ZEBRA TECHNOLOGIES CORP
Form 10-Q
November 06, 2018
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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D. C. 20549
FORM 10-Q

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

For the quarterly period ended September 29, 2018

OR

¨ TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the transition period from to

Commission File Number: 000-19406

Zebra Technologies Corporation
(Exact name of registrant as specified in its charter)

| | |
|---|---|
| Delaware | 36-2675536 |
| (State or other jurisdiction of incorporation or organization) | (I.R.S. Employer Identification No.) |

3 Overlook Point, Lincolnshire, IL 60069
(Address of principal executive offices) (Zip Code)

Registrant’s telephone number, including area code: (847) 634-6700

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 ý 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 ý No ¨

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

| | |
|---|---|
| Large accelerated filer ý | Accelerated filer ¨ |
| Non-accelerated filer ¨ (Do not check if smaller reporting company) | Smaller reporting company ¨ |
| | Emerging growth company ¨ |

If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards pursuant to section 13(a) of the Exchange Act. ¨

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

As of October 30, 2018, there were 53,804,526 shares of Class A Common Stock, $.01 par value, outstanding.

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ZEBRA TECHNOLOGIES CORPORATION AND SUBSIDIARIES
QUARTER ENDED SEPTEMBER 29, 2018
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PART I - FINANCIAL INFORMATION

Item 1. Consolidated Financial Statements
ZEBRA TECHNOLOGIES CORPORATION AND SUBSIDIARIES
CONSOLIDATED BALANCE SHEETS
(In millions, except share data)

| | September 29, 2018 (Unaudited) | December 31, 2017 |
|---|---|---|
| Assets | | |
| Current assets: | | |
| Cash and cash equivalents | $ 45 | $ 62 |
| Accounts receivable, net of allowances for doubtful accounts of $3 million as of September 29, 2018 and December 31, 2017 | 575 | 479 |
| Inventories, net | 493 | 458 |
| Income tax receivable | 37 | 40 |
| Prepaid expenses and other current assets | 51 | 24 |
| Total Current assets | 1,201 | 1,063 |
| Property, plant and equipment, net | 251 | 264 |
| Goodwill | 2,496 | 2,465 |
| Other intangibles, net | 260 | 299 |
| Long-term deferred income taxes | 91 | 119 |
| Other long-term assets | 101 | 65 |
| Total Assets | $ 4,400 | $ 4,275 |
| Liabilities and Stockholders' Equity | | |
| Current liabilities: | | |
| Current portion of long-term debt | $ 71 | $ 51 |
| Accounts payable | 498 | 424 |
| Accrued liabilities | 285 | 296 |
| Deferred revenue | 199 | 186 |
| Income taxes payable | 52 | 43 |
| Total Current liabilities | 1,105 | 1,000 |
| Long-term debt | 1,829 | 2,176 |
| Long-term deferred revenue | 161 | 148 |
| Other long-term liabilities | 92 | 117 |
| Total Liabilities | 3,187 | 3,441 |
| Stockholders' Equity: | | |
| Preferred stock, $.01 par value; authorized 10,000,000 shares; none issued | — | — |
| Class A common stock, $.01 par value; authorized 150,000,000 shares; issued 72,151,857 shares | 1 | 1 |
| Additional paid-in capital | 282 | 257 |
| Treasury stock at cost, 18,349,215 and 18,915,762 shares at September 29, 2018 and December 31, 2017, respectively | (614) | (620) |
| Retained earnings | 1,573 | 1,248 |
| Accumulated other comprehensive income (loss) | (29) | (52) |
| Total Stockholders' Equity | 1,213 | 834 |
| Total Liabilities and Stockholders' Equity | $ 4,400 | $ 4,275 |

See accompanying Notes to Consolidated Financial Statements.

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ZEBRA TECHNOLOGIES CORPORATION AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF OPERATIONS
(In millions, except share data)
(Unaudited)

| | Three Months Ended | | Nine Months Ended | |
|---|---|---|---|---|
| | September 29, 2018 | September 30, 2017 | September 29, 2018 | September 30, 2017 |
| Net sales: | | | | |
| Tangible products | $959 | $ 810 | $2,687 | $ 2,324 |
| Services and software | 133 | 125 | 394 | 372 |
| Total Net sales | 1,092 | 935 | 3,081 | 2,696 |
| Cost of sales: | | | | |
| Tangible products | 495 | 420 | 1,368 | 1,207 |
| Services and software | 92 | 86 | 271 | 248 |
| Total Cost of sales | 587 | 506 | 1,639 | 1,455 |
| Gross profit | 505 | 429 | 1,442 | 1,241 |
| Operating expenses: | | | | |
| Selling and marketing | 120 | 113 | 361 | 336 |
| Research and development | 113 | 96 | 323 | 291 |
| General and administrative | 75 | 71 | 239 | 214 |
| Amortization of intangible assets | 25 | 49 | 71 | 151 |
| Acquisition and integration costs | 6 | 4 | 8 | 50 |
| Exit and restructuring costs | 4 | 5 | 9 | 10 |
| Total Operating expenses | 343 | 338 | 1,011 | 1,052 |
| Operating income | 162 | 91 | 431 | 189 |
| Other (expenses) income: | | | | |
| Foreign exchange (loss) gain | (1) | 1 | (5) | 2 |
| Interest expense, net | (18) | (95) | (52) | (176) |
| Other, net | — | (4) | 2 | (5) |
| Total Other expenses, net | (19) | (98) | (55) | (179) |
| Income (loss) before income tax | 143 | (7) | 376 | 10 |
| Income tax expense (benefit) | 16 | 5 | 70 | (3) |
| Net income (loss) | $127 | $ (12) | $306 | $ 13 |
| Basic earnings per share | $2.37 | $ (0.23) | $5.72 | $ 0.25 |
| Diluted earnings per share | $2.34 | $ (0.23) | $5.64 | $ 0.25 |

See accompanying Notes to Consolidated Financial Statements.

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ZEBRA TECHNOLOGIES CORPORATION AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME (LOSS)
(In millions)
(Unaudited)

| | Three Months Ended | | Nine Months Ended | |
|---|---|---|---|---|
| | September 29, 2018 | September 30, 2017 | September 29, 2018 | September 30, 2017 |
| Net income (loss) | $ 127 | $ (12 ) | $ 306 | $ 13 |
| Other comprehensive income (loss), net of tax: | | | | |
| Unrealized gain (loss) on anticipated sales hedging transactions | — | (1 ) | 22 | (15 ) |
| Unrealized gain on forward interest rate swap hedging transactions | 1 | 1 | 8 | 3 |
| Foreign currency translation adjustment | — | 2 | (7 ) | 2 |
| Comprehensive income (loss) | $ 128 | $ (10 ) | $ 329 | $ 3 |

See accompanying Notes to Consolidated Financial Statements.

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ZEBRA TECHNOLOGIES CORPORATION AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF CASH FLOWS
(In millions)
(Unaudited)

| | Nine Months Ended September 29, 2018 | September 30, 2017 |
|---|---|---|
| Cash flows from operating activities: | | |
| Net income | $ 306 | $ 13 |
| Adjustments to reconcile net income to net cash provided by operating activities: | | |
| Depreciation and amortization | 131 | 209 |
| Amortization of debt issuance costs and discounts | 12 | 30 |
| Share-based compensation | 34 | 25 |
| Debt extinguishment costs | 1 | 49 |
| Deferred income taxes | 17 | (19) |
| Unrealized gain on forward interest rate swaps | (24) | (2) |
| Other, net | 2 | 3 |
| Changes in operating assets and liabilities: | | |
| Accounts receivable, net | (93) | 38 |
| Inventories, net | (16) | (145) |
| Other assets | (10) | 19 |
| Accounts payable | 69 | 10 |
| Accrued liabilities | (5) | (2) |
| Deferred revenue | 28 | 25 |
| Income taxes | 2 | (37) |
| Other operating activities | 6 | (6) |
| Net cash provided by operating activities | 460 | 210 |
| Cash flows from investing activities: | | |
| Purchases of property, plant and equipment | (48) | (36) |
| Acquisition of businesses, net of cash acquired | (72) | — |

| | | | | |
|---|---|---|---|---|
| Proceeds from sale of long-term investments | 2 | | — | |
| Purchases of long-term investments | (2 | ) | (1 | ) |
| Net cash used in investing activities | (120 | ) | (37 | ) |
| Cash flows from financing activities: | | | | |
| Payment of debt issuance costs and discounts | (2 | ) | (5 | ) |
| Payments of long-term debt | (1,307 | ) | (1,373 | ) |
| Proceeds from issuance of long-term debt | 961 | | 1,186 | |
| Payments of debt extinguishment costs | (1 | ) | (49 | ) |
| Proceeds from exercise of stock options and stock purchase plan purchases | 8 | | 9 | |
| Taxes paid related to net share settlement of equity awards | (10 | ) | (5 | ) |
| Net cash used in financing activities | (351 | ) | (237 | ) |
| Effect of exchange rate changes on cash | (6 | ) | (4 | ) |
| Net decrease in cash and cash equivalents | (17 | ) | (68 | ) |
| Cash and cash equivalents at beginning of period | 62 | | 156 | |
| Cash and cash equivalents at end of period | $ 45 | | $ 88 | |
| Supplemental disclosures of cash flow information: | | | | |
| Income taxes paid | $ 46 | | $ 54 | |
| Interest paid | $ 73 | | $ 148 | |

See accompanying Notes to Consolidated Financial Statements.

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ZEBRA TECHNOLOGIES CORPORATION AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited)
Note 1 Description of Business and Basis of Presentation

Zebra Technologies Corporation and its wholly-owned subsidiaries (“Zebra” or the “Company”) is a global leader providing innovative Enterprise Asset Intelligence (“EAI”) solutions in the automatic identification and data capture solutions industry. We design, manufacture, and sell a broad range of products that capture and move data. We also provide a full range of services, including maintenance, technical support, repair, and managed services, including cloud-based subscriptions. End-users of our products and services include those in retail and e-commerce, transportation and logistics, manufacturing, healthcare, hospitality, warehouse and distribution, energy and utilities, and education industries around the world. We provide our products and services globally through a direct sales force and an extensive network of channel partners.

Management prepared these condensed unaudited interim consolidated financial statements according to the rules and regulations of the Securities and Exchange Commission (“SEC”) for interim financial information and notes. As permitted under Article 10 of Regulation S-X and the instructions of Form 10-Q, these condensed consolidated financial statements do not include all the information and notes required by United States Generally Accepted Accounting Principles (“GAAP”) for complete financial statements, although management believes that the disclosures made are adequate to make the information not misleading. These condensed consolidated financial statements should be read in conjunction with the audited consolidated financial statements and notes included in the Annual Report on Form 10-K for the fiscal year ended December 31, 2017.

The Company reclassified $41 million of costs from Accrued liabilities to Accounts payable on the Consolidated Balance Sheets for the period ended December 31, 2017 to conform to the current period presentation. A similar reclassification was made to the Consolidated Statements of Cash Flows resulting in a change to Accounts payable and Accrued liabilities within Net cash provided by operating activities for the period ended September 30, 2017.

In the opinion of the Company, these interim financial statements include all adjustments (of a normal, recurring nature) necessary to present fairly its Consolidated Balance Sheets as of September 29, 2018, the Consolidated Statements of Operations and Comprehensive Income for the three and nine-months ended September 29, 2018 and September 30, 2017, and the Consolidated Statements of Cash Flows for the nine-months ended September 29, 2018 and September 30, 2017. These results, however, are not necessarily indicative of the results expected for the full year ending December 31, 2018.

Note 2 Significant Accounting Policies

Revenue Recognition
Revenue includes sales of hardware, supplies and services (including repair services and product maintenance service contracts, which typically occur over time, and professional services such as installation, integration and provisioning, which typically occur in the early stages of a project). The average life of repair and maintenance service contracts is approximately three years. The duration of professional service arrangements range from a day to several weeks or months. We recognize revenues when we transfer control of promised goods or services to our customers in an amount that reflects the consideration to which we expect to receive in exchange for those goods or services.

The Company elects to exclude from the transaction price sales and other taxes assessed by a governmental authority and collected by the Company from a customer. The Company also considers shipping and handling activities as part of the fulfillment costs, not as a separate performance obligation.

Recently Adopted Accounting Pronouncements

On January 1, 2018, we adopted Accounting Standards Codification 606, Revenue from Contracts with Customers ("ASC 606") applying the modified retrospective method to those contracts which were not completed as of January 1, 2018. Results for reporting periods beginning after January 1, 2018 are presented under ASC 606, while prior period amounts are not adjusted and continue to be reported in accordance with our historic accounting under ASC 605, Revenue Recognition ("ASC 605"). The adoption of ASC 606 did not have a material effect on the Company's consolidated financial statements or results of operations.

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The cumulative effect of the changes made to our consolidated January 1, 2018 balance sheet related to the adoption of ASC 606 were as follows (in millions):

| | As Reported December 31, 2017 | Adjustment | As Adjusted January 1, 2018 |
|---|---|---|---|
| Assets: | | | |
| Inventories, net (1) | $ 458 | $ (3) | $ 455 |
| Prepaid expenses and other current assets (2) | 24 | 7 | 31 |
| Long-term deferred income taxes (3) | 119 | (5) | 114 |
| Other long-term assets (4) | 65 | 12 | 77 |
| | | | |
| Liabilities: | | | |
| Deferred revenue (5) | 186 | (2) | 184 |
| Long-term deferred revenue (6) | 148 | (6) | 142 |
| | | | |
| Stockholders' Equity: | | | |
| Retained earnings | 1,248 | 19 | 1,267 |

(1) Reflects an adjustment of $(3) million related to changes in revenue recognition patterns.
(2) Reflects an adjustment of $7 million related to changes in revenue recognition patterns.
(3) Reflects the income tax effect of $(5) million related to the adjustments made for the adoption of ASC 606.
(4) Reflects an adjustment of $12 million related to the capitalization of costs to obtain contracts (primarily comprised of sales commissions associated with longer term support service contracts).
(5) Reflects an adjustment of $(3) million related to reallocation of revenue between performance obligations and $1 million related to changes in the timing of revenue recognition.
(6) Reflects an adjustment of $(6) million related to reallocation of revenue between performance obligations.

Under the modified retrospective method of adoption, we are required to disclose the impact to the Consolidated Financial Statements had we continued to follow our accounting policies under the previous revenue recognition guidance. Had the Company applied the previous revenue recognition guidance, revenue would have been $1 million lower for the quarter ended September 29, 2018 and $3 million lower for the nine-month period ended September 29, 2018.

See Note 3, Revenues for further information.

In January 2016, the FASB issued ASU 2016-01, "Financial Instruments - Overall (Subtopic 825-10): Recognition and Measurement of Financial Assets and Financial Liabilities." On January 1, 2018, the Company adopted this ASU. ASU 2016-01 amends various aspects of the recognition, measurement, presentation, and disclosure for financial instruments. The adoption of this ASU did not have a material impact to the Company's consolidated financial statements or related disclosures.

Recently Issued Accounting Pronouncements Not Yet Adopted

In June 2016, the FASB issued ASU 2016-13, "Financial Instruments - Credit Losses (Topic 326): Measurement of Credit Losses on Financial Instruments." The new standard requires the measurement and recognition of expected credit losses for financial assets held at amortized cost. It replaces the existing incurred loss impairment model with an expected loss methodology, which will result in more timely recognition of credit losses. There are two transition methods available under the new standard dependent upon the type of financial instrument, either cumulative effect or prospective. The standard will be effective for the Company in the first quarter of 2020. Earlier adoption is permitted for annual periods beginning after December 15, 2018. Management has assessed the impact of adoption of the new standard and determined there will be no material impacts to the Company's consolidated financial statements or disclosures resulting from the adoption of this ASU, which we expect to adopt in the first quarter of 2020.

In February 2016, the FASB issued ASU 2016-02, "Leases (Subtopic 842)." Also, in July 2018, the FASB issued ASU 2018-11, "Leases (Subtopic 842): Targeted Improvements." Together, these ASUs increase the transparency and comparability of organizations by recognizing lease assets and liabilities on the Consolidated Balance Sheets and disclosing key quantitative and qualitative information about leasing arrangements. The principal difference from previous guidance is that the lease assets

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and lease liabilities arising from operating leases were not previously recognized in the Consolidated Balance Sheets. The recognition, measurement and cash flows arising from a lease by a lessee have not significantly changed. The ASUs will be effective for the Company in the first quarter of 2019, with early adoption permitted. In transition, lessees and lessors are required to recognize and measure leases at either the beginning of the earliest period presented or the beginning of the period adopted, using a modified retrospective approach. Management expects to elect to not adjust the comparative reporting periods, and apply the ASUs beginning in the period of adoption. In transition, there are also a number of optional practical expedients that entities may elect to apply. Management expects to elect certain practical expedients that it will apply upon transition, which principally include the election to not reassess existing or expired contracts to determine if such contracts contain a lease or if the lease classification would differ, as well as the election to not separate lease and non-lease components for arrangements where the Company is a lessee. While Management is currently assessing the impact of these elections and adoption of this standard on its consolidated financial statements, we have identified and collected data on our significant leases and selected a system to support future accounting and disclosure requirements. At this time, we do not have an estimate of the expected increase in assets and liabilities on the Company’s consolidated balance sheet upon adoption of these ASUs in the first quarter of 2019.

In August 2018, the FASB issued ASU 2018-15, “Intangibles - Goodwill and Other - Internal-Use Software (Subtopic 350-40): Customer’s Accounting for Implementation Costs Incurred in a Cloud Computing Arrangement That Is a Service Contract”. This ASU clarifies existing guidance related to implementation costs incurred in cloud computing arrangements, including the recognition, subsequent measurement, and financial statement presentation of such costs. The standard will be effective for the Company in the first quarter of 2020, with earlier adoption permitted. Management is still assessing the impact of adoption on its consolidated financial statements.

Note 3 Revenues

As prescribed in ASC 606, the Company recognizes revenue to depict the transfer of goods or services to a customer at an amount that reflects the consideration which the entity expects to receive in exchange for those goods or services.

Performance Obligations

We enter into contract arrangements that may include various combinations of tangible products and services, which generally are capable of being distinct and accounted for as separate performance obligations. For these types of contract arrangements, we evaluate whether two or more contracts should be combined and accounted for as one single contract and whether the combined or single contract has more than one performance obligation. This evaluation requires significant judgment and the decision to combine a group of contracts or separate the combined or single contract into multiple performance obligations could change the amount of revenue recorded in the reporting period. We use the accounting guidance on “capable of being distinct” and “distinct within the context of the contract” to assist with the aforementioned evaluation.

For contract arrangements that include multiple performance obligations, we allocate the total transaction price to each performance obligation in an amount based on the estimated relative standalone selling prices for the products and/or services underlying each performance obligation. When the standalone selling prices are not directly observable, we estimate the standalone selling prices primarily based on the expected cost-plus margin approach. For arrangements comprised strictly of the sale of product and performance of maintenance type services where the standalone selling price of the maintenance service is not discernible, we estimate the standalone selling price of the maintenance contract through the use of the residual approach. When the residual approach cannot be applied, regional pricing, marketing strategies and business practices are evaluated and analyzed to derive the estimated standalone selling price through the use of a cost-plus margin methodology.

The Company recognizes revenue when transfer of control has occurred for the goods or services sold. Control is deemed to have been transferred when the customer has the ability to direct the use of and has obtained substantially all of the remaining benefits from the goods and services sold. The Company uses judgment in the evaluation of the following criteria: 1) the customer simultaneously receives and consumes the benefits provided by the transfer of goods or service; 2) the performance creates or enhances an asset that is under control of the customer; 3) the performance does not create an asset with an alternative use to the customer; and 4) the Company has an enforceable right to payment, in order to determine whether control transfers at a point in time or over time. For each performance obligation satisfied over time, the Company measures its progress toward completion to determine the timing of revenue recognition. Judgment is also used in the evaluation of the following transfer of control criteria: 1) the Company has a present right to payment for the asset; 2) the legal title to the asset has transferred to the customer; 3) the customer has physical possession of the asset; 4) the customer has the significant risks and rewards of ownership of the asset; and 5) the customer has accepted the asset, in order to determine when revenue should be recognized in a point in time revenue recognition pattern. Assuming all other criteria for revenue recognition have been met, for products and services sold on a standalone basis, revenue is generally recognized upon shipment and by using an output

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method or time-based method respectively. In cases where a bundle of products and services are delivered to the customer, judgment is required to select the method of progress which best reflects the transfer of control.

The Company’s remaining obligations that are greater than one year in duration relate primarily to repair and support services. The aggregated transaction price allocated to remaining performance obligations related to these types of service arrangements was $457 million as of September 29, 2018. We expect to recognize these performance obligations over an approximate three-year average contract term.

For some of our transactions, products are sold with a right of return, and we may also provide other rebates, price protection, or incentives, which are accounted for as variable consideration. The Company estimates the amount of variable consideration by using the expected value or the most likely amount method and reduces the revenue by those estimated amounts, only to the extent it is probable that a significant reversal in the cumulative revenue recognized will not occur. These estimates are reviewed and updated, as necessary, at the end of each reporting period.

Revenue recognized in the reporting period from performance obligations satisfied in previous periods was not material for the three and nine-month periods ended September 29, 2018.

Disaggregation of Revenue

The following table presents our revenues disaggregated by product category for each of our segments, Asset Intelligence & Tracking (“AIT”) and Enterprise Visibility & Mobility (“EVM”), for the three and nine-months ended September 29, 2018 (in millions):

| | Three Months Ended September 29, 2018 | | | Nine Months Ended September 29, 2018 | | |
|---|---|---|---|---|---|---|
| | Product Category | | | Product Category | | |
| Segment | Tangible Products | Services and Software | Total | Tangible Products | Services and Software | Total |
| AIT | $325 | $ 28 | $353 | $960 | $ 96 | $1,056 |
| EVM | 634 | 105 | 739 | 1,727 | 298 | 2,025 |
| Total | $959 | $ 133 | $1,092 | $2,687 | $ 394 | $3,081 |

In addition, refer to Note 14, Segment Information for Net sales to customers by geographic region.

We recognize revenue arising from performance obligations outlined in contracts with our customers that are satisfied at a point in time and over time. Substantially all of our revenue for tangible products is recognized at a point in time, whereby revenue for services and software is predominantly recognized over time.

Contract Balances

Progress on satisfying performance obligations under contracts with customers and the related billings and cash collections are recorded on the Consolidated Balance Sheets in Accounts receivable, net and Prepaid expenses and other current assets. The opening and closing contract assets balances were $7 million and $5 million, as of January 1, 2018 and September 29, 2018, respectively, and were recorded within Prepaid expenses and other current assets on the Consolidated Balance Sheets. These contract assets result from timing differences between the billing schedule and the products and services delivery schedules, as well as, the impact from the allocation of the transaction price among performance obligations for contracts that include multiple performance obligations. Our policy is to test these contract asset balances for impairment in accordance with ASC 310 Receivables. No impairment losses have been recorded for the three and nine-month periods ended September 29, 2018.

Deferred revenue on the Consolidated Balance Sheets, consist of payments and billings in advance of our performance. The combined short-term and long-term deferred revenue balances were $360 million and $334 million at September 29, 2018 and December 31, 2017, respectively. During the three-month and nine-month period ended September 29, 2018, the Company recognized $32 million and $152 million in revenue respectively, which was previously included in the beginning balance of deferred revenue.

Our payment terms vary by the type and location of our customer and the products or services offered. The time between invoicing and when payment is due is not significant. In instances where the timing of revenue recognition differs from the timing of invoicing, we have determined that our contracts do not include a significant financing component.

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Costs to obtain a contract

Our incremental direct costs of obtaining a contract, which consist of sales commissions and incremental fringe benefits, are deferred and amortized over the weighted-average contract term, consistent with the guidance in ASC 340 Other Assets and Deferred Costs. The incremental costs to obtain a contract, which were previously expensed as incurred under ASC 605, and the determination of the amortization period are derived at a portfolio level and the amortization is recognized on a straight-line basis. The adoption of ASC 606 required the capitalization of these costs which resulted in an adjustment to increase retained earnings. The Company recorded a $12 million increase to Other long-term assets on the Consolidated Balance Sheet as of January 1, 2018. The Company recognized amortization expense related to commissions during the three-month and nine-month period ended September 29, 2018 of $2 million and $7 million, respectively. The ending balance of the deferred commissions was $13 million as of September 29, 2018. The Company elected a practical expedient permitted by ASC 606, whereby the incremental costs of obtaining a contract are expensed as incurred if the amortization period of the assets would otherwise be one year or less.

Note 4 Inventories

Inventories are stated at the lower of a moving-average cost (which approximates cost on a first-in, first-out basis) and net realizable value. Manufactured inventory cost includes materials, labor, and manufacturing overhead. Purchased inventory cost also includes internal purchasing overhead costs.

Provisions are made to reduce excess and obsolete inventories to their estimated net realizable values. Inventory provisions are based on forecasted demand, experience with specific customers, the age and nature of the inventory, and the ability to redistribute inventory to other programs or to rework into consumable inventory.

The components of Inventories, net are as follows (in millions):

| | September 29, 2018 | December 31, 2017 |
|---|---|---|
| Raw material | $ 132 | $ 116 |
| Work in process | 5 | 1 |
| Finished goods | 356 | 341 |
| Total | $ 493 | $ 458 |

Note 5 Business Acquisition

On August 14, 2018, the Company acquired all outstanding equity interests of Xplore Technologies Corporation (“Xplore”). The Xplore business designs, integrates, and markets rugged tablets that are primarily used by industrial, government, and field service organizations. The acquisition of Xplore was intended to expand the Company’s portfolio of mobile computing devices to serve a wider range of customers.

The Xplore acquisition was accounted for under the acquisition method of accounting for business combinations. In connection with this acquisition, the Company paid $87 million in cash during the third quarter of 2018, which included, $72 million for the net assets acquired, a $9 million payment of Xplore debt as well as $6 million of other Xplore transaction-related obligations. Additionally, we incurred $6 million of cash acquisition-related costs during the third quarter (primarily third-party transaction and advisory fees), which are reflected as Acquisition and integration costs on the Consolidated Statements of Operations.

The Company utilized estimated fair values as of August 14, 2018 to allocate the total consideration paid to the net tangible and intangible assets acquired and liabilities assumed. The fair value of these net assets acquired was based on a number of estimates and assumptions as well as customary valuation procedures and techniques. While we believe these estimates provide a reasonable basis to record the net assets acquired, the purchase price allocation is considered preliminary and subject to adjustment during the measurement period, which is up to one year from the acquisition date of August 14, 2018. The primary fair value estimates considered preliminary are identifiable intangible assets, inventory, and income tax-related items.

The preliminary opening balance sheet of Xplore was included in the Company's Consolidated Balance Sheet and operating results beginning August 14, 2018. The Company has not included unaudited pro forma results, as if Xplore had been acquired as of January 1, 2018, as it would not yield materially different results.

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The preliminary purchase price allocation to assets acquired and liabilities assumed was as follows (in millions):

| | |
|---|---|
| Accounts receivable | $10 |
| Inventory | 23 |
| Identifiable intangible assets | 32 |
| Other assets acquired | 4 |
| Debt | (9 ) |
| Accounts payable | (8 ) |
| Deferred revenues | (7 ) |
| Other liabilities assumed | (6 ) |
| Net Assets Acquired | $39 |
| Goodwill on acquisition | 33 |
| Total consideration | $72 |

The $33 million of goodwill will be non-deductible for tax purposes. The goodwill principally relates to the planned expansion of the Xplore product offerings into current and new markets. This goodwill has been allocated to the EVM segment.

The preliminary purchase price allocation to identifiable intangible assets acquired was:

| | Fair Value (in millions) | Life (in years) |
|---|---|---|
| Customer-related assets | $ 16 | 9 |
| Technology-based assets | 15 | 7 |
| Trademarks | 1 | 3 |
| Total identifiable intangible assets | $ 32 | |

Note 6 Costs Associated with Exit and Restructuring Activities

In the first quarter of 2017, the Company's executive leadership approved an initiative to continue the Company's efforts to increase operational efficiency (the "Productivity Plan"). The Company expects the Productivity Plan to build upon the exit and restructuring initiatives specific to the October 2014 acquisition of the Enterprise business from Motorola Solutions, Inc. (the "Acquisition Plan"). The Company substantially completed all initiatives under the Acquisition Plan as of December 31, 2017. Actions under the Productivity Plan include organizational design changes, process improvements and automation. Exit and restructuring costs are not included in the operating results of our segments as they do not impact the specific segment measures as reviewed by our Chief Operating Decision Maker and therefore are reported as a component of Corporate, eliminations. See Note 14, Segment Information.

Total exit and restructuring charges of $21 million life-to-date specific to the Productivity Plan have been recorded through September 29, 2018 and relate to employee severance and related benefits and other expenses. Exit and restructuring charges of $4 million and $9 million were recorded in the respective three and nine-month periods ended September 29, 2018. Total remaining charges associated with this plan are expected to be less than $2 million with activities expected to be substantially complete by the end of fiscal 2018.

A rollforward of the exit and restructuring accruals is as follows (in millions):

| | Three Months Ended | | Nine Months Ended | |
|---|---|---|---|---|
| | September 29, 2018 | September 30, 2017 | September 29, 2018 | September 30, 2017 |
| Balance at the beginning of the period | $ 4 | $ 7 | $ 8 | $ 10 |
| Charged to earnings | 4 | 5 | 9 | 10 |
| Cash paid | (3 ) | (4 ) | (12 ) | (12 ) |
| Balance at the end of the period | $ 5 | $ 8 | $ 5 | $ 8 |

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The $5 million accrual as of September 29, 2018 is reflected within the Consolidated Balance Sheet as $4 million within Accrued liabilities and $1 million within Other long-term liabilities. The long-term portion of the accrual relates to non-cancellable lease payments associated with exited facilities whose latest term expires May 2021.

Note 7 Fair Value Measurements

Financial assets and liabilities are measured using inputs from three levels of the fair value hierarchy in accordance with ASC Topic 820, "Fair Value Measurements." Fair value is defined as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. It establishes a fair value hierarchy that prioritizes observable and unobservable inputs used to measure fair value into the following three broad levels:

Level 1: Quoted prices in active markets that are accessible at the measurement date for identical assets or liabilities. The fair value hierarchy gives the highest priority to Level 1 inputs (e.g. U.S. Treasuries & money market funds).

Level 2: Observable prices that are based on inputs not quoted on active markets but corroborated by market data.

Level 3: Unobservable inputs are used when little or no market data is available. The fair value hierarchy gives the lowest priority to Level 3 inputs.

In determining fair value, the Company utilizes valuation techniques that maximize the use of observable inputs and minimize the use of unobservable inputs to the extent possible. In addition, the Company considers counterparty credit risk in the assessment of fair value.

Financial assets and liabilities carried at fair value as of September 29, 2018, are classified below (in millions):

| | Level 1 | Level 2 | Level 3 | Total |
|---|---|---|---|---|
| Assets: | | | | |
| Foreign exchange contracts (1) | $ — | $ 16 | $ — | $ 16 |
| Forward interest rate swap contracts (2) | — | 14 | — | 14 |
| Money market investments related to the deferred compensation plan | 18 | — | — | 18 |
| Total Assets at fair value | $ 18 | $ 30 | $ — | $ 48 |
| Liabilities: | | | | |
| Liabilities related to the deferred compensation plan | 18 | — | — | 18 |
| Total Liabilities at fair value | $ 18 | $ — | $ — | $ 18 |

Financial assets and liabilities carried at fair value as of December 31, 2017, are classified below (in millions):

| | Level 1 | Level 2 | Level 3 | Total |
|---|---|---|---|---|
| Assets: | | | | |
| Money market investments related to the deferred compensation plan | $ 15 | $ — | $ — | $ 15 |
| Total Assets at fair value | $ 15 | $ — | $ — | $ 15 |
| Liabilities: | | | | |
| Forward interest rate swap contracts (2) | $ — | $ 18 | $ — | $ 18 |
| Foreign exchange contracts (1) | 2 | 9 | — | 11 |
| Liabilities related to the deferred compensation plan | 15 | — | — | 15 |
| Total Liabilities at fair value | $ 17 | $ 27 | $ — | $ 44 |

(1) The fair value of the foreign exchange contracts is calculated as follows:

a. Fair value of a put option contract associated with forecasted sales hedges is calculated using bid and ask rates for similar contracts.

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b. Fair value of regular forward contracts associated with forecasted sales hedges is calculated using the period-end exchange rate adjusted for current forward points.

c. Fair value of hedges against net assets is calculated at the period-end exchange rate adjusted for current forward points unless the hedge has been traded but not settled at period end (Level 2). If this is the case, the fair value is calculated at the rate at which the hedge is being settled (Level 1).

(2) The fair value of forward interest rate swaps is based upon a valuation model that uses relevant observable market inputs at the quoted intervals, such as forward yield curves, and is adjusted for the Company's credit risk and the interest rate swap terms. See gross balance reporting in Note 8, Derivative Instruments.

Note 8 Derivative Instruments

In the normal course of business, the Company is exposed to global market risks, including the effects of changes in foreign currency exchange rates and interest rates. The Company uses derivative instruments to manage its exposure to such risks and may elect to designate certain derivatives as hedging instruments under ASC 815, Derivatives and Hedging. The Company formally documents all relationships between designated hedging instruments and hedged items as well as its risk management objectives and strategies for undertaking hedge transactions. The Company does not hold or issue derivatives for trading or speculative purposes.

In accordance with ASC 815, the Company recognizes derivative instruments as either assets or liabilities on the Consolidated Balance Sheets and measures them at fair value. The following table presents the fair value of its derivative instruments (in millions):

| | Asset / (Liability) | | |
|---|---|---|---|
| | | Fair Values as of | |
| | Balance Sheet Classification | September 29, 2018 | December 31, 2017 |
| Derivative instruments designated as hedges: | | | |
| Foreign exchange contracts | Prepaid expenses and other current assets | $ 15 | $ — |
| Foreign exchange contracts | Accrued liabilities | — | (9) |
| Forward interest rate swaps | Accrued liabilities | (1) | (2) |
| Forward interest rate swaps | Other long-term liabilities | — | (8) |
| Total derivative instruments designated as hedges | | $ 14 | $ (19) |
| Derivative instruments not designated as hedges: | | | |
| Foreign exchange contracts | Prepaid expenses and other current assets | $ 1 | $ — |
| Forward interest rate swaps | Other long-term assets | 17 | — |
| Foreign exchange contracts | Accrued liabilities | — | (2) |
| Forward interest rate swaps | Accrued liabilities | (2) | (1) |
| Forward interest rate swaps | Other long-term liabilities | — | (7) |
| Total derivative instruments not designated as hedges | | $ 16 | $ (10) |
| Total net derivative asset (liability) | | $ 30 | $ (29) |

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The following table presents the gains (losses) from changes in fair values of derivatives that are not designated as hedges (in millions):

| | Gain (Loss) Recognized in Income | | | | |
|---|---|---|---|---|---|
| | | Three Months Ended | | Nine Months Ended | |
| | Statements of Operations Classification | September 29, 2018 | September 30, 2017 | September 29, 2018 | September 30, 2017 |
| Derivative instruments not designated as hedges: | | | | | |
| Foreign exchange contracts | Foreign exchange (loss) gain | $ 1 | $ (6 ) | $ 2 | $ (22 ) |
| Forward interest rate swaps | Interest expense, net | 6 | 1 | 24 | 2 |
| Total gain (loss) recognized in income | | $ 7 | $ (5 ) | $ 26 | $ (20 ) |

Activities related to derivative instruments are reflected within Net cash provided by operating activities within the Statements of Cash Flows.

Credit and Market Risk Management

Financial instruments, including derivatives, expose the Company to counterparty credit risk of nonperformance and to market risk related to currency exchange rate and interest rate fluctuations. The Company manages its exposure to counterparty credit risk by establishing minimum credit standards, diversifying its counterparties, and monitoring its concentrations of credit. The Company's counterparties are commercial banks with expertise in derivative financial instruments. The Company evaluates the impact of market risk on the fair value and cash flows of its derivative and other financial instruments by considering reasonably possible changes in interest rates and currency exchange rates. The Company continually monitors the creditworthiness of the customers to which it grants credit terms in the normal course of business. The terms and conditions of the Company's credit policies are designed to mitigate or eliminate concentrations of credit risk with any single customer.

The Company's master netting and other similar arrangements with the respective counterparties allow for net settlement under certain conditions, which are designed to reduce credit risk by permitting net settlement with the same counterparty. We elect to present the assets and liabilities of our derivative financial instruments on a net basis on the Consolidated Balance Sheets. If the derivative financial instruments had been presented gross on the Consolidated Balance Sheets, the asset and liability positions each would have been increased by $1 million as of September 29, 2018 and $11 million at December 31, 2017, respectively.

Foreign Currency Exchange Risk Management

The Company conducts business on a multinational basis in a wide variety of foreign currencies. Exposure to market risk for changes in foreign currency exchange rates arises from euro denominated external revenues, cross-border financing activities between subsidiaries, and foreign currency denominated monetary assets and liabilities. The Company manages its objective of preserving the economic value of non-functional currency denominated cash flows by initially hedging transaction exposures with natural offsets to the fullest extent possible and, once these opportunities have been exhausted, through foreign exchange forward and option contracts.

The Company manages the exchange rate risk of anticipated euro denominated sales using forward contracts which typically mature within twelve months of execution. The Company designates these derivative contracts as cash flow hedges. Unrealized gains and losses on these contracts are deferred in Accumulated other comprehensive income (loss) ("AOCI") on the Company's Consolidated Balance Sheets until the contract is settled and the hedged sale is realized. The realized gain or loss is then recorded as an adjustment to Net sales on the Consolidated Statements of Operations. Realized amounts reclassified to Net sales were a $7 million gain and a $5 million loss for the quarter ending September 29, 2018 and September 30, 2017, respectively. For the comparable nine-month period ended

September 29, 2018 and September 30, 2017, realized amounts reclassified to Net sales were a $1 million gain and a $4 million loss, respectively. As of September 29, 2018, and December 31, 2017, the notional amounts of the Company's foreign exchange cash flow hedges were €449 million and €389 million, respectively. The Company has reviewed cash flow hedges for effectiveness and determined they are highly effective.

The Company uses forward contracts, which are not designated as hedging instruments, to manage its balance sheet exposures related to its Brazilian real, British pound, Euro, Canadian dollar, Czech koruna, Australian dollar, Swedish krona, Japanese yen Singapore dollars, Mexican Peso and Chinese Yuan denominated net assets. These forward contracts typically mature within one-month after execution. Monetary gains and losses on these forward contracts are recorded in income each quarter and are

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generally offset by the transaction gains and losses related to their net asset positions. The notional values and the net fair value of these outstanding contracts are as follows (in millions):

| | September 29, 2018 | | December 31, 2017 | |
|---|---|---|---|---|
| Notional balance of outstanding contracts: | | | | |
| British Pound/U.S. Dollar | £ | 7 | £ | 13 |
| Euro/U.S. Dollar | € | — | € | 108 |
| British Pound/Euro | £ | — | £ | 5 |
| Canadian Dollar/U.S. Dollar | $ | 2 | $ | 12 |
| Czech Koruna/U.S. Dollar | Kč | | Kč | 361 |
| Brazilian Real/U.S. Dollar | R$ | — | R$ | 34 |
| Australian Dollar/U.S. Dollar | A$ | 26 | A$ | 55 |
| Swedish Krona/U.S. Dollar | kr | — | kr | 13 |
| Japanese Yen/U.S. Dollar | ¥ | 166 | ¥ | 151 |
| Singapore Dollar/U.S. Dollar | S$ | 6 | S$ | 4 |
| Mexican Peso/U.S. Dollar | Mex$ | 124 | Mex$ | |
| Chinese Yuan/U.S. Dollar | ¥ | 59 | ¥ | |
| Net fair value of asset (liability) of outstanding contracts | $ | 1 | $ | (2 ) |

The Company has significantly reduced the use of non-designated forward contracts to manage Euro exposure in the current period. In August 2018, the Company made a Euro denominated borrowing on the Revolving Credit Facility. See Note 9, Long-Term Debt. The Euro borrowing will predominately function as the hedge on the Euro exposure.

Interest Rate Risk Management

The Company's debt consists of borrowings under two term loans ("Term Loan A" and "Term Loan B"), the Revolving Credit Facility and the receivables financing facility which bear interest at variable rates plus an applicable margin. See Note 9, Long-Term Debt. As a result, the Company is exposed to market risk associated with the variable interest rate payments on the term loans, revolving credit facility and receivables financing facility.

The Company manages its exposure to changes in interest rates by utilizing interest rate swaps to hedge this exposure and to achieve a desired proportion of fixed versus floating-rate debt, based on current and projected market conditions. The Company does not enter into derivative instruments for trading or speculative purposes.

In December 2017, the Company entered into an $800 million forward long-term interest rate swap agreement to lock into a fixed LIBOR interest rate base for debt facilities subject to monthly interest payments, including Term Loan A, the Revolving Credit Facility and receivables financing facility. Under the terms of the agreement, $800 million in variable-rate debt will be swapped for a fixed interest rate with net settlement terms due effective in December 2018. The changes in fair value of these swaps are not designated as hedges and are recognized immediately as Interest expense, net on the Consolidated Statements of Operations.

The Company previously had a floating-to-fixed interest rate swap, which was designated as a cash flow hedge. This swap was terminated and hedge accounting treatment was discontinued in 2014. The terminated swap has approximately $3 million remaining to be amortized through AOCI on the Consolidated Balance Sheets and subsequently reclassified into Interest expense, net, on the Consolidated Statements of Operations through June 2021. There was less than $1 million expensed by the Company in the third quarter of 2018 and $1 million expensed for the nine-month period ended September 29, 2018.

The Company has three interest rate swaps related to Term Loan B previously entered into for the purpose of converting floating-rate debt to fixed-rate debt. The first swap was entered into with a syndicated group of commercial banks for the purpose of fixing the interest rate on the Company's floating-rate debt. The second swap largely offsets the first swap, causing interest payments to again be exposed to rate fluctuations. Neither of these instruments are designated as accounting hedges and changes in fair value are recognized in Interest expense, net on the Consolidated Statements of Operations. The third interest rate swap converting the floating-rate debt to fixed-rate debt was designated as a cash flow hedge and receives hedge accounting treatment. All three swaps have a termination date in June 2021. The Company has determined the third swap to be

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highly effective. At September 29, 2018, the Company estimated that approximately $1 million in losses on the third swap will be reclassified from AOCI on the Consolidated Balance Sheets into Interest expense, net during the next twelve months.

The interest rate swaps have future maturities consisting of the following notional amounts per year (in millions):

| | |
|---|---|
| Year 2018 | $— |
| Year 2019 | 1,344 |
| Year 2020 | 1,072 |
| Year 2021 | 1,072 |
| Year 2022 | 800 |
| Notional balance of outstanding contracts | $4,288 |

Note 9 Long-Term Debt

The following table summarizes the carrying value of the Company's long-term debt (in millions):

| | September 29, 2018 | December 31, 2017 |
|---|---|---|
| Term Loan B | $ 695 | $ 1,160 |
| Term Loan A | 608 | 679 |
| Revolving Credit Facility | 473 | 275 |
| Receivables Financing Facility | 136 | 135 |
| Total debt | $ 1,912 | $ 2,249 |
| Less: Debt issuance costs | (5) | (7) |
| Less: Unamortized discounts | (7) | (15) |
| Less: Current portion of long-term debt | (71) | (51) |
| Total long-term debt | $ 1,829 | $ 2,176 |

At September 29, 2018, the future maturities of debt, excluding debt discounts and issuance costs, are as follows (in millions):

| | |
|---|---|
| 2018 | $— |
| 2019 | 153 |
| 2020 | 54 |
| 2021 | 1,705 |
| 2022 | — |
| Thereafter | — |
| Total future maturities of long-term debt | $1,912 |

The estimated fair value of the Company's long-term debt approximated $1.9 billion at September 29, 2018 and $2.2 billion at December 31, 2017. These fair value amounts, developed based on inputs classified as Level 2 within the fair value hierarchy, represent the estimated value at which the Company's lenders could trade its debt within the financial markets and does not represent the settlement value of these long-term debt liabilities to the Company. The fair value of the long-term debt will continue to vary each period based a number of factors including fluctuations in market interest rates, as well as changes to the Company's credit ratings.

Credit Facilities

On May 31, 2018, the Company entered into Amendment No.1. to the Amended and Restated Credit Agreement ("Amendment No. 1"). Amendment No. 1 replaced the existing Term Loan A with a new Term Loan A ("Amended Term Loan A") of $670 million and increased the existing revolving credit facility from $500 million to $800 million ("Revolving Credit Facility"). Additionally, Amendment No. 1 provides for the capacity to make Euro denominated draws on the Revolving Credit Facility. As part of the Amendment No. 1, the Company entered into a partial early debt termination of $300 million and repricing of Term Loan B. Amendment No. 1 lowered the index rate spread for LIBOR loans from LIBOR + 200 bp to LIBOR + 175 bp.

In accounting for the impact of Amendment No. 1, the Company applied the provisions of ASC Subtopic 470-50, Modifications and Extinguishments ("ASC 470-50"), which resulted in the second quarter results including approximately $6 million in non-

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cash accelerated amortization of debt issuance costs and approximately $1 million of one-time pretax charges related to third party fees associated with the amendments, which are reflected as a component of Interest expense, net within the Company’s Consolidated Statements of Operations.

In addition, the issuance of Amended Term Loan A and the increase to the Revolving Credit Facility resulted in $2 million of one-time third party fees for arranger, legal, and other services, which were capitalized and will be amortized over the term of the credit facilities.

As of September 29, 2018, the Term Loan A interest rate was 3.99%, and the Term Loan B interest rate was 4.06%. Borrowings under Term Loan A and B bear interest at a variable rate. Term Loan B borrowings are subject to a floor of 2.75%. Interest payments are payable monthly or quarterly on Term Loan A and quarterly on Term Loan B. The Company has entered into interest rate swaps to manage interest rate risk on Term Loan B. See Note 8, Derivative Instruments.

Amendment No. 1 also requires the Company to prepay certain amounts in the event of certain circumstances or transactions. The Company may make prepayments against the Term Loans, in whole or in part, without premium or penalty. Under Amendment No. 1, Term Loan A will mature on July 27, 2021 and Term Loan B will mature on October 27, 2021.

The Revolving Credit Facility is available for working capital and other general corporate purposes including letters of credit. As of September 29, 2018, the Company had issued letters of credit totaling $5 million, which reduced funds available for other borrowings under the agreement to $795 million. Borrowings bear interest at a variable rate plus an applicable margin. As of September 29, 2018, the Revolving Credit Facility had an average interest rate of 3.45%. Interest payments are payable monthly or quarterly for the Revolving Credit Facility. In August 2018, the Company made a Euro denominated draw on the Revolving Credit Facility. The Revolving Credit Facility will mature and the related commitments will terminate on July 27, 2021.

Receivables Financing Facility
In December 2017, the Company entered into a receivables financing facility with a financial institution that has a borrowing limit of up to $180 million. As collateral, the Company pledges a perfected first-priority security interest in its domestically originated accounts receivable. The Company has accounted for transactions under this receivable financing facility as secured borrowings.

At September 29, 2018, the Company’s Consolidated Balance Sheets included $427 million of receivables that were pledged under the receivables financing facility, of which $136 million had been borrowed. Borrowings bear interest at a variable rate plus an applicable margin. As of September 29, 2018, the receivables financing facility had an average interest rate of 3.07% and requires monthly interest payments. The receivables financing facility will mature on November 29, 2019.

Both the Revolving Credit Facility and receivables financing facility include terms and conditions that limit the incurrence of additional borrowings and require that certain financial ratios be maintained at designated levels.

On September 29, 2018, the Company was in compliance with all debt covenants.

Note 10 Commitments and Contingencies

Warranties

In general, the Company provides warranty coverage of 1 year on mobile computers, printers and batteries. Advanced data capture products are warrantied from 1 to 5 years, depending on the product. Thermal printheads are warrantied for 6 months and battery-based products, such as location tags, are covered by a 90-day warranty. The provision for warranty expense is adjusted quarterly based on historical warranty experience.

The following table is a summary of the Company’s accrued warranty obligation (in millions):

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| | Nine Months Ended | |
|---|---|---|
| | September 29, 2018 | September 30, 2017 |
| Balance at the beginning of the period | $ 18 | $ 21 |
| Warranty expense | 25 | 21 |
| Warranty payments | (23 ) | (23 ) |
| Balance at the end of the period | $ 20 | $ 19 |

Contingencies

The Company is subject to a variety of investigations, claims, suits, and other legal proceedings that arise from time to time in the ordinary course of business, including but not limited to, intellectual property, employment, tort, and breach of contract matters. The Company currently believes that the outcomes of such proceedings, individually and in the aggregate, will not have a material adverse impact on its business, cash flows, financial position, or results of operations. Any legal proceedings are subject to inherent uncertainties, and the Company's view of these matters and its potential effects may change in the future. The Company establishes an accrued liability for loss contingencies related to legal matters when the loss is both probable and estimable. In addition, for some matters for which a loss is probable or reasonably possible, an estimate of the amount of loss or range of loss is not possible, and we may be unable to estimate the possible loss or range of losses that could potentially result from the application of non-monetary remedies.

In connection with the acquisition of the Enterprise business from Motorola Solutions, Inc., the Company acquired Symbol Technologies, Inc., a subsidiary of Motorola Solutions ("Symbol"). A putative federal class action lawsuit, Waring v. Symbol Technologies, Inc., et al., was filed on August 16, 2005 against Symbol Technologies, Inc. and two of its former officers in the United States District Court for the Eastern District of New York by Robert Waring. After the filing of the Waring action, several additional purported class actions were filed against Symbol and the same former officers making substantially similar allegations (collectively, "the New Class Actions"). The Waring action and the New Class Actions were consolidated for all purposes and on April 26, 2006, the Court appointed the Iron Workers Local # 580 Pension Fund as lead plaintiff and approved its retention of lead counsel on behalf of the putative class. At a mediation held on March 15, 2018, the parties reached an agreement in principle to settle the matter, and Zebra reached agreements with certain of its insurers to fund the settlement and therefore, no amounts have been recorded. On October 30, 2018, the Court entered the Final Judgment Approving Class Action Settlement and Order of Dismissal with Prejudice.

Unclaimed Property Voluntary Disclosure Agreement ("VDA") and Audits: The Company is currently under audit by several states related to its reporting of unclaimed property liabilities. Additionally, in December 2017, the Company entered into a VDA with the State of Delaware. The Company has engaged an outside consultant to facilitate the assessment of the estimated liability that may result from these activities. As of September 29, 2018, the Company does not expect these unclaimed property audits to have a material impact on its results of operations.

Note 11 Income Taxes

The Company's effective tax rates for the three-month and nine-month periods ended September 29, 2018 were 11.2% and 18.6%, respectively. The variances from the 2018 federal statutory rate of 21% for the three and nine months ended September 29, 2018 were attributable to the effect of lower tax rates in foreign jurisdictions and the generation of tax credits. These benefits were partially offset by increases related to foreign earnings subject to U.S. taxation, the U.S. impact of the Enterprise acquisition and certain discrete items. The discrete items included the favorable impacts of share-based compensation, adjustments to the one-time transition tax related to the Tax Cuts and Jobs Act enacted in December 2017 (“U.S. Tax Reform” or “the Act”) offset by audit settlements with the U.S. Internal Revenue Service for fiscal years 2013, 2014, and 2015 and an increase in uncertain tax positions resulting from interpretative guidance issued during the second quarter of 2018.

In the prior year, the effective tax rates for the three and nine-month periods ended September 30, 2017 were (71.4)% and (30.0)%, respectively. The variances from the 2017 federal statutory rate of 35% for the three and nine months ended September 30, 2017 were attributable to pre-tax losses in the U.S., lower tax rates in foreign jurisdictions, the generation of tax credits, and the impact of certain discrete items, which were partially offset by the U.S. impact of the Enterprise acquisition and state deferred tax expense due to changes in our business operations. The discrete items included the favorable impacts of share-based compensation as well as benefits associated with an intercompany sale of intellectual property and a rate decrease in Singapore.

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The Company earns a significant amount of its operating income outside of the U.S. The Company's policy considers its U.S. investment in directly-owned foreign affiliates to be indefinitely reinvested. Under the Act, future remittance of dividends from foreign subsidiaries to the U.S. parent will generally no longer be subject to U.S. tax when repatriated, but may be subject to withholding taxes of the payor affiliate country. Additionally, gains and losses on taxable dispositions of U.S.-owned foreign affiliates continue to be subject to U.S. tax.

Pre-tax earnings outside the United States are primarily generated in the United Kingdom, Singapore, and Luxembourg, with statutory rates of 19%, 17%, and 27%, respectively. During 2017, the Company received approval from the Singapore Economic Development Board for a tax rate of 10% with the Company's commitment to make increased investments in Singapore. The Singapore incentivized rate expires on December 31, 2018.

Quarterly, Management evaluates all jurisdictions based on historical pre-tax earnings and taxable income to determine the need for valuation allowances. Based on this analysis, a valuation allowance has been recorded for any jurisdictions where, in the Company's judgment, tax benefits will not be realized.

As part of the purchase price allocation of the stock acquisition of Xplore in the current period, the Company recorded $2 million in deferred tax assets associated with the difference between fair market value of the net assets acquired and carry-over tax basis. See Note 5 Business Acquisition.

Uncertain Tax Positions

During the third quarter of 2018, the Company settled the U.S. income tax audits for fiscal years 2013, 2014, and 2015. The settlement resulted in an incremental $2 million income tax expense including the reversal of $12 million in previously recorded unrecognized tax benefits. During the nine months ended September 29, 2018, the Company recorded a $14 million charge related to increases in income tax uncertainties for prior year tax positions, including interest and penalties. The Company is currently undergoing a UK income tax audit for fiscal years 2012 and 2014. Fiscal years 2004 through 2017 remain open to examination by multiple foreign and U.S. state taxing jurisdictions. The Company continues to believe its tax positions are supportable, however, the Company anticipates that $22 million of uncertain tax benefits may be disallowed within the next twelve months and has reflected this liability as current within the Company's Consolidated Balance Sheets. Due to uncertainties in any tax audit or litigation outcome, the Company's estimates of the ultimate settlement of uncertain tax positions may change and the actual tax benefits may differ significantly from the estimates.

Impact of U.S. Tax Reform

Enacted on December 22, 2017, the Act reduced the U.S. federal corporate tax rate from 35% to 21%, and requires companies to pay a one-time transition tax on earnings of certain foreign subsidiaries that were previously tax deferred. Based on current operations, we estimate that the Company is subject to the Global Intangible Low-Taxed Income and the Deduction for Foreign-Derived Intangible Income provisions of the Act. We estimate that the new limitations which defer U.S. interest deductions in excess of 30% of Adjusted Taxable Income are not applicable. Additionally, the Company is no longer able to deduct performance-based compensation for its covered employees which exceeds the limitation under Internal Revenue Code Section 162(m). These impacts are included in the calculation of our annual estimated effective tax rate.

The Company has updated its calculation of the one-time transition tax to a total liability of $34 million and recorded a $3 million benefit in the nine-month period ended September 29, 2018. The Company utilized a total of $27 million of available net operating losses, research and developments credits, alternative minimum tax credits, and foreign tax credits resulting in a liability of $7 million.

At September 29, 2018, in addition to the one-time transition tax, we continue to analyze the final impacts related to performance-based compensation for covered employees as well as accounting for the state income tax effects of enactment of the Act. The Company remeasured U.S. deferred tax assets and liabilities based on the rates at which they are expected to reverse in the future, which is generally 21%. However, the remeasurement of deferred taxes requires further analysis regarding the state tax impacts.

Note 12 Earnings per Share

Basic net earnings per share is calculated by dividing net income by the weighted average number of common shares outstanding for the period. Diluted earnings per share is computed by dividing net income by the weighted average number of shares assuming dilution. Dilutive common shares outstanding is computed using the Treasury Stock method and in periods of income, reflects the additional shares that would be outstanding if dilutive stock options were exercised for common shares during the period.

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Earnings per share (in millions, except share data):

| | Three Months Ended September 29, 2018 | Three Months Ended September 30, 2017 | Nine Months Ended September 29, 2018 | Nine Months Ended September 30, 2017 |
|---|---|---|---|---|
| Basic: | | | | |
| Net income (loss) | $ 127 | $ (12 ) | $ 306 | $ 13 |
| Weighted-average shares outstanding | 53,740,174 | 52,420,868 | 53,516,859 | 52,964,066 |
| Basic earnings per share | $ 2.37 | $ (0.23 ) | $ 5.72 | $ 0.25 |
| | | | | |
| Diluted: | | | | |
| Net income (loss) | $ 127 | $ (12 ) | $ 306 | $ 13 |
| Weighted-average shares outstanding | 53,740,174 | 52,420,868 | 53,516,859 | 52,964,066 |
| Dilutive shares | 684,706 | — | 720,694 | 667,433 |
| Diluted weighted-average shares outstanding | 54,424,880 | 52,420,868 | 54,237,553 | 53,631,499 |
| Diluted earnings per share | $ 2.34 | $ (0.23 ) | $ 5.64 | $ 0.25 |

Anti-dilutive options to purchase common shares are excluded from diluted earnings per share calculations. Anti-dilutive options consist primarily of stock appreciation rights (“SARs”) with an exercise price greater than the average market closing price of the Class A common stock. There were 1,139 and 914,183 anti-dilutive options for the three-month periods ended September 29, 2018 and September 30, 2017, respectively. There were 87,458 and 687,831 anti-dilutive options for the nine-month periods ended September 29, 2018 and September 30, 2017, respectively.

Note 13 Accumulated Other Comprehensive Income (Loss)

Stockholders’ equity includes certain items classified as Accumulated other comprehensive income (loss), including:

- Unrealized gain (loss) on anticipated sales hedging transactions relates to derivative instruments used to hedge the exposure related to currency exchange rates for forecasted Euro sales. These hedges are designated as cash flow hedges, and the Company defers income statement recognition of gains and losses until the hedged transaction occurs. See Note 8, Derivative Instruments for more details.
- Unrealized (loss) gain on forward interest rate swaps hedging transactions refers to the hedging of the interest rate risk exposure associated with the variable rate commitment entered into for the Enterprise Acquisition. See Note 8, Derivative Instruments for more details.
- Foreign currency translation adjustments relate to the Company’s non-U.S. subsidiary companies that have designated a functional currency other than the U.S. dollar. The Company is required to translate the subsidiary functional currency financial statements to dollars using a combination of historical, period-end, and average foreign exchange rates. This combination of rates creates the foreign currency translation adjustment component of Accumulated other comprehensive income (loss).

The components of Accumulated other comprehensive income (loss) (“AOCI”) for the nine months ended September 29, 2018 and September 30, 2017 are as follows (in millions):

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| | Unrealized gain (loss) on sales hedging | Unrealized (loss) gain on forward interest rate swaps | Currency translation adjustments | Total |
|---|---|---|---|---|
| Balance at December 31, 2016 | $ 6 | $ (15) | $ (36) | $(45) |
| Other comprehensive (loss) income before reclassifications | (22) | (2) | 2 | (22) |
| Amounts reclassified from AOCI(1) | 4 | 6 | — | 10 |
| Tax benefit (expense) | 3 | (1) | — | 2 |
| Other comprehensive (loss) income | (15) | 3 | 2 | (10) |
| Balance at September 30, 2017 | $ (9) | $ (12) | $ (34) | $(55) |
| | | | | |
| Balance at December 31, 2017 | $ (9) | $ (9) | $ (34) | $(52) |
| Other comprehensive income (loss) before reclassifications | 27 | 7 | (7) | 27 |
| Amounts reclassified from AOCI(1) | (1) | 3 | — | 2 |
| Tax (expense) | (4) | (2) | — | (6) |
| Other comprehensive income (loss) | 22 | 8 | (7) | 23 |
| Balance at September 29, 2018 | $ 13 | $ (1) | $ (41) | $(29) |

(1) See Note 8, Derivative Instruments regarding timing of reclassifications on forward interest rate swaps and sales hedges.

Note 14 Segment Information

The Company's operations consist of two reportable segments: Asset Intelligence & Tracking ("AIT") and Enterprise Visibility & Mobility ("EVM"). The reportable segments have been identified based on the financial data utilized by the Company's Chief Executive Officer (the chief operating decision maker or "CODM") to assess segment performance and allocate resources among the Company's segments. The CODM reviews adjusted operating income to assess segment profitability. Adjusted operating income excludes purchase accounting adjustments, amortization of intangible assets, acquisition and integration costs, and exit and restructuring costs. Segment assets are not reviewed by the Company's CODM and therefore are not disclosed below.

Financial information by segment is presented as follows (in millions):

| | Three Months Ended | | Nine Months Ended | |
|---|---|---|---|---|
| | September 29, 2018 | September 30, 2017 | September 29, 2018 | September 30, 2017 |
| Net sales: | | | | |
| AIT | $353 | $ 325 | $1,056 | $ 960 |
| EVM | 739 | 611 | 2,025 | 1,739 |
| Total segment net sales | 1,092 | 936 | 3,081 | 2,699 |
| Corporate, eliminations (1) | — | (1) | — | (3) |
| Total net sales | $1,092 | $ 935 | $3,081 | $ 2,696 |
| Operating income: | | | | |
| AIT(3) | $81 | $ 64 | $241 | $ 199 |
| EVM(3) | 117 | 86 | 279 | 204 |
| Total segment operating income | 198 | 150 | 520 | 403 |
| Corporate, eliminations (2) | (36) | (59) | (89) | (214) |
| Total operating income | $162 | $ 91 | $431 | $ 189 |

(1) Amounts included in Corporate, eliminations consist of purchase accounting adjustments related to the Enterprise Acquisition.

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(2) Amounts included in Corporate, eliminations consist of purchase accounting adjustments, amortization of intangible assets, acquisition and integration costs, and exit and restructuring costs.

(3) During 2018, the Company revised its methodology for allocating certain operating expenses across its two reportable segments to more accurately reflect where these operating costs are being incurred. The reallocations relate primarily to facilities, information technology, marketing and human resources expenses. All periods are presented on a comparable basis and reflect these changes. There was no impact to the Consolidated Financial Statements as a result of these reallocations.

Information regarding the Company's operations by geographic area is contained in the following table. These amounts are reported in the geographic area of the destination of the final sale.

Net sales to customers by geographic region were as follows (in millions):

| | Three Months Ended | | Nine Months Ended | |
|---|---|---|---|---|
| | September 29, 2018 | September 30, 2017 | September 29, 2018 | September 30, 2017 |
| Europe, Middle East and Africa | $348 | $ 306 | $1,034 | $ 872 |
| Latin America | 62 | 58 | 175 | 168 |
| Asia-Pacific | 140 | 119 | 389 | 350 |
| North America | 542 | 452 | 1,483 | 1,306 |
| Total Net sales | $1,092 | $ 935 | $3,081 | $ 2,696 |

Item 2.