

PALL CORP  
Form 10-Q  
June 02, 2014

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

FORM 10-Q

R Quarterly report pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934  
For the quarterly period ended April 30, 2014

or

o Transition report pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934  
For the transition period from to

Commission File Number: 001- 04311

PALL CORPORATION

(Exact name of registrant as specified in its charter)

New York  
(State or other jurisdiction of  
incorporation or organization)

11-1541330  
(I.R.S. Employer  
Identification No.)

25 Harbor Park Drive, Port Washington, NY  
(Address of principal executive offices)

11050  
(Zip Code)

(516) 484-5400  
(Registrant's telephone number, including area code)

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

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

Large accelerated filer  Accelerated filer

Non-accelerated filer  Smaller reporting company   
(Do not check if a smaller reporting  
company)

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

The number of shares of the registrant's common stock outstanding as of May 27, 2014 was 109,681,236.

Table of Contents

	Page No.
<u>PART I. FINANCIAL INFORMATION</u>	
<u>Item 1.</u> <u>Financial Statements (Unaudited).</u>	
<u>Condensed Consolidated Balance Sheets as of April 30, 2014 and July 31, 2013.</u>	<u>3</u>
<u>Condensed Consolidated Statements of Earnings for the three and nine months ended April 30, 2014 and April 30, 2013.</u>	<u>4</u>
<u>Condensed Consolidated Statements of Comprehensive Income for the three and nine months ended April 30, 2014 and April 30, 2013.</u>	<u>5</u>
<u>Condensed Consolidated Statements of Cash Flows for the nine months ended April 30, 2014 and April 30, 2013.</u>	<u>6</u>
<u>Notes to Condensed Consolidated Financial Statements.</u>	<u>7</u>
<u>Item 2.</u> <u>Management’s Discussion and Analysis of Financial Condition and Results of Operations.</u>	<u>27</u>
<u>Item 3.</u> <u>Quantitative and Qualitative Disclosures About Market Risk.</u>	<u>42</u>
<u>Item 4.</u> <u>Controls and Procedures.</u>	<u>42</u>
<u>PART II. OTHER INFORMATION</u>	
<u>Item 1.</u> <u>Legal Proceedings.</u>	<u>43</u>
<u>Item 1A.</u> <u>Risk Factors.</u>	<u>43</u>
<u>Item 2.</u> <u>Unregistered Sales of Equity Securities and Use of Proceeds.</u>	<u>44</u>
<u>Item 6.</u> <u>Exhibits.</u>	<u>44</u>
<u>SIGNATURES</u>	

## PART I. FINANCIAL INFORMATION

## ITEM 1. FINANCIAL STATEMENTS.

PALL CORPORATION AND SUBSIDIARIES  
CONDENSED CONSOLIDATED BALANCE SHEETS

(In thousands, except per share data)

(Unaudited)

	Apr 30, 2014	Jul 31, 2013
Assets:		
Current assets:		
Cash and cash equivalents	\$870,874	\$936,886
Accounts receivable	564,782	566,335
Inventory	428,648	381,047
Prepaid expenses	80,676	72,808
Other current assets	82,368	92,953
Total current assets	2,027,348	2,050,029
Property, plant and equipment	799,197	774,948
Goodwill	445,030	342,492
Intangible assets	211,586	137,243
Other non-current assets	163,104	168,127
Total assets	\$3,646,265	\$3,472,839
Liabilities and Stockholders' Equity:		
Current liabilities:		
Notes payable	\$304,959	\$169,967
Accounts payable	160,049	157,176
Accrued liabilities	307,930	312,829
Income taxes payable	57,009	60,732
Current portion of long-term debt	406	420
Dividends payable	30,159	27,947
Total current liabilities	860,512	729,071
Long-term debt, net of current portion	463,666	467,319
Income taxes payable – non-current	135,366	141,843
Deferred taxes and other non-current liabilities	365,551	319,650
Total liabilities	1,825,095	1,657,883
Stockholders' equity:		
Common stock, par value \$.10 per share	12,796	12,796
Capital in excess of par value	324,025	298,150
Retained earnings	2,424,552	2,285,031
Treasury stock, at cost	(950,506	) (740,229
Accumulated other comprehensive income/(loss):		
Foreign currency translation	130,928	84,598
Pension liability adjustment	(125,257	) (125,211
Unrealized investment gains	1,525	2,123
Unrealized gains/(losses) on derivatives	3,107	(2,302
Total accumulated other comprehensive income/(loss)	10,303	(40,792

Total stockholders' equity	1,821,170	1,814,956
Total liabilities and stockholders' equity	\$3,646,265	\$3,472,839

See accompanying notes to condensed consolidated financial statements.

PALL CORPORATION AND SUBSIDIARIES  
CONDENSED CONSOLIDATED STATEMENTS OF EARNINGS

(In thousands, except per share data)

(Unaudited)

	Three Months Ended		Nine Months Ended	
	Apr 30, 2014	Apr 30, 2013	Apr 30, 2014	Apr 30, 2013
Net sales	\$682,445	\$641,190	\$1,989,193	\$1,931,245
Cost of sales	334,371	307,111	971,146	928,120
Gross profit	348,074	334,079	1,018,047	1,003,125
Selling, general and administrative expenses	201,045	199,595	592,228	601,569
Research and development	26,644	22,608	74,890	68,582
Restructuring and other charges, net	11,542	12,824	29,910	21,497
Interest expense, net	4,747	5,298	15,919	10,747
Earnings from continuing operations before income taxes	104,096	93,754	305,100	300,730
Provision for income taxes	15,405	19,483	61,230	56,975
Net earnings from continuing operations	\$88,691	\$74,271	\$243,870	\$243,755
Earnings/(loss) from discontinued operations, net of income taxes	\$—	\$(1,206)	) \$—	\$245,552
Net earnings	\$88,691	\$73,065	\$243,870	\$489,307
Earnings per share from continuing operations:				
Basic	\$0.80	\$0.66	\$2.20	\$2.16
Diluted	\$0.80	\$0.65	\$2.17	\$2.13
Earnings/(loss) per share from discontinued operations:				
Basic	\$—	\$(0.01)	) \$—	\$2.17
Diluted	\$—	\$(0.01)	) \$—	\$2.15
Earnings per share:				
Basic	\$0.80	\$0.65	\$2.20	\$4.33
Diluted	\$0.80	\$0.64	\$2.17	\$4.28
Dividends declared per share	\$0.550	\$0.250	\$0.825	\$0.750
Average shares outstanding:				
Basic	110,183	111,964	110,946	112,979
Diluted	111,466	113,311	112,215	114,415

See accompanying notes to condensed consolidated financial statements.

PALL CORPORATION AND SUBSIDIARIES  
 CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME

(In thousands)

(Unaudited)

	Three Months Ended		Nine Months Ended	
	Apr 30, 2014	Apr 30, 2013	Apr 30, 2014	Apr 30, 2013
Net earnings	\$88,691	\$73,065	\$243,870	\$489,307
Other comprehensive income/(loss), net of income taxes:				
Foreign currency translation	25,041	(33,127 )	46,330	8,195
Pension liability adjustment	619	4,199	(46 )	8,762
Unrealized investment gains/(losses)	(224 )	(208 )	(598 )	(145 )
Unrealized gains/(losses) on derivatives	(172 )	1,548	5,409	(2,229 )
Total other comprehensive income/(loss), net of income taxes	25,264	(27,588 )	51,095	14,583
Comprehensive income	\$113,955	\$45,477	\$294,965	\$503,890

See accompanying notes to condensed consolidated financial statements.

PALL CORPORATION AND SUBSIDIARIES  
 CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

(In thousands)

(Unaudited)

	Nine Months Ended	
	Apr 30, 2014	Apr 30, 2013
Operating activities:		
Net cash provided by operating activities	\$342,164	\$206,890
Investing activities:		
Capital expenditures	(50,301	) (66,387
Acquisition of businesses, net of cash acquired	(195,262	) —
Purchases of retirement benefit assets	(29,518	) (33,503
Proceeds from retirement benefit assets	36,020	36,689
Proceeds from sale of assets	5,618	537,284
Other	(9,167	) (3,862
Net cash provided/(used) by investing activities	(242,610	) 470,221
Financing activities:		
Notes payable	134,992	10,020
Dividends paid	(88,596	) (80,197
Long-term borrowings	—	14
Repayments of short-term debt	(3,927	) —
Repayments of long-term debt	(545	) (352
Net proceeds from stock plans	13,814	31,054
Additions to deferred financing costs	—	(3,043
Purchase of treasury stock	(250,000	) (250,000
Excess tax benefits from stock-based compensation arrangements	11,327	11,774
Net cash used by financing activities	(182,935	) (280,730
Cash flow for period	(83,381	) 396,381
Cash and cash equivalents at beginning of year	936,886	500,274
Effect of exchange rate changes on cash and cash equivalents	17,369	7,312
Cash and cash equivalents at end of period	\$870,874	\$903,967
Supplemental disclosures:		
Interest paid	\$13,068	\$23,780
Income taxes paid (net of refunds)	44,782	133,417

See accompanying notes to condensed consolidated financial statements.

PALL CORPORATION AND SUBSIDIARIES  
 NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(In thousands, except per share data)  
 (Unaudited)

NOTE 1 – BASIS OF PRESENTATION

The condensed consolidated financial information of Pall Corporation and its subsidiaries (hereinafter collectively called the “Company”) included herein is unaudited. Such information reflects all adjustments of a normal recurring nature, which are, in the opinion of Company management, necessary to present fairly the Company’s consolidated financial position, results of operations and cash flows as of the dates and for the periods presented herein. These condensed consolidated financial statements should be read in conjunction with the consolidated financial statements and notes set forth in the Company’s Annual Report on Form 10-K for the fiscal year ended July 31, 2013 (“2013 Form 10-K”).

As discussed in Note 16, Discontinued Operations, on August 1, 2012, the Company sold certain assets of its blood collection, filtration and processing product line, which was a component of the Company’s Life Sciences segment, and met the criteria for discontinued operations and held for sale presentation during the third quarter of fiscal year 2012. As such, it has been reported as a discontinued operation in the Company’s condensed consolidated financial statements for all periods presented.

NOTE 2 – BALANCE SHEET DETAILS

The following tables provide details of selected balance sheet items:

	Apr 30, 2014	Jul 31, 2013
Accounts receivable:		
Billed	\$513,137	\$508,448
Unbilled	65,661	72,787
Total	578,798	581,235
Less: Allowances for doubtful accounts	(14,016 )	(14,900 )
	\$564,782	\$566,335

Unbilled receivables principally relate to revenues accrued for long-term contracts recorded under the percentage-of-completion method of accounting.

	Apr 30, 2014	Jul 31, 2013
Inventory:		
Raw materials and components	\$124,837	\$94,837
Work-in-process	109,028	94,998
Finished goods	194,783	191,212
	\$428,648	\$381,047
	Apr 30, 2014	July 31, 2013
Property, plant and equipment:		
Property, plant and equipment	\$1,757,331	\$1,650,274
Less: Accumulated depreciation and amortization	(958,134 )	(875,326 )
	\$799,197	\$774,948

## PALL CORPORATION AND SUBSIDIARIES

## NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(In thousands, except per share data)

(Unaudited)

## NOTE 3 – GOODWILL AND INTANGIBLE ASSETS

The Company completed its annual goodwill impairment test for all reporting units in the third quarter of fiscal year 2014 and determined that no impairment existed. In addition, the Company had no impairment of goodwill in the prior year. In connection with the annual goodwill impairment test, the Company estimates the fair value of its reporting units using a market approach employing Level 3 inputs as defined in the fair value hierarchy described in Note 11, Fair Value Measurements.

The following table presents changes in the carrying value of goodwill, allocated by reportable segment.

	Life Sciences	Industrial	Total
Balance as of July 31, 2013	\$ 180,896	\$ 161,596	\$ 342,492
Acquisitions	99,744	—	99,744
Foreign currency translation	1,818	976	2,794
Balance as of April 30, 2014	\$ 282,458	\$ 162,572	\$ 445,030

In connection with the acquisitions in the first nine months of fiscal year 2014, see Note 17, Acquisitions, the Company recorded the fair value of the intangible assets acquired, which were valued using the income approach. The valuation employed level 3 inputs, as defined in the fair value hierarchy.

Intangible assets consist of the following:

	Apr 30, 2014		
	Gross	Accumulated Amortization	Net
Patents and unpatented technology	\$ 166,112	\$ 64,522	\$ 101,590
Customer-related intangibles	129,777	30,480	99,297
Trademarks	16,412	6,835	9,577
Other	3,674	2,552	1,122
	\$ 315,975	\$ 104,389	\$ 211,586
	Jul 31, 2013		
	Gross	Accumulated Amortization	Net
Patents and unpatented technology	\$ 123,707	\$ 69,992	\$ 53,715
Customer-related intangibles	97,016	22,425	74,591
Trademarks	13,291	6,166	7,125
Other	4,425	2,613	1,812
	\$ 238,439	\$ 101,196	\$ 137,243

Amortization expense from continuing operations for intangible assets for the three and nine months ended April 30, 2014 was \$5,399 and \$14,778, respectively. Amortization expense from continuing operations for intangible assets for the three and nine months ended April 30, 2013 was \$4,765 and \$14,900, respectively. Amortization expense is estimated to be approximately \$5,699 for the remainder of fiscal year 2014, \$21,202 in fiscal year 2015, \$19,920 in fiscal year 2016, \$19,841 in fiscal year 2017, \$19,670 in fiscal year 2018, and \$17,316 in fiscal year 2019.

## PALL CORPORATION AND SUBSIDIARIES

## NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(In thousands, except per share data)

(Unaudited)

## NOTE 4 – TREASURY STOCK

The following table highlights the share repurchase authorizations in effect during fiscal year 2014:

	Date of Authorization		
	Sep 26, 2011	Jan 17, 2013	Total
Amount available for repurchases as of July 31, 2013	\$81,873	\$250,000	\$331,873
New authorizations	—	—	—
Utilized	(81,873 )	(168,127 )	(250,000 )
Amount available for repurchases as of April 30, 2014	\$—	\$81,873	\$81,873

The Company's shares may be purchased over time as market and business conditions warrant. There is no time restriction on these authorizations. In September 2013, the Company entered into an Accelerated Share Repurchase ("ASR") agreement with a third-party financial institution to repurchase \$125,000 of the Company's common stock. This transaction was completed in the second quarter of fiscal year 2014. Under the agreement, the Company paid \$125,000 to the financial institution. Upon completion of the transaction, the Company received a total of 1,573 shares with an average price per share of \$79.45.

In December 2013, the Company entered into a second ASR agreement with a third-party financial institution to repurchase \$125,000 of the Company's common stock. This transaction was completed in the third quarter of fiscal year 2014. Under the agreement, the Company paid \$125,000 to the financial institution. Upon completion of the transaction, the Company received a total of 1,483 shares with an average price per share of \$84.31.

During the nine months ended April 30, 2014, 935 shares were issued under the Company's stock-based compensation plans. At April 30, 2014, the Company held 18,291 treasury shares.

## NOTE 5 – CONTINGENCIES AND COMMITMENTS

With respect to the matters described in Note 14, Contingencies and Commitments, to the Company's consolidated financial statements included in the Company's 2013 Form 10-K and below, the Company has assessed the ultimate resolution of these matters and has reflected appropriate contingent liabilities in the condensed consolidated financial statements as of April 30, 2014 and July 31, 2013.

The Company and its subsidiaries are subject to certain other legal actions that arise in the normal course of business. Other than those legal proceedings and claims discussed in the 2013 Form 10-K and this Note, the Company is not facing any other legal proceedings and claims that would individually or in the aggregate have a reasonably possible material adverse effect on its financial condition or operating results. As such, any reasonably possible loss or range of loss, other than those legal proceedings discussed in the 2013 Form 10-K and this Note, is immaterial. However, the results of legal proceedings cannot be predicted with certainty. If the Company failed to prevail in several of these legal matters in the same reporting period, the operating results of a particular reporting period could be materially adversely affected.

## Environmental Matters:

With respect to the environmental matters at the Company's Pinellas Park, Florida site, previously disclosed in Note 14, Contingencies and Commitments, to the Company's consolidated financial statements included in the Company's 2013 Form 10-K, the Florida Department of Environmental Protection approved the remedial action plan in September 2013. As a result of this, the Company added \$4,440 to its environmental reserves in the first quarter of fiscal year 2014.

The Company's condensed consolidated balance sheet at April 30, 2014 includes liabilities for environmental matters of approximately \$20,738 which relate primarily to the environmental proceedings discussed in the 2013 Form 10-K and as updated in this Note. In the opinion of management, the Company is in substantial compliance with applicable environmental laws and its current accruals for environmental remediation are adequate. However, as regulatory standards under environmental laws are becoming increasingly stringent, there can be no assurance that future

developments, additional information and experience gained will not cause the Company to incur material environmental liabilities or costs beyond those accrued in its condensed consolidated financial statements.

## PALL CORPORATION AND SUBSIDIARIES

## NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(In thousands, except per share data)

(Unaudited)

## NOTE 6 – RESTRUCTURING AND OTHER CHARGES, NET

The following tables summarize the restructuring and other charges (“ROTC”) recorded in the three and nine months ended April 30, 2014 and April 30, 2013:

	Three Months Ended Apr 30, 2014			Nine Months Ended Apr 30, 2014		
	Restructuring (1)	Other (Gains)/ Charges (2)	Total	Restructuring (1)	Other (Gains)/ Charges (2)	Total
Severance benefits and other employment contract obligations	\$8,289	\$—	\$8,289	\$18,751	\$(402)	\$18,349
Professional fees and other costs, net of receipt of insurance claim payments	567	1,498	2,065	2,704	3,693	6,397
(Gain)/loss on sale and impairment of assets, net	3,986	(1,640)	2,346	3,986	(1,480)	2,506
Environmental matters	—	—	—	—	4,440	4,440
Reversal of excess restructuring reserves	(1,158)	—	(1,158)	(1,782)	—	(1,782)
	\$11,684	\$(142)	\$11,542	\$23,659	\$6,251	\$29,910
Cash	\$7,698	\$(142)	\$7,556	\$19,673	\$6,091	\$25,764
Non-cash	3,986	—	3,986	3,986	160	4,146
	\$11,684	\$(142)	\$11,542	\$23,659	\$6,251	\$29,910
	Three Months Ended Apr 30, 2013			Nine Months Ended Apr 30, 2013		
	Restructuring (1)	Other (Gains)/ Charges (2)	Total	Restructuring (1)	Other (Gains)/ Charges (2)	Total
Severance benefits and other employment contract obligations	\$5,701	\$1,452	\$7,153	\$10,896	\$2,903	\$13,799
Professional fees and other costs, net of receipt of insurance claim payments	361	531	892	1,149	2,117	3,266
(Gain)/loss on sale and impairment of assets, net	999	1,357	2,356	993	1,357	2,350
Environmental matters	—	2,715	2,715	—	2,715	2,715
Reversal of excess restructuring reserves	(292)	—	(292)	(633)	—	(633)
	\$6,769	\$6,055	\$12,824	\$12,405	\$9,092	\$21,497
Cash	\$5,770	\$4,185	\$9,955	\$11,007	\$6,709	\$17,716
Non-cash	999	1,870	2,869	1,398	2,383	3,781
	\$6,769	\$6,055	\$12,824	\$12,405	\$9,092	\$21,497



PALL CORPORATION AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(In thousands, except per share data)

(Unaudited)

(1) Restructuring:

In fiscal year 2012, the Company announced a multi-year strategic cost reduction initiative (“structural cost improvement initiative”). This initiative impacts both segments as well as the Corporate Services Group. The goal of this initiative is to properly position the Company’s cost structure globally to perform in the current economic environment without adversely impacting its growth or innovation potential.

Key components of the structural cost improvement initiative include:

• the strategic alignment of manufacturing, sales and R&D facilities to cost-effectively deliver high-quality products and superior service to the Company’s customers worldwide,

• creation of regional shared financial services centers for the handling of accounting transaction processing and other accounting functions,

• reorganization of sales functions, to more cost-efficiently deliver superior service to the Company’s customers globally, and

• reductions in headcount across all functional areas, enabled by efficiencies gained through the Company’s ERP systems, as well as in order to align to economic conditions.

Restructuring charges recorded in the three and nine months ended April 30, 2014 and April 30, 2013 primarily reflect the expenses incurred in connection with the Company’s structural cost improvement initiative as discussed above.

Restructuring charges in the three and nine months ended April 30, 2014 also includes the impairment of assets of \$3,986 related to the discontinuance of a specific manufacturing line due to excess capacity as a result of recent acquisitions.

(2) Other (Gains)/Charges:

Severance benefits and other employment contract obligations: In the three and nine months ended April 30, 2013, the Company recorded charges related to certain employment contract obligations.

Professional fees and other: In the three months ended April 30, 2014, the Company recorded costs related to the settlement of a legal matter. Furthermore, in the three and nine months ended April 30, 2014, the Company recorded acquisition related legal and other professional fees. In the three and nine months ended April 30, 2013, the Company recorded settlement related costs as well as legal and other professional fees, related to the Federal Securities Class Actions, Shareholder Derivative Lawsuits and Other Proceedings (see Note 14, Contingencies and Commitments, in the 2013 Form 10-K).

Gain on sale and impairment of assets: In the three months ended April 30, 2014, the Company recorded a gain on the sale of a building in Europe. In the three months ended April 30, 2013, the Company recorded an impairment related to a software project.

Environmental matters: As discussed in Note 5, Contingencies and Commitments, in the nine months ended April 30, 2014, the Company increased its previously established environmental reserve related to a matter in Pinellas Park, Florida. In the three months ended April 30, 2013, the Company increased its previously established environmental reserve related to a matter in Glen Cove, New York.

## PALL CORPORATION AND SUBSIDIARIES

## NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(In thousands, except per share data)

(Unaudited)

The following table summarizes the activity related to restructuring liabilities recorded for the Company's structural cost improvement initiative which began in fiscal year 2012:

	Severance	Other	Total
Original charge	\$61,852	\$3,448	\$65,300
Utilized	(27,365)	(2,798)	(30,163)
Translation	(123)	(47)	(170)
Balance at Jul 31, 2012	\$34,364	\$603	\$34,967
Additions	21,637	2,840	24,477
Utilized	(29,574)	(1,936)	(31,510)
Reversal of excess reserves	(500)	(57)	(557)
Translation	313	23	336
Balance at Jul 31, 2013	\$26,240	\$1,473	\$27,713
Additions	18,751	2,704	21,455
Utilized	(18,996)	(2,533)	(21,529)
Reversal of excess reserves	(1,682)	(100)	(1,782)
Translation	628	63	691
Balance at Apr 30, 2014	\$24,941	\$1,607	\$26,548

Excluded from the table above are restructuring liabilities relating to restructuring plans initiated in fiscal year 2010. At April 30, 2014, the balance of these liabilities was \$213.

## NOTE 7 – INCOME TAXES

The Company's effective tax rates on continuing operations for the nine months ended April 30, 2014 and April 30, 2013 were 20.1% and 18.9%, respectively. For the nine months ended April 30, 2014, the effective tax rate varied from the U.S. federal statutory rate primarily due to the benefits of foreign operations and a net tax benefit of \$10,054 from the resolution of tax audits. For the nine months ended April 30, 2013, the effective tax rate varied from the U.S. federal statutory rate primarily due to the benefits of foreign operations and a net tax benefit of \$7,757 primarily from the resolution of a U.S. tax audit partly offset by the establishment of deferred tax liabilities for the repatriation of foreign earnings.

During the nine months ended April 30, 2014, the Company reached a final settlement with Her Majesty's Revenue and Customs ("HMRC") in the United Kingdom resolving the outstanding tax positions for fiscal years ended July 2010 and July 2011. As a result, the Company reversed \$10,961 of previously recorded liabilities related to tax and penalties, as well as \$1,478 related to interest (\$1,138 net of income tax cost) that were accrued but not assessed as part of the settlement.

During the nine months ended April 30, 2013, the Company reached a final agreement with the Internal Revenue Service ("IRS") resolving the outstanding tax positions for fiscal years ended 2006 through 2008. As a result, the Company reversed \$10,193 of previously recorded liabilities related to tax and penalties, as well as \$6,704 related to interest (\$4,268 net of income tax cost) that were accrued but not assessed as part of the IRS agreement.

At April 30, 2014 and July 31, 2013, the Company had gross unrecognized income tax benefits of \$198,899 and \$203,376, respectively. During the nine months ended April 30, 2014, the amount of gross unrecognized tax benefits decreased by \$4,477, primarily due to the settlement with HMRC for fiscal years ended July 2010 and July 2011 and the expiration of various foreign statutes of limitation, partially offset by tax positions taken during the current period and the impact of foreign currency translation. As of April 30, 2014, the amount of net unrecognized income tax benefits that, if recognized, would impact the effective tax rate was \$155,469.

At April 30, 2014 and July 31, 2013, the Company had liabilities of \$17,450 and \$18,622, respectively, for potential payment of interest and penalties.



## PALL CORPORATION AND SUBSIDIARIES

## NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(In thousands, except per share data)

(Unaudited)

Due to the potential resolution of tax examinations and the expiration of various statutes of limitation, the Company believes that it is reasonably possible that the gross amount of unrecognized tax benefits may decrease within the next twelve months by a range of zero to \$55,781.

Subsequent to the balance sheet date, the Company received official notification of the resolution of a tax audit in Germany related to fiscal years 2005 through 2008. This will result in the recognition of previously unrecognized income tax benefits of approximately \$7,000 and a reversal of interest of approximately \$3,000 in the Company's fourth fiscal quarter ending July 31, 2014.

## NOTE 8 – COMPONENTS OF NET PERIODIC PENSION COST

Net periodic pension benefit cost for the Company's defined benefit pension plans includes the following components:

	Three Months Ended					
	U.S. Plans		Foreign Plans		Total	
	Apr 30, 2014	Apr 30, 2013	Apr 30, 2014	Apr 30, 2013	Apr 30, 2014	Apr 30, 2013
Service cost	\$2,169	\$2,648	\$1,005	\$1,093	\$3,174	\$3,741
Interest cost	3,028	2,617	4,398	3,899	7,426	6,516
Expected return on plan assets	(2,325 )	(2,383 )	(3,611 )	(3,937 )	(5,936 )	(6,320 )
Amortization of prior service cost/(credit)	395	392	(10 )	(12 )	385	380
Amortization of actuarial loss	1,344	2,411	1,450	1,358	2,794	3,769
Loss due to curtailments and settlements	—	16	—	—	—	16
Net periodic benefit cost	\$4,611	\$5,701	\$3,232	\$2,401	\$7,843	\$8,102
	Nine Months Ended					
	U.S. Plans		Foreign Plans		Total	
	Apr 30, 2014	Apr 30, 2013	Apr 30, 2014	Apr 30, 2013	Apr 30, 2014	Apr 30, 2013
Service cost	\$6,509	\$7,943	\$2,998	\$3,443	\$9,507	\$11,386
Interest cost	9,083	7,852	12,923	11,965	22,006	19,817
Expected return on plan assets	(6,974 )	(7,150 )	(10,591 )	(12,158 )	(17,565 )	(19,308 )
Amortization of prior service cost/(credit)	1,185	1,178	(31 )	(44 )	1,154	1,134
Amortization of actuarial loss	4,033	7,233	4,261	4,170	8,294	11,403
Loss due to curtailments and settlements	—	49	—	—	—	49
Net periodic benefit cost	\$13,836	\$17,105	\$9,560	\$7,376	\$23,396	\$24,481

## PALL CORPORATION AND SUBSIDIARIES

## NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(In thousands, except per share data)

(Unaudited)

## NOTE 9 – STOCK-BASED PAYMENT

The Company currently has four stock-based employee and director compensation award types (Restricted Stock Unit, Stock Option Plans, Management Stock Purchase Plan (“MSPP”), and Employee Stock Purchase Plan (“ESPP”)), which are more fully described in Note 15, Common Stock, to the consolidated financial statements included in the 2013 Form 10-K.

The detailed components of stock-based compensation expense recorded in the condensed consolidated statements of earnings for the three and nine months ended April 30, 2014 and April 30, 2013 are reflected in the table below:

	Three Months Ended		Nine Months Ended	
	Apr 30, 2014	Apr 30, 2013	Apr 30, 2014	Apr 30, 2013
Restricted stock units	\$5,064	\$3,978	\$15,511	\$11,895
Stock options	2,069	1,825	5,555	4,503
MSPP	961	976	2,125	2,763
ESPP	273	302	771	992
Total	\$8,367	\$7,081	\$23,962	\$20,153

## NOTE 10 – EARNINGS PER SHARE

The condensed consolidated statements of earnings present basic and diluted earnings per share. Basic earnings per share is determined by dividing income available to common shareholders by the weighted average number of common shares outstanding for the period. Diluted earnings per share considers the potential effect of dilution on basic earnings per share assuming potentially dilutive shares that meet certain criteria, such as those issuable upon exercise of stock options, were outstanding. The treasury stock method reduces the dilutive effect of potentially dilutive securities as it assumes that any cash proceeds (from the issuance of potentially dilutive securities) are used to buy back shares at the average share price during the period. Equity awards aggregating 496 and 742 shares were not included in the computation of diluted shares for the three months ended April 30, 2014 and April 30, 2013, respectively, because their effect would have been antidilutive. For the nine months ended April 30, 2014 and April 30, 2013, 524 and 586 antidilutive shares, respectively, were excluded. The following is a reconciliation between basic shares outstanding and diluted shares outstanding:

	Three Months Ended		Nine Months Ended	
	Apr 30, 2014	Apr 30, 2013	Apr 30, 2014	Apr 30, 2013
Basic shares outstanding	110,183	111,964	110,946	112,979
Effect of stock plans	1,283	1,347	1,269	1,436
Diluted shares outstanding	111,466	113,311	112,215	114,415

## PALL CORPORATION AND SUBSIDIARIES

## NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(In thousands, except per share data)

(Unaudited)

## NOTE 11 – FAIR VALUE MEASUREMENTS

The Company records certain of its financial assets and liabilities at fair value, which is the price that would be received to sell an asset or paid to transfer a liability in the principal or most advantageous market for the asset or liability in an orderly transaction between market participants at the measurement date.

The current authoritative guidance discusses valuation techniques, such as the market approach (comparable market prices), the income approach (present value of future income or cash flow), and the cost approach (cost to replace the service capacity of an asset or replacement cost). Authoritative guidance utilizes a fair value hierarchy that prioritizes the inputs to valuation techniques used to measure fair value into three broad levels. The following is a brief description of those three levels:

Level 1: Use of observable inputs such as quoted prices (unadjusted) in active markets for identical assets or liabilities.

Level 2: Use of inputs other than quoted prices included in Level 1, which are observable for the asset or liability, either directly or indirectly. These include quoted prices for similar assets or liabilities in active markets, quoted prices for identical or similar assets or liabilities in markets that are not active, or other inputs that are observable or can be corroborated by observable market data.

Level 3: Use of inputs that are unobservable.

The following table presents, for each of these hierarchy levels, the Company's financial assets and liabilities that are measured at fair value on a recurring basis as of April 30, 2014:

	Fair Value Measurements			
	As of Apr 30, 2014	Level 1	Level 2	Level 3
Financial assets carried at fair value				
Money market funds	\$3,948	\$3,948	\$—	\$—
Available-for-sale securities:				
Equity securities	4,524	4,524	—	—
Debt securities:				
Corporate	30,359	—	30,359	—
U.S. Treasury	10,416	—	10,416	—
Federal agency	16,374	—	16,374	—
Mortgage-backed	9,544	—	9,544	—
Trading securities	788	788	—	—
Derivative financial instruments:				
Foreign exchange forward contracts	3,555	—	3,555	—
Financial liabilities carried at fair value				
Derivative financial instruments:				
Foreign exchange forward contracts	689	—	689	—

## PALL CORPORATION AND SUBSIDIARIES

## NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(In thousands, except per share data)

(Unaudited)

The following table presents, for each of these hierarchy levels, the Company's financial assets and liabilities that are measured at fair value on a recurring basis as of July 31, 2013:

	Fair Value Measurements			
	As of Jul 31, 2013	Level 1	Level 2	Level 3
Financial assets carried at fair value				
Money market funds	\$6,404	\$6,404	\$—	\$—
Available-for-sale securities:				
Equity securities	176	176	—	—
Debt securities:				
Corporate	32,393	—	32,393	—
U.S. Treasury	11,543	—	11,543	—
Federal agency	20,642	—	20,642	—
Mortgage-backed	5,990	—	5,990	—
Trading securities	190	190	—	—
Derivative financial instruments:				
Foreign exchange forward contracts	301	—	301	—
Financial liabilities carried at fair value				
Derivative financial instruments:				
Foreign exchange forward contracts	3,066	—	3,066	—

The Company's money market funds and equity securities are valued using quoted market prices and, as such, are classified within Level 1 of the fair value hierarchy.

The fair value of the Company's investments in debt securities are valued utilizing third party pricing services and verified by management. The pricing services use inputs to determine fair value which are derived from observable market sources including reportable trades, benchmark curves, credit spreads, broker/dealer quotes, bids, offers, and other industry and economic events. These investments are included in Level 2 of the fair value hierarchy.

The fair values of the Company's foreign currency forward contracts are valued using pricing models, with all significant inputs derived from or corroborated by observable market data such as yield curves, currency spot and forward rates, and currency volatilities. These investments are included in Level 2 of the fair value hierarchy.

## PALL CORPORATION AND SUBSIDIARIES

## NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(In thousands, except per share data)

(Unaudited)

## NOTE 12 – INVESTMENT SECURITIES

The following is a summary of the Company's available-for-sale investment securities by category which are classified within other non-current assets in the Company's condensed consolidated balance sheets. Contractual maturity dates of debt securities held by the benefits protection trusts at April 30, 2014 range from 2014 to 2046.

	Cost/ Amortized Cost Basis	Fair Value	Gross Unrealized Holding Gains	Gross Unrealized Holding Losses	Net Unrealized Holding Gains/(Losses)
April 30, 2014					
Equity securities	\$5,029	\$4,524	\$5	\$(510)	\$(505)
Debt securities:					
Corporate	29,435	30,359	1,172	(248)	924
U.S. Treasury	10,310	10,416	215	(109)	106
Federal agency	16,075	16,374	878	(579)	299
Mortgage-backed	9,366	9,544	189	(11)	178
	\$70,215	\$71,217	\$2,459	\$(1,457)	\$1,002
July 31, 2013					
Equity securities	\$176	\$176	\$—	\$—	\$—
Debt securities:					
Corporate	31,546	32,393	1,274	(427)	847
U.S. Treasury	11,339	11,543	294	(90)	204
Federal agency	19,810	20,642	1,131	(299)	832
Mortgage-backed	5,752	5,990	238	—	238
	\$68,623	\$70,744	\$2,937	\$(816)	\$2,121

## PALL CORPORATION AND SUBSIDIARIES

## NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(In thousands, except per share data)

(Unaudited)

The following table shows the gross unrealized losses and fair value of the Company's available-for-sale investments with unrealized losses aggregated by investment category and length of time that individual securities have been in a continuous unrealized loss position:

	Less than 12 months		12 months or greater		Total	Gross Unrealized Holding Losses
	Fair Value	Gross Unrealized Holding Losses	Fair Value	Gross Unrealized Holding Losses	Fair Value	
April 30, 2014						
Debt securities:						
Corporate	\$8,865	\$(248)	\$—	\$—	\$8,865	\$(248)
U.S. Treasury	4,372	(109)	—	—	4,372	(109)
Federal agency	1,634	(63)	1,598	(516)	3,232	(579)
Mortgage-backed	1,109	(11)	—	—	1,109	(11)
Equity securities	4,326	(510)	—	—	4,326	(510)
	\$20,306	\$(941)	\$1,598	\$(516)	\$21,904	\$(1,457)
	Less than 12 months		12 months or greater		Total	
	Fair Value	Gross Unrealized Holding Losses	Fair Value	Gross Unrealized Holding Losses	Fair Value	Gross Unrealized Holding Losses
July 31, 2013						
Debt securities:						
Corporate	\$10,990	\$(427)	\$—	\$—	\$10,990	\$(427)
U.S. Treasury	3,778	(90)	—	—	3,778	(90)
Federal agency	3,701	(299)	—	—	3,701	(299)
	\$18,469	\$(816)	\$—	\$—	\$18,469	\$(816)

The following table shows the proceeds and gross gains and losses from the sale of available-for-sale investments for the three and nine months ended April 30, 2014 and April 30, 2013:

	Three Months Ended		Nine Months Ended	
	Apr 30, 2014	Apr 30, 2013	Apr 30, 2014	Apr 30, 2013
Proceeds from sales	\$4,915	\$883	\$7,973	\$13,169
Realized gross gains on sales	93	18	177	370
Realized gross losses on sales	6	—	106	5

The following is a summary of the Company's trading securities by category which are classified within other non-current assets in the Company's condensed consolidated balance sheets.

	Apr 30, 2014	Jul 31, 2013
Equity securities	\$788	\$190
Total trading securities	\$788	\$190

## PALL CORPORATION AND SUBSIDIARIES

## NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(In thousands, except per share data)

(Unaudited)

The following table shows the net gains and losses recognized on trading securities for the three and nine months ended April 30, 2014 and April 30, 2013:

	Three Months Ended		Nine Months Ended	
	Apr 30, 2014	Apr 30, 2013	Apr 30, 2014	Apr 30, 2013
Gains/(losses), net recognized for securities held	\$(1 )	\$—	\$22	\$—
Gains/(losses), net recognized for securities sold	—	—	—	—
Total gains/(losses), net recognized	\$(1 )	\$—	\$22	\$—

## NOTE 13 – DERIVATIVE INSTRUMENTS AND HEDGING ACTIVITIES

The Company manages certain financial exposures through a risk management program that includes the use of foreign exchange derivative financial instruments. Derivatives are executed with counterparties with a minimum credit rating of “A” by Standard & Poors and “A2” by Moody’s Investor Services, in accordance with the Company’s policies. The Company does not utilize derivative instruments for trading or speculative purposes. As of April 30, 2014, the Company had foreign currency forward contracts outstanding with notional amounts aggregating \$512,733, whose fair values were a net asset of \$2,866.

## Foreign Exchange Related:

## a. Derivatives Not Designated as Hedging Instruments

The risk management objective of holding foreign exchange derivatives is to mitigate volatility to earnings and cash flows due to changes in foreign exchange rates. The Company and its subsidiaries conduct transactions in currencies other than their functional currencies. These transactions include non-functional intercompany and external sales as well as intercompany and external purchases. The Company uses foreign exchange forward contracts, matching the notional amounts and durations of the receivables and payables resulting from the aforementioned underlying foreign currency transactions, to mitigate the exposure to earnings and cash flows caused by the changes in fair value of these receivables and payables from fluctuating foreign exchange rates. The notional amount of foreign currency forward contracts not designated as hedging instruments entered into during the three and nine months ended April 30, 2014 was \$664,039 and \$1,845,481, respectively. The notional amount of foreign currency forward contracts outstanding that were not designated as hedging instruments as of April 30, 2014 was \$406,572.

## b. Cash Flow Hedges

The Company uses foreign exchange forward contracts for cash flow hedging on its future transactional exposure to the Euro due to changes in market rates to exchange Euros for British Pounds. The hedges cover a British subsidiary (British Pound functional) with Euro revenues and a Swiss subsidiary (Euro functional) with British Pound expenses. The probability of the occurrence of these transactions is high and the Company’s assessment is based on observable facts including the frequency and amounts of similar past transactions. The objective of the cash flow hedges is to lock a portion of the British Pound equivalent amount of Euro sales for the British subsidiary and a portion of the Euro equivalent amount of British Pound expenses for the Swiss subsidiary at the agreed upon exchange rates in the foreign exchange forward contracts. The notional amount of foreign currency forward contracts designated as hedging instruments entered into during the three and nine months ended April 30, 2014 was \$23,174 and \$77,941. The notional amount of foreign currency forward contracts outstanding designated as hedging instruments as of April 30, 2014 was \$106,161 and covers certain monthly transactional exposures through May 2015.

## c. Net Investment Hedges

The risk management objective of designating the Company’s foreign currency loan as a hedge of a portion of its net investment in a wholly owned Japanese subsidiary is to mitigate the change in the fair value of the Company’s net investment due to changes in foreign exchange rates. The Company uses a JPY loan outstanding to hedge its equity of the same amount in the Japanese wholly owned subsidiary. The hedge of net investment consists of a JPY 9 billion loan.



PALL CORPORATION AND SUBSIDIARIES  
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)  
(In thousands, except per share data)  
(Unaudited)

The fair values of the Company's derivative financial instruments included in the condensed consolidated balance sheets are presented as follows:

April 30, 2014	Asset Derivatives Balance Sheet Location	Fair Value	Liability Derivatives Balance Sheet Location	Fair Value
Derivatives designated as hedging instruments				
Foreign exchange forward contracts	Other current assets	\$2,895	Other current liabilities	\$7
Derivatives not designated as hedging instruments				
Foreign exchange forward contracts	Other current assets	\$660	Other current liabilities	\$682
Total derivatives		\$3,555		\$689
Nonderivative instruments designated as hedging instruments				
Net investment hedge			Long-term debt, net of current portion	\$87,687
July 31, 2013	Asset Derivatives Balance Sheet Location	Fair Value	Liability Derivatives Balance Sheet Location	Fair Value
Derivatives designated as hedging instruments				
Foreign exchange forward contracts	Other current assets	\$—	Other current liabilities	\$1,941
Derivatives not designated as hedging instruments				
Foreign exchange forward contracts	Other current assets	\$301	Other current liabilities	\$1,125
Total derivatives		\$301		\$3,066
Nonderivative instruments designated as hedging instruments				
Net investment hedge			Long-term debt, net of current portion	\$91,800

## PALL CORPORATION AND SUBSIDIARIES

## NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(In thousands, except per share data)

(Unaudited)

The amounts of the gains and losses related to the Company's derivative financial instruments designated as hedging instruments for the three and nine months ended April 30, 2014 and April 30, 2013 are presented as follows:

	Amount of Gain or (Loss) Recognized in OCI on Derivatives (Effective Portion)		Location of Gain or (Loss) Reclassified from Accumulated OCI into Earnings (Effective Portion)	Amount of Gain or (Loss) Reclassified from Accumulated OCI into Earnings (Effective Portion) <sup>(a)</sup>	
				Three Months Ended Apr 30, 2014	Three Months Ended Apr 30, 2013
Derivatives in cash flow hedging relationships					
Foreign exchange forward contracts	\$305	\$1,548	Net sales	\$440	\$(615 )
			Cost of sales	171	(537 )
Total derivatives	\$305	\$1,548		\$611	\$(1,152 )

	Amount of Gain or (Loss) Recognized in OCI on Derivatives (Effective Portion)		Location of Gain or (Loss) Reclassified from Accumulated OCI into Earnings (Effective Portion)	Amount of Gain or (Loss) Reclassified from Accumulated OCI into Earnings (Effective Portion) <sup>(a)</sup>	
				Nine Months Ended Apr 30, 2014	Nine Months Ended Apr 30, 2013
Derivatives in cash flow hedging relationships					
Foreign exchange forward contracts	\$5,615	\$(2,229 )	Net sales	\$552	\$(1,002 )
			Cost of sales	(695 )	(707 )
Total derivatives	\$5,615	\$(2,229 )		\$(143 )	\$(1,709 )

There were no gains or losses recognized in earnings related to the ineffective portion of the hedging relationship (a) or related to the amount excluded from the assessment of hedge effectiveness for the three and nine months ended April 30, 2014 and April 30, 2013.

The amounts of the gains and losses related to the Company's derivative financial instruments not designated as hedging instruments for the three and nine months ended April 30, 2014 and April 30, 2013 are presented as follows:

	Location of Gain or (Loss) Recognized in Earnings on Derivatives	Amount of Gain or (Loss) Recognized in Earnings on Derivatives			
		Three Months Ended		Nine Months Ended	
		Apr 30, 2014	Apr 30, 2013	Apr 30, 2014	Apr 30, 2013
Derivatives not designated as hedging relationships					
Foreign exchange forward contracts	Selling, general and administrative expenses	\$(607 )	\$(5,206 )	\$(2,950 )	\$(15,032 )



## PALL CORPORATION AND SUBSIDIARIES

## NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(In thousands, except per share data)

(Unaudited)

The amounts of the gains and losses related to the Company's nonderivative financial instruments designated as hedging instruments for the three and nine months ended April 30, 2014 and April 30, 2013 are presented as follows:

	Amount of Gain or (Loss) Recognized in OCI on Derivatives (Effective Portion)		Location of Gain or (Loss) Reclassified from Accumulated OCI into Earnings (Effective Portion)	Amount of Gain or (Loss) Reclassified from Accumulated OCI into Earnings (Effective Portion) <sup>(b)</sup>	
	Three Months Ended Apr 30, 2014	Apr 30, 2013		Three Months Ended Apr 30, 2014	Apr 30, 2013
Nonderivatives designated as hedging relationships					
Net investment hedge	\$63	\$4,320	N/A	\$—	\$—
	Amount of Gain or (Loss) Recognized in OCI on Derivatives (Effective Portion)		Location of Gain or (Loss) Reclassified from Accumulated OCI into Earnings (Effective Portion)	Amount of Gain or (Loss) Reclassified from Accumulated OCI into Earnings (Effective Portion) <sup>(b)</sup>	
	Nine Months Ended Apr 30, 2014	Apr 30, 2013		Nine Months Ended Apr 30, 2014	Apr 30, 2013
Nonderivatives designated as hedging relationships					
Net investment hedge	\$(4,113)	\$14,757	N/A	\$—	\$—

There were no gains or losses recognized in earnings related to the ineffective portion of the hedging relationship (b) or related to the amount excluded from the assessment of hedge effectiveness for the three and nine months ended April 30, 2014 and April 30, 2013.

## NOTE 14 – ACCUMULATED OTHER COMPREHENSIVE INCOME/(LOSS)

Changes in accumulated other comprehensive income by component are presented below:

	Foreign Currency Translation	Defined Benefit Pension Plan	Unrealized investment gains/(losses)	Unrealized gains/(losses) on derivatives	Accumulated other comprehensive income/(loss)
Balance at July 31, 2013	\$84,598	\$(125,211)	\$2,123	\$(2,302)	\$(40,792)
Other comprehensive income/(loss) before reclassifications	46,330	—	(813)	5,154	50,671
Amounts reclassified from accumulated other comprehensive income (loss)	—	6,551	215	255	7,021
Foreign exchange adjustments and other	—	(6,597)	—	—	(6,597)
Balance at April 30, 2014	\$130,928	\$(125,257)	\$1,525	\$3,107	\$10,303



## PALL CORPORATION AND SUBSIDIARIES

## NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(In thousands, except per share data)

(Unaudited)

Reclassifications out of accumulated other comprehensive income are presented below:

	Three Months Ended	Nine Months Ended	Affected line item in the
	Apr 30, 2014	Apr 30, 2014	Condensed Consolidated
			Statement of Earnings
<b>Defined Benefit Pension Plan</b>			
Amortization of prior service cost	\$ (385	) \$ (1,154	) Note (a)
Recognized actuarial gain/(loss)	(2,794	) (8,294	) Note (a)
Total before tax	(3,179	) (9,448	)
Tax (expense)/benefit	958	2,897	)
Net of tax	\$ (2,221	) \$ (6,551	)
<b>Unrealized investment gains/(losses)</b>			
Realized investment gain/(losses)	\$ (217	) \$ (336	) Selling, general and
Tax (expense)/benefit	78	121	administrative
Net of tax	\$ (139	) \$ (215	)
<b>Unrealized gains/(losses) on derivatives</b>			
Foreign exchange forward contracts	\$ 440	\$ 552	Sales
Foreign exchange forward contracts	171	(695	) Cost of sales
Total before tax	611	(143	)
Tax (expense)/benefit	(102	) (112	)
Net of tax	\$ 509	\$ (255	)

(a) These accumulated other comprehensive income components are included in the computation of net periodic pension cost (see Note 8, Components of Net Periodic Pension Cost, for additional details).

## PALL CORPORATION AND SUBSIDIARIES

## NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(In thousands, except per share data)

(Unaudited)

## NOTE 15 – SEGMENT INFORMATION

The Company's reportable segments, which are also its operating segments, consist of the Company's Life Sciences and Industrial businesses.

The following table presents sales and segment profit from continuing operations by business segment reconciled to earnings from continuing operations before income taxes for the three and nine months ended April 30, 2014 and April 30, 2013.

	Three Months Ended		Nine Months Ended	
	Apr 30, 2014	Apr 30, 2013	Apr 30, 2014	Apr 30, 2013
<b>SALES:</b>				
Life Sciences	\$368,835	\$326,097	\$1,041,011	\$955,230
Industrial	313,610	315,093	948,182	976,015
Total	\$682,445	\$641,190	\$1,989,193	\$1,931,245
<b>SEGMENT PROFIT:</b>				
Life Sciences	\$88,339	\$81,195	\$252,240	\$233,514
Industrial	49,350	45,853	146,723	146,723
Total segment profit	137,689	127,048	398,963	380,237
Corporate Services Group	17,304	15,172	48,034	47,263
ROTC	11,542	12,824	29,910	21,497
Interest expense, net	4,747	5,298	15,919	10,747
Earnings from continuing operations before income taxes	\$104,096	\$93,754	\$305,100	\$300,730

## NOTE 16 – DISCONTINUED OPERATIONS

On April 28, 2012, the Company entered into an asset purchase agreement (“APA”) to sell certain assets of its blood collection, filtration and processing product line (the “Product Line”) to Haemonetics Corporation (“Haemonetics”) for approximately \$550,000. The transaction involved the transfer of manufacturing facilities and equipment in Covina, California; Tijuana, Mexico; Ascoli, Italy and a portion of the Company's operations in Fajardo, Puerto Rico. In addition to the manufacturing facilities and related equipment, the Company transferred Product Line related inventory and intangible assets. Haemonetics also assumed certain employee-related liabilities. The sale closed on August 1, 2012, and approximately 1,400 employees transitioned to Haemonetics at that time.

Separate from these manufacturing facilities, the Company also agreed to transfer related blood media manufacturing capabilities and assets to Haemonetics. The transfer of the related media lines is expected to be completed by calendar year 2016. Until that time, the Company is providing these media products to Haemonetics under a supply agreement. Under the terms of the APA, approximately \$535,000 was paid upon closing, with the balance of the purchase price payable upon the Company's delivery of the aforementioned blood media manufacturing capability and related assets. The Product Line, which was a component of the Company's Life Sciences segment, met the criteria for discontinued operations and held for sale presentation during the third quarter of fiscal year 2012 and has been reported as a discontinued operation in the Company's condensed consolidated financial statements. The Company did not allocate any portion of the Company's interest expense to discontinued operations.

## PALL CORPORATION AND SUBSIDIARIES

## NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(In thousands, except per share data)

(Unaudited)

The key components of discontinued operations for the three and nine months ended April 30, 2013 were as follows:

	Three Months Ended Apr 30, 2013	Nine Months Ended Apr 30, 2013
Net sales	\$ 344	\$ 8,867
Earnings/(loss) from discontinued operations before income taxes	\$(1,896	) \$ 392,425
Provision/(benefit) for income taxes	(690	) 146,873
Earnings/(loss) from discontinued operations, net of income taxes	\$(1,206	) \$ 245,552

Included in earnings from discontinued operations before income taxes above are a (loss)/gain on the sale of the Product Line of \$(545) and \$396,793, respectively, for the three and nine months ended April 30, 2013.

## NOTE 17 – ACQUISITIONS

During the first and second quarters of fiscal 2014, the Company completed two acquisitions - Medistad Holding BV, a European manufacturing entity, and SoloHill Engineering, Inc., a United States technology company. The aggregate consideration for these acquisitions was \$30,677, which included approximately \$3,000 of contingent consideration. On February 20, 2014, the Company acquired the Life Sciences business of ATMI, Inc. (“ATMI LifeSciences”). ATMI LifeSciences is a technology leader in the field of single-use bioprocess equipment and consumables for the biopharmaceutical and biotechnology industries. The acquisition includes the ATMI LifeSciences portfolio of custom-engineered, flexible packaging solutions, single-use storage systems, mixers and bioreactors. The Company paid a cash purchase price of \$185,000, and an additional \$5,793 related to working capital adjustments. The acquisition of ATMI LifeSciences broadens the Company's upstream presence in bioprocessing and complements its established downstream capabilities. Combined with the aforementioned acquisitions, both innovators in the single-use market, and the Company's already solid portfolio of biopharmaceutical solutions, the addition of the ATMI LifeSciences assets well positions the Company to capitalize on opportunities in the rapidly growing single-use market segment.

The above transactions (the “2014 acquisitions”) were funded with available cash and borrowings under the Company's commercial paper program. Tangible and intangible assets acquired and liabilities assumed were recognized based upon their estimated fair values at the respective closing dates. The Company is currently in the process of finalizing the valuations of acquired tangible and intangible assets and liabilities, and will make appropriate adjustments to the purchase price allocation prior to completion of the measurement period, as required.

## PALL CORPORATION AND SUBSIDIARIES

## NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(In thousands, except per share data)

(Unaudited)

The following table summarizes the preliminary estimated fair values of the assets acquired and liabilities assumed, in the aggregate, for the 2014 acquisitions as of April 30, 2014.

Purchase price, including working capital adjustments	\$221,470
Cash acquired	832
Purchase price, net of cash acquired	220,638
Accounts receivable	10,959
Inventories	22,299
Other current assets	6,891
Property, plant and equipment	30,177
Intangible assets	86,568
Other non-current assets	5,866
Total identifiable assets acquired, net of cash acquired	162,760
Current liabilities	15,722
Non-current liabilities	26,144
Total liabilities assumed	41,866
Goodwill (excess cost over value of net assets acquired)	\$99,744

The Company recorded an aggregate of \$99,744 of goodwill related to the 2014 acquisitions, none of which is expected to be deductible for income tax purposes.

The results of operations for the acquisitions since their respective acquisition dates are included in the accompanying condensed consolidated financial statements and reported in the Life Sciences segment results in Note 15, Segment Information. The impact of the 2014 acquisitions was not material, individually or in the aggregate, to the company's consolidated financial position or results from operations. Additionally, assuming these transactions had occurred at the beginning of the respective fiscal years, the consolidated pro forma results would not be materially different from reported results for the nine months ended April 30, 2014 and April 30, 2013.

## NOTE 18 – SUBSEQUENT EVENT

On May 1, 2014, the Company acquired Filter Specialists, Inc. (“FSI”), one of the industry’s leading suppliers of filter bags. FSI has developed an extremely strong brand since being established in 1972. Their technology is a direct complement to the Company's existing product line and enables it to provide a broader and more complete portfolio of products. Additionally, this acquisition will increase the Company's footprint in the automotive paint, chemical, petrochemical, oil and gas, and food and beverage markets. On the Closing Date, the Company paid a cash purchase price of \$124,000, subject to a post closing working capital adjustment.

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

The following discussion should be read together with the accompanying condensed consolidated financial statements and notes thereto and other financial information in this Form 10-Q and in the Pall Corporation and its subsidiaries (hereinafter collectively referred to as the "Company", "we" and "our") Annual Report on Form 10-K for the fiscal year ended July 31, 2013 ("2013 Form 10-K"). Certain information is presented below excluding the impact of foreign exchange translation ("translational FX") (i.e., had exchange rates not changed year over year). We consider year over year change excluding translational FX to be an important measure because by excluding the impact of volatility of exchange rates, underlying impact of volume and rate changes are evident. United States ("U.S.") Dollar amounts discussed below are in thousands, unless otherwise indicated, except per share dollar amounts. In addition, per share dollar amounts are discussed on a diluted basis. Our gross margin is impacted by the fluctuation of the costs of products that are sourced in a currency different from the currency they are sold in ("transactional FX") and our discussion of gross margin below may include references to this. We utilize certain estimates and assumptions that affect the reported financial information as well as to quantify the impact of various significant factors that contribute to the changes in our periodic results included in the discussion below.

**FORWARD-LOOKING STATEMENTS AND RISK FACTORS**

The matters discussed in this Quarterly Report contain "forward-looking statements" as defined in the Private Securities Litigation Reform Act of 1995. Forward-looking statements are those that address activities, events or developments that we intend, expect, project, believe or anticipate will or may occur in the future. All statements regarding future performance, earnings projections, earnings guidance, management's expectations about our future cash needs and effective tax rate, and other future events or developments are forward-looking statements. Forward-looking statements are those that use terms such as "may," "will," "expect," "believe," "intend," "should," "could," "anticipate," "estimate," "forecast," "project," "plan," "predict," "potential," and similar expressions. Forward-looking statements contained in this and other written and oral reports are based on management's assumptions and assessments in light of past experience and trends, current conditions, expected future developments and other relevant factors.

Our forward-looking statements are subject to risks and uncertainties and are not guarantees of future performance, and actual results, developments and business decisions may differ materially from those envisaged by our forward-looking statements. Such risks and uncertainties include, but are not limited to, those discussed in Part I-Item 1A.-Risk Factors in the 2013 Form 10-K, and other reports we file with the Securities and Exchange Commission, including: the impact of disruptions in the supply of raw materials and key components from suppliers, including limited or single source suppliers; the impact of terrorist acts, conflicts and wars or natural disasters; the extent to which special U.S. and foreign government laws and regulations may expose us to liability or impair our ability to compete in international markets; the impact of economic, political, social and regulatory instability in emerging markets, and other risks characteristic of doing business in emerging markets; fluctuations in foreign currency exchange rates and interest rates; the impact of a significant disruption in, or breach in security of, our information technology systems, or the failure to implement, manage or integrate new systems, software or technologies successfully; our ability to successfully complete or integrate acquisitions; our ability to develop innovative and competitive new products; the impact of global and regional economic conditions and legislative, regulatory and political developments; our ability to comply with a broad array of regulatory requirements; the loss of one or more members of our senior management team and our ability to recruit and retain qualified management personnel; changes in the demand for our products and the maintenance of business relationships with key customers; changes in product mix and product pricing, particularly with respect to systems products and associated hardware and devices for our consumable filtration products; product defects and unanticipated use or inadequate disclosure with respect to our products; our ability to deliver our backlog on time; increases in manufacturing and operating costs and/or our ability to achieve the savings anticipated from our structural cost improvement initiatives; the impact of environmental, health and safety laws and regulations and violations; our ability to enforce patents or protect proprietary products and manufacturing techniques; costs and outcomes of pending or future litigation and the availability of insurance or indemnification rights; changes in our effective tax rate; our ability to compete effectively in domestic and global markets; and the effect of the restrictive covenants in our debt facilities. Factors or events that

could cause our actual results to differ may emerge from time to time, and it is not possible for us to predict all of them. We make these statements as of the date of this disclosure and undertake no obligation to update them, whether as a result of new information, future developments or otherwise.

## OVERVIEW

We are a leading supplier of filtration, separation and purification technologies. Our products are used to remove solid, liquid and gaseous contaminants from a variety of liquids and gases, and are principally made by us, using our engineering capability, fluid management expertise, proprietary filter media and manufacturing expertise. Our products primarily consist of consumable filtration products and filtration systems.

We serve customers through two businesses globally: Life Sciences and Industrial. The Life Sciences business group serves customers in the BioPharmaceutical, Food & Beverage and Medical markets. The Industrial business group serves customers in the Process Technologies, Aerospace and Microelectronics markets. We operate globally in three geographic regions: the Americas; Europe (in which we include the Middle East and Africa); and Asia.

Our reporting currency is the U.S. Dollar. Because we operate through subsidiaries or branches that transact in over thirty foreign currencies around the world, our earnings are exposed to translation risk when the financial statements of the subsidiaries or branches, as stated in their functional currencies, are translated into the U.S. Dollar. We estimate that translational FX decreased sales by approximately \$600 and earnings per share by approximately 1 cent in the three months ended April 30, 2014 when compared to the three months ended April 30, 2013. We estimate that translational FX decreased sales by approximately \$21,400 and earnings per share by approximately 7 cents in the nine months ended April 30, 2014 when compared to the nine months ended April 30, 2013.

On August 1, 2012, we sold our blood collection, filtration and processing product line (the "Blood Product Line") to Haemonetics Corporation for \$550,000. We received a total of approximately \$535,000 upon closing, with the balance payable upon transfer of related blood media manufacturing capabilities and assets. The Blood Product Line was a component of our Life Sciences segment and has been reported as a discontinued operation for all periods presented. During the first and second quarters of fiscal 2014, we completed two acquisitions - Medistad Holding BV ("Medistad"), a European manufacturing entity, and SoloHill Engineering, Inc. ("SoloHill"), a U.S. technology company. The aggregate consideration for these acquisitions was approximately \$31 million, net of cash acquired, and included \$3 million of contingent consideration. On February 20, 2014 (the "Closing Date"), we acquired the Life Sciences business of ATMI, Inc. ("ATMI LifeSciences"). ATMI LifeSciences is a technology leader in the field of single-use bioprocess equipment and consumables for the biopharmaceutical and biotechnology industries. On the Closing Date, the Company paid a cash purchase price, inclusive of working capital adjustments, of approximately \$191 million. The acquisition of ATMI LifeSciences complements our upstream presence in bioprocessing and complements our established downstream capabilities. Combined with the aforementioned acquisitions, both innovators in the single-use market, and our already solid portfolio of biopharmaceutical solutions, the addition of the ATMI LifeSciences assets positions us well to capitalize on opportunities in the rapidly growing single-use market segment. These acquisitions did not have a material impact on our results from operations or financial position. See Note 17, Acquisitions, to the accompanying condensed consolidated financial statements for further detail.

## RESULTS FROM CONTINUING OPERATIONS

## Net Sales

By Segment	Three Months Ended		Nine Months Ended	
	Apr 30, 2014	Apr 30, 2013	Apr 30, 2014	Apr 30, 2013
Life Sciences	\$368,835	\$326,097	\$1,041,011	\$955,230
Industrial	313,610	315,093	948,182	976,015
Total Sales	\$682,445	\$641,190	\$1,989,193	\$1,931,245

By Product	Three Months Ended		Nine Months Ended	
	Apr 30, 2014	Apr 30, 2013	Apr 30, 2014	Apr 30, 2013
Consumables	\$603,872	\$571,029	\$1,743,842	\$1,695,683
Systems	78,573	70,161	245,351	235,562
Total Sales	\$682,445	\$641,190	\$1,989,193	\$1,931,245



The percentage change in sales for the three and nine months ended April 30, 2014 compared to the three and nine months ended April 30, 2013 by segment, with and without the impact of translational FX, are presented below:

By Segment	Three Months			Nine Months		
	% Change excluding translational FX	Translational FX	Total % Change	% Change excluding translational FX	Translational FX	Total % Change
Life Sciences	12.3	0.8	13.1	9.2	(0.2)	9.0
Industrial	0.5	(1.0)	(0.5)	(0.8)	(2.1)	(2.9)
Total	6.5	(0.1)	6.4	4.1	(1.1)	3.0

The percentage change in sales for the three and nine months ended April 30, 2014 compared to the three and nine months ended April 30, 2013 by product, with and without the impact of translational FX, are presented below:

By Product	Three Months			Nine Months		
	% Change excluding translational FX	Translational FX	Total % Change	% Change excluding translational FX	Translational FX	Total % Change
Consumables	5.7	0.1	5.8	3.9	(1.1)	2.8
Systems	13.0	(1.0)	12.0	5.7	(1.5)	4.2
Total	6.5	(0.1)	6.4	4.1	(1.1)	3.0

#### Three Months

Total sales increased approximately 7% (excluding translational FX) reflecting growth in all markets in the Life Sciences segment, including the benefit of acquisitions, and in the Microelectronics market in the Industrial segment, partly offset by a decline in the Aerospace market in the Industrial segment. Total sales in the Process Technologies market in the Industrial segment were essentially flat. The acquisitions of ATMI LifeSciences, Medistad and SoloHill contributed approximately 270 basis points to total sales growth compared to last year. More details regarding sales by segment can be found in the discussions under the section "Segment Review."

The approximate 6% increase in consumables sales (excluding translational FX) reflects the same trend as total sales discussed above. Increased pricing contributed approximately \$5,200, or about 90 basis points, to consumables sales growth, reflecting increases in both segments.

The 13% increase in system sales (excluding translational FX) reflects timing of capital projects in the Life Sciences segment, partly offset by a decline in the Fuels & Chemicals submarket of Process Technologies in the Industrial segment.

#### Nine Months

Total sales increased approximately 4% (excluding translational FX) reflecting growth in all markets in the Life Sciences segment, including the benefit of acquisitions, and in the Microelectronics market in the Industrial segment, partly offset by declines in the Process Technologies and Aerospace markets in the Industrial segment. The acquisitions of ATMI LifeSciences, Medistad and SoloHill contributed approximately 140 basis points to total sales growth compared to last year.

The approximate 4% increase in consumables sales (excluding translational FX) reflects the same trend as total sales discussed above. Increased pricing contributed approximately \$12,600, or about 70 basis points, to consumables sales growth, reflecting increases in both segments.

The increase in system sales of approximately 6% (excluding translational FX) reflects the same trend as the three months discussed above.

## Gross Margin

	Three Months Ended		Nine Months Ended	
	Apr 30, 2014	Apr 30, 2013	Apr 30, 2014	Apr 30, 2013
Gross Profit	\$348,074	\$334,079	\$1,018,047	\$1,003,125
% of sales	51.0	52.1	51.2	51.9
% Change	4.2		1.5	

## Three Months

The decrease in overall gross margin of 110 basis points primarily reflects the impact of the following unfavorable factors:

- transactional FX (principally related to the Yen and British pound),
- a higher proportion of systems sales and lower margin systems projects in the current quarter,
- lower gross margin rates from the Medistad and ATMI LifeSciences acquisitions, and
- a purchase accounting adjustment related to the step-up of acquired inventory that was sold in the period.

These factors were partly offset by improved pricing and favorable customer mix. More details regarding gross margin can be found in the discussions under the section “Segment Review.”

## Nine Months

The decrease in overall gross margin of 70 basis points primarily reflects the same factors discussed above for the three months.

## Selling, General and Administrative

	Three Months Ended		Nine Months Ended	
	Apr 30, 2014	Apr 30, 2013	Apr 30, 2014	Apr 30, 2013
Selling, general and administrative	\$201,045	\$199,595	\$592,228	\$601,569
% of sales	29.5	31.1	29.8	31.1
% Change	0.7		(1.6 )	

## Three Months

The decrease in selling, general and administrative expenses (“SG&A”) as a percent of sales of 160 basis points reflects savings generated by our structural cost improvement initiative and better fixed cost leverage. This was partly offset by:

- select investments in high growth markets; and
- inflationary increases in payroll and related costs.

## Nine Months

The decrease in SG&A as a percent of sales of 130 basis points reflects the same factors as discussed above in the three months.

## Research &amp; Development

	Three Months Ended		Nine Months Ended	
	Apr 30, 2014	Apr 30, 2013	Apr 30, 2014	Apr 30, 2013
Research and development	\$26,644	\$22,608	\$74,890	\$68,582
% of sales	3.9	3.5	3.8	3.6
% Change	17.9		9.2	

## Three Months

The increase in research and development expenses (“R&D”), reflects our strategy to increase innovation investment in the Life Sciences and Industrial segments. This was driven by our focus on new product development and development of our media and instrumentation capabilities. Additionally, the increase in R&D reflects ATMI LifeSciences related spend.

## Nine Months

The increase in R&D reflects the same factors as discussed above in the three months.

## Restructuring and Other Charges, Net

	Three Months Ended		Nine Months Ended	
	Apr 30, 2014	Apr 30, 2013	Apr 30, 2014	Apr 30, 2013
Restructuring and other charges, net	\$11,542	\$12,824	\$29,910	\$21,497

In fiscal year 2012, we announced a multi-year strategic cost reduction initiative (“structural cost improvement initiative”). This initiative impacts both segments as well as the Corporate Services Group. Our goal is to properly position our cost structure globally to perform in the current economic environment without adversely impacting our growth or innovation potential.

Key components of the structural cost improvement initiative include:

- the strategic alignment of our manufacturing, sales and R&D facilities to cost-effectively deliver high-quality products and superior service to our customers worldwide,
- creation of regional shared financial services centers for the handling of accounting transaction processing and other accounting functions,
- reorganization of sales functions, to more cost- efficiently deliver superior service to our customers globally, and
- reductions in headcount across all functional areas, enabled by efficiencies gained through our ERP systems, as well as in order to align to economic conditions.

The structural cost improvement initiative is expected to generate \$100,000 in annualized cost savings over a three year period, which will allow us to invest in resources where needed. Approximately half of the targeted \$100,000 annualized savings were achieved by the end of fiscal year 2013. We expect to achieve more than 30% of the targeted savings in fiscal year 2014 with the balance achieved in fiscal year 2015. We expect to fund these restructuring activities with cash flows generated from operating activities.

Restructuring and other charges (“ROTC”) in the three and nine months ended April 30, 2014 primarily reflect the expenses incurred in connection with our structural cost improvement initiative, as discussed above, including severance costs of \$8,289 and \$18,751 in the three and nine months ended April 30, 2014, respectively. The three and nine months ended April 30, 2014 also includes the impairment of assets of \$3,986 related to the discontinuance of a specific manufacturing line due to excess capacity as a result of recent acquisitions. In addition, the nine months ended April 30, 2014 includes an increase of \$4,440 to our previously established environmental reserves related to a matter in Pinellas Park, Florida.

ROTC in the three and nine months ended April 30, 2013 primarily reflect the expenses incurred in connection with our structural cost improvement initiative, as discussed above, including severance costs of \$5,701 and \$10,896 in the three and nine months ended April 30, 2013, respectively. In addition, the three and nine months ended April 30, 2013 includes an increase of \$2,715 to our previously established environmental reserves related to a matter in Glen Cove, New York.



The details of ROTC, as well as the activity related to restructuring liabilities that were recorded related to our structural cost improvement initiative, can be found in Note 6, Restructuring and Other Charges, Net, to the accompanying condensed consolidated financial statements.

#### Interest Expense, Net

	Three Months Ended		Nine Months Ended	
	Apr 30, 2014	Apr 30, 2013	Apr 30, 2014	Apr 30, 2013
Interest expense, net	\$4,747	\$5,298	\$15,919	\$10,747

#### Three Months

Interest expense, net, in the three months ended April 30, 2014 reflects the reversal of accrued interest of \$1,478, related to the resolution of foreign tax audits. Excluding this benefit, interest expense, net, in the three months ended April 30, 2014 would have been \$6,225. The resulting increase in net interest expense of \$927 was primarily driven by an increase in other income tax related interest expense (excluding the item referenced above), increased interest expense related to higher commercial paper borrowings and a decrease in interest income.

#### Nine Months

Interest expense, net, in the nine months ended April 30, 2014 reflects the reversal of accrued interest of \$1,478, related to the resolution of foreign tax audits. Interest expense, net, in the nine months ended April 30, 2013 reflects the reversal of accrued interest of \$6,704, related to the resolution of a U.S. tax audit. Excluding these benefits, interest expense, net, in the nine months ended April 30, 2014 and April 30, 2013 would have been \$17,397 and \$17,451, respectively. The resulting decrease in net interest expense of \$54 was primarily driven by a reduction in other income tax related interest expense (excluding the items referenced above) partly offset by increased interest expense related to higher commercial paper borrowings and a decrease in interest income.

#### Income Taxes

	Three Months Ended		Nine Months Ended	
	Apr 30, 2014	Apr 30, 2013	Apr 30, 2014	Apr 30, 2013
Income taxes	\$15,405	\$19,483	\$61,230	\$56,975
Effective tax rate (%)	14.8	20.8	20.1	18.9

The effective tax rate for the three and nine months ended April 30, 2014 reflects a net tax benefit of \$10,054 from the resolution of tax audits. The effective tax rate for the nine months ended April 30, 2013 reflects a net tax benefit of \$7,757 primarily from the resolution of a U.S. tax audit partly offset by the establishment of deferred tax liabilities for the repatriation of foreign earnings. Excluding these impacts, as well as the impact of ROTC and inventory step-up in cost of sales discussed above, the effective tax rate for the three months ended April 30, 2014 and April 30, 2013 would have been 22.5% and 21.6%, respectively. The effective tax rate for the nine months ended April 30, 2014 and April 30, 2013 would have been 22.2% and 22.2%, respectively. We expect our effective tax rate for the full fiscal year 2014 to be approximately 22.5%, exclusive of the impact of ROTC and discrete items. The actual effective tax rate for the full fiscal year 2014 may differ materially based on several factors, including the geographical mix of earnings in tax jurisdictions, enacted tax laws, the resolution of tax audits, the timing and amount of foreign dividends, state and local taxes, the ratio of permanent items to pretax book income, and the implementation of various global tax strategies as well as other factors.

#### Net Earnings

	Three Months Ended		Nine Months Ended	
	Apr 30, 2014	Apr 30, 2013	Apr 30, 2014	Apr 30, 2013
Net Earnings	\$88,691	\$74,271	\$243,870	\$243,755
Diluted earnings per share	\$0.80	\$0.65	\$2.17	\$2.13

#### Three Months

We estimate that translational FX decreased earnings per share by approximately 1 cent in the three months ended April 30, 2014 when compared to the three months ended April 30, 2013. The decrease in share count increased

diluted earnings per share by approximately 1 cent.

## Nine Months

We estimate that translational FX decreased earnings per share by approximately 7 cents in the nine months ended April 30, 2014 when compared to the nine months ended April 30, 2013. The decrease in share count increased diluted earnings per share by approximately 4 cents.

## RESULTS FROM DISCONTINUED OPERATIONS

	Three Months Ended		Nine Months Ended	
	Apr 30, 2014	Apr 30, 2013	Apr 30, 2014	Apr 30, 2013
Sales	\$—	\$344	\$—	\$8,867
Net Earnings	\$—	\$(1,206 )	\$—	\$245,552
Diluted Earnings per share	\$—	\$(0.01 )	\$—	\$2.15

Net earnings in the nine months ended April 30, 2013 reflects the gain on the sale of the Blood Product Line. More details regarding discontinued operations can be found in Note 16, Discontinued Operations, to the accompanying condensed consolidated financial statements.

## SEGMENT REVIEW

	Three Months Ended		Nine Months Ended	
	Apr 30, 2014	Apr 30, 2013	Apr 30, 2014	Apr 30, 2013
Sales:				
Life Sciences	\$368,835	\$326,097	\$1,041,011	\$955,230
Industrial	313,610	315,093	948,182	976,015
Total	\$682,445	\$641,190	\$1,989,193	\$1,931,245
Segment profit:				
Life Sciences segment profit	\$88,339	\$81,195	\$252,240	\$233,514
Industrial segment profit	49,350	45,853	146,723	146,723
Total segment profit	137,689	127,048	398,963	380,237
Corporate Services Group	17,304	15,172	48,034	47,263
ROTC	11,542	12,824	29,910	21,497
Interest expense, net	4,747	5,298	15,919	10,747
Earnings before income taxes from continuing operations	\$104,096	\$93,754	\$305,100	\$300,730

## Life Sciences

	Three Months Ended				Nine Months Ended			
	Apr 30, 2014	% of Sales	Apr 30, 2013	% of Sales	Apr 30, 2014	% of Sales	Apr 30, 2013	% of Sales
Sales	\$368,835		\$326,097		\$1,041,011		\$955,230	
Cost of sales	166,394	45.1	138,473	42.5	456,428	43.8	399,516	41.8
Gross margin	202,441	54.9	187,624	57.5	584,583	56.2	555,714	58.2
SG&A	97,391	26.4	91,897	28.2	284,441	27.3	277,216	29.0
R&D	16,711	4.5	14,532	4.5	47,902	4.6	44,984	4.7
Segment profit	\$88,339	24.0	\$81,195	24.9	\$252,240	24.2	\$233,514	24.4

SALES:	Three Months Ended		Nine Months Ended	
	Apr 30, 2014	Apr 30, 2013	Apr 30, 2014	Apr 30, 2013
By Market and Product				
BioPharmaceuticals	\$235,724	\$208,219	\$650,467	\$597,117
Food & Beverage	46,097	43,436	133,720	130,269
Medical	56,212	53,705	168,589	154,579
Total Consumables sales	\$338,033	\$305,360	\$952,776	\$881,965
Systems Sales	30,802	20,737	88,235	73,265
Total Life Sciences Sales	\$368,835	\$326,097	\$1,041,011	\$955,230
By Region				
Americas	\$108,612	\$101,994	\$308,701	\$303,810
Europe	188,073	162,284	536,828	465,309
Asia	72,150	61,819	195,482	186,111
Total Life Sciences Sales	\$368,835	\$326,097	\$1,041,011	\$955,230

Edgar Filing: PALL CORP - Form 10-Q

The percentage change in sales for the three and nine months ended April 30, 2014 compared to the three and nine months ended April 30, 2013, with and without the impact of translational FX, are presented below:

SALES % CHANGE	Three Months			Nine Months		
	% Change excluding translational FX	Translational FX	Total % Change	% Change excluding translational FX	Translational FX	Total % Change
By Market and Product						
BioPharmaceuticals	12.0	1.2	13.2	8.9	—	8.9
Food & Beverage	8.4	(2.3	) 6.1	4.6	(2.0	) 2.6
Medical	2.9	1.8	4.7	8.4	0.7	9.1
Total Consumables sales	9.9	0.8	10.7	8.2	(0.2	) 8.0
Systems Sales	48.0	0.5	48.5	21.1	(0.7	) 20.4
Total Life Sciences Sales	12.3	0.8	13.1	9.2	(0.2	) 9.0
By Region						
Americas	9.3	(2.8	) 6.5	3.7	(2.1	) 1.6
Europe	10.1	5.8	15.9	10.9	4.5	15.4
Asia	23.2	(6.5	) 16.7	13.7	(8.7	) 5.0
Total Life Sciences Sales	12.3	0.8	13.1	9.2	(0.2	) 9.0

Three Months

The acquisitions of ATMI LifeSciences, Medistad and SoloHill contributed approximately 560 basis points to Life Sciences consumables sales growth compared to last year.

BioPharmaceuticals consumables sales growth reflect overall market strength, growth in single use systems and new products, augmented by acquisitions.

Food & Beverage consumables sales growth reflects strength in the Americas and Asia, partly offset by softness in beverage production in Europe.

Medical consumables sales growth reflects the impact of the acquisition of Medistad, partly offset by lower blood media sales.

Life Sciences systems sales growth reflects timing of capital spending by BioPharmaceuticals and Food & Beverage customers.

Life Sciences segment profit grew 8.8%. Translational FX had an immaterial impact on segment profit growth.

Segment profit margin decreased 90 basis points reflecting a decline in gross margin, partly offset by the benefit from increased leverage of fixed cost SG&A on a higher sales base. The 260 basis point decline in gross margin is primarily due to:

- certain low margin systems projects in the current quarter,
- unfavorable transactional FX (principally Yen related),
- a higher proportion of systems sales to total sales, which typically carry lower margins than consumables (systems sales comprised approximately 8% of total sales compared to 6% last year),
- lower gross margin rates from the Medistad and ATMI LifeSciences acquisitions, and
- a purchase accounting adjustment related to the step-up of acquired inventory that was sold in the period.

These factors were partly offset by the benefit of favorable pricing.

Nine Months

The acquisitions of ATMI LifeSciences, Medistad and SoloHill contributed approximately 320 basis points to Life Sciences consumables sales growth compared to last year.

BioPharmaceuticals consumables sales growth reflect overall market strength, particularly in Europe and Asia, growth in single use systems and new products, augmented by acquisitions.

Food & Beverage consumables sales growth (excluding translational FX) was driven by strength in the Americas and Asia.



Medical consumables sales growth reflects an increase in sales to OEMs, augmented by the acquisition of Medistad, and growth in the Hospital Critical Care market driven by water products. These factors were partly offset by lower blood media sales.

Life Sciences systems sales growth reflects timing of capital spending by BioPharmaceuticals and Food & Beverage customers.

Life Sciences segment profit grew 8.0%. Translational FX negatively impacted the segment profit growth by approximately 110 basis points. Segment profit margin decreased 20 basis points primarily reflecting a decline in gross margin partly offset by the benefit from increased leverage of fixed cost SG&A on a higher sales base. The 200 basis point decline in gross margin reflects the same factors as in the three months discussed above.

#### Industrial

	Three Months Ended				Nine Months Ended			
	Apr 30, 2014	% of Sales	Apr 30, 2013	% of Sales	Apr 30, 2014	% of Sales	Apr 30, 2013	% of Sales
Sales	\$ 313,610		\$ 315,093		\$ 948,182		\$ 976,015	
Cost of sales	167,977	53.6	168,638	53.5	514,718	54.3	528,604	54.2
Gross margin	145,633	46.4	146,455	46.5	433,464	45.7	447,411	45.8
SG&A	86,350	27.5	92,526	29.4	259,753	27.4	277,090	28.4
R&D	9,933	3.2	8,076	2.6	26,988	2.8	23,598	2.4
Segment profit	\$ 49,350	15.7	\$ 45,853	14.6	\$ 146,723	15.5	\$ 146,723	15.0

SALES:	Three Months Ended		Nine Months Ended	
	Apr 30, 2014	Apr 30, 2013	Apr 30, 2014	Apr 30, 2013
By Market and Product				
Process Technologies	\$ 137,348	\$ 139,711	\$ 402,090	\$ 432,826
Aerospace	54,088	61,466	166,181	177,954
Microelectronics	74,403	64,492	222,795	202,938
Total Consumables sales	\$ 265,839	\$ 265,669	\$ 791,066	\$ 813,718
Systems Sales	47,771	49,424	157,116	162,297
Total Industrial Sales	\$ 313,610	\$ 315,093	\$ 948,182	\$ 976,015
By Region				
Americas	\$ 107,087	\$ 107,390	\$ 315,505	\$ 317,699
Europe	88,635	96,764	284,136	300,943
Asia	117,888	110,939	348,541	357,373
Total Industrial Sales	\$ 313,610	\$ 315,093	\$ 948,182	\$ 976,015

The percentage change in sales for the three and nine months ended April 30, 2014 compared to the three and nine months ended April 30, 2013, with and without the impact of translational FX, are presented below:

SALES % CHANGE:	Three Months			Nine Months		
	% Change excluding translational FX	Translational FX	Total % Change	% Change excluding translational FX	Translational FX	Total % Change
<b>By Market and Product</b>						
Process Technologies	(0.4	) (1.3	) (1.7	) (5.5	) (1.6	) (7.1
Aerospace	(13.4	) 1.4	(12.0	) (7.3	) 0.7	(6.6
Microelectronics	17.5	(2.1	) 15.4	15.1	(5.3	) 9.8
Total Consumables sales	1.0	(0.9	) 0.1	(0.8	) (2.0	) (2.8
Systems Sales	(1.8	) (1.5	) (3.3	) (1.2	) (2.0	) (3.2
Total Industrial Sales	0.5	(1.0	) (0.5	) (0.8	) (2.1	) (2.9
<b>By Region</b>						
Americas	1.6	(1.9	) (0.3	) 0.6	(1.3	) (0.7
Europe	(12.4	) 4.0	(8.4	) (8.5	) 2.9	(5.6
Asia	10.8	(4.5	) 6.3	4.3	(6.8	) (2.5
Total Industrial Sales	0.5	(1.0	) (0.5	) (0.8	) (2.1	) (2.9

#### Three Months

Process Technologies consumables sales were flat (excluding translational FX). The sales results excluding translational FX by key submarkets are discussed below:

- Consumables sales in the Machinery & Equipment submarket, which represented close to 25% of total Industrial consumables sales in the quarter, increased approximately 5%. Growth was driven by the mobile OEM, automotive and in-plant sectors partly offset by continued weakness in the primary metals and mining sectors.

Consumables sales in the Fuels & Chemicals submarket, which represented almost 20% of total Industrial consumables sales in the quarter, were down 8% on low-entering backlog, some continued softness in emerging markets and tough comparables in Europe.

Consumables sales in the Power Generation submarket, which represented almost 10% of total Industrial consumables sales in the quarter, increased approximately 2% driven by growth in the nuclear and wind sectors in Asia.

Aerospace consumables sales decreased on declines in both Commercial and Military Aerospace sales. This is largely the result of timing of shipments, as well as a difficult comparative, as last year included large aftermarket sales and helicopter program shipments that did not repeat.

Microelectronics consumables sales growth reflect continued market strength and new business wins. Strong consumer tablet demand is also driving growth in the display and electronic component sectors.

The decrease in Industrial systems sales primarily reflects reduced capital spending in the Fuels & Chemicals submarket.

Industrial segment profit increased 7.6%, with translational FX negatively impacting segment profit growth by approximately 250 basis points. Excluding translational FX, segment profit grew 10.1% in spite of flat sales. Segment profit margin increased 110 basis points driven by a decline in SG&A of approximately 180 basis points that was primarily attributable to our structural cost improvement initiative, partly offset by increased R&D and a slight decline in gross margin. The 10 basis point decline in gross margin is primarily due to adverse translational FX (principally Yen and British Pound) largely offset by the impact of improved pricing and favorable customer mix.

### Nine Months

Process Technologies consumables sales decreased about 6% (excluding translational FX). The sales results excluding transactional FX by key submarkets are discussed below:

Consumables sales in the Machinery & Equipment submarket, which represented a little over 20% of total Industrial consumables sales in the nine months, decreased 1% on weakness in primary metals and mining, partly offset by growth in the mobile OEM, automotive and in-plant sectors.

Consumables sales in the Fuels & Chemicals submarket, which represented almost 20% of total Industrial consumables sales in the nine months, were down about 11% on low-entering backlog and softness in emerging markets particularly China, Venezuela and Russia.

Consumables sales in the Power Generation submarket, which represented almost 10% of total Industrial consumables sales in the nine months, declined approximately 3% on market softness in Europe and the Americas, partly offset by growth in the nuclear and wind sectors in Asia.

Aerospace consumables sales decreased on declines in both Commercial and Military Aerospace sales. This is largely the result of timing of shipments, as well as a difficult comparative, as last year included large aftermarket sales and helicopter program shipments that did not repeat.

Microelectronics consumables sales were up in all three regions on continued market strength and new business wins. The decrease in Industrial systems sales primarily reflects timing of capital spending in the Fuels & Chemicals submarket.

Industrial segment profit was flat, with translational FX negatively impacting segment profit growth by approximately 470 basis points. Excluding translational FX, segment profit was up 4.7% on a sales decline of about 1%. Segment profit margin increased 50 basis points driven by a 100 basis point decline in SG&A that was primarily attributable to our structural cost improvement initiative, partly offset by increased R&D and a slight decline in gross margin.

### Corporate Services Group

	Three Months		Nine Months	
	Apr 30, 2014	Apr 30, 2013	Apr 30, 2014	Apr 30, 2013
Corporate Services Group expenses	\$ 17,304	\$ 15,172	\$ 48,034	\$ 47,263
% Change	14.1		1.6	

The increase in Corporate Services Group expenses in the three and nine months primarily reflects an increase in compensation related costs and professional fees.

### Liquidity and Capital Resources

We utilize cash flow generated from operations and our commercial paper program to meet our short-term liquidity needs. We consider our cash balances, lines of credit and access to the commercial paper and other credit markets, along with the cash typically generated from operations, to be sufficient to meet our anticipated liquidity needs.

Our cash position, net of debt, was approximately \$101,800 at April 30, 2014, compared to \$299,200 at July 31, 2013, a decrease of \$197,400. The impact of translational FX increased net cash by about \$18,500. Excluding this impact, net cash decreased by \$215,900 reflecting an increase in gross debt of \$135,400, principally to fund share repurchase in the U.S and a decrease in cash and cash equivalents of \$80,500.

As of April 30, 2014, the amount of cash and cash equivalents held by foreign subsidiaries was \$849,895. Repatriation of cash held outside the U.S. could be subject to restrictions in the host countries as well as both local and U.S. taxes. However, we do not expect these to have a material effect on our overall liquidity.

We have a five-year \$1,200,000 unsecured senior revolving credit facility (the “Facility”) with a syndicate of banks, which expires on April 11, 2018. Borrowings under the Facility bear interest at either a variable rate based upon the London InterBank Offered Rate (U.S. Dollar, British Pound, Euro, Swiss Franc and Japanese Yen borrowings) or the European Union Banking Federation Rate (Euro borrowings) or at the prime rate of the Facility Agent (U.S. Dollar borrowing only). The Facility does not permit us to exceed a maximum consolidated leverage ratio of 3.5:1, based upon the trailing four quarters’ results. In addition, the Facility includes other covenants that under certain circumstances may restrict our ability to incur additional indebtedness, make investments and other restricted payments, enter into sale and leaseback transactions, create liens and sell assets. As of April 30, 2014, we did not have any outstanding borrowings under our Facility. As of April 30, 2014, we were in compliance with all related financial and other restrictive covenants, including limitations on indebtedness.

As of April 30, 2014, we had approximately \$305,000 of outstanding commercial paper, which is recorded as notes payable in the current liability section of our accompanying condensed consolidated balance sheet. Commercial paper outstanding at April 30, 2014 carry interest rates ranging between 0.31% and 0.32% and maturities between 30 and 42 days. Commercial paper outstanding at any one time during the quarter had balances ranging from \$305,000 to \$470,000, carried interest rates ranging between 0.30% and 0.37% and original maturities between 22 and 90 days.

#### Cash Flow - Operating Activities

	Nine Months Ended	
	Apr 30, 2014	Apr 30, 2013
Net cash provided by operating activities	\$ 342,164	\$ 206,890
Less capital expenditures	50,301	66,387
Free cash flow	\$ 291,863	\$ 140,503

#### Nine Months ended April 30, 2014

The major items impacting net cash provided by operating activities include:

- net earnings from continuing operations of \$243,870;
- non-cash reconciling items in net earnings from continuing operations, such as depreciation and amortization of long-lived assets of \$84,716 and non-cash stock compensation of \$23,962; and
- payments related to our Structural Cost Improvement initiative of \$21,529.

Improved working capital management, particularly improvement in days sales outstanding, benefited net cash provided by operating activities in the nine months.

#### Nine Months ended April 30, 2013

The major items impacting net cash provided by operating activities include:

- net earnings from continuing operations of \$243,755;
- non-cash reconciling items in net earnings from continuing operations, such as depreciation and amortization of long-lived assets of \$79,481 and non-cash stock compensation of \$20,153;
- income tax and tax-related payments of approximately \$94,000 related to the settlement of, and deposits for, several years of U.S. tax audits and payments for the gain on the sale of the Blood Product Line; and
- payments related to our Structural Cost Improvement initiative of \$25,986.

Discontinued operations had an immaterial impact on net cash provided by operating activities in the period.

#### Free Cash Flow

We utilize free cash flow as one way to measure our current and future financial performance. Free cash flow is a non-GAAP financial measure and is not intended as an alternative measure of cash flow from operations as determined in accordance with GAAP. In addition, our calculation of free cash flow is not necessarily comparable to similar measures as calculated by other companies that do not use the same definition or implementation guidelines. The table above reconciles net cash provided by operating activities, inclusive of discontinued operations, to free cash flow.

The increase in free cash flow in the nine months ended April 30, 2014 compared to the nine months ended April 30, 2013 reflects the increase in net cash provided by operating activities and a decrease in capital expenditures.



Depreciation and Amortization

Depreciation expense and amortization expense are presented below:

	Nine Months Ended	
	Apr 30, 2014	Apr 30, 2013
Depreciation expense	\$69,938	\$64,581
Amortization expense	\$14,778	\$14,900
Cash Flow - Investing Activities		

	Nine Months Ended	
	Apr 30, 2014	Apr 30, 2013
Net cash (used)/provided by investing activities	\$ (242,610 )	\$ 470,221
Nine Months ended April 30, 2014		

The most significant drivers of net cash used by investing activities were:

• payments totaling \$195,262 related to the acquisitions of ATMI LifeSciences, Medistad and SoloHill, and

• capital expenditures of \$50,301.

Refer to the Overview section of the Management's Discussion and Analysis of Financial Condition and Results of Operations as well as to Note 17, Acquisitions, to the accompanying condensed consolidated financial statements for further detail on the acquisitions.

Nine Months ended April 30, 2013

The most significant drivers of net cash provided by investing activities include:

• proceeds from the sale of assets of \$537,284, primarily related to the sale of our Blood Product Line, and

• capital expenditures of \$66,387, which partly offset the above.

Cash Flow - Financing Activities

	Nine Months Ended	
	Apr 30, 2014	Apr 30, 2013
Net cash used by financing activities	\$ (182,935 )	\$ (280,730 )

Share repurchases in the nine months ended April 30, 2014 and April 30, 2013, are presented below. For further information on the Company's share buyback programs, see Note 4, Treasury Stock, to the accompanying condensed consolidated financial statements.

	Nine Months Ended	
	Apr 30, 2014	Apr 30, 2013
Share repurchases	\$250,000	\$250,000
Number of shares	3,056	3,971

In the three months ended October 31, 2013, we paid \$125,000 under an accelerated share repurchase agreement ("ASR"). Upon completion of the transaction, we received a total of 1,573 shares. In the three months ended January 31, 2014 we paid \$125,000 under another ASR agreement and upon completion of the transaction received 1,483 shares. See Note 4, Treasury Stock, to the accompanying condensed consolidated financial statements for further details.

We increased our quarterly dividend by 10% from 25 cents per share to 27.5 cents per share, effective with the dividend declared on September 24, 2013. Dividends paid in the nine months ended April 30, 2014 and April 30, 2013, are presented below:

	Nine Months Ended	
	Apr 30, 2014	Apr 30, 2013
Dividends paid	\$88,596	\$80,197
Dividends declared per share	\$0.825	\$0.750
Non-Cash Working Capital		

Non-cash working capital, which is defined as working capital excluding cash and cash equivalents, notes receivable, notes payable and the current portion of long-term debt, was approximately \$601,300 at April 30, 2014 as compared with \$554,500 at July 31, 2013. Excluding the impact of translational FX (discussed below), non-cash working capital increased approximately \$39,500 compared to July 31, 2013 principally reflecting the impact of acquisitions.

Our balance sheet is affected by spot exchange rates used to translate local currency amounts into U.S. Dollars. In comparing spot exchange rates at April 30, 2014 to those at July 31, 2013, the Euro and the British Pound have strengthened against the U.S. Dollar, and the Japanese Yen has weakened against the U.S. Dollar. The impact of translational FX, increased net inventory, net accounts receivable and other current assets by approximately \$5,500, \$7,100 and \$2,000, respectively, as compared to July 31, 2013. Additionally, the impact of translational FX increased accounts payable, accrued liabilities and income tax payable collectively by \$7,300. The combination of these translational FX impacts increased non-cash working capital by approximately \$7,300.

#### Derivatives

We manage certain financial exposures through a risk management program that includes the use of foreign exchange derivative financial instruments. Derivatives are executed with counterparties with a minimum credit rating of "A" by Standard and Poor's and "A2" by Moody's Investor Services, in accordance with our policies. We do not utilize derivative instruments for trading or speculative purposes.

We conduct transactions in currencies other than their functional currency. These transactions include non-functional currency intercompany and external sales as well as intercompany and external purchases. We use foreign exchange forward contracts, matching the notional amounts and durations of the receivables and payables resulting from the aforementioned underlying foreign currency transactions, to mitigate the exposure to earnings and cash flows caused by changing foreign exchange rates. The risk management objective of holding foreign exchange derivatives is to mitigate volatility to earnings and cash flows due to changes in foreign exchange rates.

The notional amount of foreign currency forward contracts entered into during the three and nine months ended April 30, 2014 was \$687,213 and 1,923,422, respectively. The notional amount of foreign currency forward contracts outstanding as of April 30, 2014 was \$512,733 of which \$106,161 are for cash flow hedges that cover monthly transactional exposures through May 2015. Our foreign currency balance sheet exposures resulted in the recognition of a loss within SG&A of approximately \$169 in the three months ended April 30, 2014, before the impact of the measures described above. Including the impact of our foreign exchange derivative instruments, the net recognition within SG&A was a loss of approximately \$776 in the three months ended April 30, 2014.

#### Adoption of New Accounting Pronouncements

In February 2013, the Financial Accounting Standards Board ("FASB") issued new accounting guidance which amended Accounting Standards Codification ("ASC") 220, "Comprehensive Income." The amended guidance requires entities to provide information about the amounts reclassified out of accumulated other comprehensive income by component. Additionally, entities are required to present, either on the face of the financial statements or in the notes, significant amounts reclassified out of accumulated other comprehensive income by the respective line items of net income, but only if the amount reclassified is required under U.S. generally accepted accounting principles ("GAAP") to be reclassified to net income in its entirety in the same reporting period. For other amounts that are not required under U.S. GAAP to be reclassified in their entirety to net income, an entity is required to cross-reference to other disclosures in the financial statements. The amended guidance does not change the current requirements for reporting net income or other comprehensive income. The adoption of this disclosure-only guidance did not have an impact on our condensed consolidated financial results.



#### Recently Issued Accounting Pronouncements

In April 2014, the FASB issued authoritative guidance which changes the criteria for a disposal of a component or a group of components of an entity to qualify as a discontinued operation. This revised guidance defines a discontinued operation as (i) a component of an entity or group of components that has been disposed of or is classified as held for sale that represents a strategic shift that has or will have a major effect on an entity's operations and financial results or (ii) an acquired business or nonprofit activity that is classified as held for sale on the date of acquisition. The guidance also requires expanded disclosures related to discontinued operations and added disclosure requirements for individually material disposal transactions that do not meet the discontinued operations criteria. This guidance becomes effective prospectively for our fiscal 2016 first quarter, with early adoption permitted, but only for disposals (or classifications as held for sale) that have not been reported in financial statements previously issued or available to be issued. We will apply this new guidance when it becomes effective. The adoption of this guidance is not expected to have a significant impact on our consolidated financial statements.

In July 2013, the FASB issued new accounting guidance which requires the netting of unrecognized tax benefits against a deferred tax asset for a loss or other carry forward that would apply in settlement of the uncertain tax positions. Under the new standard, unrecognized tax benefits will be netted against all available same-jurisdiction loss or other tax carry forwards that would be utilized, rather than only against carry forwards that are created by the unrecognized tax benefits. The new guidance is effective prospectively to all existing unrecognized tax benefits, but entities can choose to apply it retrospectively. The guidance will be effective for us in our first quarter of fiscal year 2015, with early adoption permitted. We are currently assessing the impact this guidance will have on our consolidated statements of financial position and cash flows.

#### ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK.

There is no material change in the market risk information disclosed in Item 7A of the 2013 Form 10-K.

#### ITEM 4. CONTROLS AND PROCEDURES.

There were no changes in the Company's internal control over financial reporting during the Company's third quarter of fiscal year 2014, that have materially affected, or are reasonably likely to materially affect, the Company's internal control over financial reporting.

As of the end of the period covered by this report, the Company carried out an evaluation, under the supervision and with the participation of the Company's management, including the Company's chief executive officer and chief financial officer, of the effectiveness of the Company's disclosure controls and procedures pursuant to Rule 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934, as amended. Based on this evaluation, the chief executive officer and chief financial officer concluded that the Company's disclosure controls and procedures are effective.

## PART II. OTHER INFORMATION

### ITEM 1. LEGAL PROCEEDINGS.

(In thousands)

As previously disclosed in the 2013 Form 10-K, the Company is subject to various regulatory proceedings and litigation, including with respect to various environmental matters. Reference is also made to Note 5, Contingencies and Commitments, to the accompanying condensed consolidated financial statements.

#### Environmental Matters:

The Company's condensed consolidated balance sheet at April 30, 2014 includes liabilities for environmental matters of approximately \$20,738, which relate primarily to the environmental proceedings discussed in the 2013 Form 10-K and Note 5, Contingencies and Commitments, to the accompanying condensed consolidated financial statements of this Form 10-Q. In the opinion of management, the Company is in substantial compliance with applicable environmental laws and its current accruals for environmental remediation are adequate. However, as regulatory standards under environmental laws are becoming increasingly stringent, there can be no assurance that future developments, additional information and experience gained will not cause the Company to incur material environmental liabilities or costs beyond those accrued in its condensed consolidated financial statements.

### ITEM 1A. RISK FACTORS.

There is no material change in the risk factors reported in Item 1A of the 2013 Form 10-K. This report contains certain forward-looking statements that reflect management's expectations regarding future events and operating performance and speak only as of the date hereof. These statements are subject to risks and uncertainties, which could cause actual results to differ materially. For a description of these risks see "Management's Discussion and Analysis of Financial Condition and Results of Operations – Forward-Looking Statements and Risk Factors."

## ITEM 2. UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS.

(a) During the period covered by this report, the Company did not sell any of its equity securities that were not registered under the Securities Act of 1933, as amended.

(b) Not applicable.

(c) The following table provides information with respect to purchases made by or on behalf of the Company or any “affiliated purchaser” of shares of the Company’s common stock.

(In thousands, except per share data)

Period	Total Number of Shares Purchased	Average Price Paid Per Share	Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs (1)	Approximate Dollar Value of Shares that May Yet Be Purchased Under the Plans or Programs (1)
February 1, 2014 to February 28, 2014	—	\$—	—	\$81,873
March 1, 2014 to March 31, 2014	—	—	—	81,873
April 1, 2014 to April 30, 2014	234	84.31	234	81,873
Total	234	\$84.31	234	

As noted in Note 4, Treasury Stock, to the accompanying condensed consolidated financial statements, the board of directors authorized amounts to be used to purchase shares of common stock over time, as market and business conditions warrant. There is no time restriction on these authorizations. In September 2013, the Company entered (1) into an Accelerated Share Repurchase (“ASR”) agreement with a third-party financial institution to repurchase \$125,000 of the Company’s common stock. This transaction was completed in the second quarter of fiscal year 2014. Under the agreement, the Company paid \$125,000 to the financial institution. Upon completion of the transaction, the Company had received a total of 1,573 shares with an average price per share of \$79.45.

In December 2013, the Company entered into a second ASR agreement with a third-party financial institution to repurchase \$125,000 of the Company’s common stock. This transaction was completed in the third quarter of fiscal year 2014. Under the agreement, the Company paid \$125,000 to the financial institution. Upon completion of the transaction, the Company received a total of 1,483 shares with an average price per share of \$84.31.

## ITEM 6. EXHIBITS.

See the Exhibit Index for a list of exhibits filed herewith or incorporated by reference herein.

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.

Pall Corporation

June 2, 2014

/s/ AKHIL JOHRI  
Akhil Johri  
Chief Financial Officer

45

---

EXHIBIT INDEX

Exhibit Number	Description of Exhibit
3(i)*	Restated Certificate of Incorporation of the Registrant as amended through September 1, 2010, filed as Exhibit 3.1(i) to the Registrant's Annual Report on Form 10-K for the fiscal year ended July 31, 2010.
3(ii)*	By-Laws of the Registrant as amended through December 12, 2012, filed as Exhibit 3.1(i) to the Registrant's Current Report on Form 8-K filed on December 17, 2012.
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 furnished pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
32.2†	Certification of Chief Financial Officer furnished pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
101.INS	XBRL Instance Document
101.SCH	XBRL Taxonomy Extension Schema Document
101.CAL	XBRL Taxonomy Extension Calculation Linkbase Document
101.LAB	XBRL Taxonomy Extension Label Linkbase Document
101.PRE	XBRL Taxonomy Extension Presentation Linkbase Document
101.DEF	XBRL Taxonomy Extension Definition Linkbase Document

\* Incorporated herein by reference.

† Exhibit filed herewith.