

PALL CORP
Form 10-Q
June 11, 2012

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

FORM 10-Q

R Quarterly report pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934
For the quarterly period ended April 30, 2012

or

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

Commission File Number: 001- 04311

PALL CORPORATION

(Exact name of registrant as specified in its charter)

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

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

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

11050
(Zip Code)

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

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

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§ 232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes No

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

Large accelerated filer Accelerated filer

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

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

The number of shares of the registrant's common stock outstanding as of June 1, 2012 was 116,202,448.

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PART I. FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS.

PALL CORPORATION AND SUBSIDIARIES
CONDENSED CONSOLIDATED BALANCE SHEETS

(In thousands, except per share data)

(Unaudited)

	Apr 30, 2012	July 31, 2011
ASSETS		
Current assets:		
Cash and cash equivalents	\$535,891	\$557,766
Accounts receivable	614,900	646,769
Inventories	402,292	444,842
Prepaid expenses	48,201	39,322
Other current assets	159,371	120,509
Assets held for sale	126,737	—
Total current assets	1,887,392	1,809,208
Property, plant and equipment	772,293	794,599
Goodwill	341,731	290,606
Intangible assets	158,310	61,735
Other non-current assets	235,128	276,268
Total assets	\$3,394,854	\$3,232,416
LIABILITIES AND STOCKHOLDERS' EQUITY		
Current liabilities:		
Notes payable	\$199,953	\$214,957
Accounts payable	171,666	225,398
Accrued liabilities	364,222	294,485
Income taxes payable	63,280	34,531
Current portion of long-term debt	482	511
Dividends payable	24,402	20,125
Total current liabilities	824,005	790,007
Long-term debt, net of current portion	487,936	491,954
Income taxes payable – non-current	149,555	175,040
Deferred taxes and other non-current liabilities	269,564	285,594
Total liabilities	1,731,060	1,742,595
Stockholders' equity:		
Common stock, par value \$.10 per share	12,796	12,796
Capital in excess of par value	272,020	246,665
Retained earnings	1,780,468	1,619,051
Treasury stock, at cost	(442,149	) (483,705
Stock option loans	(54	) (133
Accumulated other comprehensive income/(loss):		
Foreign currency translation	150,492	207,478
Pension liability adjustment	(113,141) (121,831
Unrealized investment gains	3,362	9,500

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Total stockholders' equity	40,713	95,147
Total liabilities and stockholders' equity	1,663,794	1,489,821
	\$3,394,854	\$3,232,416

See accompanying notes to condensed consolidated financial statements.

PALL CORPORATION AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF EARNINGS

(In thousands, except per share data)

(Unaudited)

	Three Months Ended		Nine Months Ended	
	Apr 30, 2012	Apr 30, 2011	Apr 30, 2012	Apr 30, 2011
Net sales	\$657,976	\$653,792	\$1,949,285	\$1,798,479
Cost of sales	323,550	321,526	941,342	867,087
Gross profit	334,426	332,266	1,007,943	931,392
Selling, general and administrative expenses	215,226	203,327	632,982	572,026
Research and development	20,780	19,308	60,351	57,198
Restructuring and other charges, net	2,861	7,723	31,001	13,921
Interest expense, net	6,351	6,068	17,682	19,176
Earnings from continuing operations before income taxes	89,208	95,840	265,927	269,071
Provision for income taxes	18,270	34,082	60,691	80,021
Net earnings from continuing operations	\$70,938	\$61,758	\$205,236	\$189,050
Earnings from discontinued operations, net of income taxes	\$7,980	\$9,311	\$27,866	\$29,092
Net earnings	\$78,918	\$71,069	\$233,102	\$218,142
Earnings per share from continuing operations:				
Basic	\$0.61	\$0.53	\$1.77	\$1.62
Diluted	\$0.60	\$0.52	\$1.74	\$1.60
Earnings per share from discontinued operations:				
Basic	\$0.07	\$0.08	\$0.24	\$0.25
Diluted	\$0.07	\$0.08	\$0.24	\$0.25
Earnings per share:				
Basic	\$0.68	\$0.61	\$2.01	\$1.87
Diluted	\$0.67	\$0.60	\$1.98	\$1.84
Dividends declared per share	\$0.210	\$0.175	\$0.595	\$0.510
Average shares outstanding:				
Basic	116,567	116,899	116,190	116,565
Diluted	118,358	118,723	117,817	118,296

See accompanying notes to condensed consolidated financial statements.

PALL CORPORATION AND SUBSIDIARIES
 CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

(In thousands)

(Unaudited)

	Nine Months Ended	
	Apr 30, 2012	Apr 30, 2011
Operating activities:		
Net cash provided by operating activities	\$326,417	\$280,956
Investing activities:		
Capital expenditures	(126,923	) (103,142
Acquisition of businesses	(167,638) —
Purchases of retirement benefit assets	(33,805	) (62,439
Proceeds from retirement benefit assets	33,422	51,307
Proceeds from sale of assets	25,604	530
Other	(9,666	) (5,099
Net cash used by investing activities	(279,006	) (118,843
Financing activities:		
Notes payable	(15,004	) 109,682
Dividends paid	(64,554	) (57,287
Long-term borrowings	104	35,145
Repayments of long-term debt	(390	) (298,405
Net proceeds from stock plans	34,845	54,487
Purchase of treasury stock	—	(64,524
Excess tax benefits from stock-based compensation arrangements	4,177	10,799
Net cash used by financing activities	(40,822	) (210,103
Cash flow for period	6,589	(47,990
Cash and cash equivalents at beginning of year	557,766	498,563
Effect of exchange rate changes on cash and cash equivalents	(28,464	) 40,923
Cash and cash equivalents at end of period	\$535,891	\$491,496
Supplemental disclosures:		
Interest paid	\$13,274	\$13,589
Income taxes paid (net of refunds)	75,401	79,850

See accompanying notes to condensed consolidated financial statements.

PALL CORPORATION AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(In thousands, except per share data)

(Unaudited)

NOTE 1 – BASIS OF PRESENTATION

The condensed consolidated financial information of Pall Corporation and its subsidiaries (hereinafter collectively called the “Company”) included herein is unaudited. Such information reflects all adjustments of a normal recurring nature, which are, in the opinion of Company management, necessary to present fairly the Company’s consolidated financial position, results of operations and cash flows as of the dates and for the periods presented herein. These condensed consolidated financial statements should be read in conjunction with the consolidated financial statements and notes set forth in the Company’s Annual Report on Form 10-K for the fiscal year ended July 31, 2011 (“2011 Form 10-K”). Certain prior year amounts have been reclassified to conform to the current year presentation.

As discussed in Note 16, Discontinued Operations, the Company has entered into an agreement to sell certain assets of its blood collection, filtration and processing product line, which was a component of the Company’s Life Sciences segment, and met both the component and held for sale criteria during the third quarter of fiscal year 2012. As such, it has been reported as a discontinued operation in the Company’s condensed consolidated financial statements.

NOTE 2 – BALANCE SHEET DETAILS

The following tables provide details of selected balance sheet items:

	Apr 30, 2012	July 31, 2011
Accounts receivable:		
Billed	\$ 546,916	\$ 553,500
Unbilled	77,290	101,652
Total	624,206	655,152
Less: Allowances for doubtful accounts	(9,306	) (8,383)
	\$ 614,900	\$ 646,769

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

	Apr 30, 2012 (a)	July 31, 2011
Inventories:		
Raw materials and components	\$ 88,266	\$ 102,745
Work-in-process	100,503	96,601
Finished goods	213,523	245,496
	\$ 402,292	\$ 444,842
Property, plant and equipment:		
Property, plant and equipment	\$ 1,639,568	\$ 1,705,559
Less: Accumulated depreciation and amortization	(867,275	) (910,960)
	\$ 772,293	\$ 794,599

(a) The amounts for inventory and property, plant and equipment as of April 30, 2012 exclude those assets that are classified as held for sale, which are \$40,651 and \$61,623, respectively. See Note 16, Discontinued Operations, for further details.

PALL CORPORATION AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(In thousands, except per share data)

(Unaudited)

NOTE 3 – GOODWILL AND INTANGIBLE ASSETS

The following table presents goodwill, allocated by reportable segment.

	Apr 30, 2012 (a)	July 31, 2011
Life Sciences	\$179,490	\$131,852
Industrial	162,241	158,754
	\$341,731	\$290,606

(a) The amount for goodwill allocated to the Life Sciences reportable segment as of April 30, 2012 excludes goodwill that is classified as held for sale of \$22,018. See Note 16, Discontinued Operations, for further details.

Intangible assets, net, consist of the following:

	Apr 30, 2012 (b)		
	Gross	Accumulated Amortization	Net
Patents and unpatented technology	\$133,333	\$69,406	\$63,927
Customer-related intangibles	95,371	11,414	83,957
Trademarks	13,207	5,104	8,103
Other	5,063	2,740	2,323
	\$246,974	\$88,664	\$158,310
	July 31, 2011		
	Gross	Accumulated Amortization	Net
Patents and unpatented technology	\$102,372	\$64,921	\$37,451
Customer-related intangibles	26,478	6,598	19,880
Trademarks	6,802	4,684	2,118
Other	4,685	2,399	2,286
	\$140,337	\$78,602	\$61,735

(b) The amount for intangible assets as of April 30, 2012 excludes intangible assets, net, that is classified as held for sale of \$567. See Note 16, Discontinued Operations, for further details.

The changes in both goodwill and intangible assets relate to the preliminary valuation of the acquisition of ForteBio®, Inc. in the third quarter of fiscal year 2012, discussed in further detail in Note 17, Acquisition, as well as an acquisition in Brazil in the first quarter of fiscal year 2012. During the third quarter, the Company completed its valuation of its acquisition in Brazil. In connection with the acquisition in Brazil, the Company recorded the fair value of the intangible assets acquired (approximately \$22,250, with the majority recorded as customer-related intangibles), which were valued using the income approach. The amount of goodwill recorded in connection with this acquisition was approximately \$9,000. In addition, the carrying amounts were also impacted by changes in foreign exchange rates used to translate the goodwill and intangible assets contained in the financial statements of foreign subsidiaries using the rates at each respective balance sheet date.

Amortization expense for intangible assets for the three and nine months ended April 30, 2012 was \$5,956 and \$14,746, respectively. Amortization expense for intangible assets for the three and nine months ended April 30, 2011 was \$3,432 and \$9,941, respectively. Amortization expense is estimated to be approximately \$6,539 for the remainder of fiscal year 2012, \$21,098 in fiscal year 2013, \$18,758 in fiscal year 2014, \$17,162 in fiscal year 2015, \$15,950 in fiscal year 2016 and \$15,891 in fiscal year 2017.

NOTE 4 – TREASURY STOCK

On October 16, 2008, the board authorized an expenditure of \$350,000 to repurchase shares. On September 26, 2011, the board authorized an additional \$250,000. The Company's shares may be purchased over time, as market and business conditions warrant. There is no time restriction on these authorizations. There were no share repurchases during the nine months ended April 30, 2012. As of April 30, 2012, \$453,037 remains to be expended under the

current board repurchase authorizations. Repurchased shares are held in treasury for use in connection with the Company's stock plans and for general corporate purposes.

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PALL CORPORATION AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(In thousands, except per share data)

(Unaudited)

During the nine months ended April 30, 2012, 1,156 shares were issued under the Company's stock-based compensation plans. At April 30, 2012, the Company held 11,807 treasury shares.

NOTE 5 – CONTINGENCIES AND COMMITMENTS

With respect to the matters described in Note 14, Contingencies and Commitments, to the Company's consolidated financial statements included in the 2011 Form 10-K, under the heading Federal Securities Class Actions, Shareholder Derivative Lawsuits and Other Proceedings, the Company has reached an agreement with the lead plaintiff to settle the consolidated putative securities class-action lawsuit originally filed in August 2007 in the United States District Court for the Eastern District of New York. Under the terms of the proposed settlement, the lawsuit will be dismissed with prejudice, without any admission of liability by the Company or the individual defendants. Both the Company and the individual defendants will receive a full and complete release of all claims asserted against them in the litigation, in exchange for the payment of an aggregate of \$22,500, substantially all of which will be funded with insurance proceeds. The proposed settlement was submitted to the United States District Court for the Eastern District of New York for preliminary approval on May 16, 2012. The agreement is subject to the execution of definitive settlement documents and court approval after the class has been notified of its terms. The Company has reflected appropriate costs, contingent liabilities and related insurance recoveries in the condensed consolidated financial statements as of April 30, 2012 and July 31, 2011.

The Company and its subsidiaries are subject to certain other legal actions that arise in the normal course of business. Other than those legal proceedings and claims discussed above and in the 2011 Form 10-K, the Company did not have any current other legal proceedings and claims that would individually or in the aggregate have a reasonably possible materially adverse affect on its financial condition or operating results. As such, any reasonably possible loss or range of loss, other than those legal proceedings discussed in this note and in the 2011 Form 10-K, is immaterial. However, the results of legal proceedings cannot be predicted with certainty. If the Company failed to prevail in several of these legal matters in the same reporting period, the operating results of a particular reporting period could be materially adversely affected.

Environmental Matters:

The Company's condensed consolidated balance sheet at April 30, 2012 includes liabilities for environmental matters of approximately \$12,632, which relate primarily to the environmental proceedings discussed in the 2011 Form 10-K. In the opinion of management, the Company is in substantial compliance with applicable environmental laws and its current accruals for environmental remediation are adequate. However, as regulatory standards under environmental laws are becoming increasingly stringent, there can be no assurance that future developments, additional information and experience gained will not cause the Company to incur material environmental liabilities or costs beyond those accrued in its condensed consolidated financial statements.

NOTE 6 – RESTRUCTURING AND OTHER CHARGES, NET

The following tables summarize the restructuring and other charges ("ROTC") recorded for the three and nine months ended April 30, 2012 and April 30, 2011:

	Three Months Ended Apr 30, 2012			Nine Months Ended Apr 30, 2012		
	Restructuring (1)	Other (Gains)/ Charges (2)	Total	Restructuring (1)	Other (Gains)/ Charges (2)	Total
Severance benefits and other employment contract obligations	\$953	\$2,604	\$3,557	\$29,255	\$11,436	\$40,691
Gain on sale of assets	—	(2,168)	(2,168)	(1,515)	(11,364)	(12,879)
Professional fees, legal settlements and other costs, net of receipt of insurance claim	1,755	(252)	1,503	3,121	145	3,266

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payments						
Reversal of excess restructuring reserves	(31) —	(31) (77) —	(77
	\$2,677	\$184	\$2,861	\$30,784	\$217	\$31,001
Cash	\$2,677	\$(942) \$1,735	\$30,784	\$(3,446) \$27,338
Non-cash(a)	—	1,126	1,126	—	3,663	3,663
	\$2,677	\$184	\$2,861	\$30,784	\$217	\$31,001

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PALL CORPORATION AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(In thousands, except per share data)

(Unaudited)

	Three Months Ended Apr 30, 2011			Nine Months Ended Apr 30, 2011			
	Restructuring (1)	Other (Gains)/ Charges (2)	Total	Restructuring (1)	Other (Gains)/ Charges (2)	Total	
Severance benefits and other employment contract obligations	\$716	\$4,631	\$5,347	\$4,169	\$4,631	\$8,800	
Professional fees and other costs, net of receipt of insurance claim payments	1,431	891	2,322	4,151	272	4,423	
Environmental matters	—	59	59	—	709	709	
Reversal of excess restructuring reserves	(5) —	(5) (11) —	(11)
	\$2,142	\$5,581	\$7,723	\$8,309	\$5,612	\$13,921	
Cash	\$2,142	\$3,241	\$5,383	\$8,309	\$3,272	\$11,581	
Non-cash	—	2,340	2,340	—	2,340	2,340	
	\$2,142	\$5,581	\$7,723	\$8,309	\$5,612	\$13,921	

(a) Reflects non-cash stock based compensation expense.

(1) Restructuring:

Restructuring charges recorded in the three and nine months ended April 30, 2012 and April 30, 2011 reflect the expenses incurred in connection with the Company's cost reduction initiatives.

Severance benefits recorded in the three and nine months ended April 30, 2012 primarily relate to global restructuring activities in the Industrial segment. The most significant restructuring activities include:

- the realignment of sales and marketing management of certain of the Company's markets,
- the reorganization of the global management structure that supports the Company's systems product line, and
- shifting resources from mature country markets to emerging regions.

Restructuring charges/(income) in the nine months ended April 30, 2012 also includes a gain on the divestiture of a non-strategic asset group.

Severance benefits recorded in the three and nine months ended April 30, 2011 primarily relate to the closure of an Industrial manufacturing facility in Europe.

(2) Other (Gains) / Charges:

Employment contract obligations and other severance benefits:

In the three and nine months ended April 30, 2012, the Company recorded charges related to certain employment contract obligations.

Gain on sale of assets:

In the three months ended April 30, 2012 the Company recored a gain on sale of assets related to the sale of a building in Europe. The nine months ended April 30, 2012 also includes a gain of \$9,196 on the sale of the Company's investment in Satair A/S.

Professional fees and other costs:

In the three and nine months ended April 30, 2012 and April 30, 2011, the Company recorded legal and other professional fees related to the Federal Securities Class Actions, Shareholder Derivative Lawsuits and Other Proceedings (see Note 5, Contingencies and Commitments) which pertain to matters that had been under audit committee inquiry as discussed in Note 2, Audit Committee Inquiry and Restatement, to the consolidated financial statements included in the Company's Annual Report on Form 10-K for the fiscal year ended July 31, 2007 ("2007 Form 10-K"). Furthermore, in the nine months ended April 30, 2012, the Company

PALL CORPORATION AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(In thousands, except per share data)

(Unaudited)

recorded costs related to the settlement of the Federal Securities Class Actions (see Note 5, Contingencies and Commitments). The receipt of insurance claim payments more than offset the costs discussed above in the three months ended April 30, 2012 and offset the majority of such costs in the nine months ended April 30, 2012 and April 30, 2011.

The following table summarizes the activity related to restructuring liabilities that were recorded in the nine months ended April 30, 2012 and in fiscal years 2011, 2010 and 2009.

	Severance	Other	Total
2012			
Original charge	\$29,255	\$3,121	\$32,376
Utilized	(23,151	) (2,121	) (25,272
Translation	271	12	283
Balance at Apr 30, 2012	\$6,375	\$1,012	\$7,387
	Severance	Other	Total
2011			
Original charge	\$4,863	\$5,507	\$10,370
Utilized	(1,817	) (5,225	) (7,042
Translation	272	68	340
Balance at Jul 31, 2011	\$3,318	\$350	\$3,668
Utilized	(3,199	) (350	) (3,549
Translation	(119	) —	(119
Balance at Apr 30, 2012	\$—	\$—	\$—
	Severance	Other	Total
2010			
Original charge (a)	\$6,034	\$5,581	\$11,615
Utilized	(2,031	) (5,441	) (7,472
Translation	1	(9	) (8
Balance at Jul 31, 2010	\$4,004	\$131	\$4,135
Utilized	(1,356	) (135	) (1,491
Translation	2	4	6
Balance at Jul 31, 2011	\$2,650	\$—	\$2,650
Utilized	(1,608	) —	(1,608
Translation	—	—	—
Balance at Apr 30, 2012	\$1,042	\$—	\$1,042

PALL CORPORATION AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(In thousands, except per share data)

(Unaudited)

	Severance	Other	Total
2009			
Original charge	\$18,938	\$4,734	\$23,672
Utilized	(12,757	) (4,133	) (16,890
Translation	412	20	432
Balance at Jul 31, 2009	6,593	621	7,214
Utilized	(4,902	) (588	) (5,490
Reversal of excess reserves	(143	) —	(143
Translation	(86	) (27	) (113
Balance at Jul 31, 2010	\$1,462	\$6	\$1,468
Utilized	(845	) (6	) (851
Reversal of excess reserves	(6	) —	(6
Translation	120	—	120
Balance at Jul 31, 2011	\$731	\$—	\$731
Utilized	(317	) —	(317
Reversal of excess reserves	(46	) —	(46
Translation	(48	) —	(48
Balance at Apr 30, 2012	\$320	\$—	\$320

(a) Excludes stock-based compensation expense of \$603

NOTE 7 – INCOME TAXES

The Company's effective tax rate on continuing operations for the nine months ended April 30, 2012 and April 30, 2011 was 22.8% and 29.7%, respectively. For the nine months ended April 30, 2012 and April 30, 2011, the effective tax rate on continuing operations varied from the U.S. federal statutory rate primarily due to the benefits of foreign operations, offset by tax costs of \$8,409 associated with the establishment of the Company's Asian headquarters recorded in the third quarter of fiscal year 2011.

At April 30, 2012 and July 31, 2011, the Company had gross unrecognized income tax benefits of \$215,798 and \$188,380, respectively. During the nine months ended April 30, 2012, the amount of gross unrecognized tax benefits increased by \$27,418, primarily due to tax positions taken during the fiscal year, partially offset by the impact of foreign currency translation and the expiration of various statutes of limitations. As of April 30, 2012, the amount of net unrecognized income tax benefits that, if recognized, would impact the effective tax rate was \$144,360.

At April 30, 2012 and July 31, 2011, the Company had liabilities of \$33,557 and \$29,652, respectively, for potential payment of interest and penalties.

Based on recent discussion with various tax authorities and due to the expiration of various statutes of limitations, the Company believes that it is reasonably possible that the gross amount of unrecognized tax benefits may decrease within the next twelve months by a range of zero to \$61,633. As a result, the Company has reclassified \$57,126 of income taxes payable and \$17,870 of interest payable from non-current liabilities to current liabilities, respectively.

PALL CORPORATION AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(In thousands, except per share data)

(Unaudited)

NOTE 8 – COMPONENTS OF NET PERIODIC PENSION COST

Net periodic pension benefit cost for the Company's defined benefit pension plans includes the following components (included in the table below is net periodic benefit cost included in discontinued operations for the three months ended April 30, 2012 and April 30, 2011 of \$185 and \$177, respectively, and \$552 and \$536 for the nine months ended April 30, 2012 and April 30, 2011, respectively):

	Three Months Ended					
	U.S. Plans		Foreign Plans		Total	
	Apr 30, 2012	Apr 30, 2011	Apr 30, 2012	Apr 30, 2011	Apr 30, 2012	Apr 30, 2011
Service cost	\$2,231	\$2,014	\$1,157	\$1,304	\$3,388	\$3,318
Interest cost	3,052	3,100	4,527	4,578	7,579	7,678
Expected return on plan assets	(2,303)	(2,202)	(3,908)	(3,554)	(6,211)	(5,756)
Amortization of prior service cost	374	615	(31)	71	343	686
Recognized actuarial loss	1,546	1,946	1,312	1,415	2,858	3,361
Gain due to curtailments and settlements	—	—	—	(23)	—	(23)
Net periodic benefit cost	\$4,900	\$5,473	\$3,057	\$3,791	\$7,957	\$9,264
	Nine Months Ended					
	U.S. Plans		Foreign Plans		Total	
	Apr 30, 2012	Apr 30, 2011	Apr 30, 2012	Apr 30, 2011	Apr 30, 2012	Apr 30, 2011
Service cost	\$6,693	\$6,044	\$3,548	\$3,912	\$10,241	\$9,956
Interest cost	9,699	9,164	13,643	13,735	23,342	22,899
Expected return on plan assets	(6,909)	(6,608)	(11,727)	(10,661)	(18,636)	(17,269)
Amortization of prior service cost	1,405	1,527	(98)	215	1,307	1,742
Recognized actuarial loss	6,546	3,880	3,944	4,245	10,490	8,125
Gain due to curtailments and settlements	—	—	—	(71)	—	(71)
Net periodic benefit cost	\$17,434	\$14,007	\$9,310	\$11,375	\$26,744	\$25,382

NOTE 9 – STOCK-BASED PAYMENT

The Company currently has four stock-based employee and director compensation award types (Restricted Stock Unit, Stock Option Plans, Management Stock Purchase Plan (“MSPP”), and Employee Stock Purchase Plan (“ESPP”)), which are more fully described in Note 15, Common Stock, to the consolidated financial statements included in the 2011 Form 10-K.

On December 14, 2011, the Company's shareholders approved the Pall Corporation 2012 Stock Compensation Plan (the “2012 Stock Plan”). The Board adopted the 2012 Stock Plan on September 26, 2011, subject to shareholder approval. The 2012 Stock Plan replaced the Pall Corporation 2005 Stock Compensation Plan (the “2005 Stock Plan”). Similar to the 2005 Stock Plan, the 2012 Stock Plan permits the Company to grant to its employees, including the Company's “named executive officers”, a variety of equity compensation (that is, stock options, restricted shares, restricted units, performance shares and performance units). In addition, the 2012 Stock Plan provides that (i) in January of each calendar year, each member of the board of directors who is not on such grant date an employee of the Company will be granted a number of annual award units as determined by the board of directors, (ii) each person who is elected a director of the Company for the first time at an annual meeting and who is not an employee of the Company on the date of such annual meeting will receive a number of annual award units as determined by the board of directors, and (iii) at the discretion of a non-employee director, 100% of the cash fees paid to such director in a

calendar year may be deferred in additional units which will be paid out either in one lump sum or in five equal annual installments upon the director ceasing to be a member of the board. Up to 7,100 shares are issuable under the 2012 Stock Plan. The number of shares available for awards under the 2012 Stock Plan will be reduced by one share for every

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PALL CORPORATION AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(In thousands, except per share data)

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one share subject to a stock option granted under the 2012 Stock Plan and will be reduced by 2.31 shares for every one share subject to a Full Value Award (i.e., restricted shares, restricted units, performance shares and performance units).

The fair value of stock options is estimated using a Black-Scholes-Merton option pricing formula and are charged to earnings over the service periods during which the options are deemed to be earned; which is generally four years. The forms of options currently approved for use in awarding options provide that the options may not be exercised within one year from the date of grant, and expire if not fully exercised within seven years from the date of grant. Generally, in any year after the first year, the options can be exercised with respect to only up to 25% of the shares subject to the option, computed cumulatively.

The fair value of the restricted unit awards is determined by reference to the closing price of the Company's common stock on the date of the award, and are charged to earnings over the service periods during which the awards are deemed to be earned; four years, in the case of units awarded to employees and upon grant, in the case of the annual award units to non-employee directors. The annual award units granted to non-employee directors of the Company (and any related dividends paid in the form of additional units) are converted to shares once the director ceases to be a member of the board of directors, other than removal for cause. Restricted stock units granted to employees vest after the fourth anniversary of the date of grant. Dividends on unvested restricted stock units vest at the same time as the restricted units for which the dividends were recorded and are forfeitable if the participant does not vest in the original award.

The detailed components of stock-based compensation expense recorded in the condensed consolidated statements of earnings for the three and nine months ended April 30, 2012 and April 30, 2011 are reflected in the table below (excluded from the table below is stock-based compensation expense included in discontinued operations for the three months ended April 30, 2012 and April 30, 2011 of \$165 and \$125, respectively, and \$496 and \$367 for the nine months ended April 30, 2012 and April 30, 2011, respectively):

	Three Months Ended		Nine Months Ended	
	Apr 30, 2012	Apr 30, 2011	Apr 30, 2012	Apr 30, 2011
Restricted stock units	\$4,541	\$4,145	\$13,880	\$10,177
Stock options	2,013	2,100	5,208	4,078
ESPP	1,415	1,118	3,980	3,180
MSPP	1,027	997	3,131	2,943
Total	\$8,996	\$8,360	\$26,199	\$20,378

NOTE 10 – EARNINGS PER SHARE

The condensed consolidated statements of earnings present basic and diluted earnings per share. Basic earnings per share is determined by dividing income available to common shareholders by the weighted average number of common shares outstanding for the period. Diluted earnings per share considers the potential effect of dilution on basic earnings per share assuming potentially dilutive shares that meet certain criteria, such as those issuable upon exercise of stock options, were outstanding. The treasury stock method reduces the dilutive effect of potentially dilutive securities as it assumes that cash proceeds (from the issuance of potentially dilutive securities) are used to buy back shares at the average share price during the period. Employee stock options and restricted stock units aggregating 575 and 98 shares were not included in the computation of diluted shares for the three months ended April 30, 2012 and April 30, 2011, respectively, because their effect would have been antidilutive. For the nine months ended April 30, 2012 and April 30, 2011, 862 and 180 antidilutive shares, respectively, were excluded. The following is a reconciliation between basic shares outstanding and diluted shares outstanding:

	Three Months Ended		Nine Months Ended	
	Apr 30, 2012	Apr 30, 2011	Apr 30, 2012	Apr 30, 2011
Basic shares outstanding	116,567	116,899	116,190	116,565

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Effect of stock plans	1,791	1,824	1,627	1,731
Diluted shares outstanding	118,358	118,723	117,817	118,296

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PALL CORPORATION AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(In thousands, except per share data)

(Unaudited)

NOTE 11 – FAIR VALUE MEASUREMENTS

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

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

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

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

Level 3: Use of inputs that are unobservable.

The following table presents, for each of these hierarchy levels, the Company's financial assets and liabilities that are measured at fair value on a recurring basis as of April 30, 2012:

	Fair Value Measurements			
	As of Apr 30, 2012	Level 1	Level 2	Level 3
Financial assets carried at fair value				
Money market funds	\$2,568	\$2,568	\$—	\$—
Available-for-sale securities:				
Equity securities	1,017	1,017	—	—
Debt securities:				
Corporate	35,641	—	35,641	—
U.S. Treasury	5,787	—	5,787	—
Federal agency	29,340	—	29,340	—
Mortgage-backed	6,363	—	6,363	—
Municipal government	1,004	—	1,004	—
Derivative financial instruments:				
Foreign exchange forward contracts	2,679	—	2,679	—
Financial liabilities carried at fair value				
Derivative financial instruments:				
Foreign exchange forward contracts	567	—	567	—

PALL CORPORATION AND SUBSIDIARIES
 NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)
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The following table presents, for each of these hierarchy levels, the Company's financial assets and liabilities that are measured at fair value on a recurring basis as of July 31, 2011:

	Fair Value Measurements			
	As of Jul 31, 2011	Level 1	Level 2	Level 3
Financial assets carried at fair value				
Money market funds	\$4,575	\$4,575	\$—	\$—
Available-for-sale securities:				
Equity securities	12,064	12,064	—	—
Debt securities:				
Corporate	32,020	—	32,020	—
U.S. Treasury	10,210	—	10,210	—
Federal agency	29,404	—	29,404	—
Mortgage-backed	6,356	—	6,356	—
Municipal government	1,002	—	1,002	—
Derivative financial instruments:				
Foreign exchange forward contracts	1,456	—	1,456	—
Financial liabilities carried at fair value				
Derivative financial instruments:				
Foreign exchange forward contracts	478	—	478	—

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

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

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

The Company completed its annual goodwill impairment test for all reporting units in the third quarter of fiscal year 2012 and determined that no impairment existed. In addition, the Company had no impairment of goodwill in the prior year. In connection with the annual goodwill impairment test, the Company estimates the fair value of its reporting units using a market approach employing level 3 inputs as defined in the fair value hierarchy.

In connection with the acquisitions in the first and third quarters of fiscal year 2012, the Company recorded the fair value of the intangible assets acquired, which were valued using the income approach. The valuation employed level 3 inputs, as defined in the fair value hierarchy.

NOTE 12 – INVESTMENT SECURITIES

The following is a summary of the Company's available-for-sale investment securities by category which are classified within other non-current assets in the Company's condensed consolidated balance sheets. Contractual maturity dates of debt securities held by the trust at April 30, 2012 range from 2012 to 2044.

PALL CORPORATION AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(In thousands, except per share data)

(Unaudited)

	Cost/ Amortized Cost Basis	Fair Value	Gross Unrealized Holding Gains	Gross Unrealized Holding Losses	Net Unrealized Holding Gains
April 30, 2012					
Equity securities	\$1,022	\$1,017	\$—	\$(5)	\$(5)
Debt securities:					
Corporate	33,903	35,641	1,789	(51)	1,738
U.S. Treasury	5,363	5,787	424	—	424
Federal agency	27,669	29,340	1,674	(3)	1,671
Mortgage-backed	6,144	6,363	244	(25)	219
Municipal government	1,000	1,004	4	—	4
	\$75,101	\$79,152	\$4,135	\$(84)	\$4,051
July 31, 2011					
Equity securities	\$2,381	\$12,064	\$9,683	\$—	\$9,683
Debt securities:					
Corporate	30,239	32,020	1,814	(33)	1,781
U.S. Treasury	9,544	10,210	666	—	666
Federal agency	28,042	29,404	1,362	—	1,362
Mortgage-backed	6,242	6,356	144	(30)	114
Municipal government	1,000	1,002	2	—	2
	\$77,448	\$91,056	\$13,671	\$(63)	\$13,608

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

	Less than 12 months		12 months or greater		Total	
	Fair Value	Gross Unrealized Holding Losses	Fair Value	Gross Unrealized Holding Losses	Fair Value	Gross Unrealized Holding Losses
April 30, 2012						
Debt securities:						
Corporate	\$5,013	\$51	\$—	\$—	\$5,013	\$51
Mortgage-backed	—	—	1,506	25	\$1,506	\$25
Federal agency	386	3	—	—	386	3
Equity securities	28	5	—	—	28	5
	\$5,427	\$59	\$1,506	\$25	\$6,933	\$84
July 31, 2011						
Debt securities:						
Mortgage-backed	\$1,502	\$30	\$—	\$—	\$1,502	\$30

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Corporate	1,985	33	—	—	1,985	33
	\$3,487	\$63	\$—	\$—	\$3,487	\$63

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PALL CORPORATION AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(In thousands, except per share data)

(Unaudited)

The following table shows the proceeds and gross gains and losses from the sale of available-for-sale investments for the three and nine months ended April 30, 2012 and April 30, 2011:

	Three Months Ended		Nine Months Ended	
	Apr 30, 2012	Apr 30, 2011	Apr 30, 2012	Apr 30, 2011
Proceeds from sales	\$5,473	\$4,891	\$26,700	\$19,103
Realized gross gains on sales	176	72	9,654	766
Realized gross losses on sales	12	8	28	20

NOTE 13 – DERIVATIVE INSTRUMENTS AND HEDGING ACTIVITIES

The Company manages certain financial exposures through a risk management program that includes the use of foreign exchange and interest rate derivative financial instruments. Derivatives are executed with counterparties with a minimum credit rating of “A” by Standard & Poors and Moody’s Investor Services, in accordance with the Company’s policies. The Company does not utilize derivative instruments for trading or speculative purposes.

Foreign Exchange Related:

a. Derivatives Not Designated as Hedging Instruments

The risk management objective of holding foreign exchange derivatives is to mitigate volatility to earnings and cash flows due to changes in foreign exchange rates. The Company and its subsidiaries conduct transactions in currencies other than their functional currencies. These transactions include non-functional intercompany and external sales as well as intercompany and external purchases. The Company uses foreign exchange forward contracts, matching the notional amounts and durations of the receivables and payables resulting from the aforementioned underlying foreign currency transactions, to mitigate the exposure to earnings and cash flows caused by the changes in fair value of these receivables and payables from fluctuating foreign exchange rates. The notional amount of foreign currency forward contracts entered into during the three and nine months ended April 30, 2012 was \$522,774 and \$1,894,385, respectively. The notional amount of foreign currency forward contracts outstanding as of April 30, 2012 was \$244,047.

b. Net Investment Hedges

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

Interest Rate Related:

As of April 30, 2012, there are no existing interest rate related derivatives.

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

April 30, 2012	Asset Derivatives		Liability Derivatives	
	Balance Sheet Location	Fair Value	Balance Sheet Location	Fair Value
Derivatives designated as hedging instruments				
Not applicable (N/A)				
Derivatives not designated as hedging instruments				
Foreign exchange forward contracts	Other current assets	\$2,679	Other current liabilities	\$567
Total derivatives		\$2,679		\$567
Nonderivative instruments designated as hedging instruments				

Net investment hedge	Long-term debt, net of current portion	\$ 112,128
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NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(In thousands, except per share data)

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July 31, 2011	Asset Derivatives Balance Sheet Location	Fair Value	Liability Derivatives Balance Sheet Location	Fair Value
Derivatives designated as hedging instruments				
N/A				
Derivatives not designated as hedging instruments				
Foreign exchange forward contracts	Other current assets			