

UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION

SECURITIES EXCHANGE ACT OF 1934
Release No. 90681 / December 16, 2020

ADMINISTRATIVE PROCEEDING
File No. 3-20170

In the Matter of

Dentsply Sirona Inc.,

Respondent.

ORDER INSTITUTING CEASE-AND-DESIST PROCEEDINGS PURSUANT TO SECTION 21C OF THE SECURITIES EXCHANGE ACT OF 1934, MAKING FINDINGS, AND IMPOSING A CEASE-AND-DESIST ORDER

I.

The Securities and Exchange Commission (“Commission”) deems it appropriate that cease-and-desist proceedings be, and hereby are, instituted pursuant to Section 21C of the Securities Exchange Act of 1934 (“Exchange Act”) against Dentsply Sirona Inc. (“DSI” or “Respondent”).

II.

In anticipation of the institution of these proceedings, Respondent has submitted an Offer of Settlement (the “Offer”) which the Commission has determined to accept. Solely for the purpose of these proceedings and any other proceedings brought by or on behalf of the Commission, or to which the Commission is a party, and without admitting or denying the findings herein, except as to the Commission’s jurisdiction over it and the subject matter of these proceedings, which are admitted, Respondent consents to the entry of this Order Instituting Cease-and-Desist Proceedings Pursuant to Section 21C of the Securities Exchange Act of 1934, Making Findings, and Imposing a Cease-And-Desist Order (“Order”), as set forth below.

III.

On the basis of this Order and Respondent's Offer, the Commission finds¹ that

Summary

1. DSI failed to make required disclosure of known trends and uncertainties in its periodic filings for the first three quarters of 2016 ("Relevant Period"). DSI sold more of its dental technologies equipment to its exclusive distributor for the United States (the "Exclusive Distributor") than the distributor could sell to retail purchasers. DSI knew during the Relevant Period that retail demand for certain of its technology products was not keeping pace with the Exclusive Distributor's purchases and that inventory levels at the Exclusive Distributor were at an all-time high. By second quarter 2016, DSI also knew that the Exclusive Distributor wanted to negotiate key terms of its next contract to reduce its inventory levels. In third quarter 2016, DSI was negotiating with the Exclusive Distributor to minimize the financial impact of the excess inventory on DSI's net sales in the future, but knew the outcome of those negotiations was uncertain. Each quarter, DSI knew the trends or uncertainties were reasonably likely to have a material unfavorable impact on net sales or revenues. When preparing its quarterly filings, however, DSI did not disclose these known trends and uncertainties to investors in its Forms 10-Q for the first three quarters of 2016. By failing to disclose these known trends and uncertainties, DSI violated Section 13(a) of the Exchange Act and Rules 12b-20 and 13a-13 thereunder.

Respondent

2. DSI is incorporated in Delaware and is headquartered in Charlotte, NC. Its common stock trades on the NASDAQ Stock Market LLC under the symbol XRAY, and is registered with the Commission pursuant to Section 12(b) of the Exchange Act.

Background

3. After the merger of Sirona Dental Systems, Inc. ("Sirona") and Denstply International Inc. in February 2016, the combined entity, DSI, described itself as the world's largest manufacturer of professional dental products and technologies. DSI reported on two operating segments – consumables and technologies. DSI's technologies segment, which was largely the legacy Sirona business, was responsible for the design, manufacture, and sales, of DSI's dental technology products.

4. Sirona contracted with the Exclusive Distributor in 2012 to distribute nearly all of Sirona's products in the United States through September 2017. The contracts, which governed different product lines, each required the Exclusive Distributor either to purchase a minimum amount of product from Sirona each year (minimum purchase requirements, or "MPRs") or pay a specified amount to Sirona, and later, DSI to maintain its status as Exclusive Distributor in the United States. The MPRs increased annually by ten percent for each product line. The contracts

¹ The findings herein are made pursuant to Respondent's Offer of Settlement and are not binding on any other person or entity in this or any other proceeding.

were material and, consequently, Sirona filed publicly available redacted versions of the contracts with the Commission. The publicly disclosed versions of the contracts did not include the amounts of the MPRs.

5. From 2013 through 2016, the Exclusive Distributor provided Sirona, and later DSI, with detailed information about its inventory and, at times, retail sales of technology products. During that time, Sirona, and later DSI, worked closely with the Exclusive Distributor to manage inventory and to help it sell technology products to end users. As part of that process, the Exclusive Distributor provided Sirona, and later DSI, with detailed inventory and, at times, sales reports for each technology product for which it had exclusive distribution rights. That information was provided to certain DSI executives and other business leaders in summary form on a quarterly and annual basis.

6. By the end of the first quarter of 2016, DSI knew that the Exclusive Distributor carried large amounts of certain DSI inventory, and that the Exclusive Distributor's inventory levels were at all-time highs. DSI also knew that this large amount of inventory was likely to negatively impact DSI's sales to the Exclusive Distributor in future time periods. From 2013 through end of the first quarter 2016, inventory at the Exclusive Distributor increased by 163% from \$74 million to \$195 million, which included a \$26 million increase in the first quarter of 2016. Throughout the Relevant Period there was approximately \$85-\$100 million of excess inventory that had accumulated in the channel. In the first quarter of 2016, DSI's reported growth for its U.S. Region's sales would have been materially lower if the Exclusive Distributor had not been motivated by the MPRs to purchase additional excess inventory. Sirona, and later DSI, also knew that sales of certain products were not keeping pace with the Exclusive Distributor's purchases, and that the Exclusive Distributor's inventory of those products was increasing because it was buying more product from DSI than it could sell. By the end of the first quarter of 2016, DSI also understood that the Exclusive Distributor's efforts to boost retail sales with respect to an important product line had not materialized.

7. In the second quarter of 2016, the Exclusive Distributor informed DSI that it was no longer committed to achieving the MPRs. Instead, the Exclusive Distributor informed DSI that it wanted to renegotiate the exclusive agreements and reduce its excess inventory, which DSI knew would impact DSI's net sales in the United States absent other developments. The excess inventory that had accumulated in the channel represented 8%-10% of DSI's reported net sales for the second quarter of 2016. The Exclusive Distributor had the contractual right to maintain exclusivity by paying DSI a one-time fee in lieu of purchasing equipment.

8. In June 2016, DSI senior executives drafted a presentation to update DSI's Board on the developments with the Exclusive Distributor. The presentation acknowledged that the Exclusive Distributor held approximately seven to nine months of inventory of major DSI product lines and concluded that the "likely scenario" was that the Exclusive Distributor would miss the overall MPR target for 2016 and the "exclusivity period would contractually end [on] 9/30/17." The presentation also recognized that the MPRs – not end-user demand – were driving DSI sales, thereby highlighting that, with respect to one important product line, DSI's "[w]holesale performance [was] somewhat disconnected from retail due to the contractual requirement to

purchase 10% above 2011 base, compounded annually.” The DSI Board was told that, as a result, inventory had built in the channel, and the Exclusive Distributor “will likely significantly reduce purchases to burn inventory.”

9. Thus, by the end of the second quarter of 2016, DSI was aware of the large inventory build, retail sales trends not keeping pace with the wholesale growth rate in the contracts, and the resulting known uncertainties associated with those trends, concluding it was likely that the Exclusive Distributor would not achieve the MPRs in 2016, would not achieve automatic extension of contractual exclusivity beyond September 2017, and would sell off its excess inventory before the end of September 2017, thereby negatively impacting sales in future periods.

10. By the end of third quarter of 2016, based on the information provided by the Exclusive Distributor, DSI knew that the Exclusive Distributor held approximately five to eleven months of DSI inventory (depending on the product line), wanted to reduce its excess DSI inventory by at least \$60-\$80 million, and that there was uncertainty surrounding whether the Exclusive Distributor would renew the exclusive agreements. In fact, by the end of September 2016, DSI and the Exclusive Distributor entered into a “stand-still” agreement to give the Exclusive Distributor time to decide whether it would satisfy the contractual requirements necessary to extend exclusivity while the parties attempted to negotiate a solution that would minimize the effect of the inventory sell off on DSI’s future sales. The excess inventory in the channel represented 9% -10% of DSI’s reported net sales for the third quarter of 2016.

11. The expected negative impact to DSI’s sales from the Exclusive Distributor selling its excess DSI inventory began to come to fruition in the fourth quarter of 2016, and would continue to impact DSI in 2017. In late November 2016, the Exclusive Distributor publicly announced that it would not continue with exclusivity beyond September 2017. As a result, over the next several quarters, the Exclusive Distributor sold off much of the nearly \$85-\$100 million in excess inventory that had accumulated in the channel. The Exclusive Distributor’s sales of excess inventory materially reduced DSI’s reported net sales for its technologies segment and its reported net sales for the U.S. region in the fourth quarter of 2016 and the first two quarters of 2017. Additionally, DSI conducted its own internal analysis in mid-2017 to determine what its internal growth would have been for technologies had DSI not sold \$100 million in excess inventory to the Exclusive Distributor. DSI concluded that without the excess inventory added to the channel, its average growth rates for years 2014 through 2016 would have been materially lower. Reevaluating its estimated future growth rates contributed to the \$1.2 billion impairment DSI took to its goodwill associated with DSI’s technologies segment on August 9, 2017.

Required Disclosures and DSI’s Quarterly Filings

12. Item 303 of Regulation S-K sets forth the requirements for disclosure in the Management Discussion & Analysis (“MD&A”) section of their quarterly and annual filings. As the Commission has previously emphasized, the MD&A is an important disclosure tool that is designed to provide investors with a perspective on a company’s business “as seen through the eyes of those who manage that business” because “management has a unique perspective on its business that only it can present.” *Commission Guidance Regarding Management’s Discussion*

and Analysis of Financial Condition and Results from Operations, Securities Act Release No. 33-8350 (December 29, 2003) (the “2003 Guidance”). Item 303(a) of Regulation S-K requires issuers’ annual filings to include discussion and analysis of “material events and uncertainties known to management that would cause reported financial information not to be necessarily indicative of future operating results or of future financial condition.” See 17 C.F.R. § 229.303(a), Instruction 3. Item 303(b) of Regulation S-K requires that issuers report material changes to financial condition or results of operations between certain prior periods in a MD&A section in quarterly filings. See 17 C.F.R. § 229.303(b). Under Item 303 of Regulation S-K, “results of operations” includes “any known trends or uncertainties that have had or that the registrant reasonably expects will have a material favorable or unfavorable impact on net sales or revenues or income from continuing operations.”

13. The Commission has articulated a two-part test for determining whether a known trend or uncertainty requires disclosure under Item 303. “Where a trend, demand, commitment, event or uncertainty is known, management must make two assessments:

(1) Is the known trend, demand, commitment, event or uncertainty likely to come to fruition? If management determines that it is not reasonably likely to occur, no disclosure is required.

(2) If management cannot make that determination, it must evaluate objectively the consequences of the known trend, demand, commitment, event or uncertainty, on the assumption that it will come to fruition. Disclosure is then required unless management determines that a material effect on the registrant’s financial condition or results of operations is not reasonably likely to occur.”

SEC Interpretation: Management’s Discussion and Analysis of Financial Condition and Results of Operations; Certain Investment Company Disclosures, Securities Act Release No. 33-6835 (May 18, 1989). In its 2003 Interpretive Release, the Commission explained that “disclosure of a trend, demand, commitment, event or uncertainty is required unless a company is able to conclude either that it is not reasonably likely that the trend, uncertainty or other event will occur or come to fruition, or that a material effect on DSI’s results of operations is not reasonably likely to occur.” See the 2003 Guidance. In its 2002 Interpretive Release, the Commission explained that the “reasonably likely” standard for disclosures mandated by Item 303 is “lower than ‘more likely than not.’” *Commission Statement about Management’s Discussion and Analysis of Financial Condition and Results of Operations*, Securities Act Release No. 33-8056 (January 22, 2002) (emphasis added). The failure to comply with Regulation S-K constitutes a violation of Section 13(a) of the Exchange Act, and in this case, also constitutes a violation of Rules 12b-20 and 13a-13.

14. During the first three quarters of 2016, DSI failed to disclose known trends and uncertainties as required by Item 303. DSI maintained a Disclosure Committee that was tasked with reviewing Respondent’s financial disclosures for completeness and accuracy. The Disclosure Committee included key members of management who knew of the inventory build at the Exclusive Distributor and retail sales trends in the first quarter of 2016, and by the second quarter of 2016, the likely failure to achieve an automatic extension of a material agreement. The

Disclosure Committee reviewed DSI's quarterly reports for the first three quarters of 2016, but there is no evidence that the Committee considered whether those known trends and uncertainties needed to be disclosed as required by Item 303 of Regulation S-K. As a result, the Disclosure Committee approved DSI's Forms 10-Q for the first three quarters of 2016 with no disclosure of the known trends or uncertainties regarding its Exclusive Distributor that DSI reasonably expected would have a material unfavorable impact on net sales.

15. DSI failed to make required disclosures of trends and uncertainties regarding the Exclusive Distributor in DSI's Forms 10-Q for the first three quarters of 2016. DSI's Form 10-Q for the first quarter of 2016 reported "positive internal sales growth . . . led by the Technologies segment" in the United States driven by "increased demand" in the U.S. This statement did not also explain that internal sales growth in the U.S. was driven by the Exclusive Distributor's desire to maintain exclusivity rather than end-user market demand alone, and the resulting inventory build at its Exclusive Distributor would likely materially impact future revenue growth.

16. DSI's Form 10-Q for the second quarter of 2016 reported "positive internal sales growth" in the technologies segment in the United States. This statement did not also explain that future sales may be negatively impacted by flat retail sales, high inventory at the Exclusive Distributor, and contract negotiations with the Exclusive Distributor that could impact sales.

17. In its Form 10-Q for the third quarter of 2016, DSI reported that the technologies segment in the United States "generated . . . positive internal sales growth . . . as a result of higher demand in this region." It also reported that "[i]nternal sales growth was positive in [the U.S.] region[] . . . and was the result of higher demand." These statements did not also explain that internal sales growth in the U.S. was driven by its Exclusive Distributor's desire to maintain exclusivity rather than end-user market demand alone, and the resulting inventory build at its Exclusive Distributor would likely impact future revenue growth, especially given the uncertainty surrounding the likely non-extension of the previously disclosed material contracts.

Violations

18. As a result of the conduct described above, DSI violated Section 13(a) of the Exchange Act and Rules 12b-20 and 13a-13 thereunder, which require every issuer of a security registered pursuant to Section 12 of the Exchange Act file with the Commission information, documents, and quarterly reports as the Commission may require, and mandate that periodic reports contain such further material information as may be necessary to make the required statements not misleading.

IV.

In view of the foregoing, the Commission deems it appropriate to impose the sanctions agreed to in Respondent's Offer.

Accordingly, it is hereby ORDERED that:

A. Pursuant to Section 21C of the Exchange Act, Respondent cease and desist from committing or causing any violations and any future violations of Section 13(a) of the Exchange Act and Rules 12b-20 and 13a-13 thereunder.

B. Respondent shall, within 14 days of the entry of this Order, pay a civil money penalty in the amount of \$1,000,000 to the Securities and Exchange Commission for transfer to the general fund of the United States Treasury, subject to Exchange Act Section 21F(g)(3). If timely payment is not made, additional interest shall accrue pursuant to 31 U.S.C. §3717.

Payment must be made in one of the following ways:

- (1) Respondent may transmit payment electronically to the Commission, which will provide detailed ACH transfer/Fedwire instructions upon request;
- (2) Respondent may make direct payment from a bank account via Pay.gov through the SEC website at <http://www.sec.gov/about/offices/ofm.htm>; or
- (3) Respondent may pay by certified check, bank cashier's check, or United States postal money order, made payable to the Securities and Exchange Commission and hand-delivered or mailed to:

Enterprise Services Center
Accounts Receivable Branch
HQ Bldg., Room 181, AMZ-341
6500 South MacArthur Boulevard
Oklahoma City, OK 73169

Payments by check or money order must be accompanied by a cover letter identifying DSI as a Respondent in these proceedings, and the file number of these proceedings; a copy of the cover letter and check or money order must be sent to Jason Burt, Division of Enforcement, Securities and Exchange Commission, 1961 Stout St., Denver, CO 80294-1961.

N. Amounts ordered to be paid as civil money penalties pursuant to this Order shall be treated as penalties paid to the government for all purposes, including all tax purposes. To preserve the deterrent effect of the civil penalty, Respondent agrees that in any Related Investor Action, it shall not argue that it is entitled to, nor shall it benefit by, offset or reduction of any award of compensatory damages by the amount of any part of Respondent's payment of a civil penalty in this action ("Penalty Offset"). If the court in any Related Investor Action grants such a Penalty Offset, Respondent agrees that it shall, within 30 days after entry of a final order granting the Penalty Offset, notify the Commission's counsel in this action and pay the amount of the Penalty Offset to the Securities and Exchange Commission. Such a payment shall not be deemed an additional civil penalty and shall not be deemed to change the amount of the civil penalty imposed in this proceeding. For purposes of this paragraph, a "Related Investor Action" means a private damages action brought against Respondent by or on behalf of one or more investors based

on substantially the same facts as alleged in the Order instituted by the Commission in this proceeding.

By the Commission.

Vanessa A. Countryman
Secretary