

ECOLAB INC
Form 10-Q
May 08, 2014

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

(Mark One)

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

For the quarterly period ended March 31, 2014

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 No. 1-9328

ECOLAB INC.

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(Exact name of registrant as specified in its charter)

Delaware
(State or other jurisdiction of
incorporation or organization)

41-0231510
(I.R.S. Employer
Identification No.)

370 Wabasha Street N., St. Paul, Minnesota 55102

(Address of principal executive offices) (Zip Code)

1-800-232-6522

(Registrant's telephone number, including area code)

(Not Applicable)

(Former name, former address and former fiscal year,
if changed since last report)

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 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 Regulations 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 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 the definitions of large accelerated filer, accelerated filer and smaller reporting company in Rule 12b-2 of the Exchange Act.

Large accelerated filer

Accelerated filer

Non-accelerated filer
(Do not check if a 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

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Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of March 31, 2014.

300,199,314 shares of common stock, par value \$1.00 per share.

PART I - FINANCIAL INFORMATION

Item 1. Financial Statements

ECOLAB INC.

CONSOLIDATED STATEMENT OF INCOME

(millions, except per share amounts)	First Quarter Ended March 31 (unaudited)	
	2014	2013
Net sales	\$ 3,336.6	\$ 2,872.1
Cost of sales (including special charges of \$6.0 in 2014 and \$2.0 in 2013)	1,819.2	1,539.7
Selling, general and administrative expenses	1,136.9	1,021.0
Special (gains) and charges	29.6	49.7
Operating income	350.9	261.7
Interest expense, net (including special charges of \$2.2 in 2013)	65.1	61.5
Income before income taxes	285.8	200.2
Provision for income taxes	91.3	39.2
Net income including noncontrolling interest	194.5	161.0
Less: Net income attributable to noncontrolling interest (including special charges of \$0.5 in 2013)	3.5	1.4
Net income attributable to Ecolab	\$ 191.0	\$ 159.6
Earnings attributable to Ecolab per common share		
Basic	\$ 0.64	\$ 0.54
Diluted	\$ 0.62	\$ 0.53
Dividends declared per common share	\$ 0.2750	\$ 0.2300
Weighted-average common shares outstanding		
Basic	300.6	295.4
Diluted	306.5	300.9

The accompanying notes are an integral part of the consolidated financial information.

ECOLAB INC.

CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME (LOSS)

(millions)	First Quarter Ended March 31	
	2014	2013
	(unaudited)	
Net income including noncontrolling interest	\$ 194.5	\$ 161.0
Other comprehensive income (loss), net of tax		
Foreign currency translation adjustments		
Foreign currency translation	(67.0)	(61.6)
Loss on net investment hedge	(3.7)	(2.2)
	(70.7)	(63.8)
Derivatives and hedging instruments		3.9
Pension and postretirement benefits		
Amortization of net actuarial loss and prior service cost included in net periodic pension and postretirement costs	2.6	10.4
Subtotal	(68.1)	(49.5)
Total comprehensive income, including noncontrolling interest	126.4	111.5
Less: Comprehensive income (loss) attributable to noncontrolling interest	3.5	(7.9)
Comprehensive income attributable to Ecolab	\$ 122.9	\$ 119.4

The accompanying notes are an integral part of the consolidated financial information.

ECOLAB INC.

CONSOLIDATED BALANCE SHEET

(millions)	March 31 2014	December 31 2013
	(unaudited)	
ASSETS		
Current assets		
Cash and cash equivalents	\$ 300.3	\$ 339.2
Accounts receivable, net	2,519.6	2,568.0
Inventories	1,367.1	1,321.9
Deferred income taxes	170.8	163.0
Other current assets	345.2	306.3
Total current assets	4,703.0	4,698.4
Property, plant and equipment, net	2,889.0	2,882.0
Goodwill	6,856.6	6,862.9
Other intangible assets, net	4,701.3	4,785.3
Other assets	413.5	407.9
Total assets	\$ 19,563.4	\$ 19,636.5

The accompanying notes are an integral part of the consolidated financial information.

(Continued)

ECOLAB INC.

CONSOLIDATED BALANCE SHEET (continued)

(millions, except shares and per share amounts)	March 31 2014	December 31 2013
	(unaudited)	
LIABILITIES AND EQUITY		
Current liabilities		
Short-term debt	\$ 1,507.4	\$ 861.0
Accounts payable	951.2	1,021.9
Compensation and benefits	474.7	571.1
Income taxes	89.3	80.9
Other current liabilities	881.8	953.8
Total current liabilities	3,904.4	3,488.7
Long-term debt	5,696.6	6,043.5
Postretirement health care and pension benefits	795.9	795.6
Other liabilities	1,893.4	1,899.3
Total liabilities	12,290.3	12,227.1
Equity (a)		
Common stock	346.4	345.1
Additional paid-in capital	4,757.0	4,692.0
Retained earnings	4,807.2	4,699.0
Accumulated other comprehensive loss	(373.3)	(305.2)
Treasury stock	(2,326.8)	(2,086.6)
Total Ecolab shareholders' equity	7,210.5	7,344.3
Noncontrolling interest	62.6	65.1
Total equity	7,273.1	7,409.4
Total liabilities and equity	\$ 19,563.4	\$ 19,636.5

(a) Common stock, 800 million shares authorized, \$1.00 par value per share, 300.2 million shares outstanding at March 31, 2014, 301.1 million shares outstanding at December 31, 2013. Shares outstanding are net of treasury stock.

The accompanying notes are an integral part of the consolidated financial information.

ECOLAB INC.

CONSOLIDATED STATEMENT OF CASH FLOWS

(millions)	First Quarter Ended March 31 (unaudited)	
	2014	2013
OPERATING ACTIVITIES		
Net income including noncontrolling interest	\$ 194.5	\$ 161.0
Adjustments to reconcile net income including noncontrolling interest to cash provided by operating activities:		
Depreciation	136.5	122.6
Amortization	80.3	62.7
Deferred income taxes	(8.3)	(26.9)
Share-based compensation expense	22.8	21.1
Excess tax benefits from share-based payment arrangements	(22.9)	(12.3)
Pension and postretirement plan contributions	(28.0)	(19.0)
Pension and postretirement plan expense	21.9	35.7
Restructuring, net of cash paid	2.7	(9.2)
Venezuela currency devaluation		23.4
Other, net	3.7	4.6
Changes in operating assets and liabilities, net of effect of acquisitions:		
Accounts receivable	38.3	30.1
Inventories	(54.8)	(54.2)
Other assets	(44.9)	(50.4)
Accounts payable	(69.6)	(38.0)
Other liabilities	(57.8)	(65.2)
Cash provided by operating activities	\$ 214.4	\$ 186.0

The accompanying notes are an integral part of the consolidated financial information.

(Continued)

ECOLAB INC.

CONSOLIDATED STATEMENT OF CASH FLOWS (continued)

(millions)	First Quarter Ended March 31 (unaudited)	
	2014	2013
INVESTING ACTIVITIES		
Capital expenditures	\$ (142.2)	\$ (129.2)
Capitalized software expenditures	(8.7)	(6.3)
Property and other assets sold	0.7	0.9
Businesses acquired and investments in affiliates, net of cash acquired	(25.3)	(91.2)
Deposit into indemnification escrow		(8.0)
Release from indemnification escrow	1.1	13.0
Cash used for investing activities	(174.4)	(220.8)
FINANCING ACTIVITIES		
Net issuances (repayments) of commercial paper and notes payable	397.5	(310.0)
Long-term debt borrowings		0.2
Long-term debt repayments	(101.4)	(1.7)
Reacquired shares	(242.6)	(22.2)
Dividends paid	(85.9)	(4.5)
Exercise of employee stock options	24.0	32.0
Excess tax benefits from share-based payment arrangements	22.9	12.3
Acquisition related contingent consideration	(87.6)	
Other, net		0.4
Cash used for financing activities	(73.1)	(293.5)
Effect of exchange rate changes on cash	(5.8)	(5.2)
Decrease in cash and cash equivalents	(38.9)	(333.5)
Cash and cash equivalents, beginning of period	339.2	1,157.8
Cash and cash equivalents, end of period	\$ 300.3	\$ 824.3

The accompanying notes are an integral part of the consolidated financial information.

ECOLAB INC.

CONDENSED NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

1. Consolidated Financial Information

The unaudited consolidated financial information for the first quarter ended March 31, 2014 and 2013 reflect, in the opinion of management, all adjustments necessary for a fair presentation of the financial position, results of operations, comprehensive income and cash flows of Ecolab Inc. (Ecolab or the company) for the interim periods presented. The financial results for any interim period are not necessarily indicative of results for the full year. The consolidated balance sheet data as of December 31, 2013 was derived from the audited consolidated financial statements, but does not include all disclosures required by accounting principles generally accepted in the United States of America. The unaudited consolidated financial information should be read in conjunction with the consolidated financial statements and notes thereto incorporated in the company s Annual Report on Form 10-K for the year ended December 31, 2013.

With respect to the unaudited financial information of the company for the first quarter ended March 31, 2014 and 2013 included in this Form 10-Q, PricewaterhouseCoopers LLP reported that they have applied limited procedures in accordance with professional standards for a review of such information. However, their separate report dated May 8, 2014 appearing herein states that they did not audit and they do not express an opinion on that unaudited financial information. Accordingly, the degree of reliance on their report on such information should be restricted in light of the limited nature of the review procedures applied. PricewaterhouseCoopers LLP is not subject to the liability provisions of Section 11 of the Securities Act of 1933, as amended (the Act), for their report on the unaudited financial information because that report is not a report or a part of a registration statement prepared or certified by PricewaterhouseCoopers LLP within the meaning of Sections 7 and 11 of the Act.

Effective in the first quarter of 2014, certain employee-related costs from the company s recently acquired businesses that were historically presented within cost of sales were revised and reclassified to selling, general and administrative expenses on the Consolidated Statement of Income. These immaterial revisions were made to conform with management s view of the respective costs within the global organizational model. Total costs reclassified were \$25.2 million for the first quarter ended March 31, 2013 and \$78.9 million for the year ended December 31, 2013.

Results for 2013 have been revised to conform to the current year presentation. The reclassification had no impact on net earnings, financial position or cash flows.

ECOLAB INC.

CONDENSED NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

2. Special (Gains) and Charges

Special (gains) and charges reported on the Consolidated Statement of Income include the following:

(millions)	First Quarter Ended March 31	
	2014	2013
Cost of sales		
Restructuring charges	\$ 6.0	\$ 2.0
Special (gains) and charges		
Restructuring charges	22.6	18.5
Champion acquisition and integration costs	6.5	7.8
Nalco merger and integration costs	1.3	3.8
Venezuela currency devaluation		23.4
Litigation related charges and other	(0.8)	(3.8)
Subtotal	29.6	49.7
Operating income subtotal	35.6	51.7
Interest expense, net		
Acquisition debt costs		2.2
Net income attributable to noncontrolling interest		
Venezuela currency devaluation		(0.5)
Total special (gains) and charges	\$ 35.6	\$ 53.4

For segment reporting purposes, special (gains) and charges are included in the Corporate segment, which is consistent with the company's internal management reporting.

Restructuring Charges

The company incurs net costs for restructuring activities associated with plans to enhance its efficiency and effectiveness and sharpen its competitiveness. These restructuring plans include net costs associated with significant actions involving employee-related severance charges, contract termination costs and asset write-downs and disposals. Employee termination costs are largely based on policies and severance plans, and include personnel reductions and related costs for severance, benefits and outplacement services. These charges are reflected in the quarter when the actions are probable and the amounts are estimable, which typically is when management approves the associated actions. Contract termination costs include charges to terminate leases prior to the end of their respective terms and other contract terminations. Asset write-downs and disposals include leasehold improvement write-downs, other asset write-downs associated with combining operations and disposal of assets.

Restructuring charges have been included as a component of both cost of sales and special (gains) and charges on the Consolidated Statement of Income. Amounts included as a component of cost of sales include supply chain related severance and other asset write-downs associated with combining operations. Restructuring liabilities have been classified as a component of both other current and non-current liabilities on the Consolidated Balance Sheet.

ECOLAB INC.

CONDENSED NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

2. Special (Gains) and Charges (continued)

Energy Restructuring Plan

On April 10, 2013, the company completed its acquisition of privately held Champion Technologies and its related company Corsicana Technologies (collectively "Champion").

In April 2013, following the completion of the acquisition of Champion, the company commenced plans to undertake restructuring and other cost-saving actions to realize its acquisition-related cost synergies as well as streamline and strengthen Ecolab's position in the fast growing global energy market (the "Energy Restructuring Plan"). Actions associated with the acquisition to improve the effectiveness and efficiency of the business include a reduction of the combined business's current global workforce by approximately 500 positions. A number of these reductions are expected to be achieved through eliminating open positions and attrition. The company also anticipates leveraging and simplifying its global supply chain, including the reduction of plant and distribution center locations and product line optimization, as well as the reduction of other redundant facilities.

The company expects to incur pretax restructuring charges of approximately \$80 million (\$55 million after tax) under the Energy Restructuring Plan through the completion of the Plan in 2015. Approximately \$35 million (\$25 million after tax) of those charges are expected to occur in 2014. During 2013, the company incurred \$27 million (\$19 million after tax) of charges related to the Energy Restructuring Plan.

The company anticipates that approximately \$60 million of the \$80 million of the pre-tax charges represent cash expenditures. The remaining pre-tax charges represent estimated asset write-downs and disposals. No decisions have been made for any asset disposals and estimates could vary depending on the actual actions taken.

As a result of restructuring activities under the Energy Restructuring Plan, the company recorded restructuring charges of \$4.9 million (\$3.0 million after tax), during the first quarter of 2014.

Restructuring charges and activity related to the Energy Restructuring Plan since inception of the underlying actions include the following:

(millions)	Energy Restructuring Plan			Total
	Employee Termination Costs	Asset Disposals	Other	

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2013 Activity:								
Recorded expense and accrual	\$	22.9	\$	3.6	\$	0.9	\$	27.4
Cash payments		(16.7)				(0.8)		(17.5)
Non-cash charges				(3.6)				(3.6)
Effect of foreign currency translation		0.6						0.6
Restructuring liability, December 31, 2013		6.8				0.1		6.9
2014 Activity:								
Recorded expense and accrual		4.4				0.5		4.9
Cash payments		(3.7)				(0.5)		(4.2)
Non-cash charges								
Effect of foreign currency translation								
Restructuring liability, March 31, 2014	\$	7.5	\$		\$	0.1	\$	7.6

Cash payments under the Energy Restructuring Plan were \$4.2 million during the first three months of 2014 and \$17.5 million during 2013. The majority of cash payments under this Plan are related to severance, with the current accrual expected to be paid over the next twelve months.

ECOLAB INC.

CONDENSED NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

2. Special (Gains) and Charges (continued)*Combined Restructuring Plan*

In February 2011, the company commenced a comprehensive plan to substantially improve the efficiency and effectiveness of its European business, as well as to undertake certain restructuring activities outside of Europe (the 2011 Restructuring Plan). Additionally, in January 2012, following the merger with Nalco Holding Company (Nalco), the company formally commenced plans to undertake restructuring actions related to the reduction of its global workforce and optimization of its supply chain and office facilities, including planned reductions of plant and distribution center locations (the Merger Restructuring Plan). During the first quarter of 2013, the company determined that because the objectives of the plans discussed above were aligned, the previously separate restructuring plans should be combined into one plan.

The combined restructuring plan (the Combined Plan) combines opportunities and initiatives from both plans and continues to follow the original format of the Merger Restructuring Plan by focusing on global actions related to optimization of the supply chain and office facilities, including reductions of plant and distribution center locations and the global workforce. Through substantial completion of the Combined Plan at the end of 2014, the company expects to incur pre-tax charges of approximately \$50 million (\$40 million after tax) during 2104. During 2013, the company incurred \$64 million (\$48 million after tax) of charges related to the Combined Plan.

The company anticipates that substantially all of the remaining Combined Plan pre-tax charges will represent net cash expenditures.

As a result of restructuring activities under the Combined Plan, the company recorded restructuring charges of \$23.7 million (\$19.8 million after tax) and \$20.8 million (\$14.3 million after tax), during the first quarter of 2014 and 2013, respectively.

Restructuring charges and activity related to the Combined Plan since inception of the underlying actions include the following:

(millions)	Combined Plan				Total
	Employee Termination Costs	Asset Disposals	Other		
2011 - 2013 Activity:					
Recorded expense and accrual	\$ 248.2	\$ (1.2)	\$ 30.7	\$	277.7
Net cash payments	(182.2)	9.1	(19.1)		(192.2)
Non-cash charges		(7.9)	(4.3)		(12.2)
Effect of foreign currency translation	(0.1)				(0.1)
Restructuring liability, December 31, 2013	65.9		7.3		73.2

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2014 Activity:

Recorded net expense and accrual	21.2			2.5		23.7
Net cash payments	(19.5)			(2.2)		(21.7)
Non-cash net charges						
Effect of foreign currency translation	0.5					0.5
Restructuring liability, March 31, 2014	\$ 68.1	\$	\$	7.6	\$	75.7

ECOLAB INC.

CONDENSED NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

2. Special (Gains) and Charges (continued)

Net cash payments under the Combined Plan were \$21.7 million during the first three months of 2014 and \$192.2 million from 2011 through 2013. The majority of cash payments under this Plan are related to severance, with the current accrual expected to be paid over a period of a few months to several quarters.

Non-restructuring Special (Gains) and Charges

Champion acquisition and integration costs

As a result of the Champion acquisition completed in 2013, the company incurred charges of \$6.5 million (\$4.1 million after tax) and \$10.0 million (\$7.1 million after tax) during the first quarter of 2014 and 2013, respectively.

Champion related costs incurred during the first quarter of 2014 and 2013 have been included as a component of special (gains) and charges and net interest expense on the Consolidated Statement of Income. Amounts included in special (gains) and charges include acquisition costs, advisory and legal fees and integration charges. Amounts included in net interest expense include the interest expense through the close date of the Champion transaction of the company's \$500 million public debt issuance in December 2012 as well as amortizable fees to secure term loans and short-term debt, all of which were initiated to fund the Champion acquisition. Further information related to the acquisition of Champion is included in Note 3.

Nalco merger and integration costs

As a result of the Nalco merger completed in 2011, the company incurred charges of \$1.3 million (\$0.9 million after tax) and \$3.8 million (\$2.7 million after tax) during the first quarter of 2014 and 2013, respectively. Nalco related special charges for 2014 and 2013 have been included as a component of special (gains) and charges on the Consolidated Statement of Income, and include integration charges.

Venezuelan currency devaluation

On February 8, 2013, the Venezuelan government devalued its currency, the Bolivar Fuerte (Bolivar). As a result of the devaluation, during the first quarter of 2013, the company recorded a charge of \$22.9 million (\$15.0 million after tax), reflected as a component of special (gains) and

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charges, due to the remeasurement of the local balance sheet. Due to the ownership structure in place in Venezuela, the company also reflected a portion of the impact of the devaluation as a component of net income (loss) attributable to noncontrolling interest on the Consolidated Statement of Income.

3. Acquisitions and Dispositions

Champion acquisition

On April 10, 2013, the company completed its acquisition of Champion, a global energy specialty products and services company delivering its offerings to the oil and gas industry. The total fair value of cash and stock consideration transferred to acquire all of Champion's stock was approximately \$2 billion. Champion's sales for the business acquired by the company were approximately \$1.3 billion in 2012. The business became part of the company's Global Energy reportable segment in the second quarter of 2013.

ECOLAB INC.

CONDENSED NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

3. Acquisitions and Dispositions (continued)

The company incurred certain acquisition related costs associated with the transaction that were expensed as incurred and are reflected in the Consolidated Statement of Income. A total of \$6.5 million and \$10.0 million were incurred during the first quarter of 2014 and 2013, respectively. Amounts included in special (gains) and charges include acquisition costs, advisory and legal fees and integration charges. Amounts included in net interest expense include the interest expense through the close date of the Champion transaction of the company's \$500 million public debt issuance in December 2012 as well as amortizable fees to secure term loans and short-term debt, all of which were initiated to fund the Champion acquisition.

The Champion acquisition has been accounted for using the acquisition method of accounting, which requires, among other things, that most assets acquired and liabilities assumed be recognized at fair value as of the acquisition date.

The following table summarizes the value of Champion assets acquired and liabilities assumed as of December 31, 2013. During 2013, adjustments of \$37.1 million were made to the preliminary purchase price allocation of the assets and liabilities assumed with a corresponding adjustment to goodwill.

Also summarized in the table, during the first quarter of 2014, net adjustments of \$16.9 million were made to the value of Champion assets acquired and liabilities assumed. As the adjustments were not significant, they have been recorded in 2014 and are not reflected in the 2013 Consolidated Balance Sheet. Purchase price allocations were finalized during the first quarter of 2014.

(millions)	Allocation at December 31, 2013	Purchase Price Adjustments	Final Allocation at March 31, 2014
Current assets	\$ 592.3	\$ (4.5)	\$ 587.8
Property, plant and equipment	357.8	(2.5)	355.3
Other assets	16.2	0.1	16.3
Identifiable intangible assets			
Customer relationships	840.0		840.0
Trademarks	120.0		120.0
Other technology	36.5		36.5
Total assets acquired	1,962.8	(6.9)	1,955.9
Current liabilities	409.5	3.6	413.1
Long-term debt	70.8		70.8
Net deferred tax liability	427.4	9.3	436.7
Noncontrolling interest and other liabilities	30.5	(2.9)	27.6
Total liabilities and noncontrolling interests assumed	938.2	10.0	948.2

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Goodwill	1,030.1	16.9	1,047.0
Total aggregate purchase price	2,054.7		