

Polymer Holdings LLC
Form 10-Q
November 14, 2005

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

(Mark One)

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

For the quarterly period ended September 30, 2005

OR

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

For the transition period from

to

Polymer Holdings LLC

(Exact name of registrant as specified in its charter)

Commission file number 333-123749

Delaware

(State or other jurisdiction of
incorporation)

20-0411521

(I.R.S. Employer Identification No.)

**700 Milam Street, 13th Floor, North Tower
Houston, TX 77002**

(Address of principal executive offices,
including zip code)

832-204-5400

(Registrant's telephone number, including area code)

KRATON Polymers LLC

(Exact name of registrant as specified in its charter)

Commission file number 333-123747

Delaware

(State or other jurisdiction of
incorporation or organization)

94-2805249

(I.R.S. Employer Identification No.)

**700 Milam Street, 13th Floor, North Tower
Houston, TX 77002**

(Address of principal executive offices,
including zip code)

832-204-5400

(Registrant's telephone number, including area code)

Indicated by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.

YES NO

Indicate by check mark whether the registrant is an accelerated filer (as defined in Rule 12b-2 of the Exchange Act). YES NO

Indicate by check mark whether the registrant is a shell company as defined in Rule 12b-2 of the Exchange Act. YES NO

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Item 6. Exhibits

Option Grant Agreement - TJ Chemical and Steven Demetriou

Option Grant Agreement - TJ Chemical and James Ball

Employment Agreement - KRATON and Kevin M. Fogarty

Option Grant Agreement - TJ Chemical and Raymond K. Guba

Profit Unit Award Agreement - KRATON Management LLC and Raymond K. Guba

Notional Unit Award Grant Agreement - KRATON and Raymond K. Guba

Certification of CEO pursuant to Section 302

Certification of Interim CFO pursuant to Section 302

Certification of CFO pursuant to Section 302

Certification of CEO and CFO pursuant to Section 906

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FORWARD LOOKING STATEMENTS

This Quarterly Report on Form 10-Q includes forward-looking statements, as that term is defined in Section 27A of the Securities Act of 1933 and Section 21E of the Securities Exchange Act of 1934. All statements, other than statements of historical fact, included or incorporated in this Form 10-Q are forward-looking statements, particularly statements about our plans, strategies and prospects under the headings Consolidated Financial Statements and Management's Discussion and Analysis of Financial Condition and Results of Operations. We may also make written or oral forward-looking statements in our Annual Report on Form 10-K, periodic reports on Form 10-Q and current reports on Form 8-K, in press releases and other written materials and in oral statements made by our officers, directors or employees to third parties. Such forward-looking statements involve known and unknown risks, uncertainties and other important factors that could cause the actual results, performance or our achievements, or industry results, to differ materially from historical results, any future results, performance or achievements expressed or implied by such forward-looking statements. Such risks and uncertainties include, but are not limited to, competitive pressures in the specialty chemicals industry, changes in prices of raw materials used in our business, changes in levels of consumer spending or preferences, overall economic conditions, the level of our indebtedness and exposure to interest rate fluctuations, governmental regulations and trade restrictions, acts of war or terrorism in the United States or worldwide, political or financial instability in the countries where our goods are manufactured and other risks and uncertainties described in this report and our other reports and documents. These statements are based on current plans, estimates and projections, and therefore you should not place undue reliance on them. Forward-looking statements speak only as of the date they are made, and we undertake no obligation to update publicly any of them in light of new information or future events.

PRESENTATION OF FINANCIAL STATEMENTS

This Form 10-Q includes financial statements and related notes that present (1) the consolidated financial position, results of operations and cash flows of Polymer Holdings LLC, which we refer to as Polymer Holdings, and its subsidiaries and (2) the consolidated financial position, results of operations and cash flows of KRATON Polymers LLC, which we refer to as KRATON, and its subsidiaries. Polymer Holdings is a holding company whose only material asset is its investment in KRATON, which is its wholly-owned subsidiary. KRATON and its subsidiaries own all of the consolidated operating assets.

Table of Contents**PART I Financial Information****ITEM 1. CONSOLIDATED FINANCIAL STATEMENTS**

Polymer Holdings LLC
 Consolidated Balance Sheets
 September 30, 2005 and December 31, 2004
 (in thousands of U.S. dollars)

	September 30, 2005 (Unaudited)	December 31, 2004 (Restated See note 1(c))
Assets		
Current assets:		
Cash and cash equivalents	\$ 71,550	\$ 46,357
Receivables, net of allowances of \$884 and \$750	150,612	120,596
Inventories of products	191,303	211,076
Inventories of materials and supplies	9,412	8,778
Other current assets	17,495	10,381
Total current assets	440,372	397,188
Property, plant, and equipment, less accumulated depreciation of \$57,654 and \$38,086	395,453	424,333
Identifiable intangible assets, less accumulated amortization of \$13,887 and \$8,002	103,809	109,694
Investment in joint venture	10,539	10,753
Deferred financing costs	14,999	16,799
Other long-term assets	9,014	8,646
Total assets	\$ 974,186	\$ 967,413
Liabilities and Member s Equity		
Current liabilities:		
Current portion of long-term debt	\$ 2,680	\$ 2,680
Accounts payable trade	64,853	79,968
Other payables and accruals	50,269	40,059
Due to related parties	11,937	14,471
Deferred income taxes	1,240	1,240
Insurance bond payable	1,380	
Total current liabilities	132,359	138,418
Long-term debt, net of current portion	562,970	556,335
Deferred income taxes	27,020	24,513
Long-term liabilities	29,317	25,629
Total liabilities	751,666	744,895
Commitments and contingencies (note 5)		
Member s equity:		

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Common equity	219,779	200,528
Accumulated other comprehensive income	2,741	21,990
Total member s equity	222,520	222,518
Total liabilities and member s equity	\$ 974,186	\$ 967,413

See accompanying notes to consolidated financial statements.

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Polymer Holdings LLC
 Consolidated Statements of Operations
 Three Months Ended September 30, 2005 and 2004
 (in thousands of U.S. dollars)
 (Unaudited)

	September 30, 2005	September 30, 2004 (Restated See note 1(c))
Revenues		
Sales	\$ 269,017	\$ 209,407
Other	7,457	1,840
Total revenues	276,474	211,247
Costs and expense		
Costs of goods sold	225,945	179,186
Gross profit	50,529	32,061
Research and development expenses	6,700	5,530
Selling, general, and administrative expenses	19,130	16,467
Depreciation and amortization of identifiable intangibles	11,548	11,185
Earnings in joint venture	(182)	11
Interest, net	11,746	11,722
Income (loss) before income taxes	1,587	(12,854)
Income tax (provision) benefit	(633)	6,848
Net income (loss)	\$ 954	\$ (6,006)

See accompanying notes to consolidated financial statements.

Polymer Holdings LLC
 Consolidated Statements of Operations
 Nine Months Ended September 30, 2005 and 2004
 (in thousand of U.S. dollars)
 (Unaudited)

	September 30, 2005	September 30, 2004 (Restated See note 1(c))
Revenues		
Sales	\$ 732,338	\$ 589,886
Other	20,287	8,738
Total revenues	752,625	598,624

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Costs and expense		
Costs of goods sold	586,145	514,692
Gross profit	166,480	83,932
Research and development expenses	19,500	17,246
Selling, general, and administrative expenses	54,692	46,503
Depreciation and amortization of identifiable intangibles	33,760	31,849
Earnings in joint venture	(1,050)	(134)
Interest, net	34,578	27,719
Income (loss) before income taxes	25,000	(39,251)
Income tax (provision) benefit	(6,159)	15,332
Net income (loss)	\$ 18,841	\$ (23,919)

See accompanying notes to consolidated financial statements.

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Polymer Holdings LLC
Consolidated Statements of Cash Flows
Nine Months Ended September 30, 2005 and 2004
(in thousands of U.S. dollars)
(Unaudited)

	September 30, 2005	September 30, 2004 (Restated See note 1(c))
Cash flows provided by (used in) operating activities:		
Net income (loss)	\$ 18,841	\$ (23,919)
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization of identifiable intangibles	33,760	31,849
Amortization of deferred financing costs	1,800	2,522
Accretion of discount on senior subordinated notes	8,645	
Change in the fair value of interest rate swaps	(128)	1,669
Loss on disposal of fixed assets	55	637
(Undistributed) distributed earnings in joint venture	(589)	427
Deferred tax provision (benefit)	483	(17,053)
Non-cash compensation	410	
Increase (decrease) in working capital:		
Accounts receivable	(43,567)	(27,426)
Due from related party	351	
Inventories	5,373	49,530
Other assets	(6,274)	(6,330)
Accounts payable, other payables and accruals, and long-term Liabilities	10,004	45,877
Net cash provided by operating activities	29,164	57,783
Cash flows (used in) provided by investing activities:		
Purchase of property, plant and equipment	(8,604)	(28,816)
Proceeds from sale of property, plant and equipment	122	88
Net cash used in investing activities	(8,482)	(28,728)
Cash flows (used in) provided by financing activities:		
Repayment of debt	(2,010)	(17,787)
Net proceeds from insurance bond	1,380	
Net cash used in by financing activities	(630)	(17,787)
Effect of exchange rate differences on cash	5,141	138
Net increase in cash and cash equivalents	25,193	11,406
Cash and cash equivalents, beginning of period	46,357	17,500

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Cash and cash equivalents, end of period	\$	71,550	\$	28,906
Supplemental disclosure cash flow information:				
Cash paid during the period for income taxes, net of refunds received	\$	1,058	\$	4,547
Cash paid during the period for interest		28,821		20,910

See accompanying notes to consolidated financial statements.

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KRATON Polymers LLC
 Consolidated Balance Sheets
 September 30, 2005 and December 31, 2004
 (in thousands of U.S. dollars)

	September 30, 2005 (Unaudited)	December 31, 2004 (Restated See note 1(c))
Assets		
Current assets:		
Cash and cash equivalents	\$ 71,550	\$ 46,357
Receivables, net of allowances of \$884 and \$750	150,612	120,596
Inventories of products	191,303	211,076
Inventories of materials and supplies	9,412	8,778
Other current assets	17,495	10,381
Total current assets	440,372	397,188
Property, plant, and equipment, less accumulated depreciation of \$57,654 and \$38,086	395,453	424,333
Identifiable intangible assets, less accumulated amortization of \$13,887 and \$8,002	103,809	109,694
Investment in joint venture	10,539	10,753
Deferred financing costs	13,275	14,973
Other long-term assets	9,014	8,646
Total assets	\$ 972,462	\$ 965,587
Liabilities and Member s Equity		
Current liabilities:		
Current portion of long-term debt	\$ 2,680	\$ 2,680
Accounts payable trade	64,853	79,968
Other payables and accruals	50,269	40,059
Due to related parties	11,937	14,471
Deferred income taxes	1,240	1,240
Insurance bond payable	1,380	
Total current liabilities	132,359	138,418
Long-term debt, net of current portion	460,653	462,663
Deferred income taxes	30,723	25,184
Long-term liabilities	29,317	25,629
Total liabilities	653,052	651,894
Commitments and contingencies (note 5)		
Member s equity:		
Common equity	316,669	291,703
Accumulated other comprehensive income	2,741	21,990

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Total member s equity	319,410	313,693
Total liabilities and member s equity	\$ 972,462	\$ 965,587

See accompanying notes to consolidated financial statements.

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KRATON Polymers LLC
Consolidated Statements of Operations
Three Months Ended September 30, 2005 and 2004
(in thousands of U.S. dollars)
(Unaudited)

	September 30, 2005	September 30, 2004 (Restated See note 1(c))
Revenues		
Sales	\$ 269,017	\$ 209,407
Other	7,457	1,840
Total revenues	276,474	211,247
Costs and expense		
Costs of goods sold	225,945	179,186
Gross profit	50,529	32,061
Research and development expenses	6,700	5,530
Selling, general, and administrative expenses	19,130	16,467
Depreciation and amortization of identifiable intangibles	11,548	11,185
Earnings in joint venture	(182)	11
Interest, net	8,683	11,722
Income (loss) before income taxes	4,650	(12,854)
Income tax (provision) benefit	(1,268)	6,848
Net income (loss)	\$ 3,382	\$ (6,006)

See accompanying notes to consolidated financial statements.

KRATON Polymers LLC
Consolidated Statements of Operations
Nine Months Ended September 30, 2005 and 2004
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	September 30, 2005	September 30, 2004 (Restated See note 1(c))
Revenues		
Sales	\$ 732,338	\$ 589,886
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Gross profit	166,480	83,932
Research and development expenses	19,500	17,246
Selling, general, and administrative expenses	54,692	46,503
Depreciation and amortization of identifiable intangibles	33,760	31,849
Earnings in joint venture	(1,050)	(134)
Interest, net	25,833	27,719
Income (loss) before income taxes	33,745	(39,251)
Income tax (provision) benefit	(9,189)	15,332
Net income (loss)	\$ 24,556	\$ (23,919)

See accompanying notes to consolidated financial statements.

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KRATON Polymers LLC
Consolidated Statements of Cash Flows
Nine Months Ended September 30, 2005 and 2004
(in thousands of U.S. dollars)
(Unaudited)

	September 30, 2005	September 30, 2004 (Restated See note 1(c))
Cash flows provided by (used in) operating activities:		
Net income (loss)	\$ 24,556	\$ (23,919)
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization of identifiable intangibles	33,760	31,849
Amortization of deferred financing costs	1,698	2,522
Changes in the fair value of interest rate swaps	(128)	1,669
Loss on disposal of fixed assets	55	637
(Undistributed) distributed earnings in joint venture	(589)	427
Deferred tax provision (benefit)	3,515	(17,053)
Non-cash compensation	410	
Increase (decrease) in working capital:		
Accounts receivable	(43,567)	(27,426)
Due from related party	351	
Inventories	5,373	49,530
Other assets	(6,274)	(6,330)
Accounts payable, other payables and accruals, and long-term liabilities	10,004	45,877
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