MILLENNIUM CHEMICALS INC
Form 10-Q
August 09, 2006

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

FORM 10-Q

x QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the quarterly period ended June 30, 2006

OR

¨ TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the transition period from ______ to ______

Commission file number 1-12091

MILLENNIUM CHEMICALS INC.

(Exact name of registrant as specified in its charter)

Delaware	**22-3436215**
(State or other jurisdiction of	**(I.R.S. Employer**
incorporation or organization)	**Identification No.)**
Two Greenville Crossing, 4001 Kennett Pike	
Suite 238, Greenville, Delaware	**19807**

(Address of principal executive offices) **(Zip Code)**

Registrant s telephone number, including area code: (713) 652-7200

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 ¨

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. (Check one): Large accelerated filer ¨ Accelerated filer ¨ Non-accelerated filer x

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

Number of shares of common stock outstanding as of June 30, 2006: 66,135,816. There is no established public trading market for the registrant s common stock.

The Registrant meets the conditions set forth in General Instructions H(1)(a) and (b) of Form 10-Q and, therefore, is filing this form with a reduced disclosure format.

PART I. FINANCIAL INFORMATION

ITEM 1. CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

MILLENNIUM CHEMICALS INC.

CONSOLIDATED STATEMENTS OF INCOME

Millions of dollars	For the three months ended June 30, 2006	For the three months ended June 30, 2005	For the six months ended June 30, 2006	For the six months ended June 30, 2005
Sales and other operating revenues				
Trade	$ 489	$ 509	$ 956	$ 949
Related parties	20	6	37	19
	509	515	993	968
Operating costs and expenses				
Cost of sales	445	424	883	789
Selling, general and administrative expenses	44	45	80	88
Research and development expenses	7	6	13	12
Asset impairments	4	3	6	5
	500	478	982	894
Operating income	9	37	11	74
Interest expense	(21)	(29)	(36)	(57)
Interest income	1	4	3	8
Other income (expense), net	49	5	21	(4)
Income (loss) before equity investment, minority interest and income taxes	38	17	(1)	21
Income from equity investment in Equistar Chemicals, LP	38	42	113	140
Income before income taxes and minority interest	76	59	112	161
Provision for (benefit from) income taxes	(39)	20	(37)	57
Income before minority interest	115	39	149	104
Minority interest	(1)	(1)	(2)	(2)
Net income	$ 114	$ 38	$ 147	$ 102

See Notes to the Consolidated Financial Statements.

MILLENNIUM CHEMICALS INC.

CONSOLIDATED BALANCE SHEETS

Millions of dollars	June 30, 2006	December 31, 2005
ASSETS		
Current assets:		
Cash and cash equivalents	$ 100	$ 279
Accounts receivable:		
Trade, net	351	331
Related parties	38	30
Inventories	412	429
Prepaid expenses and other current assets	56	64
Deferred tax assets	92	15
Total current assets	1,049	1,148
Property, plant and equipment, net	651	647
Investment in Equistar Chemicals, LP	488	464
Goodwill, net	104	104
Other assets, net	106	110
Total assets	$ 2,398	$ 2,473
LIABILITIES AND STOCKHOLDER S EQUITY		
Current liabilities:		
Current maturities of long-term debt	$ 21	$ 169
Accounts payable:		
Trade	265	305
Related parties	85	62
Accrued liabilities	149	156
Total current liabilities	520	692
Long-term debt	883	966
Other liabilities	620	644
Deferred income taxes	196	167
Commitments and contingencies		
Minority interests	46	42
Stockholder s equity (deficit):		
Common stock, $0.01 par value, 100,000,000 shares authorized, 70,935,510 shares issued	1	1
Additional paid-in capital	1,175	1,175
Retained deficit	(852)	(999)
Accumulated other comprehensive loss	(101)	(125)
Treasury stock, at cost (4,799,694 shares issued)	(90)	(90)
Total stockholder s equity (deficit)	133	(38)
Total liabilities and stockholder s equity	$ 2,398	$ 2,473

See Notes to the Consolidated Financial Statements.

MILLENNIUM CHEMICALS INC.

CONSOLIDATED STATEMENTS OF CASH FLOWS

Millions of dollars	For the six months ended June 30, 2006	2005
Cash flows from operating activities		
Net income	$ 147	$ 102
Adjustments to reconcile net income to cash provided by operating activities:		
Depreciation and amortization	53	53
Asset impairments	6	5
Equity investment in Equistar Chemicals, LP		
Amount included in net income	(113)	(140)
Distributions of earnings	89	140
Deferred income taxes	(43)	7
Debt prepayment premiums and charges	7	1
Changes in assets and liabilities that provided (used) cash:		
Accounts receivable	(21)	(30)
Inventories	27	(75)
Accounts payable	(20)	25
Other, net	(49)	(8)
Net cash provided by operating activities	83	80
Cash flows from investing activities		
Expenditures for property, plant and equipment	(28)	(21)
Other	1	
Net cash used in investing activities	(27)	(21)
Cash flows from financing activities		
Repayment of long-term debt	(247)	(29)
Issuance of long-term debt	13	3
Contribution from affiliate		6
Other	(3)	(3)
Net cash used in financing activities	(237)	(23)
Effect of exchange rate changes on cash	2	(5)
Increase (decrease) in cash and cash equivalents	(179)	31
Cash and cash equivalents at beginning of period	279	344
Cash and cash equivalents at end of period	$ 100	$ 375

See Notes to the Consolidated Financial Statements.

MILLENNIUM CHEMICALS INC.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

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MILLENNIUM CHEMICALS INC.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Continued)

1. Basis of Preparation

The accompanying consolidated financial statements are unaudited and have been prepared from the books and records of Millennium Chemicals Inc. and its subsidiaries (collectively, Millennium) in accordance with the instructions to Form 10-Q and Rule 10-01 of Regulation S-X for interim financial information. Accordingly, they do not include all of the information and notes required by generally accepted accounting principles for complete financial statements. In the opinion of management, all adjustments, consisting only of normal recurring adjustments, considered necessary for a fair presentation have been included. For further information, refer to the audited consolidated financial statements and notes thereto included in the Millennium Annual Report on Form 10-K for the year ended December 31, 2005. Certain previously reported amounts have been reclassified to conform to current period presentation.

2. Company Ownership

On November 30, 2004, Lyondell Chemical Company (Lyondell) acquired Millennium in a stock-for-stock business combination. As a result of the business combination, Millennium is a wholly-owned subsidiary of Lyondell. The consolidated financial statements of Millennium reflect its historical cost basis and, accordingly, do not reflect any purchase accounting adjustments related to the acquisition by Lyondell.

3. Accounting and Reporting Changes

In July 2006, the Financial Accounting Standards Board (FASB) issued FASB Interpretation (FIN) No. 48, *Accounting for Uncertainty in Income Taxes - An Interpretation of FASB Statement No. 109*, which clarifies the accounting for uncertain income tax positions. FIN No. 48 prescribes, among other things, a recognition threshold and measurement attribute for the financial statement recognition and measurement of an uncertain tax position. The provisions of FIN No. 48 will apply to Millennium beginning in 2007. Millennium is evaluating the impact of FIN No. 48 on its consolidated financial statements.

Effective January 1, 2006, Millennium adopted the provisions of Statement of Financial Accounting Standards (SFAS) No. 123 (revised 2004), *Share-Based Payment* using the modified prospective method and, consequently, has not adjusted results of prior periods. Millennium previously accounted for these plans using the intrinsic value method prescribed in Accounting Principles Board (APB) Opinion No. 25 and related interpretations. As a result of its acquisition by Lyondell, Millennium s use of share-based payment arrangements is minimal, and, consequently, the application of SFAS No. 123 (revised 2004) had no material effect on its consolidated financial statements.

Effective April 1, 2006, Millennium adopted the provisions of Emerging Issues Task Force (EITF) Issue No. 04-13, *Accounting for Purchases and Sales of Inventory with the Same Counterparty.* EITF Issue No. 04-13 requires that inventory purchases and sales transactions with the same counterparty that are entered into in contemplation of one another be combined for purposes of applying APB Opinion No. 29, *Accounting for Nonmonetary Transactions*. The effect was to reduce reported revenues and cost of sales for affected transactions. Millennium s application of EITF 04-13 had no material effect on its consolidated financial statements.

MILLENNIUM CHEMICALS INC.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Continued)

4. Asset Impairments

In 2003, Millennium recognized the impairment of the entire book value of property, plant and equipment at Millennium s Le Havre, France titanium dioxide (TiO_2) manufacturing plant. Capital expenditures at this plant of $4 million and $6 million for the three and six months ended June 30, 2006, respectively, and $3 million and $5 million for the three and six months ended June 30, 2005, respectively, were reflected in asset impairments. At June 30, 2006 and December 31, 2005, the carrying value of the property, plant and equipment at the Le Havre manufacturing plant was zero.

5. Investment in Equistar Chemicals, LP

Equistar Chemicals, LP (Equistar) is owned 70.5% by Lyondell and 29.5% by Millennium. As a result of Lyondell s acquisition of Millennium in 2004, Millennium and Equistar are wholly-owned subsidiaries of Lyondell. Millennium accounts for its investment in Equistar using the equity method. As a partnership, Equistar is not subject to federal income taxes.

The consolidated financial statements of Equistar reflect its historical cost basis and, accordingly, do not reflect any purchase accounting adjustments related to the acquisition by Lyondell. Summarized financial information for Equistar follows:

Millions of dollars	June 30, 2006	December 31, 2005
BALANCE SHEETS		
Total current assets	$ 2,048	$ 1,849
Property, plant and equipment, net	2,999	3,063
Investments and other assets, net	377	408
Total assets	$ 5,424	$ 5,320
Current maturities of long-term debt	$	$ 150
Other current liabilities	1,185	1,010
Long-term debt	2,160	2,161
Other liabilities and deferred revenues	412	416
Partners capital	1,667	1,583
Total liabilities and partners capital	$ 5,424	$ 5,320

MILLENNIUM CHEMICALS INC.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Continued)

5. Investment in Equistar Chemicals, LP (Continued)

Millions of dollars	For the three months ended June 30, 2006	2005	For the six months ended June 30, 2006	2005
STATEMENTS OF INCOME				
Sales and other operating revenues	$ 3,278	$ 2,700	$ 6,314	$ 5,561
Cost of sales	3,028	2,447	5,698	4,864
Selling, general and administrative expenses	61	48	109	98
Research and development expenses	9	9	17	17
Operating income	180	196	490	582
Interest expense, net	(52)	(54)	(105)	(108)
Other expense, net			(1)	
Net income	$ 128	$ 142	$ 384	$ 474
OTHER INFORMATION				
Depreciation and amortization	$ 82	$ 80	$ 164	$ 159
Expenditures for property, plant and equipment	41	34	63	69

6. Inventories

Inventories consisted of the following:

Millions of dollars	June 30, 2006	December 31, 2005
Finished goods	$ 204	$ 223
Work-in-process	42	40
Raw materials	103	106
Materials and supplies	63	60
Total inventories	$ 412	$ 429

7. Property, Plant and Equipment

The components of property, plant and equipment, at cost, and the related accumulated depreciation were as follows:

Millions of dollars	June 30, 2006	December 31, 2005
Land	$ 19	$ 20
Manufacturing facilities and equipment	1,599	1,531

Construction in progress	77	77
Total property, plant and equipment	1,695	1,628
Less accumulated depreciation	(1,044)	(981)
Property, plant and equipment, net	$ 651	$ 647

MILLENNIUM CHEMICALS INC.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Continued)

7. Property, Plant and Equipment (Continued)

Depreciation and amortization is summarized as follows:

	For the three months ended June 30,		For the six months ended June 30,	
Millions of dollars	**2006**	**2005**	**2006**	**2005**
Property, plant and equipment	$ 21	$ 21	$ 41	$ 42
Turnaround costs	3	2	5	3
Software costs	1	2	4	5
Other	1	2	3	3
Total depreciation and amortization	$ 26	$ 27	$ 53	$ 53

8. Accounts Payable

Accounts payable at June 30, 2006 and December 31, 2005 included liabilities in the amounts of $2 million and $5 million, respectively, for checks issued in excess of associated bank balances but not yet presented for collection.

9. Long-Term Debt

Long-term debt consisted of the following:

Millions of dollars	**June 30, 2006**	**December 31, 2005**
Bank Credit Facilities:		
$150 million senior secured revolving credit facility	$	$
$100 million Australian senior secured term loan due 2010	96	99
60 million U.K. asset-based revolving credit facility	12	
Other debt obligations:		
Senior Notes due 2006, 7%	9	158
Senior Notes due 2008, 9.25% ($3 million of premium)	376	463
Senior Debentures due 2026, 7.625% ($1 million of discount)	248	248
Convertible Senior Debentures due 2023, 4%	150	150
Debt payable through 2011 at interest rates ranging from 0% to 9.5%	19	19
Other	(6)	(2)
Total	904	1,135
Less current maturities	(21)	(169)
Total long-term debt, net	$ 883	$ 966

In May 2006, Millennium obtained an amendment to its $150 million senior secured revolving credit facility and in July 2006 to the indenture governing the 4% Convertible Senior Debentures primarily to exclude Millennium Holdings, LLC and its subsidiaries (collectively, Millennium Holdings), a wholly-owned subsidiary, from events-of-default provisions that could be triggered in connection with judgments against

Millennium Holdings. See Litigation section of Note 13.

MILLENNIUM CHEMICALS INC.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Continued)

9. Long-Term Debt (Continued)

In January 2006, a U.K. subsidiary of Millennium entered into a new 60 million, five-year, revolving credit facility, which, subject to permitted liens, is generally secured by the subsidiary s inventory, accounts receivable and certain other assets. Availability under the U.K. facility, which was 51 million, or approximately $65 million, at June 30, 2006, gave effect to the borrowing base as determined using a formula applied to accounts receivable and inventory balances and was reduced to the extent of borrowing and outstanding letters of credit provided under the facility. At June 30, 2006, there was 9 million, or approximately $12 million, of outstanding borrowing and no outstanding letters of credit under the facility. The U.K. facility bears interest at LIBOR plus 1.25%.

In February 2006, Millennium completed a cash tender offer for its 7% Senior Notes due 2006, purchasing $149 million principal amount of the notes and paying a premium of $2 million. In addition, during the first six months of 2006, Millennium purchased $85 million principal amount of the 9.25% Senior Notes due 2008, paying a premium of $5 million.

As of June 30, 2006, based on a quarterly test related to the price of Lyondell common stock, Millennium s 4% Convertible Senior Debentures were convertible into Lyondell common stock at a conversion rate of 73.3986 Lyondell shares per one thousand dollar principal amount of the Debentures. The principal amount of Debentures converted into shares of Lyondell common stock as of June 30, 2006 was not significant.

Current maturities of long-term debt were $21 million at June 30, 2006. At December 31, 2005, current maturities of long-term debt included $158 million of Millennium s 7% Senior Notes due 2006 and other debt of $11 million.

Amortization of debt issuance costs of less than $1 million in each of the three- and six-month periods ended June 30, 2006 and 2005 is included in interest expense in the Consolidated Statements of Income.

MILLENNIUM CHEMICALS INC.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Continued)

10. Pension and Other Postretirement Benefits

Net periodic pension costs included the following components:

	For the three months ended June 30, 2006		For the six months ended June 30, 2006	
Millions of dollars	U.S.	Non-U.S.	U.S.	Non-U.S.
Service cost	$ 2	$ 2	$ 4	$ 4
Interest cost	9	3	19	6
Recognized return on plan assets	(11)	(2)	(22)	(4)
Amortization	5	1	10	2
Net periodic pension benefit cost	$ 5	$ 4	$ 11	$ 8

	For the three months ended June 30, 2005		For the six months ended June 30, 2005	
Millions of dollars	U.S.	Non-U.S.	U.S.	Non-U.S.
Service cost	$ 2	$ 1	$ 4	$ 3
Interest cost	10	3	20	6
Recognized return on plan assets	(11)	(2)	(23)	(4)
Amortization	4	1	8	2
Net periodic pension benefit cost	$ 5	$ 3	$ 9	$ 7

Net periodic other postretirement benefit costs, which are provided to U.S. employees, were net credits of $1 million in each of the three-month periods ended June 30, 2006 and 2005 and $2 million in each of the six-month periods ended June 30, 2006 and 2005, as a result of a reduction of benefits and related prior service cost in 2004, which resulted in a net amortization credit of $4 million annually.

11. Income Taxes

The income tax provision for the six months ended June 30, 2006 was a benefit of $37 million on income before taxes and minority interest expense of $112 million. This income tax benefit primarily reflected the effects of favorable settlements of and changes in estimates for prior year items during the six months ended June 30, 2006. The annual effective tax rate for 2006 is estimated to be 10.4% as a result of the benefits recognized in the first six months.

12. Other Income (Expense), Net

Millennium s other income (expense), net, in the second quarter 2006 included a $49 million credit related to the reversal of interest accruals for prior year income tax issues, including an accrual of $18 million in the first quarter 2006, for a net benefit of $31 million in the first six months of 2006. The reversals reflected a favorable settlement of the prior year tax issues. See Note 11.

MILLENNIUM CHEMICALS INC.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Continued)

13. Commitments and Contingencies

Asset Retirement Obligation Millennium believes that there are asset retirement obligations associated with some of its facilities, but that the present value of those obligations normally is not material in the context of an indefinite expected life of the facilities. Millennium continually reviews the optimal future alternatives for its facilities. The amount and timing of costs, if any, that may be incurred as a result of such reviews are not known, and no decisions have been reached, but if a decision were reached, in accordance with local laws and customs, to retire one or more facilities in the foreseeable future, the asset retirement costs could range from $0 to $30 million, depending upon the scope of the required work and other factors. At June 30, 2006, the balance of the liability that had been recognized for all asset retirement obligations, including scheduled closure of certain landfills, was $18 million. In addition, any decision to retire a facility would result in other costs, including employment related costs.

Environmental Remediation Millennium s accrued liability for future environmental remediation costs at current and former plant sites and other remediation sites totaled $167 million as of June 30, 2006. The remediation expenditures are expected to occur over a number of years, and not to be concentrated in any single year. In the opinion of management, there is no material estimable range of reasonably possible loss in excess of the liabilities recorded for environmental remediation. However, it is possible that new information about the sites for which the accrual has been established, new technology or future developments such as involvement in investigations by regulatory agencies, could require Millennium to reassess its potential exposure related to environmental matters.

The following table summarizes the activity in Millennium s accrued environmental liability for the six-month periods ended June 30:

Millions of dollars	2006	2005
Balance at January 1	$ 168	$ 122
Additional accruals	4	1
Amounts paid	(5)	(3)
Balance at June 30	$ 167	$ 120

The liabilities for individual sites range from less than $1 million to $102 million. The $102 million liability relates to the Kalamazoo River Superfund Site.

A Millennium subsidiary has been identified as a Potential Responsible Party (PRP) with respect to the Kalamazoo River Superfund Site. The site involves cleanup of river sediments and floodplain soils contaminated with polychlorinated biphenyls, cleanup of former paper mill operations, and cleanup and closure of landfills associated with the former paper mill operations. In 2000, the Kalamazoo River Study Group (the KRSG), of which the Millennium subsidiary and other PRPs are members, submitted to the State of Michigan a Draft Remedial Investigation and Draft Feasibility Study, which evaluated a number of remedial options for the river. The estimated costs for these remedial options ranged from $0 to $2.5 billion.

MILLENNIUM CHEMICALS INC.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Continued)

13. Commitments and Contingencies (Continued)

At the end of 2001, the U.S. Environmental Protection Agency (EPA) took lead responsibility for the river portion of the site at the request of the State of Michigan. In 2004, the EPA initiated a confidential process to facilitate discussions among the agency, the Millennium subsidiary, other PRPs, the Michigan Departments of Environmental Quality and Natural Resources, and certain federal natural resource trustees about the need for additional investigation activities and different possible approaches for addressing the contamination in and along the Kalamazoo River. These discussions are continuing.

As of June 30, 2006, the probable future remediation spending associated with the river cannot be determined with certainty. Although the KRSG study identified a broad range of remedial options, not all of those options would represent reasonably possible outcomes. Management does not believe that it can identify a single remedy among those options that would represent the highest-cost reasonably possible outcome. However, in 2004, Millennium recognized a liability representing Millennium s interim allocation of 55% of the $73 million total of estimated cost of riverbank stabilization, recommended as the preferred remedy in 2000 by the KRSG study, and of certain other costs. During 2005 and 2006, this liability was increased to reflect new information obtained during the period about costs of regulatory oversight, modeling, and other associated river remediation costs. At June 30, 2006 and December 31, 2005, the balance of this liability, net of related spending, was $56 million and $57 million, respectively.

In addition, in 2004, Millennium recognized a liability primarily related to Millennium s estimated share of remediation costs for two former paper mill sites and associated landfills, which are also part of the Kalamazoo River Superfund Site. The liability was increased in the six-month period ended June 30, 2006 by $2 million to reflect new information obtained during the period regarding the probable costs associated with the remediation activity. At each of June 30, 2006 and December 31, 2005, the balance of the liability, net of related spending, was $46 million. Although no final agreement has been reached as to the ultimate remedy for these locations, Millennium has begun remediation activity related to these sites.

Millennium s ultimate liability for the Kalamazoo River Superfund Site will depend on many factors that have not yet been determined, including the ultimate remedy selected, the determination of natural resource damages, the number and financial viability of the other PRPs, and the determination of the final allocation among the PRPs.

Also, based on additional information obtained during the six-month period ended June 30, 2006, regarding remediation liabilities related to Millennium sites other than the Kalamazoo River Superfund Site, Millennium increased the estimated remediation liabilities for those sites by $2 million. The balance of these liabilities at each of June 30, 2006 and December 31, 2005 was $65 million.

Millennium currently estimates that environmentally related capital expenditures at its facilities will be approximately $5 million in 2006 and $6 million in 2007. These amounts include estimated expenditures related to air emission reductions.

Litigation Together with alleged past manufacturers of lead-based paint and lead pigments for use in paint, Millennium has been named as a defendant in various legal proceedings alleging personal injury, property damage, and remediation costs allegedly associated with the use of these products. The majority of these legal proceedings assert unspecified monetary damages in excess of the statutory minimum and, in certain cases, equitable relief such as abatement of lead-based paint in buildings. Legal proceedings relating to lead pigment or paint are in various trial stages and post-dismissal settings, some of which are on appeal.

MILLENNIUM CHEMICALS INC.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Continued)

13. Commitments and Contingencies (Continued)

One legal proceeding relating to lead pigment or paint was tried in 2002. On October 29, 2002, the judge in that case declared a mistrial after the jury declared itself deadlocked. The sole issue before the jury was whether lead pigment in paint in and on Rhode Island buildings constituted a public nuisance. The re-trial of this case began on November 1, 2005. On February 22, 2006, a jury returned a verdict in favor of the State of Rhode Island finding that the cumulative presence of lead pigments in paints and coatings on buildings in the state constitutes a public nuisance; that a Millennium subsidiary, Millennium Holdings LLC, and other defendants either caused or substantially contributed to the creation of the public nuisance; and that those defendants, including the Millennium subsidiary, should be ordered to abate the public nuisance. On February 28, 2006, the judge held that the state could not proceed with its claim for punitive damages. As a result, the jury was discharged. There will be further proceedings by the judge to determine the scope of any abatement. Millennium is considering its options, including all appropriate appeals.

Millennium s defense costs to date for lead-based paint and lead pigment litigation largely have been covered by insurance. Millennium has insurance policies that potentially provide approximately $1 billion in indemnity coverage for lead-based paint and lead pigment litigation. Millennium s ability to collect under the indemnity coverage would depend upon, among other things, the resolution of certain potential coverage defenses that the insurers have asserted or are likely to assert and the solvency of the various insurance carriers that are part of the coverage block at the time of such a request.

While Millennium believes that it has valid defenses to all the lead-based paint and lead pigment proceedings and is vigorously defending them, litigation is inherently subject to many uncertainties. Any liability that Millennium may ultimately incur, net of any insurance or other recoveries, cannot be estimated at this time.

Other Contingencies Millennium is organized under the laws of Delaware and is subject to United States Federal income taxation of corporations. However, in 1996, in order to obtain clearance from the former United Kingdom Inland Revenue (currently Her Majesty s Revenue and Customs) as to the tax-free treatment of the demerger stock dividend for United Kingdom tax purposes for Hanson plc (Hanson) and Hanson s shareholders, Hanson agreed with the United Kingdom Inland Revenue that Millennium would continue to be centrally managed and controlled in the United Kingdom at least until September 30, 2001. Millennium agreed with Hanson not to take, or fail to take, during such five-year period, any action that would result in a breach of, or constitute non-compliance with, any of the representations and undertakings made by Hanson in its agreement with the United Kingdom Inland Revenue. Effective February 4, 2002, Millennium ceased being centrally managed and controlled in the United Kingdom. Millennium believes that it has satisfied all obligations that it be managed and controlled in the United Kingdom for the requisite five-year period. During the first six months of 2006, Millennium received notice from Her Majesty s Revenue and Customs that it had no further inquiries with respect to this matter.

MILLENNIUM CHEMICALS INC.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Continued)

13. Commitments and Contingencies (Continued)

Indemnification Millennium and its joint ventures are parties to various indemnification arrangements, including arrangements entered into in connection with acquisitions, divestitures and the formation of joint ventures. For example, Millennium entered into indemnification arrangements in connection with its demerger from Hanson, and Equistar and its owner companies (including Millennium) entered into indemnification arrangements in connection with the formation of Equistar. Pursuant to these arrangements, Millennium and its joint ventures provide indemnification to and/or receive indemnification from other parties in connection with liabilities that may arise in connection with the transactions and in connection with activities prior to completion of the transactions. These indemnification arrangements typically include provisions pertaining to third party claims relating to environmental and tax matters and various types of litigation. As of June 30, 2006, Millennium has not accrued any significant amounts for such indemnification obligations, other than amounts under tax sharing agreements that have been reflected in the provision for income taxes, and is not aware of other circumstances that would be likely to lead to significant future indemnification claims against Millennium. Millennium cannot determine with certainty the potential amount of future payments under the indemnification arrangements until events arise that would trigger a liability under the arrangements.

Other Millennium and its joint ventures are, from time to time, defendants in lawsuits and other commercial disputes, some of which are not covered by insurance. Many of these suits make no specific claim for relief. Although final determination of any liability and resulting financial impact with respect to any such matters cannot be ascertained with any degree of certainty, management does not believe that any ultimate uninsured liability resulting from these matters in which it, its subsidiaries or its joint ventures currently are involved will, individually or in the aggregate, have a material adverse effect on the financial position, liquidity or results of operations of Millennium.

General In the opinion of management, the matters discussed in this note are not expected to have a material adverse effect on the financial position or liquidity of Millennium. However, the adverse resolution in any reporting period of one or more of these matters could have a material impact on Millennium s results of operations for that period, which may be mitigated by contribution or indemnification obligations of others, or by any insurance coverage that may be available.

14. Comprehensive Income

The components of comprehensive income were as follows:

	For the three months ended June 30,		For the six months ended June 30,	
Millions of dollars	**2006**	**2005**	**2006**	**2005**
Net income	$ 114	$ 38	$ 147	$ 102
Other comprehensive income (loss):				
Foreign currency translation income (loss)	9	(24)	24	(35)
Derivative instruments				(1)
Total other comprehensive income (loss)	9	(24)	24	(36)
Comprehensive income	$ 123	$ 14	$ 171	$ 66

MILLENNIUM CHEMICALS INC.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Continued)

15. Segment and Related Information

Millennium, a wholly-owned subsidiary of Lyondell, sells its products on a global basis primarily to other industrial concerns in the coatings and petrochemicals industries. Millennium operates in two reportable segments:

Inorganic chemicals, primarily manufacturing and marketing of TiO_2 and related products, and

Ethylene, co-products and derivatives (EC&D), including Millennium s acetyls business, which produces vinyl acetate monomer (VAM), acetic acid and methanol; and Millennium s equity investment in Equistar, which produces primarily ethylene, co-products such as propylene, butadiene, fuels and aromatics, and derivatives such as ethylene oxide, ethylene glycol and polyethylene.

Summarized financial information concerning reportable segments is shown in the following table for the periods presented:

Millions of dollars	Inorganic Chemicals	EC&D	Other	Total
For the three months ended June 30, 2006				
Sales and other operating revenues	$ 359	$ 122	$ 28	$ 509
Operating income (loss)	4	9	(4)	9
Income from equity investment		38		38
For the three months ended June 30, 2005				
Sales and other operating revenues	$ 342	$ 149		