W R GRACE & CO
Form 10-Q
May 05, 2016

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549
FORM 10-Q

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

For the Quarterly Period Ended March 31, 2016
OR

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

Commission File Number 1-13953
W. R. GRACE & CO.
(Exact name of registrant as specified in its charter)

Delaware	65-0773649
(State of incorporation)	(I.R.S. Employer Identification No.)

7500 Grace Drive, Columbia, Maryland 21044-4098
(Address of principal executive offices) (Zip code)
(410) 531-4000
(Registrant's telephone number, including area code)

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

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

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

Large accelerated filer ý	Accelerated filer o	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 ý

Indicate by check mark whether the registrant has filed all documents and reports required to be filed by Sections 12, 13 or 15(d) of the Securities Exchange Act of 1934 subsequent to the distribution of securities under a plan confirmed by a court. Yes ý No o

Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date.

Class	Outstanding at April 30, 2016
Common Stock, $0.01 par value per share	70,503,825 shares

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Unless otherwise indicated, in this Report the terms "Grace," "we," "us," "our" or "the Company" mean W. R. Grace & Co. and/or its consolidated subsidiaries and affiliates. Unless otherwise indicated, the contents of websites mentioned in this report are not incorporated by reference or otherwise made a part of this Report. GRACE®, the GRACE® logo and, except as otherwise indicated, the other trademarks, service marks or trade names used in the text of this Report are trademarks, service marks, or trade names of operating units of W. R. Grace & Co. or its affiliates and/or subsidiaries.

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PART I. FINANCIAL INFORMATION

Item 1. Financial Statements

Review by Independent Registered Public Accounting Firm

With respect to the interim consolidated financial statements included in this Quarterly Report on Form 10-Q for the quarter ended March 31, 2016, PricewaterhouseCoopers LLP, the Company's independent registered public accounting firm, has applied limited procedures in accordance with professional standards for a review of such information. Their report on the interim consolidated financial statements, which follows, states that they did not audit and they do not express an opinion on the unaudited interim consolidated financial statements. Accordingly, the degree of reliance on their report on the unaudited interim consolidated financial statements should be restricted in light of the limited nature of the review procedures applied. This report is not considered a "report" within the meaning of Sections 7 and 11 of the Securities Act of 1933, and, therefore, the independent accountants' liability under Section 11 does not extend to it.

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Report of Independent Registered Public Accounting Firm
To the Shareholders and Board of Directors of W. R. Grace & Co.:

We have reviewed the accompanying consolidated balance sheet of W. R. Grace & Co. and its subsidiaries as of March 31, 2016, and the related consolidated statements of operations, comprehensive income (loss), cash flows and equity for the three-month periods ended March 31, 2016 and 2015. These interim financial statements are the responsibility of the Company's management.

We conducted our review in accordance with the standards of the Public Company Accounting Oversight Board (United States). A review of interim financial information consists principally of applying analytical procedures and making inquiries of persons responsible for financial and accounting matters. It is substantially less in scope than an audit conducted in accordance with the standards of the Public Company Accounting Oversight Board (United States), the objective of which is the expression of an opinion regarding the financial statements taken as a whole. Accordingly, we do not express such an opinion.

Based on our review, we are not aware of any material modifications that should be made to the accompanying consolidated interim financial statements for them to be in conformity with accounting principles generally accepted in the United States of America.

We previously audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the consolidated balance sheet as of December 31, 2015, and the related consolidated statement of operations, comprehensive income, equity, and of cash flows for the year then ended (not presented herein), and in our report dated February 25, 2016, which included a paragraph that described the change in classification of deferred taxes on the consolidated balance sheet, we expressed an unqualified opinion on those consolidated financial statements. In our opinion, the information set forth in the accompanying consolidated balance sheet as of December 31, 2015, is fairly stated in all material respects in relation to the consolidated balance sheet from which it has been derived.

/s/ PricewaterhouseCoopers LLP
Baltimore, Maryland
May 5, 2016

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W. R. Grace & Co. and Subsidiaries
Consolidated Statements of Operations (unaudited)

	Three Months Ended March 31,	
(In millions, except per share amounts)	2016	2015
Net sales	$362.8	$397.0
Cost of goods sold	210.1	250.0
Gross profit	152.7	147.0
Selling, general and administrative expenses	68.0	77.0
Research and development expenses	11.7	12.1
Interest expense and related financing costs	22.0	24.7
Repositioning expenses	5.1	0.3
Equity in earnings of unconsolidated affiliate	(6.9)	(6.2)
Loss on early extinguishment of debt	11.1	—
Other expense (income), net	10.3	(8.6)
Total costs and expenses	121.3	99.3
Income from continuing operations before income taxes	31.4	47.7
Provision for income taxes	(24.4)	(17.5)
Income from continuing operations	7.0	30.2
(Loss) income from discontinued operations, net of income taxes	(9.9)	22.5
Net (loss) income	(2.9)	52.7
Less: Net loss attributable to noncontrolling interests	0.2	—
Net (loss) income attributable to W. R. Grace & Co. shareholders	$(2.7)	$52.7
Amounts Attributable to W. R. Grace & Co. Shareholders:		
Income from continuing operations attributable to W. R. Grace & Co. shareholders	$7.2	$30.2
(Loss) income from discontinued operations, net of income taxes	(9.9)	22.5
Net (loss) income attributable to W. R. Grace & Co. shareholders	$(2.7)	$52.7
Earnings Per Share Attributable to W. R. Grace & Co. Shareholders		
Basic earnings per share:		
Income from continuing operations	$0.10	$0.41
(Loss) income from discontinued operations, net of income taxes	(0.14)	0.31
Net (loss) income	$(0.04)	$0.72
Weighted average number of basic shares	70.6	72.8
Diluted earnings per share:		
Income from continuing operations	$0.10	$0.41
(Loss) Income from discontinued operations, net of income taxes	(0.14)	0.31
Net (loss) income	$(0.04)	$0.72
Weighted average number of diluted shares	70.6	73.5

The Notes to Consolidated Financial Statements are an integral part of these statements.

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W. R. Grace & Co. and Subsidiaries
Consolidated Statements of Comprehensive (Loss) Income (unaudited)

(In millions)	Three Months Ended March 31, 2016	2015
Net (loss) income	$(2.9)	$52.7
Other comprehensive (loss) income:		
Defined benefit pension and other postretirement plans, net of income taxes	(0.3)	(0.4)
Currency translation adjustments	(5.4)	(10.8)
Loss from hedging activities, net of income taxes	(3.0)	(1.9)
Total other comprehensive income attributable to noncontrolling interests	2.6	0.1
Total other comprehensive loss	(6.1)	(13.0)
Comprehensive (loss) income	(9.0)	39.7
Less: comprehensive income attributable to noncontrolling interests	(2.4)	(0.1)
Comprehensive (loss) income attributable to W. R. Grace & Co. shareholders	$(11.4)	$39.6

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W. R. Grace & Co. and Subsidiaries
Consolidated Statements of Cash Flows (unaudited)

(In millions)	Three Months Ended March 31, 2016	2015
OPERATING ACTIVITIES		
Net (loss) income	$(2.9)	$52.7
Less: loss (income) from discontinued operations	9.9	(22.5)
Income from continuing operations	7.0	30.2
Reconciliation to net cash provided by (used for) operating activities from continuing operations:		
Depreciation and amortization	23.2	25.2
Equity in earnings of unconsolidated affiliate	(6.9)	(6.2)
Dividends received from unconsolidated affiliate	10.0	—
Cash paid for Chapter 11 and asbestos	(1.1)	(491.4)
Provision for income taxes	24.4	17.5
Cash paid for income taxes, net of refunds	(17.2)	3.1
Loss on early extinguishment of debt	11.1	—
Cash paid for interest on credit arrangements	(9.5)	(16.5)
Defined benefit pension expense	2.9	9.5
Cash paid under defined benefit pension arrangements	(3.7)	(3.9)
Cash paid for restructuring	(4.5)	(0.6)
Cash paid for environmental remediation	(1.4)	(4.2)
Changes in assets and liabilities, excluding effect of currency translation:		
Trade accounts receivable	44.3	16.3
Inventories	(10.6)	(3.1)
Accounts payable	11.1	16.8
All other items, net	(9.5)	24.7
Net cash provided by (used for) operating activities from continuing operations	69.6	(382.6)
INVESTING ACTIVITIES		
Capital expenditures	(34.4)	(33.0)
Other investing activities	0.3	—
Net cash used for investing activities from continuing operations	(34.1)	(33.0)
FINANCING ACTIVITIES		
Borrowings under credit arrangements	9.1	261.2
Repayments under credit arrangements	(605.1)	(9.3)
Cash paid for debt financing costs	(0.1)	(0.4)
Cash paid for repurchases of common stock	(15.0)	(55.6)
Proceeds from exercise of stock options	3.8	13.7
Other financing activities	2.4	(1.6)
Distribution from GCP	750.0	—
Net cash provided by financing activities from continuing operations	145.1	208.0
Effect of currency exchange rate changes on cash and cash equivalents	2.6	(2.1)
Increase (decrease) in cash and cash equivalents from continuing operations	183.2	(209.7)
Cash flows from discontinued operations		
Net cash provided by operating activities	23.9	9.0
Net cash used for investing activities	(9.5)	(7.6)
Net cash provided by (used in) financing activities	31.4	(9.2)
Effect of currency exchange rate changes on cash and cash equivalents	(1.0)	(13.2)

Increase (decrease) in cash and cash equivalents from discontinued operations	44.8	(21.0)
Net increase (decrease) in cash and cash equivalents	228.0	(230.7)
Less: cash and cash equivalents of discontinued operations	(143.4)	—
Cash and cash equivalents, beginning of period	329.9	557.5
Cash and cash equivalents, end of period	$414.5	$326.8
Supplemental disclosure of cash flow information		
Net share settled stock option exercises	$10.0	$—

The Notes to Consolidated Financial Statements are an integral part of these statements.

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W. R. Grace & Co. and Subsidiaries
Consolidated Balance Sheets (unaudited)

(In millions, except par value and shares)	March 31, 2016	December 31, 2015
ASSETS		
Current Assets		
Cash and cash equivalents	$414.5	$ 231.3
Restricted cash and cash equivalents	9.4	9.4
Trade accounts receivable, less allowance of $1.8 (2015—$1.4)	209.1	254.5
Inventories	211.8	198.8
Other current assets	49.1	44.1
Assets of discontinued operations	—	446.4
Total Current Assets	893.9	1,184.5
Properties and equipment, net of accumulated depreciation and amortization of $1,306.3 (2015—$1,316.4)	627.4	645.3
Goodwill	336.6	336.5
Technology and other intangible assets, net	224.2	227.5
Deferred income taxes	664.0	723.1
Investment in unconsolidated affiliate	110.6	103.2
Other assets	31.7	33.9
Assets of discontinued operations	—	391.7
Total Assets	$2,888.4	$ 3,645.7
LIABILITIES AND EQUITY		
Current Liabilities		
Debt payable within one year	$78.9	$ 58.8
Accounts payable	159.8	157.8
Other current liabilities	226.1	234.4
Liabilities of discontinued operations	—	256.4
Total Current Liabilities	464.8	707.4
Debt payable after one year	1,507.7	2,114.0
Deferred income taxes	3.9	1.2
Unrecognized tax benefits	10.0	9.8
Underfunded and unfunded defined benefit pension plans	381.9	377.5
Other liabilities	125.3	115.9
Liabilities of discontinued operations	—	107.4
Total Liabilities	2,493.6	3,433.2
Commitments and Contingencies—Note 8		
Equity		
Common stock issued, par value $0.01; 300,000,000 shares authorized; outstanding: 70,533,749 (2015—70,533,515)	0.7	0.7
Paid-in capital	495.0	496.0
Retained earnings	490.9	436.3
Treasury stock, at cost: shares: 6,922,876 (2015—6,923,110)	(655.0)	(658.4)
Accumulated other comprehensive income (loss)	59.8	(66.8)
Total W. R. Grace & Co. Shareholders' Equity	391.4	207.8
Noncontrolling interests	3.4	4.7
Total Equity	394.8	212.5
Total Liabilities and Equity	$2,888.4	$ 3,645.7

The Notes to Consolidated Financial Statements are an integral part of these statements.

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W. R. Grace & Co. and Subsidiaries
Consolidated Statements of Equity (unaudited)

(In millions)	Common Stock and Paid-in Capital	Retained Earnings	Treasury Stock	Accumulated Other Comprehensive Income (Loss)	Noncontrolling Interests	Total Equity
Balance, December 31, 2014	$ 526.8	$ 292.1	$ (429.2)	$ (23.8)	$ 3.1	$ 369.0
Net income	—	52.7	—	—	—	52.7
Repurchase of common stock	—	—	(55.6)	—	—	(55.6)
Stock based compensation	1.3	—	—	—	—	1.3
Exercise of stock options	(28.9)	—	42.6	—	—	13.7
Other comprehensive income (loss)	—	—	—	(13.1)	0.1	(13.0)
Balance, March 31, 2015	$ 499.2	$ 344.8	$ (442.2)	$ (36.9)	$ 3.2	$ 368.1
Balance, December 31, 2015	$ 496.7	$ 436.3	$ (658.4)	$ (66.8)	$ 4.7	$ 212.5
Net loss	—	(2.7)	—	—	(0.2)	(2.9)
Repurchase of common stock	—	—	(15.0)	—	—	(15.0)
Stock based compensation	3.6	—	—	—	—	3.6
Exercise of stock options	(4.6)	—	18.4	—	—	13.8
Other comprehensive income (loss)	—	—	—	(8.7)	2.6	(6.1)
Distribution of GCP	—	57.3	—	135.3	(3.7)	188.9
Balance, March 31, 2016	$ 495.7	$ 490.9	$ (655.0)	$ 59.8	$ 3.4	$ 394.8

The Notes to Consolidated Financial Statements are an integral part of these statements.

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Notes to Consolidated Financial Statements

1. Basis of Presentation and Summary of Significant Accounting and Financial Reporting Policies

W. R. Grace & Co., through its subsidiaries, is engaged in specialty chemicals and specialty materials businesses on a global basis through two reportable segments: Grace Catalysts Technologies, which includes catalysts and related products and technologies used in refining, petrochemical and other chemical manufacturing applications, and Grace Materials Technologies, which includes engineered materials used in consumer, industrial, coatings, and pharmaceutical applications.

W. R. Grace & Co. conducts all of its business through a single wholly owned subsidiary, W. R. Grace & Co.–Conn. ("Grace–Conn."). Grace–Conn. owns all of the assets, properties and rights of W. R. Grace & Co. on a consolidated basis, either directly or through subsidiaries.

As used in these notes, the term "Company" refers to W. R. Grace & Co. The term "Grace" refers to the Company and/or one or more of its subsidiaries and, in certain cases, their respective predecessors.

Separation Transaction   On February 5, 2015, Grace announced a plan to separate into two independent, publicly traded companies, intended to improve Grace's strategic focus, simplify its operating structure, and allow for more efficient capital allocation. On January 27, 2016, Grace entered into a separation agreement with GCP Applied Technologies Inc., then a wholly-owned subsidiary of Grace ("GCP"), pursuant to which Grace agreed to transfer its Grace Construction Products operating segment and the packaging technologies business of its Grace Materials Technologies operating segment to GCP (the "Separation"). The Separation occurred on February 3, 2016 (the "Distribution Date"), by means of a pro rata distribution to Grace stockholders of all of the outstanding shares of GCP common stock (the "Distribution"). Under the Distribution, one share of GCP common stock was distributed for each share of Grace common stock held as of the close of business on January 27, 2016. As a result of the Distribution, GCP is now an independent public company and its common stock is listed under the symbol “GCP” on the New York Stock Exchange. GCP’s historical financial results through the Distribution Date are reflected in Grace’s Consolidated Financial Statements as discontinued operations.

Basis of Presentation   The interim Consolidated Financial Statements presented herein are unaudited and should be read in conjunction with the Consolidated Financial Statements presented in the Company's 2015 Annual Report on Form 10-K. Such interim Consolidated Financial Statements reflect all adjustments that, in the opinion of management, are necessary for a fair statement of the results of the interim periods presented; all such adjustments are of a normal recurring nature except for the impacts of adopting new accounting standards as discussed below. All significant intercompany accounts and transactions have been eliminated.

The results of operations for the three-month interim period ended March 31, 2016, are not necessarily indicative of the results of operations for the year ending December 31, 2016.

Use of Estimates   The preparation of financial statements in conformity with U.S. generally accepted accounting principles ("U.S. GAAP") requires management to make estimates and assumptions that affect the reported amount of assets and liabilities and disclosure of contingent assets and liabilities at the date of the Consolidated Financial Statements, and the reported amounts of revenues and expenses for the periods presented. Actual amounts could differ from those estimates, and the differences could be material. Changes in estimates are recorded in the period identified. Grace's accounting measurements that are most affected by management's estimates of future events are:

- Realization values of net deferred tax assets, which depend on projections of future taxable income (see Note 5);
- Pension and postretirement liabilities that depend on assumptions regarding participant life spans, future inflation, discount rates and total returns on invested funds (see Note 6); and
- Contingent liabilities, which depend on an assessment of the probability of loss and an estimate of ultimate obligation, such as litigation (see Note 8), income taxes (see Note 5), and environmental remediation (see Note 8).

Reclassifications   Certain amounts in prior years' Consolidated Financial Statements have been reclassified to conform to the current year presentation. Such reclassifications have not materially affected previously reported amounts in the Consolidated Financial Statements.

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Notes to Consolidated Financial Statements (Continued)

1. Basis of Presentation and Summary of Significant Accounting and Financial Reporting Policies (Continued)

Effect of New Accounting Standards In April 2014, the FASB issued ASU 2014-08 "Reporting Discontinued Operations and Disclosures of Disposals of Components of an Entity." This update is intended to change the requirements for reporting discontinued operations and enhance convergence of the FASB's and the International Accounting Standard Board's ("IASB") reporting requirements for discontinued operations. Grace adopted this standard in the first quarter.

In May 2014, the FASB issued ASU 2014-09 "Revenue from Contracts with Customers." This update is intended to remove inconsistencies and weaknesses in revenue requirements; provide a more robust framework for addressing revenue issues; improve comparability of revenue recognition practices across entities, industries, jurisdictions and capital markets; provide more useful information to users of financial statements through improved disclosure requirements; and simplify the preparation of financial statements by reducing the number of requirements to which an entity must refer. The new requirements were to be effective for fiscal years beginning after December 15, 2016, and for interim periods within those fiscal years, with early adoption not permitted. In August 2015, the FASB issued ASU 2015-14 "Revenue from Contracts with Customers—Deferral of the Effective Date," deferring the effective date by one year but permitting adoption as of the original effective date. The revised standard allows for two methods of adoption: (a) full retrospective adoption, meaning the standard is applied to all periods presented, or (b) modified retrospective adoption, meaning the cumulative effect of applying the new standard is recognized as an adjustment to the opening retained earnings balance. Grace does not intend to adopt the standard early and is in the process of determining the adoption method as well as the effects the adoption will have on the Consolidated Financial Statements.

In April 2015, the FASB issued ASU 2015-03 "Simplifying the Presentation of Debt Issuance Costs." This update is part of the FASB's Simplification Initiative and is also intended to enhance convergence with the IASB's treatment of debt issuance costs. The update requires that debt issuance costs related to a recognized debt liability be presented in the balance sheet as a direct deduction from the carrying amount of that debt liability, consistent with debt discounts.

In August 2015, the FASB issued ASU 2015-15 "Presentation and Subsequent Measurement of Debt Issuance Costs Associated with Line-of-Credit Arrangements." The update clarifies ASU 2015-03, allowing debt issuance costs related to line of credit arrangements to be deferred and presented as an asset and subsequently amortized ratably over the term of the line-of-credit arrangement, regardless of whether there are any outstanding borrowings on the line-of-credit arrangement. The new requirements are effective for fiscal years beginning after December 15, 2015, and for interim periods within those fiscal years, with early adoption permitted. Grace adopted this standard in the 2016 first quarter and reclassified $30.3 million of capitalized financing fees from other assets to debt payable after one year in the Consolidated Balance Sheet as of December 31, 2015.

In July 2015, the FASB issued ASU 2015-11 "Simplifying the Measurement of Inventory." This update is part of the FASB's Simplification Initiative and is also intended to enhance convergence with the IASB's measurement of inventory. The update requires that inventory be measured at the lower of cost or net realizable value for entities using FIFO or average cost methods. The new requirements are effective for fiscal years beginning after December 15, 2016, and for interim periods within those fiscal years, with early adoption permitted. Grace is currently evaluating the timing of adoption and does not expect the update to have an effect on the Consolidated Financial Statements.

In February 2016, the FASB issued ASU 2016-02 "Leases." This update is intended to increase transparency and comparability among organizations by recognizing lease assets and lease liabilities on the balance sheet and disclosing key information about leasing arrangements. The core principle of Topic 842 is that a lessee should recognize the assets and liabilities that arise from leases. A lessee should recognize in the statement of financial position a liability to make lease payments (the lease liability) and a right-of-use asset representing its right to use the underlying asset for the lease term, including optional payments where they are reasonably certain to occur. The amendments in this update are effective for fiscal years beginning after December 15, 2018, including interim periods within those fiscal years, with early adoption permitted. Grace is currently evaluating its effect on the financial statements and the timing of adoption.

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Notes to Consolidated Financial Statements (Continued)

1. Basis of Presentation and Summary of Significant Accounting and Financial Reporting Policies (Continued)

In March 2016, the FASB issued ASU 2016-09 “Compensation—Stock Compensation." This update is part of the FASB's Simplification Initiative. The areas for simplification in this update involve several aspects of the accounting for share-based payment transactions, including the income tax consequences, classification of awards as either equity or liabilities, and classification on the statement of cash flows. The amendments in this update are effective for annual periods beginning after December 15, 2016, and interim periods within those annual periods, with early adoption permitted. Grace is currently evaluating its effect on the financial statements and the timing of adoption.

2. Inventories

Inventories are stated at the lower of cost or market, and cost is determined using FIFO. Inventories consisted of the following at March 31, 2016, and December 31, 2015:

(In millions)	March 31, 2016	December 31, 2015
Raw materials	$ 49.6	$ 47.1
In process	38.4	33.4
Finished products	102.9	98.2
Other	20.9	20.1
	$ 211.8	$ 198.8

3. Debt

Components of Debt

(In millions)	March 31, 2016	December 31, 2015
5.125% senior notes due 2021, net of unamortized debt issuance costs of $8.6 at March 31, 2016 (2015—$8.9)	$ 691.4	$ 691.1
U.S. dollar term loan, net of unamortized debt issuance costs and discounts of $6.9 at March 31, 2016 (2015—$15.6)	401.5	919.3
5.625% senior notes due 2024, net of unamortized debt issuance costs of $4.4 at March 31, 2016 (2015—$4.5)	295.6	295.5
Euro term loan, net of unamortized debt issuance costs and discounts of $1.5 at March 31, 2016 (2015—$3.4)	88.3	158.7
Debt payable—unconsolidated affiliate	35.5	33.4
Deferred payment obligation	29.3	29.1
Other borrowings(1)	45.0	45.7
Total debt	1,586.6	2,172.8
Less debt payable within one year	78.9	58.8
Debt payable after one year	$ 1,507.7	$