CABOT CORP
Form 10-Q
May 07, 2015
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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 March 31, 2015

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 1-5667

Cabot Corporation

(Exact name of registrant as specified in its charter)

Delaware	**04-2271897**
(State or other jurisdiction of incorporation or organization)	**(I.R.S. Employer Identification No.)**
Two Seaport Lane	
Boston, Massachusetts	**02210-2019**
(Address of principal executive offices)	**(Zip Code)**

Registrant s telephone number, including area code: (617) 345-0100

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 has submitted electronically and posted on its corporate Web site, 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 x No ¨

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 definitions of large accelerated filer , accelerated filer and smaller reporting company in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer x	Accelerated filer ¨
Non-accelerated filer ¨ (Do not check if smaller reporting company)	Smaller reporting company ¨

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

Indicate the number of shares outstanding of each of the issuer s classes of Common Stock, as of the latest practicable date.

As of May 4, 2015 the Company had 63,466,995 shares of Common Stock, par value $1.00 per share, outstanding.

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Part I. Financial Information

Item 1. Financial Statements

CABOT CORPORATION

CONSOLIDATED STATEMENTS OF OPERATIONS

UNAUDITED

	Three Months Ended March 31		Six Months Ended March 31	
	2015	2014	2015	2014
	(In millions, except per share amounts)			
Net sales and other operating revenues	$ 694	$ 898	$ 1,506	$ 1,796
Cost of sales	555	722	1,210	1,441
Gross profit	139	176	296	355
Selling and administrative expenses	71	92	149	169
Research and technical expenses	14	16	29	31
Income from operations	54	68	118	155
Interest and dividend income	1	1	2	2
Interest expense	(14)	(13)	(27)	(27)
Other (expense) income	(2)	(8)	(3)	27
Income from continuing operations before income taxes and equity in earnings (loss) of affiliated companies	39	48	90	157
Provision for income taxes	(14)	(7)	(17)	(31)
Equity in earnings (loss) of affiliated companies, net of tax	2	(2)	3	
Income from continuing operations	27	39	76	126
Loss from discontinued operations, net of tax				(1)
Net income	27	39	76	125
Net income attributable to noncontrolling interests, net of tax	1	3	5	9
Net income attributable to Cabot Corporation	$ 26	$ 36	$ 71	$ 116
Weighted-average common shares outstanding, in millions:				
Basic	63.6	64.4	63.9	64.2
Diluted	64.1	65.1	64.4	65.0

Income per common share:								
Basic:								
Income from continuing operations attributable to Cabot Corporation	$	0.41	$	0.56	$	1.11	$	1.81
Loss from discontinued operations				(0.01)				(0.02)
Net income attributable to Cabot Corporation	$	0.41	$	0.55	$	1.11	$	1.79
Diluted:								
Income from continuing operations attributable to Cabot Corporation	$	0.41	$	0.55	$	1.10	$	1.79
Loss from discontinued operations				(0.01)				(0.02)
Net income attributable to Cabot Corporation	$	0.41	$	0.54	$	1.10	$	1.77
Dividends per common share	$	0.22	$	0.20	$	0.44	$	0.40

The accompanying notes are an integral part of these consolidated financial statements.

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CABOT CORPORATION

CONSOLIDATED STATEMENTS OF COMPREHENSIVE (LOSS) INCOME

UNAUDITED

	Three Months Ended March 31		Six Months Ended March 31	
	2015	**2014**	**2015**	**2014**
	(In millions)			
Net income	$ 27	$ 39	$ 76	$ 125
Other comprehensive loss, net of tax				
Foreign currency translation adjustment (net of tax provision of $-, $-, $1 and $1)	(131)	(8)	(234)	(29)
Pension and other postretirement benefit liability adjustments				
Pension and other postretirement benefit liability adjustments arising during the period (net of tax benefit of $-, $-, $6 and $-)			21	
Amortization of net loss and prior service credit included in net periodic pension cost (net of tax benefit of less than $1 million in all periods)	1	1	1	1
Other comprehensive loss	(130)	(7)	(212)	(28)
Comprehensive (loss) income	(103)	32	(136)	97
Net income attributable to noncontrolling interests	1	3	5	9
Noncontrolling interests foreign currency translation adjustment, net of tax	(1)	(1)	(3)	(2)
Comprehensive income attributable to noncontrolling interests, net of tax		2	2	7
Comprehensive (loss) income attributable to Cabot Corporation	$ (103)	$ 30	$ (138)	$ 90

The accompanying notes are an integral part of these consolidated financial statements.

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CONSOLIDATED BALANCE SHEETS

ASSETS

UNAUDITED

	March 31, 2015	September 30, 2014
	(In millions)	
Current assets:		
Cash and cash equivalents	$ 94	$ 67
Accounts and notes receivable, net of reserve for doubtful accounts of $8 and $7	567	688
Inventories:		
Raw materials	76	111
Work in process	1	2
Finished goods	290	341
Other	41	44
Total inventories	408	498
Prepaid expenses and other current assets	63	69
Deferred income taxes	39	42
Total current assets	1,171	1,364
Property, plant and equipment, net	1,483	1,581
Goodwill	508	536
Equity affiliates	63	68
Intangible assets, net	320	347
Assets held for rent	63	56
Deferred income taxes	74	80
Other assets	50	52
Total assets	$ 3,732	$ 4,084

The accompanying notes are an integral part of these consolidated financial statements.

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CONSOLIDATED BALANCE SHEETS

LIABILITIES AND STOCKHOLDERS EQUITY

UNAUDITED

	March 31, 2015	September 30, 2014
	(In millions, except share and per share amounts)	
Current liabilities:		
Notes payable	$ 133	$ 44
Accounts payable and accrued liabilities	386	512
Income taxes payable	36	49
Deferred income taxes	1	1
Current portion of long-term debt	1	24
Total current liabilities	557	630
Long-term debt	995	1,004
Deferred income taxes	63	68
Other liabilities	252	291
Redeemable preferred stock	28	27
Commitments and contingencies (Note I)		
Stockholders equity:		
Preferred stock:		
Authorized: 2,000,000 shares of $1 par value		
Issued and Outstanding : None and none		
Common stock:		
Authorized: 200,000,000 shares of $1 par value		
Issued: 63,702,325 and 64,634,731 shares		
Outstanding: 63,449,960 and 64,382,366 shares	63	64
Less cost of 252,365 and 252,365 shares of common treasury stock	(7)	(7)
Additional paid-in capital		49
Retained earnings	1,943	1,900
Accumulated other comprehensive loss	(273)	(64)
Total Cabot Corporation stockholders equity	1,726	1,942
Noncontrolling interests	111	122
Total stockholders equity	1,837	2,064
Total liabilities and stockholders equity	$ 3,732	$ 4,084

The accompanying notes are an integral part of these consolidated financial statements.

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CABOT CORPORATION

CONSOLIDATED STATEMENTS OF CASH FLOWS

UNAUDITED

	Six Months Ended March 31	
	2015	2014
	(In millions)	
Cash Flows from Operating Activities:		
Net income	$ 76	$ 125
Adjustments to reconcile net income to cash provided by operating activities:		
Depreciation and amortization	92	100
Impairment of assets		3
Deferred tax provision	(2)	(3)
Gain on existing investment in NHUMO		(29)
Employee benefit plan settlement	18	
Equity in earnings of affiliated companies	(3)	
Non-cash compensation	6	8
Other	(4)	
Changes in assets and liabilities:		
Accounts and notes receivable	71	(52)
Inventories	55	(76)
Prepaid expenses and other current assets		(15)
Accounts payable and accrued liabilities	(85)	(14)
Income taxes payable	(13)	1
Other liabilities	(18)	4
Cash dividends received from equity affiliates	7	21
Other	5	(4)
Cash provided by operating activities	205	69
Cash Flows from Investing Activities:		
Additions to property, plant and equipment	(70)	(70)
Change in assets held for rent	(7)	(5)
Cash paid for acquisition of business, net of cash acquired of $7		(73)
Cash used in investing activities	(77)	(148)
Cash Flows from Financing Activities:		
Borrowings under financing arrangements		13
Repayments under financing arrangements	(3)	(6)
Proceeds from long-term debt, net of issuance costs		15
Repayments of long-term debt	(32)	(7)
Decrease in notes payable, net	(1)	(5)

Proceeds from issuance of commercial paper, net		94		111
Purchases of common stock		(61)		(6)
Proceeds from sales of common stock		5		10
Cash dividends paid to noncontrolling interests		(11)		(10)
Cash dividends paid to common stockholders		(28)		(26)
Cash (used in) provided by financing activities		(37)		89
Effect of exchange rate changes on cash		(64)		(16)
Increase (Decrease) in cash and cash equivalents		27		(6)
Cash and cash equivalents at beginning of period		67		95
Cash and cash equivalents at end of period	$	94	$	89

The accompanying notes are an integral part of these consolidated financial statements.

CABOT CORPORATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

March 31, 2015

UNAUDITED

A. Basis of Presentation

The consolidated financial statements include the accounts of Cabot Corporation (Cabot or the Company) and its wholly owned subsidiaries and majority-owned and controlled U.S. and non-U.S. subsidiaries. Additionally, Cabot considers consolidation of entities over which control is achieved through means other than voting rights in the periods presented. Intercompany transactions have been eliminated in consolidation.

The unaudited consolidated financial statements have been prepared in accordance with the requirements of Form 10-Q and consequently do not include all disclosures required by Form 10-K. Additional information may be obtained by referring to Cabot s Annual Report on Form 10-K for the fiscal year ended September 30, 2014 (2014 10-K).

The financial information submitted herewith is unaudited and reflects all adjustments which are, in the opinion of management, necessary to provide a fair statement of the results for the interim periods ended March 31, 2015 and 2014. All such adjustments are of a normal recurring nature. The results for interim periods are not necessarily indicative of the results to be expected for the fiscal year.

In November 2013, the Company purchased all of Grupo Kuo S.A.B. de C.V. s (KUO) common stock in NHUMO, S.A. de C.V. (NHUMO), a carbon black joint venture between the Company and KUO in Mexico, which represented approximately 60% of the outstanding common stock of NHUMO (the NHUMO transaction). Prior to this transaction, the Company owned approximately 40% of the outstanding common stock of NHUMO, and the NHUMO entity was accounted for as an equity affiliate of the Company. The financial position, results of operations and cash flows of NHUMO are included in the Company s consolidated financial statements from the date of acquisition.

In July 2014, the Company completed the sale of its Security Materials business. The Consolidated Statements of Operations and the notes to the consolidated financial statements for all periods presented exclude the Security Materials business.

In December 2014, the Company realigned its business reporting structure into four segments that consist of Reinforcement Materials, Performance Chemicals, Purification Solutions and Specialty Fluids. The new structure is aligned with senior management changes and it better leverages Cabot s global activities across common customer applications, production, and research and development activities. Prior period segment results have been recast to reflect the realignment.

B. Significant Accounting Policies

Revenue Recognition and Accounts Receivable

Cabot recognizes revenue when persuasive evidence of an arrangement exists, delivery has occurred or services have been rendered, the price is fixed or determinable and collectability is reasonably assured. Cabot generally is able to

ensure that products meet customer specifications prior to shipment. If the Company is unable to determine that the product has met the specified objective criteria prior to shipment or if title has not transferred because of sales terms, the revenue is considered unearned and is deferred until the revenue recognition criteria are met.

Shipping and handling charges related to sales transactions are recorded as sales revenue when billed to customers or included in the sales price.

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The following table shows the relative size of the revenue recognized in each of the Company s reportable segments for the periods presented.

	Three Months Ended March 31		Six Months Ended March 31	
	2015	**2014**	**2015**	**2014**
Reinforcement Materials	53%	58%	56%	59%
Performance Chemicals	35%	30%	32%	29%
Purification Solutions	11%	9%	10%	9%
Specialty Fluids	1%	3%	2%	3%

Cabot derives the substantial majority of its revenues from the sale of products in Reinforcement Materials and Performance Chemicals. Revenue from these products is typically recognized when the product is shipped and title and risk of loss have passed to the customer. The Company offers certain of its customers cash discounts and volume rebates as sales incentives. Depending on the nature of the contract with the customer, a portion of the revenue may be recognized using proportional performance. The discounts and volume rebates are recorded as a reduction in sales at the time revenue is recognized and are estimated based on historical experience and contractual obligations. Cabot periodically reviews the assumptions underlying its estimates of discounts and volume rebates and adjusts its revenues accordingly.

Revenue in Purification Solutions is typically recognized when the product is shipped and title and risk of loss have passed to the customer. For major activated carbon injection systems projects, revenue is recognized using the percentage-of-completion method.

Revenue in Specialty Fluids arises primarily from the rental of cesium formate. This revenue is recognized throughout the rental period based on the contracted rental terms. Customers are also billed and revenue is recognized, typically at the end of the job, for cesium formate product that is not returned. The Company also generates revenues from cesium formate sold outside of a rental process and revenue is recognized upon delivery of the fluid.

Cabot maintains allowances for doubtful accounts based on an assessment of the collectability of specific customer accounts, the aging of accounts receivable and other economic information on both a historical and prospective basis. Customer account balances are charged against the allowance when it is probable the receivable will not be recovered. There is no material off-balance sheet credit exposure related to customer receivable balances.

Property, Plant and Equipment

Property, plant and equipment are recorded at cost. Depreciation of property, plant and equipment is generally calculated using the straight-line method over the estimated useful lives. The depreciable lives for buildings, machinery and equipment, and other fixed assets are twenty to twenty-five years, ten to twenty-five years, and three to twenty-five years, respectively. The cost and accumulated depreciation for property, plant and equipment sold, retired, or otherwise disposed of are removed from the Consolidated Balance Sheets and resulting gains or losses are included in earnings in the Consolidated Statements of Operations. Expenditures for repairs and maintenance are charged to expenses as incurred. Expenditures for major renewals and betterments, which significantly extend the useful lives of existing plant and equipment, are capitalized and depreciated.

CABOT CORPORATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

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UNAUDITED

Intangible Assets and Goodwill

The Company records tangible and intangible assets acquired and liabilities assumed in business combinations under the acquisition method of accounting. Amounts paid for an acquisition are allocated to the assets acquired and liabilities assumed based on their fair values at the date of acquisition. Goodwill is comprised of the purchase price of business acquisitions in excess of the fair value assigned to the net tangible and identifiable intangible assets acquired. Goodwill is not amortized, but is reviewed for impairment annually as of May 31, or when events or changes in the business environment indicate that the carrying value of the reporting unit may exceed its fair value. A reporting unit, for the purpose of the impairment test, is at or below the operating segment level, and constitutes a business for which discrete financial information is available and regularly reviewed by segment management. The separate businesses included within Performance Chemicals are considered separate reporting units. The goodwill balance relative to this segment is recorded in the Fumed Metal Oxides reporting unit within Performance Chemicals.

For the purpose of the goodwill impairment test, the Company first assesses qualitative factors to determine whether it is more likely than not that the fair value of a reporting unit is less than its carrying amount. If an initial qualitative assessment identifies that it is more likely than not that the carrying value of a reporting unit exceeds its estimated fair value, an additional quantitative evaluation is performed under the two-step impairment test. Alternatively, the Company may elect to proceed directly to the quantitative goodwill impairment test. If based on the quantitative evaluation the fair value of the reporting unit is less than its carrying amount, the Company performs an analysis of the fair value of all assets and liabilities of the reporting unit. If the implied fair value of the reporting unit s goodwill is determined to be less than its carrying amount, an impairment is recognized for the difference. The fair value of a reporting unit is based on discounted estimated future cash flows. The fair value is also benchmarked against a market approach using the guideline public companies method. The assumptions used to estimate fair value include management s best estimates of future growth rates, operating cash flows, capital expenditures and discount rates over an estimate of the remaining operating period at the reporting unit level. Should the fair value of any of the Company s reporting units decline because of reduced operating performance, market declines, changes in the discount rate, or other indicators of impairment, charges for impairment may be necessary. Based on the Company s most recent annual goodwill impairment test performed as of May 31, 2014, the fair values of the Reinforcement Materials and Fumed Metal Oxides reporting units were substantially in excess of their carrying values. At that date, the fair value of the Purification Solutions reporting unit exceeded its carrying value by approximately 9%. At March 31, 2015, the Purification Solutions reporting unit had the most significant goodwill balance, in the amount of $439 million. The future growth in the Purification Solutions segment is highly dependent on achieving the expected volumes and margins in the activated carbon based mercury removal business. These volumes and margins are highly dependent on demand for mercury removal products and the Company s successful realization of its anticipated share of volumes in this segment. The expected demand for mercury removal products significantly depends on: (1) the implementation and enforcement of environmental laws and regulations, particularly those that would require U.S. based coal-fired electric utilities to reduce the quantity of air pollutants they release, including mercury, to comply with the Mercury and Air Toxics Standards (MATS) and (2) other factors such as the anticipated usage of activated carbon in the

coal-fired energy units. In November 2014, the U.S. Supreme Court agreed to consider whether the Environmental Protection Agency (EPA) appropriately considered costs in determining whether it is necessary and appropriate to regulate hazardous air pollutants emitted by electric utilities, and oral arguments were heard by the Court in March 2015. It is not possible to predict the outcome of the Supreme Court s review of this matter.

The implementation period for the MATS regulations began in April 2015. With this recent implementation, as well as associated customer and industry feedback, the Company is reassessing its previous estimates for expected growth in volumes, prices and profitability in the Purification Solutions reporting unit. Potential drivers of growth, including the size of the overall mercury removal industry, utility adoption rates, usage levels, and pricing, among others, are still evolving. If the Company determines, based on these estimates, that the fair value of its Purification Solutions reporting unit is below the carrying amount, the Company may be required to record an asset impairment charge. With the evolving view of the market, the Company currently believes that it is reasonably possible that a non-cash impairment charge may be required. However, this is a preliminary view and Cabot expects to complete its analysis during the third fiscal quarter. This charge, if any, could be material and could impact goodwill, intangible assets, and long-lived assets. As of March 31, 2015, the carrying value of the Purification Solutions reporting unit was $1.1 billion, which included goodwill and intangibles in the amounts of $439 million and $270 million, respectively, and other long-lived assets.

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The Company uses assumptions and estimates in determining the fair value of assets acquired and liabilities assumed in a business combination. The determination of the fair value of intangible assets requires the use of significant judgment with regard to assumptions used in the valuation model. The Company estimates the fair value of identifiable acquisition-related intangible assets principally based on projections of cash flows that will arise from these assets. The projected cash flows are discounted to determine the fair value of the assets at the dates of acquisition.

Definite-lived intangible assets, which are comprised of customer relationships and developed technologies, are amortized over their estimated useful lives and are reviewed for impairment when indication of potential impairment exists, such as a significant reduction in cash flows associated with the assets. The Company evaluates indefinite-lived intangible assets, which are comprised of the trademarks of Purification Solutions, for impairment annually or when events occur or circumstances change that may reduce the fair value of the asset below its carrying amount. The annual review is performed as of May 31. The Company may first perform a qualitative assessment to determine whether it is necessary to perform the quantitative impairment test or bypass the qualitative assessment and proceed directly to performing the quantitative impairment test. The quantitative impairment test is based on discounted estimated future cash flows. The assumptions used to estimate fair value include management s best estimates of future growth rates and discount rates over an estimate of the remaining operating period at the unit of accounting level. These future growth rates depend on achieving the expected volumes and pricing levels of the products of Purification Solutions.

Long-lived Assets

The Company s long-lived assets primarily include property, plant and equipment, indefinite-lived assets, long-term investments and assets held for rent. The carrying values of long-lived assets are reviewed for impairment whenever events or changes in business circumstances indicate that the carrying amount of an asset may not be recoverable. An asset impairment is recognized when the carrying value of the asset is not recoverable based on the probability-weighted undiscounted estimated future cash flows to be generated by the asset. The Company s estimates reflect management s assumptions about selling prices, production and sales volumes, costs and market conditions over an estimate of the remaining operating period. If an impairment is indicated, the asset is written down to fair value. If the asset does not have a readily determinable market value, a discounted cash flow model may be used to determine the fair value of the asset. The key inputs to the discounted cash flow would be the same as the undiscounted cash flow noted above, with the addition of the discount rate used. In circumstances when an asset does not have separate identifiable cash flows, an impairment charge is recorded when the Company no longer intends to use the asset.

To test for impairment of assets the Company generally uses a probability-weighted estimate of the future undiscounted net cash flows of the assets over their remaining lives to determine if the value of the asset is recoverable. Long-lived assets are grouped with other assets and liabilities at the lowest level for which independent

identifiable cash flows are determinable.

Income Tax in Interim Periods

The Company records its tax provision or benefit on an interim basis using an estimated annual effective tax rate. This rate is applied to the current period ordinary income or loss to determine the income tax provision or benefit allocated to the interim period. Losses from jurisdictions for which no benefit can be recognized and the income tax effects of unusual or infrequent items are excluded from the estimated annual effective tax rate and are recognized in the impacted interim period.

Valuation allowances are provided against the future tax benefits that arise from the deferred tax assets in jurisdictions for which no benefit can be recognized. The estimated annual effective tax rate may be significantly impacted by nondeductible expenses and the Company s projected earnings mix by tax jurisdiction. Adjustments to the estimated annual effective income tax rate are recognized in the period when such estimates are revised.

CABOT CORPORATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

March 31, 2015

UNAUDITED

Inventory Valuation

Inventories are stated at the lower of cost or market. The cost of all carbon black inventories in the U.S. is determined using the last-in, first-out (LIFO) method. Had the Company used the first-in, first-out (FIFO) method instead of the LIFO method for such inventories, the value of those inventories would have been $40 million and $52 million higher as of March 31, 2015 and September 30, 2014, respectively. The cost of Specialty Fluids inventories is determined using the average cost method. The cost of other U.S. and non-U.S. inventories is determined using the FIFO method.

Cabot reviews inventory for both potential obsolescence and potential declines in anticipated selling prices. In this review, the Company makes assumptions about the future demand for and market value of the inventory, and based on these assumptions estimates the amount of any obsolete, unmarketable, slow moving or overvalued inventory. Cabot writes down the value of these inventories by an amount equal to the difference between the cost of the inventory and its estimated market value.

Pensions and Other Postretirement Benefits

The Company recognizes the funded status of defined benefit pension and other postretirement benefit plans as an asset or liability. This amount is defined as the difference between the fair value of plan assets and the benefit obligation. The Company is required to recognize as a component of other comprehensive income, net of tax, the actuarial gains/losses and prior service costs/credits that arise but were not previously required to be recognized as components of net periodic benefit cost. Other comprehensive income is adjusted as these amounts are later recognized in income as components of net periodic benefit cost.

Accumulated Other Comprehensive (Loss) Income

Accumulated other comprehensive (loss) income (AOCI), which is included as a component of stockholders equity, includes unrealized gains or losses on available-for-sale marketable securities, currency translation adjustments in foreign subsidiaries, translation adjustments on foreign equity securities and pension liability adjustments.

Recent Accounting Pronouncements

In July 2013, the Financial Accounting Standards Board (FASB) issued a new standard related to the Presentation of an Unrecognized Tax Benefit When a Net Operating Loss Carryforward, a Similar Tax Loss, or a Tax Credit Carryforward Exists . The standard requires, unless certain conditions exist, an unrecognized tax benefit or a portion of an unrecognized tax benefit to be presented in the consolidated financial statements as a reduction to a deferred tax asset for a net operating loss carryforward, similar to a tax loss or a tax credit carryforward. This standard is applicable for fiscal years beginning after December 15, 2013, and for interim periods within those years. The Company adopted this standard on October 1, 2014 and the implementation of the new standard did not have a material impact on its

consolidated financial statements.

In April 2014, the FASB issued a new standard related to Reporting Discontinued Operations and Disclosures of Disposals of Components of an Entity . The standard requires discontinued operations treatment for disposals of a component or group of components of a business that represents a strategic shift that has or will have a major impact on an entity s operations or financial results and requires additional disclosures for discontinued operations and new disclosures for individually material disposal transactions that do not meet the definition of a discontinued operation. This standard is applicable for fiscal years beginning after December 15, 2014 and for interim periods within those years with early adoption permitted, but only for disposals that have not been reported in consolidated financial statements previously issued. The Company expects to adopt this standard beginning on October 1, 2015.

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March 31, 2015

UNAUDITED

In May 2014, the FASB issued a new standard related to the Revenue from Contracts with Customers which amends the existing accounting standards for revenue recognition. The standard requires entities to recognize revenue when they transfer promised goods or services to customers in an amount that reflects the consideration the entity expects to be entitled to in exchange for those goods or services. This standard is applicable for fiscal years beginning after December 15, 2016 and for interim periods within those years and early adoption is not permitted. The Company expects to adopt this standard on October 1, 2017. In April 2015, the Financial Accounting Standards Board proposed deferring the effective date of the standard to annual periods beginning after December 15, 2017. The Company is currently evaluating the impact of the adoption of this standard on its consolidated financial statements.

In April 2015, the FASB issued a new standard simplifying the presentation of debt issuance costs by requiring debt issuance costs to be presented as a reduction of the corresponding debt liability. This will make the presentation of debt issuance costs consistent with the presentation of debt discounts or premiums. This standard is applicable for fiscal years beginning after December 15, 2015 and for interim periods within those years and early adoption is permitted. The Company expects to adopt this standard on October 1, 2016. The adoption of this standard is not expected to materially impact the Company s consolidated financial statements.

C. Acquisition of NHUMO

In November 2013, the Company purchased all of KUO s common stock in the NHUMO joint venture, which represented approximately 60% of the outstanding common stock of the joint venture. Prior to this transaction, the Company owned approximately 40% of the outstanding common stock of NHUMO, and the NHUMO entity was accounted for as an equity affiliate of the Company.

At the close of the transaction, the Company paid KUO $80 million in cash and NHUMO issued redeemable preferred stock to KUO with a redemption value of $25 million. The preferred stock accumulates dividends at a fixed rate of 6% annually and is redeemable at the option of KUO or the Company for $25 million starting in November 2018 or upon the occurrence of certain other conditions. Annual payment by NHUMO of the dividends is contingent on NHUMO achieving a minimum EBITDA (earnings before interest, taxes, depreciation and amortization) level and if such minimum EBITDA is not achieved in any year, the dividend will be accumulated and paid at the time the preferred shares are redeemed. The minimum EBITDA was achieved in 2014 and a dividend payment of $1.5 million was made in December 2014. The preferred stock issued in connection with the transaction is not mandatorily redeemable and has embedded put and call rights at the fixed redemption price. Accordingly, the instrument is accounted for as a financing obligation and has been separately presented in the Consolidated Balance Sheets as a long-term liability. Upon acquisition, the Company began consolidating NHUMO into its consolidated financial statements. Prior to closing, the Company received a $14 million dividend from NHUMO.

As of September 2014, the Company completed the valuation of its assets acquired and liabilities assumed. The allocation of the purchase price is based on the fair value of assets acquired and liabilities assumed, and Cabot s

previously held equity interest in NHUMO as of the acquisition date. During fiscal 2014, the Company recorded certain measurement period adjustments which are presented in the table below. The measurement period adjustments and the related tax impact were immaterial to the Company s consolidated financial statements. The following table presents the components and allocation of the purchase price, including the measurement period adjustments:

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	At Acquisition Date (October 31, 2013)	Measurement Period Adjustments	At Acquisition Date (As adjusted at September 30, 2014)
	(Dollars in millions)		
Assets			
Current assets	$ 54	$	$ 54
Property, plant and equipment	48		48
Other non-current assets	1		1
Intangible assets	57	6	63
Goodwill	51	(6)	45
Total assets acquired	211		211
Liabilities			
Accounts payable, accruals and other liabilities	(18)	(2)	(20)
Deferred tax liabilities - long-term	(31)	2	(29)
Total liabilities assumed	(49)		(49)
Net assets acquired	**$ 162**	**$**	**$ 162**
Cash consideration paid	80		
Fair value of redeemable preferred stock	28		
Previously held equity interest in NHUMO	54		
Total	**$ 162**		

As a result of the acquisition, the Company recorded a gain of $29 million for the difference between the carrying value and the fair value of the previously held equity interest in NHUMO, which was included in Other (expense) income in the first quarter of fiscal 2014. The fair value of $54 million for the previously held equity interest was determined based on the fair value of Cabot s pre-existing interest in NHUMO as adjusted for a control premium derived from synergies gained as a result of the Company obtaining control of NHUMO.

As part of the purchase price allocation, the Company determined that a separately identifiable intangible asset was customer relationships in the amount of $63 million, which is being amortized over a period of 20 years. The Company estimated the fair value of the identifiable acquisition-related intangible asset based on projections of cash flows that will arise from the asset. The projected cash flows are discounted to determine the fair value of the asset at

the date of acquisition. The determination of the fair value of the intangible asset acquired required the use of significant judgment with regard to assumptions in the discounted cash flow model used.

The fair value of the redeemable preferred stock was determined based on a discounted cash flow model, using the expected timing of the cash flows and an appropriate discount rate.

The excess of the purchase price, which includes the cash consideration paid, the fair value of redeemable preferred stock and the previously held equity interest in NHUMO, over the fair value of the tangible net assets and intangible asset acquired, was recorded as goodwill. The goodwill recognized is attributable to the expected growth and operating synergies that the Company expects to realize from this acquisition. Goodwill generated from the acquisition is not deductible for tax purposes.

D. Discontinued Operations

In July 2014, the Company sold its Security Materials business to SICPA SA. The Consolidated Statements of Operations for all periods presented have been recast to reflect the Security Materials business in discontinued operations.

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E. Employee Benefit Plans

Net periodic defined benefit pension and other postretirement benefit costs include the following:

	Three Months Ended March 31							
	2015		2014		2015		2014	
	Pension Benefits				Postretirement Benefits			
	U.S.	Foreign	U.S.	Foreign	U.S.	Foreign	U.S.	Foreign
	(Dollars in millions)							
Service cost	$	$ 3	$	$ 3	$	$	$	$
Interest cost	1	3	2	4	1			
Expected return on plan assets	(2)	(4)	(2)	(5)				
Amortization of prior service credit								
Amortization of actuarial loss		1		1				
Net periodic benefit (credit) cost	$ (1)	$ 3	$	$ 3	$ 1	$	$	$

	Six Months Ended March 31							
	2015		2014		2015		2014	
	Pension Benefits				Postretirement Benefits			
	U.S.	Foreign	U.S.	Foreign	U.S.	Foreign	U.S.	Foreign
	(Dollars in millions)							
Service cost	$	$ 5	$ 1	$ 5	$	$	$	$
Interest cost	3	6	4	8	1		1	
Expected return on plan assets	(5)	(8)	(5)	(10)				
Amortization of prior service credit					(1)		(1)	
Amortization of actuarial loss		2		2				
Settlement costs		18						
Net periodic benefit (credit) cost	$ (2)	$ 23	$	$ 5	$	$	$	$

Settlement of employee benefit plan

Effective October 1, 2014, the Company transferred the defined benefit obligations and pension plan assets in one of its foreign defined benefit plans to a multi-employer plan. This decision effectively moves the administrative, asset custodial, asset investment, actuarial, communication and benefit payment obligations to the multi-employer fund administrator. The plan is over 80% funded. Cabot is required to make contributions to the multi-employer fund and contributed assets by one participating employer may be used to provide benefits to employees of other participating employers since assets contributed by an employer are not segregated in a separate account or restricted to provide benefits only to employees of that employer. As a result of the transfer, a pre-tax charge of $18 million has been recorded in the six months ended March 31, 2015 as reflected in Settlement costs in the table above. The pre-tax charge consists of $27 million released from AOCI and $2 million of employer contributions at the time of the settlement, partially offset by an $11 million release of the pension liability. The settlement charge has been recorded primarily in Cost of sales in the Consolidated Statements of Operations.

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F. Goodwill and Other Intangible Assets

Cabot had goodwill balances of $508 million and $536 million at March 31, 2015 and September 30, 2014, respectively. The carrying amount of goodwill attributable to each reportable segment with goodwill balances and the changes in those balances during the period ended March 31, 2015 are as follows:

	Reinforcement Materials	Performance Chemicals	Purification Solutions	Total
	(Dollars in millions)			
Balance at September 30, 2014	$ 68	$ 10	$ 458	$ 536
Foreign currency impact	(8)	(1)	(19)	(28)
Balance at March 31, 2015	$ 60	$ 9	$ 439	$ 508

Goodwill impairment tests are performed at least annually. The Company performed its last annual impairment assessment as of May 31, 2014 and determined there was no impairment. However, recent developments have occurred and continue to evolve that could impact the Purification Solutions reporting unit s fair value. Therefore, the Company currently believes that it is reasonably possible that an asset impairment charge may be required for the Purification Solutions reporting unit in the future, which could reduce the amount of goodwill attributable to the Purification Solutions reporting unit. Refer to the Intangible Assets and Goodwill disclosure included in Note B.

The following table provides information regarding the Company s intangible assets:

	March 31, 2015			September 30, 2014		
	Gross Carrying Value	Accumulated Amortization	Net Intangible Assets	Gross Carrying Value	Accumulated Amortization	Net Intangible Assets
	(Dollars in millions)					
Intangible assets with finite lives						
Developed technologies	$ 146	$ (19)	$ 127	$ 152	$ (16)	$ 136
Customer relationships	159	(20)	139	171	(17)	154
Total intangible assets, finite lives	$ 305	$ (39)	$ 266	$ 323	$ (33)	$ 290
Trademarks, indefinite lives	54		54	57		57

Total intangible assets	$ 359	$ (39)	$ 320	$ 380	$ (33)	$ 347

Intangible assets with finite lives are amortized over their estimated useful lives, which range from sixteen to twenty years, with a weighted average amortization period of approximately nineteen years. Amortization expense for the three months ended March 31, 2015 and 2014 was $4 million and $5 million, respectively, and is included in Cost of sales and Selling and administrative expenses in the Consolidated Statements of Operations. Amortization expense for the six months ended March 31, 2015 and 2014 was $8 million and $9 million, respectively, and is included in Cost of sales and Selling and administrative expenses in the Consolidated Statements of Operations. Total amortization expense is estimated to be approximately $16 million each year for the next five fiscal years. Intangible assets with indefinite lives are evaluated for impairment at least annually. The Company performed its annual impairment assessment as of May 31, 2014, and determined there was no impairment.

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G. Stockholders Equity

In fiscal 2007, the Board of Directors authorized Cabot to repurchase up to ten million shares of Cabot s common stock in the open market or in privately negotiated transactions. This authorization did not have a set expiration date. During the first six months of fiscal 2015 and 2014, Cabot repurchased 925,700 and 379 shares, respectively, of its common stock under this authorization.

In January 2015, the Board of Directors authorized Cabot to repurchase up to five million shares of the Company s common stock in the open market or in privately negotiated transactions and cancelled the previous authorization. Cabot has repurchased 300,000 shares of its common stock under this authorization. As of March 31, 2015, 4.7 million shares remain available for repurchase under the current authorization.

During the first six months of fiscal 2015, Cabot paid cash dividends of $0.22 per share of common stock for a total of $28 million. During the first six months of fiscal 2014, Cabot paid cash dividends of $0.20 per share of common stock for a total of $26 million.

Noncontrolling interests

The following table illustrates the noncontrolling interests activity for the periods presented:

	2015	2014
	(Dollars in millions)	
Balance at September 30	$ 122	$ 132
Net income attributable to noncontrolling interests	5	9
Noncontrolling interest foreign currency translation adjustment	(3)	(2)
Noncontrolling interest dividends	(13)	(20)