

IDEXX LABORATORIES INC /DE
Form 10-Q
October 22, 2010
UNITED STATES

SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549

FORM 10-Q

(Mark One)

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

For the quarterly period ended September 30, 2010

OR

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

For the transition period from _____ to _____.

COMMISSION FILE NUMBER: 0-19271

IDEXX LABORATORIES, INC.
(Exact name of registrant as specified in its charter)

DELAWARE
(State or other jurisdiction of incorporation
or organization)

01-0393723
(IRS Employer Identification No.)

ONE IDEXX DRIVE, WESTBROOK, MAINE
(Address of principal executive offices)

04092
(ZIP Code)

207-556-0300
(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 (Do not check if a smaller reporting company) Smaller reporting company

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

Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date. The number of shares outstanding of the registrant's Common Stock, \$0.10 par value, was 57,503,819 on October 18, 2010.

IDEXX LABORATORIES, INC.
 Quarterly Report on Form 10-Q
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PART I — FINANCIAL INFORMATION

Item 1. Financial Statements.

IDEXX LABORATORIES, INC. AND SUBSIDIARIES

CONDENSED CONSOLIDATED BALANCE SHEETS

(in thousands, except per share amounts)

(Unaudited)

	September 30, 2010	December 31, 2009
ASSETS		
Current Assets:		
Cash and cash equivalents	\$ 133,512	\$ 106,728
Accounts receivable, net of reserves of \$3,089 in 2010 and \$2,331 in 2009	120,454	115,107
Inventories, net	131,555	110,425
Deferred income tax assets	24,902	25,188
Other current assets	19,488	18,890
Total current assets	429,911	376,338
Long-Term Assets:		
Property and equipment, net	200,610	199,946
Goodwill	148,597	148,705
Intangible assets, net	57,554	63,907
Other long-term assets, net	25,625	19,631
Total long-term assets	432,386	432,189
TOTAL ASSETS	\$ 862,297	\$ 808,527
LIABILITIES AND STOCKHOLDERS' EQUITY		
Current Liabilities:		
Accounts payable	\$ 25,273	\$ 19,133
Accrued liabilities	108,184	104,959
Line of credit	125,912	118,790
Current portion of long-term debt	850	813
Current portion of deferred revenue	10,714	12,610
Total current liabilities	270,933	256,305
Long-Term Liabilities:		
Deferred income tax liabilities	20,491	18,283
Long-term debt, net of current portion	3,639	4,281
Long-term deferred revenue, net of current portion	8,156	3,813
Other long-term liabilities	12,426	11,266
Total long-term liabilities	44,712	37,643
Total liabilities	315,645	293,948
Commitments and Contingencies (Note 12)		
Stockholders' Equity:		
Common stock, \$0.10 par value: Authorized: 120,000 shares;		
Issued: 97,618 and 96,334 shares in 2010 and 2009, respectively	9,762	9,633

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Additional paid-in capital	626,521	580,797
Deferred stock units: Outstanding: 117 units in 2010 and 2009	4,391	4,301
Retained earnings	929,169	824,256
Accumulated other comprehensive income	11,429	10,341
Treasury stock, at cost: 40,249 and 38,118 shares in 2010 and 2009, respectively	(1,034,658)	(914,759)
Total IDEXX Laboratories, Inc. stockholders' equity	546,614	514,569
Noncontrolling interest	38	10
Total stockholders' equity	546,652	514,579
TOTAL LIABILITIES AND STOCKHOLDERS' EQUITY	\$ 862,297	\$ 808,527

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

IDEXX LABORATORIES, INC. AND SUBSIDIARIES
 CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS
 (in thousands, except per share amounts)
 (Unaudited)

	For the Three Months Ended September 30,		For the Nine Months Ended September 30,	
	2010	2009	2010	2009
Revenue:				
Product revenue	\$ 173,297	\$ 171,527	\$ 529,871	\$ 503,488
Service revenue	96,331	87,593	289,764	257,810
Total revenue	269,628	259,120	819,635	761,298
Cost of Revenue:				
Cost of product revenue	67,076	71,543	207,773	202,114
Cost of service revenue	60,345	57,100	178,010	165,834
Total cost of revenue	127,421	128,643	385,783	367,948
Gross profit	142,207	130,477	433,852	393,350
Expenses:				
Sales and marketing	44,486	41,504	133,069	124,365
General and administrative	30,704	28,185	96,588	88,047
Research and development	17,203	16,583	51,118	49,116
Income from operations	49,814	44,205	153,077	131,822
Interest expense	(687)	(436)	(1,741)	(1,535)
Interest income	136	48	327	348
Income before provision for income taxes	49,263	43,817	151,663	130,635
Provision for income taxes	14,548	12,281	46,723	39,361
Net income	34,715	31,536	104,940	91,274
Less: Net income attributable to noncontrolling interest	21	-	27	-
Net income attributable to IDEXX Laboratories, Inc. stockholders	\$ 34,694	\$ 31,536	\$ 104,913	\$ 91,274
Earnings per Share:				
Basic	\$ 0.60	\$ 0.54	\$ 1.82	\$ 1.55
Diluted	\$ 0.59	\$ 0.52	\$ 1.76	\$ 1.50
Weighted Average Shares Outstanding:				
Basic	57,620	58,656	57,799	58,911
Diluted	59,276	60,668	59,691	60,718

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

IDEXX LABORATORIES, INC. AND SUBSIDIARIES
 CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
 (in thousands)
 (Unaudited)

	For the Nine Months Ended September 30,	
	2010	2009
Cash Flows from Operating Activities:		
Net income	\$ 104,940	\$ 91,274
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	34,117	37,218
Loss on disposal of property and equipment	1,500	2,324
Increase in deferred compensation liability	135	370
Write-down of marketable securities	-	150
Provision for uncollectible accounts	1,506	674
Provision for deferred income taxes	1,379	3,705
Share-based compensation expense	9,787	8,849
Tax benefit from exercises of stock options and vesting of restricted stock units	(13,293)	(3,851)
Changes in assets and liabilities, net of acquisitions:		
Accounts receivable	(6,916)	(1,132)
Inventories	(22,460)	(8,145)
Other assets	(5,836)	(3,126)
Accounts payable	6,107	(6,868)
Accrued liabilities	16,447	(5,241)
Deferred revenue	2,570	(698)
Net cash provided by operating activities	129,983	115,503
Cash Flows from Investing Activities:		
Purchases of property and equipment	(28,646)	(36,362)
Proceeds from disposition of pharmaceutical product lines	-	1,377
Proceeds from sale of property and equipment	86	2,056
Acquisitions of intangible assets	(244)	-
Acquisitions of businesses, net of cash acquired	-	(6,680)
Net cash used by investing activities	(28,804)	(39,609)
Cash Flows from Financing Activities:		
Borrowings (payments) on revolving credit facilities, net	7,135	(8,798)
Payment of other notes payable	(605)	(731)
Purchase of treasury stock	(117,157)	(57,966)
Proceeds from exercises of stock options and employee stock purchase plans	22,055	13,104
Tax benefit from exercises of stock options and vesting of restricted stock units	13,293	3,851
Net cash used by financing activities	(75,279)	(50,540)
Net effect of changes in exchange rates on cash	884	2,506
Net increase in cash and cash equivalents	26,784	27,860
Cash and cash equivalents at beginning of period	106,728	78,868
Cash and cash equivalents at end of period	\$ 133,512	\$ 106,728

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

IDEXX LABORATORIES, INC. AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited)

NOTE 1. BASIS OF PRESENTATION AND PRINCIPLES OF CONSOLIDATION

The accompanying condensed consolidated financial statements of IDEXX Laboratories, Inc. ("IDEXX," the "Company," "we" or "our") have been prepared in accordance with accounting principles generally accepted in the United States of America ("U.S. GAAP") for interim financial information and with the requirements of Regulation S-X, Rule 10-01 for financial statements required to be filed as a part of Form 10-Q.

The accompanying condensed consolidated financial statements include the accounts of IDEXX Laboratories, Inc. and our wholly-owned and majority-owned subsidiaries. All material intercompany transactions and balances have been eliminated in consolidation.

The accompanying condensed consolidated financial statements reflect, in the opinion of our management, all adjustments necessary for a fair presentation of our financial position and results of operations. All such adjustments are of a recurring nature. The consolidated balance sheet data at December 31, 2009 was derived from audited financial statements, but does not include all disclosures required by U.S. GAAP. The results of operations for the nine months ended September 30, 2010 are not necessarily indicative of the results to be expected for the full year or any future period. These condensed consolidated financial statements should be read in conjunction with this Quarterly Report on Form 10-Q for the quarter ended September 30, 2010, and our Annual Report on Form 10-K for the year ended December 31, 2009 filed with the Securities and Exchange Commission.

Certain reclassifications have been made to the prior year condensed consolidated financial statements to conform to the current year presentation. Reclassifications had no material impact on previously reported results of operations, financial position or cash flows.

NOTE 2. ACCOUNTING POLICIES

Significant Accounting Policies

The significant accounting policies used in preparation of these condensed consolidated financial statements for the nine months ended September 30, 2010 are consistent with those discussed in Note 3 to the consolidated financial statements in our Annual Report on Form 10-K for the year ended December 31, 2009, except for the adoption of new accounting standards during the nine months ended September 30, 2010 as discussed below.

Recent Accounting Pronouncements

On January 1, 2010, we adopted amendments to authoritative literature that modify the revenue recognition guidance for establishing separate units of accounting in a multiple element arrangement and requires the allocation of arrangement consideration to each deliverable in the arrangement based on relative selling price of the elements. The selling price for each deliverable is based on vendor-specific objective evidence ("VSOE") if available, third-party evidence ("TPE") if VSOE is not available, or best estimate of selling price ("BESP") if neither VSOE nor TPE is available. BESP must be determined in a manner that is consistent with that used to determine the price to sell the specific elements on a standalone basis. The authoritative literature permits prospective or retrospective adoption, and we elected prospective adoption. The adoption of these amendments did not have a significant impact on our financial position, results of operations, or cash flows for the nine months ended September 30, 2010, nor do we anticipate a

significant impact for the year ended December 31, 2010.

On January 1, 2010, we adopted amendments to authoritative literature that modify the revenue recognition guidance for the sale of tangible products that contain software that is more than incidental to the functionality of the product as a whole. More specifically, the revised accounting guidance indicates that when a product has tangible and software components that function together to deliver the essential functionality of the product as a whole, that product should be excluded from the scope of software revenue accounting guidance, as opposed to the previous accounting guidance where such an instrument would be subject to the rules detailed in the software revenue guidance. The authoritative literature permits prospective or retrospective adoption, and we elected prospective adoption. Certain sales of our instruments are subject to these amendments. However, the adoption of these amendments did not have a significant impact on our financial position, results of operations, or cash flows for the nine months ended September 30, 2010, nor do we anticipate a significant impact for the year ended December 31, 2010.

Our updated revenue recognition policy in its entirety reflecting the adoption of these amendments is provided in the following discussion.

Revenue Recognition

We recognize revenue when four criteria are met: (i) persuasive evidence that an arrangement exists; (ii) delivery has occurred or services have been rendered; (iii) the sales price is fixed or determinable; and (iv) collectability is reasonably assured. Revenue-generating transactions generally fall into one of the following categories of revenue recognition:

- We recognize revenue at the time of shipment to U.S. distributors for substantially all products sold through distributors because title and risk of loss pass to the distributors on delivery to the common carrier. Our distributors do not have the right to return products. We recognize revenue for the remainder of our customers when the product is delivered to the customer, except as noted below.
- We recognize revenue from the sales of instruments, non-cancelable software licenses and hardware systems upon installation (and completion of training if applicable) and the customer's acceptance of the instrument or system as we have no significant further obligations after this point in time.
 - We recognize service revenue at the time the service is performed.
- We recognize revenue associated with extended maintenance agreements ("EMAs") over the life of the contracts using the straight-line method, which approximates the expected timing in which applicable services are performed. Amounts collected in advance of revenue recognition are recorded as a current or long-term liability based on the time from the balance sheet date to the future date of revenue recognition.
- We recognize revenue on certain instrument systems under rental programs over the life of the rental agreement using the straight-line method. Amounts collected in advance of revenue recognition are recorded as a current or long-term liability based on the time from the balance sheet date to the future date of revenue recognition.
- We recognize revenue on practice information management systems sales either by allocating the revenue to each element of the sale based on relative fair values of the elements, including post-contract support when fair value for all elements is available, or by use of the residual method when only the fair value of the post-contract support is available. We recognize revenue for the system upon installation and customer acceptance and recognize revenue equal to the fair value of the post-contract support over the support period.
 - Shipping costs reimbursed by the customer are included in revenue.

Multiple element arrangements ("MEAs"). Arrangements to sell products to customers frequently include multiple deliverables. Our most significant MEAs include the sale of one or more of the instruments from the IDEXX VetLab® suite of analyzers or digital radiography systems, combined with one or more of the following products: EMAs; consumables; laboratory diagnostic and consulting services; and practice management software. Practice management software is frequently sold with post-contract customer support and implementation services. Delivery of the various products or performance of services within the arrangement may or may not coincide. Delivery of our IDEXX VetLab® instruments, digital radiography systems, and practice management software generally occurs at the onset of the arrangement. EMAs, consumables, and laboratory diagnostic and consulting services generally are delivered over a period of one to five years. In certain arrangements revenue recognized is limited to the amount invoiced or received that is not contingent on the delivery of future products and services.

When arrangements outside of the scope of software revenue recognition guidance include multiple elements, we allocate revenue to each element based on the relative selling price and recognize revenue when the elements have standalone value and the four criteria for revenue recognition have been met for each element. We establish the selling price of each element based on VSOE if available, TPE if VSOE is not available, or BESP if neither VSOE nor TPE is available. We generally determine selling price based on amounts charged separately for the delivered and undelivered elements to similar customers in standalone sales of the specific elements. When arrangements outside of the scope of software revenue recognition guidance include a separately-priced EMA, we recognize revenue related to the EMA at the stated contractual price on a straight-line basis over the life of the agreement. If there is no stated contractual price for an EMA, we recognize revenue according to the MEA policy stated above.

When arrangements within the scope of software revenue recognition guidance include multiple elements, we allocate revenue to each element based on relative fair value when VSOE exists for all elements or residual fair value when there is VSOE for the undelivered elements but no such evidence for the delivered elements. When allocating revenue based on residual fair value, the fair value of the undelivered elements is deferred and the residual revenue is allocated to the delivered elements. Revenue is recognized on any delivered elements when the four criteria for revenue recognition have been met for each element. If VSOE does not exist for the allocation of revenue to the various elements of the arrangement, all revenue from the arrangement is deferred until the earlier of the point at which such sufficient VSOE does exist or all elements of the arrangement have been delivered. We generally determine fair value based on amounts charged separately for the delivered and undelivered elements to similar customers in standalone sales of the specific elements.

Customer programs. We record estimated reductions to revenue in connection with customer marketing programs and incentive offerings that may give customers rebates or award points, or provide other incentives. Award points granted under our IDEXX Points programs may be applied to trade receivables owed to us and/or toward future purchases of our products or services. We establish accruals for estimated revenue reductions attributable to customer programs and incentive offerings for each program. Revenue reductions are recorded quarterly based on issuance of credits, points earned but not yet issued, and estimates of credits and points to be earned in the future based on current revenue. As points are redeemed we recognize the benefit of points expected to expire, or breakage, using historical forfeiture rates. On November 30 of each year, unused points granted before January 1 of the prior year expire and any variance from the breakage estimate is accounted for as a change in estimate.

Within our overall IDEXX Points program, our two most significant customer programs are Practice Developer® and SNAP® up the Savings™ (“SUTS”), both of which are offered only to North American customers. Our Practice Developer® program is a Companion Animal Group (“CAG”) awards program that permits customers to earn points by purchasing quarterly minimums in certain product and service categories, including IDEXX Reference Laboratories services, certain instrument consumables and service and maintenance agreements. For the Practice Developer® program, the accrued revenue reduction is calculated each quarter based on sales to end users during the quarter by either us or our distributors and on our estimate of future points to be issued upon sale of applicable product inventories held by distributors at the end of the quarter. SUTS is our volume incentive program for selected SNAP® tests that provides customers with benefits in the form of (1) discounts off invoice at the time of purchase and (2) points under the IDEXX Points program awarded and paid out quarterly throughout the SUTS program year (which ends on August 31) based on total purchase volume of qualified SNAP® products during the given quarter.

Doubtful accounts receivable. We recognize revenue only in those situations where collection from the customer is reasonably assured. We maintain allowances for doubtful accounts for estimated losses resulting from the inability of our customers to make required payments. We base our estimates on a detailed analysis of specific customer situations and a percentage of our accounts receivable by aging category. If the financial condition of our customers were to deteriorate, resulting in an impairment of their ability to make payments, additional allowances might be required. Account balances are charged off against the allowance when we believe the receivable will not be recovered.

NOTE 3. SHARE-BASED COMPENSATION

The following is a summary of the fair value of options, restricted stock units, deferred stock units with vesting conditions and employee stock purchase rights awarded, and share-based compensation expense incurred during the three and nine months ended September 30, 2010 and 2009 (in thousands):

	For the Three Months Ended		For the Nine Months Ended	
	September 30,		September 30,	
	2010	2009	2010	2009
Fair value of share-based compensation awards	\$ 451	\$ 437	\$ 15,806	\$ 15,692
Share-based compensation expense	3,129	2,852	9,641	8,658

The total unrecognized compensation expense for unvested awards outstanding at September 30, 2010 was \$28.1 million, net of approximately \$2.7 million related to estimated forfeitures. The weighted average remaining expense recognition period at September 30, 2010 was approximately 1.9 years.

Options

We determine the assumptions used in the valuation of option awards as of the date of grant. Differences in the stock price volatility, terms of options granted to different segments of recipients, or risk-free interest rates may necessitate distinct valuation assumptions at those grant dates. As such, we may use different assumptions for options granted throughout the year. Option awards are granted with an exercise price equal to not less than the closing market price of our common stock at the date of grant. We have never paid any cash dividends on our common stock and we have no present intention to pay a dividend; therefore, we assume that no dividends will be paid over the expected terms of option awards. The weighted averages of the valuation assumptions used to determine the fair value of each option award on the date of grant and the weighted average estimated fair values were as follows:

	For the Nine Months Ended	
	September 30,	
	2010	2009
Expected stock price volatility	31%	30%
Expected term, in years	4.9	4.8
Risk-free interest rate	2.3%	1.6%
Weighted average fair value of options granted	\$ 16.56	\$ 9.97

NOTE 4. INVENTORIES

Inventories include material, labor and overhead, and are stated at the lower of cost (first-in, first-out) or market. The components of inventories were as follows (in thousands):

	September 30,	December 31,
	2010	2009
Raw materials	\$ 26,972	\$ 28,426
Work-in-process	15,760	17,761

Finished goods	88,823	64,238
	\$ 131,555	\$ 110,425

NOTE 5. GOODWILL AND OTHER INTANGIBLE ASSETS

The changes in goodwill and intangible assets other than goodwill during the nine months ended September 30, 2010 resulted primarily from continued amortization of our intangible assets.

NOTE 6. ACCRUED LIABILITIES

Accrued liabilities consisted of the following (in thousands):

	September 30, 2010	December 31, 2009
Accrued expenses	\$ 35,099	\$ 33,094
Accrued employee compensation and related expenses	44,692	44,497
Accrued taxes	5,146	9,980
Accrued customer programs	23,247	17,388
	\$ 108,184	\$ 104,959

NOTE 7. WARRANTY RESERVES

We provide for the estimated cost of instrument warranties in cost of product revenue at the time revenue is recognized based on the estimated cost to repair the instrument over its warranty period. As we develop and sell new instruments, our provision for warranty expense increases. Cost of product revenue reflects not only estimated warranty expense for the systems sold in the current period, but also any changes in estimated warranty expense for the installed base that results from our quarterly evaluation of service experience. Our actual warranty obligation is affected by instrument performance in the customers' environments and costs incurred in servicing instruments. Should actual service rates or costs differ from our estimates, which are based on historical data and projections of future costs, revisions to our estimated warranty liability would be required.

The following is a summary of changes in accrued warranty reserves during the three and nine months ended September 30, 2010 and 2009 (in thousands):

	For the Three Months Ended September 30,		For the Nine Months Ended September 30,	
	2010	2009	2010	2009
Balance, beginning of period	\$ 2,597	\$ 3,099	\$ 3,086	\$ 2,837
Provision for warranty expense	740	1,225	2,314	3,357
Change in estimate	(463)	(225)	(1,021)	(573)
Settlement of warranty liability	(760)	(1,139)	(2,265)	(2,661)
Balance, end of period	\$ 2,114	\$ 2,960	\$ 2,114	\$ 2,960

NOTE 8. TREASURY STOCK

We primarily acquire shares by means of repurchases in the open market. We also acquire shares that are surrendered by employees in payment for the minimum required withholding taxes due on the exercise of stock options, the vesting of restricted stock units and the settlement of deferred stock units, and in payment for the exercise price of stock options.

The following is a summary of our treasury stock purchases and other receipts for the three and nine months ended September 30, 2010 and 2009 (in thousands, except per share amounts):

	For the Three Months Ended September 30,	For the Nine Months Ended September 30,
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	2010	2009	2010	2009
Shares acquired	569	375	2,131	1,467
Total cost of shares acquired	\$ 33,577	\$ 18,375	\$ 119,899	\$ 59,191
Average cost per share	\$ 58.98	\$ 48.99	\$ 56.25	\$ 40.34

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NOTE 9. INCOME TAXES

The following is a summary of our effective income tax rates for the three and nine months ended September 30, 2010 and 2009:

	For the Three Months Ended		For the Nine Months Ended	
	September 30, 2010	2009	September 30, 2010	2009
Effective income tax rate	29.5%	28.0%	30.8%	30.1%

The increases in our effective income tax rate for the three and nine months ended September 30, 2010 compared to the same periods of the prior year were due primarily to the expiration of federal research and development tax incentives that were available during the three and nine months ended September 30, 2009, partly offset by tax benefits related to U.S. manufacturing activities that were fully phased in effective January 1, 2010. During the three months ended September 30, 2010 and 2009, we recognized tax benefits of similar amounts resulting from the expiration of certain statutes of limitation. The recognition of these benefits did not impact the comparability of our effective income tax rate between the three months ended September 30, 2010 and 2009, but did result in the reduction of our effective income tax rates for the three months ended September 30, 2010 and 2009 as compared to the nine months ended September 30, 2010 and 2009, respectively.

NOTE 10. COMPREHENSIVE INCOME

The following is a summary of comprehensive income for the three and nine months ended September 30, 2010 and 2009 (in thousands):

	For the Three Months Ended		For the Nine Months Ended	
	September 30, 2010	2009	September 30, 2010	2009
Net income	\$ 34,715	\$ 31,536	\$ 104,940	\$ 91,274
Less: Net income attributable to noncontrolling interest	21	-	27	-
Net income attributable to IDEXX Laboratories, Inc. stockholders	34,694	31,536	104,913	91,274
Other comprehensive income (loss) attributable to IDEXX Laboratories, Inc. stockholders:				
Foreign currency translation adjustments	14,113	7,053	1,226	14,024
Change in fair value of foreign currency contracts classified as hedges, net of tax	(5,655)	(2,975)	640	(11,433)
Change in fair value of interest rate swaps classified as hedges, net of tax	(83)	(537)	(856)	(201)
Change in fair market value of investments, net of tax	130	133	78	375
Comprehensive income attributable to IDEXX Laboratories, Inc. stockholders	\$ 43,199	\$ 35,210	\$ 106,001	\$ 94,039

NOTE 11. EARNINGS PER SHARE

Basic earnings per share is computed by dividing net income by the weighted average number of shares of common stock and vested deferred stock units outstanding during the period. The computation of diluted earnings per share is similar to the computation of basic earnings per share, except that the denominator is increased for the assumed exercise of dilutive options and other potentially dilutive securities using the treasury stock method, unless the effect is anti-dilutive.

The following is a reconciliation of shares outstanding for basic and diluted earnings per share for the three and nine months ended September 30, 2010 and 2009 (in thousands):

	For the Three Months Ended September 30,		For the Nine Months Ended September 30,	
	2010	2009	2010	2009
Shares Outstanding for Basic Earnings per Share:				
Weighted average shares outstanding	57,500	58,540	57,676	58,799
Weighted average vested deferred stock units outstanding	120	116	123	112
	57,620	58,656	57,799	58,911
Shares Outstanding for Diluted Earnings per Share:				
Shares outstanding for basic earnings per share	57,620	58,656	57,799	58,911
Dilutive effect of options issued	1,506	1,876	1,702	1,685
Dilutive effect of restricted stock units issued	148	128	188	115
Dilutive effect of unvested deferred stock units issued	2	8	2	7
	59,276	60,668	59,691	60,718

Vested deferred stock units outstanding are included in shares outstanding for basic and diluted earnings per share because the associated shares of our common stock are issuable for no cash consideration, the number of shares of our common stock to be issued is fixed and issuance is not contingent.

Certain options to acquire shares and restricted stock units have been excluded from the calculation of shares outstanding for diluted earnings per share because they were anti-dilutive. The following table presents information concerning those anti-dilutive options and restricted stock units for the three and nine months ended September 30, 2010 and 2009 (in thousands, except per share amounts):

	For the Three Months Ended September 30,		For the Nine Months Ended September 30,	
	2010	2009	2010	2009
Weighted average number of shares underlying anti-dilutive options	598	647	654	1,362
Weighted average exercise price per underlying share of anti-dilutive options	\$ 54.67	\$ 52.91	\$ 55.03	\$ 44.76
	-	-	-	3

Weighted average number of shares underlying
anti-dilutive restricted stock units

The following table presents additional information concerning the exercise prices of vested and unvested options outstanding at the end of the period (in thousands, except per share amounts):

	September 30,	
	2010	2009
Closing price per share of our common stock	\$ 61.72	\$ 50.00
Number of shares underlying options with exercise prices below the closing price	4,083	4,390
Number of shares underlying options with exercise prices equal to or above the closing price	4	568
Total number of shares underlying outstanding options	4,087	4,958

NOTE 12. COMMITMENTS, CONTINGENCIES AND GUARANTEES

Significant commitments, contingencies and guarantees at September 30, 2010 are consistent with those discussed in Note 12 to the consolidated financial statements in our Annual Report on Form 10-K for the year ended December 31, 2009.

NOTE 13. SEGMENT REPORTING

During the second quarter of 2010, we changed the name of our Production Animal Segment to Livestock and Poultry Diagnostics (“LPD”). The reason for this change was to provide a name that more accurately reflects the products and services and customer groups to which this segment caters. There is no change in the products and services offered or in the results of operations for this segment.

The accounting policies of the segments are consistent with those discussed in Notes 1 and 13 to the consolidated financial statements in our Annual Report on Form 10-K for the year ended December 31, 2009. Intersegment revenues, which are not included in the table below, were not significant for the three and nine months ended September 30, 2010 and 2009.

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The following is a summary of segment performance for the three and nine months ended September 30, 2010 and 2009 (in thousands):

	For the Three Months Ended September 30,					Unallocated Amounts	Consolidated Total
	CAG	Water	LPD	Other			
2010							
Revenue	\$ 222,909	\$ 20,044	\$ 17,476	\$ 9,199	\$ -	\$ 269,628	
Income (loss) from operations	\$ 38,831	\$ 8,698	\$ 3,042	\$ 1,376	\$ (2,133)	\$ 49,814	
Interest expense, net						551	
Income before provision for income taxes						49,263	
Provision for income taxes						14,548	
Net income						34,715	
Net income attributable to noncontrolling interest						21	
Net income attributable to IDEXX Laboratories, Inc. stockholders						\$ 34,694	
2009							
Revenue	\$ 214,461	\$ 19,691	\$ 15,943	\$ 9,025	\$ -	\$ 259,120	
Income (loss) from operations	\$ 38,002	\$ 8,416	\$ 944	\$ (244)	\$ (2,913)	\$ 44,205	
Interest expense, net						388	
Income before provision for income taxes						43,817	
Provision for income taxes						12,281	
Net income						31,536	
Net income attributable to noncontrolling interest						-	
Net income attributable to IDEXX Laboratories, Inc. stockholders						\$ 31,536	

	For the Nine Months Ended September 30,					Unallocated Amounts	Consolidated Total
	CAG	Water	LPD	Other			
2010							
Revenue	\$ 676,646	\$ 57,356	\$ 56,577	\$ 29,056	\$ -	\$ 819,635	
Income (loss) from operations	\$ 123,477	\$ 23,738	\$ 11,964	\$ 1,838	\$ (7,940)	\$ 153,077	
Interest expense, net						1,414	
Income before provision for income taxes						151,663	

Provision for income taxes							46,723
Net income							104,940
Net income attributable to noncontrolling interest							27
Net income attributable to IDEXX Laboratories, Inc. stockholders							\$ 104,913
2009							
Revenue	\$ 625,442	\$ 54,707	\$ 53,848	\$ 27,301	\$ -		\$ 761,298
Income (loss) from operations	\$ 106,993	\$ 24,336	\$ 11,002	\$ (145)	\$ (10,364)		\$ 131,822
Interest expense, net							1,187
Income before provision for income taxes							130,635
Provision for income taxes							39,361
Net income							91,274
Net income attributable to noncontrolling interest							-
Net income attributable to IDEXX Laboratories, Inc. stockholders							\$ 91,274

The following is a summary of revenue by product and service category for the three and nine months ended September 30, 2010 and 2009 (in thousands):

	For the Three Months Ended September 30,		For the Nine Months Ended September 30,	
	2010	2009	2010	2009
CAG segment revenue:				
Instruments and consumables	\$ 88,481	\$ 83,922	\$ 258,318	\$ 239,889
Rapid assay products	35,576	37,753	115,500	116,997
Laboratory diagnostic and consulting services	82,534	76,419	248,422	222,987
Practice information systems and digital radiography	16,318	16,367	54,406	45,515
Pharmaceutical products	-	-	-	54
CAG segment revenue	222,909	214,461	676,646	625,442
Water segment revenue	20,044	19,691	57,356	54,707
LPD segment revenue	17,476	15,943	56,577	53,848
Other segment revenue	9,199	9,025	29,056	27,301
Total revenue	\$ 269,628	\$ 259,120	\$ 819,635	\$ 761,298

NOTE 14. FAIR VALUE MEASUREMENTS

U.S. GAAP defines fair value as the exchange price that would be received for an asset or paid to transfer a liability (an exit price) in the principal or most advantageous market for the asset or liability in an orderly transaction between market participants on the measurement date. U.S. GAAP also establishes a fair value hierarchy which requires an entity to maximize the use of observable inputs, where available, and minimize the use of unobservable inputs when measuring fair value.

There are three levels of inputs that may be used to measure fair value:

- Level 1 Quoted prices in active markets for identical assets or liabilities.
- Level 2 Observable inputs other than Level 1 prices, such as quoted prices for similar assets or liabilities; quoted prices in markets that are not active; or other inputs that are observable or can be corroborated by observable market data for substantially the full term of the assets or liabilities. Foreign currency exchange contracts classified as derivative instruments are valued based on the present value of the forward rate less the contract rate multiplied by the notional amount. The product of this calculation is then adjusted for counterparty risk. Interest rate swaps classified as derivative instruments are valued utilizing a discounted cash flow analysis based on the terms of the contract and the interest rate curve, and adjusted for counterparty risk.
- Level 3 Unobservable inputs that are supported by little or no market activity and that are significant to the fair value of the assets or liabilities. At September 30, 2010 and December 31, 2009, we had no Level 3 assets or liabilities.

Assets and liabilities measured at fair value are classified in their entirety based on the lowest level of input that is significant to the fair value measurement. Our assessment of the significance of a particular input to the fair value measurement in its entirety requires judgment and considers factors specific to the asset or liability. We did not have any significant nonfinancial assets or nonfinancial liabilities which required remeasurement during the nine months

ended September 30, 2010 or during the year ended December 31, 2009. We did not have any transfers between Level 1 and Level 2 measurements during the nine months ended September 30, 2010.

The following tables set forth our assets and liabilities that were measured at fair value on a recurring basis at September 30, 2010 and at December 31, 2009 by level within the fair value hierarchy (in thousands):

As of September 30, 2010	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Balance at September 30, 2010
Assets				
Money market funds(1)	\$ 32,020	\$ -	\$ -	\$ 32,020
Equity mutual funds(2)	2,030	-	-	2,030
Liabilities				
Foreign currency exchange contracts(3)	-	3,301	-	3,301
Deferred compensation(4)	2,030	-	-	2,030
Interest rate swaps(5)	-	1,959	-	1,959

As of December 31, 2009	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Balance at December 31, 2009
Assets				
Money market funds(1)	\$ 47,021	\$ -	\$ -	\$ 47,021
Equity mutual funds(2)	1,891	-	-	1,891
Liabilities				
Foreign currency exchange contracts(3)	-	4,221	-	4,221
Deferred compensation(4)	1,891	-	-	1,891
Interest rate swaps(5)	-	595	-	595

- (1) Money market funds are included within cash and cash equivalents.
- (2) Equity mutual funds relate to a deferred compensation plan that was assumed as part of a previous business combination. This amount is included within other long-term assets. See footnote 4 below for a discussion of the related deferred compensation liability.
- (3) Foreign currency exchange contracts are included within accrued liabilities and other long-term liabilities as of September 30, 2010 and within accrued liabilities as of December 31, 2009.
- (4) Deferred compensation plans are included within other long-term liabilities. The fair value of our deferred compensation plan is indexed to the performance of the underlying equity mutual funds discussed in footnote 2 above.
- (5) Interest rate swaps are included within accrued liabilities.

The estimated fair value of certain financial instruments, including cash and cash equivalents, accounts receivable, accounts payable, and the current portion of notes payable approximate carrying value due to their short maturity.

Based on current market conditions, we believe that we could obtain an unsecured short-term revolving credit facility similar to our current unsecured short-term revolving credit facility ("Credit Facility"). Applicable interest rates on borrowings under the Credit Facility generally range from 0.375 to 0.875 percentage points ("Credit Spread") above the

London interbank rate or the Canadian Dollar-denominated bankers' acceptance rate, dependent on our leverage ratio. We believe that the Credit Spread on a new facility would most likely be approximately 1.25 percentage points higher than the Credit Spread on our current Credit Facility. Despite a presumed increase in the Credit Spread, the estimated fair value of the outstanding borrowings against the Credit Facility would approximate carrying value due to the short maturity of the individual borrowings. The estimated fair value of long-term debt approximates the carrying value based on current market prices for similar debt issues with similar remaining maturities.

Financial instruments that potentially subject us to concentrations of credit risk are principally cash and cash equivalents, investments and accounts receivable. To mitigate such risk, we place our cash and cash equivalents and investments in highly-rated financial institutions and money market funds invested in government securities. Concentration of credit risk with respect to accounts receivable is limited to certain customers to whom we make substantial sales. To reduce risk, we routinely monitor the amounts owed to us by our customers and take appropriate action when necessary and, as a result, we believe that accounts receivable credit risk exposure is limited. We maintain an allowance for doubtful accounts, but historically have not experienced any significant losses related to an individual customer or group of customers in any particular industry or geographic area.

NOTE 15. DERIVATIVE INSTRUMENTS AND HEDGING

Disclosure within this footnote is presented to provide transparency about how and why we use derivative instruments, how the instruments and related hedged items are accounted for, and how the instruments and related hedged items affect our financial position, results of operations, and cash flows. Derivative instruments are recognized on the balance sheet as either assets or liabilities at fair value with a corresponding offset to other comprehensive income ("OCI"), which is net of tax.

We are exposed to certain risks related to our ongoing business operations. The primary risks that we manage by using derivative instruments are foreign currency exchange risk and interest rate risk. Our subsidiaries enter into foreign currency exchange contracts to manage the exchange risk associated with their forecasted intercompany inventory purchases and sales for the next year. From time to time, we may also enter into foreign currency exchange contracts to minimize the impact of foreign currency fluctuations associated with specific, significant transactions. Interest rate swaps are entered into to manage interest rate risk associated with \$80 million of our variable-rate debt.

The primary purpose of our foreign currency hedging activities is to protect against the volatility associated with foreign currency transactions. We also utilize natural hedges to mitigate our transaction and commitment exposures. Our corporate policy prescribes the range of allowable hedging activity. We enter into exchange contracts with large multinational financial institutions and we do not hold or engage in transactions involving derivative instruments for purposes other than risk management. Our accounting policies for these contracts are based on our designation of such instruments as hedging transactions. Market gains and losses are deferred in OCI until the contract matures, which is the period when the related obligation is settled. We primarily utilize forward exchange contracts with durations of less than 24 months.

Cash Flow Hedges

We have designated our forward currency exchange contracts and variable-to-fixed interest rate swaps as cash flow hedges. For derivative instruments that are designated as hedges, changes in the fair value of the derivative are recognized in OCI and reclassified into earnings in the same period or periods during which the hedged transaction affects earnings. We de-designate derivative instruments from hedge accounting when the probability of the hedged transaction occurring becomes less than probable, but remains reasonably possible. For de-designated instruments, the gain or loss from the time of de-designation through maturity of the instrument is recognized in earnings. Any gain or loss in OCI at the time of de-designation is reclassified into earnings in the same period or periods during which the hedged transaction affects earnings. We did not de-designate any instruments from hedge accounting treatment during the three and nine months ended September 30, 2010. The loss recognized in earnings related to de-designated instruments during the three and nine months ended September 30, 2009 was less than \$0.1 million. We immediately record in earnings the extent to which a hedge is not effective in achieving offsetting changes in fair value of the hedged item. Gains or losses related to hedge ineffectiveness recognized in earnings during the three and nine months ended September 30, 2010 and 2009 were not material. At September 30, 2010, the estimated net amount of losses that are expected to be reclassified out of accumulated OCI and into earnings within the next 12 months is \$2.3 million if exchange and interest rates do not fluctuate from the levels at September 30, 2010.

We enter into currency exchange contracts for amounts that are less than the full value of forecasted intercompany sales. Our hedging strategy related to intercompany inventory purchases is to employ the full amount of our hedges for the succeeding year at the conclusion of our budgeting process for that year, which is complete by the end of the preceding year. Quarterly, we enter into contracts to hedge incremental portions of anticipated foreign currency transactions for the current and following year. Accordingly, our risk with respect to foreign currency exchange rate fluctuations may vary throughout each annual cycle.

In March 2009, we entered into two forward fixed interest rate swap agreements to manage the economic effect of variable interest obligations on amounts borrowed under the terms of our Credit Facility. Under these agreements, beginning on March 31, 2010 the variable interest rate associated with \$80 million of borrowings outstanding under the Credit Facility became effectively fixed at 2% plus the Credit Spread through March 30, 2012. The critical terms of the interest rate swap agreements match the critical terms of the underlying borrowings, including notional amounts, underlying market indices, interest rate reset dates and maturity dates.

The notional amount of foreign currency exchange contracts to hedge forecasted intercompany sales consisted of the following (in thousands):

Currency Sold	U.S. Dollar Equivalent		
	September 30, 2010	December 31, 2009	September 30, 2009
Euro	\$ 56,506	\$ 53,091	\$ 42,849
British Pound	21,782	19,238	22,853
Canadian Dollar	19,166	18,849	22,907
Australian Dollar	8,428	7,086	6,384
Japanese Yen	10,409	9,795	8,168
	\$ 116,291	\$ 108,059	\$ 103,161

Currency Purchased	U.S. Dollar Equivalent		
	September 30, 2010	December 31, 2009	September 30, 2009
Swiss Franc	\$ 9,990	\$ 8,808	\$ 7,603

The notional amount of forward fixed interest rate swap agreements to manage variable interest obligations consisted of the following (in thousands):

	U.S. Dollar Equivalent		
	September 30, 2010	December 31, 2009	September 30, 2009
Interest rate swap	\$ 80,000	\$ 80,000	\$ 80,000

The fair values of derivative instruments and their respective classification in the condensed consolidated balance sheet consisted of the following (in thousands):

	Liability Derivatives			
	September 30, 2010		December 31, 2009	
	Balance Sheet Classification	Fair Value	Balance Sheet Classification	Fair Value
Derivatives designated as hedging instruments				
Foreign currency exchange contracts	Accrued expenses	\$ 2,636	Accrued expenses	\$ 4,221
Foreign currency exchange contracts	Other long-term liabilities	665	Other long-term liabilities	-
Interest rate swaps	Accrued expenses	1,959	Accrued expenses	595
Total derivative instruments		\$ 5,260		\$ 4,816

The effect of derivative instruments designated as cash flow hedges on the condensed consolidated balance sheet for the three and nine months ended September 30, 2010 and 2009 consisted of the following (in thousands):

Derivative instruments	Gain (Loss) Recognized in OCI on Derivative Instruments (Effective Portion)			
	For the Three Months Ended September 30,		For the Nine Months Ended September 30,	
	2010	2009	2010	2009
Foreign exchange contracts, net of tax	\$ (5,655)	\$ (2,975)	\$ 640	\$ (11,433)
Interest rate swaps, net of tax	(83)	(537)	(856)	(201)
Total loss, net of tax	\$ (5,738)	\$ (3,512)	\$ (216)	\$ (11,634)

The effect of derivative instruments designated as cash flow hedges on the condensed consolidated statement of operations for the three and nine months ended September 30, 2010 and 2009 consisted of the following (in thousands):

Derivative instruments	Classification of Gain (Loss) Reclassified from OCI into Income (Effective Portion)	Gain (Loss) Reclassified from Accumulated OCI into Income (Effective Portion)			
		For the Three Months Ended September 30,		For the Nine Months Ended September 30,	
		2010	2009	2010	2009
Foreign exchange contracts	Cost of revenue	\$ (199)	\$ 4	\$ 236	\$ 6,956

The effect of derivative instruments that have been de-designated from cash flow hedge treatment on the condensed consolidated statement of operations for the three and nine months ended September 30, 2010 and 2009 consisted of the following (in thousands):

De-designated derivative instruments	Classification of Gain (Loss) Reclassified from OCI into Income	Gain (Loss) Recognized in Income Related to De-designated Cash Flow Hedges			
		For the Three Months Ended September 30,		For the Nine Months Ended September 30,	
		2010	2009	2010	2009
Foreign exchange contracts	General and administrative expense	\$ -	\$ (31)	\$ -	\$ (73)

NOTE 16. MILESTONE PAYMENTS

In the fourth quarter of 2008, we sold our Acaress® and SURPASS® veterinary pharmaceutical products and a product under development, which were a part of our CAG segment, for cash of \$7.0 million, a short-term receivable of \$1.4 million, which was received in January 2009, and up to \$11.5 million of future payments based on the achievement of certain development and sales milestones by the acquirer of those products. In the fourth quarter of 2009, we received a milestone payment of \$2.0 million in connection with the achievement of certain development milestones by the acquirer. The acquirer has since commercialized the development product and in connection with the achievement of certain sales milestones by the acquirer in the third quarter of 2010 we recorded the earning of a milestone payment of \$1.0 million, which is reflected as a reduction to general and administrative expenses. We are now eligible to receive up to \$8.5 million in additional milestone payments based on further sales related to the product. Future sales-based milestone payments will be included in our results of operations upon achievement of the

applicable milestone.

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Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations.

This Quarterly Report on Form 10-Q contains statements which, to the extent they are not statements of historical fact, constitute "forward-looking statements." Such forward-looking statements about our business and expectations within the meaning of the Private Securities Litigation Reform Act of 1995, Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities Exchange Act of 1934, as amended, include statements relating to future revenue growth rates, earnings and other measures of financial performance, the effect of economic downturns on our business performance, demand for our products, realizability of assets, future cash flow and uses of cash, future repurchases of common stock, future levels of indebtedness and capital spending, interest expense, warranty expense, share-based compensation expense, and competition. Forward-looking statements can be identified by the use of words such as "expects," "may," "anticipates," "intends," "would," "will," "plans," "believes," "estimates," "should," and similar expressions. These forward-looking statements are intended to provide our current expectations or forecasts of future events; are based on current estimates, projections, beliefs, and assumptions; and are not guarantees of future performance. Actual events or results may differ materially from those described in the forward-looking statements. These forward-looking statements involve a number of risks and uncertainties as more fully described under the heading "Part II, Item 1A. Risk Factors" in this Quarterly Report on Form 10-Q. The risks and uncertainties discussed herein do not reflect the potential impact of any mergers, acquisitions or dispositions. In addition, any forward-looking statements represent our estimates only as of the day this Quarterly Report was first filed with the Securities and Exchange Commission ("SEC") and should not be relied upon as representing our estimates as of any subsequent date. From time to time, oral or written forward-looking statements may also be included in other materials released to the public. While we may elect to update forward-looking statements at some point in the future, we specifically disclaim any obligation to do so, even if our estimates or expectations change.

Business Overview and Trends

Operating segments. We operate primarily through three business segments: diagnostic and information technology products and services for the veterinary market, which we refer to as our Companion Animal Group ("CAG"), water quality products ("Water") and products for livestock and poultry health, which we refer to as Livestock and Poultry Diagnostics ("LPD"). Until the second quarter of 2010, LPD was referred to as our Production Animal Segment. We also operate two smaller operating segments that comprise products for dairy quality ("Dairy") and products for the human point-of-care medical diagnostics market ("OPTI Medical"). Financial information about the Dairy and OPTI Medical operating segments and other licensing arrangements are combined and presented in an "Other" category because they do not meet the quantitative or qualitative thresholds for reportable segments. See Note 13 to the condensed consolidated financial statements included in this Quarterly Report on Form 10-Q for financial information about our segments and the section entitled "Description of Business by Segment" under the heading "Item 1. Business" in our Annual Report on Form 10-K for the year ended December 31, 2009 for additional description of our segments.

CAG develops, designs, manufactures and distributes products and performs services for veterinarians, primarily related to diagnostics and information management. Water develops, designs, manufactures and distributes products to detect contaminants in water. LPD develops, designs, manufactures and distributes products to detect disease in livestock and poultry. Dairy develops, designs, manufactures and distributes products to detect contaminants in dairy products. OPTI Medical develops, designs, manufactures and distributes point-of-care electrolyte and blood gas analyzers and related consumable products for the human medical diagnostics market and also manufactures our VetStat® electrolyte and blood gas analyzer and electrolyte consumables used with our Catalyst Dx® analyzer, both of which are sold in the veterinary market.

Items that are not allocated to our operating segments are comprised primarily of corporate research and development expenses that do not align with one of our existing business or service categories, a portion of share-based compensation expense, interest income and expense, and income taxes. We estimate our share-based compensation

expense for the year and allocate the estimated expense to the operating segments. This allocation differs from the actual expense and consequently yields a difference between the total allocated share-based compensation expense and the actual expense for the total company, resulting in an unallocated amount reported under the caption “Unallocated Amounts.” We maintain active research and development programs, some of which may materialize into the development and introduction of new technology, products or services. Research and development costs incurred that are not specifically attributable to one of our existing business or service categories are reported under the caption “Unallocated Amounts.”

Use of Distributors. The instrument consumables and rapid assay products in our CAG segment are sold in the U.S. and certain other geographies by distributors. As a result, distributor purchasing dynamics have an impact on our reported sales of these products. Distributors purchase products from us and sell them to veterinary practices, who are the end users. Distributor purchasing dynamics may be affected by many factors and may be unrelated to underlying end-user demand for our products. As a result, fluctuations in distributors' inventories may cause reported results in a period not to be representative of underlying end-user demand. Therefore, we believe it is important to track distributor sales to end users and to distinguish between the impact of end-user demand and the impact of distributor purchasing dynamics on reported revenue.

Where growth rates are affected by changes in end-user demand, we refer to the impact of practice-level sales on growth. Where growth rates are affected by distributor purchasing dynamics, we refer to the impact of changes in distributors' inventories. If during the current year, distributors' inventories grew by less than those inventories grew in the comparable period of the prior year, then changes in distributors' inventories have a negative impact on our reported sales growth in the current period. Conversely, if during the current year, distributors' inventories grew by more than those inventories grew in the comparable period of the prior year, then changes in distributors' inventories have a positive impact on our reported sales growth in the current period.

At the end of a quarter, we believe that our U.S. CAG distributors typically hold inventory equivalent to approximately three to four weeks of our anticipated end-user demand for instrument consumables and rapid assay products.

Currency Impact. For the three and nine months ended September 30, 2010, approximately 24% and 25% of our revenue, respectively, was derived from products manufactured in the U.S. and sold internationally in local currencies. Strengthening of the rate of exchange for the U.S. dollar relative to other currencies has a negative impact on our revenues derived in currencies other than the U.S. dollar and on profits of products manufactured in the U.S. and sold internationally, with a weakening of the U.S. dollar having the opposite effect. In addition, to the extent that the U.S. dollar is stronger in current or future periods relative to the exchange rates in effect in the corresponding prior periods, our growth rate will be negatively affected. The impact of foreign currency denominated operating expenses and foreign currency denominated supply contracts partly offset this exposure.

During the three months ended September 30, 2010, as compared to the three months ended September 30, 2009, changes in foreign currency exchange rates reduced total company revenue by approximately \$3.2 million, due primarily to the strengthening of the U.S. dollar against the Euro and, to a lesser extent, the British pound. The impact on revenue resulting from changes in foreign currency exchange rates is a non-U.S. GAAP measure. It represents the change resulting from the difference between the average exchange rates during the current period and the same period of the prior year applied to foreign currency denominated revenues for the current period. These unfavorable impacts were partly offset by the weakening of the U.S. dollar against the Australian dollar, Canadian dollar and Japanese yen. These changes in foreign currency exchange rates impacted the revenues generated by each of our individual operating segments in a manner similar to the impact on the company as a whole.

During the nine months ended September 30, 2010, as compared to the nine months ended September 30, 2009, changes in foreign currency exchange rates increased total company revenue by approximately \$5.7 million, due primarily to the weakening of the U.S. dollar against the Canadian dollar, Australian dollar and Japanese yen. These favorable impacts were partly offset by the strengthening of the U.S. dollar against the Euro. Although the changes in foreign currency exchange rates had a net favorable impact on total company revenues for the nine months ended September 30, 2010, our LPD segment was negatively impacted since the U.S. dollar strengthened against the Euro and, compared to our other segments, a larger portion of LPD sales are generated in countries where the Euro is the local currency.

Effect of Economic Conditions. Demand for many of our products and services has been negatively affected by economic conditions that have existed over the past two years. In our CAG segment, we believe that negative consumer sentiment resulting from economic conditions has led to essentially flat patient visits to veterinary clinics, which we continued to observe for the three and nine months ended September 30, 2010 relative to the same periods in 2009. We also believe that essentially flat patient visits have negatively affected the growth rate of sales of rapid assay tests, instrument consumables, and laboratory diagnostic and consulting services. In addition, we believe that the rate of growth of sales of our instruments and digital radiography systems, which are larger capital purchases for veterinarians, has been negatively affected by continued caution among veterinarians regarding economic conditions. Weaker economic conditions have also caused our customers to remain sensitive to the pricing of our products and services resulting in lower growth due to limited price increases for certain products.

We also believe that current economic conditions have affected purchasing decisions by certain customer groups in our Water and LPD businesses. Lower water testing volumes in the regulated and non-regulated segments of our Water business have resulted from a decline in municipal studies and new home construction, respectively. Lower LPD testing volumes have resulted from a reduction in non-regulated producer and laboratory testing, as a measure to reduce operating costs, and by a reduction in testing associated with some government mandated eradication programs as a result of lower government funding.

We believe that the diversity of our products and services and the geographic diversity of our markets will partially mitigate the effects of the continuing slow economic growth and negative consumer sentiment. However, until we see improvements in broad factors that measure the economic climate both in the United States and Europe, we expect our growth rates will continue to be negatively affected.

Critical Accounting Policies and Estimates

The discussion and analysis of our financial condition and results of operations is based upon our condensed consolidated financial statements, which have been prepared in accordance with accounting principles generally accepted in the U.S. The preparation of these financial statements requires us to make estimates and judgments that affect the reported amounts of assets, liabilities, revenues and expenses, and related disclosure of contingent assets and liabilities. On an ongoing basis, we evaluate our estimates. We base our estimates on historical experience and on various assumptions that we believe to be reasonable under the circumstances, the results of which form the basis for making judgments about the carrying values of assets and liabilities that are not readily apparent from other sources. Actual results may differ from these estimates. The significant accounting policies used in preparation of these condensed consolidated financial statements for the three and nine months ended September 30, 2010 are consistent with those discussed in Note 3 to the consolidated financial statements included in our Annual Report on Form 10-K for the year ended December 31, 2009, except as discussed in Note 2 to the condensed consolidated financial statements included in this Quarterly Report on Form 10-Q. The critical accounting policies and the significant judgments and estimates used in the preparation of our condensed consolidated financial statements for the three and nine months ended September 30, 2010 are consistent with those discussed in our Annual Report on Form 10-K for the year ended December 31, 2009 in the section under the heading “Part 2, Item 7. Management’s Discussion and Analysis of Financial Condition and Results of Operations—Critical Accounting Policies and Estimates.”

Results of Operations

Three Months Ended September 30, 2010 Compared to Three Months Ended September 30, 2009

Revenue

Total Company. The following table presents revenue by operating segment:

For the Three Months Ended September 30,

Net Revenue (dollars in thousands)	2010	2009	Dollar Change	Percentage Change	Percentage Change from Currency (1)	Percentage Change from Acquisitions/ Divestitures (2)	Percentage Change Net of
							Acquisitions/ Divestitures and Currency Effect (3)
CAG	\$ 222,909	\$ 214,461	\$ 8,448	3.9%	(0.9)%	0.4%	4.4%
Water	20,044	19,691	353	1.8%	(1.0)%	-	2.8%
LPD	17,476	15,943	1,533	9.6%	(5.8)%	-	15.4%
Other	9,199	9,025	174	1.9%	(0.7)%	-	2.6%
Total	\$ 269,628	\$ 259,120	\$ 10,508	4.1%	(1.2)%	0.4%	4.9%

(1) The percentage change from currency is a non-U.S. GAAP measure. It represents the percentage change in revenue resulting from the difference between the average exchange rates during the three months ended September 30, 2010 and the same period of the prior year applied to foreign currency denominated revenues for the three months ended September 30, 2010.

(2) Represents the percentage change in revenue during the three months ended September 30, 2010 compared to the three months ended September 30, 2009 attributed to incremental revenues from businesses acquired or revenues lost from businesses divested or discontinued subsequent to June 30, 2009.

(3) We refer to this change as the change in organic revenue.

The following revenue analysis and discussion focuses on organic revenue, which reflects the results of operations net of the impact of changes in foreign currency exchange rates on sales outside the U.S. and net of incremental revenues from businesses acquired or revenues lost from businesses divested or discontinued subsequent to June 30, 2009.

Companion Animal Group. The following table presents revenue by product and service category for CAG:

For the Three Months Ended September 30,

Net Revenue (dollars in thousands)	2010	2009	Dollar Change	Percentage Change	Percentage Change from Currency (1)	Percentage Change from Acquisitions/ Divestitures (2)	Percentage Change
							Percentage Change from Acquisitions/ Divestitures and Currency

Effect
(3)

Instruments and consumables	\$ 88,481	\$ 83,922	\$ 4,559	5.4%	(1.2)%	-	6.6%
Rapid assay products							