LABORATORY CORP OF AMERICA HOLDINGS
Form 10-Q
July 27, 2018
UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549
FORM 10-Q

[X] QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d)
OF THE SECURITIES EXCHANGE ACT OF 1934

For the quarterly period ended June 30, 2018
OR
[ ] TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d)
OF THE SECURITIES EXCHANGE ACT OF 1934

For the transition period from ______ to ______

Commission file number 1-11353

LABORATORY CORPORATION OF
AMERICA HOLDINGS
(Exact name of registrant as specified in its charter)

Delaware	13-3757370
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)

358 South Main Street,	
Burlington, North Carolina	27215
(Address of principal executive offices)	(Zip Code)

(Registrant's telephone number, including area code) 336-229-1127

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

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (paragraph 232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes [X] No [ ]
Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, 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 [X]	Accelerated filer [ ]
Non-accelerated filer [ ] (Do not check if a smaller reporting company)	Smaller reporting company [ ]
	Emerging growth company [ ]

If 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 [X].

The number of shares outstanding of the issuer's common stock is 101.9 million shares, net of treasury stock as of July 25, 2018.

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PART I – FINANCIAL INFORMATION

Item 1. Financial Statements

LABORATORY CORPORATION OF AMERICA HOLDINGS AND SUBSIDIARIES
CONDENSED CONSOLIDATED BALANCE SHEETS
(in millions)
(unaudited)

	June 30, 2018	December 31, 2017
ASSETS		
Current assets:		
Cash and cash equivalents	$221.4	$ 316.6
Accounts receivable	1,520.3	1,531.0
Unbilled services	351.3	316.5
Supplies inventories	230.7	227.2
Prepaid expenses and other	286.1	308.8
Current assets held for sale	411.4	33.7
Total current assets	3,021.2	2,733.8
Property, plant and equipment, net	1,710.9	1,706.6
Goodwill, net	7,423.3	7,400.9
Intangible assets, net	4,049.5	4,166.1
Joint venture partnerships and equity method investments	58.9	58.4
Deferred income tax assets	1.7	1.9
Other assets, net	239.0	217.5
Long-term assets held for sale	—	387.8
Total assets	$16,504.5	$ 16,673.0
LIABILITIES AND SHAREHOLDERS' EQUITY		
Current liabilities:		
Accounts payable	$488.1	$ 573.9
Accrued expenses and other	739.9	793.3
Unearned revenue	393.3	380.8
Short-term borrowings and current portion of long-term debt	417.8	417.5
Current liabilities held for sale	82.4	20.2
Total current liabilities	2,121.5	2,185.7
Long-term debt, less current portion	6,039.4	6,344.6
Deferred income taxes and other tax liabilities	914.1	875.5
Other liabilities	371.8	376.0
Long-term liabilities held for sale	—	66.3
Total liabilities	9,446.8	9,848.1
Commitments and contingent liabilities		
Noncontrolling interest	20.0	20.8
Shareholders' equity:		
Common stock, 102.0 and 101.9 shares outstanding at June 30, 2018 and December 31, 2017, respectively	12.0	12.0
Additional paid-in capital	1,934.8	1,989.8
Retained earnings	6,603.1	6,196.1

Less common stock held in treasury	(1,105.2)	(1,060.1)
Accumulated other comprehensive loss	(407.0)	(333.7)
Total shareholders' equity	7,037.7	6,804.1
Total liabilities and shareholders' equity	$16,504.5	$ 16,673.0

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

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LABORATORY CORPORATION OF AMERICA HOLDINGS AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS
(in millions, except per share data)
(unaudited)

	Three Months Ended June 30,		Six Months Ended June 30,	
	2018	2017	2018	2017
Revenues	$2,866.3	$2,528.2	$5,714.6	$4,941.9
Cost of revenues	2,031.2	1,750.2	4,100.5	3,451.4
Gross profit	835.1	778.0	1,614.1	1,490.5
Selling, general and administrative expenses	395.2	357.7	792.2	700.6
Amortization of intangibles and other assets	58.5	51.4	120.8	99.0
Restructuring and other special charges	12.2	39.1	26.5	43.0
Operating income	369.2	329.8	674.6	647.9
Other income (expenses):				
Interest expense	(63.1)	(55.0)	(126.6)	(107.4)
Equity method income, net	3.0	4.5	5.5	6.8
Investment income	0.8	0.4	1.4	0.7
Other, net	2.8	(0.5)	(0.7)	(3.6)
Earnings before income taxes	312.7	279.2	554.2	544.4
Provision for income taxes	78.6	94.1	147.6	176.0
Net earnings	234.1	185.1	406.6	368.4
Less: Net (earnings) loss attributable to the noncontrolling interest	(0.3)	(0.3)	0.4	(0.6)
Net earnings attributable to Laboratory Corporation of America Holdings	$233.8	$184.8	$407.0	$367.8
Basic earnings per common share	$2.29	$1.80	$3.99	$3.59
Diluted earnings per common share	$2.27	$1.78	$3.94	$3.54

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

LABORATORY CORPORATION OF AMERICA HOLDINGS AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE EARNINGS
(in millions, except per share data)
(unaudited)

	Three Months Ended June 30,		Six Months Ended June 30,	
	2018	2017	2018	2017
Net earnings	$234.1	$185.1	$406.6	$368.4
Foreign currency translation adjustments	(121.9)	157.2	(82.6)	215.8
Net benefit plan adjustments	3.3	0.5	6.2	1.1
Other comprehensive earnings (loss) before tax	(118.6)	157.7	(76.4)	216.9
(Provision) benefit for income tax related to items of other comprehensive earnings	(7.2)	(14.9)	3.1	(20.8)
Other comprehensive earnings, net of tax	(125.8)	142.8	(73.3)	196.1
Comprehensive earnings	108.3	327.9	333.3	564.5
Less: Net (earnings) loss attributable to the noncontrolling interest	(0.3)	(0.3)	0.4	(0.6)
Comprehensive earnings attributable to Laboratory Corporation of America Holdings	$108.0	$327.6	$333.7	$563.9

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

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LABORATORY CORPORATION OF AMERICA HOLDINGS AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF CHANGES IN SHAREHOLDERS' EQUITY
(in millions)
(unaudited)

	Common Stock	Additional Paid-in Capital	Retained Earnings	Treasury Stock	Accumulated Other Comprehensive Loss	Total Shareholders' Equity
BALANCE AT DECEMBER 31, 2016	$ 12.1	$ 2,131.7	$ 4,969.0	$ (1,012.7)	$ (581.9)	$ 5,518.2
Net earnings attributable to Laboratory Corporation of America Holdings	—	—	367.8	—	—	367.8
Other comprehensive earnings, net of tax	—	—	—	—	196.1	196.1
Issuance of common stock under employee stock plans	0.1	31.3	—	—	—	31.4
Surrender of restricted stock and performance share awards	—	—	—	(46.2)	—	(46.2)
Conversion of zero-coupon convertible debt	—	12.8	—	—	—	12.8
Stock compensation	—	52.7	—	—	—	52.7
Purchase of common stock	(0.2)	(255.8)	—	—	—	(256.0)
BALANCE AT JUNE 30, 2017	$ 12.0	$ 1,972.7	$ 5,336.8	$ (1,058.9)	$ (385.8)	$ 5,876.8
BALANCE AT DECEMBER 31, 2017	$ 12.0	$ 1,989.8	$ 6,196.1	$ (1,060.1)	$ (333.7)	$ 6,804.1
Net earnings attributable to Laboratory Corporation of America Holdings	—	—	407.0	—	—	407.0
Other comprehensive earnings, net of tax	—	—	—	—	(73.3)	(73.3)
Issuance of common stock under employee stock plans	—	43.0	—	—	—	43.0
Surrender of restricted stock and performance share awards	—	—	—	(45.1)	—	(45.1)
Stock compensation	—	52.0	—	—	—	52.0
Purchase of common stock	—	(150.0)	—	—	—	(150.0)
BALANCE AT JUNE 30, 2018	$ 12.0	$ 1,934.8	$ 6,603.1	$ (1,105.2)	$ (407.0)	$ 7,037.7

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

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LABORATORY CORPORATION OF AMERICA HOLDINGS AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
(in millions)
(unaudited)

	Six Months Ended June 30,	
	2018	2017
CASH FLOWS FROM OPERATING ACTIVITIES:		
Net earnings	$406.6	$368.4
Adjustments to reconcile net earnings to net cash provided by operating activities:		
Depreciation and amortization	281.3	255.1
Stock compensation	52.0	52.7
(Gain) loss on sale of assets	(0.3)	0.6
Accreted interest on zero-coupon subordinated notes	0.1	0.2
Cumulative earnings less than distributions from equity method investments	(1.3)	(4.0)
Asset impairment	2.3	15.1
Deferred income taxes	36.0	(4.6)
Change in assets and liabilities (net of effects of acquisitions):		
Decrease (increase) in accounts receivable	13.2	(50.2)
Increase in unbilled services	(36.5)	(37.1)
Increase in inventories	(4.7)	(0.7)
(Increase) decrease in prepaid expenses and other	(27.2)	4.8
(Decrease) increase in accounts payable	(91.3)	8.6
Increase (decrease) in unearned revenue	8.3	(10.0)
Decrease in accrued expenses and other	(116.5)	(62.5)
Net cash provided by operating activities	522.0	536.4
CASH FLOWS FROM INVESTING ACTIVITIES:		
Capital expenditures	(159.7)	(141.5)
Proceeds from sale of assets	0.7	1.0
Proceeds from sale of held for sale assets	49.1	—
Acquisition of licensing technology	—	(2.3)
Investments in equity affiliates	(7.3)	(26.1)
Acquisition of businesses, net of cash acquired	(79.1)	(568.0)
Net cash used for investing activities	(196.3)	(736.9)
CASH FLOWS FROM FINANCING ACTIVITIES:		
Payments on term loan	(295.0)	—
Proceeds from revolving credit facilities	394.7	749.7
Payments on revolving credit facilities	(394.7)	(440.7)
Payments on zero-coupon subordinated notes	—	(23.2)
Noncontrolling interest distributions	(5.9)	(0.5)
Deferred payments on acquisitions	—	(1.5)
Payments on long-term lease obligations	(5.1)	(4.3)
Net proceeds from issuance of stock to employees	43.0	31.4
Purchase of common stock	(150.0)	(256.0)
Net cash (used for) provided by financing activities	(413.0)	54.9
Effect of exchange rate changes on cash and cash equivalents	(7.9)	11.8
Net (decrease) increase in cash and cash equivalents	(95.2)	(133.8)

Cash and cash equivalents at beginning of period	316.6	433.6
Cash and cash equivalents included in assets held for sale	—	(0.2)
Cash and cash equivalents at end of period	$221.4	$299.6

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

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LABORATORY CORPORATION OF AMERICA HOLDINGS AND SUBSIDIARIES
NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(dollars and shares in millions, except per share data)

1. BASIS OF FINANCIAL STATEMENT PRESENTATION

Laboratory Corporation of America® Holdings together with its subsidiaries (the Company) is a leading global life sciences company that is deeply integrated in guiding patient care, providing comprehensive clinical laboratory and end-to-end drug development services. The Company's mission is to improve health and improve lives by delivering world-class diagnostic solutions, bringing innovative medicines to patients faster and using technology to provide better care. The Company serves a broad range of customers, including managed care organizations (MCOs), biopharmaceutical companies, governmental agencies, physicians and other healthcare providers (e.g., physician assistants and nurse practitioners, generally referred to herein as physicians), hospitals and health systems, employers, patients and consumers, contract research organizations, food and nutritional companies and independent clinical laboratories. The Company believes that it generated more revenue from laboratory testing than any other company in the world in 2017.

The Company reports its business in two segments, LabCorp Diagnostics (LCD) and Covance Drug Development (CDD). For further financial information about these segments, see Note 15 (Business Segment Information). During the three months ended June 30, 2018, LCD and CDD contributed approximately 63% and 37%, respectively, of net revenues to the Company, and for the six months ended June 30, 2018, contributed approximately 63% and 37%, respectively.

The condensed consolidated financial statements include the accounts of the Company and its majority-owned subsidiaries for which it exercises control. Long-term investments in affiliated companies in which the Company exercises significant influence, but which it does not control, are accounted for using the equity method. Investments in which the Company does not exercise significant influence (generally, when the Company has an investment of less than 20.0% and no representation on the investee's board of directors) are accounted for at fair value or at cost minus impairment for those investments that do not have readily determinable fair values. All significant inter-company transactions and accounts have been eliminated. The Company does not have any variable interest entities or special purpose entities whose financial results are not included in the condensed consolidated financial statements.

The financial statements of the Company's operating foreign subsidiaries are measured using the local currency as the functional currency. Assets and liabilities are translated at exchange rates as of the balance sheet date. Revenues and expenses are translated at average monthly exchange rates prevailing during the period. Resulting translation adjustments are included in "Accumulated other comprehensive income."

The accompanying condensed consolidated financial statements of the Company are unaudited. In the opinion of management, all adjustments necessary for a fair statement of results of operations, cash flows and financial position have been made. Except as otherwise disclosed, all such adjustments are of a normal recurring nature. Interim results are not necessarily indicative of results for a full year. The year-end condensed consolidated balance sheet data was derived from audited financial statements but does not include all disclosures required by generally accepted accounting principles.

The condensed consolidated financial statements and notes are presented in accordance with the rules and regulations of the United States (U.S.) Securities and Exchange Commission (SEC) and do not contain certain information included in the Company's 2017 Annual Report on Form 10-K. Therefore, the interim statements should be read in conjunction with the consolidated financial statements and notes thereto contained in the Company's Annual Report.

Recently Adopted Guidance Revenue from Contracts with Customers

In May 2014, the Financial Accounting Standards Board (FASB) issued the converged standard on revenue recognition with the objective of providing a single, comprehensive model for all contracts with customers to improve comparability in the financial statements of companies reporting using International Financial Reporting Standards (IFRS) and U.S. Generally Accepted Accounting Principles (GAAP). The standard contains principles that an entity must apply to determine the measurement of revenue and timing of when it is recognized. The underlying principle is

that an entity must recognize revenue to depict the transfer of goods or services to customers at an amount that the entity expects to be entitled to in exchange for those goods or services.

The standard was effective for the Company beginning January 1, 2018. The Company elected to adopt the standard using the full retrospective approach, which resulted in a recasting of revenue and the related financial statement items for 2016 and 2017. During transition to the new standard, the Company also elected several practical expedients, as provided by the standard. Contracts that began and ended within the same annual reporting period were not restated. Contracts that were completed by December 31, 2017 that had variable consideration were estimated using the transaction price at the date the contract was completed. The amount of the transaction price allocated to the remaining performance obligations will not be disclosed for prior reporting periods. Contracts that were modified prior to the earliest reporting period will be reflected in the earliest reporting period with an aggregate adjustment for prior modifications.

As a result of the new standard, the Company has changed its accounting policies for revenue recognition. The significant changes under the new standard, and the quantitative impact of these changes, are detailed below.

LCD

The primary impact of the new standard to the LCD segment was classifying bad debt expense of $78.0 and $156.2 for the three and six months ended June 30, 2017, respectively, as a reduction in revenue rather than as a selling, general and administrative expense.

CDD

The primary impact of the new standard to the CDD segment was as follows:

Investigator fees: Prior to the new standard, reimbursements of investigator fees by clients were netted against the amounts paid to investigators in net revenues, on the basis that CDD was acting as the agent in arranging the investigator services. Under the new standard, revenue for investigator services and other reimbursable activities is recognized gross of fees paid to the investigators and other vendors, on the basis that a clinical study is considered a single, combined performance obligation for which CDD acts as a principal. Where CDD assumes the obligations by contract in studies involving patients, CDD is the principal because CDD may contract directly with third party clinical trial sites and investigators for investigator services and other reimbursable activities, which are combined with other CDD services in the management of a clinical study. Where CDD has assumed certain clinical trial sponsor obligations by contract in studies involving patients, CDD has primary responsibility for fulfilling its obligations associated with the full management of a clinical study, has inventory risk since it may be obligated to compensate investigators and other vendors for reimbursable activities regardless of payment by the customer, and has discretion within the framework agreed upon with the customer in setting the price of the study, including the budget for all pass-through costs, including investigator grants.

The financial impact of this change on revenue for the three and six months ended June 30, 2017 was an increase of $69.0 and $126.5, respectively. Revenue and expenses from reimbursable out-of-pocket costs were previously recognized gross as separate line items from Net revenues and Net cost of revenue in the Consolidated Statement of Operations. Under the new standard, reimbursable out-of-pocket costs continue to be recognized gross, but are no longer presented separately (i.e., expenses are included in Cost of revenues and reimbursements are included in Revenues). In the statement of financial position, unbilled investigator fees and reimbursable out of pocket costs were reclassified from “Prepaid expenses and other” to “Unbilled services” and billed investigator grants and reimbursable out-of-pocket costs were reclassified from “Prepaid expenses and other” to “Accounts receivable, net.”

Measure of progress: Prior to the new standard, service fee revenue in clinical studies was recognized on a proportional-performance basis, generally using output measures that are specific to the service provided (e.g., number of investigators enrolled, number of sites initiated, number of trial subjects enrolled and number of monitoring visits completed), while reimbursable out-of-pocket revenue was recognized when the associated expense was incurred. Changes in contract value from changes in scope were reflected once the customer agreed to the changes in scope and renegotiated pricing terms. Under the new standard, revenue in a clinical study (inclusive of budgeted reimbursable pass-through costs) is recognized using an input-based measure of progress based on costs incurred (including pass-through costs such as investigator services and reimbursable out-of-pocket expenses). If a customer’s approval of a work scope change creates an enforceable right to payment, the related revenue will be estimated and included in the measure of progress before a formal change order is executed, which results in recognition of revenue as services are provided. The financial impact of this change on revenue for the three and six months ended June 30, 2017 was a decrease of $5.7 and $18.3, respectively.

Sales commissions: Prior to the new standard, sales commissions were recorded as an expense each quarter when incurred. Under the new standard, CDD amortizes sales commissions according to the expected service period to which the commissions relate on the basis that they are recoverable through the margin inherent in the contracts and recognizes the unamortized commissions as current and long-term assets.

CDD applied the portfolio practical expedient in the new standard to determine the amortization period for assets recognized from sales commissions. Under the portfolio approach, CDD determined the weighted average contract term for groups of contracts with similar characteristics, and then amortized the capitalized sales commissions for that group over that term. CDD believes that any difference between the amortization patterns under the specific identification approach and the portfolio approach are not significant to CDD’s consolidated financial statements. The financial impact of this change on selling, general, and administrative expenses for the three and six months ended June 30, 2017 was a decrease of $0.1 and an increase of $1.2, respectively.

The total quantitative impact of the new standard on retained earnings as of January 1, 2017 was an increase of $13.2.

LABORATORY CORPORATION OF AMERICA HOLDINGS AND SUBSIDIARIES
NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(dollars and shares in millions, except per share data)

New Accounting Pronouncements

In January 2016, the FASB issued a new accounting standard that addresses certain aspects of recognition, measurement, presentation and disclosure of financial instruments. A financial instrument is defined as cash, evidence of ownership interest in a company or other entity, or a contract that both: (i) imposes on one entity a contractual obligation either to deliver cash or another financial instrument to a second entity or to exchange other financial instruments on potentially unfavorable terms with the second entity, and (ii) conveys to that second entity a contractual right either to receive cash or another financial instrument from the first entity or to exchange other financial instruments on potentially favorable terms with the first entity. The Company adopted this standard effective January 1, 2018. As a result of adoption, investments in which the Company does not exercise significant influence (generally, when the Company has an investment of less than 20.0% and no representation on the investee's board of directors) are accounted for at fair value or at cost minus impairment for those investments that do not have readily determinable fair values. The adoption of this standard did not have a material impact on the consolidated financial statements.

In February 2016, the FASB issued a new accounting standard that sets out the principles for the recognition, measurement, presentation and disclosure of leases for both parties to a contract (i.e., lessees and lessors). The new standard requires lessees to apply a dual approach, classifying leases as either finance or operating leases based on the principle of whether or not the lease is effectively a financed purchase by the lessee. This classification will determine whether lease expense is recognized based on an effective interest method or on a straight-line basis over the term of the lease. A lessee is also required to record a right-of-use asset and a lease liability for all leases with a term of greater than 12 months regardless of their classification. Leases with a term of 12 months or less will be accounted for based on guidance similar to current guidance for operating leases. The new standard requires lessors to account for leases using an approach that is substantially equivalent to existing guidance for sales-type leases, direct financing leases and operating leases. The standard is effective on January 1, 2019, with early adoption permitted. The Company will implement a new module into the current leasing software solution which will facilitate compliance with the new standard and is currently evaluating the impact that this new standard will have on the consolidated financial statements.

In June 2016, the FASB issued a new accounting standard intended to provide financial statement users with more decision-useful information about expected credit losses and other commitments to extend credit held by the reporting entity. The standard replaces the incurred loss impairment methodology in current GAAP with one that reflects expected credit losses and requires consideration of a broader range of reasonable and supportable information to inform credit loss estimates. The update is effective on January 1, 2020, with early adoption permitted. The Company is currently evaluating the impact this new standard will have on the consolidated financial statements.

In August 2016, the FASB issued a new accounting standard that makes eight targeted changes to how cash receipts and cash payments are presented and classified in the statement of cash flows. The Company adopted this standard on a retrospective basis effective January 1, 2018. As a result, the Company reclassified accreted interest paid upon conversion of its zero-coupon subordinated notes from a financing activity to an operating activity.

In January 2017, the FASB issued a new accounting standard that changes the definition of a business to assist entities with evaluating when a set of transferred assets and activities is a business. The Company adopted this standard effective January 1, 2018. The adoption of this standard did not have a material impact on the consolidated financial statements as of June 30, 2018.

In March 2017, the FASB issued a new accounting standard that requires employers that present a measure of operating income in their statement of income to include only the service cost component of net periodic pension cost and net periodic post-retirement benefit cost in operating expenses with other employee compensation costs. The other components of net benefit cost, including amortization of prior service cost/credit and settlement and curtailment effects are to be included in other, net non-operating expenses. The Company adopted this standard effective January

1, 2018. The adoption of this standard reduced operating margin due to the service cost remaining in operating expenses with no offset from the other components of net pension cost and has been applied retrospectively. The adoption of this standard had no impact on net earnings.

In May 2017, the FASB issued a new accounting standard that amends the scope of modification accounting for share-based payment arrangements and provides guidance on the types of changes to the terms or conditions of share-based payment awards to which an entity would be required to apply modification accounting. Specifically, an entity would not apply modification accounting if the fair value, vesting conditions, and classification of the awards are the same immediately before and after the modification. The Company adopted this standard effective January 1, 2018. The adoption of this standard did not have a material impact on the consolidated financial statements.

In July 2017, the FASB issued a new accounting standard intended to reduce the complexity associated with the issuer's accounting for certain financial instruments with characteristics of liabilities and equity. Specifically, a down round feature would no longer cause a free-standing equity-linked financial instrument (or embedded conversion option) to be accounted for as a

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LABORATORY CORPORATION OF AMERICA HOLDINGS AND SUBSIDIARIES
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(dollars and shares in millions, except per share data)

derivative liability at fair value with changes in fair value recognized in current earnings. This update is effective on January 1, 2019, with early adoption permitted and the option to use the retrospective or modified retrospective adoption method. The Company is currently evaluating the impact this new standard will have on the consolidated financial statements.

In August 2017, the FASB issued a new accounting standard intended to more closely align hedge accounting with companies' risk management strategies, simplify the application of hedge accounting and increase transparency as to the scope and results of hedging programs. As a result, more hedging strategies are eligible for hedge accounting. The Company early adopted this standard effective January 1, 2018, and as allowed by the standard, elected to change the methodology for assessing hedge effectiveness of net investment hedges from a method based on changes in forward exchange rates to a method based on changes in spot exchange rates. The spot methodology under this standard allows the interest accrual components of hedge instruments to be reported directly in earnings while the changes in the fair value of hedge instruments attributable to changes in the spot rate are reported in the cumulative translation adjustment section of other comprehensive income.

Reclassifications

Adoption of the standards related to revenue recognition, pension accounting and cash receipts and payments impacted previously reported results as follows:

	Condensed Consolidated Statement of Operations For the Three Months Ended June 30, 2017			
	As Previously Reported	ASC 606 Revenue Adjustments	Pension Adjustments	As Adjusted
Total revenues	$2,542.9	$ (14.7)	$ —	$2,528.2
Total cost of revenue	1,681.1	68.9	0.2	1,750.2
Gross profit	861.8	(83.6)	(0.2)	778.0
Selling, general and administrative expenses	435.3	(78.1)	0.5	357.7
Other operating and non-operating expenses, net	141.4	0.4	(0.7)	141.1
Provision for income taxes	96.2	(2.1)	—	94.1
Net earnings	188.9	(3.8)	—	185.1
Less: Net earnings attributable to noncontrolling interest	(0.3)	—	—	(0.3)
Net earnings attributable to Laboratory Corporation of America Holdings	$188.6	$ (3.8)	$ —	$184.8
Basic earnings per share	$1.84			$1.80
Diluted earnings per share	$1.82			$1.78

	Condensed Consolidated Statement of Operations For the Six Months Ended June 30, 2017			
	As previously reported	ASC 606 Revenue Adjustments	Pension Adjustments	As Adjusted
Total revenues	$4,989.9	$ (48.0)	$ —	$4,941.9
Total cost of revenue	3,324.5	126.7	0.2	3,451.4
Gross profit	1,665.4	(174.7)	(0.2)	1,490.5
Selling, general and administrative expenses	854.7	(154.9)	0.8	700.6

Other operating and non-operating expenses, net	245.9	0.6	(1.0)	245.5
Provision for income taxes	183.4	(7.4)	—	176.0
Net earnings	381.4	(13.0)	—	368.4
Less: Net earnings attributable to noncontrolling interest	(0.6)	—	—	(0.6)
Net earnings attributable to Laboratory Corporation of America Holdings	$380.8	$ (13.0)	$ —	$367.8
Basic earnings per share	$3.71			$3.59
Diluted earnings per share	$3.66			$3.54

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LABORATORY CORPORATION OF AMERICA HOLDINGS AND SUBSIDIARIES
NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(dollars and shares in millions, except per share data)

	Condensed Consolidated Statement of Cash Flows For the Six Months Ended June 30, 2017		
	As Previously Reported	Zero-Coupon Notes Adjustments	As Adjusted
Net cash provided by operating activities	$544.4	$ (8.0)	$536.4
Net cash used for investing activities	(736.9)	—	(736.9)
Net cash provided by financing activities	46.9	8.0	54.9
Effect of exchange rate changes on cash and cash equivalents	11.8	—	11.8
Net decrease in cash and cash equivalents	$(133.8)		$(133.8)

The below adjustments have been made to the December 31, 2017 balance sheet and are all the result of the implementation of ASC 606. The adjustments include a cumulative catch-up adjustment, reclassification of unbilled services, and the capitalization of contract acquisition costs.

	Condensed Consolidated Balance Sheets December 31, 2017		
	As Previously Reported	ASC 606 Revenue Adjustments	As Adjusted
Current assets	$2,682.6	$ 51.2	$2,733.8
Long-term assets	13,885.4	53.8	13,939.2
Total assets	$16,568.0	$ 105.0	$16,673.0
Current liabilities	$2,046.1	$ 139.6	$2,185.7
Long-term liabilities	7,671.1	(8.7)	7,662.4
Noncontrolling interest	20.8	—	20.8
Shareholders' equity	6,830.0	(25.9)	6,804.1
Total liabilities and shareholders' equity	$16,568.0	$ 105.0	$16,673.0

2. REVENUE

Description of Revenue

The Company's revenue by segment payers/customer groups for the three and six months ended June 30, 2018 and 2017 is as follows:

	For the Three Months Ended June, 2018						
	U.S.	Canada	United Kingdom	Switzerland	Other Europe	Other	Total
Payer/Customer							
LCD							
Clients	18%	1 %	— %	— %	— %	—%	19 %
Patients	9 %	— %	— %	— %	— %	—%	9 %
Medicare and Medicaid	10%	— %	— %	— %	— %	—%	10 %
Third-party	23%	2 %	— %	— %	— %	—%	25 %
Total LCD revenues by payer	60%	3 %	— %	— %	— %	—%	63 %

CDD							
Biopharmaceutical and medical device companies	16%	—%	5 %	5 %	4 %	7 %	37 %
Total revenues	76%	3 %	5 %	5 %	4 %	7 %	100%

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LABORATORY CORPORATION OF AMERICA HOLDINGS AND SUBSIDIARIES
NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(dollars and shares in millions, except per share data)

	For the Three Months Ended June 30, 2017						
	U.S.	Canada	United Kingdom	Switzerland	Other Europe	Other	Total
Payer/Customer							
LCD							
Clients	19%	1 %	1 %	— %	— %	—%	21 %
Patients	10%	— %	— %	— %	— %	—%	10 %
Medicare and Medicaid	10%	— %	— %	— %	— %	—%	10 %
Third-party	25%	2 %	— %	— %	— %	—%	27 %
Total LCD revenues by payer	64%	3 %	1 %	— %	— %	—%	68 %
CDD							
Biopharmaceutical and medical device companies	15%	— %	3 %	5 %	3 %	6 %	32 %
Total revenues	79%	3 %	4 %	5 %	3 %	6 %	100%

	For the Six Months Ended June, 2018						
	U.S.	Canada	United Kingdom	Switzerland	Other Europe	Other	Total
Payer/Customer							
LCD							
Clients	18%	1 %	— %	— %	— %	—%	19%
Patients	9 %	— %	— %	— %	— %	—%	9 %
Medicare and Medicaid	10%	— %	— %	— %	— %	—%	10%
Third-party	23%	2 %	— %	— %	— %	—%	25%
Total LCD revenues by payer	60%	3 %	— %	— %	— %	—%	63%
CDD							
Biopharmaceutical and medical device companies	18%	— %	4 %	5 %	4 %	6 %	37%

- our ability to develop and implement new processes and procedures to remediate the material weaknesses that exist

in our internal control over financial reporting;

- our dependence on U.S. and foreign government contracts;

- delays in approving U.S. and foreign government budgets and cuts in U.S. and foreign government defense expenditures;

- the ability of certain government agencies to unilaterally terminate or modify our contracts with them;

- our ability to successfully integrate new companies into our business and to properly assess the effects of such integration on our financial condition;

- the U.S. government s increased emphasis on awarding contracts to small businesses, and our ability to retain existing contracts or win new contracts under competitive bidding processes;

- negative audits by

the
U.S.
government;

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- the effects of politics and economic conditions on negotiations and business dealings in the various countries in which we do business or intend to do business;
- competition and technology changes in the defense and transportation industries;
- our ability to accurately estimate the time and resources necessary to satisfy

obligations under our contracts;

- the effect of adverse regulatory changes on our ability to sell products and services;

- our ability to identify, attract and retain qualified employees;

- business disruptions due to cyber security threats, physical threats, terrorist acts, acts of nature and public health crises;

- our involvement in litigation, including litigation related to patents, proprietary rights and employee misconduct;

- our reliance on subcontractors and on a limited number of third parties to manufacture and supply our products;

- our ability to comply with our development contracts and to successfully develop, introduce and sell new products, systems and services in

current and future markets;

- defects in, or a lack of adequate coverage by insurance or indemnity for, our products and systems;

- changes in U.S. and foreign tax laws, exchange rates or our economic assumptions regarding our pension plans; and

- other factors discussed elsewhere in this report.

Because the

risks, estimates, assumptions and uncertainties referred to above could cause actual results or outcomes to differ materially from those expressed in any forward-looking statements made by us or on our behalf, you should not place undue reliance on any forward-looking statements. In addition, past financial and/or operating performance is not necessarily a reliable indicator of future performance and you should not use our historical performance

to
anticipate
results
or
future
period
trends.
Further,
any
forward-looking
statement
speaks
only
as of
the
date
on
which
it is
made,
and,
except
as
required
by
law,
we
undertake
no
obligation
to
update
any
forward-looking
statement
to
reflect
events
or
circumstances
after
the
date
on
which
the
statement
is
made
or to
reflect
the
occurrence
of
unanticipated
events.
New
factors
emerge
from
time
to

time, and it is not possible for us to predict which factors will arise. In addition, we cannot assess the impact of each factor on our business or the extent to which any factor, or combination of factors, may cause actual results to differ materially from those contained in any forward-looking statements.

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ITEM 3 QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

Our market risks at December 31, 2012 have not changed significantly from those described under Item 7A. Quantitative and Qualitative Disclosure about Market Risk in our Annual Report on Form 10-K for the year ended September 30, 2012.

ITEM 4 - CONTROLS AND PROCEDURES

We performed an evaluation of the effectiveness of our disclosure controls and procedures as of December 31, 2012. The evaluation was performed with the participation of senior management of each business segment and key corporate functions, and under the supervision of our Chief Executive Officer and our Chief Financial Officer. Based upon our evaluation we identified material weaknesses in internal control over financial reporting for

such periods.

Disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934, as amended, or the Exchange Act) are designed to provide reasonable assurance that information required to be disclosed in reports 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 (SEC) and that such information is accumulated and communicated to our management, including our Chief Executive Officer and our Chief Financial Officer, as appropriate to allow timely decisions regarding required disclosures.

As described below, management has identified material weaknesses in our internal control over financial reporting, which is an integral component of our disclosure controls and procedures. As a result of those material

weaknesses, our Chief Executive Officer and our Chief Financial Officer concluded that our disclosure controls and procedures were not effective as of December 31, 2012.

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

on a timely basis. In connection with management s assessment of our internal control over financial reporting described above, management has identified the following deficiencies that constituted individually, or in the aggregate, material weaknesses in our internal control over financial reporting as of December 31, 2012:

- In our process of assessing the appropriate accounting treatment for revenue and costs for certain of our contracts with customers,

we did not maintain a sufficient number of personnel with an appropriate level of U.S. generally accepted accounting principles (GAAP) knowledge and experience or ongoing training in the application of GAAP commensurate with the number and complexity of our contracts to prevent or detect material misstatements in revenue or cost of sales in a timely manner.

- Our policies for the

review and approval of revenue recognition decisions required review and analysis by personnel with an appropriate level of GAAP knowledge and experience for contracts over certain materiality thresholds. These thresholds were not designed to ensure that sufficient review was being performed for revenue recognition decisions that could have a material impact on our financial statements.

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Because of these material weaknesses, management has concluded that we did not maintain effective internal control over financial reporting as of December 31, 2012.

Changes in Internal Control over Financial Reporting There were no changes in our internal control over financial reporting during the quarter ended December 31, 2012 that materially affected or are reasonably likely

to materially affect our internal control over financial reporting. However, as described below under Plans for Remediation of Material Weaknesses, we have continued to dedicate resources to support our efforts to improve the control environment and to remedy the control weaknesses described herein.

Plans for Remediation of Material Weaknesses

We are in the process of adding resources and have

begun developing and implementing new processes and procedures to remediate the material weaknesses that existed in our internal control over financial reporting, and our disclosure controls and procedures, as of December 31, 2012. We have also begun revising our internal revenue recognition policy and procedures documentation to reflect the changes in policy we have implemented, and providing additional training to personnel involved in the revenue recognition

process.

We are developing a remediation plan (the Remediation Plan) to address the material weaknesses described above. The Remediation Plan will ensure that each area affected by a material control weakness is put through a remediation process. The Remediation Plan entails a thorough analysis which includes the following phases:

- Define and assess each control deficiency: ensure

a thorough understanding of the as is state, process owners, and procedural or technological gaps causing the deficiency. This work is underway for all identified areas;

- Design and evaluate a remediation action for each control deficiency for each affected area: validate or improve the related policy and procedure documentation; evaluate skills of the process owners and resources dedicated to each affected

area and adjust as required. The Remediation Plan will require an assessment of all control failures; we expect that many of the recent improvements will provide an appropriate starting point for the specific action plans;

- Implement specific remediation actions: train process owners, allow time for process adoption and adequate transaction volume for next steps;

- Test

and measure the design and effectiveness of the remediation actions; test and provide feedback on the design and operating effectiveness of the controls; and,

- Management review and acceptance of completion of the remediation effort.

The Remediation Plan will be administered by our Director of Internal Audit and will involve key leaders from across the organization, including our

Chief Executive Officer and our Chief Financial Officer. The Director of Internal Audit will report quarterly and as needed to the Audit Committee of our Board of Directors on the progress made toward completion of the Remediation Plan.

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We believe the steps taken to date have improved the effectiveness of our internal control over financial reporting, however we have not completed the corrective processes and procedures identified herein. Accordingly, as we continue to monitor the effectiveness of our internal control over financial reporting in the areas affected by the material weaknesses described above, we will perform

additional procedures prescribed by management including the use of manual mitigating control procedures and employ any additional tools and resources deemed necessary to ensure that our financial statements continue to be fairly stated in all material respects.

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PART II - OTHER INFORMATION

ITEM 1 - LEGAL PROCEEDINGS

In 1997, the Ministry of Defense for the Armed Forces of the Islamic Republic of Iran obtained a U. S. District Court judgment enforcing an arbitration award in its favor against us of $2.8 million, plus arbitration costs and interest related to a contract awarded

to us
by
Iran
in
1977.
Both
parties
appealed
to the
9th Circuit
Court
of
Appeals.
In
December 2011,
a
decision
was
handed
down
upholding
the
arbitration
award
and
requiring
the
district
court
to
resolve
outstanding
issues
related
to the
amount
of
interest
to be
paid
and
whether
the
plaintiff
should
be
awarded
attorney s
fees.
Under
a
1979
Presidential
executive
order,
all
transactions
by
U.S.
citizens
with
Iran

are prohibited; however, in April 2012 we received a license from the U.S. Treasury Department allowing us to remit the arbitration award and related post-judgment interest owed totaling $8.8 million to the U.S. District Court on April 18, 2012. We had recorded a liability for the judgment amount in periods prior to 2012 and had accrued interest through the date of the payment, so there was no

impact
on
2012
earnings
related
to
this
matter
other
than
interest
accrued
of
$0.2
million.
Through
September 30,
2012
we
did
not
accrue
a
liability
for
any
additional
pre-judgment
interest,
as we
were
unable
to
estimate
a
probability
of
loss
for
these
amounts.
On
January 3,
2013,
the
District
Court
decided
in
favor
of the
plaintiff
for
pre-judgment
interest
totaling
$0.6
million.
This
amount
was
recognized

as expense in the first quarter of fiscal 2013.

ITEM 1A - RISK FACTORS

There have been no material changes to the risk factors previously disclosed in Item 1A. Risk Factors of our Annual Report on Form 10-K for the year ended September 30, 2012, other than those set forth below, which should be read in conjunction with the risk factors

disclosed therein.

Risks Relating to Our Business

We depend on government contracts for substantially all of our revenues and the loss of government contracts or a delay or decline in funding of existing or future government contracts could decrease our backlog or adversely affect our sales and cash flows and our ability to fund our growth.

Our revenues from contracts, directly or indirectly, with foreign and U.S. state, regional and local governmental agencies represented more than 99% of our total revenues in fiscal year 2012. Although these various government agencies are subject to common budgetary pressures and other factors, many of our various government customers exercise independent purchasing decisions. As a result of the concentration of business with governmental agencies,

we are vulnerable to adverse changes in our revenues, income and cash flows if a significant number of our government contracts, subcontracts or prospects are delayed or canceled for budgetary or other reasons.

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The factors that could cause us to lose these contracts and could decrease our backlog or otherwise materially harm our business, prospects, financial condition or results of operations include:

- budget constraints affecting government spending generally, or specific departments or agencies such as U.S. or foreign defense and transit agencies and regional

transit agencies, and changes in fiscal policies or a reduction of available funding;

- re-allocation of government resources as the result of actual or threatened terrorism or hostile activities or for other reasons;

- disruptions in our customers ability to access funding from capital markets;

- curtailment of government s use of outsourced service providers and government s

in-sourcing of certain services;

- the adoption of new laws or regulations pertaining to government procurement;
- government appropriations delays or blanket reductions in departmental budgets;
- suspension or prohibition from contracting with the government or any significant agency with which we conduct business;
- increased use of

shorter duration awards by the federal government in the defense industry, which increases the frequency we may need to recompete for work;

- impairment of our reputation or relationships with any significant government agency with which we conduct business;

- impairment of our ability to provide third-party guarantees and letters of credit; and

- delays in the payment of our invoices by government payment offices.

In addition, some of our international work is done at the request and at the expense of the U.S. government and its agencies. For example, our Mission Support Services (MSS) business provides services to 13 NATO forces, with the U.S. Department of Defense (DOD) compensating us for these services. Therefore, risks associated with performing

work for the U.S. government and its agencies may also apply to our international contracts.

Government spending priorities and terms may change in a manner adverse to our businesses.

In the past, our businesses have been adversely affected by significant changes in U.S. and foreign government spending during periods of declining budgets. A significant decline in overall spending,

or the decision not to exercise options to renew contracts, or the loss of or substantial decline in spending on a large program in which we participate could materially adversely affect our business, prospects, financial condition or results of operations. For example, the U.S. defense and national security budgets in general, and spending in specific agencies with which we work, such as those that are a part of the

DOD, have declined from time to time for extended periods, resulting in program delays, program cancellations and a slowing of new program starts. Although spending on defense-related programs by the U.S. government and certain foreign governments has increased in recent years, such spending has decreased in recent years for certain other foreign governments, and future levels of expenditures and authorizations for defense-related programs

may decrease, remain constant or shift to programs in areas where we do not currently provide products or services, thereby reducing the chances that we will be awarded new contracts.

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Even though our contract periods of performance for a program may exceed one year, Congress and certain foreign governments must usually approve funds for a given program each fiscal year and may significantly reduce funding of a program in a particular year. Significant reductions in these appropriations or the amount of new defense contracts awarded may affect our ability

to complete contracts, obtain new work and grow our business. Congress and such foreign governments do not always enact spending bills by the beginning of the new fiscal year. Such delays leave the affected agencies under-funded which delays their ability to contract. Future delays and uncertainties in funding could impose additional business risks on us.

In addition, the DOD has recently

increased its emphasis on awarding contracts to small businesses and awarding shorter duration contracts, each of which has the potential to reduce the amount of revenue we could otherwise earn from such contracts. Shorter duration contracts lower our backlog numbers and increase the risk associated with recompeting for a contract, as we would need to do so more often. In addition, as we may need to

expend capital resources at higher levels upon the award of a new contract, the shorter the duration of the contract, the less time we have to recoup such expenditures and turn a profit under such contract.

Sequestration may adversely affect our businesses which are dependent on federal government funding.

Pursuant to laws passed in August 2011 and January 2013, unless

the current presidential administration and Congress reach an agreement on spending cuts and increased revenues for the federal government before March 1, 2013, there will be deep and automatic cuts in defense budgets and other non-defense budgets. It is unknown what programs will be cut, over what time period and by what amount. Some programs may be cancelled in their entirety.

All of our

U.S. defense contracts are at risk of being cut or terminated. Our domestic transportation contracts could be materially harmed if transit agencies do not receive expected federal funds and are required to curtail their plans to expand or upgrade their fare collection systems. Any cuts or cancellations of our contracts may materially harm our business, prospects, financial condition and results of operations.

Failure to retain existing contracts or win new contracts under competitive bidding processes may adversely affect our revenue.

We obtain most of our contracts through a competitive bidding process, and substantially all of the business that we expect to seek in the foreseeable future likely will be subject to a competitive bidding process. Competitive bidding presents a number of risks, including:

- the need to compete against companies or teams of companies with more financial and marketing resources and more experience in bidding on and performing major contracts than we have;

- the need to compete against companies or teams of companies that may be long-term, entrenched incumbents for a particular contract for which we are competing and

that have, as a result, greater domain expertise and better customer relations;

• the need to compete to retain existing contracts that have in the past been awarded to us on a sole-source basis or as to which we have been incumbent for a long time;

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- the U.S. government s increased emphasis on awarding contracts to small businesses could preclude us from bidding on certain work or reduce the scope of work we can bid as a prime contractor and limit the amount of revenue we could otherwise earn as a prime contractor for such contracts;

- the award

of contracts to providers offering solutions at the lowest price technically acceptable which may lower the profit we may generate under a contract awarded using this pricing method or prevent us from submitting a bid for such work due to us deeming such work to be unprofitable;

- the reduction of margins achievable under any contracts awarded to us;

- the expense and delay that may arise if our competitors protest or challenge new contract awards;
- the need to bid on some programs in advance of the completion of their design, which may result in higher research and development expenditures, unforeseen technological difficulties, or increased costs which lower our profitability;
- the substantial cost and managerial

time and effort, including design, development and marketing activities, necessary to prepare bids and proposals for contracts that may not be awarded to us;

- the need to develop, introduce and implement new and enhanced solutions to our customers needs;

- the need to locate and contract with teaming partners and subcontractors; and

- the need to accurately estimate the resources and cost structure that will be required to perform any fixed-price contract that we are awarded.

We may not be afforded the opportunity in the future to bid on contracts that are held by other companies and are scheduled to expire if the agency decides to extend the existing contract. If we are unable

to
win
particular
contracts
that
are
awarded
through
the
competitive
bidding
process,
we
may
not
be
able
to
operate
in the
market
for
services
that
are
provided
under
those
contracts
for a
number
of
years.
If we
win a
contract,
and
upon
expiration
the
customer
requires
further
services
of the
type
provided
by
the
contract,
there
is
frequently
a
competitive
rebidding
process
and
there
can
be no
assurance

that we will win any particular bid, or that we will be able to replace business lost upon expiration or completion of a contract.

As a result of the complexity and scheduling of contracting with government agencies, we occasionally incur costs before receiving contractual funding by the government agency. In some circumstances, we may not be able to recover these costs in

whole or in part under subsequent contractual actions.

In addition, the customers currently serviced by our Cubic Transportation Systems segment are finite in number. The loss of any one of these customers, or the failure to win replacement awards upon expiration of contracts with such customers, could have a materially adverse impact on our results of operations.

If we are unable to consistently retain existing contracts or win new contract awards, our business, prospects, financial condition and results of operations will be adversely affected.

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Many of our U.S. government customers spend their procurement budgets through multiple-award or indefinite delivery/indefinite quantity (ID/IQ) contracts, under which we are required to compete among the awardees for post-award orders. Failure to win post-award orders could affect our ability to increase our sales.

The U.S. government can select multiple winners

under multiple-award contracts, federal supply schedules and other agency-specific ID/IQ contracts, as well as award subsequent purchase orders among such multiple winners. This means that there is no guarantee that these ID/IQ, multiple-award contracts will result in the actual orders equal to the ceiling value under the contract, or result in any actual orders. We are only eligible to compete for work (purchase orders and

delivery orders) as an awardee pursuant to government-wide acquisition contracts already awarded to us. Our failure to compete effectively in this procurement environment could reduce our sales, which would adversely affect our business, results of operations and financial condition.

The U.S. government s increased emphasis on awarding contracts to small businesses could preclude us from acting as a prime contractor and increase the

number of contracts we receive as a subcontractor to small businesses, which could decrease the amount of our revenues from such contracts. Some of these small businesses may not be financially sound, which could adversely affect our business.

There is increased emphasis by the U.S. government on awarding contracts to small businesses which may preclude companies the size of ours

from obtaining certain work, other than as a subcontractor to these small businesses. There are inherent risks in contracting with small companies that may not have the capability or financial resources to perform these contracts or administer them correctly. If a small business with which we have a subcontract fails to perform, fails to bill the government properly or fails financially, we may have difficulty

receiving
timely
payments
or
may
incur
bad
debt
write-offs
if the
small
business
is
unable
or
unwilling
to
pay
us for
work
we
perform.
In
addition,
being
a
subcontractor
may
limit
the
amount
of
revenue
we
could
otherwise
earn
as a
prime
contractor
for
such
contracts.
When
we
only
act as
a
subcontractor,
we
may
only
receive
up to
49%
of the
value
of the
contract
award,
and
such

percentage may be less should the small business partner or partners be able to service a larger piece of the award. Failure to maintain good relationships with small business partners operating in our industries could preclude us from winning work as a subcontractor as part of a large contracting consultation. This could result in significant adverse effects on our revenues, operating costs and cash flows.

Government audits of our contracts could result in a material charge to our earnings, have a negative effect on our cash position following an audit adjustment or adversely affect our ability to conduct future business.

U.S. government agencies, including the DOD and others, routinely audit and review a contractor s performance on government contracts, indirect rates and pricing

practices, and compliance with applicable contracting and procurement laws, regulations and standards. Based on the results of such audits, the auditing agency is authorized to adjust our unit prices if the auditing agency does not find them to be fair and reasonable. The auditing agency is also authorized to require us to refund any excess proceeds we received on a particular item over its final adjusted

unit
price.

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The DOD, in particular, also reviews the adequacy of, and compliance with, our internal control systems and policies, including our purchasing, accounting, financial capability, pricing, labor pool, overhead rate and management information systems. Our failure to obtain an adequate determination of our various accounting and management internal control systems from the responsible U.S. government agency

could significantly and adversely affect our business, including our ability to bid on new contracts and our competitive position in the bidding process. Failure to comply with applicable contracting and procurement laws, regulations and standards could also result in the U.S. government imposing penalties and sanctions against us, including suspension of payments and increased government scrutiny that could delay or adversely affect our ability to

invoice and receive timely payment on contracts or perform contracts, or could result in suspension or debarment from competing for contracts with the U.S. government. In addition, we could suffer serious harm to our reputation if allegations of impropriety were made against us, whether or not true.

In addition, transit authorities have the right to audit our work under their respective

contracts. If as the result of an adverse audit finding, we were suspended or prohibited from contracting with the U.S. government, any significant government agency, or a transit authority terminates its contract with us, or if our reputation or relationship with such agencies and authorities was impaired or if they otherwise ceased doing business with us or significantly decreased the amount of business done with us, it would adversely affect

our business, results of operations and financial condition.

Our international business exposes us to additional risks, including exchange rate fluctuations, foreign tax and legal regulations and political or economic instability that could harm our operating results.

Our international operations, which represented 47% of our revenues for fiscal year 2012, subject us to risks associated with operating in and

selling products or services in foreign countries, including:

- devaluations and fluctuations in currency exchange rates;
- changes in foreign laws that adversely affect our ability to sell our products or services or our ability to repatriate profits to the United States;
- increases or impositions of withholding and other taxes on remittances and

other payments by foreign subsidiaries or joint ventures to us;

- increases in investment and other restrictions or requirements by foreign governments in order to operate in the territory or own the subsidiary;
- costs of compliance with local laws, including labor laws;
- compliance with anti-corruption laws, anti-money laundering laws and sanctions;

- export control regulations and policies which govern our ability to supply foreign customers;
- unfamiliar and unknown business practices and customs;
- domestic and foreign government policies, including requirements to expend a portion of program funds locally and governmental industrial cooperation requirements;
- the complexity and necessity of

using
foreign
representatives
and
consultants
or
being
prohibited
from
such
use;

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- the uncertainty of the ability of foreign customers to finance purchases;
- imposition of tariffs or embargoes, export controls and other trade restrictions;
- potentially being prohibited from bidding for international work due to perceived conflicts or national security concerns resulting from the significant amount of work

we do for the U.S. government and its agencies;

- the difficulty of management and operation of an enterprise in various countries; and

- economic and geopolitical developments and conditions, including ongoing instability in global economies and financial markets, international hostilities, acts of terrorism and governmental reactions, inflation, trade relationships and military and political alliances.

Our foreign subsidiaries generally enter into contracts and make purchase commitments that are denominated in foreign currencies. Accordingly, we are exposed to fluctuations in exchange rates, which could have a significant impact on our results of operations. We have no control over the factors that generally affect this risk, such as economic, financial and political events and the supply of and demand

for applicable currencies. While we use foreign exchange forward and option contracts to hedge significant contract sales and purchase commitments that are denominated in foreign currencies, our hedging strategy may not prevent us from incurring losses due to exchange fluctuations.

We may not be able to receive the necessary licenses required for us to sell our export-controlled products and services overseas.

In addition, the loss of our registration as either an exporter or a broker under International Traffic in Arms Regulations (ITAR), would adversely affect our business, results of operations and financial condition.

U.S. government agencies, primarily the Directorate of Defense Trade Controls within the State Department and the Bureau of Industry Security within the U.S. Department of Commerce, must license

shipments of certain export-controlled products that we export. These licenses are required due to both the products we export and to the foreign customers we service. If we do not receive a license for an export-controlled product, we cannot ship that product. We cannot be sure of our ability to gain any licenses required to export our products, and failure to receive a required license would

eliminate our ability to make that sale. A delay in obtaining the necessary licenses to sell our export-controlled products abroad could result in delayed deliveries and delayed recognition of revenue, which could cause us reputational damage and could result in a customer s decision not to do business with us in the future. We may also be subject to inquiries by such U.S. government agencies relating to

issues involving the export-controlled products and services we export and failure to satisfactorily resolve such inquiries would adversely affect our business, results of operations and financial condition.

In addition to obtaining a license for certain of our exports outside of the United States, we are also required to maintain a standing registry under ITAR as an exporter. We operate as an exporter when

we ship certain products to our customers outside the United States. If we were to lose our registration as an exporter under ITAR, we would not be able to sell export-controlled products abroad, which would adversely affect our business, results of operations and financial condition.

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Our operating margins may decline under our fixed-price contracts if we fail to accurately estimate the time and resources necessary to satisfy our obligations.

Approximately 72% of our revenues in 2012 were from fixed-price contracts under which we bear the risk of cost overruns. Our profits are adversely affected if our costs under these contracts

exceed the assumptions we used in bidding for the contract. We may therefore need to absorb any increases in our supply costs and may not be able to pass such costs increases along to our customers. Sometimes we are required to fix the price for a contract before the project specifications are finalized, which increases the risk that we will incorrectly price these contracts. The complexity

of many of our engagements makes accurately estimating the time and resources required more difficult.

We may not receive the full amounts estimated under the contracts in our total backlog, which could reduce our net sales in future periods below the levels anticipated and which makes backlog an uncertain indicator of future operating results.

As of December 31,

2012, our total backlog was $2,816.4 million. Orders may be cancelled and scope adjustments may occur, and we may not realize the full amounts of net sales that we may anticipate in our backlog numbers. There can be no assurance that the projects underlying the contracts and purchase orders will be placed or completed or that amounts included in our backlog ultimately will be billed and

collected. Additionally, the timing of receipt of net sales, if any, on contracts included in our backlog could change. The failure to realize amounts reflected in our backlog could materially adversely affect our business, financial condition and results of operations in future periods.

We may be liable for civil or criminal penalties under a variety of complex laws and regulations, and changes

in governmental regulations could adversely affect our business and financial condition.

Our businesses must comply with and are affected by various government regulations that impact our operating costs, profit margins and our internal organization and operation of our businesses. These regulations affect how we do business and, in some instances, impose added costs. Any changes in applicable laws could adversely affect

our business and financial condition. Any material failure to comply with applicable laws could result in contract termination, price or fee reductions or suspension or debarment from contracting. The more significant regulations include:

- the Federal Acquisition Regulations (FAR) and all department and agency supplements, which comprehensively regulate the formation, administration and performance of U.S. government contracts;

- the Truth in Negotiations Act and implementing regulations, which require certification and disclosure of all cost and pricing data in connection with contract negotiations;

- the ITAR, which control the export and import of defense related articles and services on the United States Munitions Control List;

- laws, regulations and executive orders restricting the use

and dissemination of information classified for national security purposes and the exportation of certain products and technical data;

- regulations of most state and regional agencies and foreign governments similar to those described above;

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- the trade sanctions laws and regulations administered by the U.S. Department of the Treasury s Office of Foreign Assets Control;
- the Foreign Corrupt Practices Act and the U.K. Bribery Act;
- the Sarbanes-Oxley Act of 2002 and the Dodd-Frank Wall Street Reform and Protection Act;

- healthcare reform laws and regulations, including those enacted under the Patient Protection and Affordable Care Act, as amended by the Health Care and Education Affordability Reconciliation Act of 2010; and

- tax laws and regulations in the U.S. and in other countries in which we operate;

- the civil False Claims Act, which provides for

substantial civil penalties for violations, including for submission of a false or fraudulent claim to the U.S. government for payment or approval;

- the Procurement Integrity Act, which requires evaluation of ethical conflicts surrounding procurement activity and establishing certain employment restrictions for individuals who participate in the procurement process; and

- the Small Business Act and the Small

Business Administration, or the SBA, size status regulations, which regulate eligibility for performance of government contracts which are set aside for, or a preference is given in the evaluation process if awarded to, specific types of contractors such as small businesses and minority-owned businesses.

The FAR and many of our U.S. government contracts contain organizational conflicts of interest clauses that may limit our

ability to compete for or perform certain other contracts. Organizational conflicts of interest arise when we engage in activities that provide us with an unfair competitive advantage. A conflict of interest issue that precludes our competition for or performance on a significant program or contract could harm our prospects and negative publicity about a conflict of interest issue could damage our reputation.

In addition, the U.S. and foreign governments may revise existing contract rules and regulations or adopt new contract rules and regulations at any time and may also face restrictions or pressure regarding the type and amount of services it may obtain from private contractors. For instance, Congressional legislation and initiatives dealing with procurement reform and shifts in the buying practices of U.S. government agencies resulting from

those proposals could have adverse effects on government contractors, including us. Any of these changes could impair our ability to obtain new contracts or renew contracts under which we currently perform when those contracts are eligible for recompetition. Any new contracting methods could be costly or administratively difficult for us to implement, which would adversely affect our business, results of operations and financial

condition.

Our failure to identify, attract and retain qualified technical and management personnel could adversely affect our existing businesses, financial condition and results of operations.

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We may not be able to identify, attract or retain qualified technical personnel, including engineers, computer programmers and personnel with security clearances required for classified work, or management personnel to supervise such activities that are necessary for maintaining and growing our existing businesses, which could adversely affect our financial condition and results of operations.

The technically complex nature of our operations results in difficulties finding qualified staff. In our defense businesses especially, experienced personnel possessing required security clearances are finite in number. A number of our employees maintain a top secret clearance level. Obtaining and maintaining security clearances for employees involves a lengthy process, and it is difficult to identify, recruit and retain employees who already hold security clearances. If our cleared

employees lose or are unable to timely obtain security clearances or we lose a facility clearance, our U.S. government customers may terminate the contract or decide not to renew it upon its expiration. As a result, to the extent we cannot obtain or maintain the required security clearances for a particular contract, or we fail to obtain them on a timely basis, we may not generate the sales anticipated from the contract,

which could harm our operating results. To the extent we are not able to obtain facility security clearances or engage employees with the required security clearances for a particular contract, we will be unable to perform that contract and we may not be able to compete for or win new awards for similar work.

We may incur significant costs in protecting

our intellectual property which could adversely affect our profit margins. Our inability to obtain, maintain and enforce our patents and other proprietary rights could adversely affect our businesses prospects and competitive positions.

We seek to protect our proprietary technology and inventions through patents and other proprietary-right protection, and also rely on trademark laws to protect our brand. However, we

may fail to obtain the intellectual property rights necessary to provide us with a competitive advantage, and any of our owned or licensed intellectual property rights could be challenged, invalidated, circumvented, infringed or misappropriated. We may also fail to apply for or obtain intellectual property protection in important foreign countries, and the laws of some foreign countries do not protect proprietary rights to the same extent as the

laws
of the
United
States.
If we
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unable
to
obtain
or
maintain
these
protections,
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may
not
be
able
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prevent
third
parties
from
using
our
technology
and
inventions,
which
could
adversely
affect
our
business.
We
may
incur
significant
expense
in
obtaining,
maintaining,
defending
and
enforcing
our
intellectual
property
rights.
We
may
fail to
take
the
actions
necessary
to
enforce
our
intellectual
property
rights

and
even
if we
attempt
to
enforce
such
rights
we
may
ultimately
be
unsuccessful,
and
such
efforts
may
result
in our
intellectual
property
rights
being
challenged,
limited
in
scope,
or
declared
invalid
or
unenforceable.
Also,
some
aspects
of our
business
and
services
may
rely
on
technologies
and
software
developed
by or
licensed
from
third
parties,
and
we
may
not
be
able
to
maintain
our
relationships
with

such third parties or enter into similar relationships in the future on reasonable terms or at all.

We also rely on trade secrets, proprietary know-how and continuing technological innovation to remain competitive. We have taken measures to protect our trade secrets and know-how, including seeking to enter into confidentiality agreements with our employees, consultants and advisors, but the measures we

have taken may not be sufficient. For example, confidentiality agreements may not provide adequate protection or may be breached. We generally control and limit access to our product documentation and other proprietary information, but other parties may independently develop our know-how or otherwise obtain access to our technology, which could adversely affect our businesses prospects and competitive position.

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Assertions by third parties that we violate their intellectual property rights could have a material adverse effect on our business, financial condition and results of operations.

Third parties may claim that we, our customers, licensees or parties indemnified by us are infringing upon or otherwise violating their intellectual property rights. Such claims

may be made by competitors seeking to obtain a competitive advantage or by other parties. Additionally, in recent years, individuals and groups have begun purchasing intellectual property assets for the purpose of making claims of infringement and attempting to extract settlements from companies like ours. Any claims that we violate a third party s intellectual property rights can be time consuming and costly to

defend and distract management s attention and resources, even if the claims are without merit. Such claims may also require us to redesign affected products and services, enter into costly settlement or license agreements or pay costly damage awards, or face a temporary or permanent injunction prohibiting us from marketing or providing the affected products and services. Even if we have an agreement to indemnify us against

such costs, the indemnifying party may be unable to uphold its contractual obligations. If we cannot or do not license the infringed technology on favorable terms or cannot or do not substitute similar technology from another source, our revenue and earnings could be adversely impacted.

We compete primarily for government contracts against many companies that are larger, better capitalized and better known

than us. If we are unable to compete effectively, our business and prospects will be adversely affected.

Our businesses operate in highly competitive markets. Many of our competitors are larger, better financed and better known companies who may compete more effectively than we can. In order to remain competitive, we must keep our capabilities technically advanced and compete on price and

on value added to our customers. Our ability to compete may be adversely affected by limits on our capital resources and our ability to invest in maintaining and expanding our market share. Consolidation in the industries in which we operate and government budget cuts have led to pressure being placed on the margins we may earn on any contracts we win. In addition, should the

transportation market move towards requiring contractors to provide up-front financing for contracts they are awarded (for example, our contract for the Chicago Open Standards Fare System), we may need to compete more heavily on the basis of our financial strength, which may limit the contracts we can service at any one time.

The terms of our financing arrangements may restrict our

financial and operational flexibility, including our ability to invest in new business opportunities.

We currently have unsecured borrowing arrangements. The terms of these borrowing arrangements include provisions that limit our levels of debt and require minimum levels of net worth and coverage of fixed charges. We may incur future obligations that would subject us to additional covenants that affect our financial

and operational flexibility or subject us to different events of default. In addition, the cost of servicing such debt could divert resources which may otherwise be used to develop our businesses.

Our current $200.0 million unsecured revolving credit agreement expires in May 2017. The available line of credit on the agreement is reduced by any letters of credit issued under the

agreement. As of December 31, 2012, there were borrowings of $25.0 million outstanding under the agreement, of which $5.0 million was repaid in February, 2013. Our borrowings under the agreement bear interest at a variable rate (1.6% at December 31, 2012). In addition, as of December 31, 2012, there were letters of credit outstanding under the agreement totaling $42.4 million, which reduced the available line of credit to

$132.6 million at that date.

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We also have a secured letter of credit facility agreement with a bank that expires in March 2013. We are currently negotiating an extension of the agreement for approximately one year. As of December 31, 2012 there were letters of credit outstanding under this agreement of $63.4 million. In support of this facility, we placed $68.8 million of our

cash on deposit in the U.K. as collateral in a restricted account with the bank providing the facility. We are required to leave the cash in the restricted account so long as the bank continues to maintain associated letters of credit under the facility. The maximum amount of letters of credit currently allowed by the facility is $66.8 million, and any increase above this amount would

require bank approval and additional restricted funds to be placed on deposit. We may choose at any time to terminate the facility and move the associated letters of credit to another credit facility. Letters of credit outstanding under this facility do not reduce the available line of credit available under the revolving credit agreement described above.

Our development contracts may be

difficult for us to comply with and may expose us to third-party claims for damages.

We are often party to government and commercial contracts involving the development of new products and systems. These contracts typically contain strict performance obligations and project milestones. We cannot assure you we will comply with these performance obligations or meet these project milestones in the future. If we

are unable to comply with these performance obligations or meet these milestones, our customers may terminate these contracts and, under some circumstances, recover damages or other penalties from us. If other parties elect to terminate their contracts or seek damages from us, it could materially harm our business and negatively impact our stock price.

Our revenues could be less than expected

if we are not able to deliver services or products as scheduled due to disruptions in supply.

Since our internal manufacturing capacity is limited, we use contract manufacturers. While we use care in selecting our manufacturers, we have less control over the reliability of supply, quality and price of products or components than if we manufactured them. In some cases, we

obtain
products
from
a sole
supplier
or a
limited
group
of
suppliers.
Consequently,
we
risk
disruptions
in our
supply
of
key
products
and
components
if our
suppliers
fail or
are
unable
to
perform
because
of
shortages
in
raw
materials,
operational
problems,
strikes,
natural
disasters,
financial
condition
or
other
factors.
We
may
have
disputes
with
our
vendors
arising
from,
among
other
things,
the
quality
of
products
and
services

or customer concerns about the vendor. If any of our vendors fail to timely meet their contractual obligations or have regulatory compliance or other problems, our ability to fulfill our obligations may be jeopardized. Economic downturns can adversely affect a vendor s ability to manufacture or deliver products. Further, vendors may also be enjoined from manufacturing and distributing products to us as a result of litigation filed by

third parties, including intellectual property litigation. If we were to experience difficulty in obtaining certain products, there could be an adverse effect on our results of operations and on our customer relationships and our reputation. Additionally, our key vendors could also increase pricing of their products, which could negatively affect our ability to win contracts by offering competitive prices.

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Any material supply disruptions could adversely affect our ability to perform our obligations under our contracts and could result in cancellation of contracts or purchase orders, penalties, delays in realizing revenues, payment delays, as well as adversely affect our ongoing product cost structure.

Our future success will depend on our ability

to develop new products, systems and services that achieve market acceptance in our current and future markets.

Both our commercial and government businesses are characterized by rapidly changing technologies and evolving industry standards. Accordingly, our performance depends on a number of factors, including our ability to:

- identify emerging technological trends in our current and target markets;

- develop and maintain competitive products, systems and services;

- enhance our offerings by adding technological innovations that differentiate our products, systems and services from those of our competitors; and

- develop, manufacture and bring to market cost-effective offerings quickly.

We believe that, in order to remain competitive in the future,

we will need to continue to develop new products, systems and services, which will require the investment of significant financial resources. The need to make these expenditures could divert our attention and resources from other projects, and we cannot be sure that these expenditures ultimately will lead to the timely development of new products, systems or services. We currently spend approximately 1 to 2% of

our
annual
net
sales
on
R&D
efforts,
primarily
in our
Cubic
Defense
Systems
(CDS)
and
Cubic
Transportation
Systems
(CTS)
segments.
There
can
be no
assurances
that
this
percentage
will
not
increase
should
we
require
increased
innovations
to
successfully
compete
in the
markets
we
serve.
We
may
also
experience
delays
in
completing
development
and
introducing
certain
new
products,
systems
or
services
in the
future
due
to
their

design complexity. Any delays could result in increased costs of development or redirect resources from other projects. In addition, we cannot provide assurances that the markets for our products, systems or services will develop as we currently anticipate, which could significantly reduce our revenue and harm our business. Furthermore, we cannot be sure that our competitors will not develop competing products, systems or

services that gain market acceptance in advance of ours, or that cause our existing products, systems or services to become non-competitive or obsolete, which could adversely affect our results of operations.

If we deliver products or systems with defects, our reputation will be harmed, revenue from, and market acceptance of, our products and systems will decrease and we could expend

significant capital and resources as a result of such defects.

Our products and systems are complex and frequently operate in high-performance, challenging environments. Notwithstanding our internal quality specifications, our products and systems have sometimes contained errors, defects and bugs when introduced. If we deliver products or systems with errors, defects or bugs, our reputation and the market acceptance and sales of our

products and systems would be harmed. Further, if our products or systems contain errors, defects or bugs, we may be required to expend significant capital and resources to alleviate such problems and incur significant costs for product recalls and inventory write-offs. Defects could also lead to product liability lawsuits against us or against our customers, and could also damage our reputation. We have agreed

to indemnify our customers in some circumstances against liability arising from defects in our products and systems. In the event of a successful product liability claim, we could be obligated to pay damages significantly in excess of our product liability insurance limits.

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We face certain significant risk exposures and potential liabilities that may not be covered adequately by insurance or indemnity.

We are exposed to liabilities that are unique to the products and services we provide. A significant portion of our business relates to designing, developing, manufacturing, operating and maintaining advanced defense and transportation systems

and products. New technologies associated with these systems and products may be untested or unproven. In addition, certain activities in connection with which our training systems are used or our services are provided are inherently dangerous. While in some circumstances we may receive indemnification from U.S. and foreign governments, and we maintain insurance for certain risks, the amount of our insurance or indemnity may

not
be
adequate
to
cover
all
claims
or
liabilities,
and
we
may
be
forced
to
bear
substantial
costs
from
an
accident
or
incident.
It
also
is not
possible
for us
to
obtain
insurance
to
protect
against
all
operational
risks
and
liabilities.
Substantial
claims
resulting
from
an
incident
in
excess
of the
indemnification
we
receive
and
our
insurance
coverage
would
harm
our
financial
condition,
results
of

operations and cash flows. Moreover, any accident or incident for which we are liable, even if fully insured, could negatively affect our standing with our customers and the public, thereby making it more difficult for us to compete effectively, and could significantly impact the cost and availability of adequate insurance in the future.

We may acquire other companies, which could increase

our costs or liabilities or be disruptive to our business.

Part of our strategy involves the acquisition of other companies. For example, in December 2012, we acquired the operating assets of NEK Special Programs Group, LLC, a special operation forces training business, including more than 200 operational and technical experts. We cannot assure you that we will be able to integrate

acquired companies successfully without substantial expense, delay or operational or financial problems. Such expenses, delays or operational or financial problems may include the following:

- we may need to divert management resources to integration, which may adversely affect our ability to pursue other more profitable activities;
- integration may be difficult as a result of the necessity

of coordinating geographically separated organizations, integrating personnel with disparate business backgrounds and combining different corporate cultures;

- we may not be able to eliminate redundant costs anticipated at the time we select acquisition candidates; and

- one or more of our acquisition candidates may have unexpected liabilities, fraud risk, or adverse operating issues that we fail to discover

through our due diligence procedures prior to the acquisition.

As a result, the integration of acquired businesses may be costly and may adversely impact our results of operations and financial condition.

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Our employees may engage in misconduct or other improper activities, which could harm our business, financial condition and results of operations.

We are exposed to the risk of employee fraud or other misconduct. Employee misconduct could include intentionally failing to comply with U.S. government procurement regulations, engaging in unauthorized activities, attempting to

obtain reimbursement for improper expenses, or submitting falsified time records, which could result in legal proceedings against us, lost contracts or reduced revenues. For example, see Item 3. Legal Proceedings of our Annual Report on Form 10-K for the year ended September 30, 2012 for a discussion of certain litigation relating to misconduct by one of our former employees. Employee misconduct could also involve improper use of our

customers sensitive or classified information, which could result in regulatory sanctions against us and serious harm to our reputation. It is not always possible to deter employee misconduct, and the precautions we take to prevent and detect this activity may not be effective in controlling unknown or unmanaged risks or losses, which could harm our business, financial condition and results of operations. In addition,

alleged or actual employee misconduct could result in investigations or prosecutions of employees engaged in the subject activities, which could result in unanticipated consequences or expenses and management distraction for us regardless of whether we are alleged to have any responsibility.

The funding and costs associated with our pension plans may cause our earnings, cash flows, and shareholders equity to fluctuate

significantly from year to year.

Certain of our employees in the U.S. are covered by a noncontributory defined benefit pension plan and approximately one-half of our European employees are covered by a contributory defined benefit pension plan. The impact of these plans on our GAAP earnings may be volatile in that the amount of expense we record for our pension plans may materially change

from year to year because those calculations are sensitive to changes in several key economic assumptions, including discount rates, inflation, salary growth, expected return on plan assets, retirement rates and mortality rates. Changes in these factors affect our plan funding, cash flows, earnings, and shareholders equity.

In recent years, we have taken certain actions to mitigate the effect of our

defined benefit pension plans on our financial results. For example, benefits under the U.S. plan were frozen as of December 31, 2006, so no new benefits have accrued after that date, and benefits under the European plan were frozen as of September 30, 2010, though the European plan is a final pay plan, which means that benefits will be adjusted for increases in the salaries of participants until their

retirement or departure from the company. U.S. and European employees hired subsequent to the dates of freezing of the respective plans are not eligible for participation in the defined benefit plans. For more information on how these factors could impact earnings, cash flows and shareholders equity, see Item 7. Management s Discussion and Analysis of Financial Condition and Results of Operations Critical Accounting Policies, Estimates and Judgments Pension

Costs in our Annual Report on Form 10-K for the year ended September 30, 2012.

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Risks Relating to Our Common Stock and the Securities Markets

The price of our common stock may fluctuate significantly, and you could lose all or part of your investment.

Our common stock has traded as high as $57.75 and as low as $37.16 since October 1, 2010. An active, liquid

and orderly market for our common stock may not be sustained, which could depress the trading price of our common stock. The market price of our common stock could fluctuate significantly for various reasons, which include:

- our quarterly or annual earnings or those of our competitors;
- the public s reaction to our press releases, our other public announcements

and our filings with the Securities and Exchange Commission;

- changes in earnings estimates or recommendations by research analysts who track our common stock or the stocks of our competitors;

- new laws or regulations or new interpretations of laws or regulations applicable to our business;

- changes in accounting standards, policies, guidance, interpretations

or principles;

- changes in general conditions in the domestic and global economies or financial markets, including those resulting from war, incidents of terrorism or responses to such events;

- litigation involving our company or investigations or audits by regulators into the operations of our company or our competitors;

- strategic action by our

competitors; and

- sales of common stock by our directors, executive officers and significant shareholders.

In addition, the stock market in general has experienced extreme price and volume fluctuations that have often been unrelated or disproportionate to the operating performance of those companies. Broad market and industry factors may seriously affect the market price of our common

stock, regardless of actual operating performance. In addition, in the past, following periods of volatility in the overall market and the market price of a particular company s securities, securities class action litigation has often been instituted against these companies. If litigation is instituted against us, it could result in substantial costs and a diversion of our management s attention and resources.

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Our Executive Chairman of the Board of Directors beneficially owns a large percentage of our common stock and as a result can exert significant influence over us.

As of December 31, 2012, Walter C. Zable, our Executive Chairman of the Board of Directors, and Karen Zable Cox, Mr. Zable s sister, beneficially owned an aggregate of 9,257,526 shares,

or
approximately
34.6%,
of our
common
stock.
Of
these
shares,
an
aggregate
of
8,826,396
shares,
or
approximately
33.0%
of our
common
stock,
were
owned
by
trusts,
of
which
Mr. Zable
and
Ms. Cox
are
co-trustees.
In
their
capacities
as
co-trustees,
Mr. Zable
and
Ms. Cox
share
voting
and
dispositive
power
over
the
shares
owned
by
such
trusts.
Accordingly,
Mr. Zable
and
Ms. Cox
may
be
able
to
substantially
influence
all

matters requiring approval by our shareholders, including the election of directors and the approval of mergers or other business combination transactions. Circumstances may arise in which the interests of these shareholders could conflict with the interests of our other shareholders. These shareholders could delay or prevent a change in control of Cubic even if such a transaction would be beneficial to our other shareholders.

Your percentage ownership in us may be diluted by future issuances of capital stock, which could reduce your influence over matters on which shareholders vote.

Our board of directors has the authority, without action or vote of our shareholders, to issue all or any part of our authorized but unissued shares of common stock, including shares issuable upon the exercise

of options, shares that may be issued in the future under our 2005 Equity Incentive Plan or shares of our authorized but unissued preferred stock. Issuances of common stock or preferred voting stock could reduce your influence over matters on which our shareholders vote and, in the case of issuances of preferred stock, likely could result in your interest in us being subject to the prior rights

of holders of that preferred stock.

Provisions in our charter documents and Delaware law could delay or prevent a change in control of Cubic.

Provisions of our amended and restated certificate of incorporation and amended and restated bylaws may discourage, delay or prevent a merger, acquisition or other change in control that shareholders may consider favorable,

including transactions in which shareholders might otherwise receive a premium for their shares. In addition, these provisions may frustrate or prevent any attempt by our shareholders to replace or remove our current management by making it more difficult to replace or remove our board of directors. These provisions include:

- prior to the date of the transaction, an affirmative vote

of the holders of at least 66-2/3% of our outstanding common stock is required for the approval, adoption or authorization of a business combination;

- a prohibition on shareholder action through written consent;

- a requirement that special meetings of shareholders be called only by our board of directors or by a committee of our board of directors that has been

duly designated to do so by our board of directors;

- the authority of our board of directors to issue preferred stock with such terms as our board of directors may determine; and

- a requirement for the affirmative vote of the holders of at least 66-2/3% of the total voting power of all outstanding shares of our voting stock to amend our amended

and restated bylaws, or to amend specific provisions of our amended and restated certificate of incorporation.

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In addition, Delaware law prohibits a publicly held Delaware corporation from engaging in a business combination with an interested shareholder, generally a person who, together with its affiliates, owns or within the last three years has owned 15% of our voting stock, for a period of three years after the date of the transaction in which the person

became an interested shareholder, unless the business combination is approved in a prescribed manner. Accordingly, Delaware law may discourage, delay or prevent a change in control of our company.

If we are unable to pay semiannual dividends at the targeted level, our reputation and stock price may be harmed.

In August 2012, our board of directors approved a semiannual dividend

on common stock of $0.12 per share. We have paid uninterrupted semiannual dividends to our shareholders since 1971, and, in fiscal 2012, we paid $6.4 million of cash dividends to our shareholders.

The dividend program requires the use of a portion of our cash flows. Our ability to continue to pay semiannual dividends will depend on our ability to generate sufficient cash flows

from operations in the future. This ability may be subject to certain economic, financial, competitive and other factors that are beyond our control. Our board of directors may, at its discretion, decrease the targeted semiannual dividend amount or entirely discontinue the payment of dividends at any time. Any failure to pay dividends after we have announced our intention to do so may adversely affect our reputation

and investor confidence in us, and negatively impact our stock price.

If securities or industry analysts cease to publish research or publish inaccurate or unfavorable research about our business, our stock price and trading volume could decline.

The trading market for our common stock depends in part on the research and reports that securities or industry

analysts
publish
about
us or
our
business.
If one
or
more
of the
analysts
who
cover
us
downgrade
our
stock
or
publish
inaccurate
or
unfavorable
research
about
our
business,
our
stock
price
would
likely
decline.
If one
or
more
of
these
analysts
cease
coverage
of our
company
or fail
to
publish
reports
on us
regularly,
demand
for
our
stock
could
decrease,
which
might
cause
our
stock
price
and
trading

volume
to
decline.

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ITEM 6 - EXHIBITS

(a) The following exhibits are included herein:

Exhibit No.	Description
3.1	Amended and Restated Certificate of Incorporation. Incorporated by reference to Form 10-Q filed for the quarter ended June, 30, 2006, file No. 001-08931, Exhibit 3.1.
3.2	Amended and Restated Bylaws. Incorporated by reference to Form 10-K filed for the fiscal year ended September 30, 2010, file No. 001-08931, Exhibit 3.2.
10.1*	Amended and Restated Deferred Compensation Plan dated January 1, 2013. Attached hereto as Exhibit 10.1.
31.1	Certification of Chief Executive Officer pursuant to Section 302 of the Sarbanes-Oxley

	Act of 2002.
31.2	Certification of Chief Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
32.1	Certification of Chief Executive Officer pursuant to 18 U.S.C. Section 1350
32.2	Certification of Chief Financial Officer pursuant to 18 U.S.C. Section 1350
101	Financial statements from the Cubic Corporation Quarterly Report on Form 10-Q for the quarter ended December 31, 2012, formatted in Extensible Business Reporting Language (XBRL): (i) Condensed Consolidated Statements of Income, (ii) Condensed Consolidated Statements of Comprehensive Income, (iii) Condensed Consolidated Balance Sheets, (iv) Condensed Consolidated Statements of Cash Flows, and (v) Notes to Condensed Consolidated Financial Statements.

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*
Indicates management contract or

compensatory plan or arrangement.

SIGNATURES

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

CUBIC CORPORATION

Date	February 11, 2013	/s/ John D. Thomas John D. Thomas Executive Vice President and Chief Financial Officer (Principal Financial Officer)
Date	February 11, 2013	/s/ Mark A. Harrison

Mark A. Harrison
Senior Vice President and Corporate Controller (Principal Accounting Officer)