. corporate income tax structure. Among the revisions impacting our effective tax rate are a lower U.S. corporate statutory rate going from 35% to 21% effective January 1, 2018 and changes to the way foreign earnings are taxed. As a September fiscal year filer, the lower corporate income tax rate was phased in with a U.S. statutory federal rate of 24.5% in fiscal year ended September 28, 2018, and a rate of 21% for the fiscal year ended September 27, 2019.

During fiscal year 2019, our effective tax rate varied from the U.S. federal statutory rate of 21.0% primarily because of the favorable impact of changes to the U.S. corporate tax structure resulting from U.S. Tax Reform, U.S. research and development tax credits, and tax windfalls for share-based compensation. These favorable U.S. tax items are offset by increases resulting from losses in certain foreign jurisdictions for which no benefit is recognized and earnings in other foreign jurisdictions that are taxed at higher rates.

During fiscal year 2018, our effective tax rate varied from the U.S. federal statutory rate primarily because of the favorable impact of changes to the U.S. corporate tax structure resulting from U.S. Tax Reform. The effective tax rate also differs from the U.S. federal statutory rate due to increases resulting from U.S. state income tax expense, losses in certain foreign jurisdictions for which no benefit is recognized, earnings in other foreign jurisdictions that are taxed at higher rates, and limitations on the deductibility of officers' compensation. These are offset by decreases due to U.S. research and development credits, tax windfalls for share-based compensation, and the release of a valuation allowance against loss carryforwards in certain foreign jurisdictions.

The SEC issued guidance under Staff Accounting Bulletin No. 118, Income Tax Accounting Implications of the Tax Cuts and Jobs Act ("SAB 118") that allows for reasonable estimated amounts to be recorded and a measurement period of up to one year from the date of enactment to revise these provisional amounts as new information is obtained and additional guidance is issued. During the three months ended December 28, 2018, the Company completed its analysis of U.S. Tax Reform, and the accounting for the income tax effects has been finalized for the measurement period under SAB 118, with no significant adjustments from the provisional amounts. During fiscal year 2019, additional U.S. Tax Reform provisions, including GILTI (global intangible low-taxed income), BEAT (base-erosion anti-abuse tax), FDII (foreign-derived intangible income), limitations on interest expense deductions (if certain conditions apply), and other components became effective for us and, if applicable, have been included in the calculation of our fiscal year 2019 tax provision. The determination of the tax effects of U.S. Tax Reform may change following future legislation or further interpretation of U.S. Tax Reform from various U.S. Federal and state tax authorities.

The guidance for accounting for U.S. Tax Reform requires taxpayers to make an election regarding the accounting for GILTI. This policy election is to either: (1) treat GILTI as a period cost if and when incurred, or (2) recognize deferred taxes for basis differences that are expected to reverse as GILTI in future years. During fiscal year 2019, we made the accounting policy election to account for GILTI under the period cost method.

## Discussion of Results of Operations for Fiscal Year 2018 and 2017

### *Revenues, net*

(In millions)	Fiscal Years		\$ Change	% Change
	2018	2017		
Medical	\$ 602.0	\$ 556.9	\$ 45.1	8%
Industrial	171.4	141.2	30.2	21%
Total revenues, net	<u>\$ 773.4</u>	<u>\$ 698.1</u>	<u>\$ 75.3</u>	11%
<i>Medical as a percentage of total revenues</i>	78%	80%		
<i>Industrial as a percentage of total revenues</i>	22%	20%		

Medical revenues increased \$45.1 million primarily due to an increase in sales of high-end radiographic digital detectors with the addition of revenues from the acquisition of the medical imaging business ("Acquired Detector Business") of PerkinElmer, Inc., and from increased sales of X-ray tubes, including CT tubes to our OEM customers in China, and high voltage cables. These increases in medical revenues were partially offset by a decrease in sales of 3-D dental digital detectors and low-end radiographic.

Industrial revenues increased \$30.2 million due to increased sales of digital detectors from the addition of the Acquired Detector Business, and from increased sales of high-voltage industrial cables. These increases were partially offset by a decrease of industrial digital detectors.



## Revenues by Region

(In millions)	Fiscal Years		\$ Change	% Change
	2018	2017		
Americas	\$ 275.8	\$ 239.8	\$ 36.0	15%
EMEA	254.5	219.5	35.0	16%
APAC	243.1	238.8	4.3	2%
Total revenues, net	\$ 773.4	\$ 698.1	\$ 75.3	11%
<i>Americas as a percentage of total revenues</i>	<i>36%</i>	<i>34%</i>		
<i>EMEA as a percentage of total revenues</i>	<i>33%</i>	<i>31%</i>		
<i>APAC as a percentage of total revenues</i>	<i>31%</i>	<i>34%</i>		

The Americas revenues increased \$36.0 million primarily due to increased sales of digital detectors from the addition of the Acquired Detector Business. EMEA revenues increased \$35.0 million primarily due to increased sales of digital detectors from the addition of the Acquired Detector Business partially offset by lower sales of security and inspection products and digital detectors. APAC revenues increased \$4.3 million due to increased sales of digital detectors from the addition of the Acquired Detector Business and higher sales of X-ray tubes, partially offset by lower sales of digital detectors.

## Gross Margin

(In millions)	Fiscal Years		\$ Change	% Change
	2018	2017		
Medical	\$ 190.5	\$ 193.6	\$ (3.1)	(2)%
Industrial	63.4	59.9	3.5	6 %
Total gross margin	\$ 253.9	\$ 253.5	\$ 0.4	— %
<i>Medical gross margin %</i>	<i>31.6%</i>	<i>34.8%</i>		
<i>Industrial gross margin %</i>	<i>37.0%</i>	<i>42.4%</i>		
<i>Total gross margin %</i>	<i>32.8%</i>	<i>36.3%</i>		

The decrease in total gross margin percentage was due primarily to a product mix shift to lower margin products, restructuring charges of \$7.3 million, including inventory markdowns of \$3.1 million, higher digital detector product and indirect costs in our Santa Clara facility and the impact of tariffs in the fourth quarter. The decrease in medical gross margin percentage were primarily due to product mix shifts towards lower margin X-ray tubes and higher digital detector unit products costs in our Santa Clara facility. The decrease in industrial gross margin percentage were primarily due to product mix shifts towards lower margin cargo scanning products and price erosion in this same product category.

## Operating Expenses

(In millions)	Fiscal Years		\$ Change	% Change
	2018	2017		
Research and development	\$ 83.0	\$ 67.3	\$ 15.7	23%
<i>As a percentage of total revenues</i>	<i>10.7%</i>	<i>9.6%</i>		
Selling, general and administrative <sup>(1)</sup>	\$ 123.4	\$ 102.5	\$ 20.9	20%
<i>As a percentage of total revenues</i>	<i>16.0%</i>	<i>14.7%</i>		
Impairment of intangible assets	\$ 3.0	\$ —	\$ 3.0	n/a
<i>As a percentage of total revenues</i>	<i>0.4%</i>	<i>—</i>		
Operating expenses	\$ 209.4	\$ 169.8	\$ 39.6	23%
<i>As a percentage of total revenues</i>	<i>27.1%</i>	<i>24.3%</i>		

(1) Selling, general and administrative expenses include \$12.4 million of corporate costs allocated to us by Varian in fiscal year 2017.

### Research and Development

The increase in research and development expenses as a percentage of revenue was due to the continued acceleration and development of digital detector projects and prototype materials costs for CT X-ray tubes.

### Selling, General and Administrative

Selling, general and administrative expenses as a percentage of total revenues increased primarily as a result of restructuring and impairment charges related to the Acquired Detector Business, increased amortization of intangible assets, increased share-based compensation expense and an increase in costs related to implementation of certain productivity initiatives.

### Impairment of intangible assets

Impairment of intangible assets for fiscal year 2018 were \$3.0 million, while there was no impairment of intangible assets for fiscal year 2017. In connection with the restructuring plan that was announced in July 2018 we recorded an impairment charge of \$3.0 million related to certain intangible assets. See Note 4. *Restructuring* included in the notes to our consolidated financial statements for further information.

### Interest and Other Income (Expense), Net

The following table summarizes our interest and other income (expense), net:

(In millions)	Fiscal Years		\$ Change
	2018	2017	
Interest income	\$ 0.2	\$ 0.2	\$ —
Interest expense	(21.7)	(12.3)	(9.4)
Other income (expense), net	2.7	3.2	(0.5)
Interest and other expenses, net	<u>\$ (18.8)</u>	<u>\$ (8.9)</u>	<u>\$ (9.9)</u>

The increase in interest and other income (expense), net was primarily due to higher interest expense as a result of higher weighted average interest rates and higher weighted average outstanding borrowings under our credit agreement and foreign currency translation losses, partially offset by income from equity method investments.

### Taxes on Earnings

	Fiscal Years	
	2018	2017
Effective tax rate	(10.1)%	30.5%

We had an income tax benefit of \$2.6 million and an income tax expense of \$22.8 million for the year ended September 28, 2018 and September 29, 2017, respectively, for effective rates of (10.1)% and 30.5%, respectively.

On December 22, 2017, the Tax Cuts and Jobs Act of 2017 (“U.S. Tax Reform”) was enacted in the U.S. which significantly revised the U.S. corporate income tax structure. Among the revisions impacting our effective tax rate are a lower U.S. corporate statutory rate going from 35% to 21% effective January 1, 2018 and changes to the way foreign earnings are taxed. As a September fiscal year filer, the lower corporate income tax rate has been phased in resulting in a U.S. statutory federal rate of 24.5% for the fiscal year ended September 28, 2018.

During fiscal year 2018, our effective tax rate varied from the U.S. federal statutory rate of 24.5% primarily because of the favorable impact of changes to the U.S. corporate tax structure resulting from U.S. Tax Reform. The effective tax rate also differs from the U.S. federal statutory rate due to increases resulting from U.S. state income tax expense, losses in certain foreign jurisdictions for which no benefit is recognized, earnings in other foreign jurisdictions that are taxed at higher rates, and limitations on the deductibility of officers' compensation. These are offset by decreases due to U.S. research and development credits, tax windfalls for share-based compensation, and the release of a valuation allowance against loss carryforwards in certain foreign jurisdictions.

During fiscal year 2017, our effective tax rate varied from the U.S. federal statutory rate of 35% primarily because of a difference in the mix of earnings by jurisdiction, and overall global tax structure for Varex as a stand-alone company compared to the prior year when it was part of Varian. It was also impacted by the benefit of adjustments to certain deferred tax assets and the release of valuation allowances in jurisdictions where increased earnings allowed for the utilization of net operating loss carryforwards.

During fiscal year 2018, as a result of U.S. Tax Reform, we recorded income tax expense of \$3.7 million for the tax on the deemed repatriation of deferred foreign earnings offset by a tax benefit of \$10.9 million due to the revaluation of net deferred taxes.

## Liquidity and Capital Resources

We assess our liquidity in terms of our ability to generate cash to fund our operating, including working capital and investing activities. We continue to generate sufficient cash from operating activities and believe that our operating cash flow, availability under our existing credit facility, current working capital and other sources of liquidity will be sufficient to allow us to continue to invest in our existing businesses, consummate strategic acquisitions and manage our capital structure on a short and long-term basis. Availability under our credit facility was \$91.0 million as of September 27, 2019, although on October 8, 2019, we permanently reduced the revolving credit commitment under the credit facility by \$25.0 million to \$125.0 million. Although we believe that our future cash from operations, together with our access to banking and capital markets, will provide adequate resources to fund our operating and financing needs, our access to, and the availability of, financing on acceptable terms in the future will be affected by many factors, including: (i) the liquidity of the overall capital markets and (ii) the current state of the economy. There can be no assurances that we will continue to have access to these markets on terms acceptable to us. See “Risk Factors” for a further discussion. Subsequent to fiscal year 2019 we did not comply with the covenant under the Credit Agreement to timely deliver our fiscal year 2019 annual financial statements. However, upon the filing of this Annual Report with the SEC, we will be able to deliver the fiscal year 2019 annual financial statements within the 30-day cure period set forth in the Credit Agreement and consequently no event of default will occur. At September 27, 2019 we had \$364.4 million in long-term debt and \$30.7 million of current maturities of long-term debt, net of deferred issuance costs of \$5.7 million. See Note 8. *Borrowings* in the notes to our consolidated financial statements for more information regarding our existing credit facility.

### Cash and Cash Equivalents

The following table summarizes our cash and cash equivalents:

(In millions)	September 27, 2019	September 28, 2018	\$ Change	% Change
Cash and cash equivalents	\$ 29.9	\$ 51.9	\$ (22.0)	(42.4)%

### Borrowings

The following table summarizes the changes in our debt outstanding:

(In millions)	September 27, 2019	September 28, 2018	\$ Change	% Change
Current portion of Term Facility	\$ 29.4	\$ 25.0	\$ 4.4	17.6 %
Current portion of other long-term debt	1.3	—	1.3	n/a
Revolving Credit Facility	59.0	28.0	31.0	110.7 %
Long-Term portion of Term Facility	308.6	345.0	(36.4)	(10.6)%
Long-term portion of other debt	2.5	—	2.5	n/a
Total debt outstanding, gross	400.8	398.0	2.8	0.7 %
Debt issuance costs	(5.7)	(8.2)	2.5	(30.5)%
Total debt outstanding, net	\$ 395.1	\$ 389.8	\$ 5.3	1.4 %

## Cash Flows

(In millions)	Fiscal Years		
	2019	2018	2017
Net cash flow provided by (used in):			
Operating activities	\$ 71.9	\$ 85.3	\$ 75.2
Investing activities	(93.2)	(25.2)	(292.0)
Financing activities	(0.1)	(90.4)	263.3
Effects of exchange rate changes on cash and cash equivalents	(0.7)	(0.5)	0.9
Net increase (decrease) in cash and cash equivalents	\$ (22.1)	\$ (30.8)	\$ 47.4

*Net Cash Provided by Operating Activities.* Cash from operating activities consists primarily of net earnings adjusted for certain non-cash items, including share-based compensation, depreciation, amortization and impairment of intangible assets, inventory write-downs deferred income taxes, amortization of deferred loan costs, income and loss from equity investments and the effect of changes in operating assets and liabilities.

For fiscal year 2019, compared to fiscal year 2018, net cash provided by operating activities were as follows:

- Net earnings were \$15.8 million compared to \$28.3 million,
- Non-cash adjustments to net earnings of \$51.4 million compared to \$51.0 million,
- Operating assets and liabilities activity:
  - Accounts receivable decreased by \$14.8 million compared to \$9.0 million,
  - Inventories increased by \$11.1 million compared to \$2.4 million,
  - Prepaid expenses and other assets decreased \$4.3 million compared to \$2.0 million,
  - Accounts payable decreased by \$9.0 million compared to an increase of \$5.2 million,
  - Accrued liabilities and other long-term operating liabilities increased by \$10.9 million compared to a decrease of \$10.2 million, and
  - Deferred revenues decreased by \$5.2 million compared to an increase of \$2.4 million.

For fiscal year 2017, net cash provided by operating activities was \$75.2 million and consisted of net earnings of \$52.0 million, increases from non-cash items of \$29.2 million and decreases from operating assets and liabilities activities of \$6.0 million.

*Net cash used in investing activities.* Cash used in investing activities was \$93.2 million, \$25.2 million, and \$292.0 million for the fiscal years 2019, 2018 and 2017, respectively. Net cash used in investing activities for fiscal year 2019 related primarily to the April 2019, acquisition of 98.2% of the outstanding shares of common stock of Direct Conversion for \$69.5 million in cash, net of cash acquired, and capital expenditures for property plant and equipment of \$19.8 million. Net cash used in investing activities for fiscal year 2018 related primarily to an acquisition of an industrial imaging solutions provider for \$4.8 million, and capital expenditures for property plant and equipment of \$20.4 million. Net cash used in investing activities for fiscal year 2017 related to the Acquired Detector Business for \$271.8 million (net of cash acquired) and capital expenditures for property plant and equipment of \$20.2 million.

*Net Cash Provided by (Used in) Financing Activities.* Financing activities for the fiscal year 2019 primarily consisted of borrowings under our credit agreements of \$85.4 million, repayments of borrowings of \$87.0 million, and net proceeds from equity plans of \$2.5 million. Financing activities for the fiscal year 2018 primarily consisted of borrowings under our credit agreements of \$10.0 million, repayments of borrowings of \$106.0 million, and net proceeds from equity plans of \$4.8 million. Financing activities for the fiscal years 2017 primarily consisted of borrowings under our credit agreements of \$749.0 million and net transfers from Varian of \$5.0 million, partially offset by distributions to Varian of \$227.1 million, repayments of borrowings of \$255.0 million and payment of debt issuance costs of \$11.9 million.

## Days Sales Outstanding

Trade accounts receivable days sales outstanding (“DSO”) was 63 days and 68 days at September 27, 2019 and September 28, 2018, respectively. Our accounts receivable and DSO are impacted by a number of factors, primarily including the timing of product shipments, collections performance, payment terms, the mix of revenues from different regions and the effects of economic instability.

## Contractual Obligations

The following table summarizes, as of September 27, 2019, the total amount of future payments due in various future periods:

(In millions)	Payments Due by Period				
	Total	Fiscal Year 2020	Fiscal Years 2021-2022	Fiscal Years 2023-2024	Beyond
Operating lease obligations	\$ 20.5	\$ 7.5	\$ 10.1	\$ 2.7	\$ 0.2
Principal payments on borrowings	400.8	30.7	370.1	—	—
DpiX fixed cost commitment	3.7	3.7	—	—	—
Dividends to redeemable interest	4.2	0.6	1.2	1.2	1.2
Total	\$ 429.2	\$ 42.5	\$ 381.4	\$ 3.9	\$ 1.4

We lease office space under non-cancelable operating leases. The leases expire at various dates through 2025, excluding extensions at our option, and contain provisions for rental adjustments, including in certain cases, adjustments based on increases in the Consumer Price Index. The leases generally contain renewal provisions for varying periods of time.

For further discussion regarding our borrowings, see Note 8. *Borrowings* included in the notes to our consolidated financial statements.

In October 2013, we entered into an amended agreement with dpiX and other parties that, among other things, provides us with the right to 50% of dpiX's total manufacturing capacity produced after January 1, 2014. The amended agreement requires us to pay for 50% of the fixed costs (as defined in the amended agreement), as determined at the beginning of each calendar year. For the remainder of calendar year 2019, we estimate that we have fixed cost commitments of \$3.7 million related to this amended agreement. The fixed cost commitment for future periods will be determined and approved by the dpiX board of directors at the beginning of each calendar year. The amended agreement will continue unless the ownership structure of dpiX changes (as defined in the amended agreement).

In October 2015, we committed to grant the noncontrolling shareholders of MeVis: (1) an annual recurring net compensation of €0.95 per MeVis share; and, (2) a put right for their MeVis shares at €19.77 per MeVis share. As of September 27, 2019, noncontrolling shareholders together held approximately 0.5 million shares of MeVis, representing 26.3% of the outstanding shares.

## Contingencies

From time to time, we are a party to or otherwise involved in legal proceedings, claims and government inspections or investigations, customs and duty audits and other matters both inside and outside the United States, arising in the ordinary course of our business or otherwise. Such matters are subject to many uncertainties and outcomes are not predictable with assurance.

See Part 1, Item 3 of this Annual Report for additional information regarding legal proceedings and Note 11, *Commitments and Contingencies* in the notes to our consolidated financial statements for further information regarding certain of our contractual obligations and contingencies, which discussion is incorporated herein by reference.

## Off-Balance Sheet Arrangements

In conjunction with the sale of our products in the ordinary course of business, and consistent with industry practice, we provide standard indemnification of business partners and customers for losses suffered or incurred for property damages, death and injury and for patent, copyright or any other intellectual property infringement claims by any third parties with respect to our products. The terms of these indemnification arrangements are generally perpetual. Except for losses related to property damages, the maximum potential amount of future payments we could be required to make under these arrangements is unlimited. As of September 27, 2019, we have not incurred any material costs to defend lawsuits or settle claims related to these indemnification arrangements. As a result, we believe the estimated fair value of these arrangements is minimal.

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

## **Critical Accounting Policies and Estimates**

The preparation of our consolidated financial statements and related disclosures in conformity with GAAP requires us to make estimates and assumptions that affect the reported amounts of assets, liabilities, revenues and expenses. These estimates and assumptions are based on historical experience and on various other factors that we believe are reasonable under the circumstances. Our critical accounting policies that are affected by accounting estimates require us to use judgments, often as a result of the need to make estimates and assumptions regarding matters that are inherently uncertain, and actual results could differ materially from these estimates. For a discussion of how these estimates and other factors may affect our business, see “Risk Factors.”

We periodically review our accounting policies, estimates and assumptions and make adjustments when facts and circumstances dictate. Such accounting policies require us to use judgments, often as a result of the need to make estimates and assumptions regarding matters that are inherently uncertain, and actual results could differ materially from these estimates. For a discussion of how these estimates and other factors may affect our business, see Item 1A, “Risk Factors.”

### ***Inventories***

Inventories are valued at the lower of cost or net realizable value. Costs include materials, labor and manufacturing overhead and is computed using standard cost (which approximates actual cost) on a first-in-first-out basis. We evaluate the carrying value of our inventories taking into consideration such factors as historical and anticipated future sales compared to quantities on hand and the prices we expect to obtain for products in our various markets. We adjust excess and obsolete inventories to net realizable value and write-downs of excess and obsolete inventories are recorded as a component of cost of revenues.

### ***Goodwill and Intangible Assets***

Goodwill is initially recorded when the purchase price paid for a business acquisition exceeds the estimated fair value of the net identified tangible and intangible assets acquired. Our future operating performance will be impacted by the future amortization of these acquired intangible assets and potential impairment charges related to these intangibles or to goodwill if indicators of impairment exist. The allocation of the purchase price from business acquisitions to goodwill and intangible assets could have a material impact on our future operating results. In addition, the allocation of the purchase price of the acquired businesses to goodwill and intangible assets requires us to make significant estimates and assumptions, including estimates of future cash flows expected to be generated by the acquired assets and the appropriate discount rate for those cash flows. Should conditions differ from management’s estimates at the time of the acquisition, material write-downs of intangible assets and/or goodwill may be required, which would adversely affect our operating results.

We evaluate goodwill for impairment at least annually or whenever an event occurs or circumstances change that would more likely than not reduce the fair value of a reporting unit below its carrying amount. The evaluation includes consideration of qualitative factors including industry and market considerations, overall financial performance, and other relevant events and factors affecting the reporting unit. If we determine that a quantitative analysis is necessary, the impairment test for goodwill is a two-step process. Step one consists of a comparison of the fair value of a reporting unit against its carrying amount, including the goodwill allocated to each reporting unit. We determine the fair value of our reporting units based on a combination of income and market approaches. The income approach is based on the present value of estimated future cash flows of the reporting units and the market approach is based on a market multiple calculated for each reporting unit based on market data of other companies engaged in similar business. If the carrying amount of the reporting unit is in excess of its fair value, step two requires the comparison of the implied fair value of the reporting unit’s goodwill against the carrying amount of the reporting unit’s goodwill. Any excess of the carrying value of the reporting unit’s goodwill over the implied fair value of the reporting unit’s goodwill is recorded as an impairment loss.

In fiscal years 2019, 2018 and 2017, we performed the annual goodwill impairment test for our two reporting units and found no impairment. We performed the annual goodwill analysis as of the first day of the fourth quarter of each fiscal year (using balances as of the end of the third quarter of that fiscal year). For both reporting units, based upon the annual goodwill analysis that we performed as of the first day of the fourth quarter of the respective fiscal years, either step one of the impairment test was not completed based on evaluation of qualitative factors or, if step one was completed, the fair value was substantially in excess of carrying value. However, significant changes in our projections about our operating results or other factors could cause us to make interim assessments of impairments in any quarter that could result in some or all of the goodwill being impaired.

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

### ***Impairment of Investments***

We have investments in privately held companies that are accounted for under the equity method of accounting as we hold at least a 20% ownership interest or have the ability to exercise significant influence in these investments. We monitor these investments for events or circumstances indicative of potential impairment, and we make appropriate reductions in carrying values if we determine that an impairment charge is required, based primarily on the financial condition, near-term prospects and recent financing activities of the investee.

### ***Taxes on Earnings***

Current income tax expense is the amount of income taxes expected to be payable for the current year. Deferred income tax liabilities or assets are established for the expected future tax consequences resulting from the differences in financial reporting and tax bases of assets and liabilities. A valuation allowance is provided if it is more likely than not that some or all of the deferred tax assets will not be realized. In addition, we provide reserves for uncertain tax positions when such tax positions do not meet the recognition thresholds or measurement standards prescribed by the authoritative guidance for accounting for income taxes. Amounts for uncertain tax positions are adjusted in periods when new information becomes available or when positions are effectively settled. Interest and penalties related to uncertain tax positions are recognized as a component of income tax expense.

On December 22, 2017, the U.S. Government enacted comprehensive tax legislation commonly referred to as the Tax Cuts and Jobs Act of 2017 (“U. S. Tax Reform”). U.S. Tax Reform significantly revised the U.S. corporate income tax structure including a lower corporate statutory rate and changes to the way foreign earnings are taxed. U.S. GAAP requires that the impact of tax legislation be recognized in the period in which the law is enacted. In accordance with these rules, we are including the impact of certain provisions of U.S. Tax Reform to the extent they are effective during the current reporting period.

### ***Backlog***

Backlog is the accumulation of all orders for which revenues have not been recognized and are still considered valid. Backlog also includes a small portion of billed service contracts that are included in deferred revenue. Our total backlog at September 27, 2019 was \$265.2 million, a decrease of 13.9% from the backlog of \$308.1 million at September 28, 2018.

Orders may be revised or canceled, either according to their terms or as customers’ needs change. Consequently, it is difficult to predict with certainty the amount of backlog that will result in revenues. We perform a quarterly review to verify that outstanding orders in the backlog remain valid. Aged orders that are not expected to be converted to revenues are deemed dormant and are reflected as a reduction in the backlog amounts in the period identified.

In addition to orders for which revenues have not been recognized and are still considered valid, we have pricing agreements with many of our established customers that span multi-year periods. These pricing agreements include volume ranges under which orders are placed.

### ***Recent Accounting Standards or Updates Not Yet Effective***

See Note 1, *Summary of Significant Accounting Policies* of the notes to the consolidated financial statements for a description of recent accounting standards, including the expected dates of adoption and the estimated effects on our consolidated financial statements.

## **Item 7A. Quantitative and Qualitative Disclosures about Market Risks**

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

### ***Foreign Currency Exchange Rate Risk***

A significant portion of our customers are outside the United States, while our financial statements are denominated, and our products are generally priced in U.S. Dollars. A strong U.S. Dollar may result in pricing pressure for our customers that are located outside the United States and that conduct their businesses in currencies other than the U.S. Dollar. Such pricing pressure has caused, and could continue to cause, some of our customers to ask for discounted prices, delay purchasing decisions, consider moving to insourcing supply of components or migrating to lower cost alternatives. In addition, because our business is global and some payments may be made in local currency, fluctuations in foreign currency exchange rates can impact our revenues and expenses and/or the profitability in U.S. Dollars of products and services that we provide in foreign markets.

We may enter into foreign currency forward and option contracts with financial institutions to protect against foreign exchange risks associated with certain existing assets and liabilities, and net investments in foreign subsidiaries. We generally hedge portions of forecasted foreign currency, typically for one month. In addition, we hold a cross-currency swap between the Euro and U.S. Dollar as a Net Investment Hedge of our recent acquisition of Direct Conversion. Depending on the spot rate between the Euro and U.S. Dollar at the time of settlement and whether we have sufficient Euros available, we may have to borrow incrementally in U.S. Dollars to settle this obligation. However, we may choose not to hedge certain foreign exchange exposures for a variety of reasons including, but not limited to, accounting considerations or the prohibitive economic cost of hedging particular exposures.

### ***Credit and Counterparty Risk***

We use a centralized approach to manage substantially all of our cash and to finance our operations. Our cash and cash equivalents may be exposed to a concentration of credit risk and we may also be exposed to credit risk and interest rate risk to the extent that we enter into credit facilities.

We perform ongoing credit evaluations of our customers and we maintain what we believe to be strong credit controls in evaluating and granting customer credit, including performing ongoing evaluations of our customers' financial condition and creditworthiness and often using letters of credit and requiring industrial customers to provide a down payment.

### ***Interest Rate Risk***

At September 27, 2019, we had total borrowings of \$395.1 million (net of deferred loan costs). Borrowings under our credit facilities bear interest at floating interest rates. As a result, we are exposed to fluctuations in interest rates to the extent of our borrowings under the credit facilities. As part of our overall risk management program, we entered into several interest rate swaps designed as cash flow hedges, to hedge the floating LIBOR components of our interest rate which represented a notional value of \$264.4 million of our debt as of September 27, 2019. Excluding the amount of our borrowings that is subject to fixed interest rates under our interest rate swaps, and assuming the current level of borrowings remained the same, we estimate that our interest expense would change by approximately \$1.3 million annually for each one percentage point change in the average interest rate under our borrowings.

See Note 7. *Financial Derivatives and Hedging Activities* and Note 8. *Borrowings* of the notes to our consolidated financial statements for further information on interest rate hedging activities and borrowings.

### ***Commodity Price Risk***

We are exposed to market risks related to volatility in the prices of raw materials used in our products. The prices of these raw materials fluctuate in response to changes in supply and demand fundamentals and our product margins and level of profitability tend to fluctuate with changes in these raw materials prices. We try to protect against such volatility through various business strategies. During the fiscal year ended September 27, 2019, we did not have any commodity derivative instruments in place to manage our exposure to price changes.

## **Item 8. Financial Statements and Supplementary Data.**

The Consolidated Financial Statements and Schedules listed in the Index to Financial Statements, Schedules and Exhibits on page F-1 are filed as part of this Annual Report and incorporated in this Item 8 by reference.

## **Item 9. Changes in and Disagreements with Accountants on Accounting and Financial Disclosure.**

None.

## **Item 9A. Controls and Procedures.**

### ***Evaluation of Disclosure Controls and Procedures***

Our disclosure controls and procedures, as defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934, are designed to ensure that information required to be disclosed in the reports that we file or submit under the Exchange Act is recorded, processed, summarized, and reported within the time periods specified in the rules and forms of the Securities and Exchange Commission and to ensure that such information required to be disclosed is accumulated and communicated to management, including



our principal executive and financial officers, as appropriate to allow timely decisions regarding required disclosure. The Chief Executive Officer (CEO) and the Chief Financial Officer (CFO), with assistance from other members of management, have evaluated the effectiveness of our disclosure controls and procedures as of September 27, 2019 and, based on their evaluation, the CEO and CFO have concluded that the disclosure controls and procedures were not effective as of such date due to the material weaknesses in internal control over financial reporting described below.

To address the material weaknesses described below, and prior to filing this Annual Report on Form 10-K, we performed additional analysis and other post-closing procedures to determine our consolidated financial statements are prepared in accordance with generally accepted accounting principles. Based on these procedures, management has concluded that our consolidated financial statements included in this Form 10-K have been prepared in accordance with generally accepted accounting principles and our CEO and CFO have certified that, based on their knowledge, the consolidated financial statements, and other financial information included in this Form 10-K, fairly present in all material respects the financial condition, results of operations and cash flows for the periods presented. PricewaterhouseCoopers LLP, an independent registered public accounting firm, has issued an unqualified opinion on our consolidated financial statements, which appears herein.

### ***Management's Annual Report on Internal Control Over Financial Reporting***

Our management is responsible for establishing and maintaining adequate internal control over our financial reporting as defined in Rules 13a-15(f) and 15d-15(f) under the Exchange Act. Our internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles and includes those policies and procedures that:

- (1) pertain to the maintenance of records that in reasonable detail accurately and fairly reflect our transactions and the dispositions of our assets;
- (2) provide reasonable assurance that our transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles and that our receipts and expenditures are being made only in accordance with appropriate authorizations; and
- (3) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use or disposition of our assets that could have a material effect on our financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

Under the supervision and with the participation of our management, we assessed the effectiveness of our internal control over financial reporting as of September 27, 2019, using the criteria described in *Internal Control-Integrated Framework (2013)* issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO).

A material weakness is a deficiency, or a combination of deficiencies, in internal control over financial reporting, such that there is a reasonable possibility that a material misstatement of our annual or interim financial statements will not be prevented or detected on a timely basis.

We have identified the following control deficiencies that constituted material weaknesses in our internal control over financial reporting as of September 27, 2019:

- We did not design and maintain an effective risk assessment process to identify and assess the risks in our business processes, specifically, we did not adequately identify new and evolving risks of material misstatement and design and implement controls to address those risks as a result of changes to our business operating environment including adoption of new accounting principles. We also did not maintain an effective control environment as we had an insufficient complement of resources with the requisite knowledge and experience to create the proper environment for effective internal control over financial reporting such that corrective activities to our internal control over financial reporting are appropriately applied, prioritized, and implemented in a timely manner. Although these deficiencies did not result in adjustments to our consolidated financial statements, until remediated, they could result in material misstatements potentially impacting all financial statement accounts and disclosures in our annual or interim consolidated financial statements that would not be prevented or detected. These material weaknesses contributed to the following control deficiencies, which are also considered to be material weaknesses:



- We did not design and maintain effective controls related to accounting for revenue, deferred revenue and related accounts receivable, including maintaining effective business process controls to prevent or detect misstatements in the processing of customer transactions. Specifically, we did not design and maintain effective controls related to the review of the completeness and accuracy of customer order entry, quantity and pricing. Additionally, we did not design and maintain effective controls for the effect of the adoption of and continuous accounting for Revenue from Contracts with Customers (“ASC 606”) to prevent and detect misstatements.
- We did not design and maintain effective controls related to accounting for inventory and cost of revenues, including maintaining effective business process controls to prevent or detect misstatements in the accuracy and valuation of inventory. Specifically, we did not maintain effective controls related to inventory count procedures, the valuation of inventory at lower of cost and net realizable value and presentation and disclosure of inventory classifications.
- We did not design and maintain effective controls over our financial reporting close process to prevent or detect material misstatements in our financial statements. Specifically, we did not maintain an effective business performance monitoring review control at our international entities, maintain effective controls related to the elimination of intercompany balances, design and maintain controls to identify post-close events which occur before the financial statements are available to be issued and design and maintain effective control over the review of the statement of cash flows.

The deficiencies in revenue, inventory and financial reporting close process resulted in immaterial audit adjustments and out of period adjustments to the Company’s consolidated financial statements for the fiscal years ended and as of September 27, 2019 and September 28, 2018 and respective interim periods. Additionally, until remediated, these deficiencies could result in a material misstatement impacting the aforementioned accounts and disclosures in our annual or interim consolidated financial statements that would not be prevented or detected. Accordingly, our management has determined these deficiencies constitute material weaknesses.

Because of the material weaknesses described above, management concluded that we did not maintain effective internal control over financial reporting as of September 27, 2019.

A subsidiary of Varex acquired Direct Conversion AB on April 29, 2019. Management has excluded Direct Conversion AB from its evaluation of the effectiveness of internal control over financial reporting as of September 27, 2019. The total assets and total revenues of Direct Conversion represent approximately 0.8% and 0.8%, respectively, of the related consolidated financial statements amounts as of and for the fiscal year ended September 27, 2019.

Our independent registered public accounting firm, PricewaterhouseCoopers LLP, has issued an adverse audit report on the effectiveness of our internal control over financial reporting as of September 27, 2019, which appears herein.

### ***Status of Remediation Efforts***

#### ***Remediation of Material Weaknesses Reported in Fiscal Year 2018 Form 10-K***

We have devoted substantial effort to remediating the areas of material weakness identified in fiscal year 2018 and continue to perform a risk assessment process to identify, design, implement, and re-evaluate the control activities. While we continue to enhance our risk assessment process to ensure that it is comprehensive, management concluded that certain material weaknesses identified in fiscal year 2018 and reported in our Annual Report on Form 10-K as of September 28, 2018, were remediated in fiscal year 2019. Specifically, material weaknesses were remediated in the areas of:

- 1) information technology general controls (ITGCs) around user access and program change controls; and
- 2) accounting for our operations in Germany, including maintaining effective business process controls and segregation of duties related to the authorization of transactions and journal entries, and the cutoff, completeness and accuracy of transactions.

#### ***Implementation of improvements in ITGCs around user access and program change controls included the following:***

- *Performance of Control Environment Review* - As part of the overall risk assessment process, we identified relevant applications and tools to enhance overall controls compliance.
- *Implementation of Control Design Review* - We made significant changes to the control environment by redesigning certain controls to be aligned with the Control Objectives for Information and Related Technology (COBIT) framework and designing additional controls to ensure all identified risks were addressed. The result is effectively designed information technology general controls in the areas of change management, computer operations, backup and recovery, and security were subject to review. Security controls were reviewed by application.

- *Performance of Deficiency Specific Remediation Plans* - We implemented remediation plans for each of the deficiencies, categorized by remediation actions, process implementation, and control rationalization. Our remediation plans were focused on identifying and mitigating the risk, and our design effectiveness and operational testing were performed.
- *User Access:*
  - Sensitive access identified as being inappropriate was removed from our users of in-scope systems.
  - Implemented real time monitoring in the form of reports and e-mail notifications. This monitoring acts as an alert whenever sensitive access has been executed.
  - Sensitive access can now only be used through a specific defined process and requires a service ticket in advance. We review sensitive access for appropriateness quarterly.
  - Implemented a specific segregation of duties rule-set, ensuring conflict-free roles are maintained, and user level segregation of duty conflicts are identified for remediation or mapping to certified mitigating controls.
  - Enhanced the provisioning process by adding a preventative control for new and updated user access by incorporating our specific segregation of duties rule-set to ensure on-going compliance is maintained, and sensitive access and segregation of duty conflicts are not re-introduced into the environment.
  - Completed a user access review for all accounts within our ERP system.
- *Change Management:*
  - We implemented an updated change management process and policy, including documented pre-approvals, testing procedures, and post approvals, as needed.
  - Appropriate segregation of duties were implemented over making source code changes and migrating changes to the production environment. Our users with developer access do not have access to push code to production.

*Improved Germany Control Environment* - We engaged outside consultants in Germany to perform a detailed review of business process control documentation, including segregation of duties, authorization of transactions, journal entries, cutoff, completeness and accuracy of transactions, key controls to execute remediation activities, and to implement appropriate controls, assess design and test operating effectiveness, and formalize our corporate-level review and approval.

#### *Ongoing Remediation Efforts*

Management has been implementing, and continues to implement, measures designed to ensure (a) that control deficiencies contributing to the remaining material weaknesses in the areas of risk assessment, control environment, revenue, inventory, and financial reporting close are remediated, and (b) that these controls are designed, implemented, and operating effectively. Specifically, we are implementing the following changes:

- **Risk Assessment Process** - We are devoting substantial effort in performing a comprehensive risk assessment process to identify, design, implement, and re-evaluate our control activities related to the above mentioned material weakness in our internal control over financial reporting, including monitoring controls related to the design and operating effectiveness of certain control activities pertaining to our business process environment, as more fully discussed below.
- **Control Environment** - We are committed to and are developing plans to attract, develop, and retain additional competent individuals in alignment with our objectives to remediate areas of material weakness, and to create the proper environment for effective internal control over financial reporting such that corrective activities to our internal control over financial reporting are appropriately applied, prioritized, and implemented in a timely manner. In addition, we are reviewing our oversight and supervision of our outside consultants that assist in our evaluation of internal controls and improving project management over internal controls
- **Revenue Processes** - We are implementing controls over (i) standard contract reviews, (ii) customer invoice reviews, (iii) review of monthly sales order changes and (iv) an addition of a management review control that reviews and approves the summary of service billings for the period. We revised the revenue recognition controls due to the transition to ASC 606 and will continue to improve our review controls around the completeness and accuracy of customer order entry, quantity and pricing, and the continuing accounting for ASC 606.
- **Inventory Processes** - We are implementing controls over (i) review of inventory adjustments and approvals and (ii) review over variance analysis. We continue to improve our inventory count procedures, review and valuation controls over inventory.
- **Financial Close Processes** - To be consistent with our consolidated monthly closing financial statement review meetings, we continue to enhance controls over international business performance reviews to include improved documentation of items for follow-up and resolution, expand our review over completeness and accuracy of intercompany balances, design controls

to identify post-close events which occur before the financial statements are available to be issued and enhance controls over the review of the statement of cash flows.

The following represent ongoing remediation efforts related to implemented enhancements to our control environment that we believe will support our ongoing remediation efforts of any remaining material weaknesses:

*Formal ICOFR Function* - We are enhancing our control environment to include a formal internal control over financial reporting (ICOFR) compliance project management office (PMO) and ICOFR execution function. The roles and responsibilities of the PMO include the management of overall ICOFR timelines, coordination and communication with external and internal audit, process owner working sessions and related follow-up activities, coordination with international operations, and oversight of Company's remediation efforts. The Company has supplemented its internal resources with outside consultants recognized as experts in ICOFR program execution and have augmented process owner awareness and accountability with various training protocols as well as an ICOFR execution and monitoring program application.

*Risk Management Committee* - We formed an executive Risk Management Committee, which meets regularly, to review risk management and internal audit status updates, ICOFR status, and other compliance areas of focus. A detailed remediation and compliance plan, related timeline and critical milestones were developed, and reviewed with the committee on a regular basis.

*Monthly / Quarterly Financial Process* - We are implementing an improved financial close process and reporting process that includes;

- i. Monthly closing calendar supplementing the existing quarterly close calendar.
- ii. Monthly closing financial statement review meetings with process owners and financial reporting leadership.
- iii. Disclosure committee meetings, which include formal documented quarterly meetings with relevant business unit heads and other corporate functions to ensure all potential issues are escalated and resolved prior to finalizing the financial statements.
- iv. The financial statements are reviewed and approved by the disclosure committee, key financial management, legal department, the audit committee and other relevant process owners prior to filing.
- v. We have implemented controls to ensure the appropriate foreign currency rates are utilized in the financial reporting close process.
- vi. Quarterly, account reconciliations are reviewed and approved in accordance with our Account Reconciliation Policy.
- vii. We have implemented controls to ensure the segment and geographic reporting is correct.

We believe that these actions will remediate the remaining material weaknesses, although additional changes and improvements may be identified and adopted as we continue to evaluate and implement our remediation plans. The material weaknesses will not be considered remediated until the applicable controls operate for a sufficient period of time and management has concluded, through testing, that the controls are operating effectively. In particular, the material weakness for risk assessment and control environment will not be considered remediated until the material weaknesses within revenue, inventory and financial reporting close have been remediated. As a result, until remediated, these material weaknesses could result in material misstatements potentially impacting all financial statement accounts and disclosures in our annual or interim consolidated financial statements that would not be prevented or detected.

### ***Changes in Internal Control Over Financial Reporting***

During the quarter ended September 27, 2019, we determined that there was an additional material weakness related to our control environment, as well as additions to the material weakness in the financial reporting close process, as described above.

The remediation activities described below are changes in internal control over financial reporting during the quarter ended September 27, 2019 that have materially affected, or are reasonably likely to materially affect, our ICOFR.

*Improvements to Entity Level Controls* - We operated entity and corporate-level controls to support the overall control environment over financial reporting, including enhanced training and development activities around control ownership and operation, improved technologies to facilitate certifications, ongoing documentation and testing efforts, and increased accountability and overall communication.

*Specific Analysis of Deficiencies and Identification of Remediation Activities* - We implemented a systematic risk-based approach for identifying and implementing remediation efforts to address the six (6) material weaknesses disclosed in fiscal year 2018. We performed a detailed review of all deficiencies that were previously disclosed as material weaknesses: risk assessment, ITGC / user access, revenue, inventory, Germany operations, and the financial reporting close process.

**Item 9B. Other Information**

None.

## **PART III**

### **Item 10. Directors, Executive Officers and Corporate Governance**

#### **Directors and Executive Officers**

The information required by this item with respect to our executive officers is set forth in Part I of this Annual Report on Form 10-K and information relating to the availability of our code of conduct for executive officers and directors is set out below. The other information required by this item is incorporated by reference from our definitive proxy statement for the 2020 Annual Meeting of Stockholders under the captions “Proposal One — Election of Directors.” and “Stock Ownership-Section 16(a) Beneficial Ownership Reporting Compliance.” Our definitive proxy statement for the 2020 Annual Meeting of Stockholders will be filed with the SEC no later than 120 days after September 27, 2019.

#### **Code of Conduct**

We have adopted a Code of Conduct that applies to all of our executive officers and directors. The Code of Conduct is available on our website at <http://www.vareximaging.com>, and may be found as follows:

1. From our main web page, first click “Investors.”
2. Next click on “Governance Highlights” under “Corporate Governance” in the drop-down menu.
3. Finally, click on “Code of Conduct.”

We intend to satisfy the disclosure requirements under Item 5.05(c) of Form 8-K regarding an amendment to, or waiver from, a provision of the Code of Conduct that applies to our principal executive officer, principal financial officer, principal accounting officer or controller or persons performing similar functions by posting such information on our website, specified above.

### **Item 11. Executive Compensation.**

The information required by this item is incorporated by reference from our definitive proxy statement for the 2020 Annual Meeting of Stockholders under the caption “Executive Compensation.”

### **Item 12. Security Ownership of Certain Beneficial Owners and Management and Related Stockholder Matters.**

The information required by this item is incorporated by reference from our definitive proxy statement for the 2020 Annual Meeting of Stockholders under the caption “Stock Ownership” and “Executive Compensation.”

### **Item 13. Certain Relationships and Related Transactions and Director Independence.**

The information required by this item with respect to certain relationships and related transactions is incorporated by reference from our definitive proxy statement for the 2020 Annual Meeting of Stockholders under the caption “Certain Relationships and Related Transactions.” The information required by this item with respect to director and committee member independence is incorporated by reference from our definitive proxy statement for the 2020 Annual Meeting of Stockholders under the caption “Proposal One-Election of Directors.”

### **Item 14. Principal Accountant Fees and Services.**

The information required by this item is incorporated by reference from our definitive proxy statement for the 2020 Annual Meeting of Stockholders under the caption “Proposal Four-Ratification of the Appointment of Our Independent Registered Public Accounting Firm.”

## PART IV

**Item 15. Exhibits, Consolidated Financial Statements and Financial Statement Schedules.**

Documents filed as part of this annual report include:

1. *Consolidated Financial Statements.* We have filed the consolidated financial statements listed in the index to Consolidated Financial Statements, Schedules and Exhibits on page F-1 as part of this annual report on Form-10K.
2. *Financial Statement Schedules and Other:* All financial statement schedules have been omitted because they are not applicable, or not material or the required information is shown in the consolidated financial statements or the notes thereto.
3. *Exhibits.* The exhibits listed below are filed as part of this annual report on Form 10-K.

<b>Exhibit Number</b>	<b>Description</b>
2.1*	<a href="#"><u>Separation and Distribution Agreement, dated as of January 27, 2017, by and between Varian and (incorporated by reference to Exhibit 2.1 to Company's Current Report on Form 8-K filed January 30, 2017, SEC File No. 001-37860).</u></a>
2.2*	<a href="#"><u>Master Purchase and Sale Agreement, dated as of December 21, 2016, by and between Varian Medical Systems, Inc. and PerkinElmer, Inc. (incorporated by reference to Exhibit 2.2 to Company's Amendment No. 3 to the Registration Statement on Form 10 filed December 30, 2016, SEC File No. 001-37860).</u></a>
2.3*	<a href="#"><u>Amendment No.1 to Master Purchase and Sale Agreement, entered into as of January 17, 2017, by and between PerkinElmer, Inc. and Varian Medical Systems, Inc. (incorporated by reference to Exhibit 2.2 to Company's Quarterly Report on Form 10-Q filed May 12, 2017, SEC File No. 001-37860).</u></a>
2.4*	<a href="#"><u>Assignment and Assumption Agreement, dated January 27, 2017, by and between Varian Medical Systems, Inc. and Varex Imaging Corporation (incorporated by reference to Exhibit 2.3 to Company's Quarterly Report on Form 10-Q filed May 12, 2017, SEC File No. 001-37860).</u></a>
2.5*	<a href="#"><u>Amendment No.2 to Master Purchase and Sale Agreement, entered into as of April 28, 2017, by and between PerkinElmer, Inc. and Varex Imaging Corporation (incorporated by reference to Exhibit 2.4 to Company's Quarterly Report on Form 10-Q filed May 12, 2017, SEC File No. 001-37860).</u></a>
3.1*	<a href="#"><u>Amended and Restated Certificate of Incorporation, dated January 27, 2017 (as corrected December 11, 2017) (incorporated by reference to Exhibit 3.1 to the Company's Annual Report on Form 10-K filed November 27, 2018, SEC File No. 001-37860).</u></a>
3.2*	<a href="#"><u>Amended and Restated Bylaws of Company, as amended January 27, 2017 (incorporated by reference to Exhibit 3.2 to Company's Current Report on Form 8-K filed January 30, 2017, SEC File No. 001-37860).</u></a>
4.1**	<a href="#"><u>Information required by Item 202(a) through (d) and (f) of Regulation S-K for each class of Company securities that is registered under Section 12 of the Exchange Act.</u></a>
10.1*	<a href="#"><u>Transition Services Agreement, dated as of January 27, 2017, by and between Varian and Company (incorporated by reference to Exhibit 10.1 to Company's Current Report on Form 8-K filed January 30, 2017, SEC File No. 001-37860).</u></a>
10.2*	<a href="#"><u>Tax Matters Agreement, dated as of January 27, 2017 by and between Varian and Company (incorporated by reference to Exhibit 10.2 to Company's Current Report on Form 8-K filed January 30, 2017, SEC File No. 001-37860).</u></a>
10.3*	<a href="#"><u>Employee Matters Agreement, dated as of January 27, 2017, by and between Varian and Company (incorporated by reference to Exhibit 10.3 to Company's Current Report on Form 8-K filed January 30, 2017, SEC File No. 001-37860).</u></a>

10.4\*

[Intellectual Property Matters Agreement, dated as of January 27, 2017, by and between Varian and Company \(incorporated by reference to Exhibit 10.4 to Company's Current Report on Form 8-K filed January 30, 2017, SEC File No. 001-37860\).](#)

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10.5*	<a href="#"><u>Trademark License Agreement, dated as of January 27, 2017, by and between Varian and Company (incorporated by reference to Exhibit 10.5 to Company's Current Report on Form 8-K filed January 30, 2017, SEC File No. 001-37860).</u></a>
10.6*++	<a href="#"><u>Credit Agreement, dated as of May 1, 2017, by and among Company as Borrower, the Lenders referred to therein, as Lenders, and Bank of America, N.A., as Administrative Agent, Swingline Lender and Issuing Lender (incorporated by reference to Exhibit 10.1 to Company's Quarterly Report on Form 10-Q filed August 14, 2017, SEC File No. 001-37860).</u></a>
10.7*	<a href="#"><u>Credit Agreement, dated as of January 25, 2017, by and among Varex Imaging Corporation as Borrower, the Lenders referred to herein, as Lenders, and Wells Fargo Bank, National Association, as Administrative Agent, Swingline Lender and Issuing Lender, Wells Fargo Securities, LLC, as Sole Lead Arranger and Sole Bookrunner (incorporated by reference to Exhibit 10.6 to Company's Current Report on Form 8-K filed January 30, 2017, SEC File No. 001-37860).</u></a>
10.8*†	<a href="#"><u>Varex Imaging Corporation 2017 Omnibus Stock Plan (incorporated by reference to Exhibit 99.1 to the Company's Form S-8, filed January 27, 2017, SEC File No. 001-37860).</u></a>
10.9*†	<a href="#"><u>Form of Nonqualified Stock Option Agreement under the 2017 Omnibus Stock Plan (incorporated by reference to Exhibit 10.1 to Company's Current Report on Form 8-K filed February 16, 2017, SEC File No. 001-37860).</u></a>
10.10*†	<a href="#"><u>Form of Restricted Stock Unit Award Agreement under the 2017 Omnibus Stock Plan (incorporated by reference to Exhibit 10.2 to Company's Current Report on Form 8-K filed February 16, 2017, SEC File No. 001-37860).</u></a>
10.11*†	<a href="#"><u>Varex Imaging Corporation 2017 Employee Stock Purchase Plan (incorporated herein by reference to Exhibit 99.2 to the Company's Form S-8, filed January 27, 2017, SEC File No. 001-37860).</u></a>
10.12*†	<a href="#"><u>Varex Imaging Corporation Management Incentive Plan (incorporated by reference to Exhibit 10.9 to Company's Current Report on Form 8-K filed January 30, 2017, SEC File No. 001-37860).</u></a>
10.13*†	<a href="#"><u>Form of Change in Control Agreement (incorporated by reference to Exhibit 10.10 to Company's Current Report on Form 8-K filed January 30, 2017, SEC File No. 001-37860).</u></a>
10.14*†	<a href="#"><u>Form of Indemnification Agreement (incorporated by reference to Exhibit 10.11 to Company's Current Report on Form 8-K filed January 30, 2017, SEC File No. 001-37860).</u></a>
10.15*†	<a href="#"><u>Varex Imaging Corporation 2016 Deferred Compensation Plan (incorporated by reference to Exhibit 10.6 to Amendment No. 2 to Form 10 filed by Company on December 8, 2016, SEC File No. 001-37860).</u></a>
10.16*†	<a href="#"><u>Varex Imaging Corporation Frozen Deferred Compensation Plan (incorporated by reference to Exhibit 10.7 to Amendment No. 2 to Form 10 filed by the Registrant on December 8, 2016, SEC File No. 001-37860).</u></a>
10.17*†	<a href="#"><u>Form of Grant Agreement for Deferred Stock Units under the 2017 Omnibus Stock Plan (incorporated by reference to Exhibit 10.17 to Company's Annual Report on Form 10-K filed Dec. 13, 2017, SEC File No. 001-378601).</u></a>
10.18*†	<a href="#"><u>Form of Grant Agreement for Deferred Stock Units under the 2017 Omnibus Stock Plan.</u></a>
10.19*	<a href="#"><u>Amendment to Credit Agreement dated September 28, 2018 (incorporated by reference to Exhibit 10.1 to Company's Current Report on Form 8-K filed on October 3, 2018, SEC File 001-37860).</u></a>
10.20*	<a href="#"><u>Amendment No. 2 to Credit Agreement, dated September 28, 2018 with Bank of America, N.A., as administrative agent, and the other lender parties thereto (incorporated by reference to Exhibit 10.1 to Company's Current Report on Form 8-K filed on October 3, 2018, SEC File 001-37860).</u></a>
10.21*	<a href="#"><u>Amendment No. 3 dated March 21, 2019 to Credit Agreement with Bank of America, N.A., as administrative agent, and the other lender parties thereto (incorporated by reference to Exhibit 10.2 to Company's Quarterly Report on Form 10-Q filed on May 8, 2019, SEC File 001-37860).</u></a>
10.22*	<a href="#"><u>Amendment No. 4 to Credit Agreement dated September 26, 2019 between Varex Imaging Corporation, Bank of America, N.A., as administrative agent and the lenders and guarantors party thereto (incorporated by reference to</u></a>

[Exhibit 10.1 to Company's Current Report on Form 8-K filed on October 2, 2019, SEC File 001-37860\).](#)

10.23\*

[Share Purchase Agreement dated March 21, 2019 between Varex Imaging Corporation, Varex Imaging Investments, B.V. and certain shareholders of Direct Conversions AB \(publ\) \(incorporated by reference to Exhibit 10.1 to Company's Quarterly Report on Form 10-Q filed on May 8, 2019, SEC File 001-37860\).](#)

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21.1**	<a href="#"><u>List of Subsidiaries as of November 5, 2019</u></a>
23.1**	<a href="#"><u>Consent of Independent Registered Public Accounting Firm</u></a>
31.1**	<a href="#"><u>Chief Executive Officer Certification Pursuant to Rule 13a-14(a) of the Securities Exchange Act.</u></a>
31.2**	<a href="#"><u>Chief Financial Officer Certification Pursuant to Rule 13a-14(a) of the Securities Exchange Act.</u></a>
32.1**	<a href="#"><u>Certification pursuant to 18 U.S.C. Section 1350 as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.</u></a>
32.2**	<a href="#"><u>Certification pursuant to 18 U.S.C. Section 1350 as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.</u></a>
101.INS**	XBRL Instance Document - the instance document does not appear in the Interactive Data File because its XBRL tags are embedded within the Inline XBRL 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
*	Incorporated herein by reference
**	Filed herewith
†	Management contract or compensatory agreement.
++	Portions of this exhibit have been omitted pursuant to a confidential treatment request filed pursuant to Rule 24b-2 of the Securities Exchange Act of 1934, as amended.

## **Item 16. Form 10-K Summary**

None

## SIGNATURES

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

### VAREX IMAGING CORPORATION

Date: December 20, 2019

By: /s/ CLARENCE R. VERHOEF

**Clarence R. Verhoef**

**Senior Vice President and Chief Financial Officer**

***(Duly Authorized Officer and Principal Financial Officer)***

Pursuant to the requirements of the Securities Exchange Act of 1934, this report has been signed below by the following persons on behalf of the registrant and in the capacities and on the dates indicated.

<u>Signature</u>	<u>Capacity</u>	<u>Date</u>
<u>/s/ SUNNY S. SANYAL</u> Sunny S. Sanyal	President and Chief Executive Officer and Director <i>(Principal Executive Officer)</i>	December 20, 2019
<u>/s/ CLARENCE R. VERHOEF</u> Clarence R. Verhoef	Senior Vice President and Chief Financial Officer <i>(Principal Financial Officer)</i>	December 20, 2019
<u>/s/ KEVIN B. YANKTON</u> Kevin B. Yankton	Corporate Controller and Chief Accounting Officer <i>(Principal Accounting Officer)</i>	December 20, 2019
<u>/s/ RUEDIGER NAUMANN-ETIENNE</u> Ruediger Naumann-Etienne	Chairman of the Board	December 20, 2019
<u>/s/ JOCELYN D. CHERTOFF</u> Jocelyn D. Chertoff	Director	December 20, 2019
<u>/s/ CHRISTINE A. TSINGOS</u> Christine A. Tsingos	Director	December 20, 2019
<u>/s/ JAY K. KUNKEL</u> Jay K. Kunkel	Director	December 20, 2019
<u>/s/ ERICH R. REINHARDT</u> Erich R. Reinhardt	Director	December 20, 2019
<u>/s/ WALTER M ROSEBROUGH, JR.</u> Walter M Rosebrough, Jr.	Director	December 20, 2019



## INDEX TO CONSOLIDATED FINANCIAL STATEMENTS

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<a href="#"><u>Consolidated Statements of Earnings for the fiscal years ended 2019, 2018 and 2017</u></a>	<a href="#"><u>F-5</u></a>
<a href="#"><u>Consolidated Statements of Comprehensive Earnings for the fiscal years ended 2019, 2018 and 2017</u></a>	<a href="#"><u>F-6</u></a>
<a href="#"><u>Consolidated Balance Sheets as of the end of fiscal years 2019 and 2018</u></a>	<a href="#"><u>F-7</u></a>
<a href="#"><u>Consolidated Statements of Cash Flows for the fiscal years ended 2019, 2018 and 2017</u></a>	<a href="#"><u>F-8</u></a>
<a href="#"><u>Consolidated Statements of Equity for the fiscal years 2019, 2018 and 2017</u></a>	<a href="#"><u>F-9</u></a>
<a href="#"><u>Notes to the Consolidated Financial Statements</u></a>	<a href="#"><u>F-10</u></a>

## **Report of Independent Registered Public Accounting Firm**

To the Board of Directors and Stockholders of Varex Imaging Corporation

### ***Opinions on the Financial Statements and Internal Control over Financial Reporting***

We have audited the accompanying consolidated balance sheets of Varex Imaging Corporation and its subsidiaries (the “Company”) as of September 27, 2019 and September 28, 2018, and the related consolidated statements of earnings, of comprehensive earnings, of equity and of cash flows for each of the three years in the period ended September 27, 2019, including the related notes (collectively referred to as the “consolidated financial statements”). We also have audited the Company's internal control over financial reporting as of September 27, 2019, based on criteria established in *Internal Control - Integrated Framework* (2013) issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO).

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of the Company as of September 27, 2019 and September 28, 2018, and the results of its operations and its cash flows for each of the three years in the period ended September 27, 2019 in conformity with accounting principles generally accepted in the United States of America. Also in our opinion, the Company did not maintain, in all material respects, effective internal control over financial reporting as of September 27, 2019, based on criteria established in *Internal Control - Integrated Framework* (2013) issued by the COSO because material weaknesses in internal control over financial reporting existed as of that date related to (i) ineffective risk assessment process to identify and assess the risks in the Company's business processes, (ii) ineffective control environment as the Company had an insufficient complement of resources with the requisite knowledge and experience to create the proper environment for effective internal control over financial reporting such that corrective activities to the Company's internal control over financial reporting are appropriately applied, prioritized, and implemented in a timely manner, (iii) ineffective controls related to accounting for revenue, deferred revenue and related accounts receivable, including maintaining effective business process controls to prevent or detect misstatements in the processing of customer transactions, and the effect of the adoption of and continuous accounting for Revenue from Contracts with Customers, (iv) ineffective controls related to accounting for inventory and cost of revenues, including maintaining effective business process controls to prevent or detect misstatements in the accuracy, valuation, presentation and disclosure of inventory, and (v) ineffective controls over the Company's financial reporting close process to prevent or detect misstatements in the financial statements, including ineffective business performance monitoring review control over the Company's international entities, ineffective controls related to elimination of intercompany balances, ineffective controls to identify post-close events which occur before the financial statements are available to be issued, and ineffective controls over the review of the statement of cash flows.

A material weakness is a deficiency, or a combination of deficiencies, in internal control over financial reporting, such that there is a reasonable possibility that a material misstatement of the annual or interim financial statements will not be prevented or detected on a timely basis. The material weaknesses referred to above are described in Management's Annual Report on Internal Control Over Financial Reporting appearing under Item 9A. We considered these material weaknesses in determining the nature, timing, and extent of audit tests applied in our audit of the September 27, 2019 consolidated financial statements, and our opinion regarding the effectiveness of the Company's internal control over financial reporting does not affect our opinion on those consolidated financial statements.

### ***Change in Accounting Principle***

As discussed in Note 18 to the consolidated financial statements, the Company changed the manner in which it accounts for revenue effective September 29, 2018.

### ***Basis for Opinions***

The Company's management is responsible for these consolidated financial statements, for maintaining effective internal control over financial reporting, and for its assessment of the effectiveness of internal control over financial reporting included in management's report referred to above. Our responsibility is to express opinions on the Company's consolidated financial statements and on the Company's internal control over financial reporting based on our audits. We are a public accounting firm registered with the Public Company Accounting Oversight Board (United States) (PCAOB) and are required to be independent with respect to the Company in accordance with the U.S. federal securities laws and the applicable rules and regulations of the Securities and Exchange Commission and the PCAOB.



We conducted our audits in accordance with the standards of the PCAOB. Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the consolidated financial statements are free of material misstatement, whether due to error or fraud, and whether effective internal control over financial reporting was maintained in all material respects.

Our audits of the consolidated financial statements included performing procedures to assess the risks of material misstatement of the consolidated financial statements, whether due to error or fraud, and performing procedures that respond to those risks. Such procedures included examining, on a test basis, evidence regarding the amounts and disclosures in the consolidated financial statements. Our audits also included evaluating the accounting principles used and significant estimates made by management, as well as evaluating the overall presentation of the consolidated financial statements. Our audit of internal control over financial reporting included obtaining an understanding of internal control over financial reporting, assessing the risk that a material weakness exists, and testing and evaluating the design and operating effectiveness of internal control based on the assessed risk. Our audits also included performing such other procedures as we considered necessary in the circumstances. We believe that our audits provide a reasonable basis for our opinions.

As described in Management's Annual Report on Internal Control Over Financial Reporting, management has excluded Direct Conversion AB from its assessment of internal control over financial reporting as of September 27, 2019 because it was acquired by the Company in a purchase business combination during the fiscal year ended September 27, 2019. We have also excluded Direct Conversion AB from our audit of internal control over financial reporting. Direct Conversion AB is a wholly-owned subsidiary whose total assets and total revenues excluded from management's assessment and our audit of internal control over financial reporting represent 0.8% and 0.8%, respectively, of the related consolidated financial statement amounts as of and for the year ended September 27, 2019.

### ***Definition and Limitations of Internal Control over Financial Reporting***

A company's internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. A company's internal control over financial reporting includes those policies and procedures that (i) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; (ii) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and (iii) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the company's assets that could have a material effect on the financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

### ***Critical Audit Matters***

The critical audit matters communicated below are matters arising from the current period audit of the consolidated financial statements that were communicated or required to be communicated to the audit committee and that (i) relate to accounts or disclosures that are material to the consolidated financial statements and (ii) involved our especially challenging, subjective, or complex judgments. The communication of critical audit matters does not alter in any way our opinion on the consolidated financial statements, taken as a whole, and we are not, by communicating the critical audit matters below, providing separate opinions on the critical audit matters or on the accounts or disclosures to which they relate.

### ***Consolidated Financial Statements - Impact of Resources and Controls Related to Risk Assessment and Financial Reporting***

The completeness and accuracy of the consolidated financial statements, including the financial condition, results of operations and cash flows, is dependent on, in part, (i) designing and maintaining monitoring controls related to the identification and assessment of risk in the business process environment, (ii) designing and maintaining financial reporting controls, including information technology general controls, and financial reporting close controls related to review of international operations, intercompany balances, post-close events and the statement of cash flows, and (iii) maintaining sufficient resources to create the proper environment for effective internal control over financial reporting.



The principal considerations for our determination that performing procedures relating to the consolidated financial statements - impact of resources and controls related to risk assessment and financial reporting is a critical matter are there was a high degree of auditor judgment, subjectivity and effort in performing procedures and evaluating audit evidence related to information systems and businesses processes, which affect substantially all financial statement account balances and disclosures. As described above in the “Opinions on the Financial Statements and Internal Control over Financial Reporting” section, material weaknesses were identified as of September 27, 2019 related to (i) ineffective risk assessment, (ii) ineffective control environment, and (iii) the financial reporting close process. Additionally, as previously disclosed by management, material weaknesses related to (i) information technology general controls and (ii) accounting for the Company’s operations in Germany existed during the year ended September 27, 2019.

Addressing the matter involved performing procedures and evaluating audit evidence in connection with forming our overall opinion on the financial statements. These procedures included, among others, evaluating the nature and extent of audit procedures performed and evidence obtained. These procedures also included manually testing the completeness and accuracy of system reports or other information generated by the Company's Information Technology (IT) systems.

#### *Revenue Recognition, including Adoption of the New Revenue Accounting Standard*

As described in Notes 1 and 18 to the consolidated financial statements, the Company’s consolidated revenue was \$780.6 million for the year ended September 27, 2019. Effective September 29, 2018, the Company adopted the new revenue accounting standard. The Company determines revenue recognition through the following steps: identification of the contract, or contracts, with a customer, identification of the performance obligations in the contract, determination of the transaction price, allocation of the transaction price to the performance obligations in the contract, and recognition of revenue when, or as, a performance obligation is satisfied. The Company’s revenues are derived primarily from the sale of hardware and services and are recognized net of any value-added or sales tax and net of sales discounts.

The principal considerations for our determination that performing procedures relating to revenue recognition, including adoption of the new revenue accounting standard, is a critical audit matter are there was a high degree of auditor judgment, subjectivity and effort in performing procedures and in evaluating the audit evidence obtained related to revenue recognition, including the adoption of the new revenue accounting standard. As described above in the “Opinions on the Financial Statements and Internal Control over Financial Reporting” section, a material weakness was identified as of September 27, 2019 related to the accounting for revenue, deferred revenue and related accounts receivable, specifically including the review of the completeness and accuracy of customer order entry, quantity and pricing, and the effect of the adoption of and continuous accounting for revenue from contracts with customers.

Addressing the matter involved performing procedures and evaluating audit evidence in connection with forming our overall opinion on the consolidated financial statements. These procedures included, among others, evaluating management’s process for determining the application of the new revenue accounting standard to the Company’s revenue, evaluating the reasonableness of management’s judgments, and evaluating the impacts of adoption identified by management. Testing management’s application of the new revenue accounting standard included examining revenue arrangements on a test basis, including assessing the terms and conditions of the arrangement and performing procedures to test the adjustments recorded upon adoption. These procedures also included (i) manually testing the completeness and accuracy of system reports or other information generated by the Company’s IT systems and (ii) evaluating the nature and extent of audit procedures performed and evidence obtained.

#### *Inventories*

As described in Note 1 to the consolidated financial statements, the Company’s consolidated inventory balance was \$248.2 million as of September 27, 2019. The Company values inventories at the lower of cost or net realizable value. Costs include materials, labor and manufacturing overhead and is computed using standard cost (which approximates actual cost) on a first-in-first-out basis. The Company evaluates the carrying value of its inventories taking into consideration such factors as historical and anticipated future sales compared to quantities on hand and the prices the Company expects to obtain for products in its various markets. The Company adjusts excess and obsolete inventories to net realizable value and write-downs of excess and obsolete inventories are recorded as a component of cost of revenues.

The principal considerations for our determination that performing procedures relating to inventories is a critical audit matter are there was a high degree of auditor judgment, subjectivity and effort in performing procedures and in evaluating audit evidence related to the existence and valuation of inventory. As described above in the “Opinions on the Financial Statements and Internal Control over Financial Reporting” section, a material weakness was identified as of September 27, 2019 related to accounting for inventory and



cost of revenue, specifically including maintaining effective controls related to inventory count procedures, the valuation of inventory at lower of cost and net realizable value, and presentation and disclosure of inventory classifications.

Addressing the matter involved performing procedures and evaluating audit evidence in connection with forming our overall opinion on the consolidated financial statements. These procedures included, among others, performing procedures to test the existence of inventories and evaluating and testing management's process for determining the valuation of inventories. These procedures also included (i) manually testing the completeness and accuracy of system reports or other information generated by the Company's IT systems and (ii) evaluating the nature and extent of audit procedures performed and evidence obtained.

#### *Acquisition of Direct Conversion AB - Intangible Assets*

As described in Note 2 to the consolidated financial statements, the Company completed the acquisition of Direct Conversion AB for net consideration of \$79.4 million in 2019, which resulted in \$32.9 million of intangible assets being recorded. Those intangible assets were comprised primarily of developed technology of \$18.4 million and customer relationships of \$9.0 million. Intangibles were valued primarily using a discounted cash flow, which included estimated revenue growth and discount rate.

The principal considerations for our determination that performing procedures relating to the intangible assets recorded with the acquisition of Direct Conversion AB is a critical audit matter are there was a high degree of auditor judgment and subjectivity in applying procedures relating to the fair value measurement of intangible assets acquired due to the significant judgment by management when developing the fair value of the intangible assets. Significant audit effort was required in performing procedures to evaluate the discounted cash flow, the estimated revenue growth, and the discount rate. The audit effort also involved the use of professionals with specialized skill and knowledge.

Addressing the matter involved performing procedures and evaluating audit evidence in connection with forming our overall opinion on the financial statements. These procedures included testing the effectiveness of controls relating to the acquisition accounting, including controls over management's valuation of intangible assets and controls over development of the assumptions related to the valuation of intangible assets, including discounted cash flow, estimated revenue growth, and the discount rate. These procedures also included, among others (i) reading the purchase agreement, (ii) testing management's process for estimating the fair value of intangible assets, and (iii) testing the completeness and accuracy of the data used in the discounted cash flow and evaluating the reasonableness of significant assumptions, including the discounted cash flow, the estimated revenue growth and the discount rate. Evaluating the reasonableness of the discounted cash flow, including the revenue growth, involved considering the past performance of the acquired business, as well as economic and industry forecasts, and considering whether they were consistent with evidence obtained in other areas of the audit. Professionals with specialized skill and knowledge were used to assist in evaluating the appropriateness of the valuation methods and evaluating significant assumptions, including the discount rate.

/s/ PricewaterhouseCoopers LLP

Salt Lake City, Utah  
December 20, 2019

We have served as the Company's auditor since 2016.

**VAREX IMAGING CORPORATION**  
**CONSOLIDATED STATEMENTS OF EARNINGS**

(In millions, except per share amounts)	Fiscal Years		
	2019	2018	2017
Revenues, net	\$ 780.6	\$ 773.4	\$ 698.1
Cost of revenues	523.9	519.5	444.6
Gross margin	256.7	253.9	253.5
Operating expenses:			
Research and development	78.1	83.0	67.3
Selling, general and administrative	128.1	123.4	102.5
Impairment of intangible assets	4.8	3.0	—
Total operating expenses	211.0	209.4	169.8
Operating earnings	45.7	44.5	83.7
Interest income	0.1	0.2	0.2
Interest expense	(21.1)	(21.7)	(12.3)
Other (expense) income, net	(3.2)	2.7	3.2
Interest and other expenses, net	(24.2)	(18.8)	(8.9)
Earnings before taxes	21.5	25.7	74.8
Taxes (benefit) on earnings	5.7	(2.6)	22.8
Net earnings	15.8	28.3	52.0
Less: Net earnings attributable to noncontrolling interests	0.3	0.8	0.4
Net earnings attributable to Varex	\$ 15.5	\$ 27.5	\$ 51.6
<b>Net earnings per common share attributable to Varex</b>			
Basic	\$ 0.41	\$ 0.73	\$ 1.37
Diluted	\$ 0.40	\$ 0.72	\$ 1.36
<b>Weighted average common shares outstanding</b>			
Basic	38.2	37.9	37.6
Diluted	38.6	38.4	38.0

*See accompanying notes to the consolidated financial statements.*

**VAREX IMAGING CORPORATION**  
**CONSOLIDATED STATEMENTS OF COMPREHENSIVE EARNINGS**

<b>(In millions)</b>	<b>Fiscal Years</b>		
	<b>2019</b>	<b>2018</b>	<b>2017</b>
Net earnings	\$ 15.8	\$ 28.3	\$ 52.0
Other comprehensive (loss) earnings, net of tax:			
Unrealized (loss) gain on interest rate swap contracts	(6.2)	5.2	0.6
Unrealized (loss) gain on defined benefit obligations	(1.3)	(0.2)	0.2
Other comprehensive (loss) earnings, net of tax	(7.5)	5.0	0.8
Comprehensive earnings	8.3	33.3	52.8
Less: Comprehensive earnings attributable to noncontrolling interests	0.3	0.8	0.4
Comprehensive earnings attributable to Varex	\$ 8.0	\$ 32.5	\$ 52.4

*See accompanying notes to the consolidated financial statements.*

**VAREX IMAGING CORPORATION**  
**CONSOLIDATED BALANCE SHEETS**

(In millions, except share amounts)	September 27, 2019	September 28, 2018
<b>Assets</b>		
Current assets:		
Cash and cash equivalents	\$ 29.9	\$ 51.9
Accounts receivable, net of allowance for doubtful accounts of \$1.0 and \$0.6 at September 27, 2019 and September 28, 2018, respectively	141.0	154.0
Inventories	248.2	235.1
Prepaid expenses and other current assets	19.3	17.1
Total current assets	\$ 438.4	\$ 458.1
Property, plant and equipment, net	142.3	144.9
Goodwill	290.8	243.6
Intangibles assets, net	86.3	73.8
Investments in privately-held companies	53.6	51.0
Other assets	27.5	16.5
<b>Total assets</b>	<b>\$ 1,038.9</b>	<b>\$ 987.9</b>
<b>Liabilities, redeemable noncontrolling interests and stockholders' equity</b>		
Current liabilities:		
Accounts payable	\$ 58.2	\$ 66.3
Accrued liabilities	75.7	47.5
Current maturities of long-term debt	30.7	25.0
Deferred revenues	10.5	13.2
Total current liabilities	\$ 175.1	\$ 152.0
Long-term debt, net	364.4	364.8
Deferred tax liabilities	8.2	23.2
Other long-term liabilities	32.5	8.5
Total liabilities	\$ 580.2	\$ 548.5
Commitments and contingencies (Note 11)		
Redeemable noncontrolling interests	10.5	11.1
Equity:		
Preferred stock, \$.01 par value: 20,000,000 shares authorized, none issued	—	—
Common stock, \$.01 par value: 150,000,000 shares authorized		
Shares issued and outstanding: 38,371,305 and 38,026,597 at September 27, 2019 and September 28, 2018, respectively	0.4	0.4
Additional paid-in capital	371.8	357.6
Accumulated other comprehensive (loss) income	(1.7)	5.8
Retained earnings	74.4	62.4
Total Varex stockholders' equity	\$ 444.9	\$ 426.2
Noncontrolling interests	3.3	2.1
Total stockholders' equity	\$ 448.2	\$ 428.3

<b>Total liabilities, redeemable noncontrolling interests and stockholders' equity</b>	<b>\$</b>	<b>1,038.9</b>	<b>\$</b>	<b>987.9</b>
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*See accompanying notes to the consolidated financial statements.*

**VAREX IMAGING CORPORATION**  
**CONSOLIDATED STATEMENTS OF CASH FLOWS**

(In millions)	Fiscal Years		
	2019	2018	2017
<b>Cash flows from operating activities:</b>			
Net earnings	\$ 15.8	\$ 28.3	\$ 52.0
Adjustments to reconcile net earnings to net cash provided by operating activities:			
Share-based compensation expense	11.7	10.0	8.4
Depreciation	23.5	26.0	16.9
Amortization of intangible assets	15.7	16.2	10.5
Impairment of intangible assets	4.8	3.0	—
Other assets impairment charges	—	1.3	—
Inventory write-down	3.1	3.1	—
Deferred taxes	(12.9)	(7.7)	(8.9)
Amortization of deferred loan costs	2.4	2.3	1.8
Loss (gain) from equity method investments, net of dividends received	2.3	(3.9)	(1.3)
Other, net	0.8	0.7	1.8
Changes in assets and liabilities, net of effects of acquisitions:			
Accounts receivable	14.8	9.0	(23.1)
Inventories	(11.1)	(2.4)	(4.2)
Prepaid expenses and other assets	4.3	2.0	(10.1)
Accounts payable	(9.0)	5.2	4.9
Accrued operating liabilities and other long-term operating liabilities	10.9	(10.2)	28.1
Deferred revenues	(5.2)	2.4	(1.6)
Net cash provided by operating activities	71.9	85.3	75.2
<b>Cash flows from investing activities:</b>			
Purchases of property, plant and equipment	(19.8)	(20.4)	(20.2)
Acquisitions of businesses, net of cash acquired	(69.5)	(4.8)	(271.8)
Investments in privately-held companies	(3.9)	—	—
Net cash used in investing activities	(93.2)	(25.2)	(292.0)
<b>Cash flows from financing activities:</b>			
Net transfers from parent	—	—	5.0
Distributions to Varian Medical Systems, Inc.	—	—	(227.1)
Taxes related to net share settlement of equity awards	(2.1)	(2.3)	(1.9)
Borrowings under credit agreements	85.4	10.0	749.0
Repayments of borrowing under credit agreements	(87.0)	(106.0)	(255.0)
Proceeds from exercise of stock options	0.8	3.8	2.8
Proceeds from shares issued under employee stock purchase plan	3.8	3.3	—
Excess tax benefits from share-based compensation	—	—	2.4
Payment of debt issuance costs	(0.5)	(0.4)	(11.9)
Contributions from noncontrolling partner	—	1.8	—
Dividends paid to redeemable noncontrolling interest	(0.5)	(0.6)	—
Net cash (used in) provided by financing activities	(0.1)	(90.4)	263.3
Effects of exchange rate changes on cash and cash equivalents and restricted cash	(0.7)	(0.5)	0.9
Net (decrease) increase in cash and cash equivalents and restricted cash	(22.1)	(30.8)	47.4

Cash and cash equivalents and restricted cash at beginning of period	53.4	84.2	36.8
Cash and cash equivalents and restricted cash at end of period	<u>\$ 31.3</u>	<u>\$ 53.4</u>	<u>\$ 84.2</u>
Supplemental cash flow information:			
Cash paid for interest	\$ 19.9	\$ 19.3	\$ 9.8
Cash paid for income tax	8.2	13.8	6.0
Supplemental non-cash activities:			
Purchases of property, plant and equipment financed through accounts payable	\$ 1.8	\$ 2.0	\$ 4.0
Transfers of property, plant and equipment from Varian Medical Systems, Inc.	—	—	15.0
Other non-cash transfers to Varian Medical Systems, Inc.	—	—	1.6

*See accompanying notes to the consolidated financial statements.*

# VAREX IMAGING CORPORATION

## CONSOLIDATED STATEMENTS OF EQUITY

(In millions)	Common Stock		Additional Paid-in Capital	Net Parent Investment	Accumulated Other Comprehensive Income (Loss)	Retained Earnings	Total Varex Equity	Noncontrolling Interests	Total Stockholders' Equity
	Shares	Amount							
<b>September 30, 2016</b>	—	—	—	526.0	—	—	526.0	—	526.0
Net earnings	—	—	—	16.5	—	35.1	51.6	—	51.6
Net transfers from parent	—	—	—	18.4	—	—	18.4	—	18.4
Distribution to Varian Medical Systems	—	—	—	(227.1)	—	—	(227.1)	—	(227.1)
Conversion of net parent investment into common stock	37.4	0.4	333.4	(333.8)	—	—	—	—	—
Exercise of stock options	0.1	—	2.8	—	—	—	2.8	—	2.8
Common stock issued upon vesting of restricted shares	0.2	—	—	—	—	—	—	—	—
Shares withheld on vesting of restricted stock	(0.1)	—	(1.9)	—	—	—	(1.9)	—	(1.9)
Share-based compensation	—	—	6.2	—	—	—	6.2	—	6.2
Unrealized gain on interest rate swap contracts, net of tax	—	—	—	—	0.6	—	0.6	—	0.6
Unrealized gain on defined benefit obligations, net of tax	—	—	—	—	0.2	—	0.2	—	0.2
Tax impacts to APIC related to share-based award activity	—	—	2.4	—	—	—	2.4	—	2.4
Other	—	—	(0.2)	—	—	—	(0.2)	—	(0.2)
<b>September 29, 2017</b>	<b>37.6</b>	<b>0.4</b>	<b>342.7</b>	<b>—</b>	<b>0.8</b>	<b>35.1</b>	<b>379.0</b>	<b>—</b>	<b>379.0</b>
Net earnings	—	—	—	—	—	27.5	27.5	0.3	27.8
Exercise of stock options	0.2	—	3.8	—	—	—	3.8	—	3.8
Common stock issued upon vesting of restricted shares	0.2	—	—	—	—	—	—	—	—
Shares withheld on vesting of restricted stock	(0.1)	—	(2.2)	—	—	—	(2.2)	—	(2.2)
Common stock issued under employee stock purchase plan	0.1	—	3.3	—	—	—	3.3	—	3.3
Share-based compensation	—	—	10.0	—	—	—	10.0	—	10.0
Unrealized gain on interest rate swap contracts, net of tax	—	—	—	—	5.2	—	5.2	—	5.2
Unrealized loss on defined benefit obligations, net of tax	—	—	—	—	(0.2)	—	(0.2)	—	(0.2)
Capital contribution by noncontrolling interest	—	—	—	—	—	—	—	1.8	1.8
Other	—	—	—	—	—	(0.2)	(0.2)	—	(0.2)
<b>September 28, 2018</b>	<b>38.0</b>	<b>\$ 0.4</b>	<b>\$ 357.6</b>	<b>\$ —</b>	<b>\$ 5.8</b>	<b>\$ 62.4</b>	<b>\$ 426.2</b>	<b>\$ 2.1</b>	<b>\$ 428.3</b>
Effect of adoption of ASC 606	—	—	—	—	—	(3.5)	(3.5)	—	(3.5)
Net earnings	—	—	—	—	—	15.5	15.5	(0.2)	15.3
Exercise of stock options	—	—	0.8	—	—	—	0.8	—	0.8
Common stock issued upon vesting of restricted shares	0.2	—	—	—	—	—	—	—	—
Shares withheld on vesting of restricted stock	—	—	(2.1)	—	—	—	(2.1)	—	(2.1)
Common stock issued under employee stock purchase plan	0.2	—	3.8	—	—	—	3.8	—	3.8
Share-based compensation	—	—	11.7	—	—	—	11.7	—	11.7
Unrealized loss on interest rate swap contracts, net of tax	—	—	—	—	(6.2)	—	(6.2)	—	(6.2)
Unrealized loss on defined benefit obligations, net of tax	—	—	—	—	(1.3)	—	(1.3)	—	(1.3)
Noncontrolling interest acquired/consolidated	—	—	—	—	—	—	—	1.4	1.4
<b>September 27, 2019</b>	<b>38.4</b>	<b>\$ 0.4</b>	<b>\$ 371.8</b>	<b>\$ —</b>	<b>\$ (1.7)</b>	<b>\$ 74.4</b>	<b>\$ 444.9</b>	<b>\$ 3.3</b>	<b>\$ 448.2</b>

*See accompanying notes to the consolidated financial statements.*



## **VAREX IMAGING CORPORATION**

### **NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

#### **1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES**

##### ***Description of Business***

Varex Imaging Corporation (the “Company,” “Varex” or “Varex Imaging”) designs, manufactures, sells and services a broad range of Medical products, which include X-ray imaging components, including X-ray tubes, digital detectors and accessories, high voltage connectors, image processing software and workstations, computer-aided diagnostic software, collimators, automatic exposure control devices, generators, ionization chambers and buckys, for use in a range of applications, including radiographic or fluoroscopic imaging, mammography, computed tomography, oncology and computer-aided detection. The Company sells its products to imaging system original equipment manufacturer (“OEM”) customers for incorporation into new medical diagnostic, radiation therapy, dental, and veterinary, to independent service companies, distributors and directly to end-users for replacement purposes.

The Company also designs, manufactures, sells and services industrial products, which include Linatron® X-ray accelerators, imaging processing software and image detection products for security and inspection purposes, such as cargo screening at ports and borders and nondestructive examination in a variety of applications. The Company generally sells security and inspection products to OEM customers who incorporate Varex’s products into their inspection systems. The Company conducts an active research and development program to focus on new technology and applications in both the medical and industrial X-ray imaging markets.

Varex Imaging Corporation was incorporated in Delaware on July 18, 2016 for the purpose of holding the assets and liabilities associated with the Company's business and separated from Varian Medical Systems, Inc. (“Varian”) on January 28, 2017, upon which Varian completed the distribution of 100% of the outstanding common stock of Varex to Varian stockholders. Following the separation and distribution, Varex became an independent publicly-traded company and is listed on the NASDAQ Global Select Market under the ticker “VREX.”

##### ***Basis of Presentation and Principle of Consolidation***

The accompanying consolidated financial statements are audited and have been prepared by the Company pursuant to the rules and regulations of the Securities and Exchange Commission (“SEC”) and prepared in accordance with accounting principles generally accepted in the United States (“GAAP”). Prior to January 28 2017, the date of separation and distribution, the financial statements were prepared on a stand-alone basis and were derived from Varian’s consolidated financial statements and records as it operated as part of Varian prior to the distribution, in conformity with GAAP. Prior to the separation and distribution, the consolidated financial statements included allocations of certain Varian corporate expenses these costs were allocated to the Company on the basis of direct usage when identifiable or other systematic measures that reflect utilization of services provided to or benefits received by the Company.

All transactions between the Company and Varian prior to the separation have been included in the accompanying consolidated financial statements. All intercompany transactions while the Company operated as part of Varian were considered to be effectively settled for cash and are reflected as a component of financing activities as net transfers from (to) Varian in the consolidated statements of cash flows at the time the transactions were recorded.

Prior to the separation, the Company was dependent upon Varian for its working capital and financing requirements, as Varian uses a centralized approach to cash management and financing of its operations. Financial transactions relating to the Company were accounted for through the net parent investment account. Cash and cash equivalents held by Varian were not allocated to the Company.

Net parent investment in the consolidated statements of equity represents Varian’s historical investment in the Company, the net effect of transactions with and allocations from Varian and the Company’s accumulated earnings.

##### ***Reclassification***

The Company has reclassified \$3.0 million from selling, general and administrative expense to impairment of intangible assets for the year ended September 28, 2018, to conform to the current year's presentation. Such reclassifications had no impact on net earnings as previously reported.

## Segment Reporting

The Company has two reportable operating segments; (i) Medical and (ii) Industrial, which aligns with how its CEO, who is the Company's Chief Operating Decision Maker ("CODM"), reviews the Company's performance. See Note 15. *Segment Information*, included in this report, for further information on the Company's segments.

## Fiscal Year

The fiscal years of the Company as reported are the 52 or 53-week period ending on the Friday nearest September 30. Fiscal year 2019 was the 52-week period that ended on September 27, 2019. Fiscal year 2018 was the 52-week period that ended on September 28, 2018. Fiscal year 2017 was the 52-week period that ended on September 29, 2017.

## Variable Interest Entities

For entities in which the Company has variable interests, the Company focuses on identifying which entity has the power to direct the activities that most significantly impact the variable interest entity's economic performance and which enterprise has the obligation to absorb losses or the right to receive benefits from the variable interest entity. If the Company is the primary beneficiary of a variable interest entity, the assets, liabilities and results of operations of the variable interest entity will be included in the Company's consolidated financial statements. As of September 27, 2019, the Company had two variable interest entities neither of which were consolidated.

## Use of Estimates

The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the consolidated financial statements and the reported amounts of revenues and expenses during the reporting periods. Such estimates include the valuation of inventories, goodwill and intangible assets, impairment on investments, and taxes on earnings. Actual results could differ from these estimates.

## Cash and Cash Equivalents

The Company considers currency on hand, demand deposits, time deposits and all highly-liquid investments with an original maturity of three months or less at the date of purchase to be cash and cash equivalents.

## Restricted Cash

Restricted cash primarily consists of cash collateral related to certain leases and inventory arrangements. Restricted cash is included in other assets on the consolidated balance sheet. Cash and cash equivalents and restricted cash as reported within the consolidated statements of cash flows consisted of the following:

	Twelve Months Ended September 27, 2019		Twelve Months Ended September 28, 2018	
	Beginning of Period	End of Period	Beginning of Period	End of Period
Cash and cash equivalents	\$ 51.9	\$ 29.9	\$ 83.3	\$ 51.9
Restricted cash	1.5	1.4	0.9	1.5
Cash and cash equivalents and restricted cash as reported per statement of cash flows	<u>\$ 53.4</u>	<u>\$ 31.3</u>	<u>\$ 84.2</u>	<u>\$ 53.4</u>

## Fair Value

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

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



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

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

### ***Derivative instruments and hedging activities***

The Company records all derivatives on the balance sheet at fair value. Derivatives designated as a hedge are recorded on the Consolidated Balance Sheets at fair value as of the reporting date. For derivative instruments that are designated and qualify as cash flow hedges, the gain or loss on the derivative is reported as a component of other comprehensive income or loss and reclassified from accumulated other comprehensive loss into earnings when the hedged transaction affects earnings. For derivatives that are designated and qualify as net investment hedges, the gain or loss on the derivative is reported as a component of other comprehensive income or loss. Time value is excluded and the cash payments are recognized as an adjustment to interest expense. A qualitative assessment of hedge effectiveness is performed on a quarterly basis, unless facts and circumstances indicate the hedge may no longer be highly effective.

### ***Concentration of Risk***

Financial instruments that potentially expose the Company to concentrations of credit risk consist principally of cash, cash equivalents and trade accounts receivable. Cash held with financial institutions may exceed the Federal Deposit Insurance Corporation insurance limits or similar limits in foreign jurisdictions. The Company has not experienced any losses on its deposits of cash and cash equivalents. The Company performs ongoing credit evaluations of its customers and, except for government tenders, group purchases and orders with a letter of credit, its industrial customers often provide a down payment. The Company maintains an allowance for doubtful accounts based upon the expected collectability of all accounts receivable. The Company obtains some of the components in its products from a limited group of suppliers or from a single-source supplier. The Company has neither experienced nor expects any significant disruptions to its operations due to supplier concentration.

Credit is extended to customers based on an evaluation of the customer's financial condition, and collateral is not required. During the periods presented, one of the Company's Medical segment customers accounted for a significant portion of revenues, which is as follows:

	Fiscal Year		
	2019	2018	2017
Canon Medical Systems Corporation	17.3%	18.1%	19.3%

Canon Medical Systems Corporation accounted for 10.1% and 9.8% of the Company's accounts receivable as of September 27, 2019 and September 28, 2018, respectively.

### ***Inventories***

Inventories are valued at the lower of cost or net realizable value. Costs include materials, labor and manufacturing overhead and is computed using standard cost (which approximates actual cost) on a first-in-first-out basis. The Company evaluates the carrying value of its inventories taking into consideration such factors as historical and anticipated future sales compared to quantities on hand and the prices the Company expects to obtain for products in its various markets. The Company adjust excess and obsolete inventories to net realizable value and write-downs of excess and obsolete inventories are recorded as a component of cost of revenues.

The following table summarizes the Company's inventories, net:

(In millions)	September 27, 2019	September 28, 2018
Raw materials and parts	\$ 160.1	\$ 149.9
Work-in-process	27.9	25.4
Finished goods	60.2	59.8
Total inventories	<u>\$ 248.2</u>	<u>\$ 235.1</u>

### ***Property, Plant and Equipment, net***

Property, plant and equipment are stated at cost, net of accumulated depreciation. Major improvements are capitalized, while repairs and maintenance are expensed as incurred. Depreciation are computed using the straight-line method over the estimated useful lives of the assets. Land is not subject to depreciation, but land improvements are depreciated over fifteen years. Land leasehold rights and leasehold improvements are depreciated over the lesser of their estimated useful lives or remaining lease terms. Buildings are depreciated over twenty years. Machinery and equipment are depreciated over their estimated useful lives, which range from three years to seven years. Assets subject to lease are depreciated over the lesser of their estimated useful lives or remaining lease terms. Estimated useful lives are periodically reviewed and, when appropriate, changes are made prospectively. When certain events or changes in operating conditions occur, asset lives may be adjusted, and an impairment assessment may be performed on the recoverability of the carrying amounts. When assets are retired or otherwise disposed of, the assets and related accumulated depreciation are removed from the accounts.

The following table summarizes the Company's property, plant and equipment, net:

<b>(In millions)</b>	<b>September 27, 2019</b>	<b>September 28, 2018</b>
Land	\$ 8.3	\$ 8.3
Buildings and leasehold improvements	134.4	138.1
Machinery	170.7	166.1
Construction in progress	28.5	23.1
	<u>\$ 341.9</u>	<u>\$ 335.6</u>
Accumulated depreciation and amortization	(199.6)	(190.7)
Property, plant, and equipment, net	<u>\$ 142.3</u>	<u>\$ 144.9</u>

The Company recorded depreciation expense of \$23.5 million, \$26.0 million and \$16.9 million, in fiscal years 2019, 2018 and 2017, respectively. During fiscal year 2019 the company recorded accelerated depreciation of \$4.5 million on the machinery and equipment used in the fabrication of amorphous silicon glass at its facility in Santa Clara, CA. See Note 4. *Restructuring*, included in this report, for further information. During fiscal year 2018 the company recorded accelerated depreciation of \$4.2 million on the machinery and equipment used in the fabrication of amorphous silicon glass at its facility in Santa Clara, CA. See Note 4. *Restructuring*, included in this report, for further information.

### ***Investments***

The Company accounts for its equity investments in privately-held companies under the equity method of accounting if the Company has the ability to exercise significant influence in these investments. Distributions received from an equity method investment are classified using the cumulative earnings approach. Under the cumulative earnings approach, distributions up to the amount of cumulative equity in earnings recognized will be treated as returns on investment as operating cash flows and those in excess of that amount will be treated as returns of investment as investing cash flows. The Company monitors these equity investments for impairment and makes appropriate reductions in carrying values if the Company determines that impairment charges are required based primarily on the financial condition and near-term prospects of these companies.

### ***Goodwill and Intangible Assets***

Goodwill is recorded when the purchase price of an acquisition exceeds the fair value of the net identified tangible and intangible assets acquired. Purchased intangible assets are carried at cost, net of accumulated amortization, and are included in intangible assets in the Company's consolidated balance sheets. Intangible assets with finite lives are amortized over their estimated useful lives of primarily two years to seven years using the straight-line method.

### ***Impairment of Long-lived Assets, Intangible Assets and Goodwill***

The Company reviews long-lived assets and identifiable intangible assets with finite lives for impairment whenever events or changes in circumstances indicate that the carrying amount of these assets may not be recoverable. The Company assesses these assets for impairment based on their estimated undiscounted future cash flows. If the carrying value of the assets exceeds the estimated future undiscounted cash flows, the Company recognizes an impairment loss based on the excess of the carrying amount over the fair value of the assets.



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

During the fiscal year ended September 27, 2019 and 2018, the Company recognized \$4.8 million and \$3.0 million of impairments of intangible assets related to the restructuring activities see Note 4. *Restructuring*, included in this report. No goodwill impairment charges were recognized for any of the prior periods presented. No impairment charges were recognized in fiscal year 2017.

### ***Loss Contingencies***

From time to time, the Company is a party to or otherwise involved in legal proceedings, claims and government inspections or investigations, customs and duties audits and other loss contingency matters, both inside and outside the United States, arising in the ordinary course of its business or otherwise. The Company accrues amounts, to the extent an unfavorable outcome is determined to be probable and the losses can be reasonably estimated, that it believes are adequate to address any liabilities related to legal proceedings and other loss contingencies that it believes will result in a probable loss.

### ***Product Warranty***

The Company warrants most of its products for a specific period of time, usually 12 to 24 months from delivery or acceptance, against material defects. The Company provides for the estimated future costs of warranty obligations in cost of revenues when the related revenues are recognized. The accrued warranty costs represent the best estimate at the time of sale of the total costs that the Company will incur to repair or replace product parts that fail while still under warranty.

The amount of the accrued estimated warranty costs obligation for established products is primarily based on historical experience as to product failures adjusted for current information on repair costs. For new products, estimates include the historical experience of similar products, as well as a reasonable allowance for warranty expenses associated with new products. On a quarterly basis, the Company reviews the accrued warranty costs and updates the historical warranty cost trends, if required.

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

(In millions)	Fiscal Years	
	2019	2018
Accrued product warranty, at beginning of period	\$ 7.3	\$ 7.0
Charged to cost of revenues	12.9	11.6
Actual product warranty expenditures	(12.1)	(11.3)
Accrued product warranty, at end of period	<u>\$ 8.1</u>	<u>\$ 7.3</u>

### ***Revenue Recognition***

Effective September 29, 2018, the Company adopted the requirements of Accounting Standards Update ("ASU") 2014-09 and related amendments, Revenue from Contracts with Customers ("ASC 606"), which superseded all prior revenue recognition methods and industry-specific guidance. See "Recently Adopted Accounting Pronouncements" below.

The Company's revenues are derived primarily from the sale of hardware and services. The Company recognizes its revenues net of any value-added or sales tax and net of sales discounts.

The Company sells a high proportion of its X-ray products to a limited number of OEM customers. X-ray tubes, digital detectors and image-processing tools and security and inspection products are generally sold on a stand-alone basis. However, the



Company occasionally sells its digital detectors, X-ray tubes and imaging processing tools as a package that is optimized for digital X ray imaging and sells its Linatron ® X-ray accelerators together with its imaging processing software and image detection products to OEM customers that incorporate them into their inspection systems. Service contracts are often sold with certain security and inspection products and computer-aided detection products.

The Company determines revenue recognition through the following steps:

- Identification of the contract, or contracts, with a customer
- Identification of the performance obligations in the contract
- Determination of the transaction price
- Allocation of the transaction price to the performance obligations in the contract
- Recognition of revenue when, or as, a performance obligation is satisfied

### ***Deferred Revenues***

Deferred revenue primarily represents (i) the amount received applicable to non-software products for which parts and services under the warranty contracts have not been delivered, and (ii) the amount received for service contracts for which the services have not been rendered.

### ***Allowance for Doubtful Accounts***

The Company evaluates the creditworthiness of customers prior to authorizing shipment for all major sale transactions. On a quarterly basis, the Company evaluates aged items in the accounts receivable aging report and provide an allowance in an amount deemed adequate for doubtful accounts. If the evaluation of customers' financial conditions does not reflect a future ability to collect outstanding receivables, additional provisions may be needed. We had an allowance for doubtful accounts of \$1.0 million and \$0.6 million as of September 27, 2019 and September 28, 2018, respectively.

### ***Share-Based Compensation Expense***

The Company has an equity-based incentive plan that provides for the grant of nonqualified stock options and restricted stock units to directors, officers and other employees. The Company also permits employees to purchase shares under the Varex employee stock purchase plan. Prior to the separation, the Company's employees historically participated in Varian's equity-based incentive plans. Share-based compensation expense through the date of separation included allocations to the Company based on the awards and terms previously granted to its employees as well as an allocation of Varian's corporate and shared functional employee expenses.

The Company values stock options granted and the option component of the shares of common stock purchased under the equity-based incentive plans and stock purchased under the employee stock purchase plan using the Black-Scholes option-pricing model. Share-based compensation expense for restricted stock units is measured using the fair value of the Company's stock on the date of grant and is amortized over the award's respective service period. The Black-Scholes option-pricing model requires the input of certain assumptions, and changes in the assumptions can materially affect the fair value estimates of share-based payment awards.

The Company measures and recognizes expense for all share-based payment awards based on their fair values. Share-based compensation expense recognized in the consolidated statements of earnings includes compensation expense for the share-based payment awards based on the grant date fair value estimated in accordance with the guidance on share-based compensation. Share-based compensation expense recognized is based on the value of the portion of share-based payment awards that is ultimately expected to vest. The Company attributes the value of share-based compensation to expense using the straight-line method. The Company considers only the direct tax impacts of share-based compensation awards when calculating the amount of tax windfalls or shortfalls. For additional information, see Note 13. *Employee Stock Plans*, included in this report.

### ***Shipping and Handling Costs***

Shipping and handling costs are included as a component of cost of revenues.

### ***Research and Development***

Research and development costs have been expensed as incurred. These costs primarily include employees' compensation, consulting fees and material costs.

### ***Software Development Costs***

Costs for the development of new software products and substantial enhancements to existing software products are expensed as incurred until technological feasibility has been established, at which time any additional costs would be capitalized. No costs associated with the development of software have been capitalized, as the Company believes its current software development process is essentially completed concurrent with the establishment of technological feasibility.

### ***Taxes on Earnings***

Current income tax expense is the amount of income taxes expected to be payable for the current year. Deferred income tax liabilities or assets are established for the expected future tax consequences resulting from the differences in financial reporting and tax bases of assets and liabilities. A valuation allowance is provided if it is more likely than not that some or all of the deferred tax assets will not be realized. In addition, we provide reserves for uncertain tax positions when such tax positions do not meet the recognition thresholds or measurement standards prescribed by the authoritative guidance for accounting for income taxes. Amounts for uncertain tax positions are adjusted in periods when new information becomes available or when positions are effectively settled. Interest and penalties related to uncertain tax positions are recognized as a component of income tax expense.

On December 22, 2017, the U.S. Government enacted comprehensive tax legislation commonly referred to as the Tax Cuts and Jobs Act of 2017 (“U. S. Tax Reform”). U.S. Tax Reform significantly revised the U.S. corporate income tax structure including a lower corporate statutory rate and changes to the way foreign earnings are taxed. U.S. GAAP requires that the impact of tax legislation be recognized in the period in which the law is enacted. In accordance with these rules, we are including the impact of certain provisions of U.S. Tax Reform to the extent they are effective during the current reporting period.

### ***Foreign Currency Translation***

The Company uses the U.S. Dollar predominately as the functional currency of its foreign operations. Gains and losses from remeasurement of foreign currency balances into U.S. Dollars are included in the consolidated statements of earnings. For the foreign subsidiary where the local currency is the functional currency, translation adjustments of foreign currency financial statements into U.S. dollars are recorded to a separate component of accumulated other comprehensive (loss) earnings.

### ***Accounting Standards Recently Adopted***

In November 2016, the Financial Accounting Standards Board (“FASB”) issued ASU 2016-18, Statement of Cash Flows (Topic 230): Restricted Cash (“ASU 2016-18”), which requires that the statement of cash flows explain the change in the total amount of restricted cash during the period and other additional disclosures. The Company adopted ASU 2016-18 in the first quarter of 2019 using the retrospective transition method and the Company's consolidated statements of cash flows have been retrospectively adjusted to reflect restricted cash balances. Net cash flows for fiscal years 2019, 2018 and 2017 did not change as a result of adopting ASU 2016-18.

The Company adopted ASU 2016-15, Statement of Cash Flows (Topic 230): Classification of Certain Cash Receipts and Cash Payments (“ASU 2016-15”), which was issued to reduce the diversity in practice in how certain transactions are classified in the statement of cash flows. The Company adopted ASU 2016-15 in the first quarter of 2019 retrospectively. Net cash flows for fiscal years 2019, 2018 and 2017 did not change as a result of adopting ASU 2016-15.

The Company adopted ASC 606 as of September 29, 2018, using the modified retrospective transition method applied to those contracts which were not completed as of that date. The Company recorded a net reduction to retained earnings of \$4.1 million, net of tax, as of September 29, 2018 due to the impact of adopting ASC 606. During the second quarter of 2019 the Company recorded an increase to retained earnings of \$0.6 million, net of tax, to correct an error that was not quantitatively or qualitatively material to the current period, related to the adoption of ASC 606. The net cumulative impact of adopting ASC 606 was \$3.5 million, net of tax. Refer to Note 18. *Revenue Recognition*, included in this report for the detailed impact of adopting ASC 606.

In August 2017, the FASB issued ASU 2017-12, Derivatives and Hedging (Topic 815): Targeted Improvements to Accounting for Hedging Activities, which amends the application of hedge accounting and improves financial reporting of hedging relationships to more accurately present the economic effects of risk management activities in the financial statements. The ASU is effective for public companies for annual reporting periods beginning after December 15, 2018, with early adoption permitted. The Company early adopted the provisions of ASU 2017-12 during the quarter ended September 27, 2019, using the modified retrospective method. The adoption did not have an impact on the consolidated financial statements.

### ***Recent Accounting Standards Updates Not Yet Effective***

In February 2018, the FASB issued ASU 2018-02, Income Statement-Reporting Comprehensive Income (Topic 220): Reclassification of Certain Tax Effects from Accumulated Other Comprehensive Income, which allows a reclassification from accumulated other comprehensive income to retained earnings for stranded tax effects resulting from U.S. federal tax legislation commonly referred to as the Tax Cuts and Jobs Act, which was enacted in December 2017 (the “2017 Tax Act”). ASU 2018-02 is effective for fiscal years beginning after December 15, 2018, and interim periods within those fiscal years. Early adoption is permitted. The Company does not expect that the adoption of this guidance will have a material impact on its consolidated financial statements.

In January 2017, the FASB issued ASU 2017-04 which clarified its guidance to simplify the measurement of goodwill by eliminating the Step 2 impairment test. The new guidance requires companies to perform the goodwill impairment test by comparing the fair value of a reporting unit with its carrying amount. The amendment will be effective for the Company beginning in its first quarter of fiscal year 2021. The amendment is required to be adopted prospectively. The Company is evaluating the impact of adopting this amendment to its consolidated financial statements.

In June 2016, the FASB issued ASU 2016-13, "Measurement of Credit Losses on Financial Instruments." This ASU replaces the incurred loss impairment methodology with a methodology that reflects expected credit losses and requires consideration of a broader range of reasonable and supportable information to inform credit loss estimates. In addition, the ASU requires new disclosures. This standard will be effective for the Company's interim and annual periods beginning with the first quarter of fiscal 2021, and must be applied on a modified retrospective basis. The Company is currently evaluating the potential impact of this standard.

In February 2016, the FASB issued ASU 2016-02 on accounting for leases. The new standard is intended to provide enhanced transparency and comparability by requiring lessees to record right-of-use assets and corresponding lease liabilities on the balance sheet. The new standard will continue to classify leases as either finance or operating, with classification affecting the pattern of expense recognition in the statement of earnings. The new standard is required to be adopted using a modified retrospective method to each prior reporting period presented with various optional practical expedients. The new standard will be effective for the Company beginning in its first quarter of fiscal year 2020 with early adoption permitted. The Company has not completed its assessment of the new standard, but anticipate that the most substantial change to its consolidated financial statements will be a gross-up of its total assets and liabilities. The adoption is not expected to materially impact our results of operations in the upcoming fiscal years and interim periods. The Company will continue to monitor the overall impact of adoption and update our disclosures as appropriate.

## **2. BUSINESS COMBINATIONS**

### ***Acquisition of Direct Conversion AB (publ)***

On April 29, 2019, Varex completed the acquisition of 98.2% of the outstanding shares of common stock of Direct Conversion AB (publ) (“Direct Conversion”) for \$69.5 million in cash, net of cash acquired, the assumption of Direct Conversion's debt of \$4.5 million and deferred consideration equal to \$9.9 million or 0.3 million shares of the Company’s common stock (subject to reduction to settle indemnity claims) to be paid on the first anniversary of the closing with a mixture of cash and shares of Varex common stock. The acquisition of Direct Conversion expands our detector product portfolio to include photon counting technology. This technology will allow Varex to expand its range of imaging applications and offer new solutions to both Medical and Industrial customers.

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The following table summarizes the preliminary purchase price allocation:

(In millions)	Fair Value
Allocation of the purchase consideration:	
Accounts receivable	\$ 2.4
Inventories	5.7
Prepaid expenses and other current assets	0.7
Property, plant, and equipment	0.9
Goodwill	47.2
Intangible assets	32.9
<b>Total assets acquired</b>	<b>89.8</b>
Accounts payable	(1.0)
Accrued liabilities	(1.5)
Current maturities of long-term debt	(1.0)
Deferred revenues	(0.9)
Long-term debt	(3.5)
Other long-term liabilities	(1.1)
<b>Total liabilities assumed</b>	<b>(9.0)</b>
<b>Noncontrolling interest</b>	<b>(1.4)</b>
<b>Net assets acquired, less noncontrolling interest</b>	<b>\$ 79.4</b>
Net cash paid	\$ 69.5
Deferred consideration	9.9
<b>Total consideration</b>	<b>\$ 79.4</b>

The Company recorded the assets acquired and liabilities assumed at their preliminary estimated fair values. Intangibles were valued primarily using a discounted cash flow, which included estimated revenue growth and discount rate. Due to the complexity of this transaction as of September 27, 2019, the Company had not finalized the determination of the fair values allocated to various assets and liabilities, including, but not limited to, inventory; deferred tax assets and liabilities; intangible assets and the residual amount allocated to goodwill. The fair value assigned to goodwill is primarily attributable to expected synergies. The goodwill related to the Direct Conversion acquisition is not tax deductible.

The following amounts represent the determination of the fair value and estimated weighted average useful lives of identifiable intangible assets for the Direct Conversion, which are amortized straight-line:

(In millions)	Fair Value	Estimated Weighted Average Useful Life (In Years)
Backlog	\$ 0.2	1
Trade names	2.5	5
Developed technology	18.4	10
In-process research and development	2.8	indefinite
Customer relationships	9.0	10
Total intangible assets acquired	<u>\$ 32.9</u>	

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The following amounts represent revenues by reporting segment from Direct Conversion from the acquisition date of April 29, 2019, through September 27, 2019:

<b>(In millions)</b>	<b>Direct Conversion Revenue</b>
Medical	\$ 4.5
Industrial	1.8
Total Direct Conversion revenues	<u>\$ 6.3</u>

The acquisition of Direct Conversion did not have a significant impact on our consolidated results of operations on a pro forma basis for the current or prior years.

### ***Acquisition of Virtual Media Integration***

On August 31, 2018, the Company completed the acquisition of Virtual Media Integration, Ltd. (“VMI”) from MISTRAS Group, Inc for \$4.8 million. VMI is a provider of computed and digital radiography and X-ray film digitizer systems for industrial non-destructive testing. The acquired assets and liabilities of the VMI business were allocated to the Industrial reporting segment. The acquisition related costs were included in the consolidated statements of earnings under selling, general and administrative expenses.

The following table summarizes the purchase price allocation:

<b>(In millions)</b>	<b>Fair Value</b>
Allocation of the purchase consideration:	
Accounts Receivable	\$ 0.2
Inventories	1.0
Other assets	0.2
Intangibles	1.6
Goodwill	1.5
Other liabilities	(0.2)
Net assets acquired	<u>4.3</u>
Post-closing adjustments	0.5
Total cash consideration	<u>\$ 4.8</u>

### ***Acquisition of PerkinElmer’s Medical Imaging Business***

On May 1, 2017, the Company completed the acquisition of the medical imaging business (“Acquired Detector Business”) of PerkinElmer, Inc. (“PKI”) for \$277.4 million, or \$273.2 million after post-closing working capital adjustments. The acquisition consisted of PerkinElmer Medical Holdings, Inc. and Dexela Limited, together with certain assets of PKI and its direct and indirect subsidiaries relating to digital flat panel X-ray detectors that serve as components for industrial, medical, dental and veterinary X-ray imaging systems. The Acquired Detector Business included about 280 employees, with operations in Santa Clara, California as well as operations in Germany, the Netherlands, China and the United Kingdom. The acquisition of the Acquired Detector Business was pursuant to the Master Purchase and Sale Agreement, dated December 21, 2016 (the “Purchase Agreement”), by and between PKI and Varian and the subsequent Assignment and Assumption Agreement, dated January 27, 2017, by and between Varian and Varex, pursuant to which Varian assigned and conveyed all of its rights, obligations, title and interest in the Purchase Agreement to Varex.

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The following amounts represent the determination of the fair value of identifiable assets acquired and liabilities for the Acquired Detector Business:

(In millions)	Fair Value
Total cash consideration	\$ 273.2
Allocation of the purchase consideration:	
Cash	1.4
Accounts Receivable	18.7
Inventory	34.7
Prepays and other current assets	0.6
Property, plant, and equipment	21.4
Other assets, non-current	2.0
Intangibles	81.1
Goodwill	167.3
Total assets acquired	\$ 327.2
Current liabilities	\$ (17.2)
Other liabilities, non-current	(36.8)
Total liabilities assumed	(54.0)
Net assets acquired	\$ 273.2

The fair value assigned to goodwill is attributable to expected cost synergy opportunities. Included in the goodwill recorded for the Acquired Detector Business is approximately \$35 million that will be deductible for income tax purposes in Germany, China and the Netherlands. The remaining goodwill related to the stock acquisition in the United States is not tax deductible. Also, as a result of the acquisition, non-current deferred income tax liability increased by approximately \$31 million related to basis differences for both tangible and intangible assets acquired as part of the stock purchases in the United States and the United Kingdom, and asset purchases in Germany, the Netherlands and China.

The following amounts represent the determination of the fair value of identifiable intangible assets for the Acquired Detector Business, which are amortized straight-line:

(In millions)	Fair Value	Estimated Useful Life (In Years)
Favorable leasehold interests	\$ 3.8	16
Backlog	1.2	1
Trade names	1.4	5
Developed technology	37.7	7
In-process research and development	4.0	indefinite
Customer relationships	33.0	7
Total intangible assets acquired	\$ 81.1	

The following amounts represent revenues by reporting segment from the Acquired Detector Business from the acquisition date of May 1, 2017 through September 29, 2017:

(In millions)	May 1, 2017 through September 29, 2017
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Acquired Detector Business	
Medical	\$ 41.1
Industrial	20.2
Total Acquired Detector Business revenues	<u>\$ 61.3</u>

### *Unaudited Pro Forma Information*

The unaudited pro-forma amounts presented below for the fiscal year 2017 are presented for informational purposes only. In addition to the Company's results for the periods presented, the amounts below also include effects of the Acquired Detector Business as if it had been consummated on October 1, 2016. These unaudited pro-forma results include effects that are directly attributable to the acquisition which include the amortization of intangible assets, interest expense, and other adjustments, including estimated tax effects. The unaudited pro-forma results do not reflect any operating efficiencies or potential cost savings which may result from the consolidation of the Acquired Detector Business and are not necessarily indicative of what the actual results of operations of the combined company would have been if the acquisition had occurred at the beginning of the period presented nor are they indicative of future results of operations or results that might have been achieved had the acquisition been consummated as of October 3, 2015.

(In millions)	Fiscal Year	
	2017	
Revenue	\$	777.8
Operating earnings	\$	84.7
Net earnings	\$	43.1
Net earnings per share, basic	\$	1.15
Net earnings per share, diluted	\$	1.13

### **3. RELATED-PARTY TRANSACTIONS**

#### *Investment in Privately-Held Companies*

The Company has a 40% ownership interest in dpiX Holding LLC (“dpiX Holding”), a four-member consortium that has a 100% ownership interest in dpiX LLC (“dpiX”), a supplier of amorphous silicon based thin film transistor arrays for digital flat panel image detectors. In accordance with the dpiX Holding Agreement, net profits or losses are allocated to the members, in accordance with their ownership interests.

The equity investment in dpiX Holding is accounted for under the equity method of accounting. When the Company recognizes its share of net profits or losses of dpiX Holding, profits or losses in inventory purchased from dpiX are eliminated until realized by the Company. In fiscal years 2019, 2018 and 2017, the Company recorded (loss) and income on the equity investment in dpiX Holding of \$(1.1) million, \$3.4 million and \$0.8 million, respectively. Income and loss on the equity investment in dpiX Holding is included in other (expense) income, net in the consolidated statements of earnings. The carrying value of the equity investment in dpiX Holding, which was included in investments in privately-held companies on the consolidated balance sheets, was \$48.1 million and \$48.9 million at September 27, 2019 and September 28, 2018, respectively.

In fiscal years 2019, 2018 and 2017, the Company purchased glass transistor arrays from dpiX totaling \$23.5 million, \$19.3 million and \$24.7 million, respectively. These purchases of glass transistor arrays are included as a component of inventories on the consolidated balance sheets or cost of revenues in the consolidated statements of earnings for these fiscal years.

As of September 27, 2019 and September 28, 2018, the Company had accounts payable to dpiX totaling \$3.6 million and \$3.7 million, respectively.

In October 2013, the Company entered into an amended agreement with dpiX and other parties that, among other things, provides the Company with the right to 50% of dpiX’s total manufacturing capacity produced after January 1, 2014. The amended agreement requires the Company to pay for 50% of the fixed costs (as defined in the amended agreement), as determined at the beginning of each calendar year. As of September 27, 2019, the Company estimated it has fixed cost commitments of \$3.7 million related to this amended agreement through the remainder of calendar year 2019. The fixed cost commitment for future periods will be determined and approved by the dpiX board of directors at the beginning of each calendar year. The amended agreement will continue unless the ownership structure of dpiX changes (as defined in the amended agreement).

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

of its involvement with dpiX is limited to the carrying value of the Company's investment of \$48.1 million and fixed cost commitments of \$3.7 million.

In November 2018, the Company and CETTEEN GmbH (“CETTEEN”), formed a German limited liability company that governs the affairs and conduct of the business of VEC Imaging Verwaltungsgesellschaft GmbH (“VEC”), a joint venture formed to develop technology to be used in X-ray imaging components. In accordance with the VEC agreement, net profits or losses are allocated to the members, in accordance with their ownership interest. The Company's investment in VEC is accounted for under the equity method. The Company has made contributions totaling \$2.9 million, and has committed to contribute an additional \$2.2 million, as milestones are achieved, and to provide certain full time employees to support prototyping and manufacturing activities in exchange for a 50% interest in VEC. CETTEEN made contributions of certain assets including intellectual property in exchange for a 50% interest in VEC. The Company's investment in VEC was \$2.0 million as of September 27, 2019.

#### 4. RESTRUCTURING

Following the acquisition of the medical imaging business from PKI in May of 2017, management began a multiyear program to consolidate the acquired operations, reduce costs, improve productivity and realize synergies.

In March 2018, the Company made the decision to transfer the complementary metal oxide semiconductor (“CMOS”) research and development capability from the U.K. to the U.S. and to permanently close the operation of the acquired detector business in London. The company will continue to develop the CMOS technology in the U.S. due to its competitive advantages, product differentiation and future economic benefit. In connection with this initiative, we recorded \$1.7 million in restructuring charges during fiscal year 2018.

In July 2018, the Company committed to a plan to relocate the production of amorphous silicon glass for digital detectors, from its Santa Clara facility, to the jointly owned dpiX fabrication facility in Colorado. In July 2019, the Company committed to close its Santa Clara facility and to relocate the remaining production to its other existing facilities. The Company expects operations at the Santa Clara facility to cease by the end of December 2020 and all activities related to the closure of the facility to be complete by the end of March 2021. In connection with the relocation of the glass production and site closure the Company recorded \$16.1 million and \$14.2 million of restructuring and impairment charges during fiscal year 2019 and 2018, respectively. Fiscal year 2019 intangible asset impairment charges consisted of in-process research and development related to certain projects that were discontinued as a result of the Santa Clara facility closure. Fiscal year 2018 intangible asset impairment charges were related to a favorable leasehold interest that was impaired as a result of the amorphous silicon glass relocation. The Company expects to incur an additional \$8.1 million to \$12.1 million of restructuring charges through March 2021.

The Company also incurred approximately \$2.8 million and \$0.8 million of other unrelated restructuring expenses during fiscal years 2019 and 2018, respectively.

Cash outflows associated with these restructuring charges are limited to employee termination expenses, facility closure and equipment sales and disposals. Below is a detail of restructuring charges incurred during the 2019 and 2018 fiscal years, which predominately relate to the Company's Medical segment:

(In millions)	Location of Restructuring Charges in Consolidated		
	Statements of Earnings	September 27, 2019	September 28, 2018
Other assets impairment charges	Selling, general and administrative	\$ —	\$ 1.3
Inventory write downs	Cost of revenues	3.1	3.1
Intangible assets impairment	Impairment of intangible assets	4.8	3.0
Accelerated depreciation	Cost of revenues	4.5	4.2
Severance costs	Selling, general and administrative	6.2	4.3
Facility closure costs	Selling, general and administrative	0.3	0.8
Total restructuring charges		\$ 18.9	\$ 16.7

## 5. OTHER FINANCIAL INFORMATION

The following table summarizes the Company's accrued liabilities:

(In millions)	September 27, 2019	September 28, 2018
Accrued compensation and benefits	\$ 32.1	\$ 27.0
Product warranty	8.1	7.3
Income taxes payable	10.7	1.4
Payable to Varian Medical Systems	—	2.3
Right of return liability	6.9	—
Deferred consideration	8.9	—
Other	9.0	9.5
Total accrued liabilities	<u>\$ 75.7</u>	<u>\$ 47.5</u>

The following table summarizes the Company's other long-term liabilities:

(In millions)	September 27, 2019	September 28, 2018
Long-term income tax payable	\$ 3.9	\$ 3.5
Environment liabilities	0.9	1.3
Defined benefit obligation liability	5.5	3.3
Long-term right of return liability	19.5	—
Long-term other	2.7	0.4
Total other long-term liabilities	<u>\$ 32.5</u>	<u>\$ 8.5</u>

The following table summarizes the Company's other income (expense), net:

(In millions)	Fiscal Years		
	2019	2018	2017
Income (loss) from equity method investments	\$ (2.3)	\$ 3.9	\$ 1.3
Change in fair value of deferred consideration	1.0	—	—
Realized income (loss) on foreign currencies	(1.9)	(1.2)	1.9
Total other income (expense), net	<u>\$ (3.2)</u>	<u>\$ 2.7</u>	<u>\$ 3.2</u>

## 6. NET EARNINGS PER SHARE

Basic net earnings per common share is computed by dividing the net earnings for the period by the weighted average number of shares of common stock outstanding during the reporting period. Diluted net earnings per common share reflects the effects of potentially dilutive securities, which is computed by dividing net earnings by the sum of the weighted average number of common shares outstanding and dilutive common shares, which consists of stock options and unvested restricted stock.

A reconciliation of the numerator and denominator used in the calculation of basic and diluted net income per common share is as follows:

(In millions, except per share amounts)	Fiscal Year		
	2019	2018	2017
Net earnings attributable to Varex	\$ 15.5	\$ 27.5	\$ 51.6
Weighted average shares outstanding - basic	38.2	37.9	37.6
Dilutive effect of potential common shares	0.4	0.5	0.4
Weighted average shares outstanding - diluted	38.6	38.4	38
Net earnings per share attributable to Varex - basic	\$ 0.41	\$ 0.73	\$ 1.37
Net earnings per share attributable to Varex - diluted	\$ 0.40	\$ 0.72	\$ 1.36
Anti-dilutive employee shared based awards, excluded	1.9	1.2	1.0

The Company excludes potentially dilutive common shares (consisting of shares underlying stock options and the employee stock purchase plan) from the computation of diluted weighted average shares outstanding if the inclusion of the shares underlying these stock awards would be anti-dilutive to earnings per share.

## 7. FINANCIAL DERIVATIVES AND HEDGING ACTIVITIES

As part of the Company's overall risk management practices, the Company enters into financial derivatives to manage its financial exposures to foreign currency exchange rates and interest rates.

The Company records all derivatives on the consolidated balance sheets at fair value. The accounting for changes in the fair value of derivatives depends on the intended use of the derivative, whether the Company has elected to designate a derivative in a hedging relationship and apply hedge accounting, and whether the hedging relationship has satisfied the criteria necessary to apply hedge accounting. A qualitative assessment of hedge effectiveness is performed on a quarterly basis, unless facts and circumstances indicate the hedge may no longer be highly effective. The changes in fair value for all trades that are not designated for hedge accounting are recognized in current period earnings. The Company does not offset fair value amounts recognized for derivative instruments in its consolidated balance sheets for presentation purposes.

Credit risk related to derivative transactions reflects the risk that a party to the transaction could fail to meet its obligation under the derivative contracts. Therefore, the Company's exposure to the counterparty's credit risk is generally limited to the amounts, if any, by which the counterparty's obligations to the Company exceed the Company's obligations to the counterparty. The Company's policy is to enter into contracts only with financial institutions which meet certain minimum credit ratings to help mitigate counterparty credit risk.

### *Derivatives Designated as Hedging Instruments - Cash Flow Hedges*

The Company uses interest rate swap contracts as cash flow hedges to manage its exposure to fluctuations in LIBOR interest rates. Interest rate swap contracts hedging variable rate debt effectively fix the LIBOR component of its interest rate for a specific period of time.

As of September 27, 2019, the Company had the following outstanding derivatives designated as cash flow hedging instruments:

(In millions, except for number of instruments)	Number of Instruments	Notional Value
Interest Rate Swap Contracts	6	\$ 264.4

The following table summarizes the amount of pre-tax earnings recognized from derivative instruments for the periods indicated and the line items in the accompanying statements of operations where the results are recorded for cash flow hedges:



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(In millions)	Amount of Gain or (Loss) Recognized in OCI on Derivative Fiscal Year Ended			Location of Gain or (Loss) Reclassified from Accumulated OCI into Income	Amount of Gain or (Loss) Reclassified from Accumulated OCI into Income Fiscal Year Ended		
	2019	2018	2017		2019	2018	2017
Interest Rate Swap Contracts	\$ (6.3)	\$ 6.9	\$ 0.6	Interest expense	\$ 1.9	\$ 0.1	\$ (0.3)

The Company expects that \$0.1 million of the accumulated other comprehensive (loss) income related to cash flow hedges will be realized in pre-tax earnings over the next 12 months, but the amount will vary depending on interest rates.

These derivative instruments are subject to master netting agreements giving effect to rights of offset with each counterparty. None of the balances were eligible for netting. The following table summarizes the gross fair values of derivative instruments as of the periods indicated and the line items in the accompanying consolidated balance sheets where the instruments are recorded.

(In millions)		Derivative Assets			Derivative Liabilities	
		September 27, 2019	September 28, 2018		September 27, 2019	September 28, 2018
<b>Derivatives designated as cash flow hedges</b>	<b>Balance sheet location</b>			<b>Balance sheet location</b>		
Interest rate swap contracts	Other current assets	\$ —	\$ 2.2	Other current liabilities	\$ —	\$ —
Interest rate swap contracts	Other non-current assets	—	5.5	Other non-current liabilities	(0.5)	—
		<u>\$ —</u>	<u>\$ 7.7</u>		<u>\$ (0.5)</u>	<u>\$ —</u>

#### Derivatives Designated as Hedging Instruments - Net Investment Hedges

The Company uses cross currency swap contracts as net investment hedges to manage its risk of variability in foreign currency-denominated net investments in wholly-owned international operations. All changes in fair value of the derivatives designated as net investment hedges are reported in accumulated other comprehensive (loss) income along with the foreign currency translation adjustments on those investments. As of September 27, 2019, the Company had the following outstanding derivatives designated as net investment hedging instruments:

(In millions, except for number of instruments)	Number of Instruments	Notional Value
Cross Currency Swap Contracts	4	\$ 77.7

The following table summarizes the amount of pre-tax earnings recognized from derivative instruments for the periods indicated and the line items in the accompanying statements of operations where the results are recorded for net investment hedges:

(In millions)	Amount of Gain or (Loss) Recognized in OCI on Derivative Fiscal Year Ended			Location of Gain or (Loss) Recognized in Income on Derivative (Amount Excluded from Effectiveness Testing)	Amount of Gain or (Loss) Recognized in Income on Derivative (Amount Excluded from Effectiveness Testing)		
	2019	2018	2017		2019	2018	2017
Cross Currency Swap Contracts	\$ (0.2)	\$ —	\$ —	Interest expense	\$ 0.2	\$ —	\$ —

These derivative instruments are subject to master netting agreements giving effect to rights of offset with each counterparty. None of the balances were eligible for netting. The following table summarizes the gross fair values of derivative instruments as of the periods indicated and the line items in the accompanying consolidated balance sheets where the instruments are recorded:

(In millions)		Derivative Assets			Derivative Liabilities	
		September 27, 2019	September 28, 2018		September 27, 2019	September 28, 2018
<b>Derivatives designated as net investment hedges</b>	<b>Balance sheet location</b>			<b>Balance sheet location</b>		
Cross currency swap contracts	Other current assets	—	—	Other current liabilities	(0.2)	—
		<u>\$ —</u>	<u>\$ —</u>		<u>\$ (0.2)</u>	<u>\$ —</u>



### Balance Sheet Hedges

The Company also enters into foreign currency forward contracts to hedge fluctuations associated with foreign currency denominated monetary assets and liabilities, primarily cash, third-party accounts receivable, accounts payable, and intercompany receivables and payables. These forward contracts expire within 30 days. These forward contracts are not designated for hedge accounting treatment, therefore, the change in fair value of these derivatives is recorded as a component of other income (expense) and offsets the change in fair value of the foreign currency denominated assets and liabilities, which are also recorded in other income (expense). The effect of derivative instruments not designated as hedges for fiscal year 2019 was a loss of \$1.5 million, which was primarily related to the purchase price hedge established following the announcement of the Company's planned acquisition of Direct Conversion. The Company does not, and does not intend to use derivative financial instruments for speculative or trading purposes.

The following table shows the notional amounts of outstanding foreign currency contracts entered into under its balance sheet hedge program as of September 27, 2019:

In millions	Notional Value of Derivatives not Designated as Hedging Instruments:	
	Buy contracts	Sell contract
Japanese yen	\$ 0.9	\$ —
Swiss franc	—	(1.0)
Chinese renminbi	1.8	—
Euro	8.8	—
	<u>\$ 11.5</u>	<u>\$ (1.0)</u>

## 8. BORROWINGS

The following table summarizes the Company's short-term and long-term debt:

(In millions, except for percentages)	September 27, 2019		September 28, 2018	
	Amount	Weighted-Average Interest Rate	Amount	Weighted-Average Interest Rate
Current maturities of long-term debt				
Term facility	\$ 29.4	5.6%	\$ 25.0	4.2%
Other debt	1.3		—	
Total current maturities of long-term debt	<u>\$ 30.7</u>		<u>\$ 25.0</u>	
Non-current maturities of long-term debt:				
Revolving credit facility	\$ 59.0	5.6%	\$ 28.0	4.2%
Term facility	308.6	5.6%	345.0	4.2%
Other debt	2.5		—	
Debt issuance costs	(5.7)		(8.2)	
Non-current maturities of long-term debt	<u>364.4</u>		<u>364.8</u>	
Total long-term debt, net	<u>\$ 395.1</u>		<u>\$ 389.8</u>	

### Existing Credit Facility

On May 1, 2017 and in connection with the Acquired Detector Business, the Company entered into a new secured revolving credit facility (the “Revolving Credit Facility”) in an aggregate principal amount of up to \$200.0 million with a five-year term, and a

secured term facility (the “Term Facility” and together with the Revolving Credit Facility, the “Credit Agreement”) in an aggregate principal amount of \$400.0 million. The Term Facility will be repaid over five years, with 5.0% payable in quarterly installments

during each of the first two years of the term thereof, 7.5% payable in quarterly installments during the third and fourth years of the term thereof, and 10% payable in quarterly installments in the fifth year of the term thereof, with the remaining amount due at maturity. Varex used the net proceeds from the Term Facility, and the net proceeds from approximately \$97.0 million drawn on the Revolving Credit Facility, to pay the purchase price for the Acquired Detector Business, plus related credit facility fees, and to repay all of Varex's obligations under the Previous Credit Agreement. Both the Term Facility and Revolving Credit Facility expire on May 1, 2022.

The Credit Agreement contains various customary restrictive covenants that limits, among other things, the incurrence of indebtedness by Varex and its subsidiaries, the grant or incurrence of liens by Varex and its subsidiaries, the entry into sale and leaseback transactions by Varex and its subsidiaries, and the entry into certain fundamental change transactions by Varex and its subsidiaries. It also contains customary events of default and certain financial covenants. The Company agreed to maintain financial covenants, which include maximum consolidated total leverage ratio, maximum senior secured leverage ratio, maximum capital expenditures and a minimum consolidated fixed charge coverage ratio. The Company was in compliance with all financial covenants under the Credit Agreement as of September 27, 2019.

The Credit Agreement is secured by the stock and assets of Varex's material subsidiaries. The Credit Agreement has several borrowing and interest rate options including the following indices: (a) LIBOR rate, or (b) the base rate (equal to the greater of the prime rate, the federal funds rate plus 0.50% or the LIBOR rate for a one-month period plus 1.00%). Loans under the Credit Agreement bear interest at a rate per annum using the applicable indices plus a varying interest rate margin of between 1.75% and 2.75% (for LIBOR rate loans) and 0.75%-1.75% (for base rate loans). The Credit Agreement also provides for fees applicable to amounts available to be drawn under outstanding letters of credit of 0.125%, and a fee on unused commitments which ranges from 0.25% to 0.40%.

On October 3, 2018, the Company, in accordance with the terms of the Credit Agreement, provided notice to the administrative agent that effective as of October 10, 2018, the Company had permanently reducing the revolving credit commitment under the Credit Agreement by \$50.0 million to \$150.0 million. The reduction in the revolving credit commitment reduced the fees paid by the Company in connection with such commitment.

Subsequent to fiscal year 2019, the Company, in accordance with the terms of the Credit Agreement, provided notice to the administrative agent that effective as of October 8, 2019, the Company was permanently reducing the revolving credit commitment under the Credit Agreement by \$25.0 million to \$125.0 million.

Subsequent to fiscal year 2019, the Company did not comply with the covenant under the Credit Agreement to timely deliver the Company's fiscal year 2019 annual financial statements. However, upon the filing of this Annual Report with the SEC, the Company will be able to deliver the fiscal year 2019 annual financial statements within the 30-day cure period set forth in the Credit Agreement and consequently no event of default will occur.

At September 27, 2019, the Company had \$364.4 million in non-current maturities of long-term debt outstanding, net of deferred debt issuance costs of \$5.7 million, and \$30.7 million of current maturities of long-term debt outstanding.

Future principal payments of the long-term debt outstanding as of September 27, 2019 are as follows:

**(In millions)**

**Fiscal years:**

2020	\$	30.7
2021		34.3
2022		335.8
Total debt outstanding		400.8
Less: current maturities of long-term debt		(30.7)
Non-current portion of long -term debt	\$	370.1

## 9. FAIR VALUE

### *Assets/Liabilities Measured at Fair Value on a Recurring Basis*

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

(In millions)	Fair Value Measurements at September 27, 2019			
	Quoted Prices in Active Markets for Identical Assets and Liabilities (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Total
Assets:				
Cash equivalents - money market funds	\$ —	\$ 8.8	\$ —	\$ 8.8
Total assets measured at fair value	\$ —	\$ 8.8	\$ —	\$ 8.8
Liabilities:				
Derivative liabilities	\$ —	\$ 0.7	\$ —	\$ 0.7
Deferred consideration	8.9	—	—	8.9
Total liabilities measured at fair value	\$ 8.9	\$ 0.7	\$ —	\$ 9.6

As of September 27, 2019, the total outstanding borrowings under the Company's credit agreement were \$395.1 million, net of deferred loan costs, which approximated its fair value because it is carried at a market observable interest rate that resets periodically and is categorized as Level 2 in the fair value hierarchy. The fair values of certain of the Company's financial instruments, including bank deposits included in cash and cash equivalents, accounts receivable and accounts payable, also approximate their fair values due to their short maturities.

There were no financial assets or liabilities measured on a recurring basis using significant unobservable inputs (Level 3) and there were no transfers in or out of Level 1, 2 or 3 during fiscal year 2018.

At September 28, 2018, the Company determined the following levels of inputs for the following assets or liabilities:

(In millions)	Fair Value Measurements at September 28, 2018			
	Quoted Prices in Active Markets for Identical Assets and Liabilities (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Total
Assets:				
Cash equivalents - Money market funds	\$ —	\$ 18.4	\$ —	\$ 18.4
Derivative assets	—	7.7	—	7.7
Total assets measured at fair value	\$ —	\$ 26.1	\$ —	\$ 26.1
Liabilities:				
Derivative liabilities	\$ —	\$ —	\$ —	\$ —

## 10. GOODWILL AND INTANGIBLE ASSETS

The following table reflects goodwill by reportable operating segment:

(In millions)	Medical	Industrial	Total
Balance at September 28, 2018	\$ 147.0	\$ 96.6	\$ 243.6
Business combination	26.0	21.2	47.2
Balance at September 27, 2019	<u>\$ 173.0</u>	<u>\$ 117.8</u>	<u>\$ 290.8</u>

The following table reflects the gross carrying amount and accumulated amortization of the Company's finite-lived intangible assets included in other assets in the consolidated balance sheets:

(In millions)	September 27, 2019			September 28, 2018		
	Gross Carrying Amount	Accumulated Amortization	Net Carrying Amount	Gross Carrying Amount	Accumulated Amortization	Net Carrying Amount
Acquired existing technology	\$ 74.1	\$ (28.4)	\$ 45.7	\$ 57.9	\$ (21.8)	\$ 36.1
Patents, licenses and other	12.7	(8.4)	4.3	9.9	(7.4)	2.5
Customer contracts and supplier relationship	50.7	(17.2)	33.5	42.6	(11.4)	31.2
Total intangible assets with finite lives	137.5	(54.0)	83.5	110.4	(40.6)	69.8
In-process R&D with indefinite lives	2.8	0.0	2.8	4.0	0.0	4.0
Total intangible assets	<u>\$ 140.3</u>	<u>\$ (54.0)</u>	<u>\$ 86.3</u>	<u>\$ 114.4</u>	<u>\$ (40.6)</u>	<u>\$ 73.8</u>

Amortization expense for intangible assets was \$15.7 million, \$16.2 million and \$10.5 million in fiscal years 2019, 2018 and 2017, respectively. The Company recognized an impairment loss of \$4.8 million and \$3.0 million in fiscal years 2019 and 2018, respectively. These impairment costs were included in the consolidated statements of earnings under impairment of intangible assets.

As of September 27, 2019, the estimated future amortization expense of intangible assets with finite lives is as follows:

(In millions)	
Fiscal years:	
2020	\$ 17.2
2021	16.3
2022	14.7
2023	13.7
2024	9.1
Thereafter	12.5
<b>Total</b>	<u>\$ 83.5</u>

## 11. COMMITMENTS AND CONTINGENCIES

### Lease Commitments

At September 27, 2019, the Company was committed to minimum rentals under non-cancelable operating leases (including rent escalation clauses) for fiscal years 2020 through 2024 and thereafter, as follows: \$7.5 million, \$5.4 million, \$4.7 million, \$1.8 million, \$0.9 million, and \$0.2 million, respectively. Rental expenses were \$5.1 million, \$5.3 million, and \$4.0 million for fiscal years 2019, 2018 and 2017, respectively.

### ***Other Commitments***

See Note 3. *Related Party Transactions*, included in this report, for additional information about the Company's commitments to dpiX.

See Note 12. *Redeemable Noncontrolling Interests & Noncontrolling Interests*, included in this report, for additional information about the Company's commitment to the noncontrolling shareholders of MeVis.

The Company has an environmental liability of approximately \$0.9 million as of September 27, 2019.

### ***Contingencies***

From time to time, the Company is a party to or otherwise involved in legal proceedings, claims and government inspections or investigations, customs and duty audits, other contingency matters, both inside and outside the United States, arising in the ordinary course of its business or otherwise. The Company accrues amounts for probable losses, to the extent they can be reasonably estimated, that it believes are adequate to address any liabilities related to legal proceedings and other loss contingencies that the Company believes will result in a probable loss (including, among other things, probable settlement value). A loss or a range of loss is disclosed when it is reasonably possible that a material loss will be incurred and can be estimated or when it is reasonably possible that the amount of a loss, when material, will exceed the recorded provision. The Company did not have any contingent liabilities as of September 27, 2019 and September 28, 2018. Legal expenses are expensed as incurred.

## **12. REDEEMABLE NONCONTROLLING INTERESTS & NONCONTROLLING INTERESTS**

In April 2019, a subsidiary of Varex completed the acquisition of 98.2% of the outstanding shares of common stock of Direct Conversion. As the Company has majority voting rights it has consolidated Direct Conversion's operations in its consolidated financial statements and recorded the noncontrolling interest. The noncontrolling interest related to Direct Conversion is included in noncontrolling interest in the equity section of the Company's consolidated balance sheet. Earnings representing the noncontrolling interest's portion of Direct Conversion's income from operations is included in the Company's consolidated statements of earnings.

In September 2018, the Company entered into a partnership in Saudi Arabia. The Company has majority voting rights with an approximate 75% interest. Accordingly, the Company has consolidated the operations of the Saudi Arabia partnership in our consolidated financial statements and recorded the noncontrolling interests. The noncontrolling interest related to the partner's 25% interest in the joint venture is included in noncontrolling interest in the equity section of the Company's consolidated balance sheet. Earnings representing the noncontrolling partner's share of income from operations is included in the Company's consolidated statements of earnings.

In April 2015, the Company completed the acquisition of 73.5% of the then outstanding shares of MeVis Medical Solutions AG ("MeVis"), a public company based in Bremen, Germany that provides image processing software and services for cancer screening. In August 2015, the Company, through one of its German subsidiaries, entered into a domination and profit and loss transfer agreement (the "DPLTA") with MeVis. In October 2015, the DPLTA became effective upon its registration at the local court of Bremen, Germany. Under the DPLTA, MeVis subordinates its management to the Company and undertakes to transfer all of its annual profits and losses to the Company. In return, the DPLTA grants the noncontrolling shareholders of MeVis: (1) an annual recurring net compensation of €0.95 per MeVis share starting from January 1, 2015 and (2) a put right for their MeVis shares at €19.77 per MeVis share. Upon effectiveness of the DPLTA, the noncontrolling interests in MeVis became redeemable as a result of the put right and were reclassified to temporary equity. As of September 27, 2019, the redemption value of redeemable noncontrolling interests in MeVis was \$10.5 million.

During fiscal year 2018, an immaterial number of MeVis' shares were purchased under the put right. As of September 27, 2019, noncontrolling shareholders together held approximately 0.5 million shares of MeVis, representing 26.3% of the outstanding shares.

Changes in redeemable noncontrolling interests and noncontrolling interests were as follows:

(In millions)	Fiscal Years			
	2019		2018	
	Redeemable Noncontrolling Interests	Noncontrolling Interests	Redeemable Noncontrolling Interests	Noncontrolling Interest
<b>Balance at beginning of period</b>	\$ 11.1	\$ 2.1	\$ 11.2	\$ —
Net earnings attributable to noncontrolling interests	0.5	(0.2)	0.5	0.3
Contributions from noncontrolling interests	—	1.4	—	1.8
Dividend distributions	(0.5)	—	(0.6)	—
Other	(0.6)	—	—	—
<b>Balance at end of period</b>	<u>\$ 10.5</u>	<u>\$ 3.3</u>	<u>\$ 11.1</u>	<u>\$ 2.1</u>

### 13. EMPLOYEE STOCK PLANS

#### *Employee Stock Plans*

The Company's employees participate in Varex Imaging Corporation 2017 Omnibus Stock Plan (the “2017 Stock Plan”) and Varex Imaging Corporation 2017 Employee Stock Purchase Plan (the “2017 ESPP”) which allows the grants of stock options, restricted stock units and performance shares among other types of awards.

In January 2017, Varex stockholders approved the 2017 ESPP, which provides eligible employees with an opportunity to purchase shares of Varex common stock at 85% of the lower of its fair market value at the start and end of a six months purchase period. The 2017 ESPP provides for the purchase of up to one million shares of Varex common stock.

#### *Share-Based Compensation Expense*

Share-based compensation expense recognized in the consolidated statements of earnings is based on awards ultimately expected to vest. Share-based compensation expense includes expenses related to the Company's direct employees. Prior to the separation, Varian also charged the Company for the allocated share-based compensation costs of certain employees of Varian who provided selling, general and administrative services on the Company's behalf.

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

(In millions)	Fiscal Year		
	2019	2018	2017
Cost of revenues	\$ 1.2	\$ 1.3	\$ 0.9
Research and development	2.2	1.8	1.5
Selling, general and administrative <sup>(1)</sup>	8.3	6.9	6.0
<b>Total share-based compensation expense</b>	<u>\$ 11.7</u>	<u>\$ 10.0</u>	<u>\$ 8.4</u>

(1) Includes allocated share-based compensation of \$0.8 million for fiscal year 2017 and represents charges by Varian to the Company for certain Varian employees who provided general and administrative services on the Company's behalf.

The unrecognized share-based compensation cost as of September 27, 2019 was \$23.1 million, and is expected to be recognized in the next 3 to 4 fiscal years. As of September 27, 2019, there were approximately 1.2 million and 0.7 million shares of common stock available for future issuances under the 2017 Stock Plan and the 2017 ESPP, respectively.

The Company utilized the Black-Scholes valuation model for estimating the fair value of stock options granted and the option component of ESPP grants. The Company calculated the fair value of option grants and option component of ESPP grants on the respective dates of grant using the following weighted average assumptions:

	Employee Stock Option Plan			Employee Stock Purchase Plans		
	Fiscal Year			Fiscal Year		
	2019	2018	2017	2019	2018	2017
Expected term (in years)	4.6	4.8	4.2	0.5	0.5	0.5
Risk-free interest rate	2.5%	2.6%	1.6%	2.5%	2.0%	1.0%
Expected volatility	33.9%	31.8%	23.6%	43.9%	34.1%	28.0%
Expected dividend	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%
Weighted average fair value at grant date	\$10.19	\$11.57	\$8.08	\$7.81	\$8.92	\$7.81

Option valuation methods, including Black-Scholes, require the input of subjective assumptions, which are discussed below.

#### ***Risk-Free Interest Rate***

The interest rates used are based on the implied yield currently available on U.S. Treasury zero-coupon issues with an equivalent remaining term equal to the expected life of the award.

#### ***Expected Term***

Options granted generally vest over a period of 36 to 48 months and expire 7 to 10 years from date of grant. Employee stock purchase plan offering periods are 6 months and provides eligible employees with an opportunity to purchase shares of Varex common stock at 85% of the lower of its fair market value at the start and end of a six-month purchase period.

#### ***Expected Dividend Yield***

The dividend rate used is zero as the Company has never paid any cash dividends on its common stock and does not anticipate doing so in the foreseeable future. The Company is also restricted from paying dividends on common stock under its credit facility.

#### ***Expected Volatility***

Authoritative accounting guidance on stock-based compensation indicates that companies should consider volatility over a period generally commensurate with the expected or contractual term of the stock option. Adequate Company-specific data does not exist for this time period as the Company began trading in January 2017. The volatility variable used is a blended approach by using the Company's historic data for the years it has been publicly traded and a benchmark of other comparable companies' volatility rates for the prior years.

### Stock Option Activity

The following table summarizes the activity for stock options under Varex's employee incentive plans for the Company's employees:

(In thousands, except per share amounts and the remaining term)	Options	Price range	Weighted Average Exercise Price	Weighted Average Remaining Term (in years)	Aggregate Intrinsic Value (1)
Outstanding at September 28, 2018	2,011	\$22.63 — \$37.60	\$ 30.35		
Granted	297	\$31.42 — \$31.42	31.42		
Canceled, expired or forfeited	(4)	\$31.08 — \$31.08	31.08		
Exercised	(35)	\$22.84 — \$27.77	23.38		
Outstanding at September 27, 2019	2,269	\$22.63 — \$37.60	\$ 30.60	4.1	\$ 1,220.3
Exercisable at September 27, 2019	1,477	\$22.63 — \$37.60	\$ 29.67	3.4	\$ 1,220.3

(1) The aggregate intrinsic value represents the total pre-tax intrinsic value, which is computed based on the difference between the exercise price and the closing price of Varex common stock of \$28.28 as of September 27, 2019, the last trading date of the Company's respective fiscal years, and which represents the amount that would have been received by the option holders had all option holders exercised their options and sold the shares received upon exercise as of that date.

The weighted-average grant-date fair value of options granted during fiscal years 2019, 2018 and 2017 was \$3.0 million, \$3.1 million and \$9.2 million respectively. The total intrinsic value of the options exercised during the years ended September 27, 2019, September 28, 2018 and September 29, 2017 was \$0.2 million, \$1.7 million and \$1.4 million respectively.

### Restricted Stock Units, Restricted Stock Awards and Deferred Stock Units

The following table summarizes the activity for restricted stock units, restricted stock awards and deferred stock units under Varex's employee incentive plans for the Company's employees:

(In thousands, except per share amounts)	Number of Shares	Weighted Average Grant-Date Fair Value
Balance at September 28, 2018	641	\$ 33.60
Granted	288	31.29
Vested	(201)	31.56
Canceled or expired	(50)	34.13
Balance at September 27, 2019	678	\$ 33.18

The total grant-date fair value of shares granted in fiscal year was \$9.0 million, \$10.1 million and \$11.4 million for fiscal years 2019, 2018 and 2017, respectively. Shares outstanding at September 27, 2019, September 28, 2018 and September 29, 2017 had an estimated market value of \$19.2 million, \$18.4 million and \$17.8 million, respectively.

## 14. TAXES ON EARNINGS

Income tax expense is based on reported income or loss before income taxes. Deferred income taxes reflect the effect of temporary differences between asset and liability amounts that are recognized for financial reporting purposes and the amounts that are recognized for income tax purposes. These deferred taxes are measured by applying currently enacted tax laws. Valuation allowances are recognized to reduce deferred tax assets to the amount that is more likely than not to be realized.

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Taxes on earnings were as follows:

(In millions)	Fiscal Years		
	2019	2018	2017
Current provision:			
Federal	\$ 9.2	\$ (2.1)	\$ 24.8
State and local	1.3	(0.3)	1.6
Foreign	6.8	7.5	5.3
Total current	17.3	5.1	31.7
Deferred provision (benefit):			
Federal	(10.0)	(7.0)	(7.0)
State and local	(1.6)	0.7	(1.0)
Foreign	—	(1.4)	(0.9)
Total deferred	(11.6)	(7.7)	(8.9)
Taxes on earnings	\$ 5.7	\$ (2.6)	\$ 22.8

Earnings before taxes are generated from the following geographic areas:

(In millions)	Fiscal Years		
	2019	2018	2017
United States	\$ 5.9	\$ 3.7	\$ 55.5
Foreign	15.6	22.0	19.3
Earnings before taxes	\$ 21.5	\$ 25.7	\$ 74.8

The effective tax rate differs from the U.S. federal statutory tax rate as a result of the following:

	Fiscal Years		
	2019	2018	2017
Federal statutory income tax rate	21.0 %	24.5 %	35.0 %
State and local taxes, net of federal tax benefit	(0.9)%	1.1 %	1.3 %
Revaluation of deferred tax liabilities for US statutory change	— %	(41.8)%	— %
Mandatory repatriation tax on foreign earnings	1.9 %	13.0 %	— %
Domestic production activities deduction	— %	(0.8)%	(2.4)%
Research and development credit	(10.2)%	(11.1)%	(2.6)%
Prior year deferred tax adjustments	4.7 %	1.9 %	(4.0)%
Foreign Rate Difference	6 %	0.8 %	— %
Change in valuation allowance	11.2 %	(1.9)%	3.8 %
US Tax Reform - International Provisions	(4.7)%	— %	— %
Other	(2.5)%	4.2 %	(0.6)%
Effective tax rate	26.5 %	(10.1)%	30.5 %

On December 22, 2017, the Tax Cuts and Jobs Act of 2017 (U.S. Tax Reform) was enacted in the U.S. which significantly revised the U.S. corporate income tax structure. Among the revisions impacting our effective tax rate are a lower U.S. corporate statutory rate going from 35% to 21% effective January 1, 2018 and changes to the way foreign earnings are taxed. As a September fiscal year filer, the lower corporate income tax rate is phased in from a U.S. statutory federal rate of 24.5% in fiscal year ending September 28, 2018 to a rate of 21% for the fiscal year ending September 27, 2019.

During fiscal year 2019, the Company's effective tax rate varied from the U.S. federal statutory rate of 21% primarily because of the favorable impact of changes to the U.S. corporate tax structure resulting from U.S. Tax Reform, and U.S. research and development tax credits. These favorable U.S. tax items are offset by losses in certain foreign jurisdictions for which no benefit is recognized and earnings in other foreign jurisdictions that are taxed at higher rates.

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During fiscal year 2018, the Company's effective tax rate varied from the U.S. federal statutory rate primarily because the favorable impact of changes to the U.S. corporate tax structure resulting from U.S. Tax Reform. During fiscal years 2018 and 2017, the effective tax rate also differs from the U.S. federal statutory rate due to increases resulting from U.S. state income tax expense, losses in certain foreign jurisdictions for which no benefit is recognized, earnings in other foreign jurisdictions that are taxed at higher rates, and limitations on the deductibility of officers' compensation. These are offset by decreases due to U.S. research and development credits, tax windfalls for share-based compensation, and the release of a valuation allowance against loss carryforwards in certain foreign jurisdictions.

The SEC issued guidance under Staff Accounting Bulletin No. 118, Income Tax Accounting Implications of the Tax Cuts and Jobs Act ("SAB 118") that allows for reasonable estimated amounts to be recorded and a measurement period of up to one year from the date of enactment to revise these provisional amounts as new information is obtained and additional guidance is issued. During the three months ended December 28, 2018, the Company completed its analysis of U.S. Tax Reform, and the accounting for the income tax effects has been finalized for the measurement period under SAB 118, with no significant adjustments from the provisional amounts. During fiscal year 2019, additional U.S. Tax Reform provisions, including GILTI (global intangible low-taxed income), BEAT (base-erosion anti-abuse tax), FDII (foreign-derived intangible income), limitations on interest expense deductions (if certain conditions apply), and other components became effective for the Company and, if applicable, have been included in the calculation of the fiscal year 2019 tax provision. The determination of the tax effects of U.S. Tax Reform may change following future legislation or further interpretation of U.S. Tax Reform from U.S. Federal and state tax authorities.

The guidance for accounting for U.S. Tax Reform requires taxpayers to make an election regarding the accounting for GILTI. This policy election is to either: (1) treat GILTI as a period cost if and when incurred, or (2) recognize deferred taxes for basis differences that are expected to reverse as GILTI in future years. During the first quarter of fiscal year 2019, the Company has made the accounting policy election to account for GILTI under the period cost method.

Significant components of deferred tax assets and liabilities are as follows:

(In millions)	September 27, 2019	September 28, 2018
<b>Deferred Tax Assets:</b>		
Inventory adjustments	\$ 5.6	\$ 4.2
Share-based compensation	3.1	0.8
Product warranty	1.6	1.4
Deferred compensation	1.1	0.9
Net operating loss carryforwards	24.3	3.3
Accrued vacation	1.0	1.3
Credit carryforwards	1.9	1.8
Other	7.5	4.7
	<u>46.1</u>	<u>18.4</u>
Valuation allowance	(18.8)	(4.0)
<b>Total deferred tax assets</b>	<u>27.3</u>	<u>14.4</u>
<b>Deferred Tax Liabilities:</b>		
Acquired intangibles	(19.3)	(15.2)
Property, plant and equipment	(10.6)	(14.3)
Investments in privately held companies	(3.3)	(4.1)
Other	(2.3)	(4.0)
<b>Total deferred tax liabilities</b>	<u>(35.5)</u>	<u>(37.6)</u>
<b>Net deferred tax liabilities</b>	<u>\$ (8.2)</u>	<u>\$ (23.2)</u>
<b>Reported As:</b>		
Deferred tax assets	\$ 27.3	\$ 14.4
Deferred tax liabilities	(35.5)	(37.6)
<b>Net deferred tax liabilities</b>	<u>\$ (8.2)</u>	<u>\$ (23.2)</u>

As a result of the changes to the U.S. taxation of foreign earnings included in U.S. Tax Reform, the Company reevaluated its previous indefinite reinvestment assertion with respect to these earnings during fiscal year 2018, which resulted in the Company revoking its assertion for current and future earnings for all countries, while maintaining the assertion that historic earnings are



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indefinitely reinvested outside the U.S. The Company has modified this prior assertion for the year ended September 27, 2019 with respect to the acquisition of Direct Conversion. The modification was to assert that all earnings for Direct Conversion, located primarily in Sweden and Finland, are indefinitely reinvested in those countries. Due to the level of earnings available for repatriation, the treaty benefits applicable to jurisdictions in which those earnings are located, and the now favorable U.S. tax treatment of repatriated foreign earnings, the amount of deferred tax liability recorded related to the potential repatriation is approximately \$0.1 million. This estimated liability is for U.S. State income taxes and foreign withholding taxes that would apply if the foreign earnings were actually repatriated in the form of a dividend.

As of September 27, 2019, the Company has net operating loss carryforwards of approximately \$24.3 million with \$4.4 million expiring between 2020 and 2030 and \$19.9 million carried forward indefinitely.

The valuation allowance relates primarily to net operating losses in certain foreign jurisdictions where, based on the weight of available evidence, it is more likely than not that the tax benefit of the net operating losses will not be realized. The valuation allowance increased by \$14.8 million during fiscal year 2019 and decreased by \$0.3 million during fiscal year 2018. The increase during the current year was primarily related to the acquisition of Direct Conversion that included deferred tax assets subject to a valuation allowance as of acquisition. Changes in the Company's valuation allowance for deferred tax assets were as follows:

(In millions)	Fiscal Years		
	2019	2018	2017
Valuation allowance balance—beginning of fiscal year	\$ 4.0	\$ 4.3	\$ 2.5
Increases resulting from business combinations	12.0	—	—
Other increases	2.8	2.2	2.5
Other decreases	—	(2.5)	(0.7)
Valuation allowance balance—end of fiscal year	<u>\$ 18.8</u>	<u>\$ 4.0</u>	<u>\$ 4.3</u>

During fiscal year 2019, the Company paid U.S. and foreign taxes of approximately \$8.2 million. In fiscal year 2018, the Company paid U.S. and foreign taxes of approximately \$13.8 million.

The Company accounts for uncertainty in income taxes following a two-step approach for recognizing and measuring uncertain tax positions. The first step is to evaluate the tax position for recognition by determining whether the weight of available evidence indicates that it is more likely than not that, based on the technical merits, the position will be sustained on audit, including resolution of related appeals or litigation processes, if any. The second step is to measure the tax benefit as the largest amount that is more than 50% likely of being realized upon settlement.

Changes in the Company's unrecognized tax benefits were as follows:

(In millions)	Fiscal Years	
	2019	2018
Unrecognized tax benefits balance—beginning of fiscal year	\$ 0.6	\$ 0.5
Subtractions based on tax positions related to a prior year	(0.2)	—
Additions based on tax positions related to the current year	0.2	0.1
Unrecognized tax benefits balance—end of fiscal year	<u>\$ 0.6</u>	<u>\$ 0.6</u>

As of September 27, 2019 and September 28, 2018, the total amount of gross unrecognized tax benefits was \$0.6 million and \$0.6 million, respectively, all of which would affect the effective tax rate if recognized.

The Company includes interest and penalties related to income taxes within taxes on earnings on the Combined Statements of Earnings. For the year ended September 27, 2019, \$0.1 million interest and penalties have been included for this period. For the year ended September 28, 2018 any interest or penalties related to unrecognized tax benefits are minimal and have been included in the balance for that period.

The Company files U.S. Federal and state income tax returns and non-U.S. income tax returns in various jurisdictions. All of these returns are subject to examination by their respective taxing jurisdictions from the date of filing through each applicable statute of

limitation period. The Company's significant operations up to the date of separation have historically been included in Varian's U.S. federal and state income tax returns and non-U.S. jurisdiction tax returns. Material liabilities arising related to the pre-spin operations

would be the responsibility of Varian. Other periods for entities acquired are still open and subject to examination. Generally, periods prior to 2009 are no longer subject to examination.

## 15. SEGMENT INFORMATION

The Company has two reportable operating segments Medical and Industrial. The segments align the Company's products and service offerings with customer use in medical and industrial markets and are consistent with how the Company's Chief Executive Officer, who is also its CODM, evaluates the business for the allocation of resources. The CODM allocates resources to and evaluates the financial performance of each operating segment primarily based on revenues and gross margin. The operating and reportable segment structure provides alignment between business strategies and operating results.

### *Description of Segments*

The Medical segment designs, manufactures, sells and services X-ray imaging components for use in a range of applications, including radiographic and fluoroscopic imaging, mammography, computed tomography, radiation therapy and computer-aided detection. The Company provides a broad range of X-ray imaging components for Medical customers including X-ray tubes, digital flat panel detectors, generators, high voltage connectors, image-processing software and workstations, computer-aided diagnostic software, collimators, automatic exposure control devices, generators, ionization chambers and buckys. The Company's X-ray imaging components are primarily sold to imaging system OEM customers that incorporate them into their medical diagnostic, radiation therapy, dental, veterinary and industrial imaging systems. The Company also sells its X-ray imaging components to independent service companies, distributors and directly to end-users for replacement purposes.

The Industrial segment designs, manufactures, sells and services products for use in the security and industrial inspection applications, such as airport security, cargo screening at ports and borders and nondestructive examination in a variety of applications. The products include Linatron X-ray accelerators, X-ray tubes, digital flat panel detectors, high voltage connectors and image processing software that we generally sell to OEM customers that incorporate these products into their inspection systems.

Accordingly, the following information is provided for purposes of achieving an understanding of operations, but it may not be indicative of the financial results of the reported segments were they independent organizations. In addition, comparisons of the Company's operations to similar operations of other companies may not be meaningful.

Information related to the Company's segments is as follows:

(In millions)	Fiscal Year		
	2019	2018	2017
Revenues			
Medical	\$ 596.8	\$ 602.0	\$ 556.9
Industrial	183.8	171.4	141.2
Total revenues	780.6	773.4	698.1
Gross margin			
Medical	188.9	190.5	193.6
Industrial	67.8	63.4	59.9
Total gross margin	256.7	253.9	253.5
Total operating expenses	211.0	209.4	169.8
Interest and other expenses, net	(24.2)	(18.8)	(8.9)
Earnings before taxes	21.5	25.7	74.8
Taxes (benefit) on earnings	5.7	(2.6)	22.8
Net earnings	15.8	28.3	52.0
Less: Net earnings attributable to noncontrolling interests	0.3	0.8	0.4
Net earnings attributable to Varex	\$ 15.5	\$ 27.5	\$ 51.6

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The following table summarizes the Company's total assets by its reportable segments:

(In millions)	September 27, 2019	September 28, 2018
<b>Identifiable assets:</b>		
Medical	\$ 794.3	\$ 770.6
Industrial	244.6	217.3
Total reportable segments	<u>\$ 1,038.9</u>	<u>\$ 987.9</u>

### Geographic Information

(In millions)	Revenues			Property, plant and equipment, net	
	Fiscal Years			Fiscal Years	
	2019	2018	2017	2019	2018
United States	\$ 275.3	\$ 268.8	\$ 231.9	\$ 122.6	\$ 127.9
Latin America	7.3	7.0	7.9	—	—
EMEA	269.0	254.5	219.5	11.4	8.7
APAC	229.0	243.1	238.8	8.3	8.3
Total company	<u>\$ 780.6</u>	<u>\$ 773.4</u>	<u>\$ 698.1</u>	<u>\$ 142.3</u>	<u>\$ 144.9</u>

The Company operates various manufacturing and marketing operations outside the United States. Latin America includes Brazil and Mexico. EMEA includes Europe, Russia, the Middle East, India and Africa. APAC includes Asia and Australia. Revenues by region are based on the known final destination of products sold.

## 16. EMPLOYEE BENEFIT PLANS

Varex's 401(k) plan became effective on January 1, 2017. Varex's 401(k) plan is intended to be qualified under Section 401(a) of the Code with the 401(k) plan's related trust intended to be tax exempt under Section 501(a) of the Code and intended for all full-time employees in the United States. This plan allows employees to contribute a portion of their pretax salary up to the maximum dollar limitation prescribed by the Internal Revenue Service. Prior to Varex's 401(k) plan becoming effective, Company employees participated in Varian's 401(k) plan. The Company made matching contributions to the plan totaling \$6.7 million, \$6.5 million and \$4.3 million in fiscal years 2019, 2018 and 2017, respectively.

The Company also maintains defined benefit plans for employees located outside the US. The net pension liability is included in non-current liability on the Company's consolidated balance sheets and totaled \$5.5 million and \$3.3 million as of September 27, 2019 and September 28, 2018, respectively. The Company's net periodic benefit costs for the Company's defined benefit plans was not material for fiscal years 2019, 2018 and 2017.

## 17. OTHER COMPREHENSIVE INCOME

The following table presents the changes in the accumulated balances for each component of other comprehensive income (loss):

(In millions)	Unrealized Gain (Loss) on Derivative Financial Instruments	Unrealized Gain on Defined Benefit Obligations	Accumulated Other Comprehensive Income
Balance at September 28, 2018	\$ 5.8	\$ —	\$ 5.8
Other comprehensive loss before reclassifications	(8.3)	(1.9)	(10.2)
Income tax benefit	2.1	0.6	2.7
Balance at September 27, 2019	<u>\$ (0.4)</u>	<u>\$ (1.3)</u>	<u>\$ (1.7)</u>

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No amounts were reclassified out of accumulated other comprehensive income during fiscal years 2019 and 2018.

## 18. REVENUE RECOGNITION

The Company adopted ASC 606 on September 29, 2018, using the modified retrospective method for all contracts not completed as of the date of adoption. The reported results for fiscal year 2019 reflect the application of ASC 606 guidance while the reported results for fiscal year 2018 were prepared under the guidance of ASC 605, "Revenue Recognition." The primary impacts of the adoption include: (1) recording a separate contract liability and contract asset related to the sale of X-ray tubes that were sold with an option for the customer to require the Company to repurchase specific parts of the X-ray tube at a specific price; and (2) recording a liability related to the deferral of revenue for service type warranties that are provided to certain customers who purchase Linatron® X-ray accelerators.

The Company has made the following accounting policy elections and elected to use certain practical expedients, as permitted by the FASB, in applying ASC 606: (1) the Company accounts for amounts collected from customers for sales and other taxes, net of related amounts remitted to tax authorities; (2) the Company does not adjust the promised amount of consideration for the effects of a significant financing component, if, at contract inception, the Company expects the period between the time when the Company transfers a promised good or service to the customer and the time when the customer pays for that good or service will be one year or less; (3) the Company expenses costs to obtain a contract as they are incurred if the expected period of benefit, and therefore the amortization period, is one year or less; (4) the Company accounts for shipping and handling activities that occur after control transfers to the customer as a fulfillment cost rather than an additional promised service and these fulfillment costs are included as a component of cost of revenues; and (5) the Company does not assess whether promised goods or services are performance obligations if they are immaterial in the context of the contract with the customer.

### *Transaction price and allocation to performance obligations*

Transaction prices of products or services are typically based on contracted rates. To the extent that the transaction price includes variable consideration, the Company estimates the amount of variable consideration that should be included in the transaction price utilizing the expected value method when there is a large number of transactions with similar characteristics or the most likely amount method when there are two possible outcomes, depending on the circumstances of the transaction, to which the Company expects to be entitled. Variable consideration is included in the transaction price if, in the Company's judgment, it is probable that a significant future reversal of cumulative revenue under the contract will not occur. Estimates of variable consideration and determination of whether to include estimated amounts in the transaction price are based largely on an assessment of the Company's anticipated performance and all information (historical, current and forecasted) that is reasonably available.

The Company allows customers to return specific parts of purchased X-ray tubes for a partial refund credit, which is identified as variable consideration. ASC 606-10-55-23 requires that for sales with a right of return, revenue is reduced for expected returns, a liability is recorded for expected returns, and an asset is recorded for the right to recover products from customers on settling the liability. The Company recognizes a reduction to revenue and cost of sales at the time of sale and a corresponding contract liability and contract asset. The Company records this estimate based on the historical volume of product returns and adjusts the estimate on a quarterly basis based on the current quarter sales and current quarter returns.

If a contract contains a single performance obligation, the entire transaction price is allocated to the single performance obligation. Contracts that contain multiple performance obligations require an allocation of the transaction price based on the estimated relative standalone selling prices of the promised products or services underlying each performance obligation. The Company determines standalone selling prices based on the price at which the performance obligation is sold separately.

The beginning net cumulative-effect adjustment to the balance sheet for the adoption of ASC 606 is as follows:

(In millions)	Balance at September 28, 2018	Adjustment Due to ASC 606	Balance at September 29, 2018
<b>Assets:</b>			
Prepaid expenses and other current assets	\$ 17.1	\$ 6.4	\$ 23.5
Other assets	16.5	18.0	34.5
<b>Liabilities and Equity:</b>			
Deferred revenues	13.2	0.3	13.5
Accrued liabilities	47.5	7.1	54.6
Deferred tax liabilities	23.2	(0.8)	22.4
Other long-term liabilities	8.5	21.3	29.8
Retained earnings	62.4	(3.5)	58.9



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The following tables compare the reported consolidated balance sheet and statement of operations for fiscal year ended September 27, 2019, to the amounts that would have been reported if ASC 605 had been in effect:

(In millions)	September 27, 2019	
	Balance without Adoption	As Reported
<b>Assets:</b>		
Prepaid expenses and other current assets	\$ 13.1	\$ 19.3
Other assets	\$ 10.0	\$ 27.5
<b>Liabilities and equity:</b>		
Deferred revenues	\$ 9.9	\$ 10.5
Accrued liabilities	\$ 68.8	\$ 75.7
Deferred tax liabilities	\$ 9.1	\$ 8.2
Other long-term liabilities	\$ 12.1	\$ 32.5
Retained earnings	\$ 77.7	\$ 74.4

(In millions)	Twelve Months Ended September 27, 2019	
	Balance without Adoption	As Reported
Revenues	781.2	780.6
Cost of revenues	524.7	523.9
Taxes on earnings	5.7	5.7
Net earnings attributable to Varex	15.3	15.5

### ***Contracts and performance obligations***

The Company accounts for a contract with a customer when there is an approval and commitment from both parties, the rights of the parties are identified, payment terms are identified, the contract has commercial substance and collectability of the consideration is probable. The Company's performance obligations consist mainly of transferring control of products and services identified in the contracts or purchase orders. For each contract, the Company considers the obligation to transfer products and services to the customer, which are distinct, to be performance obligations.

### ***Revenue recognition***

Revenue is recognized when, or as, obligations under the terms of a contract are satisfied, which occurs when control of the promised products or services is transferred to customers. Revenue is measured as the amount of consideration the Company expects to receive in exchange for transferring products or services to a customer.

Product revenue is recognized when the customer obtains control of the Company's product, which occurs at a point in time, and may be upon shipment or upon delivery based on the contractual shipping terms of a contract.

Service revenue is recognized over time as the services are rendered to the customer based on the extent of progress towards completion of the performance obligation. The Company recognizes service revenue over the term of the service contract. Services are expected to be transferred to the customer throughout the term of the contract and the Company believes recognizing revenue ratably over the term of the contract best depicts the transfer of value to the customer.

### ***Disaggregation of Revenue***

Revenue is disaggregated from contracts between geography and by reportable operating segment, which the Company believes best depicts how the nature, amount, timing, and uncertainty of revenues and cash flows are affected by economic factors. Refer to Note 15. *Segment Information*, included in this report, for the disaggregation of the Company's revenue based on reportable operating segments and disaggregated by geographic region.



### ***Contract Balances***

Contract assets are included within the prepaid expenses and other current assets, and other assets balances. Contract liabilities, which also includes refund obligations are included within the accrued liabilities, deferred revenues, and other long-term liabilities balances. The following table summarizes the changes in the contract assets and refund liabilities for the twelve months ended September 27, 2019:

<b>(In millions)</b>		<b>Contact Assets</b>	
Balance at September 29, 2018		\$	24.4
Costs recovered from product returns during the period			(6.4)
Contract asset from shipments of products, subject to return during the period			5.7
Balance at September 27, 2019		\$	23.7

<b>(In millions)</b>		<b>Refund Liabilities</b>	
Balance at September 29, 2018		\$	27.1
Recognition of revenue included in beginning of year refund liability			(7.0)
Additions to refund liabilities			6.3
Balance at September 27, 2019		\$	26.4

### ***Remaining Performance Obligations***

Remaining performance obligations represent the transaction price of firm orders for which revenue has not yet been recognized. As of September 27, 2019, total remaining performance obligations amounted to \$265.2 million. The Company expects to recognize a majority of the remaining performance obligations over the next 12 months.

### ***Costs to Obtain or Fulfill a Customer Contract***

The Company has certain costs to obtain and fulfill a customer contract, such as commissions and shipping costs. The Company recognizes the incremental costs of obtaining contracts as an expense when incurred if the amortization period of the assets that the Company otherwise would have recognized is one year or less. Incremental costs of obtaining contracts that would be recognized over greater than one year are not material. The Company accounts for shipping and handling activities related to contracts with customers as costs to fulfill the promise to transfer the associated products. These costs are included as a component of cost of revenues.

## **19. SUBSEQUENT EVENTS**

On October 1, 2019, the Company, in accordance with the terms of the Credit Agreement, provided notice to the administrative agent that effective as of October 8, 2019, the Company was permanently reducing the revolving credit commitment under the Credit Agreement by \$25.0 million to \$125.0 million. The reduction in the revolving credit commitment will also reduce the fees paid by the Company in connection with such commitment.