

PATTERSON COMPANIES, INC.

Form 10-Q

March 04, 2010

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**UNITED STATES**  
**SECURITIES AND EXCHANGE COMMISSION**

Washington, D.C. 20549

**FORM 10-Q**

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

**FOR THE QUARTERLY PERIOD ENDED JANUARY 23, 2010.**

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

**Commission File No. 0-20572**

**PATTERSON COMPANIES, INC.**

**(Exact name of registrant as specified in its charter)**

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**Minnesota** **41-0886515**  
(State of incorporation) (I.R.S. Employer Identification No.)  
**1031 Mendota Heights Road, St. Paul, Minnesota 55120**

(Address of principal executive offices, including zip code)

**(651) 686-1600**

(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

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

Patterson Companies, Inc. had outstanding 122,757,864 shares of common stock as of March 1, 2010.

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<u>Safe Harbor Statement Under The Private Securities Litigation Reform Act Of 1995:</u>	

This Form 10-Q for the period ended January 23, 2010, contains certain forward-looking statements as defined in the Private Securities Litigation Reform Act of 1995, which may be identified by the use of forward-looking terminology such as may, will, expect, anticipate, estimate, believe, goal, or continue, or comparable terminology that involves risks and uncertainties that are qualified in their entirety by cautionary language set forth herein under the caption Factors That May Affect Future Operating Results, in the Company's 2009 Annual Report on Form 10-K filed June 24, 2009 and other documents previously filed with the Securities and Exchange Commission.

**Table of Contents****PART I - FINANCIAL INFORMATION****PATTERSON COMPANIES, INC.****CONDENSED CONSOLIDATED BALANCE SHEETS**

(In thousands)

	<b>January 23, 2010 (Unaudited)</b>	<b>April 25, 2009</b>
<b>ASSETS</b>		
Current assets:		
Cash and cash equivalents	\$ 267,782	\$ 158,065
Receivables, net	471,316	476,156
Inventory	302,637	269,934
Prepaid expenses and other current assets	35,903	33,440
<b>Total current assets</b>	<b>1,077,638</b>	<b>937,595</b>
Property and equipment, net	168,657	166,500
Long-term receivables, net	64,932	51,572
Goodwill	770,085	747,104
Identifiable intangibles, net	226,260	220,932
Other	15,243	9,917
<b>Total assets</b>	<b>\$ 2,322,815</b>	<b>\$ 2,133,620</b>
<b>LIABILITIES AND STOCKHOLDERS EQUITY</b>		
Current liabilities:		
Accounts payable	\$ 184,035	\$ 180,933
Accrued payroll expense	58,160	45,105
Other accrued expenses	88,957	84,855
Income taxes payable		1,407
Current maturities of long-term debt		22,000
<b>Total current liabilities</b>	<b>331,152</b>	<b>334,300</b>
Long-term debt	525,000	525,000
Other long-term liabilities	88,311	88,000
<b>Total liabilities</b>	<b>944,463</b>	<b>947,300</b>
<b>STOCKHOLDERS EQUITY</b>		
Common stock	\$ 1,228	\$ 1,220
Additional paid-in capital	36,483	20,320
Accumulated other comprehensive income (loss)	16,545	(8,867)
Retained earnings	1,444,058	1,293,609
Notes receivable from ESOP	(119,962)	(119,962)
<b>Total stockholders equity</b>	<b>1,378,352</b>	<b>1,186,320</b>
<b>Total liabilities and stockholders equity</b>	<b>\$ 2,322,815</b>	<b>\$ 2,133,620</b>

See accompanying notes.

**Table of Contents****PATTERSON COMPANIES, INC.****CONDENSED CONSOLIDATED STATEMENTS OF INCOME**

(In thousands, except per share amounts)

(Unaudited)

	<b>Three Months Ended</b>		<b>Nine Months Ended</b>	
	<b>January 23, 2010</b>	<b>January 24, 2009</b>	<b>January 23, 2010</b>	<b>January 24, 2009</b>
Net sales	\$ 820,084	\$ 811,023	\$ 2,424,614	\$ 2,314,343
Cost of sales	544,015	541,914	1,623,324	1,539,929
Gross profit	276,069	269,109	801,290	774,414
Operating expenses	182,302	177,567	546,247	520,676
Operating income	93,767	91,542	255,043	253,738
Other income and (expense):				
Interest income	2,122	1,048	6,491	4,840
Interest expense	(6,406)	(7,000)	(19,383)	(23,235)
Other (loss) gain	(10)	(793)	480	(1,776)
Income before taxes	89,473	84,797	242,631	233,567
Income taxes	33,424	31,990	92,182	87,893
Net income	\$ 56,049	\$ 52,807	\$ 150,449	\$ 145,674
Earnings per share:				
Basic	\$ 0.47	\$ 0.45	\$ 1.27	\$ 1.24
Diluted	\$ 0.47	\$ 0.45	\$ 1.26	\$ 1.23
Weighted average common shares:				
Basic	118,518	117,624	118,324	117,645
Diluted	119,434	118,134	119,097	118,391

See accompanying notes.

**Table of Contents****PATTERSON COMPANIES, INC.****CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS**

(Dollars in thousands)

(Unaudited)

	<b>Nine Months Ended</b>	
	<b>January 23, 2010</b>	<b>January 24, 2009</b>
<b>Operating activities:</b>		
Net income	\$ 150,449	\$ 145,674
<b>Adjustments to reconcile net income to net cash provided by operating activities:</b>		
Depreciation	17,910	16,327
Amortization	10,324	5,188
Share-based compensation	6,618	5,800
Excess tax benefits from share-based compensation	(381)	(317)
Bad debt expense	3,047	3,136
Change in assets and liabilities, net of acquired	(34,840)	(103,274)
<b>Net cash provided by operating activities</b>	<b>153,127</b>	<b>72,534</b>
<b>Investing activities:</b>		
Additions to property and equipment, net	(17,506)	(22,838)
Acquisitions, net	(28,151)	(109,942)
<b>Net cash used in investing activities</b>	<b>(45,657)</b>	<b>(132,780)</b>
<b>Financing activities:</b>		
Payments of long-term debt		(130,008)
(Payments on) Borrowings from credit facility	(22,000)	63,000
Common stock issued, net	9,995	10,275
Excess tax benefits from share-based compensation	381	317
<b>Net cash used in financing activities</b>	<b>(11,624)</b>	<b>(56,416)</b>
<b>Effect of exchange rate changes on cash</b>	<b>13,871</b>	<b>(29,618)</b>
<b>Net increase in cash and cash equivalents</b>	<b>109,717</b>	<b>(146,280)</b>
<b>Cash and cash equivalents at beginning of period</b>	<b>158,065</b>	<b>308,164</b>
<b>Cash and cash equivalents at end of period</b>	<b>\$ 267,782</b>	<b>\$ 161,884</b>

See accompanying notes.

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**PATTERSON COMPANIES, INC.**

**NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**

*(In thousands, except share and per share data, unless otherwise indicated)*

*(Unaudited)*

**January 23, 2010**

**NOTE 1 GENERAL**

*Basis of Presentation*

In the opinion of management, the accompanying unaudited condensed consolidated financial statements contain all adjustments necessary to present fairly the financial position of the Company as of January 23, 2010 and the results of operations and the cash flows for the periods ended January 23, 2010 and January 24, 2009. Such adjustments are of a normal recurring nature. The results of operations for the periods ended January 23, 2010 and January 24, 2009, are not necessarily indicative of the results to be expected for the full year. These financial statements should be read in conjunction with the financial statements included in the 2009 Annual Report on Form 10-K filed on June 24, 2009.

The condensed consolidated financial statements of Patterson Companies, Inc. include the assets and liabilities of PDC Funding Company, LLC ( PDC Funding ) and PDC Funding Company II, LLC ( PDC Funding II ), wholly owned subsidiaries and separate legal entities under Minnesota law. PDC Funding and PDC Funding II are fully consolidated special purpose entities of the Company established to sell customer installment sale contracts to outside financial institutions in the normal course of business. The assets of PDC Funding and PDC Funding II would be available first and foremost to satisfy the claims of its creditors. There are no known creditors of PDC Funding or PDC Funding II.

*Fiscal Year End*

The fiscal year end of the Company is the last Saturday in April. The third quarter and the first nine months of fiscal 2010 and 2009 represent the 13 and 39 weeks ended January 23, 2010 and January 24, 2009, respectively.

*Comprehensive Income*

Total comprehensive income was \$53,100 and \$175,861 for the three and nine months ended January 23, 2010, respectively, and \$51,735 and \$100,101 for the three and nine months ended January 24, 2009. Other than net income, comprehensive income also includes foreign currency translation adjustments. Foreign currency translation adjustments do not include a provision for income tax because earnings from foreign operations are considered to be indefinitely reinvested outside the U.S. During the nine months ended January 23, 2010, comprehensive income was positively affected by changes in foreign currency exchange rates, whereas comprehensive income was negatively affected by changes in foreign currency exchange rates during the nine months ended January 24, 2009.



**Table of Contents***Earnings Per Share*

The following table sets forth the computation of basic and diluted earnings per share (shares in thousands):

	<b>Three Months Ended</b>		<b>Nine Months Ended</b>	
	<b>January 23, 2010</b>	<b>January 24, 2009</b>	<b>January 23, 2010</b>	<b>January 24, 2009</b>
<b>Denominator:</b>				
Denominator for basic earnings per share weighted-average shares	118,518	117,624	118,324	117,645
Effect of dilutive securities stock options, restricted stock, and stock purchase plans	916	510	773	746
 Denominator for diluted earnings per share adjusted weighted average shares	 119,434	 118,134	 119,097	 118,391

Options to purchase 869 and 1,057 shares of common stock during the three and nine months ended January 23, 2010, respectively, and 1,606 and 989 shares during the three and nine months ended January 24, 2009, respectively, were excluded from the calculation of diluted earnings per share because the effect would have been anti-dilutive. Unvested restricted stock awards excluded from the calculation of diluted earnings per share were 0 and 80 shares during the three and nine months ended January 23, 2010, respectively, and 337 and 248 shares during the three and nine months ended January 24, 2009, respectively, because the effect would have been anti-dilutive.

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*Recently Issued Accounting Pronouncements*

In June 2009, the Financial Accounting Standards Board (FASB) issued Statement of Financial Accounting Standards (SFAS) No. 168, The FASB Accounting Standards Codification and the Hierarchy of Generally Accepted Accounting Principles a replacement of FAS 162. The new standard establishes only two levels of U.S. generally accepted accounting principles (GAAP), authoritative and non-authoritative. The FASB Accounting Standards Codification (ASC) became the single source of authoritative, nongovernmental U.S. GAAP, except for rules and interpretive releases of the SEC, which will continue to be sources of authoritative U.S. GAAP for SEC registrants. All other non-grandfathered, non-SEC accounting literature not included in the ASC became non-authoritative upon adoption. The new guidance became effective for the Company's second quarter of fiscal 2010. Since the new standard did not change U.S. GAAP, there was no change to the Company's Condensed Consolidated Financial Statements other than to update references to U.S. GAAP to be in conformity with the ASC.

The Company adopted the provisions of ASC Topic No. 820, Fair Value Measurements and Disclosures (ASC 820) as of April 27, 2008 for fair value measurements of certain financial assets and liabilities and for nonfinancial assets and liabilities measured at fair value on at least an annual basis. The provisions were adopted for nonfinancial assets and liabilities not measured at fair value on at least an annual basis as of April 26, 2009. These provisions define fair value, establish a framework for measuring fair value, and expand disclosure requirements. The adoption had no impact on the Company's financial condition, results of operations or cash flows.

In December 2007, the FASB issued guidance codified into ASC Topic No. 805, Business Combinations, which replaced previous business combination accounting guidance. The new guidance revises how an acquirer recognizes and measures in its financial statements the identifiable assets acquired, the liabilities, any non-controlling interest in the acquiree and the goodwill acquired. The guidance as amended includes recognition provisions for assets acquired and liabilities assumed that arise from contingencies and the treatment of contingent purchase price. It also requires additional disclosure requirements intended to enable users to evaluate the nature and financial effects of the business combination. The Company adopted the new guidance on April 26, 2009, and applied the provisions prospectively to all new acquisitions closing on or after that date. The adoption did not have a material impact on the Company's financial condition, results of operations or cash flows.

In June 2009, the FASB issued guidance codified into ASC Topic No. 860, Transfers and Servicing (ASC 860) which amends the derecognition guidance in former FASB Statement No. 140 and eliminates the exemption from consolidation for qualifying special-purpose entities. Also in June 2009, the FASB issued guidance codified into ASC Topic No. 810, Consolidation (ASC 810) which amends the consolidation guidance applicable to variable interest entities. The amendments will significantly affect the overall consolidation analysis under former FASB Interpretation No. 46(R). Both ASC 860 and ASC 810 are effective for fiscal years beginning after November 15, 2009. The Company is evaluating the impact ASC 860 and ASC 810 will have on its financial condition, results of operations and cash flows.

In October 2009, the FASB issued Accounting Standards Update (ASU) No. 2009-13, Multiple-Deliverable Revenue Arrangements (ASU 2009-13). This update amends ASC Topic 605-25, Revenue Recognition Multiple-Deliverable Revenue Arrangements to remove the criterion that entities must use objective and reliable evidence of fair value in separately accounting for deliverables and provides

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entities with a hierarchy of evidence that must be considered when allocating arrangement consideration. The update also requires entities to allocate arrangement consideration to the separate units of accounting based on the deliverables' relative selling price. The provisions will be effective for revenue arrangements entered into or materially modified in the Company's fiscal year 2012 and must be applied prospectively. The Company is currently evaluating the impact of the provisions of ASU 2009-13.

In January 2010, the FASB issued ASU 2010-06, Fair Value Measurements and Disclosures (Topic 820): Improving Disclosures about Fair Value Measurements (ASU 2010-06). ASU 2010-06 includes new disclosure requirements related to fair value measurements, including transfers in and out of Levels 1 and 2 and additional information about Level 3 activity. The new disclosures are required in interim and annual reporting periods beginning after December 15, 2009, except for the disclosures relating to Level 3 activity, which are effective for fiscal years beginning after December 15, 2010 and for interim periods within those fiscal years. The Company is currently evaluating the impact of ASU 2010-06.

**NOTE 2 GOODWILL AND OTHER INTANGIBLE ASSETS**

The goodwill balances and related activity by business segment as of April 25, 2009 and January 23, 2010 are as follows:

	Balance at April 25, 2009	Acquisition Activity	Translation And Other Activity	Balance at January 23, 2010
Dental Supply	\$ 127,127	\$ 9,829	\$ (7,205)	\$ 129,751
Rehabilitation Supply	498,730	25,369	701	524,800
Veterinary Supply	121,247		(5,713)	115,534
Total	\$ 747,104	\$ 35,198	\$ (12,217)	\$ 770,085

The increase in the acquisition activity column during the nine month period ended January 23, 2010 primarily reflects the purchase price allocations of acquisitions. The translation and other activity column primarily reflects reclassifications from goodwill to other intangible assets related to fiscal 2009 acquisitions, based on final asset valuations. The purchase price allocations of certain acquisitions are preliminary and are subject to adjustment for changes in the preliminary assumptions pending additional information, including final asset valuations from a third party firm.

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Balances of other intangible assets excluding goodwill are as follows:

	January 23, 2010	April 25, 2009
<b>Unamortized - indefinite lived:</b>		
Copyrights, trade names and trademarks	\$ 77,847	\$ 77,847
<b>Amortized:</b>		
Distribution agreement, customer lists and other	206,792	190,975
Less: Accumulated amortization	(58,379)	(47,890)
Net amortized other intangible assets	148,413	143,085
<b>Total identifiable intangible assets, net</b>	<b>\$ 226,260</b>	<b>\$ 220,932</b>

**NOTE 3 DERIVATIVE FINANCIAL INSTRUMENTS**

The Company is a party to certain offsetting and identical interest rate cap agreements. The cap agreements are not designated for hedge accounting treatment and were entered into to fulfill certain covenants of a sale agreement between a commercial paper conduit managed by JPMorgan Chase Bank, N.A. and PDC Funding. The cap agreements provide a credit enhancement feature for the financing contracts sold by PDC Funding to the commercial paper conduit, and replace a minimum interest rate margin previously required under the sale agreement.

The cap agreements are cancelled and new agreements entered into periodically to maintain consistency with the dollar maximum of the sale agreements and the maturity of the underlying financing contracts. PDC Funding has purchased two interest rate caps from banks with combined notional amounts of \$367 million and a maturity date of February 2015. Patterson Companies, Inc. has sold two identical interest rate caps to the same banks. Similarly to the above agreements, PDC Funding II and Patterson Companies, Inc. entered into offsetting and identical interest rate swap agreements. These agreements have an amortizing notional amount of \$110 million and a maturity date of July 2015.

In addition to the identical purchased and sold interest rate contracts described above, the Company has entered into two interest rate swap agreements with banks to economically hedge the interest rate risk associated with portions of the finance contracts that have been sold. As of January 23, 2010, the agreements have notional amounts of approximately \$22 million and \$28 million, respectively, and maturity dates of November 2011 and February 2012, respectively.

None of the Company's interest rate contracts qualify for hedge accounting treatment and, accordingly, the Company records the fair value of the agreements as an asset or liability and the change in any period as income or expense of the period in which the change occurs.

The following table presents the fair value of the interest rate contracts included in the consolidated balance sheets:

Derivative type	Location	Assets		Location	Liabilities	
		Fair Value At			Fair Value At	
		January 23, 2010	April 25, 2009		January 23, 2010	April 25, 2009
Interest rate contracts	Other noncurrent Assets	\$ 9.0	\$ 2.6	Other noncurrent liabilities	\$ 10.2	\$ 4.3

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The following table presents the effect of interest rate contracts on the consolidated statements of income:

<b>Derivative type</b>	<b>Location of gain(loss) recognized on derivative</b>	<b>Three Months Ended January 23, 2010</b>	<b>Nine Months Ended January 23, 2010</b>
Interest rate contracts	Other income (expense), net	\$ (0.2)	\$ (0.8)

**NOTE 4 FAIR VALUE MEASUREMENTS**

The Company adopted the disclosure requirements of ASC Topic 820, Fair Value Measurements and Disclosures (ASC 820) at the beginning of fiscal 2009. ASC 820 establishes the following hierarchy which prioritizes the inputs used to measure fair value from market based assumptions to entity specific assumptions as follows:

**Level 1 -** Quoted prices in active markets for identical assets and liabilities at the measurement date.

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

**Level 3 -** Unobservable inputs for which there is little or no market data available. These inputs reflect management's assumptions of what market participants would use in pricing the asset or liability.

The Company's hierarchy for its assets and liabilities measured at fair value on a recurring basis as of January 23, 2010 is as follows:

	<b>Total</b>	<b>Quoted Prices in Active Markets (Level 1)</b>	<b>Significant Other Observable Inputs (Level 2)</b>	<b>Significant Unobservable Inputs (Level 3)</b>
	<b>(in millions)</b>			
<b>Assets:</b>				
Cash equivalents	\$ 101.8	\$ 101.8		
Derivative instruments	9.0		\$ 9.0	
Total assets	\$ 110.8	\$ 101.8	\$ 9.0	\$
<b>Liabilities:</b>				
Derivative instruments	\$ 10.2	\$	\$ 10.2	\$

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*Cash equivalents* The Company values cash equivalents at transaction price. The carrying value of cash equivalents, including government securities and money market funds, approximates fair value. Maturities of cash equivalents are less than three months.

*Derivative instruments* The Company's derivative instruments consist of interest rate contracts. These instruments are valued using inputs such as interest rates and credit spreads.

### NOTE 5 CUSTOMER FINANCING

As a convenience to its customers, the Company offers several different financing alternatives including both a Company sponsored program and a third party program. For the third party program, the Company acts as a facilitator between the customer and the third party financing entity with no on-going involvement in the financing transaction. Under the Company sponsored program, equipment purchases by customers with strong credit are financed to a maximum of \$0.4 million for any one customer. The Company generally sells the customers' financing contracts to outside financial institutions in the normal course of its business. The Company currently has two arrangements under which it sells these contracts.

In fiscal 2003, the Company initiated an agreement to sell its equipment finance contracts to a commercial paper conduit managed by JPMorgan Chase Bank N.A. To participate in the commercial paper conduit, the Company was required to establish a special purpose entity (SPE), PDC Funding Company, LLC, a consolidated, wholly owned subsidiary. The Company transfers financing contracts to the SPE and in turn, the SPE sells the contracts to the commercial paper conduit. The SPE does not issue any debt. While there is no recourse to the Company by the commercial paper conduit on the sale of contracts, the Company receives only 90% of the principal amount of the contracts upon the sale. The remaining 10% of the proceeds is held by the conduit as security against the eventual performance of the portfolio. The holdback receivable from the conduit is recorded as a non-current asset, which is carried at its estimated fair market value. The capacity of this arrangement with the conduit is a maximum of \$367 million.

The Company also maintains an agreement with U.S. Bank National Association, as agent, whereby the U.S. Bank group purchases customers' financing contracts. The Company has established another SPE, PDC Funding LLC II (PDC II), as a consolidated, wholly owned subsidiary, which sells financing contracts to the U.S. Bank group. The Company receives 94% of the principal amounts of the contracts upon sale with the remaining 6% of the proceeds held by the banks as security against the eventual performance of the portfolio. The holdback receivable from the banks is recorded as a non-current asset, which is carried at its estimated fair market value. The capacity under the agreement is \$110 million.

These financing arrangements are accounted for as a sale of assets under the provisions of ASC Topic 860-20, Sales of Financial Assets. The Company sold approximately \$202.2 million and \$134.9 million of its contracts under these arrangements during the first nine months of fiscal 2010 and 2009, respectively. The Company retains servicing responsibilities under both agreements, for which it is paid a servicing fee. The servicing fees received by the Company are considered adequate compensation for services rendered. Accordingly, no servicing asset or liability has been recorded. The agreements require the Company to maintain a minimum current ratio and maximum leverage ratio. The Company was in compliance with the covenants at January 23, 2010.

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Included in current receivables in the condensed consolidated balance sheets are approximately \$151.8 million and \$136.1 million as of January 23, 2010 and April 25, 2009, respectively, of finance contracts not yet sold by the Company. Finance contracts sold under the arrangements and outstanding as of January 23, 2010 were \$403.4 million. The holdback receivable under the arrangements was approximately \$57.3 million and \$45.1 million as of January 23, 2010 and April 25, 2009, respectively. Since the internal financing program began in 1994, bad debt write-offs have amounted to less than one-percent of the loans originated.

**NOTE 6 SEGMENT REPORTING**

Patterson Companies, Inc. is comprised of three reportable segments: dental, veterinary, and rehabilitation supply. The Company's reportable business segments are strategic business units that offer similar products and services to different customer bases. The dental supply segment provides a virtually complete range of consumable dental products, clinical and laboratory equipment and value-added services to dentists, dental laboratories, institutions and other dental healthcare providers throughout North America. The veterinary supply segment provides consumable supplies, equipment, diagnostic products, biologicals (vaccines) and pharmaceuticals to companion-pet veterinary clinics in the majority of regions throughout the United States. The rehabilitation supply segment provides a comprehensive range of distributed and self-manufactured rehabilitation medical supplies and non-wheelchair assistive products to acute care hospitals, long-term care facilities, rehabilitation clinics, dealers and schools.

The accounting policies of the segments are the same as those described in the summary of significant accounting policies set forth in Note 1 to the consolidated financial statements included in the Company's 2009 Annual Report on Form 10-K filed June 24, 2009. The Company evaluates segment performance based on operating income. The corporate office general and administrative expenses are included in the dental supply segment and consist of home office support costs in areas such as informational technology, finance, human resources and facilities. The cost to operate the distribution centers are allocated to the operating units based on the through-put of the unit.

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The following table presents information about the Company's reportable segments:

	Three Months Ended		Nine Months Ended	
	January 23, 2010	January 24, 2009	January 23, 2010	January 24, 2009
Net Sales				
Dental supply	\$ 572,073	\$ 584,140	\$ 1,620,231	\$ 1,640,862
Rehabilitation supply	96,240	81,611	322,777	281,346
Veterinary supply	151,771	145,272	481,606	392,135
<b>Total</b>	<b>\$ 820,084</b>	<b>\$ 811,023</b>	<b>\$ 2,424,614</b>	<b>\$ 2,314,343</b>
Operating income				
Dental supply	\$ 75,001	\$ 73,747	\$ 193,261	\$ 196,028
Rehabilitation supply	12,859	11,676	42,617	40,196
Veterinary supply	5,907	6,119	19,165	17,514
<b>Total</b>	<b>\$ 93,767</b>	<b>\$ 91,542</b>	<b>\$ 255,043</b>	<b>\$ 253,738</b>

The following table presents sales information by product for the Company:

	Three Months Ended		Nine Months Ended	
	January 23, 2010	January 24, 2009	January 23, 2010	January 24, 2009
Net Sales				
Consumable and printed products	\$ 501,141	\$ 476,196	\$ 1,586,534	\$ 1,468,110
Equipment and software	249,324	271,384	636,979	653,642
Other	69,619	63,443	201,101	192,591
<b>Total</b>	<b>\$ 820,084</b>	<b>\$ 811,023</b>	<b>\$ 2,424,614</b>	<b>\$ 2,314,343</b>



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

**OVERVIEW**

This Management's Discussion and Analysis of Financial Condition and Results of Operations (MD&A) should be read in conjunction with the MD&A included in our 2009 Annual Report on Form 10-K filed June 24, 2009, for important background information regarding, among other things, an overview of the markets in which we operate and our business strategies.

**RESULTS OF OPERATIONS**

The following table sets forth, for the periods indicated, the percentage of net sales represented by certain operational data.

	Three Months Ended		Nine Months Ended	
	January 23, 2010	January 24, 2009	January 23, 2010	January 24, 2009
Net sales	100.0%	100.0%	100.0%	100.0%
Cost of sales	66.3%	66.8%	67.0%	66.5%
Gross margin	33.7%	33.2%	33.0%	33.5%
Operating expenses	22.2%	21.9%	22.5%	22.5%
Operating income	11.4%	11.3%	10.5%	11.0%
Other (expense) income, net	(0.5)%	(0.8)%	(0.5)%	(0.9)%
Income before taxes	10.9%	10.5%	10.0%	10.1%
Net income	6.8%	6.5%	6.2%	6.3%

***QUARTER ENDED JANUARY 23, 2010 COMPARED TO QUARTER ENDED JANUARY 24, 2009.***

**Net Sales.** Consolidated net sales for the three months ended January 23, 2010 ( Current Quarter ) increased 1.1% to \$820.1 million, compared to \$811.0 million for the three months ended January 24, 2009 ( Prior Quarter ). Acquisitions contributed 2.0% to sales growth and changes in foreign currency translation rates increased sales by 1.3%.

Dental segment sales of \$572.1 million were 2.1% lower than \$584.1 million in the Prior Quarter. Acquisitions accounted for 0.8% of sales growth in the Current Quarter, while the impact of currency translation rates improved sales by 1.5%. Consumable sales grew 1.9% in the Current Quarter. Excluding the impact of acquisitions and foreign currency, consumables grew slightly in the Current Quarter, marking the first time consumables sales have experienced internal growth since the fall of 2008 when the economy started to deteriorate sharply.

Dental equipment and software sales faced a difficult comparison with the Prior Quarter, when the Company outperformed the overall dental equipment market. In addition, the Company believes the purchasing decisions of dental practitioners for new equipment are continuing to be affected by the weak economy. In the Current Quarter, total dental equipment and software sales declined 9.6%, including a decrease in basic dental equipment such as chairs, units and lights of 11.1%. Sales of CEREC dental restorative systems were down 3.5% compared to the Prior Quarter.

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Sales of other services and products in the Dental segment rose 9.7% in the Current Quarter.

Veterinary segment sales grew 4.5% to \$151.8 million, driven by improved consumables sales. Equipment sales were down 12.5% from the Prior Quarter.

In the Current Quarter, Rehabilitation segment sales were \$96.2 million, a 17.9% increase from \$81.6 million in the Prior Quarter. Acquisitions contributed 14.6% to sales growth and favorable changes in foreign currency translation rates further benefited Current Quarter sales by 2.1%. The acquisition contribution was driven mostly by the April 2009 acquisition of Mobilis Health Care Group (Mobilis) in the United Kingdom and the June 2009 acquisition of Empi Therapy Solutions (Empi) in the United States.

**Gross Margins.** Consolidated gross margin was 33.7%, an increase of 50 basis points from the Prior Quarter, primarily as a result of product mix. Dental gross margin improved 70 basis points and was positively impacted by the increased mix of consumables sales compared to basic equipment sales and increased software and related service revenues.

Gross margin of the Veterinary and Rehabilitation segments increased 40 basis points and decreased 70 basis points, respectively. The higher gross margin in the Veterinary segment was due to product mix. The decline in the Rehabilitation gross margin was due mostly to the impact of the Mobilis and Empi acquisitions. The impact of these acquisitions is expected to continue to lessen as they become more fully integrated into the existing business.

**Operating Expenses.** The consolidated operating expense ratio was 22.2%, an increase of 30 basis points from the Prior Quarter due mostly to acquisitions, including expenses related to integration and the amortization of intangible assets.

The operating expense ratio of the Dental segment was 20 basis points higher than in the Prior Quarter, reflecting increased fixed costs on a lower sales volume and acquisition-related expenses. The Veterinary segment's operating expense ratio was 70 basis points higher than the Prior Quarter due to higher levels of amortization expense. Operating expenses as a percent of sales at the Rehabilitation segment were 30 basis points higher in the Current Quarter due to integration expenses related to recent acquisitions.

**Operating Income.** Current Quarter operating income was \$93.8 million, or 11.4% of net sales. In the Prior Quarter, operating income was \$91.5 million, or 11.3% of net sales. The operating margin improvement was driven by the 50 basis points increase in gross margin, partly offset by the 30 basis increase in the operating expense ratio as described above.

**Other (Expense) Income, Net.** Net other expense was \$4.3 million in the Current Quarter compared to net other expense of \$6.7 million in the Prior Quarter. During the Prior Quarter, the Company made a scheduled payment of \$130 million on long-term debt.

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**Income Taxes.** The effective income tax rate for the Current Quarter was 37.4%. In the Prior Quarter, the rate was 37.7%. For the full fiscal year 2010, the Company expects the effective tax rate to approximate 37.8% compared to 37.5% for full fiscal year 2009. The expected increase for fiscal 2010 is due primarily to the increase in the effective state income tax rate.

**Earnings Per Share.** Earnings per diluted share was \$0.47 in the Current Quarter compared to \$0.45 in the Prior Quarter.

### *NINE MONTHS ENDED JANUARY 23, 2010 COMPARED TO NINE MONTHS ENDED JANUARY 24, 2009.*

**Net Sales.** Consolidated net sales for the nine months ended January 23, 2010 ( Current Period ) totaled \$2,424.6 million compared to \$2,314.3 million for the nine months ended January 24, 2009 ( Prior Period ). Total sales growth of 4.8% included a contribution from acquisitions of 5.0%. The impact of changes in foreign currency translation rates was neutral. The sales of all three of the Company's business units have been negatively affected by the downturn in the economy that began in the fall of 2008.

Dental segment sales of \$1,620.2 million were down 1.3% from the Prior Period. Acquisitions added 0.9% to Current Period sales, while the impact of currency translation rates was nominal. Consumable sales declined 0.9% and were affected by a high level of unemployment caused by the weak general economy and the deferral of high-level and discretionary services by patients for economic related reasons.

Dental equipment and software sales declined 3.8% compared to the Prior Period. Sales of basic dental equipment were especially impacted by the economic recession and declined 10.2% in the Current Period. This decline in basic equipment was partly offset by sales of CEREC dental restorative systems, which grew 27.2%. The Company believes the recession has caused many dentists to limit their investments to equipment with rapid rates of return, such as CEREC. Sales of other services and products in the Dental segment rose 4.9% in the Current Period.

The 22.8% sales growth of the Veterinary segment to \$481.6 million in the Current Period was primarily due to the October 2008 acquisition of the Columbus Serum Company. Excluding acquisitions, the increase in sales was 6.7%.

In the Current Period, Rehabilitation segment sales of \$322.8 million were 14.7% higher than the \$281.3 million of sales in the Prior Period. Acquisitions contributed 13.7% to sales growth, while unfavorable changes in foreign currency translation rates reduced Current Period sales by 1.0%.

**Gross Margins.** Consolidated gross margin declined 50 basis points to 33.0% in the Current Period, due in part to the relative sales growth of the Veterinary segment which generates a lower gross margin than the other two segments.

Dental gross margin, which improved 50 basis points, benefited from an increased mix of consumables sales compared to basic equipment sales and increased software and related service revenues generated by the December 2008 Dolphin acquisition. Gross margin of the Veterinary segment decreased 80 basis points in the Current Period due mostly to the effect of the Columbus Serum acquisition and lower levels of vendor rebates earned.

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The Rehabilitation segment's gross margin declined 60 basis points in the Current Period. The impact of the recent acquisitions was the primary factor in the decrease. This impact is expected to lessen as the acquisitions are more fully integrated into the existing business.

**Operating Expenses.** The consolidated operating expense ratio of 22.5% was flat with the Prior Period. The Company has instituted a range of expense control measures over the past year in response to the economic downturn that have slowed expense growth, however the impact of these measures has been lessened by expenses related to the integration of recent acquisitions.

The operating expense ratio of the Dental segment was 40 basis points higher than in the Prior Period, reflecting increased fixed costs on lower sales volume and acquisition-related expenses. Operating expenses as a percent of sales improved 40 basis points in the Veterinary segment from leverage on higher revenues. The Rehabilitation segment's operating expense ratio increased 50 basis points due primarily to the expense structures of recent acquisitions.

**Operating Income.** Current Period operating income totaled \$255.0 million, or 10.5% of net sales, compared to Prior Period operating income of \$253.7 million, or 11.0% of net sales. As discussed above, the main factor in the lower Current Period operating margin was a decrease in gross margin of 50 basis points.

**Other (Expense) Income, Net.** Net other expense was \$12.4 million in the Current Period compared to net other expense of \$20.2 million in the Prior Period. The primary factor in the decrease of net other expense was lower interest expense, which was \$3.8 million lower in the Current Period due to the repayment of \$130 million of debt in November 2008.

**Income Taxes.** The effective income tax rate for the Current Period was 38.0% compared to 37.6% in the Prior Period. The increase in the rate for the Current Period results primarily from an increase in the effective state income tax rate.

**Earnings Per Share.** Earnings per diluted share was \$1.26 in the Current Period compared to \$1.23 in the Prior Period.

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***LIQUIDITY AND CAPITAL RESOURCES***

The Company's cash flow from operating activities in the nine months ended January 23, 2010 ( Current Period ) was \$153.1 million, compared to \$72.5 million in the nine months ended January 24, 2009 ( Prior Period ). The most significant factor in the difference in operating cash flow between periods is due to a financing promotion on CEREC products during the Prior Period. One financing option allowed qualified customers to defer payments for one year. Since the Company generally cannot sell a contract to one of its funding sources until the first payment is received, these contracts were not eligible to be sold in the Prior Period. In the Current Period, the Company began selling these contracts. In the Current Period, the Company sold approximately \$35 million of these contracts and expects to sell an additional \$40 million of the contracts generated in the Prior Period before the end of fiscal 2010.

Net cash used in investing activities in the Current Period was \$45.7 million compared to \$132.8 million in the Prior Period. Current Period activity is primarily related to acquisitions for which cash used was \$28.2 million, including Empi Therapy Solutions, a rehabilitation equipment and supply distributor, and Global Medical and Dental, a dental equipment and supply distributor. In the Prior Period, cash used for acquisitions was \$109.9 million, mostly used in the acquisition of Columbus Serum, a full service distributor of companion-pet veterinary supplies, equipment and pharmaceuticals, and of Dolphin Imaging Systems, LLC and Dolphin Practice Management, LLC, providers of 3D imaging and practice management software for specialized dental practitioners. Capital expenditures in the Current Period were \$17.5 million, down from \$22.8 million in the Prior Period. The Company expects full year fiscal 2010 capital expenditures to be approximately \$30 million to \$35 million, including the purchase of a distribution facility in the fourth quarter of fiscal 2010 that will accommodate the consolidation of several smaller distribution centers.

Net cash used in financing activities was \$11.6 million in the Current Period compared to \$56.4 million in the Prior Period. In the Current Period, the Company repaid \$22 million on a revolving credit facility. In the Prior Period, the Company made a scheduled \$130 million payment on long-term debt, which was partially offset by \$63 million in borrowings on the Company's revolving credit facility. As of January 23, 2010, there were no borrowings outstanding under a \$300 million revolving credit facility that is available until November 2012. Funds provided by financing activities are generated mostly from the proceeds on the sale of shares of Company stock under various employee based programs. Similar amounts were provided by such programs in the Current and Prior Periods.

During the Current Period, foreign currencies of the Company's Canadian and overseas operations strengthened against the U.S. Dollar, while in the Prior Period these foreign currencies weakened against the U.S. Dollar. The effect of these exchange rate changes on cash was to increase cash balances by \$13.9 million in the Current Period and reduce cash balances by \$29.6 million in the Prior Period.

The Company expects funds generated by operations, existing cash balances and availability under existing debt facilities will be sufficient to meet the Company's working capital needs and finance anticipated expansion plans and strategic initiatives over the next twelve months.

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***CRITICAL ACCOUNTING POLICIES AND ESTIMATES***

There have been no material changes in the Company's Critical Accounting Policies and Estimates, as disclosed in its 2009 Annual Report on Form 10-K filed June 24, 2009.

***RECENTLY ISSUED ACCOUNTING PRONOUNCEMENTS***

In June 2009, the Financial Accounting Standards Board (FASB) issued Statement of Financial Accounting Standards (SFAS) No. 168, The FASB Accounting Standards Codification and the Hierarchy of Generally Accepted Accounting Principles—a replacement of FAS 162. The new standard establishes only two levels of U.S. generally accepted accounting principles (GAAP), authoritative and non-authoritative. The FASB Accounting Standards Codification (ASC) became the single source of authoritative, nongovernmental U.S. GAAP, except for rules and interpretive releases of the SEC, which will continue to be sources of authoritative U.S. GAAP for SEC registrants. All other non-grandfathered, non-SEC accounting literature not included in the ASC became non-authoritative upon adoption. The new guidance became effective for the Company's second quarter of fiscal 2010. Since the new standard did not change U.S. GAAP, there was no change to the Company's Condensed Consolidated Financial Statements other than to update references to U.S. GAAP to be in conformity with the ASC.

The Company adopted the provisions of ASC Topic No. 820, Fair Value Measurements and Disclosures (ASC 820) as of April 27, 2008 for fair value measurements of certain financial assets and liabilities and for nonfinancial assets and liabilities measured at fair value on at least an annual basis. The provisions were adopted for nonfinancial assets and liabilities not measured at fair value on at least an annual basis as of April 26, 2009. These provisions define fair value, establish a framework for measuring fair value, and expand disclosure requirements. The adoption had no impact on the Company's financial condition, results of operations or cash flows.

In December 2007, the FASB issued guidance codified into ASC Topic No. 805, Business Combinations, which replaced previous business combination accounting guidance. The new guidance revises how an acquirer recognizes and measures in its financial statements the identifiable assets acquired, the liabilities, any non-controlling interest in the acquiree and the goodwill acquired. The guidance as amended includes recognition provisions for assets acquired and liabilities assumed that arise from contingencies and the treatment of contingent purchase price. It also requires additional disclosure requirements intended to enable users to evaluate the nature and financial effects of the business combination. The Company adopted the new guidance on April 26, 2009, and applied the provisions prospectively to all new acquisitions closing on or after that date. The adoption did not have a material impact on the Company's financial condition, results of operations or cash flows.

In June 2009, the FASB issued guidance codified into ASC Topic No. 860, Transfers and Servicing (ASC 860) which amends the derecognition guidance in former FASB Statement No. 140 and eliminates the exemption from consolidation for qualifying special-purpose entities. Also in June 2009, the FASB issued guidance codified into ASC Topic No. 810, Consolidation (ASC 810) which amends the consolidation guidance applicable to variable interest entities. The amendments will significantly affect the overall consolidation analysis under former FASB Interpretation No. 46(R). Both ASC 860 and ASC 810 are effective for fiscal years beginning after November 15, 2009. The Company is evaluating the impact ASC 860 and ASC 810 will have on its financial condition, results of operations and cash flows.

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In October 2009, the FASB issued Accounting Standards Update (ASU) No. 2009-13, *Multiple-Deliverable Revenue Arrangements* (ASU 2009-13). This update amends ASC Topic 605-25, *Revenue Recognition—Multiple-Deliverable Revenue Arrangements* to remove the criterion that entities must use objective and reliable evidence of fair value in separately accounting for deliverables and provides entities with a hierarchy of evidence that must be considered when allocating arrangement consideration. The update also requires entities to allocate arrangement consideration to the separate units of accounting based on the deliverables' relative selling price. The provisions will be effective for revenue arrangements entered into or materially modified in the Company's fiscal year 2012 and must be applied prospectively. The Company is currently evaluating the impact of the provisions of ASU 2009-13.

In January 2010, the FASB issued ASU 2010-06, *Fair Value Measurements and Disclosures (Topic 820): Improving Disclosures about Fair Value Measurements* (ASU 2010-06). ASU 2010-06 includes new disclosure requirements related to fair value measurements, including transfers in and out of Levels 1 and 2 and additional information about Level 3 activity. The new disclosures are required in interim and annual reporting periods beginning after December 15, 2009, except for the disclosures relating to Level 3 activity, which are effective for fiscal years beginning after December 15, 2010 and for interim periods within those fiscal years. The Company is currently evaluating the impact of ASU 2010-06.

## ***FACTORS THAT MAY AFFECT FUTURE OPERATING RESULTS***

Certain information of a non-historical nature contains forward-looking statements. Words such as *believes, expects, plans, estimates, intends*, and variations of such words are intended to identify such forward-looking statements. These statements are not guaranties of future performance and are subject to certain risks, uncertainties or assumptions that are difficult to predict; therefore, the Company cautions shareholders and prospective investors that the following important factors, among others, could cause the Company's actual operating results to differ materially from those expressed in any forward-looking statements. The statements under this caption are intended to serve as cautionary statements within the meaning of the Private Securities Litigation Reform Act of 1995. The following information is not intended to limit in any way the characterization of other statements or information under other captions as cautionary statements for such purpose. The order in which such factors appear below should not be construed to indicate their relative importance or priority. The Company assumes no obligation to update any forward-looking statements, whether as a result of new information, future events or otherwise.

Economic conditions and volatility in the financial markets could adversely affect our operating results and financial condition. The ability to predict the demand for capital goods by customers is extremely difficult in the current economic environment, which could lead to increased volatility in the Company's revenues for these types of products.

The Company's ability to meet increased competition from national, regional and local full-service distributors and mail-order distributors of dental, veterinary and rehabilitation and assistive living products, while maintaining current or improved profit margins.

The ability of the Company to effectuate modifications to the business models of its three operating units to address changes in the individual markets of those business units.

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The ability of the Company to consolidate the distribution, information systems, human resources, financial and other administrative functions of its three business units into jointly shared services which meet the needs of the individual business units.

The ability of the Company to manage rapidly changing energy and commodity prices.

The ability of the Company to retain its base of customers and to increase its market share.

The ability of the Company to provide for an orderly management succession, including the ability to recruit skilled personnel for the business, and then identify and train our personnel for their transition into key roles to support the long-term growth of the business.

The ability of the Company to maintain satisfactory relationships with qualified and motivated sales personnel.

The continued ability of the Company to maintain satisfactory relationships with key vendors and the ability of the Company to create relationships with additional manufacturers of quality, innovative products.

Changes in the economics of dentistry affecting dental practice growth and the demand for dental products, including the ability and willingness of dentists to invest in high-technology diagnostic and therapeutic products.

Reduced growth in expenditures for dental services by private dental insurance plans.

The accuracy of the Company's assumptions concerning future per capita expenditures for dental services, including assumptions as to population growth and the demand for preventive dental services such as periodontic, endodontic and orthodontic procedures.

The rate of growth in demand for infection control products currently used for prevention of the spread of communicable diseases such as AIDS, hepatitis and herpes.

Changes in the economics of the veterinary supply market, including reduced growth in per capita expenditures for veterinary services and reduced growth in the number of households owning pets.

The effects of healthcare related legislation and regulation, which may affect expenditures or reimbursements for rehabilitation and assistive products.



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

There have been no material changes since April 25, 2009 in the Company's market risk. For further information on market risk, refer to Item 7A in the Company's 2009 Annual Report on Form 10-K filed June 24, 2009.

**ITEM 4. CONTROLS AND PROCEDURES**

Under the supervision and with the participation of the Company's management, including the Company's President and Chief Executive Officer ( CEO ) and its Chief Financial Officer ( CFO ), management evaluated the effectiveness of the design and operation of the Company's disclosure controls and procedures (as defined in Rule 13a-15(e) and 15d-15(e) under the Exchange Act) as of January 23, 2010. Based upon their evaluation of these disclosure controls and procedures, the CEO and CFO concluded that the disclosure controls and procedures were effective as of January 23, 2010.

There were no changes in the Company's internal control over financial reporting (as defined in Rule 13a-15(f) or 15d-15(f) under the Exchange Act) that occurred during the quarter ended January 23, 2010 that have materially affected, or are reasonably likely to materially affect, the Company's internal control over financial reporting.

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**PART II - OTHER INFORMATION**

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

(c) In September 2004, the Company's Board of Directors approved a stock repurchase program under which the Company could have repurchased up to six million shares of common stock. In December 2007, the Company's Board of Directors expanded this authorization to allow for the purchase of up to twenty five million shares of common stock. As of January 23, 2010, 5,905,430 shares remain available for purchase under the authorization, which expires on December 31, 2012.

**ITEM 6. EXHIBITS**

The exhibits listed in the accompanying exhibit index are filed as part of this Quarterly Report on Form 10-Q.

All other items under Part II have been omitted because they are inapplicable or the answers are negative, or were previously reported in the 2009 Annual Report on Form 10-K filed June 24, 2009.

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**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.

**PATTERSON COMPANIES, INC.**  
(Registrant)

Dated: March 4, 2010

By: /s/ R. Stephen Armstrong  
R. Stephen Armstrong  
Executive Vice President, Chief Financial Officer  
and Treasurer  
(Principal Financial Officer and Principal  
Accounting Officer)

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**EXHIBIT INDEX**

<b>Exhibit Number</b>	<b>Exhibit Description</b>
31.1	Certification of the Chief Executive Officer pursuant to Rule 13a-14(a) or 15d-14(a) under the Securities Exchange Act of 1934, as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
31.2	Certification of the Chief Financial Officer pursuant to Rule 13a-14(a) or 15d-14(a), under the Securities Exchange Act of 1934, as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
32	Certifications of the Chief Executive Officer and Chief Financial Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002