CARDINAL HEALTH INC
Form 10-Q
February 06, 2014
Table of Contents

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549
Form 10-Q

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

For the quarterly period ended December 31, 2013

or

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

For the transition period from _____ to _____
Commission File Number: 1-11373

Cardinal Health, Inc.
(Exact name of registrant as specified in its charter)

Ohio	31-0958666
(State or other jurisdiction of incorporation or organization)	(IRS Employer Identification No.)
7000 Cardinal Place, Dublin, Ohio	43017
(Address of principal executive offices)	(Zip Code)

(614) 757-5000
(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 þ No o

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Website, 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 þ No o

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

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

The number of the registrant's common shares, without par value, outstanding as of January 31, 2014, was the following: 342,888,531.

Cardinal Health, Inc. and Subsidiaries

Table of Contents

Item	Index*	Page
	Part I. Financial Information	
1	Financial Statements	2
	Condensed Consolidated Statements of Earnings for the Three and Six Months Ended December 31, 2013 and 2012 (Unaudited)	2
	Condensed Consolidated Statements of Comprehensive Income for the Three and Six Months Ended December 31, 2013 and 2012 (Unaudited)	3
	Condensed Consolidated Balance Sheets at December 31, 2013 (Unaudited) and June 30, 2013	4
	Condensed Consolidated Statements of Cash Flows for the Six Months Ended December 31, 2013 and 2012 (Unaudited)	5
	Notes to Condensed Consolidated Financial Statements	6
2	Management's Discussion and Analysis of Financial Condition and Results of Operations	13
3	Quantitative and Qualitative Disclosures About Market Risk	17
4	Controls and Procedures	17
	Part II. Other Information	
1	Legal Proceedings	18
1A	Risk Factors	18
2	Unregistered Sales of Equity Securities and Use of Proceeds	18
6	Exhibits	19
	Signatures	20

* Items not listed are inapplicable.

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Item 1: Financial Statements
Condensed Consolidated Statements of Earnings (Unaudited)

	Three Months Ended December 31		Six Months Ended December 31	
(in millions, except per common share amounts)	2013	2012	2013	2012
Revenue	$22,240	$25,232	$46,763	$51,121
Cost of products sold	20,895	24,008	44,155	48,739
Gross margin	1,345	1,224	2,608	2,382
Operating expenses:				
Distribution, selling, general and administrative expenses	766	699	1,497	1,388
Restructuring and employee severance	10	1	20	6
Amortization and other acquisition-related costs	56	25	105	53
Impairments and loss on disposal of assets	9	5	9	6
Litigation (recoveries)/charges, net	(15)	(12)	(13)	(34)
Operating earnings	519	506	990	963
Other income, net	(6)	(4)	(10)	(12)
Interest expense, net	33	27	66	53
Earnings before income taxes and discontinued operations	492	483	934	922
Provision for income taxes	217	180	320	347
Earnings from continuing operations	275	303	614	575
Earnings from discontinued operations, net of tax	3	—	3	—
Net earnings	$278	$303	$617	$575
Basic earnings per common share:				
Continuing operations	$0.80	$0.89	$1.80	$1.69
Discontinued operations	0.01	—	0.01	—
Net basic earnings per common share	$0.81	$0.89	$1.81	$1.69
Diluted earnings per common share:				
Continuing operations	$0.79	$0.88	$1.78	$1.67
Discontinued operations	0.01	—	0.01	—
Net diluted earnings per common share	$0.80	$0.88	$1.79	$1.67
Weighted-average number of common shares outstanding:				
Basic	342	340	341	340
Diluted	346	343	345	344
Cash dividends declared per common share	$0.3025	$0.2750	$0.6050	$0.5125

See notes to condensed consolidated financial statements.

Condensed Consolidated Statements of Comprehensive Income (Unaudited)

	Three Months Ended December 31		Six Months Ended December 31	
(in millions)	2013	2012	2013	2012
Net earnings	$278	$303	$617	$575
Other comprehensive income:				
Net change in foreign currency translation adjustments	4	11	28	36
Net unrealized gain on derivative instruments, net of tax	3	2	3	1
Total other comprehensive income, net of tax	7	13	31	37
Total comprehensive income	$285	$316	$648	$612

See notes to condensed consolidated financial statements.

Condensed Consolidated Balance Sheets

(in millions)	December 31, 2013 (Unaudited)	June 30, 2013
Assets		
Current assets:		
Cash and equivalents	$ 2,741	$1,901
Trade receivables, net	4,876	6,304
Inventories, net	8,478	8,373
Prepaid expenses and other	1,153	1,192
Total current assets	17,248	17,770
Property and equipment, net	1,407	1,489
Goodwill and other intangibles, net	5,556	5,574
Other assets	798	986
Total assets	$ 25,009	$25,819
Liabilities and Shareholders' Equity		
Current liabilities:		
Accounts payable	$ 11,221	$12,295
Current portion of long-term obligations and other short-term borrowings	255	168
Other accrued liabilities	1,886	2,127
Total current liabilities	13,362	14,590
Long-term obligations, less current portion	3,679	3,686
Deferred income taxes and other liabilities	1,379	1,568
Shareholders' equity:		
Preferred shares, without par value:		
Authorized—500 thousand shares, Issued—none	—	—
Common shares, without par value:		
Authorized—755 million shares, Issued—364 million shares at December 31, 2013 and June 30, 2013	2,961	2,953
Retained earnings	4,446	4,038
Common shares in treasury, at cost: 21 million shares and 25 million shares at December 31, 2013 and June 30, 2013, respectively	(917)	(1,084)
Accumulated other comprehensive income	99	68
Total shareholders' equity	6,589	5,975
Total liabilities and shareholders' equity	$ 25,009	$25,819

See notes to condensed consolidated financial statements.

Condensed Consolidated Statements of Cash Flows (Unaudited)

	Six Months Ended December 31	
(in millions)	2013	2012
Cash flows from operating activities:		
Net earnings	$617	$575
Earnings from discontinued operations, net of tax	(3)	—
Earnings from continuing operations	614	575
Adjustments to reconcile earnings from continuing operations to net cash provided by operating activities:		
Depreciation and amortization	234	176
Impairments and loss on disposal of assets	9	6
Share-based compensation	48	46
Provision for bad debts	29	9
Change in operating assets and liabilities, net of effects from acquisitions:		
Decrease in trade receivables	1,420	228
Increase in inventories	(100)	(536)
Increase/(decrease) in accounts payable	(1,088)	31
Other accrued liabilities and operating items, net	(178)	(97)
Net cash provided by operating activities	988	438
Cash flows from investing activities:		
Acquisition of subsidiaries, net of cash acquired	(50)	(126)
Additions to property and equipment	(90)	(62)
Proceeds from maturities of held-to-maturity securities	—	71
Net cash used in investing activities	(140)	(117)
Cash flows from financing activities:		
Net change in short-term borrowings	73	17
Reduction of long-term obligations	(1)	(6)
Net proceeds from issuance of common shares	139	26
Tax proceeds/(disbursements) from share-based compensation	39	(12)
Dividends on common shares	(208)	(165)
Purchase of treasury shares	(50)	(200)
Net cash used in financing activities	(8)	(340)
Net increase/(decrease) in cash and equivalents	840	(19)
Cash and equivalents at beginning of period	1,901	2,274
Cash and equivalents at end of period	2,741	2,255

See notes to condensed consolidated financial statements.

1. Summary of Significant Accounting Policies

Basis of Presentation

Our condensed consolidated financial statements include the accounts of all majority-owned and controlled subsidiaries, and all significant intercompany transactions and amounts have been eliminated. References to "we," "our" and similar pronouns in this Quarterly Report on Form 10-Q refer to Cardinal Health, Inc. and its majority-owned and controlled subsidiaries unless the context requires otherwise. The results of businesses acquired or disposed of are included in the condensed consolidated financial statements from the effective date of the acquisition or up to the date of disposal, respectively.

Our condensed consolidated financial statements have been prepared in accordance with the U.S. Securities and Exchange Commission ("SEC") instructions to Quarterly Reports on Form 10-Q and include all of the information and disclosures required by accounting principles generally accepted in the United States ("GAAP") for interim financial reporting. The preparation of financial statements in conformity with GAAP requires us to make estimates and assumptions that affect amounts reported in the condensed consolidated financial statements and accompanying notes. Actual amounts may differ from these estimated amounts. In addition, operating results presented for this fiscal 2014 interim period are not necessarily indicative of the results that may be expected for the full fiscal year ending June 30, 2014.

These condensed consolidated financial statements are unaudited and are presented pursuant to the rules and regulations of the SEC. Accordingly, the condensed consolidated financial statements included in this Quarterly Report on Form 10-Q for the quarter ended December 31, 2013 (this "Form 10-Q") should be read in conjunction with the audited consolidated financial statements and related notes contained in our Annual Report on Form 10-K for the fiscal year ended June 30, 2013 (the "2013 Form 10-K"). In our opinion, all adjustments necessary for a fair presentation of the condensed consolidated financial statements have been included. Except as disclosed elsewhere in this Form 10-Q, all such adjustments are of a normal and recurring nature.

Walgreens Contract

Our pharmaceutical distribution contract with Walgreen Co. ("Walgreens") expired on August 31, 2013. Sales to Walgreens generated approximately 20 percent of our consolidated revenue for fiscal 2013.

CVS Contracts

In December 2013, we announced the signing of an agreement with CVS Caremark Corporation (“CVS”) to form a U.S.-based generic sourcing entity (“Sourcing JV”). Both companies are contributing their sourcing and supply chain expertise to the 50/50 joint venture and are committing to source generic pharmaceuticals through it. The Sourcing JV, which we expect to be operational as soon as July 1, 2014, will have an initial term of 10 years. Under this arrangement, the Sourcing JV will negotiate generic supply contracts on behalf of both companies; however, it will not own products or hold inventory on behalf of either company. The arrangement includes a quarterly payment of $25 million over the term that we will pay to CVS. No physical assets will be contributed by either company to the Sourcing JV, and minimal funding will be provided to capitalize the entity. The venture is subject to the completion of final documentation and customary closing conditions.

Also during the three months ended December 31, 2013, we entered into a three-year extension, through June 2019, of our existing pharmaceutical distribution contracts with CVS.

Recent Financial Accounting Standards

In February 2013, the Financial Accounting Standards Board ("FASB") issued amended accounting guidance related to reclassifications out of accumulated other comprehensive income ("AOCI"). An entity is required to present, either parenthetically on the face of the statement where net income is presented or in the notes, the significant amounts, by component, reclassified out of AOCI by the respective line items of net income and to report changes in its AOCI balances by component. We adopted this amended guidance on a prospective basis in the first quarter of fiscal 2014 and have elected to report reclassifications out of AOCI in Note 10 in this Form 10-Q. The adoption of this guidance

did not impact our financial position or results of operations.

In January 2013, the FASB issued updated guidance to limit the scope of the balance sheet offsetting disclosures to derivatives, repurchase agreements and securities lending transactions to the extent they are offset in the financial statements or subject to an enforceable master netting arrangement or similar arrangement. We adopted this amended guidance on a retrospective basis in the first quarter of fiscal 2014. The adoption of this guidance did not impact our financial position or results of operations. See Note 8 for additional information regarding fair value measurements.

In July 2012, the FASB issued amended accounting guidance related to testing indefinite-lived intangible assets for impairment. Under this guidance, a company is no longer required to calculate the fair value of an indefinite-lived intangible asset unless the company determines, based on a qualitative assessment, that it is more likely than not that its estimated fair value is less than its carrying amount. We adopted this amended guidance in the first quarter of fiscal 2014. The adoption of this guidance did not impact our financial position or results of operations.

2. Acquisitions

While we have completed acquisitions during the six months ended December 31, 2013, the pro forma results of operations and the results of operations for acquisitions since the acquisition date have not been separately disclosed because the effects were not significant enough compared to the consolidated financial statements, individually or in the aggregate.

AssuraMed

On March 18, 2013, we completed the acquisition of AssuraMed, Inc. ("AssuraMed") for $2.07 billion, net of cash acquired, in an all-cash transaction. The acquisition of AssuraMed, a provider of medical supplies to homecare providers and patients in the home, expands our ability to serve this patient base. The assessment of fair value is preliminary and is based on information that was available at the time the condensed consolidated financial statements were prepared.

The following table summarizes the estimated fair values of the assets acquired and liabilities assumed at the acquisition date for AssuraMed:

(in millions)	Amount
Identifiable intangible assets	$627
Cash and equivalents	25
Trade receivables	117
Inventories	69
Prepaid expenses and other	90
Property and equipment	40
Accounts payable	(71)
Other accrued liabilities	(24)
Deferred income taxes and other liabilities	(180)
Total identifiable net assets acquired	693
Goodwill	1,402
Total net assets acquired	$2,095

3. Restructuring and Employee Severance

The following tables summarize restructuring and employee severance costs related to our restructuring activities:

	Three Months Ended December 31	
(in millions)	2013	2012
Employee-related costs (1)	$4	$—
Facility exit and other costs (2)	6	1
Total restructuring and employee severance	$10	$1

	Six Months Ended December 31	
(in millions)	2013	2012
Employee-related costs (1)	$8	$5
Facility exit and other costs (2)	12	1
Total restructuring and employee severance	$20	$6

(1) Employee-related costs primarily consist of termination benefits provided to employees who have been involuntarily terminated and duplicate payroll costs during transition periods.

(2) Facility exit and other costs primarily consist of lease termination costs, accelerated depreciation, equipment relocation costs, project consulting fees and costs associated with restructuring our delivery of information technology infrastructure services.

On January 30, 2013, we announced a restructuring plan within our Medical segment. Under this restructuring plan, among other things, we are moving production of procedure kits from our facility in Waukegan, Illinois to other facilities and selling property and consolidating office space in Waukegan, Illinois. We recognized restructuring costs of $6 million and $12 million related to this restructuring plan during the three and six months ended December 31, 2013, respectively, which primarily consisted of facility exit and other costs.

We currently estimate the total costs associated with this restructuring plan to be approximately $77 million on a pre-tax basis, of which $51 million was recognized in fiscal 2013 and $20 million was recognized during the six months ended December 31, 2013, including the write-down of the property in Waukegan, Illinois as discussed in Note 4. The estimated $6 million remaining costs to be recognized through the end of fiscal 2014 consist of facility exit and other costs.

The following table summarizes activity related to liabilities associated with restructuring and employee severance:

(in millions)	Employee-Related Costs	Facility Exit and Other Costs	Total
Balance at June 30, 2013	$55	$2	$57

Additions	12	1	13
Payments and other adjustments	(28)	(2)	(30)
Balance at December 31, 2013	$39	$1	$40

4. Impairments and Loss on Disposal of Assets

In connection with our Medical segment restructuring plan discussed in Note 3, the property in Waukegan, Illinois met the criteria for classification as held for sale at December 31, 2013. As a result, during the three months ended December 31, 2013, we recognized an $8 million loss to write down this property to the estimated fair value, less costs to sell, of $24 million, which is included in prepaid expenses and other in the condensed consolidated balance sheets. The fair value was estimated using inputs such as broker listings and sales agreements and thus represents a Level 2 nonrecurring fair value measurement.

5. Goodwill and Other Intangible Assets

Goodwill

The following table summarizes the changes in the carrying amount of goodwill, by segment and in total:

(in millions)	Pharmaceutical	Medical	Total
Balance at June 30, 2013	$2,094	$2,507	$4,601
Goodwill acquired, net of purchase price adjustments	21	9	30
Foreign currency translation adjustments and other	5	(1)	4
Balance at December 31, 2013	$2,120	$2,515	$4,635

Other Intangible Assets

Other intangible assets are amortized over periods ranging from one to twenty years. The following tables summarize other intangible assets by class at:

	December 31, 2013		
(in millions)	Gross Intangible	Accumulated Amortization	Net Intangible
Indefinite-life intangibles:			
Trademarks and other	$11	$—	$11
Total indefinite-life intangibles	11	—	11
Definite-life intangibles:			
Customer relationships	1,011	311	700
Trademarks, trade names and patents	213	60	153
Non-compete agreements	15	11	4
Other	108	55	53
Total definite-life intangibles	1,347	437	910
Total other intangible assets	$1,358	$437	$921

(in millions)	June 30, 2013 Gross Intangible	Accumulated Amortization	Net Intangible
Indefinite-life intangibles:			
Trademarks and other	$11	$—	$11
Total indefinite-life intangibles	11	—	11
Definite-life intangibles:			
Customer relationships	982	230	752
Trademarks, trade names and patents	209	49	160
Non-compete agreements	15	10	5
Other	101	56	45
Total definite-life intangibles	1,307	345	962
Total other intangible assets	$1,318	$345	$973

Total amortization of intangible assets was $46 million and $23 million for the three months ended December 31, 2013 and 2012, respectively, and $92 million and $44 million for the six months ended December 31, 2013 and 2012, respectively. Estimated annual amortization of intangible assets for the remainder of fiscal 2014 through 2018 is as follows: $92 million, $157 million, $143 million, $131 million and $95 million.

6. Income Taxes

Fluctuations in our provision for income taxes as a percentage of pre-tax earnings (“effective tax rate”) are due to changes in international and U.S. state effective tax rates and discrete items.

During the three months ended December 31, 2013, the effective tax rate of 44.1 percent was impacted by net unfavorable discrete items of $38 million, which increased the rate by 7.7 percentage points. The discrete items include the unfavorable impact of remeasurement of unrecognized tax benefits ($56 million) as a result of proposed assessments of additional tax.

During the six months ended December 31, 2013, the effective tax rate of 34.2 percent was impacted by net favorable discrete items of $23 million, which reduced the rate by 2.4 percentage points. The discrete items include the favorable impact of the settlement of federal and state tax controversies ($67 million) and the unfavorable impact of remeasurement of unrecognized tax benefits ($56 million).

During the three and six months ended December 31, 2012, the effective tax rate of 37.2 percent and 37.6 percent was impacted by net unfavorable discrete items of $2 million and $6 million, which increased the rate by 0.3 and 0.6 percentage points, respectively.

We had $520 million and $650 million of unrecognized tax benefits at December 31, 2013 and June 30, 2013, respectively. The December 31, 2013 and June 30, 2013 balances include $339 million and $371 million, respectively, of unrecognized tax benefits that, if recognized, would have an impact on the effective tax rate. The remaining unrecognized tax benefits relate to tax positions for which ultimate deductibility is highly certain but for which there is uncertainty as to the timing of such deductibility. Recognition of these tax benefits would not affect our effective tax rate. We include the full amount of unrecognized tax benefits in deferred income taxes and other liabilities in the condensed consolidated balance sheets.

We recognize accrued interest and penalties related to unrecognized tax benefits in the provision for income taxes. At December 31, 2013 and June 30, 2013 we had $140 million and $198 million, respectively, accrued

for the payment of interest and penalties. These balances are gross amounts before any tax benefits and are included in deferred income taxes and other liabilities in the condensed consolidated balance sheets.

It is reasonably possible that there could be a change in the amount of unrecognized tax benefits within the next 12 months due to activities of the U.S. Internal Revenue Service ("IRS") or other taxing authorities, including proposed assessments of additional tax, possible settlement of audit issues, reassessment of existing unrecognized tax benefits

or the expiration of applicable statutes of limitations. We estimate that the range of the possible change in unrecognized tax benefits within the next 12 months is a net decrease of approximately zero to $75 million, exclusive of penalties and interest.

We file income tax returns in the U.S. federal jurisdiction, various U.S. state jurisdictions and various foreign jurisdictions. We are generally subject to audit by taxing authorities for fiscal years 2003 through the current fiscal year.

During the six months ended December 31, 2013, the IRS closed audits of fiscal years 2003 through 2005. The IRS is currently conducting audits of fiscal years 2006 through 2010, and our transfer pricing arrangements continue to be under consideration as part of these audits. While the IRS has made and could make proposed adjustments to our transfer pricing arrangements, or other matters, we are defending our reported tax positions, and have accounted for the unrecognized tax benefits associated with our tax positions.

We are a party to a tax matters agreement with CareFusion Corporation ("CareFusion"), under which CareFusion is obligated to indemnify us for certain tax exposures and transaction taxes prior to our fiscal 2010 spin-off of CareFusion. The indemnification receivable was $190 million and $186 million at December 31, 2013 and June 30, 2013, respectively, and is included in other assets in the condensed consolidated balance sheets.

7. Contingent Liabilities and Litigation

Legal Proceedings

We become involved from time to time in disputes, litigation and regulatory matters incidental to our business, including governmental investigations and enforcement actions, personal injury claims, employment matters, commercial disputes, intellectual property matters, government contract compliance matters, disputes regarding environmental clean-up costs, claims in connection with acquisitions and divestitures, and other matters arising out of the normal conduct of our business. We intend to vigorously defend ourselves in such litigation.

We may be named from time to time in qui tam actions, which are cases initiated by private parties purporting to act on behalf of federal or state governments that allege that false claims have been submitted or have been caused to be submitted for payment by the government. After a private party has filed a qui tam action, the government must investigate the private party's claim and determine whether to intervene in the matter. These actions may remain under seal while the government makes this determination.

In addition, we occasionally may suspect that products we manufacture, market or distribute do not meet product specifications, published standards or regulatory requirements. In such circumstances, we investigate and take appropriate corrective action. Such actions can lead

to product recalls, costs to repair or replace affected products, temporary interruptions in product sales and action by regulators.

We accrue for contingencies related to disputes, litigation and regulatory matters if it is probable that a liability has been incurred and the amount of the loss can be reasonably estimated. Because litigation is inherently unpredictable and unfavorable developments or resolutions can occur, assessing contingencies is highly subjective and requires judgments about future events. We regularly review contingencies to determine whether our accruals and related disclosures are adequate. The amount of ultimate loss may differ from these estimates.

We are unable to estimate a range of reasonably possible loss for matters described below, since damages or fines have not been specified and the proceedings are in early stages with significant uncertainty as to factual issues. We do not believe, based on currently available information, that the outcomes of these matters will have a material adverse effect on our financial condition, though the outcomes could be material to our results of operations for a particular period.

We recognize income from the favorable outcome of litigation when we receive the associated cash or assets.

We recognize estimated loss contingencies for litigation and regulatory matters and income from favorable resolution of litigation in litigation (recoveries)/charges, net in our condensed consolidated statements of earnings.

Lakeland, Florida Distribution Center DEA Investigation and Related Matters

In February 2012, the U.S. Drug Enforcement Administration (the "DEA") issued an order to show cause and immediate suspension of our Lakeland, Florida distribution center's registration to distribute controlled substances, asserting that we failed to maintain required controls against the diversion of controlled substances. In May 2012, we entered into a settlement agreement with the DEA under which our Lakeland registration will remain suspended until May 2014 and the DEA confirmed that it was planning no further administrative actions at any of our other facilities based on conduct prior to the settlement. The settlement agreement did not foreclose the possibility of the U.S. Department of Justice (the “DOJ”) seeking civil fines for conduct covered by the settlement agreement. In that regard, we are providing information to and in discussions with the DEA and the DOJ.

State of West Virginia vs. Cardinal Health, Inc.

In June 2012, the West Virginia Attorney General filed, and in January 2014 amended, complaints against 13 pharmaceutical wholesale distributors, including us, in the Circuit Court of Boone County, West Virginia alleging, among other things, that the distributors failed to maintain effective controls to guard against diversion of controlled substances in West Virginia, failed to report suspicious orders of controlled substances in accordance with the West Virginia Uniform Controlled Substances Act and were negligent in distributing controlled substances to pharmacies that serve individuals who abuse controlled substances. In addition to injunctive and other equitable relief, the complaints seek monetary damages and the creation of a court-supervised fund, to be financed by the defendants in these actions, for a medical monitoring program focused on prescription drug abuse.

DOJ Civil Investigative Demand

In September 2012, we received a civil investigative demand from the

DOJ under the federal False Claims Act. The demand required us to produce documents relating to the structure of discounts offered or provided to our customers. In October 2013, the DOJ informed us that it was closing its investigation.

Federal False Claims Investigation

The DOJ has requested information in connection with an investigation of possible violations of the federal False Claims Act with respect to our Medical segment’s administration of a prime vendor agreement with the federal government. We are cooperating with the DOJ in this matter.

Antitrust Litigation Proceeds

We recognized income resulting from settlements of class action antitrust claims in which we were a class member of $16 million and $12 million during the three months ended December 31, 2013 and 2012, respectively, and $16 million and $34 million during the six months ended December 31, 2013 and 2012, respectively.

8. Fair Value Measurements

Fair value is defined as the price that would be received upon selling an asset or the price paid to transfer a liability on the measurement date. It focuses on the exit price in the principal or most advantageous market for the asset or liability in an orderly transaction between willing market participants. A three-tier fair value hierarchy is established as a basis for considering such assumptions and for inputs used in the valuation methodologies in measuring fair value. This hierarchy requires entities to maximize the use of observable inputs and minimize the use of unobservable inputs. The three levels of inputs used to measure fair values are as follows:

Level 1 - Observable prices in active markets for identical assets and liabilities.

Level 2 - Observable inputs other than quoted prices in active markets for identical assets and liabilities.

Level 3 - Unobservable inputs that are supported by little or no market activity and that are significant to the fair value of the assets and liabilities.

Recurring Fair Value Measurements

The following tables present the fair values for those assets measured on a recurring basis at:

	December 31, 2013			
(in millions)	Level 1	Level 2	Level 3	Total
Cash equivalents (1)	$595	$—	$—	$595
Forward contracts (2)	—	17	—	17
Other investments (3)	105	—	—	105
Total	$700	$17	$—	$717

	June 30, 2013			
(in millions)	Level 1	Level 2	Level 3	Total
Cash equivalents (1)	$348	$—	$—	$348
Forward contracts (2)	—	12	—	12
Other investments (3)	89	—	—	89
Total	$437	$12	$—	$449

(1) Cash equivalents are comprised of highly liquid investments purchased with a maturity of three months or less. The carrying value of these cash equivalents approximates fair value due to their short-term maturities.

(2) The fair value of interest rate swaps, foreign currency contracts and commodity contracts is determined based on the present value of expected future cash flows considering the risks involved, including non-performance risk, and using discount rates appropriate for the respective maturities. Observable Level 2 inputs are used to determine the present value of expected future cash flows. The fair value of these derivative contracts, which are subject to master netting arrangements under certain circumstances, is presented on a gross basis in the condensed consolidated balance sheets.

(3) The other investments balance includes investments in mutual funds, which are used to offset fluctuations in deferred compensation liabilities. These mutual funds primarily invest in the equity securities of companies with large market capitalization and high quality fixed income debt securities. The fair value of these investments is determined using quoted market prices.

9. Financial Instruments and Other Financing Arrangements

Financial Instruments

We utilize derivative financial instruments to manage exposure to certain risks related to our ongoing operations. The primary risks managed through the use of derivative instruments include interest rate risk, currency exchange risk and commodity price risk. We do not use derivative instruments for trading or speculative purposes. While the majority of our derivative instruments are designated as hedging instruments, we also enter into derivative instruments that are designed to hedge a risk, but are not designated as hedging instruments. These derivative instruments are adjusted to current fair value through earnings at the end of each period. Our derivative and hedging programs are consistent with those described in our 2013 Form 10-K.

During the six months ended December 31, 2013, we entered into pay-floating interest rate swaps with total notional amounts of $300 million. These swaps have been designated as fair value hedges of our fixed rate debt and are included in other assets in the condensed consolidated balance sheets at December 31, 2013.

Fair Value of Financial Instruments

The carrying amounts of cash and equivalents, trade receivables, net, accounts payable and other accrued liabilities at December 31, 2013 and June 30, 2013 approximate fair value due to their short-term maturities.

The following table summarizes the estimated fair value of our long-term obligations and other short-term borrowings compared to the respective carrying amounts at:

(in millions)	December 31, 2013	June 30, 2013
Estimated fair value	$3,995	$3,899
Carrying amount	3,934	3,854

The estimated fair value of our long-term obligations and other short-term borrowings is estimated based on either the quoted market prices for the same or similar issues or other inputs derived from available market information, which represents a Level 2 measurement. See Note 8 for further information regarding fair value measurements.

Other Financing Arrangements

On October 15, 2013, we reduced our committed receivables sales facility program from $950 million to $700 million in light of the expiration of our pharmaceutical distribution contract with Walgreens. Our committed receivables sales facility program is available to us through Cardinal Health Funding, LLC ("CHF"), which was organized for the sole purpose of buying receivables and selling undivided interests in those receivables

to third-party purchasers. Although consolidated in accordance with GAAP, CHF is a separate legal entity from Cardinal Health and from our subsidiary that sells the receivables to CHF. CHF is designed to be a special purpose, bankruptcy-remote entity whose assets are available solely to satisfy the claims of its creditors.

10. Shareholders' Equity

During the six months ended December 31, 2013, we repurchased 1.0 million common shares having an aggregate cost of $50 million. The average price paid per common share was $51.65.

During the six months ended December 31, 2012, we repurchased 4.9 million common shares having an aggregate cost of $200 million. The average price paid per common share was $40.63.

We funded the repurchases with available cash. The common shares repurchased are held in treasury to be used for general corporate purposes.

Accumulated Other Comprehensive Income

The following table summarizes the changes in the balance of AOCI by component and in total:

(in millions)	Foreign Currency Translation Adjustments	Unrealized Gain on Derivatives, net of tax	Accumulated Other Comprehensive Income
Balance at June 30, 2013	$54	$14	$68
Other comprehensive income, net of tax before reclassifications	28	4	32
Amounts reclassified to earnings	—	(1)	(1)
Total other comprehensive income, net of tax	28	3	31
Balance at December 31, 2013	$82	$17	$99

11. Earnings Per Share

The following tables reconcile the number of common shares used to compute basic and diluted earnings per share:

	Three Months Ended December 31	
(in millions)	2013	2012
Weighted-average common shares–basic	342	340
Effect of dilutive securities:		
Employee stock options, restricted share units and performance share units	4	3
Weighted-average common shares–diluted	346	343

	Six Months Ended December 31	
(in millions)	2013	2012
Weighted-average common shares–basic	341	340
Effect of dilutive securities:		
Employee stock options, restricted share units and performance share units	4	4
Weighted-average common shares–diluted	345	344

The potentially dilutive employee stock options, restricted share units and performance share units that were antidilutive were zero and 12 million for the three months ended December 31, 2013 and 2012, respectively,

and 2 million and 12 million for the six months ended December 31, 2013 and 2012, respectively.

12. Segment Information

Our operations are principally managed on a products and services basis and are comprised of two operating segments, which are the same as our reportable segments: Pharmaceutical and Medical. The factors for determining the reportable segments include the manner in which management evaluates our performance combined with the nature of the individual business activities.

The following tables present revenue for each reportable segment and reconciling items necessary to agree to amounts reported in the condensed consolidated statements of earnings:

	Three Months Ended December 31	
(in millions)	2013	2012
Pharmaceutical (1)	$19,443	$22,747
Medical	2,799	2,487
Total segment revenue	22,242	25,234
Corporate (2)	(2)	(2)
Total revenue	$22,240	$25,232

	Six Months Ended December 31	
(in millions)	2013	2012
Pharmaceutical (1)	$41,256	$46,244
Medical	5,511	4,879
Total segment revenue	46,767	51,123
Corporate (2)	(4)	(2)
Total revenue	$46,763	$51,121

(1) The decrease in Pharmaceutical segment revenue is primarily due to the expiration of our pharmaceutical distribution contract with Walgreens.

(2) Corporate revenue consists of the elimination of inter-segment revenue.

We evaluate segment performance based upon segment profit, among other measures. Segment profit is segment revenue, less segment cost of products sold, less segment distribution, selling, general and administrative ("SG&A") expenses. Segment SG&A expenses include share-based compensation expense as well as allocated corporate expenses for shared functions, including corporate management, corporate finance, financial and customer care shared services, human resources, information technology and legal. Corporate expenses are allocated to the segments based upon headcount, level of benefit provided and ratable allocation. Other income, net, interest expense, net and provision for income taxes are not allocated to the segments.

Restructuring and employee severance, amortization and other acquisition-related costs, impairments and loss on disposal of assets and litigation (recoveries)/charges, net are not allocated to the segments. In addition, certain investment and other spending are not allocated to the segments. Investment spending generally includes the first-year spend for certain projects that require incremental investments in the form of additional operating expenses. We encourage our segments and corporate functions to identify investment projects that will promote innovation and provide future returns. As approval decisions for such projects are dependent upon executive management, the expenses for such projects are often retained at Corporate. Investment spending within Corporate was $6 million and $7 million for the three months ended December 31, 2013 and 2012, respectively, and $10 million and $7 million

for the six months ended December 31, 2013 and 2012, respectively.

The following tables present segment profit by reportable segment and reconciling items necessary to agree to amounts reported in the condensed consolidated statements of earnings:

	Three Months Ended December 31	
(in millions)	2013	2012
Pharmaceutical	$482	$441

Medical	131	94
Total segment profit	613	535
Corporate	(94)	(29)
Total operating earnings	$519	$506

	Six Months Ended December 31	
(in millions)	2013	2012
Pharmaceutical	$916	$841
Medical	238	168
Total segment profit	1,154	1,009
Corporate	(164)	(46)
Total operating earnings	$990	$963

The following table presents total assets for each reportable segment and reconciling items necessary to agree to amounts reported in the condensed consolidated balance sheets at the dates indicated below:

(in millions)	December 31, 2013	June 30, 2013
Pharmaceutical (1)	$14,985	$16,258
Medical	6,558	6,521
Corporate	3,466	3,040
Total assets	$25,009	$25,819

(1) The decrease in Pharmaceutical segment assets is primarily due to the expiration of our pharmaceutical distribution contract with Walgreens.

13. Share-Based Compensation

Share-Based Compensation Plans

We maintain stock incentive plans (collectively, the “Plans”) for the benefit of certain of our officers, directors and employees. The following tables provide total share-based compensation expense by type of award:

	Three Months Ended December 31	
(in millions)	2013	2012
Restricted share unit expense	$15	$14
Employee stock option expense	5	5
Performance share unit expense	4	3
Total share-based compensation	$24	$22

	Six Months Ended December 31	
(in millions)	2013	2012
Restricted share unit expense	$31	$29
Employee stock option expense	10	12
Performance share unit expense	7	5
Total share-based compensation	$48	$46

The total tax benefit related to share-based compensation was $8 million for both the three months ended December 31, 2013 and 2012,

respectively, and $17 million and $16 million for the six months ended December 31, 2013 and 2012, respectively.

Stock Options

Employee stock options granted under the Plans generally vest in equal annual installments over three years and are exercisable for periods ranging from seven to ten years from the grant date. All stock options are exercisable at a price equal to the market value of the common shares underlying the option on the grant date and, when exercised, are issued out of treasury shares.

The following table summarizes all stock option transactions under the Plans:

(in millions, except per share amounts)	Stock Options	Weighted-Average Exercise Price per Common Share
Outstanding at June 30, 2013	15	$36.97
Granted	2	51.77
Exercised	(4)	39.82
Canceled and forfeited	—	—
Outstanding at December 31, 2013	13	$38.45
Exercisable at December 31, 2013	8	$34.31

At December 31, 2013, the total pre-tax compensation cost, net of estimated forfeitures, related to nonvested stock options not yet recognized was $33 million, which is expected to be recognized over a weighted-average period of two years. The following table provides additional data related to stock option activity at:

(in millions, except contractual lives)	December 31, 2013	June 30, 2013
Aggregate intrinsic value of outstanding options at period end	$356	$156
Aggregate intrinsic value of exercisable options at period end	$262	$113
Weighted-average remaining contractual life of outstanding options (in years)	5	4
Weighted-average remaining contractual life of exercisable options (in years)	3	3

Stock options are granted to our officers and certain employees. The fair values were estimated on the grant date using a lattice valuation model. We believe the lattice model provides reasonable estimates because it has the ability to take into account individual exercise patterns based on changes in our stock price and other variables, and it provides for a range of input assumptions.

Restricted Share Units

Restricted share units granted under the Plans generally vest in equal annual installments over three years. The fair value is determined by the grant date market price of our common shares. Restricted share units accrue cash dividend equivalents that are payable upon vesting of the awards.

The following table summarizes all transactions related to restricted share units under the Plans:

(in millions, except per share amounts)	Restricted Share Units	Weighted-Average Grant Date Fair Value per Share
Nonvested at June 30, 2013	3	$38.74
Granted	1	51.96
Vested	(1)	37.41
Canceled and forfeited	—	—
Nonvested at December 31, 2013	3	$45.20

At December 31, 2013, the total pre-tax compensation cost, net of estimated forfeitures, related to nonvested restricted share units not yet recognized was $102 million, which is expected to be recognized over a weighted-average period of two years.

Performance Share Units

Performance share units vest over a three-year performance period based on achievement of specific performance goals. Based on the extent to which the targets are achieved, vested shares may range from zero to 200 percent of the target award amount. The fair value of performance share units is determined by the grant date market price of our common shares. The compensation expense associated with nonvested performance share units is dependent on our periodic assessment of the probability of the targets being achieved and our estimate of the number of shares that will ultimately be issued. Performance share units accrue cash dividend equivalents that are payable upon vesting of the awards.

During the six months ended December 31, 2013, 274 thousand performance share units were granted at target at a weighted-average fair value per share of $51.49. Also during the six months ended December 31, 2013, 157 thousand performance share units with an initial two-year performance period and a weighted-average grant date fair value per share of $41.60 vested based on achievement of 143 percent of the target performance goal. At December 31, 2013, there were 868 thousand nonvested performance share units with a weighted-average grant date fair value per share of $44.39.

At December 31, 2013, the total pre-tax compensation cost, net of estimated forfeitures, related to nonvested performance share units not yet recognized was $21 million, which is expected to be recognized over a weighted-average period of two years.

Item 2: Management’s Discussion and Analysis of Financial Condition and Results of Operations

The discussion and analysis presented below is concerned with material changes in financial condition and results of operations for our condensed consolidated balance sheets at December 31, 2013 and June 30, 2013, and for our condensed consolidated statements of earnings for the three and six months ended December 31, 2013 and 2012. This discussion and analysis should be read in conjunction with “Management’s Discussion and Analysis of Financial Condition and Results of Operations” included in our 2013 Form 10-K.

Portions of this Form 10-Q (including information incorporated by reference) include “forward-looking statements.” The words “expect,” “anticipate,” “intend,” “plan,” “believe,” “will,” “should,” “could,” “would,” “project,” “continue,” “likel expressions, among others, generally identify “forward-looking statements,” which speak only as of the date the statements were made. The matters discussed in these forward-looking statements are subject to risks, uncertainties and other factors that could cause actual results to differ materially from those made, projected or implied in the forward-looking statements. The most significant of these risks, uncertainties and other factors are described in "Part II, Item 1A: Risk Factors" of this Form 10-Q, Exhibit 99.1 to this Form 10-Q and "Part I, Item 1A: Risk Factors" of our 2013 Form 10-K. Except to the extent required by applicable law, we undertake no obligation to update or revise any forward-looking statements, whether as a result of new information, future events, or otherwise.

Overview

We are a healthcare services company providing pharmaceutical and medical products and services that help pharmacies, hospitals, ambulatory surgery centers, clinical laboratories, physician offices and other healthcare providers focus on patient care while reducing costs, enhancing efficiency and improving quality. We also provide medical products to patients in the home.

We report our financial results in two segments: Pharmaceutical and Medical.

Revenue for the three and six months ended December 31, 2013 was $22.2 billion and $46.8 billion, a 12 percent and 9 percent decrease, respectively, from the prior-year periods largely due to the previously disclosed expiration of our pharmaceutical distribution contract with Walgreen Co. ("Walgreens") on August 31, 2013. Gross margin increased 10 percent to $1.3 billion and 9 percent to $2.6 billion for the three and six months ended December 31, 2013, respectively, reflecting the positive impact of acquisitions, margin rate expansion and sales growth from new and existing pharmaceutical distribution customers, partially offset by the expiration of our pharmaceutical distribution contract with Walgreens.

Operating earnings increased 2 percent to $519 million and 3 percent to $990 million for the three and six months ended December 31, 2013, respectively. Both periods were impacted by the factors discussed above as well as an increase in distribution, selling, general and administrative expenses and intangible asset amortization related to the acquisition of AssuraMed, Inc. ("AssuraMed").

Earnings from continuing operations were down 9 percent to $275 million and up 7 percent to $614 million for the three and six months ended December 31, 2013, respectively. Both periods were impacted by the factors discussed above and a tax charge ($56 million) due to proposed

assessments of additional tax. The six months ended December 31, 2013 also included a $63 million favorable impact from the settlement of federal and state tax controversies during the first quarter of fiscal 2014.

Our cash and equivalents balance was $2.7 billion at December 31, 2013, compared to $1.9 billion at June 30, 2013. The increase in cash and equivalents during the six months ended December 31, 2013 was driven by net cash provided by operating activities of $988 million, which includes the decrease in our net working capital associated with the expiration of our pharmaceutical distribution contract with Walgreens. We plan to continue to execute a balanced deployment of available capital to position ourselves for sustainable competitive advantage and to enhance shareholder value.

Walgreens Contract

The expiration of our pharmaceutical distribution contract with Walgreens unfavorably impacted period-over-period comparisons of revenue and operating earnings during the three and six months ended December 31, 2013. We expect

the contract expiration to have an adverse impact on our period-over-period comparisons of revenue and operating earnings during the remainder of fiscal 2014 and the first quarter of fiscal 2015.

CVS Contracts

In December 2013, we announced the signing of an agreement with CVS Caremark Corporation (“CVS”) to form a U.S.-based generic sourcing entity ("Sourcing JV"). Both companies are contributing their sourcing and supply chain expertise to the 50/50 joint venture and are committing to source generic pharmaceuticals through it. The Sourcing JV, which we expect to be operational as soon as July 1, 2014, will have an initial term of 10 years. Under this arrangement, the Sourcing JV will negotiate generic supply contracts on behalf of both companies; however, it will not own products or hold inventory on behalf of either company. The arrangement includes a quarterly payment of $25 million over the term that we will pay to CVS. No physical assets will be contributed by either company to the Sourcing JV, and minimal funding will be provided to capitalize the entity. The venture is subject to the completion of final documentation and customary closing conditions.

Also during the three months ended December 31, 2013, we entered into a three-year extension, through June 2019, of our existing pharmaceutical distribution contracts with CVS.

Acquisitions

We did not complete any acquisitions that were significant, individually or in the aggregate, during the six months ended December 31, 2013. In March 2013, we acquired AssuraMed, a provider of medical supplies to homecare providers and patients in the home. This acquisition increased revenue and operating earnings for the three and six months ended December 31, 2013.

Trends

While pharmaceutical price appreciation on some generic products positively impacted our margins during the first half of fiscal 2014, there is no assurance that this price appreciation will continue in the future.

Results of Operations

Revenue

	Three Months Ended December 31		
(in millions)	2013	2012	Change
Pharmaceutical	$19,443	$22,747	(15)%
Medical	2,799	2,487	13 %
Total segment revenue	22,242	25,234	(12)%
Corporate	(2)	(2)	N.M.
Total revenue	$22,240	$25,232	(12)%

	Six Months Ended December 31		
(in millions)	2013	2012	Change
Pharmaceutical	$41,256	$46,244	(11)%
Medical	5,511	4,879	13 %
Total segment revenue	46,767	51,123	(9)%
Corporate	(4)	(2)	N.M.
Total revenue	$46,763	$51,121	(9)%

Pharmaceutical Segment

Revenue for the three and six months ended December 31, 2013 compared to the prior-year periods was negatively impacted by the expiration of our pharmaceutical distribution contract with Walgreens ($5.2 billion and $6.9 billion, respectively). Revenue for the six months ended December 31, 2013 was also negatively impacted by the expiration of our pharmaceutical distribution contract with Express Scripts, Inc. on September 30, 2012 ($2.0 billion). These decreases were partially offset by sales growth from new and existing pharmaceutical distribution customers ($1.8 billion and $3.7 billion, respectively).

Medical Segment

Revenue for the three and six months ended December 31, 2013 compared to the prior-year periods reflects the benefit of acquisitions ($278 million and $547 million, respectively) and increased net volume from existing customers ($48 million and $121 million, respectively).

Cost of Products Sold

As a result of the same factors affecting the change in revenue, cost of products sold decreased $3.1 billion (13 percent) and $4.6 billion (9 percent) compared to the prior-year periods. See the gross margin discussion below for additional drivers impacting cost of products sold.

Gross Margin

	Three Months Ended December 31		
(in millions)	2013	2012	Change
Gross margin	$1,345	$1,224	10 %

	Six Months Ended December 31		
(in millions)	2013	2012	Change
Gross margin	$2,608	$2,382	9 %

Gross margin increased during the three and six months ended December 31, 2013 compared to the prior-year periods, driven by the positive impact of acquisitions ($77 million and $150 million, respectively). The increase in gross margin also reflects margin rate expansion ($51 million and $18 million, respectively), excluding the impact from the expiration of our pharmaceutical distribution contract with Walgreens.

Margin rate expansion for both periods was driven by strong performance from both generic programs and branded agreements, including the impact of price appreciation. Gross margin for the three months ended December 31, 2013 was unfavorably impacted by $14 million due to lower sales, which includes the impact from the expiration of our pharmaceutical distribution contract with Walgreens and is partially offset by sales growth from new and existing

pharmaceutical distribution customers. Gross margin for the six months ended December 31, 2013 was positively impacted by $51 million due to sales growth from new and existing pharmaceutical distribution customers and is partially offset by the expiration of our pharmaceutical distribution contract with Walgreens.

Distribution, Selling, General and Administrative ("SG&A") Expenses

	Three Months Ended December 31			
(in millions)	2013	2012	Change	
SG&A expenses	$766	$699	10	%
	Six Months Ended December 31			
(in millions)	2013	2012	Change	
SG&A expenses	$1,497	$1,388	8	%

SG&A expenses increased during the three and six months ended December 31, 2013 compared to the prior-year period primarily due to acquisitions ($37 million and $75 million, respectively).

Segment Profit and Consolidated Operating Earnings

	Three Months Ended December 31			
(in millions)	2013	2012	Change	
Pharmaceutical	$482	$441	9	%
Medical	131	94	40	%
Total segment profit	613	535	15	%
Corporate	(94)	(29)	N.M.	
Total operating earnings	$519	$506	2	%
	Six Months Ended December 31			
(in millions)	2013	2012	Change	
Pharmaceutical	$916	$841	9	%
Medical	238	168	41	%
Total segment profit	1,154	1,009	14	%
Corporate	(164)	(46)	N.M.	
Total operating earnings	$990	$963	3	%

Pharmaceutical Segment Profit

The increase in Pharmaceutical segment profit during the three and six months ended December 31, 2013 was due in part to margin rate expansion, excluding the impact from the expiration of our pharmaceutical distribution contract with Walgreens. Margin rate expansion for both periods was driven by strong performance from both generic programs and branded agreements, including the impact of price appreciation. Pharmaceutical segment profit for the three months ended December 31, 2013 was unfavorably impacted by lower sales, which includes the impact from the expiration of our pharmaceutical distribution contract with Walgreens and is partially offset by sales growth from new and existing pharmaceutical distribution customers. Pharmaceutical segment profit for the six months ended December 31, 2013 was also positively impacted

by sales growth from new and existing pharmaceutical distribution customers and is partially offset by the expiration of our pharmaceutical distribution contract with Walgreens.

Medical Segment Profit

The principal driver for the increase in Medical segment profit during the three and six months ended December 31, 2013 was the positive impact of acquisitions.

Consolidated Operating Earnings

In addition to revenue, gross margin and SG&A expenses discussed above, operating earnings were impacted by the following:

	Three Months Ended December 31	
(in millions)	2013	2012
Restructuring and employee severance	$10	$1
Amortization and other acquisition-related costs	56	25
Impairments and loss on disposal of assets	9	5
Litigation (recoveries)/charges, net	(15)	(12)

	Six Months Ended December 31	
(in millions)	2013	2012
Restructuring and employee severance	$20	$6
Amortization and other acquisition-related costs	105	53
Impairments and loss on disposal of assets	9	6
Litigation (recoveries)/charges, net	(13)	(34)

Restructuring and Employee Severance

On January 30, 2013, we announced a restructuring plan within our Medical segment. Under this restructuring plan, among other things, we are moving production of procedure kits from our facility in Waukegan, Illinois to other facilities and selling property and consolidating office space in Waukegan, Illinois. We recognized restructuring costs of $6 million and $12 million related to this restructuring plan during the three and six months ended December 31, 2013, respectively, which primarily consisted of facility exit and other costs.

We currently estimate the total costs associated with this restructuring plan to be approximately $77 million on a pre-tax basis, of which $51 million was recognized in fiscal 2013 and $20 million was recognized during the six months ended December 31, 2013, including the write-down of the property in Waukegan, Illinois as discussed below. The estimated $6 million remaining costs to be recognized through the end of fiscal 2014 consist of facility exit and other costs.

Amortization and Other Acquisition-Related Costs

Amortization of acquisition-related intangible assets was $46 million and $22 million for the three months ended December 31, 2013 and 2012, respectively, and $91 million and $43 million for the six months ended December 31, 2013 and 2012, respectively. The increase in amortization during the three and six months ended December 31, 2013 was primarily due to intangible assets from the acquisition of AssuraMed.

Impairments and Loss on Disposal of Assets

In connection with our Medical segment restructuring plan, during the three months ended December 31, 2013, we recognized an $8 million loss to write down property in Waukegan, Illinois to the estimated fair value, less costs to sell.

Litigation (Recoveries)/Charges, Net

We recognized income resulting from settlements of class action antitrust claims in which we were a class member of $16 million and $12 million during the three months ended December 31, 2013 and 2012, respectively, and $16 million and $34 million during the six months ended December 31, 2013 and 2012, respectively.

Earnings Before Income Taxes and Discontinued Operations

In addition to the items discussed above, earnings before income taxes and discontinued operations were impacted by the following:

	Three Months Ended December 31			
(in millions)	2013	2012	Change	
Other income, net	$(6)	$(4)	N.M.	
Interest expense, net	33	27	23	%
	Six Months Ended December 31			
(in millions)	2013	2012	Change	
Other income, net	$(10)	$(12)	N.M.	
Interest expense, net	66	53	25	%

Interest Expense, Net

The increase in interest expense, net for the three and six months ended December 31, 2013 compared to the prior-year period was primarily due to $1.3 billion of notes issued in connection with the AssuraMed acquisition during the third quarter of fiscal 2013.

Provision for Income Taxes

Generally, fluctuations in the effective tax rate are due to changes within international and U.S. state effective tax rates resulting from our business mix and discrete items.

During the three months ended December 31, 2013, the effective tax rate of 44.1 percent was impacted by net unfavorable discrete items of $38 million, which increased the rate by 7.7 percentage points. The discrete items include the unfavorable impact of remeasurement of unrecognized tax benefits ($56 million) as a result of proposed assessments of additional tax.

During the six months ended December 31, 2013, the effective tax rate of 34.2 percent was impacted by net favorable discrete items of $23 million, which reduced the rate by 2.4 percentage points. The discrete items include the favorable impact of the settlement of federal and state tax controversies ($67 million) and the unfavorable impact of remeasurement of unrecognized tax benefits ($56 million).

During the three and six months ended December 31, 2012, the effective tax rate of 37.2 percent and 37.6 percent was impacted by net unfavorable discrete items of $2 million and $6 million, which increased the rate by 0.3 and 0.6 percentage points, respectively.

Ongoing Audits

During the six months ended December 31, 2013, the U.S. Internal Revenue Service ("IRS") closed audits of fiscal years 2003 through 2005. The IRS is currently conducting audits of fiscal years 2006 through 2010.

Liquidity and Capital Resources

We currently believe that, based upon available capital resources (cash on hand and access to committed credit facilities) and projected operating

cash flow, we have adequate capital resources to fund working capital needs; currently anticipated capital expenditures, business growth and expansion; contractual obligations; payments for tax settlements; and current and projected debt service requirements, dividends and share repurchases. If we decide to engage in one or more additional acquisitions, depending on the size and timing of such transactions, we may need to access capital in addition to cash on hand and our existing committed credit facilities.

Cash and Equivalents

Our cash and equivalents balance was $2.7 billion at December 31, 2013, compared to $1.9 billion at June 30, 2013. At December 31, 2013, our cash and equivalents were held in cash depository accounts with major banks or invested in high quality, short-term liquid investments.

The increase in cash and equivalents during the six months ended December 31, 2013 was driven by net cash provided by operating activities of $988 million, offset by dividends of $208 million.

Net cash provided by operating activities of $988 million includes the impact of the expiration of our pharmaceutical distribution contract with Walgreens, which resulted in a significant net working capital decrease. Net cash provided by operating activities was also impacted by other changes in working capital, including the timing of inventory purchases.

We use days sales outstanding ("DSO"), days inventory on hand ("DIOH") and days payable outstanding ("DPO") to evaluate our working capital performance.

	December 31	
	2013	2012
Days sales outstanding	19.7	22.0
Days inventory on hand (1)	29.7	27.0
Days payable outstanding (1)	39.3	37.8

(1) Chargeback billings, which are used in the above calculations, were $4.8 billion and $4.1 billion for the three months ended December 31, 2013 and 2012, respectively.

Changes in working capital can vary significantly depending on factors such as customer payments of accounts receivable, the timing of inventory purchases and payments to vendors in the regular course of business.

The changes in DSO and DPO are primarily a result of the expiration of our pharmaceutical distribution contract with Walgreens. DIOH increased primarily as a result of the expiration of our pharmaceutical distribution contract with Walgreens and the timing of inventory purchases.

The cash and equivalents balance at December 31, 2013 included $446 million of cash held by subsidiaries outside of the United States. Although the vast majority of this cash is available for repatriation, permanently bringing the money into the United States could trigger U.S. federal, state and local income tax obligations. As a U.S. parent company, we may temporarily access cash held by our foreign subsidiaries without becoming subject to U.S. federal income tax through intercompany loans.

Credit Facilities and Commercial Paper

On October 15, 2013, we reduced our committed receivables sales facility program from $950 million to $700 million in light of the expiration of our pharmaceutical distribution contract with Walgreens. In addition to our committed receivables sales facility, our sources of liquidity include a $1.5 billion revolving credit facility and a commercial paper program of up to $1.5 billion, backed by the revolving credit facility.

We had no outstanding balance under the committed receivables sales facility program and no outstanding borrowings from the commercial paper program at December 31, 2013. We also had no outstanding balance under the revolving credit facility at December 31, 2013, except for $42 million of standby letters of credit. Our revolving credit facility and committed receivables sales facility program require us to maintain a consolidated interest coverage ratio, as of any fiscal quarter end, of at least 4-to-1 and a consolidated leverage ratio of no more than 3.25-to-1. As of December 31, 2013, we were in compliance with these financial covenants.

Capital Expenditures

Capital expenditures were $90 million and $62 million during the six months ended December 31, 2013 and 2012, respectively.

Dividends

On November 6, 2013, our Board of Directors approved the quarterly dividend of $0.3025 per share, or $1.21 on an annualized basis, which was paid on January 15, 2014 to shareholders of record on January 2, 2014.

On February 5, 2014, our Board of Directors approved our 118th consecutive regular quarterly dividend, payable to shareholders of record on April 1, 2014.

Share Repurchases

During the six months ended December 31, 2013, we repurchased $50 million of our common shares. We funded the repurchases with cash on hand.

On October 29, 2013, our Board of Directors approved a $1.0 billion share repurchase program, which expires on December 31, 2016. At December 31, 2013, we had $1.35 billion remaining under our current repurchase authorization, of which $350 million expires on August 31, 2015 and the remainder expires on December 31, 2016.

Off-Balance Sheet Arrangements

We had no significant off-balance sheet arrangements at December 31, 2013.

Contractual Obligations

Other than our agreement with CVS to form the Sourcing JV, there has been no material change in our outstanding contractual obligations since the end of fiscal 2013 through December 31, 2013.

Recent Financial Accounting Standards

See Note 1 of the “Notes to Condensed Consolidated Financial Statements” for a discussion of recent financial accounting standards.

Critical Accounting Policies and Sensitive Accounting Estimates

Refer to the Critical Accounting Policies and Sensitive Accounting Estimates section of "Part II, Item 7: Management's Discussion and Analysis of Financial Condition and Results of Operations" in our 2013 Form 10-K. There have been no material changes to our critical accounting policies and sensitive accounting estimates since the end of fiscal 2013 through December 31, 2013.

Item 3: Quantitative and Qualitative Disclosures About Market Risk

There have been no material changes in the quantitative and qualitative market risks since the end of fiscal 2013 through December 31, 2013 from those reported in our 2013 Form 10-K.

Item 4: Controls and Procedures

Evaluation of Disclosure Controls and Procedures

We evaluated, with the participation of our principal executive officer and principal financial officer, the effectiveness of our disclosure controls and procedures (as defined in Rule 13a-15(e) under the Securities Exchange Act of 1934 (the "Exchange Act")) as of December 31, 2013. Based on this evaluation, our principal executive officer and principal financial officer have concluded that our disclosure controls and procedures were effective as of December 31, 2013 to provide reasonable assurance that information required to be disclosed in our reports under the Exchange Act is recorded, processed, summarized and reported within the time periods specified in the SEC rules and forms and that such information is accumulated and communicated to management to allow timely decisions regarding required disclosure.

Changes in Internal Control Over Financial Reporting

There were no changes in our internal control over financial reporting during the quarter ended December 31, 2013 that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

Item 1: Legal Proceedings

In addition to the proceedings described below, the legal proceedings described in Note 6 of the "Notes to Condensed Consolidated Financial Statements" are incorporated in this "Item 1: Legal Proceedings" by reference.

In June 2012, Henry Stanley, Jr., a purported shareholder, filed a derivative action on behalf of Cardinal Health, Inc. in the U.S. District Court for the Southern District of Ohio (the "federal action") against the current and certain former members of our Board of Directors. A similar action was filed by Daniel Himmel, a purported shareholder, in the Common Pleas Court of Delaware County, Ohio (the "state action") against the current and certain former members of our Board of Directors and certain of our officers. The complaints alleged that the defendants breached their fiduciary duties in connection with the U.S. Drug Enforcement Administration's suspension of our Lakeland, Florida distribution center's registration to distribute controlled substances in February 2012, and the suspension and reinstatement of such registrations at three of our facilities in 2007 and 2008. The state action also made claims based on corporate waste and unjust enrichment. The complaints sought, among other things, unspecified money damages from the defendants and an award of attorney's fees. In October 2012, the U.S. District Court dismissed the federal action with prejudice, and in August 2013, the U.S. Court of Appeals affirmed the decision. In July 2013, the Common Pleas Court dismissed the state action, and in October 2013, the plaintiff voluntarily dismissed an appeal of the court's decision with prejudice. In September 2013, the plaintiff in the federal action made demand on our Board of Directors to take action against current and certain former members of our Board of Directors to recover damages based on the allegations made in the federal action. A special committee of independent directors investigated the allegations made in the demand. After receiving and evaluating the special committee's findings and recommendations, our Board of Directors determined in February 2014 that pursuing the claims set forth in the shareholder demand was not in the best interest of the company.

Item 1A: Risk Factors

You should carefully consider the risk factor below and other information in this Form 10-Q and the risk factors discussed in "Part I, Item 1A: Risk Factors" and other risks discussed in our 2013 Form 10-K and our filings with the SEC since June 30, 2013. These risks could materially and adversely affect our results of operations, financial condition, liquidity and cash flows. Our business also could be affected by risks that we are not presently aware of or that we currently consider immaterial to our operations.

The anticipated benefits of our generic sourcing joint venture with CVS may not be realized.

In December 2013, we and CVS signed an agreement to form the Sourcing JV and we agreed to pay CVS $25 million per quarter over 10 years. If we are unable to successfully and timely implement the Sourcing JV or if we do not realize the expected benefits from the Sourcing JV, our results of operations and financial condition could be adversely affected.

Item 2: Unregistered Sales of Equity Securities and Use of Proceeds

The following table provides information about purchases we made of our common shares during the three months ended December 31, 2013:

Issuer Purchases of Equity Securities

Period	Total Number of Shares Purchased (1)	Average Price Paid per Share	Total Number of Shares Purchased as Part of Publicly Announced Programs (2)	Approximate Dollar Value of Shares That May Yet be Purchased Under the Programs (2) (in millions)
October 1 – 31, 2013	470	$54.44	—	$1,350

November 1 – 30, 2013	5,430	64.47	—	1,350
December 1 – 31, 2013	254	66.68	—	1,350
Total	6,154	$63.80	—	$1,350

(1) Includes 470, 287 and 254 common shares purchased in October, November and December 2013, respectively, through a rabbi trust as investments of participants in our Deferred Compensation Plan and 5,143 common shares tendered in November 2013 by equity compensation plan participants to satisfy tax withholding and pay the exercise price upon exercise of outstanding stock options.

(2) On August 8, 2012, our Board of Directors approved a $750 million share repurchase program, which expires on August 31, 2015. On October 29, 2013, our Board of Directors approved an additional $1.0 billion share repurchase program, which expires on December 31, 2016. During the three months ended December 31, 2013, we did not repurchase any of our common shares under these programs.

Item 6: Exhibits

Exhibit Number	Exhibit Description
3.1	Amended and Restated Articles of Incorporation of Cardinal Health, Inc., as amended (incorporated by reference to Exhibit 3.1 to Cardinal Health's Quarterly Report on Form 10-Q for the quarter ended September 30, 2008, File No. 1-11373)
3.2	Cardinal Health, Inc. Restated Code of Regulations (incorporated by reference to Exhibit 3.2 to Cardinal Health's Current Report on Form 8-K filed on August 10, 2012, File No. 1-11373)
10.1	Fourth Amended and Restated Receivables Purchase Agreement, dated as of November 1, 2013, among Cardinal Health Funding, LLC, as Seller, Griffin Capital, LLC, as Servicer, the Conduits party thereto, the Financial Institutions party thereto, the Managing Agents party thereto, the LC Banks party thereto and The Bank of Tokyo-Mitsubishi UFJ, Ltd., New York Branch, as the Agent (incorporated by reference to Exhibit 10.1 to Cardinal Health's Quarterly Report on Form 10-Q for the quarter ended September 30, 2013, File No. 1-11373)
10.2	Fifth Amended and Restated Performance Guaranty, dated as of November 1, 2013, executed by Cardinal Health, Inc. in favor of Cardinal Health Funding, LLC (incorporated by reference to Exhibit 10.2 to Cardinal Health's Quarterly Report on Form 10-Q for the quarter ended September 30, 2013, File No. 1-11373)
12.1	Computation of Ratio of Earnings to Fixed Charges
31.1	Certification of Chief Executive Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
31.2	Certification of Chief Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
32.1	Certification of Chief Executive Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002
32.2	Certification of Chief Financial Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002
99.1	Statement Regarding Forward-Looking Information
101.INS	XBRL Instance Document
101.SCH	XBRL Taxonomy Extension Schema Document
101.CAL	XBRL Taxonomy Extension Calculation Linkbase Document
101.DEF	XBRL Taxonomy Definition Linkbase Document
101.LAB	XBRL Taxonomy Extension Label Linkbase Document
101.PRE	XBRL Taxonomy Extension Presentation Linkbase Document

Cardinal Health Website

We use our website as a channel of distribution for material information about us. Important information, including news releases, earnings and analyst presentations and financial information is routinely posted and accessible on the Investors page at www.cardinalhealth.com. In addition, our website allows investors and other interested persons to sign up to automatically receive email alerts when we post news releases, SEC filings and certain other information on our website.

Table of Contents

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.

Cardinal Health, Inc.

Date: February 6, 2014

/s/ GEORGE S. BARRETT
George S. Barrett
Chairman and Chief Executive Officer

/s/ JEFFREY W. HENDERSON
Jeffrey W. Henderson
Chief Financial Officer