DOVER Corp
Form 10-Q
July 21, 2016

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

FORM 10-Q

(Mark One)
x QUARTERLY REPORT PURSUANT TO SECTION 13 or 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the quarterly period ended June 30, 2016

or

o TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the transition period from to

Commission File Number: 1-4018

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

Delaware	53-0257888
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)

3005 Highland Parkway	
Downers Grove, Illinois	60515
(Address of principal executive offices)	(Zip Code)

(630) 541-1540
(Registrant's telephone number, including area code)

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

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

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

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

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

The number of shares outstanding of the Registrant's common stock as of July 14, 2016 was 155,215,908.

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Item 1. Financial Statements

DOVER CORPORATION
CONDENSED CONSOLIDATED STATEMENTS OF EARNINGS
(in thousands, except per share data)
(unaudited)

	Three Months Ended June 30,		Six Months Ended June 30,	
	2016	2015	2016	2015
Revenue	$1,686,345	$1,758,628	$3,308,618	$3,474,129
Cost of goods and services	1,055,132	1,104,060	2,088,141	2,192,402
Gross profit	631,213	654,568	1,220,477	1,281,727
Selling and administrative expenses	437,411	402,695	880,859	837,329
Operating earnings	193,802	251,873	339,618	444,398
Interest expense, net	32,157	31,988	63,871	64,025
Other income, net	(2,854)	(1,256)	(16,376)	(5,443)
Earnings before provision for income taxes and discontinued operations	164,499	221,141	292,123	385,816
Provision for income taxes	46,209	65,507	74,477	112,992
Earnings from continuing operations	118,290	155,634	217,646	272,824
Earnings from discontinued operations, net	—	176,762	—	269,082
Net earnings	$118,290	$332,396	$217,646	$541,906
Earnings per share from continuing operations:				
Basic	$0.76	$0.98	$1.40	$1.70
Diluted	$0.76	$0.97	$1.39	$1.69
Earnings per share from discontinued operations:				
Basic	$—	$1.11	$—	$1.68
Diluted	$—	$1.10	$—	$1.66
Net earnings per share:				
Basic	$0.76	$2.10	$1.40	$3.38
Diluted	$0.76	$2.07	$1.39	$3.35
Weighted average shares outstanding:				
Basic	155,180	158,640	155,122	160,137
Diluted	156,595	160,398	156,414	161,876
Dividends paid per common share	$0.42	$0.40	$0.84	$0.80

See Notes to Condensed Consolidated Financial Statements

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DOVER CORPORATION
CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE EARNINGS
(in thousands)
(unaudited)

	Three Months Ended June 30,		Six Months Ended June 30,	
	2016	2015	2016	2015
Net earnings	$118,290	$332,396	$217,646	$541,906
Other comprehensive (loss) earnings, net of tax				
Foreign currency translation adjustments:				
Foreign currency translation (losses) gains during period	(41,992)	39,287	(33,223)	(44,542)
Reclassification of foreign currency translation gains to earnings upon sale of subsidiaries	—	(2,837)	—	(3,117)
Total foreign currency translation	(41,992)	36,450	(33,223)	(47,659)
Pension and other postretirement benefit plans:				
Amortization of actuarial losses included in net periodic pension cost	1,416	2,590	2,825	5,188
Amortization of prior service costs included in net periodic pension cost	1,040	1,227	2,081	2,455
Total pension and other postretirement benefit plans	2,456	3,817	4,906	7,643
Changes in fair value of cash flow hedges:				
Unrealized net (losses) gains arising during period	(162)	(807)	(211)	351
Net losses reclassified into earnings	213	570	166	471
Total cash flow hedges	51	(237)	(45)	822
Other	(448)	277	1,392	491
Other comprehensive (loss) earnings	(39,933)	40,307	(26,970)	(38,703)
Comprehensive earnings	$78,357	$372,703	$190,676	$503,203

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DOVER CORPORATION
CONDENSED CONSOLIDATED BALANCE SHEETS
(in thousands)
(unaudited)

	June 30, 2016	December 31, 2015
Current assets:		
Cash and cash equivalents	$255,140	$ 362,185
Receivables, net of allowances of $19,402 and $18,050	1,180,146	1,120,490
Inventories, net	833,907	802,895
Prepaid and other current assets	110,563	133,440
Total current assets	2,379,756	2,419,010
Property, plant and equipment, net	853,584	854,269
Goodwill	4,034,499	3,737,389
Intangible assets, net	1,499,894	1,413,223
Other assets and deferred charges	211,359	182,185
Total assets	$8,979,092	$ 8,606,076
Current liabilities:		
Notes payable and current maturities of long-term debt	$344,157	$ 151,122
Accounts payable	723,693	650,880
Accrued compensation and employee benefits	197,166	223,039
Accrued insurance	102,219	99,642
Other accrued expenses	252,373	235,971
Federal and other taxes on income	20,759	6,528
Total current liabilities	1,640,367	1,367,182
Long-term debt, net	2,607,066	2,603,655
Deferred income taxes	593,776	575,709
Other liabilities	424,148	414,955
Stockholders' equity:		
Total stockholders' equity	3,713,735	3,644,575
Total liabilities and stockholders' equity	$8,979,092	$ 8,606,076

See Notes to Condensed Consolidated Financial Statements

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DOVER CORPORATION
CONDENSED CONSOLIDATED STATEMENT OF STOCKHOLDERS' EQUITY
(in thousands, except share data)
(unaudited)

	Common Stock $1 Par Value	Additional Paid-In Capital	Retained Earnings	Accumulated Other Comprehensive Earnings (Loss)	Treasury Stock	Total Stockholders' Equity
Balance at December 31, 2015	$256,113	$928,409	$7,686,642	$ (254,573)	$(4,972,016)	$3,644,575
Net earnings	—	—	217,646	—	—	217,646
Dividends paid	—	—	(130,654)	—	—	(130,654)
Common stock issued for the exercise of share-based awards	211	(7,651)	—	—	—	(7,440)
Tax benefit from the exercise of share-based awards	—	2,218	—	—	—	2,218
Share-based compensation expense	—	14,360	—	—	—	14,360
Other comprehensive earnings, net of tax	—	—	—	(26,970)	—	(26,970)
Balance at June 30, 2016	$256,324	$937,336	$7,773,634	$ (281,543)	$(4,972,016)	$3,713,735

Preferred Stock: $100 par value per share; 100,000 shares authorized; no shares issued.

See Notes to Condensed Consolidated Financial Statements

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DOVER CORPORATION
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
(in thousands)
(unaudited)

	Six Months Ended June 30, 2016	2015
Operating Activities of Continuing Operations		
Net earnings	$217,646	$541,906
Adjustments to reconcile net earnings to cash from operating activities:		
Earnings from discontinued operations, net	—	(269,082)
Depreciation and amortization	176,698	158,209
Share-based compensation	14,360	18,851
Gain on sale of assets	(1,530)	—
Gain on sale of business	(11,228)	—
Cash effect of changes in assets and liabilities:		
Accounts receivable	429	17,459
Inventories	(16,429)	861
Prepaid expenses and other assets	(5,449)	1,025
Accounts payable	5,377	6,588
Accrued compensation and employee benefits	(42,534)	(87,716)
Accrued expenses and other liabilities	16,135	(21,313)
Accrued and deferred taxes, net	11,746	(17,805)
Other, net	(23,940)	1,260
Net cash provided by operating activities of continuing operations	341,281	350,243
Investing Activities of Continuing Operations		
Additions to property, plant and equipment	(72,652)	(71,763)
Acquisitions (net of cash and cash equivalents acquired)	(475,236)	(6,500)
Proceeds from the sale of property, plant and equipment	5,804	7,723
Proceeds from the sale of businesses	47,300	685,000
Other	(488)	—
Net cash (used in) provided by investing activities of continuing operations	(495,272)	614,460
Financing Activities of Continuing Operations		
Purchase of common stock	—	(500,134)
Proceeds from exercise of share-based awards, including tax benefits	3,966	3,481
Change in commercial paper and notes payable, net	185,556	(396,100)
Dividends paid to stockholders	(131,253)	(127,659)
Payments to settle employee tax obligations on exercise of share-based awards	(7,440)	(4,478)
Reduction of long-term debt	—	(42)
Net cash provided by (used in) financing activities of continuing operations	50,829	(1,024,932)
Cash Flows from Discontinued Operations		
Net cash used in operating activities of discontinued operations	—	(10,053)
Net cash used in investing activities of discontinued operations	—	(1,984)
Net cash used in discontinued operations	—	(12,037)

Effect of exchange rate changes on cash and cash equivalents	(3,883)	(14,147)
Net decrease in cash and cash equivalents	(107,045)	(86,413)
Cash and cash equivalents at beginning of period	362,185	681,581
Cash and cash equivalents at end of period	$255,140	$595,168

See Notes to Condensed Consolidated Financial Statements

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NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(Amounts in thousands except share data and where otherwise indicated)

1. Basis of Presentation

The accompanying unaudited Condensed Consolidated Financial Statements, in accordance with Securities and Exchange Commission ("SEC") rules for interim periods, do not include all of the information and notes for complete financial statements as required by accounting principles generally accepted in the United States of America. As such, the accompanying unaudited Condensed Consolidated Financial Statements should be read in conjunction with the Dover Corporation ("Dover" or the "Company") Annual Report on Form 10-K for the year ended December 31, 2015, which provides a more complete understanding of the Company's accounting policies, financial position, operating results, business, properties, and other matters. The year end Condensed Consolidated Balance Sheet was derived from audited financial statements. Certain amounts in the prior year have been reclassified to conform to the current year presentation.

It is the opinion of management that these financial statements reflect all adjustments necessary for a fair statement of the interim results. The results of operations of any interim period are not necessarily indicative of the results of operations for the full year.

2. Acquisitions

During the six months ended June 30, 2016, the Company acquired three businesses within the Fluids segment for net cash consideration of $475,236.

The following acquisitions were made during the six months ended June 30, 2016.
2016 Acquisitions

Date	Type	Company / Product Line Acquired	Location (Near)	Segment
January 7	Stock	Tokheim Group S.A.S.	Dundee, UK	Fluids
Manufacturer of fuel dispensers, retail automation systems and payment solutions.				
May 25	Stock	Fairbanks Environmental LTD	Skelmersdale, UK	Fluids
Provider of monitoring and optimization software and tools centered around fuel management and on-site services.				
June 13	Stock	ProGauge	Milan, Italy	Fluids
Provider of automatic tank gauge solutions, including a variety of tank probes, consoles, and related software and calibration services for service stations to measure and monitor fuel tank levels.				

The following presents the allocation of acquisition cost to the assets acquired and liabilities assumed, based on their estimated fair values:

	Total
Current assets, net of cash acquired	$101,243
Property, plant and equipment	31,240
Goodwill	301,577
Intangible assets	192,065
Other non-current assets	5,564
Current liabilities	(105,699)
Non-current liabilities	(50,754)

Net assets acquired	$475,236

The amounts assigned to goodwill and major intangible asset classifications for the 2016 acquisitions are as follows:

	Amount allocated	Useful life (in years)
Goodwill - Non deductible	$301,577	na
Customer intangibles	101,898	10
Trademarks	24,866	15
Other intangibles	65,301	10
	$493,642	

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NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(Amounts in thousands except share data and where otherwise indicated)

The goodwill identified by these acquisitions reflect the benefits expected to be derived from product line expansion and operational synergies. Upon consummation of the acquisitions, with the exception of a minor noncontrolling interest in the Tokheim China subsidiary, these businesses are now wholly-owned by Dover.

The Company has substantially completed the purchase price allocations for the 2016 acquisitions. As additional information is obtained about these assets and liabilities within the measurement period (not to exceed one year from the date of acquisition), the Company will refine its estimates of fair value to allocate the purchase price more accurately. Purchase price allocation adjustments may arise through working capital adjustments, asset appraisals or to reflect additional facts and circumstances in existence as of the acquisition date. Identified measurement period adjustments will be recorded, including any related impacts to net earnings, in the reporting period in which the adjustments are determined and may be significant. See Note 6 Goodwill and Other Intangible Assets for purchase price adjustments.

The unaudited Condensed Consolidated Statements of Earnings include the results of these businesses from the date of acquisition.

Pro Forma Information

The following unaudited pro forma information illustrates the impact of both 2016 and 2015 acquisitions on the Company's revenue and earnings from continuing operations for the three and six months ended June 30, 2016 and 2015. In 2015, the Company acquired four businesses in separate transactions for net cash consideration of $567,843.

The 2016 and 2015 pro forma information assumes that the 2016 and 2015 acquisitions had taken place at the beginning of the prior year. Pro forma earnings are also adjusted to reflect the comparable impact of additional depreciation and amortization expense (net of tax) resulting from the fair value measurement of tangible and intangible assets relating to 2016 and 2015 acquisitions.

	Three Months Ended June 30,		Six Months Ended June 30,	
	2016	2015	2016	2015
Revenue from continuing operations:				
As reported	$1,686,345	$1,758,628	$3,308,618	$3,474,129
Pro forma	1,690,286	1,884,970	3,324,674	3,725,932
Earnings from continuing operations:				
As reported	$118,290	$155,634	$217,646	$272,824
Pro forma	120,556	165,251	229,031	286,930
Basic earnings per share from continuing operations:				
As reported	$0.76	$0.98	$1.40	$1.70
Pro forma	0.78	1.04	1.48	1.79
Diluted earnings per share from continuing operations:				
As reported	$0.76	$0.97	$1.39	$1.69
Pro forma	0.77	1.03	1.46	1.77

3. Disposed and Discontinued Operations

Management evaluates Dover's businesses periodically for their strategic fit within its operations and may from time to time sell or discontinue certain operations for various reasons.

Disposed Businesses

On February 17, 2016, the company completed the sale of Texas Hydraulics. This disposal did not represent a strategic shift in operations and, therefore, did not qualify for presentation as a discontinued operation. Upon disposal of the business the Company recognized total proceeds of $47,300, which resulted in a gain on sale of $11,228 included within Other income, net within the Condensed Consolidated Statements of Earnings.

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(Amounts in thousands except share data and where otherwise indicated)

Discontinued Operations

The results of discontinued operations for the three and six months ended June 30, 2015 reflect the net earnings of businesses held for sale, Datamax O'Neil and Sargent Aerospace, prior to their respective sale dates. On March 2, 2015, the Company completed the sale of Datamax O'Neil for total proceeds of $185,000, which resulted in a net gain on sale of $87,781. On April 24, 2015, the Company completed the sale of Sargent Aerospace for total proceeds of $500,000, which resulted in a net gain on sale of $177,800.

Summarized results of the Company’s discontinued operations are as follows:

	Three Months Ended June 30, 2015	Six Months Ended June 30, 2015
Revenue	$8,374	$72,869
Gain on sale, net of tax	178,227	265,581
(Loss) earnings from operations before taxes	(272)	8,708
Provision for income taxes	(1,193)	(5,207)
(Loss) earnings from operations, net of tax	(1,465)	3,501
Earnings from discontinued operations, net of tax	$176,762	$269,082

The Company had no assets or liabilities classified as held for sale as of June 30, 2016 and December 31, 2015.

4. Inventories, net

	June 30, 2016	December 31, 2015
Raw materials	$354,170	$ 333,551
Work in progress	154,841	135,624
Finished goods	436,755	443,032
Subtotal	945,766	912,207
Less reserves	(111,859)	(109,312)
Total	$833,907	$ 802,895

5. Property, Plant and Equipment, net

	June 30, 2016	December 31, 2015
Land	$56,104	$ 55,567
Buildings and improvements	555,345	546,809
Machinery, equipment and other	1,780,162	1,772,031
Subtotal	2,391,611	2,374,407
Less accumulated depreciation	(1,538,027)	(1,520,138)
Total	$853,584	$ 854,269

Depreciation expense totaled $44,501 and $38,408 for the three months ended June 30, 2016 and 2015, respectively. For the six months ended June 30, 2016 and 2015, depreciation expense was $89,530 and $78,616, respectively.

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NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(Amounts in thousands except share data and where otherwise indicated)

6. Goodwill and Other Intangible Assets

The following table provides the changes in carrying value of goodwill by segment for the six months ended June 30, 2016:

	Energy	Engineered Systems	Fluids	Refrigeration & Food Equipment	Total
Balance at December 31, 2015	$1,047,180	$1,473,864	$655,745	$ 560,600	$3,737,389
Acquisitions	—	—	301,577	—	301,577
Purchase price adjustments	—	363	4,688	580	5,631
Disposition of business	—	(9,615)	—	—	(9,615)
Foreign currency translation	1,463	1,394	(3,747)	407	(483)
Balance at June 30, 2016	$1,048,643	$1,466,006	$958,263	$ 561,587	$4,034,499

As noted in Note 3 Disposed and Discontinued Operations, the Company completed the sale of its Texas Hydraulics business during the six months ended June 30, 2016. As a result of this sale, the Engineered Systems goodwill balance was reduced by $9,615.

During the six months ended June 30, 2016, the Company recorded adjustments totaling $5,631 to goodwill relating to purchase price adjustments as a result of working capital adjustments and refinements of estimates to assets acquired and liabilities assumed for the 2015 acquisitions of Gemtron, JK Group, Gala Industries and Reduction Engineering Scheer. During the three months ended June 30, 2016, the Company recorded an adjustment of $17,200 to goodwill as a result of working capital adjustments for the acquisition of Tokheim in the first quarter of 2016. This reduction in price is included in Acquisitions in the table above.

In accordance with the applicable accounting standard, Dover performs its annual goodwill impairment testing in the fourth quarter of each year. In addition to the annual impairment test, the Company is required to regularly assess whether a triggering event has occurred which would require interim impairment testing. The Company has considered the economic environments in which its businesses operate, particularly those reporting units exposed to the decline in oil and gas markets, and the long-term outlook for those businesses. The Company has determined that a triggering event has not occurred which would require impairment testing at this time.

The following table provides the gross carrying value and accumulated amortization for each major class of intangible asset:

	June 30, 2016		December 31, 2015	
	Gross Carrying Amount	Accumulated Amortization	Gross Carrying Amount	Accumulated Amortization
Amortized intangible assets:				
Trademarks	$175,774	$ 52,863	$150,926	$ 45,536
Patents	152,110	119,160	150,570	112,399
Customer Intangibles	1,661,639	658,738	1,567,048	595,635
Unpatented Technologies	134,203	58,896	137,919	56,495
Drawings & Manuals	39,437	22,473	34,232	15,760
Distributor Relationships	117,272	41,421	64,614	37,610
Other	26,898	19,532	23,923	18,168
Total	2,307,333	973,083	2,129,232	881,603

Unamortized intangible assets:		
Trademarks	165,644	165,594
Total intangible assets, net	$1,499,894	$1,413,223

Amortization expense totaled $43,593 and $39,619 for the three months ended June 30, 2016 and 2015, respectively. For the six months ended June 30, 2016 and 2015, amortization expense was $87,168 and $79,593, respectively.

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(Amounts in thousands except share data and where otherwise indicated)

7. Restructuring Activities

The following table details restructuring charges incurred by segment for the periods presented:

	Three Months Ended June 30,		Six Months Ended June 30,	
	2016	2015	2016	2015
Energy	$5,610	$2,556	$12,026	$20,378
Engineered Systems	773	747	2,740	5,102
Fluids	2,764	58	7,990	2,155
Refrigeration & Food Equipment	52	(243)	73	(525)
Corporate	—	—	757	111
Total	$9,199	$3,118	$23,586	$27,221

These amounts are classified in the unaudited Condensed Consolidated Statements of Earnings as follows:

Cost of goods and services	$4,329	$2,474	$10,180	$9,928
Selling and administrative expenses	4,870	644	13,406	17,293
Total	$9,199	$3,118	$23,586	$27,221

The restructuring expenses of $9,199 and $23,586 incurred in the three and six months ended June 30, 2016 related to restructuring programs initiated during 2016 and 2015. These programs are designed to better align the Company's costs and operations with current market conditions through targeted facility consolidations, headcount reductions and other measures to further optimize operations. The Company expects the programs currently underway to be substantially completed in the next twelve to eighteen months.

The $9,199 of restructuring charges incurred during the second quarter of 2016 primarily included the following items:

- The Energy segment incurred restructuring charges of $5,610 related to various programs across the segment focused on workforce reductions and field and facility consolidations. These programs were initiated to better align cost base with the anticipated demand environment.

- The Fluids segment recorded $2,764 of restructuring charges principally related to headcount reductions and facility consolidations at various businesses across the segment.

- The Engineered Systems segment and Refrigeration and Food Equipment segment incurred restructuring charges related primarily to headcount reductions.

The following table details the Company’s severance and other restructuring accrual activity:

	Severance	Exit	Total
Balance at December 31, 2015	$11,036	$2,955	$13,991
Restructuring charges	17,052	6,534	23,586
Payments	(16,973)	(2,595)	(19,568)
Foreign currency translation	10	36	46
Other, including write-offs of fixed assets and acquired balances	2,374	(2,374)	—
Balance at June 30, 2016	$13,499	$4,556	$18,055

The accrual balance at June 30, 2016 primarily reflects restructuring plans initiated during the year, as well as ongoing lease commitment obligations for facilities closed in earlier periods.

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(Amounts in thousands except share data and where otherwise indicated)

8. Borrowings

Borrowings consist of the following:

	June 30, 2016	December 31, 2015
Short-term		
Current portion of long-term debt	$7,157	$ 122
Commercial paper	337,000	151,000
	$344,157	$ 151,122

	June 30, 2016	December 31, 2015
Long-term		
5.45% 10-year notes due March 15, 2018	349,423	349,258
2.125% 7-year notes due December 1, 2020 (Euro-denominated)	330,303	328,592
4.30% 10-year notes due March 1, 2021	449,878	449,865
3.150% 10-year notes due November 15, 2025	397,105	396,951
6.65% 30-year debentures due June 1, 2028	199,569	199,552
5.375% 30-year debentures due October 15, 2035	296,924	296,844
6.60% 30-year notes due March 15, 2038	248,080	248,036
5.375% 30-year notes due March 1, 2041	346,069	345,989
Other, less current installments	2,496	2,255
Total long-term debt	2,619,847	2,617,342
Unamortized debt issuance costs	(12,781)	(13,687)
Long-term debt, net of debt issuance costs	$2,607,066	$2,603,655

The Company adopted new accounting guidance effective January 1, 2016 which requires debt issuance costs related to a recognized debt liability be presented in the balance sheet as a direct reduction of the carrying amount of the related debt. Upon adoption, the Company reclassified $13,687 from assets to long-term debt to reflect this guidance in the comparable balance as of December 31, 2015.

The Company maintains a $1.0 billion five-year unsecured revolving credit facility with a syndicate of banks (the "Credit Agreement") which expires on November 10, 2020. The Company was in compliance with its revolving credit and other long-term debt covenants at June 30, 2016 and had a coverage ratio of 9.7 to 1.0. The Company primarily uses this facility as liquidity back-up for its commercial paper program and has not drawn down any loans under the facility and does not anticipate doing so. The Company generally uses commercial paper borrowings for general corporate purposes, funding of acquisitions, and repurchases of its common stock.

Interest expense and interest income for the three and six months ended June 30, 2016 and 2015 were as follows:

	Three Months Ended June 30,		Six Months Ended June 30,	
	2016	2015	2016	2015
Interest expense	$33,779	$33,053	$67,097	$66,058
Interest income	(1,622)	(1,065)	(3,226)	(2,033)
Interest expense, net	$32,157	$31,988	$63,871	$64,025

Letters of Credit

As of June 30, 2016, the Company had approximately $100,319 outstanding in letters of credit and guarantees with financial institutions which expire at various dates within 2016 through 2023. These letters of credit are primarily maintained as security for insurance, warranty, and other performance obligations.

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NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(Amounts in thousands except share data and where otherwise indicated)

9. Financial Instruments

Derivatives

The Company is exposed to market risk for changes in foreign currency exchange rates due to the global nature of its operations and certain commodity risks. In order to manage these risks the Company has hedged portions of its forecasted sales and purchases to occur within the next twelve months that are denominated in non-functional currencies, with currency forward or collar contracts designated as cash flow hedges. At June 30, 2016 and December 31, 2015, the Company had contracts with U.S. dollar equivalent notional amounts of $41,375 and $37,735, respectively, to exchange foreign currencies, principally the U.S. dollar, Chinese Yuan, Pound Sterling, Canadian Dollar, and Euro. The Company believes it is probable that all forecasted cash flow transactions will occur.

In addition, the Company had outstanding contracts with a total notional amount of $72,022 and $51,369 at June 30, 2016 and December 31, 2015, respectively, that are not designated as hedging instruments. These instruments are used to reduce the Company's exposure for operating receivables and payables that are denominated in non-functional currencies.

The following table sets forth the fair values of derivative instruments held by the Company as of June 30, 2016 and December 31, 2015 and the balance sheet lines in which they are recorded:

	Fair Value Asset (Liability)		
	June 30, 2016	December 31, 2015	Balance Sheet Caption
Foreign currency forward / collar contracts	$329	$ 170	Prepaid / Other assets
Foreign currency forward / collar contracts	(551)	(452)	Other accrued expenses

The amount of gains or losses from hedging activity recorded in earnings is not significant, and the amount of unrealized gains and losses from cash flow hedges that are expected to be reclassified to earnings in the next twelve months is not significant; therefore, additional tabular disclosures are not presented. There are no amounts excluded from the assessment of hedge effectiveness, and the Company's derivative instruments that are subject to credit risk contingent features were not significant.

The Company is exposed to credit loss in the event of nonperformance by counterparties to the financial instrument contracts held by the Company; however, nonperformance by these counterparties is considered unlikely as the Company’s policy is to contract with highly-rated, diversified counterparties.

Additionally, the Company has designated the €300.0 million of Euro-denominated notes issued December 4, 2013 as a hedge of a portion of its net investment in Euro-denominated operations. Due to the high degree of effectiveness between the hedging instruments and the exposure being hedged, fluctuations in the value of the Euro-denominated debt due to exchange rate changes are offset by changes in the net investment. Accordingly, changes in the value of the Euro-denominated debt are recognized in the cumulative translation adjustment section of other comprehensive income to offset changes in the value of the net investment in Euro-denominated operations.

Gains (losses) on net investment hedges are recognized in other compressive earnings (losses) as a part of foreign currency translation adjustments as follows:

	Three Months Ended June 30,	Six Months Ended June 30,

	2016	2015	2016	2015
Gain (loss) on Euro-denominated debt	$4,500	$(6,975)	$(1,665)	$28,375
Loss on Swiss franc cross-currency swap	—	(2,716)	—	(4,049)
Total gain (loss) on net investment hedges before tax	4,500	(9,691)	(1,665)	24,326
Tax (expense) benefit	(1,575)	3,392	583	(8,514)
Net gain (loss) on net investment hedges, net of tax	$2,925	$(6,299)	$(1,082)	$15,812

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Fair Value Measurements

ASC 820, "Fair Value Measurements and Disclosures," establishes a fair value hierarchy that requires the Company to maximize the use of observable inputs and minimize the use of unobservable inputs when measuring fair value. A financial instrument's categorization within the hierarchy is based on the lowest level of input that is significant to the fair value measurement. ASC 820 establishes three levels of inputs that may be used to measure fair value.

Level 1 inputs are quoted prices (unadjusted) in active markets for identical assets or liabilities.

Level 2 inputs include inputs other than Level 1 that are observable, either directly or indirectly, such as quoted prices in active markets for similar assets and liabilities, 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 for substantially the full term of assets or liabilities.

Level 3 inputs are unobservable inputs in which little or no market data exists, therefore requiring an entity to develop its own assumptions.

The following table presents the Company's assets and liabilities measured at fair value on a recurring basis as of June 30, 2016 and December 31, 2015:

	June 30, 2016 Level 2	December 31, 2015 Level 2
Assets:		
Foreign currency cash flow hedges	$ 329	$ 170
Liabilities:		
Foreign currency cash flow hedges	551	452

In addition to fair value disclosure requirements related to financial instruments carried at fair value, accounting standards require interim disclosures regarding the fair value of all of the Company's financial instruments.

The estimated fair value of long-term debt, net of unamortized debt issuance costs at June 30, 2016 and December 31, 2015 was $3,103,540 and $2,880,734, respectively, compared to the carrying value of $2,607,066 and $2,603,655, respectively. The estimated fair value of long-term debt is based on quoted market prices for similar instruments and is, therefore, classified as Level 2 within the fair value hierarchy.

The carrying values of cash and cash equivalents, trade receivables, accounts payable, and notes payable are reasonable estimates of their fair values as of June 30, 2016 and December 31, 2015 due to the short-term nature of these instruments.

10. Income Taxes

The effective tax rates for continuing operations for the three months ended June 30, 2016 and 2015 were 28.1% and 29.6%, respectively. Excluding unfavorable net discrete items in each period, the effective tax rates for the three months ended June 30, 2016 and 2015 were 27.3% and 29.3%, respectively. The discrete items for the three months ended June 30, 2016 resulted primarily from reassessment of the realizable benefits of certain state credits. The 2015 discrete items principally resulted from the conclusion of certain state tax audits and an adjustment of the tax accounts to the return filed. The reduction in the effective tax rate year over year is principally due to a change in the geographic mix of earnings as well as restructuring of foreign operations.

The effective tax rates for continuing operations for the six months ended June 30, 2016 and 2015 were 25.5% and 29.3%, respectively. Excluding net discrete items in each period, the effective tax rate for the six months ended June 30, 2016 and 2015 was 27.6% and 29.3%, respectively. The decrease in the effective tax rate for the six months ended June 30, 2016 relative to the prior year is primarily due to the revaluation of deferred tax balances as a result of a tax rate reduction in a non U.S. jurisdiction.

Dover and its subsidiaries file tax returns in the U.S., including various state and local returns, and in other foreign jurisdictions. We believe adequate provision has been made for all income tax uncertainties. The Company is routinely audited by taxing authorities in its filing jurisdictions, and a number of these audits are currently underway. The Company believes that within the next twelve months uncertain tax positions may be resolved and statutes of limitations will expire, which could result in a decrease

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in the gross amount of unrecognized tax benefits of approximately zero to $18,310. A portion of these unrecognized tax benefits relate to companies previously reported as discontinued operations.

11. Equity Incentive Program

The Company typically grants equity awards annually at its regularly scheduled first quarter meeting of the Compensation Committee of the Board of Directors. During the first and second quarters of 2016, the Company issued stock-settled appreciation rights ("SARs") covering 1,346,354 shares, performance share awards of 79,561 and restricted stock units of 244,707.

The Company uses the Black-Scholes option pricing model to determine the fair value of each SAR on the date of grant. Expected volatilities are based on Dover's stock price history, including implied volatilities from traded options on Dover stock. The Company uses historical data to estimate SAR exercise and employee termination patterns within the valuation model. The expected life of SARs granted is derived from the output of the option valuation model and represents the average period of time that SARs granted are expected to be outstanding. The interest rate for periods within the contractual life of the SARs is based on the U.S. Treasury yield curve in effect at the time of grant.

The assumptions used in determining the fair value of the SARs awarded during the respective periods are as follows:

	SARs	
	2016	2015
Risk-free interest rate	1.05 %	1.51 %
Dividend yield	3.09 %	2.24 %
Expected life (years)	4.6	5.1
Volatility	26.17 %	27.19 %
Grant price	$57.25	$73.28
Fair value per share at date of grant	$9.25	$14.55

The performance share awards granted in 2015 and 2016 are considered performance condition awards as attainment is based on Dover's performance relative to established internal metrics. The fair value of these awards was determined using Dover's closing stock price on the date of grant. The expected attainment of the internal metrics for these awards is analyzed each reporting period, and the related expense is adjusted based on expected attainment, if that attainment differs from previous estimates. The cumulative effect on current and prior periods of a change in attainment is recognized in compensation cost in the period of change.

The fair value and average attainment used in determining compensation cost for the performance shares issued in 2015 and 2016 is as follows for the six months ended June 30, 2016:

	Performance shares	
	2016	2015
Fair value per share at date of grant	$57.25	$73.28
Average attainment rate reflected in expense	45.14 %	29.81 %

Stock-based compensation is reported within selling and administrative expenses in the accompanying unaudited Condensed Consolidated Statements of Earnings. The following table summarizes the Company’s compensation expense relating to all stock-based incentive plans:

	Three Months Ended June 30,	Six Months Ended June 30,

	2016	2015	2016	2015
Pre-tax compensation expense	$2,973	$5,464	$14,360	$18,851
Tax benefit	(1,030)	(1,917)	(5,080)	(6,681)
Total stock-based compensation expense, net of tax	$1,943	$3,547	$9,280	$12,170

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12. Commitments and Contingent Liabilities

Litigation

A few of the Company's subsidiaries are involved in legal proceedings relating to the cleanup of waste disposal sites identified under federal and state statutes that provide for the allocation of such costs among "potentially responsible parties." In each instance, the extent of the Company's liability appears to be very small in relation to the total projected expenditures and the number of other "potentially responsible parties" involved and is anticipated to be immaterial to the Company. In addition, a few of the Company's subsidiaries are involved in ongoing remedial activities at certain current and former plant sites, in cooperation with regulatory agencies, and appropriate reserves have been established. At June 30, 2016 and December 31, 2015, the Company has reserves totaling $31,806 and $30,595, respectively, for environmental and other matters, including private party claims for exposure to hazardous substances, that are probable and estimable.

The Company and certain of its subsidiaries are also parties to a number of other legal proceedings incidental to their businesses. These proceedings primarily involve claims by private parties alleging injury arising out of use of the Company's products, patent infringement, employment matters, and commercial disputes. Management and legal counsel, at least quarterly, review the probable outcome of such proceedings, the costs and expenses reasonably expected to be incurred and currently accrued to-date, and the availability and extent of insurance coverage. The Company has reserves for legal matters that are probable and estimable and not otherwise covered by insurance, and at June 30, 2016 and December 31, 2015, these reserves are not significant. While it is not possible at this time to predict the outcome of these legal actions, in the opinion of management, based on the aforementioned reviews, the Company is not currently involved in any legal proceedings which, individually or in the aggregate, could have a material effect on its financial position, results of operations, or cash flows.

Warranty Accruals

Estimated warranty program claims are provided for at the time of sale. Amounts provided for are based on historical costs and adjusted for new claims. The changes in the carrying amount of product warranties through June 30, 2016 and 2015 are as follows:

	2016	2015
Beginning Balance, January 1	$44,466	$49,388
Provision for warranties	29,148	24,877
Settlements made	(26,649)	(28,390)
Other adjustments, including acquisitions and currency translation	3,011	(517)
Ending balance, June 30	$49,976	$45,358

13. Employee Benefit Plans

Retirement Plans

The Company offers defined contribution retirement plans which cover the majority of its U.S. employees, as well as employees in certain other countries. In addition, the Company sponsors qualified defined benefit pension plans covering certain employees of the Company and its subsidiaries. The plans' benefits are generally based on years of service and employee compensation. The Company also provides to certain management employees, through non-qualified plans, supplemental retirement benefits in excess of qualified plan limits imposed by federal tax law.

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The following tables set forth the components of the Company's net periodic expense relating to retirement benefit plans:

Qualified Defined Benefits

	Three Months Ended June 30,				Six Months Ended June 30,			
	U.S. Plan		Non-U.S. Plans		U.S. Plan		Non-U.S. Plans	
	2016	2015	2016	2015	2016	2015	2016	2015
Service Cost	$3,479	$3,916	$1,405	$1,663	$6,957	$7,831	$2,778	$3,351
Interest Cost	5,761	5,791	1,394	1,476	11,523	11,582	2,769	2,962
Expected return on plan assets	(9,699)	(10,393)	(1,974)	(2,011)	(19,397)	(20,786)	(3,922)	(4,030)
Amortization:								
Prior service cost	183	224	(100)	22	366	448	(199)	45
Recognized actuarial loss	1,610	3,155	675	661	3,219	6,310	1,340	1,336
Transition obligation	—	—	1	9	—	—	2	