W R GRACE & CO
Form 10-Q
November 08, 2006

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

FORM 10-Q

(Mark One)

x	**QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**
	FOR THE QUARTERLY PERIOD ENDED SEPTEMBER 30, 2006 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.

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

7500 Grace Drive
Columbia, Maryland 21044
(410) 531-4000
(Address and phone number of principal executive offices)

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 is a large accelerated filer, an accelerated filer, or a non-accelerated filer. See definition of accelerated filer and large accelerated filer in Rule 12b-2 of the Exchange Act.

Large accelerated filer o Accelerated filer x Non-accelerated filer 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

68,260,965 shares of Common Stock, $0.01 par value, were outstanding at October 31, 2006.

W. R. GRACE & CO. AND SUBSIDIARIES

Table of Contents

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 three and nine months ended September 30, 2006 and 2005, 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 financial statements. Accordingly, the degree of reliance on their report on the unaudited interim 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.

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 September 30, 2006, and the related consolidated statements of operations, shareholders equity (deficit) and comprehensive income (loss) for each of the three-month and nine-month periods ended September 30, 2006 and September 30, 2005 and the consolidated statements of cash flows for the nine-month periods ended September 30, 2006 and September 30, 2005. 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 interim consolidated financial statements for them to be in conformity with accounting principles generally accepted in the United States of America.

The accompanying interim consolidated financial statements have been prepared assuming that the Company will continue as a going concern. As discussed in Notes 1 and 2 to the interim consolidated financial statements, on April 2, 2001, the Company and substantially all of its domestic subsidiaries voluntarily filed for protection under Chapter 11 of the United States Bankruptcy Code, which raises substantial doubt about the Company s ability to continue as a going concern in its present form. Management s intentions with respect to this matter are also described in Notes 1 and 2. The accompanying interim consolidated financial statements do not include any adjustments that might result from the outcome of this uncertainty.

We have previously audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the consolidated balance sheet as of December 31, 2005, and the related consolidated statements of operations, cash flows, shareholders equity (deficit) and comprehensive income (loss) for the year then ended, management s assessment of the effectiveness of the Company s internal control over financial reporting as of December 31, 2005 and the effectiveness of the Company s internal control over financial reporting as of December 31, 2005; and in our report dated March 10, 2006, we expressed (i) an unqualified opinion on those consolidated financial statements with an explanatory paragraph relating to the Company s ability to continue as a going concern and, (ii) unqualified opinions on management s assessment of the effectiveness of the Company s internal control over financial reporting and on the effectiveness of the Company s internal control over financial reporting. The consolidated financial statements and management s assessment of the effectiveness of internal control over financial reporting referred to above are not presented herein. In our opinion, the information set forth in the accompanying consolidated balance sheet as of December 31, 2005, is fairly stated in all material respects in relation to the consolidated balance sheet from which it has been derived.

/s/ PRICEWATERHOUSECOOPERS LLP
McLean, Virginia

November 8, 2006

I-2

W. R. Grace & Co. and Subsidiaries
Consolidated Statements of Operations (Unaudited)
In millions, except per share amounts

	Three Months Ended September 30, 2006	2005	Nine Months Ended September 30, 2006	2005
Net sales	**$ 741.4**	$ 653.4	**$ 2,129.1**	$ 1,933.1
Cost of goods sold, exclusive of depreciation and amortization shown separately below	**483.8**	426.0	**1,392.0**	1,258.4
Selling, general and administrative expenses, exclusive of net pension expense and depreciation and amortization shown separately below	**148.6**	109.5	**418.3**	344.9
Depreciation and amortization	**29.2**	30.5	**85.7**	91.2
Research and development expenses	**15.5**	14.9	**46.1**	45.1
Net pension expense	**15.9**	17.3	**47.5**	54.4
Interest expense and related financing costs	**18.8**	13.4	**54.5**	41.3
Provision for environmental remediation			**30.0**	
Other (income) expense	**(6.3)**	(4.4)	**(22.1)**	(34.4)
	705.5	607.2	**2,052.0**	1,800.9
Income (loss) before Chapter 11 expenses, income taxes, and minority interest	**35.9**	46.2	**77.1**	132.2
Chapter 11 expenses, net	**(12.0)**	(9.3)	**(32.2)**	(19.9)
Income (loss) before income taxes and minority interest	**23.9**	36.9	**44.9**	112.3
Benefit from (provision for) income taxes	**2.4**	2.6	**(5.4)**	(26.0)
Minority interest in consolidated entities	**(7.9)**	(7.4)	**(26.2)**	(18.4)
Net income (loss)	**$ 18.4**	$ 32.1	**$ 13.3**	$ 67.9
Basic earnings (loss) per share:				
Net income (loss)	**$ 0.27**	$ 0.48	**$ 0.20**	$ 1.02
Weighted average number of basic shares	**68.3**	66.9	**67.7**	66.8
Diluted earnings (loss) per share:				

Mutual funds

U.S. fixed income		1,302,196						1,302,196
U.S. equity		465,718						465,718
U.S. small cap		347,228						347,228
International equity		288,161						288,161
Global fixed income		224,776						224,776
Commodities		42,182						42,182
Equity								
International equity		1,576,152						1,576,152
U.S. equity		2,891,184						2,891,184
Fixed income								
U.S. bonds		72,237		275,157		7,830		355,224
U.S. treasuries and agencies		266,567		137,462				404,029
Asset-backed securities				20,276				20,276
International bonds		3,640		866,846				870,486
Convertible securities		1,882		4,769				6,651
Total investments at fair value		14,395,408		1,804,583		7,830		16,207,821
Investments measured at NAV								10,379,988
Total investments	$	14,395,408	$	1,804,583	$	7,830	$	26,587,809

Table of Contents

The following table states the change in fair value of the Master Trusts Level 3 assets for the year ended December 31, 2014 (in thousands):

	Fair Value January 1, 2014	Transfer Out	Transfer In	Acquisitions	Dispositions	Realized Loss	Change in Unrealized Loss	Fair Value December 31, 2014
Fixed income								
International bonds	$ 6,467	$ (6,467)	$	$	$	$	$	$
U.S. bonds			8,320	2,018	(2,469)	(28)	(11)	7,830
Total investments	$ 6,467	$ (6,467)	$ 8,320	$ 2,018	$ (2,469)	$ (28)	$ (11)	$ 7,830

Assets are monitored to assess the appropriate levels assigned within the fair value hierarchy. Changes in economic conditions, such as bankruptcy, default or delisting, may require the transfer of an asset from one fair value level to another. When such a transfer occurs, it is recognized as of the end of the reporting period. Transfers out of international bonds to U.S. bonds reflect a change in classification.

Fully Benefit-Responsive Investment Contracts

The Plan holds a portfolio of synthetic investment contracts that meet the criteria of a FBRIC. These investment contracts are reported at contract value on the Statements of Net Assets Available for Benefits, as provided by the contract issuer. The contract value is the relevant measurement of the FBRICs because this is the amount participants would receive if they were to initiate permitted transactions under the terms of the Plan. The contract value of the investment contracts represents contributions plus earnings, less participant withdrawals and administrative expenses. The underlying investments of the FBRICs are included in the Master Trust s assets at contract value, which as reported by the insurance companies and banks, was approximately $1.8 billion at both December 31, 2015 and 2014.

The synthetic investment contracts held by the Plan include wrapper contracts that provide a guarantee that the credit rate will not fall below zero percent. The wrap contracts are held with insurance companies and banks. In a typical wrap contract, the wrap issuer agrees to pay the fund the difference between the contract value and the fair value of the covered assets once the fair value has been totally exhausted. Though relatively unlikely, this could happen if the fund experiences significant redemptions during a time when the fair value of the fund s covered assets is below their contract value and fair value is ultimately reduced to zero. Standard & Poor s (S&P) rated the issuers of these contracts and the contracts underlying the securities from AA- to A+ at both December 31, 2015 and 2014.

Certain events limit the ability of the Plan to transact at contract value with the issuer. These events include the following: (1) substantive modification of the Plan, including complete or partial plan termination or merger with another plan; (2) any change in law, regulation, or administrative ruling that could have a material adverse effect on the fund s cash flow; (3) the Plan s failure to qualify under section 401(k) of the Code; (4) bankruptcy of the Plan sponsor or other Plan sponsor events which cause a significant withdrawal from the Plan; and (5) defaults in the debt securities that comprise the covered assets in excess of certain limits. The Plan administrator does not believe the occurrence of any such event is probable at this time.

- 14 -

In addition, certain events allow the issuer to terminate the contracts with the Plan and settle at an amount different from contract value. Those events may be different under each contract. Such events may include the following: (1) an uncured violation of the Plan s investment guidelines; (2) a breach of material obligation under the contract; (3) a material misrepresentation; and (4) a material amendment to the agreements without the consent of the issuer.

8. Derivatives

In the normal course of operations, the Master Trust s assets and liabilities may include derivative financial instruments. Derivatives involve, in varying degrees, elements of credit and market volatility risks in excess of more traditional investment holdings such as equity and debt instruments. The contract or notional amounts disclosed in this footnote provide a measure of the Master Trust s involvement in such instruments but are not indicative of potential loss. The intent is to use derivative financial instruments as economic hedges to manage various risks such as market volatility risk, foreign currency exchange rate risk, interest rate risk or credit risk associated with the Master Trust s investment assets or to express investment managers views of future market movements efficiently.

At December 31, 2015 and 2014, the Master Trust utilized futures, options, foreign currency forwards, interest rate and credit derivatives to manage risks such as price risk, foreign currency exchange rate risk, interest rate sensitivity and credit risk.

Futures Contracts

Upon entering into a future contract on behalf of the Master Trust, the investment manager is required to pledge to the broker an amount of cash or securities equal to the minimum initial margin requirements of the exchange on which the contract is traded. Pursuant to the contract, the investment manager agrees to receive from or pay to the broker an amount of cash equal to the daily fluctuation in the value of the contract. Such receipts or payments are known as variation margin and are recorded on a daily basis by the trustee as a realized gain or loss equal to the difference in the value of the contract between daily closing prices.

Option Contracts

Purchased and written option contracts are agreements between two parties giving the owner, under a purchased option, the right, but not the obligation, to buy or sell a specified item at a fixed price (exercise or strike) during a specified period and, under a written option, the obligation to buy or sell a specified item at a fixed price. When the investment manager buys or writes an option contract, a nonrefundable fee (the premium) is paid or received by the Master Trust, recorded as an asset or liability and subsequently adjusted to the current market value of the option purchased or written. The premiums paid or received from buying or writing options are recorded as realized gains or losses when the options expire. The difference between the premium and the amount paid or received on effecting a closing purchase or sale transaction is also treated as a realized gain or loss. If an option is exercised, the premium paid or received is recorded as a realized gain or loss if sold or an adjustment to cost of the underlying investment if acquired upon exercise.

Foreign Currency Forward Contracts

Foreign currency forward contracts are agreements to exchange foreign currencies at a specified future date and rate, the terms of which are not standardized on an exchange. Risk arises both from the possible inability of the counterparties to meet the terms of the contracts (credit risk) and from the movements in foreign currency exchange rates (market risk). The contracts are recorded at fair value on the date the contract is entered into, which is typically zero.

Table of Contents

Interest Rate Derivatives

An interest rate swap is a bilateral contract between a buyer and a seller under which the buyer and seller agree to exchange payments based on interest rate movements, typically fixed versus floating rates on an agreed upon notional amount. Counterparty risk, or the risk associated with the party one enters into a contract with, is an important consideration for all forms of contractual agreement that are settled over-the-counter.

Credit Derivatives

A credit derivative is a bilateral contract between a buyer and a seller under which the seller agrees to provide protection to the buyer against the credit risk of a particular entity (reference entity or reference credit). Credit derivatives generally require that the seller of credit protection make payments to the buyer upon the occurrence of predefined credit events.

These triggering events may include the market standard of failure to pay on indebtedness, bankruptcy of the reference credit, debt restructuring, or the acceleration of indebtedness. The seller of such protection may not be required to make payments until a specified amount of losses has occurred with respect to the portfolio and/or may only be required to pay for losses up to a specified amount.

Credit derivatives are used primarily to help mitigate credit risk in the Master Trust s corporate bonds portfolio or to address investment managers views on the likelihood of future credit events. Through these contracts, the Master Trust either purchases or writes protection on either a single name or a portfolio of reference credits. The credit derivatives written by the Master Trust include credit default swaps (CDS).

A CDS is a contract in which, for a fee, a protection seller agrees to reimburse a protection buyer for any losses that occur due to a credit event on a reference entity. If there is no credit default event or settlement trigger, as defined by the specific derivative contract, then the protection seller makes no payments to the protection buyer and receives only the contractually specified fee. However, if a credit event occurs as defined in the specific derivative contract sold, the protection seller will be required to make a payment to the protection buyer.

Table of Contents

The notional amounts and fair values of the derivative instruments as of December 31, 2015 and 2014 are presented below. The fair values presented in the tables are included in the Statements of Net Assets Available for Benefits under Investments at fair value (in thousands):

	December 31, 2015		December 31, 2014	
	Notional Amount	Fair Value	Notional Amount	Fair Value
Equity				
Futures contracts	$ 30,734	$ (248)	$ 16,518	$ (103)
Futures contracts	(10,392)	(160)	(1,015)	(39)
Total	$ 20,342	$ (408)	$ 15,503	$ (142)
Fixed Income				
Futures contracts	$ 201,971	$ (1,033)	$ 285,394	$ 4,583
Futures contracts	(235,329)	414	(138,876)	(435)
Fixed income options			1,458	1,724
Fixed income options			(1,388)	(2,034)
Interest rate swaps	130,979	785	268,069	(2,520)
CDS	3,600	(16)	5,900	(161)
CDS	104,624	240	148,100	1,241
Total	$ 205,845	$ 390	$ 568,657	$ 2,398
Commodities				
Futures contracts	$ 33,417	$ (1,394)	$ 34,545	$ (2,266)
Total	$ 33,417	$ (1,394)	$ 34,545	$ (2,266)
Foreign Exchange				
Futures contracts	$ (790,072)	$ 815	$	$
Forwards contracts	34,215	(406)	78,829	476
Forwards contracts	523,140	1,730	635,422	8,875
Forwards contracts	714,129	2,415	955,839	(18,274)
Foreign exchange options			154	1,622
Foreign exchange options	(53)		(163)	(9)
Total	$ 481,359	$ 4,554	$ 1,670,081	$ (7,310)

9. Reconciliation of Financial Statements to Form 5500

The following table reconciles the Net assets available for benefits per the Statements of Net Assets Available for Benefits to the Plan s Form 5500 Asset and Liability Statement at December 31 (in thousands):

		2015		2014
Net assets available for benefits per the financial statements	$	4,676,483	$	4,822,303
Adjustment for deemed no post default payments		(10,074)		(9,154)
Adjustment from contract value to fair value for fully benefit-responsive investment contracts				8,233
Net assets available for benefits per Form 5500	$	4,666,409	$	4,821,382

- 17 -

Table of Contents

The following table reconciles the Net change per the Statement of Changes in Net Assets Available for Benefits to Net income per the Plan s Form 5500 Income and Expense Statement for the year ended December 31, 2015 (in thousands):

		2015
Net change per the financial statements	$	(145,820)
Adjustment for deemed no post default payments		(920)
Adjustment from fair value to contract value for fully benefit-responsive investment contracts		(8,233)
Net income per Form 5500	$	(154,973)

- 18 -

Table of Contents

VERIZON SAVINGS AND SECURITY PLAN FOR NEW YORK AND NEW ENGLAND ASSOCIATES

EIN: 23-2259884

Plan # 011

Schedule H, Line 4(i) Schedule of Assets (Held at End of Year)

As of December 31, 2015

(in thousands of dollars)

Identity of Issue, Borrower, Lessor, or Similar Party	Description of Investment, Including Maturity Date, Rate of Interest, Collateral, Par, or Maturity Value	Current Value
Notes receivable from participants*	0-15 years maturity at 3.25% - 10.50%	$ 201,016

** Party-in-interest*

Cost information is not required because investments are participant-directed.

- 19 -

Table of Contents

SIGNATURE

Pursuant to the requirements of the Securities Exchange Act of 1934, the Verizon Employee Benefits Committee has duly caused this annual report to be signed on its behalf by the undersigned hereunto duly authorized.

VERIZON SAVINGS AND SECURITY PLAN FOR NEW YORK AND NEW ENGLAND ASSOCIATES

By: /s/ Marc C. Reed
Marc C. Reed
(Chairperson, Verizon Employee Benefits Committee)
Date: June 24, 2016

- 20 -

Table of Contents

Exhibit Index

23.1 Consent of Independent Registered Public Accounting Firm