SURMODICS INC
Form 10-K/A
May 10, 2016
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UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, DC 20549

Form 10-K/A

Amendment No. 1

ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d)

OF THE SECURITIES EXCHANGE ACT OF 1934

For the fiscal year ended September 30, 2015

Commission file number 0-23837

SURMODICS, INC.

(Exact Name of Registrant as Specified in Its Charter)

Minnesota (State or other jurisdiction of incorporation or organization)	41-1356149 (IRS Employer Identification No.)
9924 West 74th Street Eden Prairie, Minnesota (Address of Principal Executive Offices)	55344 (Zip Code)

(Registrant’s Telephone Number, Including Area Code)

(952) 500-7000

Securities registered pursuant to Section 12(b) of the Act:

Title of Each Class	Name of Exchange on Which Registered
Common Stock, $0.05 par value	NASDAQ Global Select Market

Securities registered pursuant to Section 12(g) of the Act:

None

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. Yes o No x

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act. Yes o No x

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 x 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 x No o

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K. x

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. (Check one):

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

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

The aggregate market value of the Common Stock held by shareholders other than officers, directors or holders of more than 5% of the outstanding stock of the registrant as of March 31, 2015 was approximately $245 million (based upon the closing sale price of the registrant's Common Stock on such date).

The number of shares of the registrant's Common Stock outstanding as of December 1, 2015 was 12,944,326.

DOCUMENTS INCORPORATED BY REFERENCE

Portions of the Registrant's Proxy Statement for the Registrant's 2016 Annual Meeting of Shareholders are incorporated by reference into Part III.

Explanatory Note

SurModics, Inc. (the "Company," "we," "us," or "our") is filing this Amendment No. 1 on Form 10-K/A (this "Amendment") t its annual report on Form 10-K for the fiscal year ended September 30, 2015, which was originally filed on December 4, 2015 (the "Original Filing"), to amend and revise Item 9A of Part II, "Controls and Procedures," with respect to (1) our conclusions regarding the effectiveness of our disclosure controls and procedures and our internal control over financial reporting and (2) Deloitte & Touche LLP's ("Deloitte") related attestation report due to a material weakness in our internal control over financial reporting identified subsequent to the issuance of our Original Filing. Item 15 of Part IV, "Exhibits and Financial Statement Schedules", has also been amended to revise the reference to Deloitte's opinion on our Internal Control Over Financial Reporting in its Report of Independent Registered Public Accounting Firm on our consolidated financial statements and financial statement schedule as of and for the three years in the period ended September 30, 2015.

As required by Rule 12b-15 under the Securities Exchange Act of 1934, as amended (the "Exchange Act"), new certifications of our principal executive officer and principal financial officer are also being filed as exhibits to this Amendment. This Amendment should be read in conjunction with the Original Filing, which continues to speak as of the date of the Original Filing. Except as specifically noted above, this Amendment does not modify or update disclosures in the Original Filing. Accordingly, this Amendment does not reflect events occurring after the filing of the Original Filing or modify or update any related or other disclosures.

ITEM 9. CHANGES IN AND DISAGREEMENTS WITH ACCOUNTANTS ON ACCOUNTING AND FINANCIAL DISCLOSURE.

None.

ITEM 9A. CONTROLS AND PROCEDURES.

1. Disclosure Controls and Procedures.

We maintain disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) under the Exchange Act that are designed to ensure that information required to be disclosed in our reports filed under the Exchange Act, is recorded, processed, summarized and reported within the time periods specified in the SEC's rules and forms, and that such information is accumulated and communicated to our management, including our Chief Executive Officer and Chief Financial Officer, as appropriate, to allow timely decisions regarding required disclosure. In designing and evaluating the disclosure controls and procedures, management recognized that any controls and procedures, no matter how well designed and operated, can provide only reasonable assurance of achieving the desired control objectives, and management necessarily was required to apply its judgment in evaluating the cost-benefit relationship of possible controls and procedures. Our disclosure controls and procedures are designed to provide a reasonable level of assurance of reaching our desired disclosure control objectives.

We carried out an evaluation under the supervision and with the participation of management, including our Chief Executive Officer and Chief Financial Officer, of the effectiveness of the design and operation of our disclosure controls and procedures as of September 30, 2015, the end of the period covered by this report. Previously, based on that evaluation, our Chief Executive Officer and Chief Financial Officer concluded that our disclosure controls and procedures were effective as of September 30, 2015. However, due to the material weakness in internal control over financial reporting described below, our Chief Executive Officer and Chief Financial Officer have concluded that our disclosure controls and procedures were not effective as of September 30, 2015.

2. Internal Control over Financial Reporting.

(a) Management's Annual Report on Internal Control Over Financial Reporting (Revised)

The Company's management is responsible for establishing and maintaining adequate internal control over financial reporting for the Company, as such term is defined in Exchange Act Rule 13a-15(f). In connection with the Original Filing, management conducted an evaluation of the design and operating effectiveness of our internal control over financial reporting based on the criteria established in Internal Control — Integrated Framework (2013) issued by the Committee of Sponsoring Organizations of the Treadway Commission ("COSO"). Based on its evaluation, management concluded internal control over financial reporting was effective as of September 30, 2015.

In April 2016, the Company became aware of royalty overpayments made by customers pursuant to license agreements for products incorporating certain of the Company's technologies no longer covered by an unexpired patent. The Company did not identify that certain amounts reported by the customers were not in accordance with the terms of the license agreement and should have been deferred or refunded to the customers, resulting in an overstatement of revenue. As a result of the identification of the overstatement of royalty revenue, management reevaluated the design and operating effectiveness of internal control over financial reporting and concluded that its internal control over financial reporting as of September 30, 2015 was not effective due to a material weakness in the design and operating effectiveness of its transactional and review controls related to recognition of royalty revenue. A material weakness is a deficiency, or combination of deficiencies, in internal control over financial reporting such that

there is reasonable possibility that a material misstatement of the Company's annual or interim financial statements will not be prevented or detected on a timely basis. Because the deficiencies related to the Company's controls over recognition of royalty revenue could result in a misstatement of royalty revenue and related accounts and disclosures that could be material to the annual or interim consolidated financial statements, such deficiencies represent a material weakness in our internal control over financial reporting. Accordingly, management has revised its report on internal control over financial reporting.

Management analyzed the impact of the overstatement of royalty revenue resulting from the identified material weakness and concluded that it did not have a material impact on our previously issued consolidated financial statements. Notwithstanding the material weakness in our internal control over financial reporting, we have concluded that the consolidated financial statements and other financial information included in the Original Filing, fairly present in all material respects our financial condition, results of operations and cash flows as of, and for, the periods presented.

The foregoing has been approved by our management, including our Chief Executive Officer and Chief Financial Officer, who have been involved with the reassessment and analysis of our internal control over financial reporting.

Deloitte & Touche LLP, the independent registered public accounting firm that audited the consolidated financial statements included in this Form 10-K/A, has issued the attestation report below regarding the Company's internal control over financial reporting.

(b) Attestation Report of the Independent Registered Public Accounting Firm.

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

To the Board of Directors and Stockholders of

SurModics, Inc.

Eden Prairie, Minnesota

We have audited the internal control over financial reporting of SurModics, Inc. and subsidiaries (the "Company") as of September 30, 2015, based on criteria established in Internal Control — Integrated Framework (2013) issued by the Committee of Sponsoring Organizations of the Treadway Commission. The Company's management is responsible for maintaining effective internal control over financial reporting and for its assessment of the effectiveness of internal control over financial reporting, included in the accompanying Management’s Annual Report on Internal Control Over Financial Reporting (Revised). Our responsibility is to express an opinion on the Company's internal control over financial reporting based on our audit.

We conducted our audit in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether effective internal control over financial reporting was maintained in all material respects. Our audit included obtaining an understanding of internal control over financial reporting, assessing the risk that a material weakness exists, testing and evaluating the design and operating effectiveness of internal control based on the assessed risk, and performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion.

A company's internal control over financial reporting is a process designed by, or under the supervision of, the company's principal executive and principal financial officers, or persons performing similar functions, and effected by the company's board of directors, management, and other personnel to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. A company's internal control over financial reporting includes those policies and procedures that (1) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; (2) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and (3) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the company's assets that could have a material effect on the financial statements.

Because of the inherent limitations of internal control over financial reporting, including the possibility of collusion or improper management override of controls, material misstatements due to error or fraud may not be prevented or detected on a timely basis. Also, projections of any evaluation of the effectiveness of the internal control over financial reporting to future periods are subject to the risk that the controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

In our report dated December 4, 2015, we expressed an unqualified opinion on the effectiveness of the Company’s internal control over financial reporting. As described in the following paragraph, a material weakness was subsequently identified as a result of deficiency in the design and operation of the Company’s controls related to recognition of royalty revenue. Accordingly, management has revised its assessment about the effectiveness of the Company’s internal control over financial reporting and our present opinion on the effectiveness of the Company’s internal control over financial reporting as of September 30, 2015, as expressed herein, is different from that expressed

in our previous report.

A material weakness is a deficiency, or a combination of deficiencies, in internal control over financial reporting, such that there is a reasonable possibility that a material misstatement of the company’s annual or interim financial statements will not be prevented or detected on a timely basis. The following material weakness has been identified and included in management's assessment: a material weakness in the design and operating effectiveness of its transactional and review controls related to recognition of royalty revenue. This material weakness was considered in determining the nature, timing, and extent of audit tests applied in our audit of the consolidated financial statements as of and for the year ended September 30, 2015, of the Company and this report does not affect our report on such financial statements and financial statement schedule.

In our opinion, because of the effect of the material weakness identified above on the achievement of the objectives of the control criteria, the Company has not maintained effective internal control over financial reporting as of September 30, 2015, based on the criteria established in Internal Control — Integrated Framework (2013) issued by the Committee of Sponsoring Organizations of the Treadway Commission.

We have also audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the consolidated financial statements and financial statement schedule as of and for the year ended September 30, 2015 of the Company and our report dated December 4, 2015 expressed an unqualified opinion on those consolidated financial statements and financial statement schedule.

/s/ DELOITTE & TOUCHE LLP

Minneapolis, Minnesota

December 4, 2015 (May 10, 2016 as to the effects of the material weakness described in Management's Annual Report on Internal Control Over Financial Reporting (Revised))

c. Changes in Internal Controls Over Financial Reporting.

There were no changes in our internal control over financial reporting during the quarter ended September 30, 2015 that have materially affected, or are reasonable likely to materially affect, our internal control over financial reporting.

Plan for Remediation of Material Weakness

With oversight from the Audit Committee, the Company's management is in the process of developing and implementing remediation plans to address the material weakness described above.

PART IV

ITEM 15. EXHIBITS AND FINANCIAL STATEMENT SCHEDULES.

(a) The documents filed as part of this report on the pages indicated:

1. Financial Statements

The following statements are included in this report on the pages indicated:

2. Financial Statement Schedule. See Schedule II — "Valuation and Qualifying Accounts" in this section of this Form 10-K. All other schedules are omitted because they are inapplicable, not required, or the information is in the consolidated financial statements or related notes.

3. Listing of Exhibits. The following exhibits which are filed with this report:

23 Consent of Deloitte & Touche LLP.**

24 Power of Attorney (included on signature page of this Form 10-K).**

31.1 Certification of Chief Executive Officer Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.**

31.2 Certification of Chief Financial Officer Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.**

32.1 Certification of Chief Executive Officer Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.**

32.2 Certification of Chief Financial Officer Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.**

SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, the Registrant has duly caused this Report to be signed on its behalf by the undersigned, thereunto duly authorized.

SURMODICS, INC.

By: /s/ Andrew D. C. LaFrence
Andrew D. C. LaFrence
Vice President of Finance and
Chief Financial Officer

Dated: May 10, 2016

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

EXHIBIT INDEX TO FORM 10-K

For the Fiscal Year Ended September 30, 2015

SURMODICS, INC.

Exhibit

23*	Consent of Deloitte & Touche LLP.
24*	Power of Attorney (included on signature page of this Form 10-K).
31.1*	Certification of Chief Executive Officer Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
31.2*	Certification of Chief Financial Officer Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
32.1*	Certification of Chief Executive Officer Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
32.2*	Certification of Chief Financial Officer Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.

*Filed herewith

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

To the Board of Directors and Stockholders of

SurModics, Inc.

Eden Prairie, Minnesota

We have audited the accompanying consolidated balance sheets of SurModics, Inc. and subsidiaries (the "Company") as of September 30, 2015 and 2014, and the related consolidated statements of income, comprehensive income, stockholders' equity, and cash flows for each of the three years in the period ended September 30, 2015. Our audits also included the financial statement schedule listed in the Index at Item 15. These consolidated financial statements and financial statement schedule are the responsibility of the Company's management. Our responsibility is to express an opinion on the consolidated financial statements and financial statement schedule based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, such consolidated financial statements present fairly, in all material respects, the financial position of SurModics, Inc. and subsidiaries as of September 30, 2015 and 2014, and the results of their operations and their cash flows for each of the three years in the period ended September 30, 2015, in conformity with accounting principles generally accepted in the United States of America. Also, in our opinion, such financial statement schedule, when considered in relation to the basic consolidated financial statements taken as a whole, presents fairly, in all material respects, the information set forth therein.

We have also audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the Company's internal control over financial reporting as of September 30, 2015, based on the criteria established in Internal Control — Integrated Framework (2013) issued by the Committee of Sponsoring Organizations of the Treadway Commission and our report dated December 4, 2015, May 10, 2016 as to the effects of the material weakness described in Management’s Annual Report on Internal Control Over Financial Reporting (Revised), which expressed an adverse opinion on the Company's internal control over financial reporting because of a material weakness.

/s/ DELOITTE & TOUCHE LLP

Minneapolis, Minnesota

December 4, 2015

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SurModics, Inc. and Subsidiaries

Consolidated Balance Sheets

As of September 30

	2015	2014
	(In thousands, except share and per share data)	
ASSETS		
Current Assets:		
Cash and cash equivalents	$55,588	$43,511
Available-for-sale securities	—	3,040
Accounts receivable, net of allowance for doubtful accounts of $10 and $42 as of September 30, 2015 and 2014, respectively	7,478	4,751
Inventories	2,979	2,817
Deferred tax assets	546	394
Prepaids and other	1,198	751
Current assets of discontinued operations	—	16
Total Current Assets	67,789	55,280
Property and equipment, net	12,968	13,133
Available-for-sale securities	—	16,823
Deferred tax assets	6,704	6,718
Intangible assets, net	2,760	2,946
Goodwill	8,010	8,010
Other assets, net	479	1,979
Total Assets	$98,710	$104,889
LIABILITIES AND STOCKHOLDERS' EQUITY		
Current Liabilities:		
Accounts payable	$781	$1,028
Accrued liabilities:		
Compensation	2,772	2,061
Accrued other	1,099	881
Deferred revenue	48	52
Current liabilities of discontinued operations	—	45
Total Current Liabilities	4,700	4,067
Deferred revenue, less current portion	217	226
Other long-term liabilities	1,920	1,845
Total Liabilities	6,837	6,138
Commitments and Contingencies (Note 12)		
Stockholders' Equity:		
Series A preferred stock — $.05 par value, 450,000 shares authorized; no shares issued and outstanding	—	—

Common stock — $.05 par value, 45,000,000 shares authorized; 12,945,157 and 13,606,545 shares issued and outstanding, respectively	647	680
Additional paid-in capital	3,060	2,662
Accumulated other comprehensive income	5	1,528
Retained earnings	88,161	93,881
Total Stockholders' Equity	91,873	98,751
Total Liabilities and Stockholders' Equity	$98,710	$104,889

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

SurModics, Inc. and Subsidiaries

Consolidated Statements of Income

For the Years Ended September 30

	2015	2014	2013
	(In thousands, except per share data)		
Revenue:			
Royalties and license fees	$31,763	$30,277	$29,774
Product sales	24,925	22,798	22,506
Research and development	5,210	4,364	3,852
Total revenue	61,898	57,439	56,132
Operating costs and expenses:			
Product costs	8,619	8,016	7,898
Research and development	16,165	15,550	15,079
Selling, general and administrative	15,525	15,297	13,859
Restructuring charges	—	—	476
Claim settlement	2,500	—	—
Total operating costs and expenses	42,809	38,863	37,312
Operating income from continuing operations	19,089	18,576	18,820
Other income (loss):			
Investment income, net	156	238	268
Impairment losses on strategic investments	(1,500)	(1,184)	(158)
Gains on sale of strategic investments	—	709	1,293
Other income, net	496	133	137
Other (loss) income	(848)	(104)	1,540
Income from continuing operations before income taxes	18,241	18,472	20,360
Income tax provision	(6,294)	(6,265)	(5,781)
Income from continuing operations	11,947	12,207	14,579
Discontinued operations:			
(Loss) income from discontinued operations, net of income taxes	—	(176)	588
Loss on sale of discontinued operations, net of income taxes	—	—	—
(Loss) Income from discontinued operations	—	(176)	588
Net income	$11,947	$12,031	$15,167
Basic income (loss) per share:			
Continuing operations	$0.92	$0.90	$1.01
Discontinued operations	(0.00)	(0.01)	0.04
Net income	$0.92	$0.88	$1.05
Diluted income (loss) per share:			
Continuing operations	$0.90	$0.88	$0.99
Discontinued operations	(0.00)	(0.01)	0.04
Net income	$0.90	$0.87	$1.03
Weighted average number of shares outstanding:			
Basic	13,029	13,632	14,464

Diluted	13,289	13,876	14,731

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

SurModics, Inc. and Subsidiaries

Consolidated Statements of Comprehensive Income

For the Years Ended September 30

	2015	2014	2013
	(In thousands)		
Net income	$11,947	$12,031	$15,167
Other comprehensive (loss) income, net of tax:			
Unrealized holding (losses) gains on available-for-sale securities arising during the period	(1,208)	1,559	235
Reclassification adjustment for realized gains included in net income	(315)	(89)	(217)
Other comprehensive (loss) income	(1,523)	1,470	18
Comprehensive income	$10,424	$13,501	$15,185

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

SurModics, Inc. and Subsidiaries

Consolidated Statements of Stockholders' Equity

For the Years Ended September 30

	Common Stock Shares	Amount	Additional Paid-In Capital	Accumulated Other Comprehensive Income	Retained Earnings	Total Stockholders' Equity
	(In thousands)					
Balance at September 30, 2012	14,657	$ 733	$ 18,346	$ 40	$ 75,869	$ 94,988
Net income	—	—	—	—	15,167	15,167
Other comprehensive income, net of tax	—	—	—	18	—	18
Issuance of common stock	20	1	274	—	—	275
Common stock repurchased	(796)	(40)	(18,769)	—	—	(18,809)
Common stock options exercised, net	10	1	143	—	—	144
Purchase of common stock to pay employee taxes	—	—	(41)	—	—	(41)
Reduction of excess tax benefit from stock-based compensation plans	—	—	(477)	—	—	(477)
Stock-based compensation	—	—	2,552	—	—	2,552
Balance at September 30, 2013	13,891	695	2,028	58	91,036	93,817
Net income	—	—	—	—	12,031	12,031
Other comprehensive income, net of tax	—	—	—	1,470	—	1,470
Issuance of common stock	163	8	261	—	—	269
Common stock repurchased	(485)	(25)	(2,330)	—	(9,186)	(11,541)
Common stock options exercised, net	38	2	241	—	—	243
Purchase of common stock to pay employee taxes	—	—	(1,111)	—	—	(1,111)
Excess tax benefit from stock-based compensation plans	—	—	236	—	—	236
Stock-based compensation	—	—	3,337	—	—	3,337
Balance at September 30, 2014	13,607	680	2,662	1,528	93,881	98,751
Net income	—	—	—	—	11,947	11,947
Other comprehensive loss, net of tax	—	—	—	(1,523)	—	(1,523)
Issuance of common stock	139	7	272	—	—	279
Common stock repurchased	(848)	(42)	(2,485)	—	(17,473)	(20,000)
Common stock options exercised, net	47	2	429	—	—	431

Purchase of common stock to pay employee taxes	—	—	(631)	—	(194)	(825)
Excess tax benefit from stock-based compensation plans	—	—	432	—	—	432
Stock-based compensation	—	—	2,381	—	—	2,381
Balance at September 30, 2015	12,945	$ 647	$ 3,060	$ 5	$ 88,161	$ 91,873

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

SurModics, Inc. and Subsidiaries

Consolidated Statements of Cash Flows

For the Years Ended September 30

	2015	2014	2013
	(In thousands)		
Operating Activities:			
Net income	$11,947	$12,031	$15,167
Adjustments to reconcile net income to net cash provided by operating activities from continuing operations:			
Loss (income) from discontinued operations	—	176	(588)
Depreciation and amortization	2,805	2,715	2,886
Gains on sales of available-for-sale securities, net and strategic investments	(492)	(842)	(1,430)
Impairment losses on strategic investments	1,500	1,184	158
Stock-based compensation	2,381	3,337	2,552
Deferred taxes	93	(352)	(492)
Excess tax (benefit) deficiency from stock-based compensation plans	(432)	(236)	477
(Gain) loss on disposals of property and equipment	(39)	2	(62)
Change in operating assets and liabilities, excluding the impact of discontinued operations:			
Accounts receivable	(2,727)	581	(263)
Inventories	(162)	511	196
Prepaids and other	141	(23)	(40)
Accounts payable and accrued liabilities	373	(738)	238
Income taxes	(309)	116	(989)
Deferred revenue	(13)	75	(29)
Net cash provided by operating activities from continuing operations	15,066	18,537	17,781
Investing Activities:			
Purchases of property and equipment	(1,877)	(2,278)	(1,919)
Cash proceeds from sale of property and equipment	42	—	77
Purchases of available-for-sale securities	(3,376)	(138,363)	(45,053)
Sales and maturities of available-for-sale securities	22,199	162,673	44,853
Business combination	(270)	—	—
Cash received from sale of strategic investments	21	709	2,236
Cash transferred to discontinued operations	(45)	(354)	(116)
Net cash provided by investing activities from continuing operations	16,694	22,387	78
Financing Activities:			
Excess tax benefit (deficiency) from stock-based compensation plans	432	236	(477)
Issuance of common stock	710	512	419
Repurchase of common stock	(20,000)	(12,545)	(17,805)
Purchases of common stock to pay employee taxes	(825)	(1,111)	(41)
Net cash used in financing activities from continuing operations	(19,683)	(12,908)	(17,904)
Net cash provided by (used in) continuing operations	12,077	28,016	(45)
Discontinued Operations:			

Net cash used in operating activities	(45)	(354)	(116)
Net cash provided by investing activities	—	—	—
Net cash provided by financing activities	45	354	116
Net cash provided by discontinued operations	—	—	—
Net change in cash and cash equivalents	12,077	28,016	(45)
Cash and Cash Equivalents:			
Beginning of year	43,511	15,495	15,540
End of year	$55,588	$43,511	$15,495
Supplemental Information:			
Cash paid for income taxes	$6,510	$6,295	$7,115
Noncash financing and investing activities:			
Acquisition of property and equipment on account	$22	$11	$26
Share repurchase accrual	$—	$—	$1,004
Issuance of performance shares, restricted and deferred stock units	$2,250	$3,007	$—
Accrual of business combination contingent consideration	$305	$—	$—

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

SurModics, Inc. and Subsidiaries

Notes to Consolidated Financial Statements

1. Description

SurModics, Inc. and subsidiaries ("SurModics" or "the Company") is a leading provider of medical device and in vitro diagnostic technologies to the healthcare industry. The Company derives its revenue from three primary sources: (1) royalties and license fees from licensing its proprietary drug delivery and surface modification technologies and in vitro diagnostic formats to customers; (2) the sale of reagent chemicals to licensees and the sale of stabilization products, antigens, substrates and surface coatings to the diagnostic and biomedical research markets; and (3) research and development fees generated on customer projects.

Effective with the acquisition of Creagh Medical Ltd. ("Creagh") on November 20, 2015, and subsequent to the fiscal year end 2015, the Company will be engaged in contract research and development, as well as manufacturing of balloon catheters used in a variety of interventional cardiology applications.

Basis of Presentation

The consolidated financial statements include all accounts and wholly-owned subsidiaries, and have been prepared in accordance with accounting principles generally accepted in the United States of America ("U.S.") ("GAAP"). All inter-company transactions have been eliminated.

2. Summary of Significant Accounting Policies and Select Balance Sheet Information

Cash and Cash Equivalents

Cash and cash equivalents consist of financial instruments with original maturities of three months or less and are stated at cost which approximates fair value and may include money market instruments, certificates of deposit, repurchase agreements and commercial paper instruments.

Investments

Investments consist principally of U.S. government and government agency obligations, mortgage-backed securities and corporate and municipal debt securities and were classified as available-for-sale at September 30, 2014. Available-for-sale securities are reported at fair value with unrealized gains and losses, net of tax, excluded from the consolidated statements of income and reported in the consolidated statements of comprehensive income as well as a separate component of stockholders' equity in the consolidated balance sheets, except for other-than-temporary impairments, which are reported as a charge to current earnings. A loss would be recognized when there is an other-than-temporary impairment in the fair value of any individual security classified as available-for-sale, with the associated net unrealized loss reclassified out of accumulated other comprehensive income with a corresponding adjustment to other income (loss). This adjustment results in a new cost basis for the investment. Investments for which management has the intent and ability to hold to maturity are classified as held-to-maturity and reported at amortized cost. When an other-than-temporary impairment in the fair value of any individual security classified as held-to-maturity occurs, the Company writes down the security to fair value with a corresponding adjustment to other

income (loss). Interest earned on debt securities, including amortization of premiums and accretion of discounts, is included in other income (loss). Realized gains and losses from the sales of debt securities, which are included in other income (loss), are determined using the specific identification method.

During the quarter ended June 30, 2015, the Company liquidated its investment portfolio to support corporate initiatives, as a result the ending balance of available-for-sale investments as of September 30, 2015 was zero. The amortized cost, unrealized holding gains and losses, and fair value of available-for-sale securities as of September 30, 2014 were as follows (in thousands):

	Amortized Cost	Unrealized Gains	Unrealized Losses	Fair Value
U.S. government and government agency obligations	$ 7,397	$ 12	$ (15)	$7,394
Mortgage-backed securities	5,576	43	(74)	5,545
Municipal bonds	1,173	5	(3)	1,175
Asset-backed securities	2,370	3	(4)	2,369
Corporate bonds	1,829	6	(5)	1,830
Equity securities	2	1,548	—	1,550
Total	$ 18,347	$ 1,617	$ (101)	$19,863

As of September 30, 2014, the Company concluded that the unrealized losses related to the available-for-sale securities shown above were not other-than-temporary as the Company did not have the intent to sell, nor was is it more likely than not that the Company would be required to sell such securities, before recovery of their amortized cost.

The following table summarizes sales of available-for-sale securities for the years ended September 30, 2015, 2014 and 2013 (in thousands):

	2015	2014	2013
Proceeds from sales	$22,199	$162,673	$44,853
Gross realized gains	$548	$134	$179
Gross realized losses	$(73)	$(1)	$(43)

There were no held-to-maturity debt securities at September 30, 2015 or 2014.

Inventories

Inventories are principally stated at the lower of cost or market using the specific identification method and include direct labor, materials and overhead. Inventories consisted of the following components as of September 30 (in thousands):

	2015	2014
Raw materials	$1,264	$1,056
Finished products	1,715	1,761
Total	$2,979	$2,817

Property and Equipment

Property and equipment are stated at cost, less any impairment, and are depreciated using the straight-line method over the estimated useful lives of the assets. The Company recorded depreciation expense of $2.0 million, $2.0 million and $2.1 million for the years ended September 30, 2015, 2014 and 2013, respectively.

The September 30, 2015 and 2014 balances in construction-in-progress include the cost of enhancing the capabilities of the Company’s Eden Prairie, Minnesota facility. As assets are placed in service, construction-in-progress is transferred to the specific property and equipment categories and depreciated over the estimated useful lives of the assets.

Property and equipment consisted of the following components as of September 30 (in thousands):

	Useful Life (In years)	2015	2014
Land	N/A	$4,359	$4,359
Laboratory fixtures and equipment	3 to 10	12,941	12,858
Buildings and improvements	3 to 20	16,444	16,114
Office furniture and equipment	3 to 10	3,473	3,060
Construction-in-progress		1,168	1,158
Less accumulated depreciation		(25,417)	(24,416)
Property and equipment, net		$12,968	$13,133

Other Assets

Other assets consisted principally of strategic investments as of September 30 as follows (in thousands):

	2015	2014
CeloNova BioSciences, Inc.	$—	$1,500
ViaCyte, Inc.	479	479
Other assets, net	$479	$1,979

In February 2011, the stent technology of Nexeon MedSystems, Inc. (“Nexeon”) was acquired by CeloNova BioSciences, Inc. (“CeloNova”). Prior to the acquisition by CeloNova, Nexeon created a wholly-owned subsidiary, Nexeon Stent, to hold the company’s stent-related assets. Nexeon distributed to its stockholders the Nexeon Stent stock which was exchanged for Series B-1 preferred shares of CeloNova. CeloNova is a privately-held Texas-based medical technology company that is marketing a variety of medical products. The Company’s investment in CeloNova, which is accounted for under the cost method, represents less than a 2% ownership interest. The Company does not exert significant influence over CeloNova’s operating or financial activities.

On November 10, 2015 Boston Scientific Corporation announced its intent to acquire CeloNova’s interventional radiology portfolio for $70 million plus potential milestone payments. This acquisition is expected to close by December 31, 2015. The Company recognized an other-than-temporary impairment loss of $1.5 million related to its investment in CeloNova in the fourth quarter fiscal 2015 based on the indicated value of this transaction.

The Company has invested a total of $1.2 million in ThermopeutiX, Inc. (“ThermopeutiX”), a California-based early stage company developing novel medical devices for the treatment of vascular and neurovascular diseases. In addition to the investment, SurModics has licensed its hydrophilic and hemocompatible coating technologies to ThermopeutiX for use with its devices. The Company’s investment in ThermopeutiX, which is accounted for under the cost method, represents an ownership interest of less than 20%. The Company does not exert significant influence over ThermopeutiX’s operating or financial activities. In the fourth quarter of fiscal 2014, the Company recognized an other-than-temporary impairment loss of $1.2 million based on capital funding initiatives and current operating conditions of ThermopeutiX.

The Company has invested a total of $5.3 million in ViaCyte, Inc. (“ViaCyte”), a privately-held California-based biotechnology firm that is developing a unique treatment for diabetes using coated islet cells, the cells that produce insulin in the human body. In fiscal 2006, the Company determined that its investment in ViaCyte was impaired and that the impairment was other-than-temporary. Accordingly, the Company recorded an impairment loss of $4.7 million. In the second quarter of fiscal 2013, the Company recorded an additional other-than-temporary impairment loss on this investment totaling $0.1 million based on a financing round and market valuations. The balance of the investment of $0.5 million, which is accounted for under the cost method, represents less than a 1% ownership interest. The Company does not exert significant influence over ViaCyte’s operating or financial activities.

The Company had invested a total of $2.5 million in Vessix Vascular, Inc. (“Vessix”) and recognized an other-than-temporary impairment loss on this investment totaling $2.4 million in fiscal 2010, based on market valuations and a pending financing round for Vessix. Vessix was purchased by Boston Scientific Corporation in November 2012. The Company recorded a gain of approximately $1.2 million in the consolidated statements of income gains on sale of strategic investments line, on the sale of this investment in the first quarter of fiscal 2013. In fiscal 2014, the Company recorded a $0.7 million gain upon achievement by Vessix of a clinical milestone and a sales milestone for calendar 2013. Total potential maximum additional proceeds of $3.3 million may be received in fiscal 2016 through fiscal 2017 depending on Vessix’s achievement of future sales milestones. No amounts have been recorded associated with these future milestones given the level of uncertainty that exists. Any potential additional income will be recognized once the milestones are achieved.

The Company transferred its original investment of $2,000 in Intersect ENT, Inc. (“Intersect ENT”) out of other assets to short-term available-for-sale investments upon completion of Intersect ENT’s initial public offering (“IPO”) in July 2014. The Company recognized a gain on this investment in other income of $0.5 million during the year ended

September 30, 2015 as the investment was sold.

The Company has invested a total of $6.5 million in Nexeon, a privately-held West Virginia-based medical technology company, commencing in July 2007 and has recognized losses under the equity method of accounting as well as other-than-temporary impairment losses of $4.1 million in fiscal 2010 and less than $0.1 million in fiscal 2013. In the fourth quarter of fiscal 2013, the Company recognized an other-than-temporary impairment loss based on Nexeon's capital funding initiatives of approximately $1.0 million. The carrying value of this investment was zero as of September 30, 2015 and 2014.

The total carrying value of cost method investments is reviewed quarterly for changes in circumstances or the occurrence of events that suggest the Company's investment may not be recoverable. The fair value of cost method investments is not adjusted if there are no identified events or changes in circumstances that may have a material adverse effect on the fair value of the investment.

In the fiscal years ended September 30, 2015 and 2014, the Company recognized revenue of less than $0.1 million in each period and in the fiscal year ended September 30, 2013 the Company recognized revenue of $0.1 million from activity with companies in which it had a strategic investment.

Intangible Assets

Intangible assets consist principally of acquired patents and technology, customer relationships, licenses and trademarks. The Company recorded amortization expense of $0.8 million, $0.7 million and $0.7 million for the years ended September 30, 2015, 2014 and 2013, respectively. During the year ended September 30, 2015, the Company acquired certain assets from ImmunO4, LLC resulting in an increase in customer lists, non-compete and other intangible assets of $0.3 million, $0.2 million and $0.1 million, respectively.

Intangible assets consisted of the following as of September 30 (in thousands):

	2015			
	Weighted Average Original Life (Years)	Gross Carrying Amount	Accumulated Amortization	Net
Definite-lived intangible assets:				
Customer lists	9.0	$ 5,132	$ (4,363)	$ 769
Core technology	8.0	530	(530)	0
Non-compete	5.0	230	(12)	218
Patents and other	16.8	2,321	(1,128)	1,193
Subtotal		8,213	(6,033)	2,180
Unamortized intangible assets:				
Trademarks		580	—	580
Total		$ 8,793	$ (6,033)	$ 2,760

	2014			
	Weighted Average Original Life (Years)	Gross Carrying Amount	Accumulated Amortization	Net
Definite-lived intangible assets:				
Customer lists	9.0	$ 4,857	$ (3,813)	$ 1,044
Core technology	8.0	530	(475)	55
Patents and other	16.8	2,256	(989)	1,267
Subtotal		7,643	(5,277)	2,366
Unamortized intangible assets:				
Trademarks		580	—	580
Total		$ 8,223	$ (5,277)	$ 2,946

Based on the intangible assets in service as of September 30, 2015, estimated amortization expense for each of the next five fiscal years is as follows (in thousands):

2016	$690
2017	279

2018	233
2019	233
2020	221

Future amortization amounts presented above are estimates. Actual future amortization expense may be different, as a result of future acquisitions, impairments, changes in amortization periods, or other factors.

Goodwill

Goodwill represents the excess of the cost of an acquired entity over the fair value assigned to the assets purchased and liabilities assumed in connection with a company's acquisition. Goodwill is not amortized but is subject, at a minimum, to annual tests for impairment in accordance with accounting guidance for goodwill. The carrying amount of goodwill is evaluated annually, and between annual evaluations if events occur or circumstances change indicating that it is more likely than not that the fair value of a reporting unit is less than its carrying amount.

Goodwill is evaluated for impairment based on an assessment of qualitative factors to determine whether the existence of events or circumstances leads to a determination that it is more likely than not that the fair value of a reporting unit is less than its carrying

amount (Step 0). If, after assessing the totality of events or circumstances, an entity determines it is not more likely than not that the fair value of a reporting unit is less than its carrying amount, then performing the two-step impairment test becomes unnecessary.

The two-step impairment test requires SurModics to compare the fair value of the reporting units to which goodwill was assigned to their respective carrying values (Step 1 of the impairment test). In calculating fair value, the Company would use the income approach as its primary indicator of fair value, with the market approach used as a test of reasonableness. The income approach is a valuation technique under which the Company estimates future cash flows using the reporting units' financial forecasts. Future estimated cash flows would be discounted to their present value to calculate fair value. The market approach establishes fair value by comparing SurModics to other publicly traded guideline companies or by analysis of actual transactions of similar businesses or assets sold. The income approach would be tailored to the circumstances of the Company's business, and the market approach would be completed as a secondary test to ensure that the results of the income approach are reasonable and in line with comparable companies in the industry. The summation of the Company's reporting units' fair values would be compared and reconciled to its market capitalization as of the date of its impairment test.

In the situation where a reporting unit's carrying amount exceeds its fair value, the amount of the impairment loss must be measured. The measurement of the impairment (Step 2 of the impairment test) is calculated by determining the implied fair value of a reporting unit's goodwill. In calculating the implied fair value of goodwill, the fair value of the reporting unit is allocated to all other assets and liabilities of that unit based on their fair values. The excess of the fair value of a reporting unit over the amount assigned to its other assets and liabilities is the implied fair value of goodwill. The goodwill impairment is measured as the excess of the carrying amount of goodwill over its implied fair value.

The Company's reporting units are the In Vitro Diagnostics operations known as its In Vitro Diagnostics unit which contains its BioFX branded products and the SurModics device drug delivery and hydrophilic coatings operations known as the Medical Device unit. Inherent in the determination of fair value of the reporting units are certain estimates and judgments, including the interpretation of current economic indicators and market valuations as well as the Company's strategic plans with regard to its operations.

The $8.0 million of goodwill at September 30, 2015 and 2014 is related to the In Vitro Diagnostics reporting unit and represents the gross value from the acquisition of BioFX Laboratories, Inc. in 2007. The Company performed its annual impairment test of goodwill (Step 0) as of August 31, 2015, and did not record any goodwill impairment charges during fiscal 2015 as there were no indicators of impairment associated with the In Vitro Diagnostics reporting unit. The Company also did not record any goodwill impairment charges related to the In Vitro Diagnostics reporting unit during fiscal 2014 or 2013.

Valuation of Long-Lived Assets

Accounting guidance requires the Company to evaluate periodically whether events and circumstances have occurred that may affect the estimated useful life or the recoverability of the remaining balance of long-lived assets, such as property and equipment and intangibles with finite lives. If such events or circumstances were to indicate that the carrying amount of these assets may not be recoverable, the Company would estimate the future cash flows expected to result from the use of the assets and their eventual disposition. If the sum of the expected future cash flows (undiscounted and without interest charges) were less than the carrying amount of the assets, the Company would recognize an impairment charge to reduce such assets to their fair value.

Revenue Recognition

The Company recognizes revenue when all of the following criteria are met: (1) persuasive evidence of an arrangement exists; (2) shipment has occurred or delivery has occurred if the terms specify destination; (3) the sales price is fixed or determinable; and (4) collectability is reasonably assured. When there are additional performance requirements, revenue is recognized when all such requirements have been satisfied. Under revenue arrangements with multiple deliverables, the Company recognizes each separable deliverable as it is earned.

The Company derives its revenue from three primary sources: (1) royalties and license fees from licensing its proprietary drug delivery and surface modification technologies and in vitro diagnostic formats to customers; (2) the sale of reagent chemicals to licensees and the sale of stabilization products, antigens, substrates and surface coatings to the diagnostic and biomedical research markets; and (3) research and commercial development fees generated on customer projects.

Taxes collected from customers and remitted to governmental authorities are excluded from revenue and amounted to $0.1 million for each of the years ended September 30, 2015, 2014 and 2013.

Royalties and license fees. The Company licenses technology to third parties and collects royalties. Royalty revenue is generated when a customer sells products incorporating the Company’s licensed technologies. Royalty revenue is recognized as licensees report

it to the Company, and payment is typically submitted concurrently with the report. For stand-alone license agreements, up-front license fees are recognized over the term of the related licensing agreement. Minimum royalty fees are recognized in the period earned.

Revenue related to a performance milestone is recognized upon the achievement of the milestone, as defined in the respective agreements and provided the following conditions have been met:

- The milestone payment is non-refundable;
- The milestone involved a significant degree of risk, and was not reasonably assured at the inception of the arrangement;
- Accomplishment of the milestone involved substantial effort;
- The amount of the milestone payment is commensurate with the related effort and risk; and
- A reasonable amount of time passed between the initial license payment and the first and subsequent milestone payments.

If these conditions have not been met, the milestone payment is deferred and recognized over the term of the agreement.

Product sales. Product sales to third parties consist of direct and distributor sales and are recognized at the time of shipment. The Company's sales terms provide no right of return outside of the standard warranty policy. Payment terms are generally set at 30-45 days.

Research and development. The Company performs third-party research and development activities, which are typically provided on a time and materials basis. Generally, revenue for research and development is recorded as performance progresses under the applicable contract.

Arrangements with multiple deliverables. Revenue arrangements with multiple deliverables requires the Company to:

(i) disclose whether multiple deliverables exist, how the deliverables in an arrangement should be separated, and how the consideration should be allocated;

(ii) allocate revenue in an arrangement using estimated selling prices ("ESP") of deliverables if a vendor does not have vendor-specific objective evidence of selling price ("VSOE") or third-party evidence of selling price ("TPE"); and

(iii) allocate revenue using the relative selling price method.

The Company accounts for revenue using a multiple attribution model in which consideration allocated to research and development activities is recognized as performed, and milestone payments are recognized when the milestone events are achieved, when such activities and milestones are deemed substantive. Accordingly, in situations where a unit of accounting includes both a license and research and development activities, and when a license does not have stand-alone value, the Company applies a multiple attribution model in which consideration allocated to the license is recognized ratably, consideration allocated to research and development activities is recognized as performed and milestone payments are recognized when the milestone events are achieved, when such activities and milestones are deemed substantive.

The Company enters into license and development arrangements that may consist of multiple deliverables which could include a license(s) to SurModics' technology, research and development activities, manufacturing services, and product sales based on the needs of its customers. For example, a customer may enter into an arrangement to obtain a license to SurModics' intellectual property which may also include research and development activities, and supply of products manufactured by SurModics. For these services provided, SurModics could receive upfront license fees upon

signing of an agreement and granting the license, fees for research and development activities as such activities are performed, milestone payments contingent upon advancement of the product through development and clinical stages to successful commercialization, fees for manufacturing services and supply of product, and royalty payments based on customer sales of product incorporating SurModics' technology. The Company's license and development arrangements generally do not have refund provisions if the customer cancels or terminates the agreement. Typically all payments made are non-refundable.

The Company is required to evaluate each deliverable in a multiple element arrangement for separability. The Company is then required to allocate revenue to each separate deliverable using a hierarchy of VSOE, TPE, or ESP. In many instances, the Company is not able to establish VSOE for all deliverables in an arrangement with multiple elements. This may be a result of the Company infrequently selling each element separately or having a limited history with multiple element arrangements. When VSOE cannot be established, the Company attempts to establish a selling price of each element based on TPE. TPE is determined based on competitor prices for similar deliverables when sold separately.

When the Company is unable to establish a selling price using VSOE or TPE, the Company uses ESP in its allocation of arrangement consideration. The objective of ESP is to determine the price at which the Company would transact a sale if the product or service were sold on a stand-alone basis. ESP is generally used for highly customized offerings.

The Company determines ESP for undelivered elements by considering multiple factors including, but not limited to, market conditions, competitive landscape and past pricing arrangements with similar features. The determination of ESP is made through consultation with the Company's management, taking into consideration the marketing strategies for each business unit.

Deferred Revenue

Amounts received prior to satisfying the above revenue recognition criteria are recorded as deferred revenue in the accompanying consolidated balance sheets, with deferred revenue to be recognized beyond one year being classified as non-current deferred revenue. The Company had deferred revenue of $0.3 million for September 30, 2015 and 2014.

Customer advances are accounted for as a liability until all criteria for revenue recognition have been met.

Customer Concentrations

The Company's licensed technologies provide royalty revenue, which represents the largest revenue stream to the Company. The Company has licenses with a diverse base of customers and certain customers have multiple products using the Company's technology. Medtronic plc ("Medtronic") is the Company's largest customer at 26% of total revenue for fiscal 2015. Medtronic has several separately licensed products that generate royalty revenue for SurModics, none of which represented more than 6% of SurModics' total revenue. No other individual customer using licensed technology constitutes more than 10% of the Company's total revenue.

The Company's licensing agreements with many of its customers, including most of its significant customers, cover many licensed products that each separately generates royalty revenue. This structure reduces the potential risk to the Company's operations that may result from reduced sales (or the termination of a license) of a single product for any specific customer.

Research and Development

Research and development costs are expensed as incurred. Some research and development costs are related to third-party contracts, and the related revenue is recognized as described in "Revenue Recognition" above. Costs associated with customer-related research and development include specific project direct labor costs and material expenses as well as an allocation of overhead costs based on direct labor dollars.

Use of Estimates

The preparation of consolidated financial statements in conformity with U.S. GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, the disclosure of contingent assets and liabilities at the date of the consolidated financial statements and the reported amounts of revenue and expenses during the reporting period. Ultimate results could differ from those estimates.

Income Per Share Data

Basic income per common share is calculated based on the weighted average number of common shares outstanding during the period. Diluted income per common share is computed by dividing income by the weighted average number of common and common equivalent shares outstanding during the period. The Company's only potentially dilutive common shares are those that result from dilutive common stock options and non-vested stock relating to restricted stock awards, restricted stock units and performance shares.

The following table sets forth the denominator for the computation of basic and diluted income per share (in thousands):

	2015	2014	2013
Net income from continuing operations available to common shareholders	$11,947	$12,207	$14,579
Basic weighted average shares outstanding	13,029	13,632	14,464
Dilutive effect of outstanding stock options, non-vested restricted stock, restricted stock units and performance shares	260	244	267
Diluted weighted average shares outstanding	13,289	13,876	14,731

The calculation of weighted average diluted shares outstanding excludes outstanding common stock options associated with the right to purchase 0.5 million, 0.5 million and 0.4 million shares for fiscal 2015, 2014 and 2013, respectively, as their inclusion would have had an antidilutive effect on diluted income per share.

New Accounting Pronouncements

Accounting Standards to be Adopted

In July 2013, the Financial Accounting Standards Board (“FASB”) issued amended guidance on the financial statement presentation of an unrecognized tax benefit when a net operating loss carryforward exists, similar to a tax loss, or tax credit carryforward. The guidance requires an unrecognized tax benefit, or a portion of an unrecognized tax benefit, be presented as a reduction of a deferred tax asset when a net operating loss carryforward exists, or similar tax loss, or tax credit carryforward, with certain exceptions. This accounting guidance was adopted during the first quarter of fiscal 2015. The adoption did not have a material impact on the Company’s financial position, results of operation or cash flows.

In May 2014, the FASB issued new revenue recognition guidance for recognizing revenue from contracts with customers that provides a five-step analysis of transactions to determine when and how revenue is recognized. The guidance states that a Company should recognize revenue which depicts the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled to receive in exchange for those goods or services. The new standard will also result in enhanced disclosures about revenue related to the nature, amount, timing, and uncertainty of revenue and cash flows arising from contracts with customers. The standard also requires quantitative and qualitative disclosures about customer contracts, significant judgments and changes in judgments, and assets recognized from the costs to obtain or fulfill a contract. Additionally, the FASB has provided guidance for transactions that were not previously addressed comprehensively, and improved guidance for multiple-element arrangements. The original pronouncement was effective for the Company beginning in fiscal 2018 (October 1, 2017), and early adoption was not permitted. On July 9, 2015 the FASB approved a one-year deferral of the effective date for the revenue recognition standard. As a result of the one-year deferral, the revenue recognition

standard is effective for the Company beginning in fiscal 2019 (October 1, 2018), however, the Company may adopt this guidance as of the original effective date. This guidance can be adopted by the Company either retrospectively (October 1, 2016) or as a cumulative-effect adjustment as of the date of adoption. The Company is currently evaluating the impact that the adoption of this new accounting guidance will have on the Company's results of operations, cash flows and financial position.

No other new accounting pronouncement issued or effective has had, or is expected to have, a material impact on the Company's consolidated financial statements..

3. Discontinued Operations

On November 1, 2011, the Company entered into a definitive agreement (the "Purchase Agreement") to sell substantially all of the assets of its wholly-owned subsidiary, SurModics Pharmaceuticals, to Evonik Degussa Corporation ("Evonik"). Under the terms of the Purchase Agreement, the entire portfolio of products and services of SurModics Pharmaceuticals, including the Company's Current Good Manufacturing Practices ("cGMP") development and manufacturing facility located in Birmingham, Alabama, were sold. The Company retained all accounts receivable and the majority of liabilities associated with SurModics Pharmaceuticals incurred prior to closing. The sale (the "Pharma Sale") closed on November 17, 2011. The total consideration received from the Pharma Sale was $30.0 million in cash. As part of the Pharma Sale, SurModics agreed not to compete in the restricted business (as defined in the Purchase Agreement) for a period of five years and to indemnify Evonik against specified losses in connection with SurModics Pharmaceuticals, including certain contingent consideration obligations related to the acquisition by SurModics Pharmaceuticals of the

portfolio of intellectual property and drug delivery projects from PR Pharmaceuticals, Inc. ("PR Pharma") and other specified excluded liabilities, including the litigation matter with Southern Research Institute ("SRI") described below. SurModics retained responsibility for repayment obligations related to an agreement with various governmental authorities associated with creation of jobs in Alabama. These repayment obligations were settled or terminated in the second and third quarters of fiscal 2013 with payments totaling $325,000 repaid to the governmental authorities and a gain of $1.3 million recognized in the fiscal year ended September 30, 2013.

The following is a summary of the operating results of SurModics Pharmaceuticals discontinued operations for the years ended September 30 (in thousands):

	2014	2013
Total revenue	$—	$—
(Loss) income from discontinued operations	$(260)	$1,136
Income tax benefit (provision)	84	(548)
(Loss) income from discontinued operations, net of income taxes	$(176)	$588
Loss on sale of discontinued operations	$—	$—
Income tax benefit	—	—
Loss on sale of discontinued operations, net of income Taxes	$—	$—

The assets and liabilities of discontinued operations as of September 30 were immaterial to the consolidated financial statements.

In June 2014, the Company resolved the previously disclosed litigation involving SRI, two of SRI's former employees and SurModics Pharmaceuticals. Additionally, in September 2014, the Company reached a final settlement with a second inventor, one of SRI's former employees, of the technology subject to the SRI litigation matter. In connection with the resolution of the litigation, the Company recorded an additional expense, within discontinued operations, of $0.3 million during fiscal 2014. Additionally, in the fourth quarter of fiscal 2014, SurModics submitted a bid of less than $0.1 million related to our indemnification obligations to Evonik related to a contingent consideration matter associated with the PR Pharma intellectual property purchased by Evonik in the Pharma Sale. SurModics was notified in October 2014 that the bid was accepted and made a payment made at that time. The assets and liabilities of discontinued operations as of September 30, 2014 include the amount associated with the bid for the legal rights.

4. Fair Value Measurements

The accounting guidance on fair value measurements defines fair value, establishes a framework for measuring fair value under U.S. GAAP, and expands disclosures about fair value measurements. The guidance is applicable for all financial assets and financial liabilities and for all nonfinancial assets and nonfinancial liabilities recognized or disclosed at fair value in the consolidated financial statements on a recurring basis. Fair value is defined as the exchange price that would be received from selling an asset or paid to transfer a liability (an exit price) in an orderly transaction between market participants at the measurement date. When determining the fair value measurements for assets and liabilities required or permitted to be recorded at fair value, the Company considers the principal or most advantageous market in which it would transact and also considers assumptions that market participants would use when pricing the asset or liability, such as inherent risk, transfer restrictions and risk of nonperformance.

Fair Value Hierarchy

Accounting guidance on fair value measurements requires that assets and liabilities carried at fair value be classified and disclosed in one of the following three categories:

Level 1 — Quoted (unadjusted) prices in active markets for identical assets or liabilities.

The Company’s Level 1 assets as of September 30, 2014 consisted of its investment in Intersect ENT and certain U.S. government and government agency obligations. The fair market value of the Intersect ENT investment was based on the quoted price of Intersect ENT shares as traded on the NASDAQ Global Market Stock Exchange. This investment was sold in the second quarter of

fiscal 2015 generating a realized gain of $0.5 million. The fair market value of certain U.S. government and government agency obligations were based on observable prices in highly active treasury and agency security markets for identical securities.

Level 2 — Observable inputs other than quoted prices included in Level 1, such as 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 for substantially the full term of the asset or liability.

The Company's Level 2 assets as of September 30, 2015 consisted of money market funds and commercial paper instruments. For the year ended September 30, 2014 the Company's Level 2 assets consisted of money market funds, commercial paper instruments, U.S. Treasury securities, corporate bonds, municipal bonds, U.S. government agency securities, government agency and municipal securities and certain asset-backed and mortgage-backed securities. Fair market values for these assets are based on quoted vendor prices and broker pricing where all significant inputs are observable. The Company performs limited tests of the quoted vendor prices based on available U.S. Treasury security pricing on government websites as a means of validating the third party pricing. To ensure the accuracy of quoted vendor prices and broker pricing, the Company performs regular reviews of investment returns to industry benchmarks and sample tests of individual securities to validate quoted vendor prices with other available market data.

Level 3 — Unobservable inputs to the valuation methodology that are supported by little or no market activity and that are significant to the measurement of the fair value of the assets or liabilities. Level 3 assets and liabilities include those whose fair value measurements are determined using pricing models, discounted cash flow methodologies or similar valuation techniques, as well as significant management judgment or estimation.

There were no Level 3 assets at September 30, 2015 or 2014 and there was no Level 3 activity during fiscal 2015.

In valuing assets and liabilities, the Company is required to maximize the use of quoted market prices and minimize the use of unobservable inputs. The Company did not significantly change its valuation techniques from prior periods.

Assets and Liabilities Measured at Fair Value on a Recurring Basis

In instances where the inputs used to measure fair value fall into different levels of the fair value hierarchy, the fair value measurement has been determined based on the lowest level input that is significant to the fair value measurement in its entirety. The Company's assessment of the significance of a particular item to the fair value measurement in its entirety requires judgment, including the consideration of inputs specific to the asset or liability. During the year ended September 30, 2015, the Company liquidated all of its available-for-sale debt and equity securities and is invested solely in cash equivalents as of September 30, 2015. The following table presents information about the Company's assets and liabilities measured at fair value on a recurring basis as of September 30, 2015 (in thousands):

	Quoted Prices in Active Markets for	Significant Other Observable Inputs	Significant Unobservable Inputs (Level 3)	Total Fair Value as of September 30, 2015

	Identical Instruments (Level 1)	(Level 2)		
Assets:				
Cash equivalents	$ —	$ 53,591	$ —	$ 53,591
Total assets measured at fair value	$ —	$ 53,591	$ —	$ 53,591

The following table presents information about the Company's assets and liabilities measured at fair value on a recurring basis as of September 30, 2014 (in thousands):

	Quoted Prices in Active Markets for Identical Instruments (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Total Fair Value as of September 30, 2014
Assets:				
Cash equivalents	$ —	$ 40,100	$ —	$ 40,100
Available-for-sale equity securities	1,550	—	—	1,550
Available-for-sale debt securities:				
U.S. government and government agency obligations	—	7,394	—	7,394
Mortgage-backed securities	—	5,545	—	5,545
Municipal bonds	—	1,175	—	1,175
Asset-backed securities	—	2,369	—	2,369
Corporate bonds	—	1,830	—	1,830
Total assets measured at fair value	$ 1,550	$ 58,413	$ —	$ 59,963

Valuation Techniques

The valuation techniques used to measure the fair value of assets are as follows:

Cash equivalents — These assets are classified as Level 2 and are carried at historical cost which is a reasonable estimate of fair value because of the relatively short time between origination of the instrument and its expected realization.

Available-for-sale equity securities – This asset is classified as Level 1 and represents the Company's investment in Intersect ENT. This investment was valued based on the quoted market price of Intersect ENT shares.

Available-for-sale debt securities — These securities are classified as Level 2 and include various types of debt securities. These securities are valued based on quoted vendor prices in active markets underlying the securities.

Assets and Liabilities Measured at Fair Value on a Non-Recurring Basis

The Company's investments in non-marketable securities of private companies are accounted for using the cost method as the Company does not exert significant influence over the investees' operating or financial activities. These investments are measured at fair value on a non-recurring basis when they are deemed to be other-than-temporarily impaired. In determining whether a decline in value of non-marketable equity investments in private companies has occurred and is other-than-temporary, an assessment is made by considering available evidence, including the general

market conditions in the investee's industry, the investee's product development status and subsequent rounds of financing and the related valuation and/or the Company's participation in such financings. The Company also assesses the investee's ability to meet business milestones and the financial condition and near-term prospects of the individual investee, including the rate at which the investee is using its cash and the investee's need for possible additional funding at a potentially lower valuation. The valuation methodology for determining the decline in value of non-marketable equity securities is based on inputs that require management judgment and are Level 3 inputs.

In the fourth quarter of fiscal 2015, the Company recognized an other-than-temporary impairment loss of $1.5 million based on the indicated value of a third-party transaction expected to close by December 31, 2015. See Note 2 for further information.

In the fourth quarter of fiscal 2014, the Company recognized an other-than-temporary impairment loss of $1.2 million based on capital funding initiatives and current operating conditions of ThermopeutiX. See Note 2 for further information.

5. Stockholders' Equity

Repurchase of Common Stock

Shares are repurchased from time to time to support the Company's stock-based compensation programs and to return capital to stockholders. The Company accounts for repurchases of common stock using the par value method.

On January 28, 2013, the Company's Board of Directors authorized the repurchase of up to an additional $10.0 million of the Company's outstanding common stock. As of June 30, 2013, the Company had completed the January 2013 authorization as well as the remaining $0.3 million under a previous authorization as the Company repurchased a cumulative 405,290 shares at an average price of $25.47 per share.

On July 29, 2013, the Company's Board of Directors authorized the repurchase of up to an additional $20.0 million of the Company's outstanding common stock through open-market purchases, private transactions, block trades, accelerated share repurchase transactions, tender offers, or by any combination of such methods. Through September 30, 2013, the Company had repurchased 390,353 shares at an average price of $21.71 under the July 2013 authorization. The Company had $11.5 million available for future share repurchases as of September 30, 2013.

During fiscal 2014, the Company repurchased an aggregate of 485,777 shares of common stock for a total of $11.5 million under the July 2013 authorization at an average price of $23.77 per share. The July 2013 authorized amount was used as of September 30, 2014 with a small amount remaining. During fiscal 2013, the Company repurchased an aggregate of 795,643 shares of common stock for a total of $18.8 million under the May 2012, January 2013 and July 2013 authorizations, including $1.0 million associated with open market repurchases at September 30, 2013.

On November 5, 2014, the Company's Board of Directors authorized it to repurchase up to $30.0 million of the Company's outstanding common stock in open-market purchases, privately negotiated transactions, block trades, accelerated share repurchase transactions, tender offers or by any combination of such methods. The authorization has no fixed expiration date. As part of the accelerated share repurchase ("ASR") program discussed below, the Company repurchased 758,143 shares of common stock on November 11, 2014 and 89,721 of common stock on July 8, 2015, the date that the ASR program was completed. As adjusted for the final ASR program settlement, $10.0 million remained available for future repurchases under the November 5, 2014 authorization.

On November 11, 2014, the Company entered into an accelerated share repurchase program with Wells Fargo Bank, National Association. In connection with this agreement, the Company made a $20.0 million payment to the bank and immediately received an initial delivery of 758,143 shares of its common stock with a fair value of $16.0 million as of the purchase date. Effective as of the date of the initial share purchase, the transaction was accounted for as a share retirement, resulting in a reduction of common stock of less than $0.1 million, additional paid-in capital of $2.5 million and retained earnings of $13.5 million. The remaining $4.0 million of the Company's payment was also reported as a reduction in retained earnings. The specific number of shares that the Company ultimately purchased under the ASR agreement was based on the volume weighted average price of the Company's common stock during the purchase period, less an agreed upon discount. In the aggregate the Company purchased 847,864 shares under the ASR program for an average price of $23.59 per share. Based on the facts associated with the agreement, the forward contract was indexed to the Company's common stock and met the U.S. GAAP requirements to be classified as permanent equity as of July 8, 2015.

On November 6, 2015, the Company's Board of Directors authorized the repurchase of up to $20.0 million of the Company's outstanding common stock in addition to the $10.0 million authorization which remains available from the November 5, 2014 authorization.

6. Stock-Based Compensation Plans

The Company has stock-based compensation plans under which it grants stock options, restricted stock awards, performance share awards, restricted stock units and deferred stock units. Accounting guidance requires all share-based payments to be recognized as an operating expense, based on their fair values, over the requisite service period. The Company's stock-based compensation expenses for the years ended September 30 were allocated to the following expense categories (in thousands):

	2015	2014	2013
Product costs	$24	$16	$22
Research and development	226	175	180
Selling, general and administrative	2,131	3,146	2,350
Total stock-based compensation expense	$2,381	$3,337	$2,552

As of September 30, 2015, approximately $1.9 million of total unrecognized compensation costs related to non-vested awards is expected to be recognized over a weighted average period of approximately 2.1 years. Such costs include $0.2 million based on payout levels associated with performance share awards that are currently anticipated to be fully expensed because the performance conditions are expected to be met above the minimum levels for each award period.

Stock Option Awards

The Company uses the Black-Scholes option pricing model to determine the weighted average grant date fair value of stock options. Weighted average per share fair values of stock options granted during fiscal 2015, 2014 and 2013 were $7.26, $8.72 and $8.69, respectively. The assumptions used as inputs in the model for the years ended September 30 were as follows:

	2015	2014	2013
Risk-free interest rates	1.43 %	1.19 %	0.60 %
Expected life	4.5 years	4.6 years	4.8 years
Expected volatility	43 %	45 %	49 %
Dividend yield	0 %	0 %	0 %

The risk-free interest rate assumption was based on the U.S. Treasury's rates for U.S. Treasury zero-coupon bonds with maturities similar to those of the expected term of the award. The expected life of options granted is determined based on the Company's experience. Expected volatility is based on the Company's stock price movement over a period approximating the expected term. Based on management's judgment, dividend rates are expected to be zero for the expected life of the options. The Company also estimates forfeitures of options granted, which are based on historical experience.

Non-qualified stock options are granted at fair market value on the grant date. Non-qualified stock options expire in seven to ten years or upon termination of employment or service as a Board member. With respect to members of our Board, non-qualified stock options generally become exercisable on a pro-rata basis over the one-year period following the date of grant. With respect to our employees, non-qualified stock options generally become exercisable with respect to 25% of the shares on each of the first four anniversaries following the grant date.

Non-qualified stock options granted prior to May 2008 generally become exercisable with respect to 20% of the shares on each of the first five anniversaries following the grant date, and non-qualified stock options granted to the Company's employees subsequent to April 2008 generally become exercisable with respect to 25% of the shares on each of the first four anniversaries following the grant date.

The Company modified non-qualified stock option awards granted to Board members in February 2014, which resulted in acceleration of the stock option vesting period. The modification changed the vesting period to a pro-rata basis over a one-year period from a four-year period and resulted in an increase to stock option expense of $0.5 million in fiscal 2014.

Shareholders approved the 2009 Equity Incentive Plan ("2009 Plan") at the February 8, 2010 Annual Meeting of Shareholders. The 2009 Plan has 1,500,000 shares authorized, plus the number of shares that have not yet been awarded under the 2003 Equity Incentive Plan, or were awarded and subsequently returned to the pool of available shares under the 2003 Equity Incentive Plan pursuant to its terms. At September 30, 2015, there were 938,391 shares available for future awards. As of September 30, 2015, the aggregate intrinsic value of the option shares outstanding and option shares exercisable was $4.5 million and $3.8 million, respectively. At September 30, 2015, the average remaining contractual life of options outstanding and options exercisable was 3.2 and 2.4 years, respectively. The total pre-tax intrinsic value of options exercised during fiscal 2015 and 2014 was $1.7 million and $1.4 million, respectively. The intrinsic value represents the difference between the exercise price and the fair market value of the

Company’s common stock on the last day of the respective fiscal period end.

The following table summarizes all stock options activity and stock options outstanding and exercisable under the stock option plans during fiscal 2015, 2014 and 2013:

	Number of Shares	Weighted Average Exercise Price
Outstanding at September 30, 2012	1,325,438	$ 21.25
Granted	178,924	20.85
Exercised	(10,273)	14.40
Forfeited	(125,105)	33.47
Outstanding at September 30, 2013	1,368,984	20.13
Granted	138,837	22.71
Exercised	(190,434)	14.42
Forfeited	(106,768)	31.26
Outstanding at September 30, 2014	1,210,619	20.35
Granted	164,401	21.24
Exercised	(166,422)	14.54
Forfeited	(90,590)	35.35
Outstanding at September 30, 2015	1,118,008	20.10
Exercisable at September 30, 2015	797,045	$ 20.04

The stock-based compensation table includes stock options activity related to discontinued operations, however, there were no stock options outstanding or exercisable related to discontinued operations as of September 30, 2015, 2014 or 2013.

Restricted Stock Awards

The Company has entered into restricted stock agreements with certain key employees, covering the issuance of common stock (“Restricted Stock”). Under accounting guidance, these shares are considered to be non-vested shares. The Restricted Stock is released to the key employees if they are employed by the Company at the end of the vesting period. Compensation has been recognized for the estimated fair value of the common shares and is being charged to income over the vesting term. The stock-based compensation table above includes Restricted Stock expenses recognized related to these awards, which totaled $0.3 million, $0.2 million and $0.1 million during fiscal 2015, 2014 and 2013, respectively.

The following table summarizes all restricted stock awards activity during fiscal 2015, 2014 and 2013:

	Number of Shares	Weighted Average

		Grant Price
Balance at September 30, 2012	4,000	$ 22.11
Vested	5,234	23.88
Forfeited	(4,000)	22.11
Balance at September 30, 2013	5,234	23.88
Granted	22,155	22.67
Vested	(7,991)	23.98
Forfeited	(774)	22.58
Balance at September 30, 2014	18,624	22.45
Granted	18,073	21.84
Vested	(7,606)	22.28
Forfeited	(1,316)	22.16
Balance at September 30, 2015	27,775	$ 22.12

The stock-based compensation table includes restricted stock awards activity related to discontinued operations, however, there were no restricted stock awards outstanding related to discontinued operations as of September 30, 2015, 2014 or 2013.

Performance Share Awards

The Company has entered into performance share agreements with certain key employees, covering the issuance of common stock ("Performance Shares"). The Performance Shares vest upon the achievement of all or a portion of certain performance objectives, which must be achieved during the performance period. The Performance Shares are not issued and outstanding until the performance objectives are met. Performance objectives selected by the Organization and Compensation Committee of the Board of Directors (the "Committee") were cumulative earnings per share and cumulative revenue for the three-year performance periods for fiscal 2012 (2012 – 2014), fiscal 2013 (2013 – 2015), fiscal 2014 (2014 – 2016) and fiscal 2015 (2015 – 2017). Assuming that the minimum performance level is attained, the number of shares that may actually vest will vary based on performance from 20% (minimum) to 200% (maximum). Shares will be issued to participants as soon as practicable following the end of the performance periods subject to Committee approval and verification of results. The compensation cost related to the number of shares to be granted under each performance period is fixed on the grant date, which is the date the performance period begins. Compensation expense is recognized in each period based on management's best estimate of the achievement level of the specified performance objectives for Performance Shares. In fiscal 2015, the Company recognized expense of $0.5 million related to probable achievement of performance objectives for three-year Performance Shares granted in fiscal 2015, 2014 and 2013. In fiscal 2014, the Company recognized expense of $0.6 million related to probable achievement of performance objectives for three-year Performance Shares granted in fiscal 2014, 2013 and 2012. In fiscal 2013, the Company recognized expense of $1.2 million related to probable achievement of performance objectives for three-year Performance Shares granted in fiscal 2012 and 2011. The stock-based compensation table above includes the Performance Shares expenses.

The fair values of the Performance Shares, at target, were $0.9 million, $0.9 million and $0.9 million for grants awarded in fiscal 2015, 2014 and 2013, respectively.

The aggregate number of shares that could be awarded to key employees if the minimum, target and maximum performance goals are met, based upon the fair value at the date of grant is as follows:

Performance Period	Minimum Shares	Target Shares	Maximum Shares
Fiscal 2013 – 2015	8,551	42,753	85,506
Fiscal 2014 - 2016	7,861	39,303	78,606
Fiscal 2015 – 2017	8,440	42,199	84,398

The Fiscal 2013 – 2015 awards are expected to be finalized in December 2015 at an estimated 41,727 shares based on performance objective results. Based on the Company's performance through September 30, 2015, it is estimated that approximately 3,930 shares may be earned for the Fiscal 2014 – 2016 performance period and that approximately 10,676 shares may be earned for the Fiscal 2015 – 2017 performance period.

1999 Employee Stock Purchase Plan

Under the 1999 Employee Stock Purchase Plan ("Stock Purchase Plan"), the Company is authorized to issue up to 400,000 shares of common stock. All full-time and part-time employees can choose to have up to 10% of their annual compensation withheld, with a limit of $25,000, to purchase the Company's common stock at purchase prices defined within the provisions of the Stock Purchase Plan. As of September 30, 2015 and 2014, there were less than $0.1 million of employee contributions in each period included in accrued liabilities in the consolidated balance sheets. Stock compensation expense recognized related to the Stock Purchase Plan totaled $0.1 million, $0.1 million and $0.1

million, during fiscal 2015, 2014 and 2013, respectively. The stock-based compensation table above includes the Stock Purchase Plan expenses.

Restricted Stock and Deferred Stock Units

The Company has awarded a total of 23,736 restricted stock units ("RSU") in fiscal 2015 and 2014 under the 2009 Equity Incentive Plan to non-employee directors with forfeiture of 3,068 RSUs in fiscal 2015. The Company modified the RSU awards granted to Board members in February 2014, which resulted in acceleration of the RSU award vesting period. The modification changed the vesting period to a pro-rata basis over a one-year period from a three-year period and resulted in an increase to RSU award expense of $0.2 million in fiscal 2014. RSU awards are not considered issued or outstanding common stock of the Company until they vest. The estimated fair value of the RSU awards was calculated based on the closing market price of SurModics' common stock on the date of grant. Compensation expense has been recognized for the estimated fair value of the common shares and is being charged to income over the vesting term. The stock-based compensation table above includes RSU expenses recognized related to these awards, which totaled $0.2 million, $0.4 million and $0.1 million for fiscal 2015, 2014 and 2013, respectively.

Directors can also elect to receive their annual fees for services to the Board in deferred stock units ("DSUs"). Certain directors elected this option beginning on January 1, 2013 which has resulted in 18,934 units issued with a total value of $0.4 million. These DSUs are fully vested. Stock-based compensation expense related to DSU awards, totaled $0.1 million in both fiscal 2015 and 2014.

7. Restructuring Charges

During the fiscal years ended September 30, 2015 and 2014, the Company did not incur any restructuring charges. The restructuring charge for fiscal 2013 described below has been presented separately as restructuring charges in the consolidated statements of income.

In September 2013 (fiscal 2013), the Company announced a realignment of its business to enhance focus on key growth initiatives. As a result of the organizational change, the Company eliminated approximately 6% of its workforce. These employee terminations occurred across various functions, and the reorganization plan was completed by the end of fiscal 2013. The Company recorded total pre-tax restructuring charges of $0.5 million in the fourth quarter of fiscal 2013, which consisted of severance pay and benefits expenses.

The following table summarizes the restructuring accrual activity (in thousands):

	Employee Severance and Benefits	Facility-Related Costs	Total
Balance at September 30, 2012	$ 10	$ 182	$192
Accrual/(reversal) during the year	534	(58)	476
Cash payments	(145)	(107)	(252)
Balance at September 30, 2013	$ 399	$ 17	$416
Accrual/(reversal) during the year	(20)	(2)	(22)
Cash payments	(379)	(15)	(394)
Balance at September 30, 2014	$ —	$ —	$—

8. Revolving Credit Facility

On November 4, 2013, the Company entered into a three-year $20.0 million secured revolving credit facility. The Company's obligations under the credit facility are secured by substantially all of its and its subsidiaries' assets, other than intellectual property and real estate. Borrowings under the credit facility, if any, will bear interest at a benchmark

rate plus a margin ranging from 1.375% to 2.00% based on the Company's leverage ratio. A facility fee is payable on unused commitments at a rate of 0.20% per annum.

On November 20, 2015, the credit facility was further amended and modified to increase the size of stock repurchases that may be effected by the Company to $30.0 million without the consent of the lender.

In connection with the credit facility, the Company is required to maintain certain financial covenants related to a maximum leverage ratio and a minimum earnings before income tax, depreciation and amortization ("EBITDA") amount and to comply with nonfinancial covenants. As of September 30, 2015, the Company has no debt outstanding and was in compliance with all financial.

9. Income Taxes

The Company accounts for income taxes under the asset and liability method prescribed in accounting guidance. Deferred tax assets and liabilities are recognized for the future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases. A valuation allowance is provided when it is more likely than not that some portion or all of a deferred tax asset will not be realized. The ultimate realization of deferred tax assets depends on the generation of future taxable income during the period in which related temporary differences become deductible. Management considers the scheduled reversal of deferred tax liabilities, projected future taxable income and tax planning strategies in this assessment. Deferred tax assets and liabilities are measured using the enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. The effect on deferred tax assets and liabilities of a change in tax rates is recognized in income in the period that includes the enactment date of such change.

Income taxes from continuing operations in the accompanying consolidated statements of income for the fiscal years ended September 30 are as follows (in thousands):

	2015	2014	2013
Current provision:			
Federal	$6,065	$6,470	$6,048
State and foreign	136	147	225
Total current provision	6,201	6,617	6,273
Deferred provision (benefit):			
Federal	58	(347)	(552)
State	35	(5)	60
Total deferred provision (benefit)	93	(352)	(492)
Total provision	$6,294	$6,265	$5,781

The reconciliation of the difference between amounts calculated at the statutory U.S. federal tax rate of 35% for the fiscal years ended September 30 and the Company's effective tax rate from continuing operations is as follows (in thousands):

	2015	2014	2013
Amount at statutory U.S. federal income tax rate	$6,385	$6,465	$7,126
Change because of the following items:			
State income taxes, net of federal benefit	67	118	278
Stock-based compensation	16	21	25
Valuation allowance change	348	120	(699)
Tax reserve change	34	(121)	(128)
Federal manufacturing deduction	(268)	(235)	(266)
Federal research and development credit	(74)	(67)	(324)
Other	(214)	(36)	(231)
Income tax provision	$6,294	$6,265	$5,781

The federal research and development tax credit for fiscal 2015 and 2014 includes the benefit generated for the period from October 1, 2014 to December 31, 2014 and October 1, 2013 to December 31, 2013, respectively, prior to the expiration of the benefit in each period. The federal research and development credit for fiscal 2013 above includes $0.2 million related to a retroactive 2012 U.S. research and development tax credit for the period from January 1, 2012 to December 31, 2012 which was recognized in fiscal 2013 as a discrete tax benefit resulting from the January 2013 signing of the American Taxpayer Relief Act of 2012.

The Company recorded an income tax benefit from discontinued operations of $0.1 million in fiscal 2014, an income tax expense of $0.5 million in fiscal 2013, an income tax expense of $1.1 million in fiscal 2012 and an income tax benefit of $0.6 million associated with the sale of discontinued operations assets in fiscal 2012.

The components of deferred income taxes consisted of the following as of September 30 and result from differences in the recognition of transactions for income tax and financial reporting purposes (in thousands):

	2015	2014
Depreciable assets	$1,618	$1,612
Deferred revenue	96	101
Accruals and reserves	145	324
Stock-based compensation	4,194	4,373
Impaired strategic investments	4,186	3,674
Unrealized gains on investments	—	(550)
Capital loss carryforward	1,456	1,650
Other	1,276	764
Valuation allowance	(5,721)	(4,836)
Total deferred tax assets	7,250	7,112
Less current deferred tax assets	(546)	(394)
Noncurrent deferred tax assets	$6,704	$6,718

As of September 30, 2015 and 2014, the Company recorded a deferred tax asset valuation allowance of $5.7 million and $4.8 million, respectively. The valuation allowances are primarily related to capital loss carryforwards created by impairment losses on strategic investments and state R&D credit carryforwards. The increase in fiscal 2015 primarily relates to creation of valuation allowances associated with a loss created by the impairment of certain of the Company's strategic investments and an increase in state research and development tax credit carry-forwards.

Unrecognized tax benefits are the differences between a tax position taken, or expected to be taken in a tax return, and the benefit recognized for accounting purposes pursuant to accounting guidance. A reconciliation of the beginning and ending amount of unrecognized tax benefits, excluding interest and penalties, is as follows (in thousands):

	2015	2014	2013
Beginning of fiscal year	$1,216	$1,300	$1,435
Increases in tax positions for prior years	50	43	27
Decreases in tax positions for prior years	(10)	(1)	(278)
Increases in tax positions for current year	146	149	122
Lapse of the statute of limitations	(154)	(275)	(6)
End of fiscal year	$1,248	$1,216	$1,300

The total amount of unrecognized tax benefits excluding interest and penalties that, if recognized, would affect the effective tax rate as of September 30, 2015, 2014 and 2013, respectively, are $0.9 million, $0.9 million and $1.0 million. Currently, the Company does not expect the liability for unrecognized tax benefits to change significantly in the next 12 months with the above balances classified on the consolidated balance sheets in other long-term liabilities. Interest and penalties related to unrecognized tax benefits are recorded in income tax expense. As of September 30, 2015, 2014 and 2013, a gross balance of $0.6 million, $0.6 million and $0.7 million, respectively, has been accrued related to the unrecognized tax benefits balance for interest and penalties.

The Company files income tax returns, including returns for its subsidiaries, in the U.S. federal jurisdiction and in various state jurisdictions. Uncertain tax positions are related to tax years that remain subject to examination. The Internal Revenue Service ("IRS") commenced an examination of the Company's U.S. income tax return for fiscal 2012 in the first quarter of fiscal 2014. The examination was completed in the fourth quarter of fiscal 2014 with a payment made associated with a timing adjustment. U.S. income tax returns for years prior to fiscal 2012 are no longer subject to examination by federal tax authorities. For tax returns for state and local jurisdictions, the Company is no longer subject to examination for tax years generally before fiscal 2005.

10. Defined Contribution Plan

The Company has a 401(k) retirement and savings plan for the benefit of qualifying employees. The Company matches 50% of employee contributions on the first 6% of eligible compensation. Company contributions totaling $0.3 million, $0.2 million and $0.2 million have been expensed in the years ended September 30, 2015, 2014 and 2013, respectively.

11. Amounts Reclassified Out of Accumulated Other Comprehensive Income

Amounts reclassified out of Accumulated Other Comprehensive Income ("AOCI") totaled $0.3 million and $0.1 million on a pre-tax basis for the fiscal years ended September 30, 2015 and 2014, respectively. The amounts reclassified out of AOCI are associated with unrealized gains on available-for-sale securities that were realized on the sale of the securities and are presented in other income, net in the consolidated statements of income.

12. Commitments and Contingencies

Litigation. From time to time, the Company has been, and may become, involved in various legal actions involving its operations, products and technologies, including intellectual property and employment disputes. The outcomes of these legal actions are not within the Company's complete control and may not be known for prolonged periods of time. In some actions, the claimants seek damages, as well as other relief, including injunctions barring the sale of products that are the subject of the lawsuit, which, if granted, could require significant expenditures or result in lost revenue. The Company records a liability in the consolidated financial statements for these actions when a loss is known or considered probable and the amount can be reasonably estimated. If the reasonable estimate of a known or probable loss is a range, and no amount within the range is a better estimate, the minimum amount of the range is accrued. If a loss is possible but not known or probable, and can be reasonably estimated, the estimated loss or range of loss is disclosed. In most cases, significant judgment is required to estimate the amount and timing of a loss to be recorded.

In the Company's Quarterly Reports on Form 10-Q for the periods ended March 31, 2015, and June 30, 2015, it was disclosed a notice was received from a customer alleging an overpayment of approximately $5.7 million in royalties covering the period January 2009 through September 2014 (the "Claim"). On September 29, 2015, the Company entered into a settlement and release agreement resolving the Claim. Under the agreement, among other things, (a) the Company agreed to pay the customer $2.5 million to settle the Claim, (b) the customer agreed to pay the Company approximately $0.5 million for undisputed royalties that were unpaid and were not previously recognized, during fiscal 2015, and (c) the Company and the customer agreed to a mutual release relating to the Claim and certain other claims by the Company for royalties owed by the customer. In connection with the settlement, in the fourth quarter of fiscal 2015, the Company recognized revenue of approximately $0.5 million and recorded a charge of approximately $2.5 million.

InnoCore Technologies BV. In March 2006, the Company entered into a license agreement whereby SurModics obtained an exclusive license to a drug delivery coating for licensed products within the vascular field which included peripheral, coronary and neurovascular biodurable stent product. The license requires an annual minimum payment of 200,000 euros (equivalent to $223,000 using a euro to US $ exchange rate of 1.11707 as of September 30, 2015) until the last patent expires which is currently estimated to be September 2027. The total minimum future payments associated with this license are approximately $2.7 million. The license is currently utilized with one of SurModics' drug delivery customers.

PR Pharmaceuticals, Inc. In November 2008, SurModics Pharmaceuticals acquired certain contracts and assets of PR Pharma to enhance its portfolio of drug delivery technologies for the pharmaceutical and biotechnology industries. The Company agreed to indemnify Evonik, for a period of five years, for up to $2.5 million of contingent consideration obligations owed to the sellers of PR Pharma related to a future patent issuance milestone when it sold substantially all of the SurModics Pharmaceuticals assets to Evonik on November 17, 2011. In the fourth quarter of fiscal 2014, SurModics submitted a bid of less than $0.1 million related to our indemnification obligations to Evonik related to a contingent consideration matter associated with the PR Pharma intellectual property purchased by Evonik in the Pharma Sale. SurModics was notified in October 2014 that the bid was accepted with a payment made at that time.

Operating Leases. The Company leases certain facilities under noncancelable operating lease agreements. Rent expense for the years ended September 30, 2015, 2014 and 2013 was $0.1 million for each period. Annual commitments pursuant to operating lease agreements are as follows (in thousands):

Year Ended September 30,	
2016	$73
2017	68
2018	70
2019	72
2020	74
Thereafter	12
Total minimum lease payments	$369

13. Operating Segment Information

The accounting standards for reporting information about operating segments define operating segments as components of an enterprise about which separate financial information is available that is evaluated regularly by the chief operating decision maker, who is the Company's Chief Executive Officer, in deciding how to allocate resources and in assessing performance. For financial accounting and reporting purposes, the Company reports its results for the two reportable segments as follows: (1) the Medical Device unit, which is comprised of surface modification coating technologies to improve access, deliverability, and predictable deployment of medical devices, as well as drug delivery coating technologies to provide site-specific drug delivery from the surface of a medical device, with end markets that include coronary, peripheral, and neuro-vascular, and urology, among others, and (2) the In Vitro Diagnostics unit, which consists of component products and technologies for diagnostic test kits and biomedical research applications, with products that include protein stabilization reagents, substrates, antigens and surface coatings.

The tables below present segment revenue, operating income from continuing operations and depreciation and amortization, for the years ended September 30, as follows (in thousands):

	2015	2014	2013
Revenue:			
Medical Device	$45,944	$43,068	$41,153
In Vitro Diagnostics	15,954	14,371	14,979
Total revenue	$61,898	$57,439	$56,132
Operating income (loss):			
Medical Device	$21,192	$22,636	$21,164
In Vitro Diagnostics	4,484	3,459	4,222
Total segment operating income	25,676	26,095	25,386
Corporate	(6,587)	(7,519)	(6,566)
Total operating income from continuing operations	$19,089	$18,576	$18,820
Depreciation and amortization:			
Medical Device	$1,138	$1,136	$1,255
In Vitro Diagnostics	873	850	864
Corporate	794	729	767
Total depreciation and amortization	$2,805	$2,715	$2,886

The Corporate category includes expenses for administrative corporate functions, such as executive, corporate accounting, legal, human resources and Board of Directors related, that have not been fully allocated to the Medical Device and In Vitro Diagnostics segments. Corporate also includes expenses, such as litigation, which are not specific to a segment and thus not allocated to the operating segments.

Corporate segment results above for fiscal 2014 include increased stock option expense of $0.9 million related to a modification of equity awards granted to Board members.

Corporate segment results above for fiscal 2013 include restructuring charges of $0.5 million and recovery of legal fees associated with the SRI litigation of $1.0 million.

Asset information by segment is not presented because the Company does not provide its chief operating decision maker assets by segment, as the data is not readily available.

Major Customers

Revenue from customers that equaled or exceeded 10% of total revenue was as follows for the years ended September 30:

	2015	2014	2013
Medtronic	26 %	19 %	19 %

The revenue from the customer listed is derived from two primary sources: licensing and product sales. The percentage of revenue increased in fiscal 2015 as a result of Medtronic's merger with Covidien PLC on January 26, 2015.

Geographic Revenue

Geographic revenue was as follows for the years ended September 30:

	2015		2014		2013	
Domestic	77	%	78	%	79	%
Foreign	23	%	22	%	21	%

14. Subsequent Events

On November 6, 2015, the Company's Board of Director authorized it to repurchase up to an additional $20.0 million of the Company's outstanding stock in open-market purchases, privately negotiated transactions, block trades, accelerated share repurchase transactions, tender offers or by any combination of such methods. With this authorization, the Company may currently repurchase up to $30.0 million of its outstanding stock. The authorization has no fixed expiration date.

On November 20, 2015, the Company acquired 100% of the outstanding common shares and voting shares of Creagh located in Ballinasloe, Ireland. The results of Creagh's operations will be included in the Company's consolidated financial statements as of the Creagh acquisition date. The acquisition was financed with cash on hand. The Company acquired Creagh for up to €30 million ($32.1 million), including an upfront payment of €18 million ($19.3 million), and up to €12 million ($12.8 million) based on achievement of revenue and value-creating operational milestones through September 30, 2018. The payment of the milestones will occur in the quarter ending December 31, 2018.

Creagh is a provider of innovative, efficient and cost-effective design and manufacture of high-quality PTA balloon catheters. Since 2006, Creagh has grown its technical and product capability with PTA products approved throughout the world, including Europe, the United States, and Japan. With these resources, the Company is uniquely positioned to offer a total solutions approach from product design and development, through in-house extrusion, balloon forming, top-assembly, packaging and regulatory capabilities to approved products for exclusive distribution. The acquisition is a major step forward in the Company's strategy to transform its Medical Device segment from being a provider of coatings technologies, to offering whole-product solutions to medical device customers in the large and growing global interventional vascular market.

The Company has excluded the purchase price allocations and pro forma disclosures for the Creagh acquisition as the initial accounting is currently incomplete. The Company is currently in the process of obtaining an initial valuation related to the acquired assets and liabilities.

On November 20, 2015, the Company's credit facility was amended and modified to increase the size of stock repurchases that can be effected by the Company by $20.0 million.

15. Quarterly Financial Data (Unaudited)

The following is a summary of the unaudited quarterly results for the years ended September 30, 2015 and 2014 (in thousands, except per share data).

	First Quarter	Second Quarter	Third Quarter	Fourth Quarter
Fiscal 2015				
Total revenue	$14,205	$14,415	$15,914	$17,364
Operating income from continuing operations	5,034	3,932	5,857	4,266
Income from continuing operations	3,614	3,051	3,924	1,358
Loss from discontinued operations	—	—	—	—
Net income	3,614	3,051	3,924	1,358
Basic income (loss) per share(1):				
Continuing operations	0.27	0.24	0.30	0.10
Discontinued operations	0.00	0.00	(0.00)	(0.00)
Net income	0.27	0.24	0.30	0.10
Diluted income (loss) per share(1):				
Continuing operations	0.27	0.23	0.30	0.10
Discontinued operations	0.00	0.00	(0.00)	(0.00)
Net income	0.27	0.23	0.30	0.10
Fiscal 2014				
Total revenue	$13,883	$13,604	$14,616	$15,336
Operating income from continuing operations	4,329	3,480	5,333	5,434
Income from continuing operations	3,630	2,459	3,674	2,444
Loss from discontinued operations	—	—	(76)	(100)
Net income	3,630	2,459	3,598	2,344
Basic income (loss) per share(1):				
Continuing operations	0.26	0.18	0.27	0.18
Discontinued operations	0.00	0.00	(0.01)	(0.01)
Net income	0.26	0.18	0.26	0.17
Diluted income (loss) per share(1):				
Continuing operations	0.26	0.18	0.27	0.18
Discontinued operations	0.00	0.00	(0.01)	(0.01)
Net income	0.26	0.18	0.26	0.17

(1) The sum of the quarterly income (loss) per share amounts may not equal the annual income (loss) per share total because of changes in the weighted average number of shares outstanding that occurred during the year.

In the fourth quarter of fiscal 2015, the Company recorded expense related to the settlement of a claim of $2.5 million, a $1.5 million impairment loss on a strategic investment and recognized $0.8 million in previously contingent royalties.

In the third quarter of fiscal 2015, the Company recorded a $0.6 million one-time customer royalty payment related to periods prior to the third quarter fiscal 2015.

In the second quarter of fiscal 2015, the Company recorded a $0.5 million gain on a strategic investment in Intersect ENT shares.

In the fourth quarter of fiscal 2014, the Company recorded a $1.2 million impairment loss on strategic investments.

In the second quarter of fiscal 2014, the Company recorded a $0.9 million stock-based compensation expense related to modification of Board of Directors options and other equity awards vesting periods.

In the first quarter of fiscal 2014, the Company recorded a gain of $0.7 million associated with contingent consideration paid associated with the sale of a strategic investment.