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

FORM 10-Q

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

For the quarterly period ended January 3, 2020

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	**81-3434516**
(State or other jurisdiction of incorporation or organization)	**(I.R.S. Employer Identification Number)**

1678 S. Pioneer Road	**Salt Lake City Utah**	**84104**
(Address of principal executive offices)		**(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

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	☒	Accelerated filer	☐
Non-Accelerated filer	☐	Smaller reporting company	☐

Emerging growth company ☐

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 February 11, 2020, there were 38.5 million shares of the registrant's common stock outstanding.

VAREX IMAGING CORPORATION

FORM 10-Q for the Quarter Ended January 3, 2020

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PART I

FINANCIAL INFORMATION

Item 1. Financial Statements

VAREX IMAGING CORPORATION
CONDENSED CONSOLIDATED STATEMENTS OF EARNINGS
(Unaudited)

	Three Months Ended	
(In millions, except per share amounts)	**January 3, 2020**	**December 28, 2018**
Revenues, net	$ 200.1	$ 185.7
Cost of revenues	139.0	125.7
Gross margin	61.1	60.0
Operating expenses:		
Research and development	21.7	18.8
Selling, general and administrative	34.8	30.8
Total operating expenses	56.5	49.6
Operating earnings	4.6	10.4
Interest expense	(5.4)	(5.1)
Other expense, net	(0.4)	(1.2)
Interest and other expense, net	(5.8)	(6.3)
(Loss) earnings before taxes	(1.2)	4.1
Taxes on earnings	—	1.1
Net (loss) earnings	(1.2)	3.0
Less: Net earnings attributable to noncontrolling interests	0.1	—
Net (loss) earnings attributable to Varex	$ (1.3)	$ 3.0
Net (loss) earnings per common share attributable to Varex		
Basic	$ (0.03)	$ 0.08
Diluted	$ (0.03)	$ 0.08
Weighted average common shares outstanding		
Basic	38.5	38.1
Diluted	38.5	38.3

See accompanying notes to the condensed consolidated financial statements.

VAREX IMAGING CORPORATION
CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE (LOSS) EARNINGS
(Unaudited)

	Three Months Ended	
(In millions)	**January 3, 2020**	**December 28, 2018**
Net (loss) earnings	$ (1.2)	$ 3.0
Other comprehensive (loss) earnings, net of tax:		
Unrealized (loss)/gain on interest rate swap contracts	—	(2.3)
Foreign currency translation adjustments	(0.9)	—
Other comprehensive (loss) earnings, net of tax	(0.9)	(2.3)
Comprehensive (loss) earnings	(2.1)	0.7
Less: Comprehensive earnings attributable to noncontrolling interests	0.1	—
Comprehensive (loss) earnings attributable to Varex	$ (2.2)	$ 0.7

See accompanying notes to the condensed consolidated financial statements.

VAREX IMAGING CORPORATION
CONDENSED CONSOLIDATED BALANCE SHEETS
(Unaudited)

(In millions, except share and per share amounts)	January 3, 2020	September 27, 2019
Assets		
Current assets:		
Cash and cash equivalents	$ 30.0	$ 29.9
Accounts receivable, net	122.9	141.0
Inventories	269.1	248.2
Prepaid expenses and other current assets	18.2	19.3
Total current assets	440.2	438.4
Property, plant and equipment, net	146.2	142.3
Goodwill	290.8	290.8
Intangible assets, net	81.8	86.3
Investments in privately-held companies	54.9	53.6
Operating lease assets	25.1	—
Other assets	29.4	27.5
Total assets	$ 1,068.4	$ 1,038.9
Liabilities, redeemable noncontrolling interests and equity		
Current liabilities:		
Accounts payable	$ 73.2	$ 58.2
Accrued liabilities and other current liabilities	70.9	75.7
Current operating lease liabilities	6.7	—
Current maturities of long-term debt	30.4	30.7
Deferred revenues	9.7	10.5
Total current liabilities	190.9	175.1
Long-term debt, net	350.9	364.4
Deferred tax liabilities	8.9	8.2
Operating lease liabilities	19.2	—
Other long-term liabilities	36.6	32.5
Total liabilities	606.5	580.2
Commitments and contingencies		
Redeemable noncontrolling interests	10.7	10.5
Equity:		
Preferred stock, $.01 par value: 20,000,000 shares authorized, none issued	—	—
Common stock, $.01 par value:		
Authorized shares - 150,000,000		
Shares issued and outstanding - 38,494,349 and 38,371,305 at January 3, 2020 and September 27, 2019, respectively.	0.4	0.4
Additional paid-in capital	377.6	371.8
Accumulated other comprehensive loss	(2.6)	(1.7)
Retained earnings	72.5	74.4
Total Varex equity	447.9	444.9
Noncontrolling interests	3.3	3.3
Total equity	451.2	448.2
Total liabilities, redeemable noncontrolling interests and equity	$ 1,068.4	$ 1,038.9

See accompanying notes to the condensed consolidated financial statements.

VAREX IMAGING CORPORATION
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
(Unaudited)

	Three Months Ended	
(In millions)	**January 3, 2020**	**December 28, 2018**
Cash flows from operating activities:		
Net (loss) earnings	$ (1.2)	$ 3.0
Adjustments to reconcile net earnings to net cash provided by operating activities:		
Share-based compensation expense	3.2	2.6
Depreciation	5.2	9.8
Amortization of intangible assets	4.5	3.7
Deferred taxes	0.5	(2.5)
Income from equity method investments	(0.7)	(0.8)
Amortization of deferred loan costs	0.6	0.6
Other, net	—	0.1
Changes in assets and liabilities, net of effects of acquisition:		
Accounts receivable	18.5	20.6
Inventories	(21.1)	(22.0)
Prepaid expenses and other assets	3.7	3.7
Accounts payable	15.4	(0.5)
Accrued liabilities and other current and long-term operating liabilities	(4.8)	3.1
Deferred revenues	(0.8)	(1.4)
Net cash provided by operating activities	23.0	20.0
Cash flows from investing activities:		
Purchases of property, plant and equipment	(8.1)	(3.4)
Acquisitions of businesses, net of cash acquired	(1.2)	—
Contributions and advances to joint ventures	(1.3)	—
Net cash used in investing activities	(10.6)	(3.4)
Cash flows from financing activities:		
Borrowings under credit agreements	3.0	4.0
Repayments of borrowing under credit agreements	(17.8)	(19.0)
Proceeds from exercise of stock options	1.1	—
Proceeds from shares issued under employee stock purchase plan	1.8	1.9
Other financing activities	(0.1)	—
Net cash used in financing activities	(12.0)	(13.1)
Effects of exchange rate changes on cash and cash equivalents and restricted cash	(0.3)	(0.4)
Net increase in cash and cash equivalents and restricted cash	0.1	3.1
Cash and cash equivalents and restricted cash at beginning of period	31.3	53.4
Cash and cash equivalents and restricted cash at end of period	$ 31.4	$ 56.5
Supplemental cash flow information:		
Cash paid for interest	$ 5.0	$ 3.0
Cash paid for income tax	0.5	0.6
Supplemental non-cash activities:		
Purchases of property, plant and equipment financed through accounts payable	$ 0.8	$ 1.8

See accompanying notes to the condensed consolidated financial statements.

VAREX IMAGING CORPORATION
CONDENSED CONSOLIDATED STATEMENTS OF EQUITY
(Unaudited)

	Three Months Ended January 3, 2020							
	Common Stock		Additional Paid-in Capital	Accumulated Other Comprehensive Loss	Retained Earnings	Total Varex Equity	Noncontrolling Interests	Total Equity
(In millions)	Shares	Amount						
September 27, 2019	38.4	$ 0.4	$ 371.8	$ (1.7)	$ 74.4	$ 444.9	$ 3.3	$ 448.2
Cumulative effect of accounting changes	—	—	—	—	(0.6)	(0.6)	—	(0.6)
Net earnings	—	—	—	—	(1.3)	(1.3)	—	(1.3)
Exercise of stock options	—	—	1.1	—	—	1.1	—	1.1
Common stock issued under employee stock purchase plan	0.1	—	1.8	—	—	1.8	—	1.8
Share-based compensation	—	—	3.2	—	—	3.2	—	3.2
Currency translation adjustments	—	—	—	(0.9)	—	(0.9)	—	(0.9)
Other	—	—	(0.3)	—	—	(0.3)	—	(0.3)
January 3, 2020	38.5	$ 0.4	$ 377.6	$ (2.6)	$ 72.5	$ 447.9	$ 3.3	$ 451.2

	Three Months Ended December 28, 2018							
	Common Stock		Additional Paid-in Capital	Accumulated Other Comprehensive Income (Loss)	Retained Earnings	Total Varex Equity	Noncontrolling Interests	Total Equity
(In millions)	Shares	Amount						
September 28, 2018	38.0	$ 0.4	$ 357.6	$ 5.8	$ 62.4	$ 426.2	$ 2.1	$ 428.3
Cumulative effect of accounting change	—	—	—	—	(4.1)	(4.1)	—	(4.1)
Net earnings	—	—	—	—	3.0	3.0	(0.2)	2.8
Common stock issued under employee stock purchase plan	0.1	—	1.9	—	—	1.9	—	1.9
Share-based compensation	—	—	2.6	—	—	2.6	—	2.6
Unrealized loss on interest rate swap contracts, net of tax	—	—	—	(2.3)	—	(2.3)	—	(2.3)
December 28, 2018	38.1	$ 0.4	$ 362.1	$ 3.5	$ 61.3	$ 427.3	$ 1.9	$ 429.2

See accompanying notes to the condensed consolidated financial statements.

VAREX IMAGING CORPORATION
NOTES TO THE CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited)

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 imaging systems, to independent service companies, distributors and directly to end-users for replacement purposes.

The Company also designs, manufacturers, 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 and is listed on the NASDAQ Global Select Market under the ticker "VREX."

Basis of Presentation and Principle of Consolidation

The accompanying condensed consolidated financial statements are unaudited. These condensed consolidated financial statements 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 of America ("GAAP"). In the opinion of management, these condensed consolidated financial statements include all adjustments, consisting only of normal recurring adjustments, necessary for a fair statement of the results for the interim periods.

These condensed consolidated financial statements and the accompanying notes are unaudited and should be read in conjunction with the consolidated financial statements for the fiscal years ended 2019, 2018 and 2017 included in the Company's Form 10-K, which was filed with the SEC on December 20, 2019. The Company considers events or transactions that occur after the balance sheet date, but before the financial statements are issued, to provide additional evidence relative to certain estimates or to identify matters that require additional disclosures. Except for the change in certain policies upon adoption of the accounting standards described below, there have been no material changes to the Company's significant accounting policies, compared to the accounting policies described in Note 1, *Summary of Significant Accounting Policies*, in the Company's Annual Report on Form 10-K for fiscal year 2019.

Segment Reporting

The Company has two reportable operating segments, Medical and Industrial, which align with how its Chief Executive Officer, who has been identified as the Company's Chief Operating Decision Maker ("CODM"), views and measures the Company's business performance. See Note 16, *Segment Information*, 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 2020 is the 53-week period ending October 2, 2020. Fiscal year 2019 was the 52-week period that ended on September 27, 2019. The fiscal quarters ended January 3, 2020 and December 28, 2018 were 14-week and 13-week periods, respectively.

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 condensed 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.

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 condensed consolidated balance sheet. Cash and cash equivalents and restricted cash as reported within the condensed consolidated statements of cash flows consisted of the following:

	Three Months Ended January 3, 2020		Three Months Ended December 28, 2018	
	Beginning of Period	End of Period	Beginning of Period	End of Period
Cash and cash equivalents	$ 29.9	$ 30.0	$ 51.9	$ 55.1
Restricted cash	1.4	1.4	1.5	1.4
Cash and cash equivalents and restricted cash as reported per statement of cash flows	$ 31.3	$ 31.4	$ 53.4	$ 56.5

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, as follows:

	Three Months Ended	
	January 3, 2020	December 28, 2018
Canon Medical Systems Corporation	18.8%	18.3%

Canon Medical Systems Corporation accounted for 14.5% and 10.1% of the Company’s accounts receivable as of January 3, 2020 and September 27, 2019, respectively.

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, 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.

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, the Company bases warranty

estimates on historical experience for similar products and adds 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:

	Three Months Ended	
(In millions)	**January 3, 2020**	**December 28, 2018**
Accrued product warranty, at beginning of period	$ 8.1	$ 7.3
Charged to cost of revenues	4.1	2.0
Product warranty expenditures	(3.2)	(2.7)
Accrued product warranty, at end of period	$ 9.0	$ 6.6

Leases

The Company determines if an arrangement is or contains a lease at the inception of an arrangement. The Company's operating lease right-of-use ("ROU") assets represents the right to use an underlying asset over the lease term and lease liabilities represent its obligation to make lease payments arising from the lease. ROU assets may also include initial direct costs incurred and prepaid lease payments, less lease incentives. Lease liabilities and their corresponding ROU assets are recognized based on the present value of lease payments over the lease term, discounted using the Company's incremental borrowing rate ("IBR"). The Company recognizes operating leases with lease terms of more than twelve months in operating lease assets, current operating lease liabilities, and operating lease liabilities on its condensed consolidated balance sheets. The Company recognizes finance leases with lease terms of more than twelve months in property, plant, and equipment, net, accrued liabilities and other current liabilities, and other long-term liabilities on its condensed consolidated balance sheets. For purposes of calculating lease liabilities and the corresponding ROU assets, the Company's lease term may include options to extend or terminate the lease when it is reasonably certain that it will exercise that option.

Recently Adopted Accounting Pronouncements

In February 2016, the Financial Accounting Standards Board (the"FASB") issued Accounting Standards Update ("ASU") No. 2016-02, Leases ("Topic 842"), referred to as ASC 842. The purpose of ASC 842 is to increase the transparency and comparability among organizations by recognizing lease assets and liabilities on the balance sheet, including those previously classified as operating leases under U.S. GAAP, and disclosing key information about leasing arrangements. ASC 842, as amended, is effective for public entities for annual periods beginning after December 15, 2018, including interim periods within those annual periods and is effective for the Company in fiscal year 2020. The Company adopted the standard using the transition method provided by ASC Update No. 2018-11, Leases ("Topic 842"): Targeted Improvements. Under this method, the Company applied the new leasing rules on September 28, 2019, rather than at the earliest comparative period presented in the financial statements. Prior periods were presented in accordance with the existing lease guidance under ASC 840.

Upon transition, the Company applied the package of practical expedients permitted under ASC 842 transition guidance to its entire lease portfolio at September 28, 2019. As a result, the Company was not required to reassess (i) whether any expired or existing contracts are or contain leases, (ii) the classification of any expired or existing leases, and (iii) initial direct costs for any existing leases. Also, the Company applied the hindsight practical expedient. Furthermore, as a lessee the Company elected to combine lease and non-lease components for the majority of its leases, which means that the Company accounted for each separate lease component and the non-lease components associated with that lease component as a single lease component. The only asset class that did not combine lease and non-lease components were vehicle leases.

The most significant impact of the standards for the Company relate to the recognition of the right-of-use assets and lease liabilities for the operating leases in the balance sheet. Upon adoption of the new lease standard, the Company recognized operating lease right-of-use assets and finance lease right-of-use assets of $26.8 million and $0.6 million, respectively, and corresponding operating lease liabilities and finance lease liabilities of $27.5 million and $0.6 million, respectively. This includes the recording of the Company's existing capital leases as finance leases at transition. The cumulative impact of adoption was a $0.3 million decrease to retained earnings. Refer to Note 3, *Leases,* for a detailed impact of adopting this standard and its impact on the consolidated financial statements and related disclosures.

In February 2018, the FASB issued ASU 2018-02, *Reclassification of Certain Tax Effects from Accumulated Other Comprehensive Income*, which provides the option to reclassify certain income tax effects related to the Tax Cuts and Jobs Act passed

in December of 2017 between accumulated other comprehensive income and retained earnings and also requires additional

disclosures. The amendments in this ASU are effective for all entities for fiscal years beginning after December 15, 2018, and interim periods within those fiscal years. Effective September 28, 2019, the Company adopted ASU 2018-02 and it did not have a material effect on the Company's financial statements and related disclosures.

Recent Accounting Standards or Updates Not Yet Effective

In December 2019, the FASB issued ASU 2019-12 which simplifies the accounting for income taxes by removing certain exceptions to the current guidance, and improving the consistent application of and simplification of other areas of the guidance. The standard is effective for the Company beginning in the first quarter of fiscal year 2022. Early adoption is permitted. The Company is evaluating the impact of adopting this guidance to its condensed 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. Early adoption is permitted. The Company is evaluating the impact of adopting this amendment to its condensed 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 evaluating the potential impact of this standard to its condensed consolidated financial statements.

2. REVENUE RECOGNITION

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 accounts for revenue in accordance with ASC Topic 606, *Revenue from Contracts with Customers*.

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.

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.

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 generally 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 generally 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.

The following table disaggregates the Company’s revenue by geographic region:

	Three Months Ended	
(In millions)	**January 3, 2020**	**December 28, 2018**
Americas	$ 70.3	$ 68.4
EMEA	65.2	62.6
APAC	64.6	54.7
	$ 200.1	$ 185.7

Revenue in the United States of America was $68.9 million and $67.2 million for the three months ended January 3, 2020 and December 28, 2018, respectively.

Refer to Note 16, *Segment Information*, for the disaggregation of the Company’s revenue based on reportable operating segments.

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 and other current liabilities, deferred revenues, and other long-term liabilities balances. The following table summarizes the changes in the contract assets and refund liabilities for the three months ended January 3, 2020:

(In millions)	**Contract Assets**
Balance at September 28, 2019	$ 23.7
Costs recovered from product returns during the period	(0.8)
Contract asset from shipments of products, subject to return during the period	1.6
Balance at January 3, 2020	$ 24.5

(In millions)	Refund Liabilities
Balance at September 28, 2019	$ 26.4
Release of refund liability included in beginning of year refund liability	(0.9)
Additions to refund liabilities	1.7
Balance at January 3, 2020	$ 27.2

Remaining Performance Obligations

Remaining performance obligations represent the transaction price of firm orders for which revenue has not yet been recognized. As of January 3, 2020, total remaining performance obligations amounted to $268.3 million. The Company expects to recognize 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.

3. LEASES

On September 28, 2019, the Company adopted a new accounting standard that amends the guidance for the accounting and reporting of leases. The determination of whether an arrangement is, or contains, a lease is performed at the inception of the arrangement. The Company has operating and finance leases for office space, warehouse and manufacturing space, vehicles and certain equipment. The Company's lease agreements do not contain any material residual value guarantees, variable lease costs, bargain purchase options or restrictive covenants. The Company does not have any lease transactions with related parties. Leases with an initial term of 12 months or less are generally not recorded on the balance sheet and expense for these leases is recognized on a straight-line basis over the lease term. The Company's leases have remaining lease terms of one year to approximately five years, some of which may include options to extend the leases for up to six years and some include options to terminate early. These options have been included in the determination of the lease liability when it is reasonably certain that the option will be exercised.

Right-of-use assets represent the Company's right to use an underlying asset for the lease term and lease liabilities represent the Company's obligation to make lease payments arising from the lease contract. Operating lease liabilities and their corresponding right-of-use assets are recorded based on the present value of fixed lease payments over the expected lease term. The interest rate implicit in lease contracts is typically not readily determinable. As such, our incremental borrowing rate is based on a credit-adjusted risk-free rate, which best approximates a secured rate over a similar term of lease.

The following table presents supplemental balance sheet information related to the Company's operating and finance leases:

		January 3, 2020	
(In millions)	**Balance Sheet Location**	**Operating Leases**	**Finance Leases**
Assets			
Operating lease right-of-use assets	*Operating lease assets*	$ 25.1	$ —
Finance lease right-of-use assets	*Property, plant and equipment, net*	$ —	$ 0.6
Liabilities			
Operating lease liabilities (current)	*Current operating lease liabilities*	$ 6.7	$ —
Finance lease liabilities (current)	*Accrued liabilities and other current liabilities*	$ —	$ 0.2
Operating lease liabilities (non-current)	*Operating lease liabilities*	$ 19.2	$ —
Finance lease liabilities (non-current)	*Other long-term liabilities*	$ —	$ 0.4

The following table presents the weighted average remaining lease term and discount rate information related to the Company's operating and finance leases:

	January 3, 2020	
	Operating Leases	**Finance Leases**
Weighted average remaining lease term (in years)	5.2	3.0
Weighted average discount rate	4.2%	3.8%

The following table provides information related to the Company’s operating and finance leases:

(In millions)	**Three Months Ended January 3, 2020**
Total operating lease costs (a)	$ 2.1
Total finance lease costs	$ 0.1
Operating cash flows from operating leases	$ 2.0
Financing cash flows from finance leases	0.1
Total cash paid for amounts included in the measurement of lease liabilities	$ 2.1

(a) Includes variable and short-term lease expense, which were immaterial for the three months ended January 3, 2020.

As of January 3, 2020, maturities of operating lease and finance lease liabilities for each of the following five years and a total thereafter were as follows:

(In millions)		
Fiscal years:	**Operating Leases**	**Finance Leases**
2020 remaining	$ 5.8	$ 0.2
2021	6.5	0.2
2022	5.6	0.1
2023	3.3	0.1
2024	2.5	—
Thereafter	5.3	—
Total future lease payments	$ 29.0	$ 0.6
Less: imputed interest	(3.2)	—
Present value of lease liabilities	25.8	0.6

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.

4. BUSINESS COMBINATION

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.

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
Total assets acquired	$	89.8
Accounts payable	$	(1.0)
Accrued liabilities and other current 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)
Total liabilities assumed	$	(9.0)
Noncontrolling interest	$	(1.4)
Net assets acquired, less noncontrolling interest	$	79.4
Net cash paid	$	69.5
Deferred consideration		9.9
Total consideration	$	79.4

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 January 3, 2020, the Company had not finalized the determination of the fair values allocated to various assets and liabilities, including, but not limited to, 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	$	32.9	

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

During the first quarter of fiscal year 2020, the Company made a $1.2 million acquisition to enhance our X-ray tube development and manufacturing operations.

5. 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 operating 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. During the three months ended January 3, 2020 and December 28, 2018, the Company recorded (loss) and income on the equity investment in dpiX Holding of $0.9 million and $(0.7) million, respectively. Income and loss on the equity investment in dpiX Holding is included in other expense, net in the condensed consolidated statements of earnings. The carrying value of the equity investment in dpiX Holding was $48.5 million and $48.1 million at January 3, 2020 and September 27, 2019, respectively.

During the three months ended January 3, 2020 and December 28, 2018, the Company purchased glass transistor arrays from dpiX totaling $5.9 million and $2.8 million, respectively. These purchases of glass transistor arrays are included as a component of inventories on the condensed consolidated balance sheets or cost of revenues in the condensed consolidated statements of earnings.

As of January 3, 2020, and September 27, 2019, the Company had accounts payable to dpiX totaling $3.4 million and $3.6 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 January 3, 2020, the Company had no remaining fixed cost commitments related to the agreement remaining for calendar year 2019. In January 2020, the fixed cost commitment was determined and approved by the dpiX board of directors to be $12.7 million for calendar year 2020. The amended agreement will continue unless the ownership structure of dpiX changes as provided 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 $48.5 million and fixed cost commitments.

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 for use 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. As of January 3, 2020, the Company has made contributions totaling $4.2 million, and has committed to contribute an additional $1.1 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 $3.0 million and $2.0 million at January 3, 2020 and September 27, 2019, respectively .

6. RESTRUCTURING

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 September 2020 and all activities related to the closure of the facility to be complete by the end of December 2020. In connection with the relocation of the glass production and site closure the Company recorded $0.8 million and $5.1 million for the three months ended January 3, 2020 and December 28, 2018, respectively. The Company expects to incur an additional $7.3 million to $11.3 million of restructuring charges through December 2020.

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 three months ended January 3, 2020 and December 28, 2018, respectively, which predominately relate to the Company's Medical segment:

		Three Months Ended	
(In millions)	**Location of Restructuring Charges in Consolidated Statements of Earnings**	**January 3, 2020**	**December 28, 2018**
Accelerated depreciation	Cost of revenues	$ 0.3	$ 4.2
Severance costs	Selling, general and administrative	0.5	0.9
Total restructuring charges		$ 0.8	$ 5.1

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 January 3, 2020, the Company had the following outstanding derivatives designated as hedging instruments:

(In millions, except for number of instruments)	**Number of Instruments**	**Notional Value**
Interest Rate Swap Contracts	6	$ 253.1

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:

	Amount of Gain (Loss) Recognized in OCI on Derivative Three months ended		**Location of Gain or (Loss) Reclassified from Accumulated OCI into Income**	**Amount of Gain (Loss) Reclassified from Accumulated OCI into Income Three months ended**	
(In millions)	**January 3, 2020**	**December 28, 2018**		**January 3, 2020**	**December 28, 2018**
Interest Rate Swap Contracts	$ —	$ (2.5)	Interest expense	$ —	$ 0.4

The Company expects that approximately $(0.3) 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. The following table summarizes the 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 and Liabilities	
Derivatives designated as cash flow hedges	**Balance sheet location**	**January 3, 2020**	**September 27, 2019**
Interest rate swap contracts	Accrued liabilities and other current liabilities	$ (0.3)	$ —
Interest rate swap contracts	Other long-term liabilities	(0.2)	(0.5)
		$ (0.5)	$ (0.5)

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 January 3, 2020, 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:

	Amount of Gain (Loss) Recognized in OCI on Derivative Three months 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)**	
(In millions)	**January 3, 2020**	**December 28, 2018**		**January 3, 2020**	**December 28, 2018**
Cross Currency Swap Contracts	$ (0.8)	$ —	Interest expense	$ 0.4	$ —

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 and Liabilities	
Derivatives designated as net investment hedges	**Balance sheet location**	**January 3, 2020**	**September 27, 2019**
Cross Currency Swap Contracts	Other current assets	$ 1.3	$ —
Cross Currency Swap Contracts	Other long-term liabilities	(2.2)	—
		$ (0.9)	$ —

Balance Sheet Hedges

The Company's foreign currency management objective is to mitigate the potential impact of currency fluctuations on the value of its U.S. dollar cash flows and to reduce the variability of certain cash flows at the subsidiary level. 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 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 as of January 3, 2020:

(In millions)	Notional Value of Derivatives not Designated as Hedging Instruments: Buy contracts	Sell contract
Japanese yen	$ 2.3	$ —
Swiss franc	—	(1.0)
Chinese renminbi	1.7	—
Euro	—	(3.4)
	$ 4.0	$ (4.4)

8. 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.

	Fair Value Measurements at January 3, 2020			
(In millions)	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	$ —	$ 4.7	$ —	$ 4.7
Derivative assets	—	1.3	—	1.3
Total assets measured at fair value	$ —	$ 6.0	$ —	$ 6.0
Liabilities:				
Derivative liabilities	$ —	$ 2.7	$ —	$ 2.7
Deferred consideration	9.7	—	—	9.7
Total liabilities measured at fair value	$ 9.7	$ 2.7	$ —	$ 12.4

As of January 3, 2020, the outstanding borrowings under the Company's credit agreement were $381.3 million, net of deferred loan costs, which approximated its fair value. 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. The Company has elected to use the income approach to value its derivative instruments using standard valuation techniques and Level 2 inputs, such as currency spot rates, forward points and credit default swap spreads. 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 the three months ended January 3, 2020.

At September 27, 2019, the Company determined the following levels of inputs at fair value for the following assets or liabilities:

	Fair Value Measurements at September 27, 2019			
(In millions)	**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

9. INVENTORIES

The following table summarizes the Company's inventories:

(In millions)	**January 3, 2020**	**September 27, 2019**
Raw materials and parts	$ 184.2	$ 160.1
Work-in-process	27.6	27.9
Finished goods	57.3	60.2
Total inventories	$ 269.1	$ 248.2

10. GOODWILL AND INTANGIBLE ASSETS

The following table reflect goodwill by reportable operating segment:

(In millions)	**Medical**	**Industrial**	**Total**
Balance at September 27, 2019	$ 173.0	$ 117.8	$ 290.8
Balance at January 3, 2020	$ 173.0	$ 117.8	$ 290.8

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 condensed consolidated balance sheets:

	January 3, 2020			September 27, 2019		
(In millions)	**Gross Carrying Amount**	**Accumulated Amortization**	**Net Carrying Amount**	**Gross Carrying Amount**	**Accumulated Amortization**	**Net Carrying Amount**
Acquired existing technology	$ 74.1	$ (30.8)	$ 43.3	$ 74.1	$ (28.4)	$ 45.7
Patents, licenses and other	12.7	(8.7)	4.0	12.7	(8.4)	4.3
Customer contracts and supplier relationship	50.7	(19.0)	31.7	50.7	(17.2)	33.5
Total intangible assets with finite lives	137.5	(58.5)	79.0	137.5	(54.0)	83.5
In-process R&D with indefinite lives	2.8	0.0	2.8	2.8	0.0	2.8
Total intangible assets	$ 140.3	$ (58.5)	$ 81.8	$ 140.3	$ (54.0)	$ 86.3

Amortization expense for intangible assets was $4.5 million and $3.7 million for the three months ended January 3, 2020 and December 28, 2018, respectively.

11. BORROWINGS

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

(In millions, except for percentages)	January 3, 2020 Amount	January 3, 2020 Weighted-Average Interest Rate	September 27, 2019 Amount	September 27, 2019 Weighted-Average Interest Rate	$ Change
Current maturities of long-term debt					
Term facility	$ 29.4	5.3%	$ 29.4	5.6%	$ —
Other debt	1.0		1.3		(0.3)
Total current maturities of long-term debt	$ 30.4		$ 30.7		$ (0.3)
Non-current maturities of long-term debt:					
Revolving credit facility	$ 52.0	5.3%	$ 59.0	5.6%	$ (7.0)
Term facility	301.1	5.3%	308.6	5.6%	(7.5)
Other debt	2.6		2.5		0.1
Debt issuance costs	(4.8)		(5.7)		0.9
Non-current maturities of long-term debt	350.9		364.4		(13.5)
Total long-term debt, net	$ 381.3		$ 395.1		$ (13.8)

Existing Credit Facility

On May 1, 2017 Varex entered into a new secured revolving credit facility (the “Revolving Credit Facility”) in an aggregate principal amount of up to $200 million with a term of five years, 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 million, which is subsequently amended. The Company reduced the Revolving Credit Facility to $150 million on October 3, 2018 and to $125 million on October 1, 2019. At January 3, 2020, the Company had $73.0 million of the Revolving Credit Facility available for borrowings, subject to covenants contained in the Credit Agreement. 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. 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 January 3, 2020.

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%.

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, a publicly traded 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 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.

At January 3, 2020, noncontrolling shareholders together held approximately 0.5 million shares of MeVis, representing 26.3% of the outstanding shares.

Changes in redeemable noncontrolling interests were as follows:

(In millions)	Redeemable Noncontrolling Interests	Noncontrolling Interest
Balance at beginning of period, September 27, 2019	$ 10.5	$ 3.3
Net earnings attributable to noncontrolling interests	0.1	—
Other, including foreign currency remeasurement	0.1	—
Balance at end of period, January 3, 2020	$ 10.7	$ 3.3

13. NET (LOSS) EARNINGS PER SHARE

Basic net (loss) earnings per common share is computed by dividing the net (loss) earnings for the period by the weighted average number of shares of common stock outstanding during the reporting period. Diluted net (loss) earnings per common share reflects the effects of potentially dilutive securities, which is computed by dividing net (loss) earnings by the sum of the weighted average number of common shares outstanding and dilutive common shares, which consists of shares underlying stock options, unvested stock awards and purchase rights granted under the employee stock purchase plan.

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

	Three Months Ended	
(In millions, except per share amounts)	January 3, 2020	December 28, 2018
Net earnings attributable to Varex	$ (1.3)	$ 3.0
Weighted average shares outstanding - basic	38.5	38.1
Dilutive effect of potential common shares	—	0.2
Weighted average shares outstanding - diluted	38.5	38.3
Net earnings per share attributable to Varex - basic	$ (0.03)	$ 0.08
Net earnings per share attributable to Varex - diluted	$ (0.03)	$ 0.08
Anti-dilutive shared based awards, excluded	1.7	2.1

The Company excludes potentially dilutive common shares (consisting of shares underlying stock options, unvested stock awards and purchase rights granted under 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 (loss) earnings per share. Because the

Company incurred a net loss for the three months ended January 3, 2020, none of the potentially dilutive common shares were included in the diluted share calculation for that period as they would have been anti-dilutive.

14. EMPLOYEE STOCK PLANS

Share-Based Compensation Expense

Share-based compensation expense recognized in the condensed 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.

The table below summarizes the effect of recording the share-based compensation expense (which includes the option component of the employee stock purchase plan shares):

	Three Months Ended	
(In millions)	**January 3, 2020**	**December 28, 2018**
Cost of revenues	$ 0.3	$ 0.3
Research and development	0.6	0.5
Selling, general and administrative	2.3	1.8
Total share-based compensation expense	$ 3.2	$ 2.6

Stock Option Activity

The following table summarizes the activity for stock options under Varex's 2017 Omnibus Stock Plan and 2017 Employee Stock Purchase Plan for the Company's employees:

	Options Outstanding				
(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 27, 2019	2,269	$22.63 - $37.60	$ 30.60		
Granted	—	—	—		
Canceled, expired or forfeited	(19)	$22.84 - $37.10	30.99		
Exercised	(49)	$22.84 - $22.84	22.84		
Outstanding at January 3, 2020	2,201	$22.63 - $37.60	$ 30.77	3.92	$ 1,735.0
Exercisable at January 3, 2020	1,500	$22.63 - $37.60	$ 30.04	3.34	$ 1,735.0

(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 $30.00 as of January 3, 2020, the last trading date of the Company's first quarter, 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.

Restricted Stock Units

The following table summarizes the activity for restricted stock units under Varex's 2017 Omnibus Stock Plan for the Company's employees:

(In thousands, except per share amounts)	**Number of Shares**	**Weighted Average Grant-Date Fair Value**
Balance at September 27, 2019	678	$ 33.18
Granted	3	26.78
Vested	(2)	30.21
Canceled or expired	(8)	33.49

Balance at January 3, 2020	671	$ 33.16

15. TAXES ON EARNINGS

	Three Months Ended	
	January 3, 2020	December 28, 2018
Estimated effective tax rate	0.9%	26.8%

The Company recognized an income tax benefit of $0.0 million and an income tax expense of $1.1 million for the three months ended January 3, 2020 and December 28, 2018, respectively, for effective rates of 0.9% and 26.8%, respectively.

The Company's effective tax rate for the three months ended January 3, 2020, decreased primarily due to losses in certain jurisdictions for which no benefit can be recorded due to full valuation allowance positions and a nearly equivalent overall pre-tax book loss.

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 indefinitely reinvested outside the U.S. The Company is maintaining this prior assertion for the quarter ended January 3, 2020. 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 repatriated in the form of a dividend.

16. 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:

	Three Months Ended	
(In millions)	**January 3, 2020**	**December 28, 2018**
Revenues		
Medical	$ 155.6	$ 143.9
Industrial	44.5	41.8
Total revenues	$ 200.1	$ 185.7
Gross margin		
Medical	$ 43.8	$ 45.1
Industrial	17.3	14.9
Total gross margin	$ 61.1	$ 60.0
Total operating expenses	56.5	49.6
Interest and other income (expenses), net	(5.8)	(6.3)
Earnings before taxes	(1.2)	4.1
Taxes on earnings	—	1.1
Net earnings	(1.2)	3.0
Less: Net earnings attributable to noncontrolling interests	0.1	—
Net earnings attributable to Varex	$ (1.3)	$ 3.0

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

(In millions)	**January 3, 2020**	**September 27, 2019**
Identifiable assets		
Medical	$ 830.8	$ 794.3
Industrial	237.6	244.6
Total reportable segments	$ 1,068.4	$ 1,038.9

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

The following discussion and analysis of the financial condition and results should be read together with our Annual Report on Form 10-K for the fiscal year ended September 27, 2019.

Forward-Looking Statements

This Quarterly Report on Form 10-Q (this "Quarterly Report") contains "forward-looking" statements within the meaning of the Private Securities Litigation Reform Act of 1995, which provides a "safe harbor" for statements about future events, products and future financial performance that are based on the beliefs of, estimates made by, and information currently available to the management of Varex Imaging Corporation ("we," "our," "us," the "Company," "Varex," or "Varex Imaging"). The outcome of the events described in these forward-looking statements are subject to risks and uncertainties (including the risks and uncertainties contained in Part II, Item 1A - Risk Factors of this Quarterly Report), and actual results and the outcome or timing of certain events may differ significantly from those projected in these forward-looking statements or management's current expectations.

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 that involve risks and uncertainties that could cause our actual results and the outcome and timing of certain events to differ materially from those projected or management's current expectations.

Any forward-looking statement made in this Quarterly 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. By making forward-looking statements, we have not assumed any obligation to, and you should not expect us to, update or revise those statements because of new information, future events or otherwise.

Overview

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. Varex has 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 on X-ray imaging products we sell to customers outside the United States. 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 has matured from initial product introductions that were made over 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.

To help mitigate the impact of trade war conflicts 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. 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, 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.

Critical Accounting Policies and Estimates

The preparation of our condensed 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.

We periodically review our accounting policies, estimates and assumptions and make adjustments when facts and circumstances dictate. Refer to our Annual Report on Form 10-K for the fiscal year ended September 27, 2019 filed with the SEC on December 20, 2019 and Note **1** "Summary of Significant Accounting Policies" of the notes to the condensed consolidated financial statements of this report for further details. Our critical accounting policies that are affected by accounting estimates include revenue recognition, impairment of investments, assessment of recoverability of goodwill and intangible assets, valuation of derivative instruments, valuation of warranty obligations, and taxes on earnings. Such accounting policies require us to use judgments, often as a result of the need to make estimates and assumptions regarding matters that are inherently uncertain, and actual results could differ materially from these estimates. There have been no material changes to our critical accounting policies, estimates and assumptions or the judgments affecting the application of those estimates and assumptions since the filing of our Annual Report on Form 10-K for year ended September 27, 2019, except for the adoption of Accounting Standards Update No. 2016-02, *Leases* ("Topic 842"), referred to as ASC 842, effective September 28, 2019.

Fiscal Year

Our fiscal year is a 52 or 53-week period ending on the Friday nearest September 30. Fiscal year 2020 is the 53-week period ending October 2, 2020. Fiscal year 2019 was a 52-week period that ended on September 27, 2019. The fiscal quarters ended January 3, 2020 and December 28, 2018 were 14-week and 13-week periods, respectively.

Discussion of Results of Operations for the Three Months Ended January 3, 2020 Compared to the Three Months Ended December 28, 2018

Revenues

	Three Months Ended			
(In millions)	**January 3, 2020**	**December 28, 2018**	**$ Change**	**% Change**
Medical	$ 155.6	$ 143.9	$ 11.7	8.1%
Industrial	44.5	41.8	2.7	6.5%
Total revenues	$ 200.1	$ 185.7	$ 14.4	7.8%
Medical as a percentage of total revenues	*77.8%*	*77.5%*		
Industrial as a percentage of total revenues	*22.2%*	*22.5%*		

Medical revenues increased by $11.7 million primarily due to increased sales of CT X-ray tubes and digital detectors and X-ray tubes for oncology applications, partially offset by decreased sales of radiographic digital detectors.

Industrial revenues increased $2.7 million primarily due to increased sales of X-ray tubes for airport security.

Gross Margin

	Three Months Ended			
(In millions)	**January 3, 2020**	**December 28, 2018**	**$ Change**	**% Change**
Medical	$ 43.8	$ 45.1	$ (1.3)	(2.9)%
Industrial	17.3	14.9	2.4	16.1 %
Total gross margin	$ 61.1	$ 60.0	$ 1.1	1.8 %
Medical gross margin %	*28.1%*	*31.3%*		
Industrial gross margin %	*38.9%*	*35.6%*		
Total gross margin %	*30.5%*	*32.3%*		

The decrease in total gross margin percentage was due to the decrease in medical gross margin percentage. The decrease in medical gross margin percentage was primarily due to additional reserves for the settlement of a German customs audit, higher warranty and slow-moving inventory reserves and customer price decreases for digital detectors. The industrial gross margin percentage increased due to a favorable mix of higher margin products.

Operating Expenses

(In millions)	Three Months Ended January 3, 2020	Three Months Ended December 28, 2018	$ Change	% Change
Research and development	$ 21.7	$ 18.8	$ 2.9	15.4%
As a percentage of total revenues	*10.8%*	*10.1%*		
Selling, general and administrative	$ 34.8	$ 30.8	$ 4.0	13.0%
As a percentage of total revenues	*17.4%*	*16.6%*		
Operating expenses	$ 56.5	$ 49.6	$ 6.9	13.9%
As a percentage of total revenues	*28.2%*	*26.7%*		

Research and Development

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. Research and development costs increased to 10.8% of revenues for the first quarter of 2020 due to an additional week of expenses in the quarter and the addition of Direct Conversion.

Selling, General and Administrative

Selling, general and administrative expenses for the first quarter of 2020 increased to 17.4% primarily due to an additional week of expenses in the quarter and higher audit and consulting fees.

Interest and Other Expense, Net

The following table summarizes the Company's interest and other expense, net:

(In millions)	Three Months Ended January 3, 2020	Three Months Ended December 28, 2018	$ Change
Interest expense	(5.4)	(5.1)	(0.3)
Other (expense) income, net	(0.4)	(1.2)	0.8
Interest and other expense, net	$ (5.8)	$ (6.3)	$ 0.5

Interest and other expense, net decreased, primarily due to an increase in our income from equity method investments compared to the three months ended December 28, 2018.

Taxes on Earnings

	Three Months Ended January 3, 2020	Three Months Ended December 28, 2018
Estimated effective tax rate	0.9%	26.8%

We recognized an income tax benefit of $0.0 million and an income tax expense of $1.1 million for the three months ended January 3, 2020 and December 28, 2018, respectively, for effective rates of 0.9% and 26.8%, respectively.

Our effective tax rate for the three months ended January 3, 2020, decreased primarily due to losses in certain jurisdictions for which no benefit can be recorded due to full valuation allowance positions and a nearly equivalent overall pre-tax book loss.

Liquidity and Capital Resources

We assess our liquidity in terms of our ability to generate cash to fund our operating and investing activities. We continue to generate substantial cash from operating activities and believe that our operating cash flow, credit facility, 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 $73.0 million as of January 3, 2020.

Cash and Cash Equivalents

The following table summarizes our cash and cash equivalents:

(In millions)	January 3, 2020	September 27, 2019	$ Change
Cash and cash equivalents	$ 30.0	$ 29.9	$ 0.1

Borrowings

The following table summarizes the changes in our debt outstanding:

(In millions)	January 3, 2020	September 27, 2019	$ Change
Current portion of Term Facility	$ 29.4	$ 29.4	$ —
Current portion of other long-term debt	1.0	1.3	(0.3)
Revolving Credit Facility	52.0	59.0	(7.0)
Long-term portion of Term Facility	301.1	308.6	(7.5)
Long-term portion of other debt	2.6	2.5	0.1
Total debt outstanding, gross	386.1	400.8	(14.7)
Debt issuance costs	(4.8)	(5.7)	0.9
Total debt outstanding, net	$ 381.3	$ 395.1	$ (13.8)

Cash Flows

	Three Months Ended	
(In millions)	January 3, 2020	December 28, 2018
Net cash flow provided by (used in):		
Operating activities	$ 23.0	$ 20.0
Investing activities	(10.6)	(3.4)
Financing activities	(12.0)	(13.1)
Effects of exchange rate changes on cash and cash equivalents and restricted cash	(0.3)	(0.4)
Net increase in cash and cash equivalents and restricted cash	$ 0.1	$ 3.1

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

For the three months ended January 3, 2020, compared to the three months ended December 28, 2018, cash provided by operating activities were as follows:

- Net (loss) earnings were $(1.2) million compared to $3.0 million
- Non-cash adjustments to net earnings of $13.3 million compared to $13.5 million
- Operating assets and liabilities activity:
  - Accounts receivable decreased by $18.5 million compared to $20.6 million,
  - Inventories increased by $21.1 million compared to $22.0 million,
  - Prepaid expenses and other assets decreased by $3.7 million compared to $3.7 million,
  - Accounts payable increased by $15.4 million compared to a decrease of $0.5 million, and
  - Accrued liabilities and other current and long-term operating liabilities decreased by $4.8 million compared to an increase of $3.1 million.

Net Cash Used in Investing Activities. Net cash used in investing activities was $10.6 million and $3.4 million for the three months ended January 3, 2020 and December 28, 2018, respectively. The increase in cash used in investing activities was primarily due to an increase in capital expenditures for property plant and equipment during the three months ended January 3, 2020.

Net Cash Used in Financing Activities. Financing activities for the three months ended January 3, 2020 consisted of borrowings under our credit agreement of $3.0 million and repayments of borrowings of $17.8 million. Financing activities for the three months ended December 28, 2018 consisted of borrowings under our credit agreement of $4.0 million, and repayments of borrowings of $19.0 million.

Days Sales Outstanding

Trade accounts receivable days sales outstanding ("DSO") was 55 days at January 3, 2020 and 63 days at September 27, 2019. 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

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. As of January 3, 2020, we had no fixed cost commitments related to this agreement remaining for calendar year 2019. In January 2020, the fixed cost commitment was determined and approved by the dpiX board of directors to be $12.7 million for calendar year 2019. 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 January 3, 2020, noncontrolling shareholders together held approximately 0.5 million shares of MeVis, representing 26.3% of the outstanding shares. See Note 12, "Redeemable Noncontrolling Interests" of the notes to the condensed consolidated financial statements for more information.

Contingencies

From time to time, we are 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 our business or otherwise. Such matters are subject to many uncertainties and outcomes are not predictable with assurance.

Off-Balance Sheet Arrangements

In conjunction with the sale of our products in the ordinary course of business, we provide standard indemnification of business partners and customers for losses suffered or incurred for property damages, death and injury and for patent, copyright or any other intellectual property infringement claims by any third parties with respect to our products. The terms of these indemnification arrangements are generally perpetual. Except for losses related to property damages, the maximum potential amount of future payments we could be required to make under these arrangements is unlimited. As of January 3, 2020, 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 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. There is no maximum limit on the indemnification that may be required under these obligations. As of January 3, 2020, we have not incurred any material costs related to these indemnification obligations. As a result, we believe the estimated fair value of these obligations is minimal.

Recent Accounting Standards or Updates Not Yet Effective

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

Item 3. 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 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 in-sourcing supply of components or migrate 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 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 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 January 3, 2020, we had total borrowings of $381.3 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 $253.1 million of our debt as of January 3, 2020. See Note 7, "Financial Derivatives and Hedging Activities" for further information on hedging activities. 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.

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 three months ended January 3, 2020, we did not have any commodity derivative instruments in place to manage our exposure to price changes.

Item 4. Controls and Procedures

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 January 3, 2020 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 that were disclosed in our Annual Report on Form 10-K for the fiscal year ended September 27, 2019.

Changes in Internal Control Over Financial Reporting

In addition to the implementation of the remediation measures described below, during the quarter ended January 3, 2020, in connection with our adoption of ASU 842, we implemented new controls related to the adoption process, the gathering and validation of our lease population, and the accounting and disclosures for right of use assets and lease liabilities. There were no other changes in our internal control over financial reporting that occurred during the period covered by this report that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

Remediation

As previously described in Part II, Item 9A of our Annual Report on Form 10-K for the fiscal year ended September 27, 2019, we began implementing a remediation plan to address the material weaknesses mentioned above. 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 these controls are operating effectively.

PART II

OTHER INFORMATION

Item 1. Legal Proceedings

We are subject to various claims, complaints and legal actions in the normal course of business from time to time. We do not believe we have any currently pending litigation for which the outcome could have a material adverse effect on our operations or financial position.

Item 1A. Risk Factors

The following risk factors and other information included in this quarterly report on Form 10-Q 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 the three months ended January 3, 2020, that accounted for 19% of its revenue. Varex's ten largest customers as a group accounted for approximately 53% and 52% of its revenue for the three months ended January 3, 2020 and December 28, 2018, 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, 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 66% and 64% of Varex's total revenues during the three months ended January 3, 2020 and December 28, 2018, respectively. As a result, 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;
- natural disasters and pandemics;
- 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 Varex's business, profitability and ability to meet its obligations.

As of January 3, 2020, Varex's total combined indebtedness was approximately $381.3 million (net of deferred loan costs). 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 $253.1 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 our 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 regained 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.

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 our 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 our 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 in our Annual Report on Form 10-K, for the fiscal year ended September 27, 2019, 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 Varex'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

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

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 $22.73 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.

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 or 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 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

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,

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.

New accounting pronouncements or changes in interpretation or application of generally accepted accounting principles may materially and adversely affect Varex's operating results.

VaVarex 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. New accounting pronouncements, or a change in interpretations of, or its application of, existing 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, make it more difficult to compare its financial results to prior periods, and could cause Varex to delay required filings under the Exchange Act, such as the delay that occurred with the filing of this Quarterly Report on Form 10-Q to implement ASC 842.

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 its 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;
- 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, 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 2. Unregistered Sales of Equity Securities and Use of Proceeds

None.

Item 3. Defaults Upon Senior Securities

None.

Item 4. Mine Safety Disclosures

Not applicable.

Item 5. Other Information

None.

Item 6. Exhibits

(a) Exhibits required to be filed by Item 601 of Regulation S-K:

Exhibit No.	Description
3.1	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).
3.2	Amended and Restated Bylaws of the Company, as amended January 27, 2017 (incorporated by reference to Exhibit 3.2 to the Company's Current Report on Form 8-K filed January 30, 2017, SEC File No. 001-37860).
31.1*	Chief Executive Officer Certification Pursuant to Rule 13a-14(a) of the Securities Exchange Act
31.2*	Chief Financial Officer Certification Pursuant to Rule 13a-14(a) of the Securities Exchange Act
32.1*	Certification pursuant to 18 U.S.C. Section 1350 as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002
32.2*	Certification pursuant to 18 U.S.C. Section 1350 as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002
101.INS*	XBRL Instance Document - 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
104*	Cover Page Interactive Data File - (formatted as Inline XBRL and contained in Exhibit 101)

* Filed herewith.

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: February 18, 2020

By: /s/ CLARENCE R. VERHOEF

Clarence R. Verhoef
Senior Vice President and Chief Financial Officer
(Duly Authorized Officer and Principal Financial Officer)