BROWN FORMAN CORP
Form 10-Q
December 07, 2016
United States
Securities and Exchange Commission
Washington, D.C. 20549

FORM 10-Q
(Mark One)

þ QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15 (d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the quarterly period ended October 31, 2016
OR
o 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. 001-00123

Brown-Forman Corporation
(Exact name of Registrant as specified in its Charter)

Delaware	61-0143150
(State or other jurisdiction of incorporation or organization)	(IRS Employer Identification No.)

850 Dixie Highway	
Louisville, Kentucky	40210
(Address of principal executive offices)	(Zip Code)

(502) 585-1100
(Registrant's telephone number, including area code)

N/A
(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 þ No o

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 during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes þ No o

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 þ	Accelerated filer o
Non-accelerated filer o (Do not check if a smaller reporting company)	Smaller reporting company o

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

Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date: November 30, 2016

Class A Common Stock ($.15 par value, voting)	169,054,545
Class B Common Stock ($.15 par value, nonvoting)	215,717,222

BROWN-FORMAN CORPORATION
Index to Quarterly Report Form 10-Q

PART I - FINANCIAL INFORMATION

Item 1. Financial Statements (Unaudited)

BROWN-FORMAN CORPORATION
CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS
(Unaudited)
(Dollars in millions, except per share amounts)

	Three Months Ended October 31,		Six Months Ended October 31,	
	2015	2016	2015	2016
Sales	$1,096	$1,055	$1,995	$1,911
Excise taxes	242	225	444	420
Net sales	854	830	1,551	1,491
Cost of sales	268	278	475	486
Gross profit	586	552	1,076	1,005
Advertising expenses	115	107	209	190
Selling, general, and administrative expenses	171	163	340	326
Other expense (income), net	(2)	(9)	(2)	(15)
Operating income	302	291	529	504
Interest income	—	1	1	1
Interest expense	12	16	22	28
Income before income taxes	290	276	508	477
Income taxes	90	79	152	135
Net income	$200	$197	$356	$342
Earnings per share:				
Basic	$0.49	$0.51	$0.87	$0.87
Diluted	$0.49	$0.50	$0.86	$0.87
Cash dividends per common share:				
Declared	$—	$—	$0.3150	$0.3400
Paid	$0.1575	$0.1700	$0.3150	$0.3400

See notes to the condensed consolidated financial statements.

3

BROWN-FORMAN CORPORATION
CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME
(Unaudited)
(Dollars in millions)

	Three Months Ended		Six Months Ended	
	October 31,		October 31,	
	2015	2016	2015	2016
Net income	$200	$197	$356	$342
Other comprehensive income (loss), net of tax:				
Currency translation adjustments	(4)	(18)	(28)	(85)
Cash flow hedge adjustments	(4)	9	12	21
Postretirement benefits adjustments	6	4	10	7
Net other comprehensive income (loss)	(2)	(5)	(6)	(57)
Comprehensive income	$198	$192	$350	$285

See notes to the condensed consolidated financial statements.

BROWN-FORMAN CORPORATION
CONDENSED CONSOLIDATED BALANCE SHEETS
(Unaudited)
(Dollars in millions)

	April 30, 2016	October 31, 2016
Assets		
Cash and cash equivalents	$ 263	$ 211
Accounts receivable, less allowance for doubtful accounts of $9 and $9 at April 30 and October 31, respectively	559	660
Inventories:		
Barreled whiskey	666	833
Finished goods	187	235
Work in process	116	121
Raw materials and supplies	85	97
Total inventories	1,054	1,286
Other current assets	357	373
Total current assets	2,233	2,530
Property, plant and equipment, net	629	651
Goodwill	590	743
Other intangible assets	595	640
Deferred tax assets	17	16
Other assets	119	140
Total assets	$ 4,183	$ 4,720
Liabilities		
Accounts payable and accrued expenses	$ 501	$ 554
Accrued income taxes	19	13
Short-term borrowings	271	337
Total current liabilities	791	904
Long-term debt	1,230	1,917
Deferred tax liabilities	101	150
Accrued pension and other postretirement benefits	353	335
Other liabilities	146	131
Total liabilities	2,621	3,437
Commitments and contingencies		
Stockholders' Equity		
Common stock:		
Class A, voting, $0.15 par value	13	25
Class B, nonvoting, $0.15 par value	21	43
Additional paid-in capital	114	74
Retained earnings	4,065	4,283
Accumulated other comprehensive income (loss), net of tax	(350)	(407)
Treasury stock, at cost (59,143,000 and 68,230,000 shares at April 30 and October 31, respectively)	(2,301)	(2,735)
Total stockholders' equity	1,562	1,283
Total liabilities and stockholders' equity	$ 4,183	$ 4,720

See notes to the condensed consolidated financial statements.

BROWN-FORMAN CORPORATION
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
(Unaudited)
(Dollars in millions)

	Six Months Ended October 31,	
	2015	2016
Cash flows from operating activities:		
Net income	$356	$342
Adjustments to reconcile net income to net cash provided by operations:		
Depreciation and amortization	27	28
Stock-based compensation expense	8	7
Deferred income taxes	(8)	(7)
Changes in assets and liabilities, excluding the effects of acquisition of business	(222)	(201)
Cash provided by operating activities	161	169
Cash flows from investing activities:		
Acquisition of business, net of cash acquired	—	(307)
Additions to property, plant, and equipment	(65)	(36)
Computer software expenditures	(1)	(1)
Cash used for investing activities	(66)	(344)
Cash flows from financing activities:		
Net change in short-term borrowings	113	6
Proceeds from long-term debt	490	717
Debt issuance costs	(5)	(5)
Net payments related to exercise of stock-based awards	(6)	(5)
Excess tax benefits from stock-based awards	13	—
Acquisition of treasury stock	(739)	(442)
Dividends paid	(130)	(134)
Cash provided by (used for) financing activities	(264)	137
Effect of exchange rate changes on cash and cash equivalents	(6)	(14)
Net decrease in cash and cash equivalents	(175)	(52)
Cash and cash equivalents, beginning of period	370	263
Cash and cash equivalents, end of period	$195	$211

See notes to the condensed consolidated financial statements.

6

BROWN-FORMAN CORPORATION
NOTES TO THE CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited)

In these notes, “we,” “us,” and “our” refer to Brown-Forman Corporation.

1. Condensed Consolidated Financial Statements

We prepared the accompanying unaudited condensed consolidated financial statements pursuant to the rules and regulations of the U.S. Securities and Exchange Commission for interim financial information. In accordance with those rules and regulations, we condensed or omitted certain information and disclosures normally included in annual financial statements prepared in accordance with U.S. generally accepted accounting principles (GAAP). We suggest that you read these condensed financial statements together with the financial statements and footnotes included in our annual report on Form 10-K for the fiscal year ended April 30, 2016 (2016 Form 10-K).

In our opinion, the accompanying financial statements include all adjustments, consisting only of normal recurring adjustments (unless otherwise indicated), necessary for a fair statement of our financial results for the periods covered by this report.

We prepared the accompanying financial statements on a basis that is substantially consistent with the accounting principles applied in our 2016 Form 10-K, but made the following changes during fiscal 2017:

- Effective beginning May 1, 2016, we changed our presentation of excise taxes from the gross method (included in sales and costs) to the net method (excluded from sales). As a result, the amounts presented as “net sales” in our financial statements now exclude excise taxes. We believe the change in presentation to the net method is preferable because it is more representative of the internal financial information reviewed by management in assessing our performance and more consistent with the presentation used by our major competitors in their external financial statements. Prior period financial statements have been recast to conform to the new presentation.

- We adopted new guidance related to certain aspects of the accounting for stock-based compensation, including the income tax consequences. Under the new guidance, we recognize all tax benefits related to stock-based compensation as an income tax benefit in our statement of operations, and include all income tax cash flows within operating activities in our statement of cash flows. Under the previous accounting guidance, we recognized some of those tax benefits (excess tax benefits) as additional paid-in capital and classified that amount as a financing activity in our statement of cash flows. We adopted these provisions of the new guidance on a prospective basis as of May 1, 2016. As a result, our net income and operating cash flows for the six months ended October 31, 2016, include excess tax benefits of $3 million. Prior period financial statements have not been adjusted.

Also, under the new guidance, we recognize the excess tax benefits during the period in which the related awards vest or are exercised. Under the previous accounting guidance, we recognized those benefits during the period in which they reduced taxes payable. We adopted this provision of the new guidance on a modified retrospective basis with a cumulative-effect adjustment of $10 million to retained earnings as of May 1, 2016.

Also, as discussed in Note 12, our Class A and Class B common shares were split on a two-for-one basis during August 2016. As a result, all share and per share amounts reported in the accompanying financial statements and related notes are presented on a split-adjusted basis.

New accounting pronouncements to be adopted. The Financial Accounting Standards Board (FASB) has issued new accounting guidance on various topics that may impact our financial statements upon our adoption of the new guidance. The following table shows the date by which we must adopt the new guidance for each topic and the permitted method(s) of adoption:

Topic	Date	Method(s)
Revenue from contracts with customers	May 1, 2018	Retrospective or modified retrospective
Classification of certain cash receipts and cash payments on statement of cash flows	May 1, 2018	Retrospective
Income tax consequences of intra-entity transfers of assets other than inventory	May 1, 2018	Modified retrospective
Leases	May 1, 2019	Modified retrospective
Credit losses	May 1, 2020	Modified retrospective

We are currently evaluating the potential impact of the new guidance on our financial statements. While we have not yet determined our plans for adoption, we do not currently expect to adopt any of the new guidance prior to the required adoption date.

2. Inventories

Inventories are valued at the lower of cost or market. Some of our consolidated inventories are valued using the last-in, first-out (LIFO) method, which we use for the majority of our U.S. inventories. If the LIFO method had not been used, inventories at current cost would have been $248 million higher than reported as of April 30, 2016, and $258 million higher than reported as of October 31, 2016. Changes in the LIFO valuation reserve for interim periods are based on a proportionate allocation of the estimated change for the entire fiscal year.

3. Income Taxes

Our consolidated interim effective tax rate is based upon our expected annual operating income, statutory tax rates, and income tax laws in the various jurisdictions in which we operate. Significant or unusual items, including adjustments to accruals for tax uncertainties, are recognized in the quarter in which the related event occurs. The effective tax rate of 28.4% for the six months ended October 31, 2016, is based on an expected tax rate of 29.2% on ordinary income for the full fiscal year, as adjusted for the recognition of a net tax benefit related to discrete items arising during the period and interest on previously provided tax contingencies. Our expected tax rate includes current fiscal year additions for existing tax contingency items.

As discussed in Note 1, we adopted new accounting guidance for stock-based compensation, including the income tax consequences. As a result, our effective tax rate for the six months ended October 31, 2016, reflects the impact of $3 million of tax benefits related to stock-based compensation that we recognized as a discrete item during the period.

4. Earnings Per Share

We calculate basic earnings per share by dividing net income available to common stockholders by the weighted average number of common shares outstanding during the period. Diluted earnings per share further includes the dilutive effect of stock-based compensation awards. We calculate that dilutive effect using the “treasury stock method” (as defined by GAAP).

The following table presents information concerning basic and diluted earnings per share:

(Dollars in millions, except per share amounts)	Three Months Ended October 31,		Six Months Ended October 31,	
	2015	2016	2015	2016
Net income available to common stockholders	$200	$ 197	$356	$ 342
Share data (in thousands):				
Basic average common shares outstanding	408,110	389,050	411,116	390,994
Dilutive effect of stock-based awards	2,751	2,798	2,750	2,895
Diluted average common shares outstanding	410,861	391,848	413,866	393,889
Basic earnings per share	$0.49	$ 0.51	$0.87	$ 0.87
Diluted earnings per share	$0.49	$ 0.50	$0.86	$ 0.87

We excluded common stock-based awards for approximately 830,000 shares and 1,937,000 shares from the calculation of diluted earnings per share for the three months ended October 31, 2015 and 2016, respectively. We excluded common stock-based awards for approximately 1,059,000 shares and 1,555,000 shares from the calculation of diluted earnings per share for the six months ended October 31, 2015 and 2016, respectively. We excluded those awards because they were not dilutive for those periods under the treasury stock method.

5. Commitments and Contingencies

We operate in a litigious environment, and we are sued in the normal course of business. Sometimes plaintiffs seek substantial damages. Significant judgment is required in predicting the outcome of these suits and claims, many of which take years to adjudicate. We accrue estimated costs for a contingency when we believe that a loss is probable and we can make a reasonable estimate of the loss, and then adjust the accrual as appropriate to reflect changes in facts and circumstances. We do not believe it is reasonably possible that these existing loss contingencies, individually or in the aggregate, would have a material adverse effect on our financial position, results of operations, or liquidity. No material accrued loss contingencies are recorded as of October 31, 2016.

We have guaranteed the repayment by a third-party importer of its obligation under a bank credit facility that it uses in connection with its importation of our products in Russia. If the importer were to default on that obligation, which we believe is unlikely, our maximum possible exposure under the existing terms of the guaranty would be approximately $22 million (subject to changes in foreign currency exchange rates). Both the fair value and carrying amount of the guaranty are insignificant.

As of October 31, 2016, our actual exposure under the guaranty of the importer's obligation is approximately $11 million. We also have accounts receivable from that importer of approximately $14 million at October 31, 2016, which we expect to collect in full.

Based on the financial support we provide to the importer, we believe it meets the definition of a variable interest entity. However, because we do not control this entity, it is not included in our consolidated financial statements.

6. Debt

Our long-term debt (net of unamortized discount and issuance costs) consists of:

(Principal and carrying amounts in millions)	April 30, 2016	October 31, 2016
1.00% notes, $250 principal amount, due January 15, 2018	$ 249	$ 249
2.25% notes, $250 principal amount, due January 15, 2023	248	248
1.20% notes, €300 principal amount, due July 7, 2026	—	326

2.60% notes, £300 principal amount, due July 7, 2028	—	360
3.75% notes, $250 principal amount, due January 15, 2043	248	248
4.50% notes, $500 principal amount, due July 15, 2045	485	486
	$ 1,230	$ 1,917

We issued senior, unsecured notes with an aggregate principal amount of 300 million euros in July 2016. Interest on these notes will accrue at a rate of 1.20% and be paid annually. As of October 31, 2016, the carrying amount of these notes was $326 million ($329 million principal, less unamortized discounts and issuance costs). These notes are due on July 7, 2026.

In addition, we issued senior, unsecured notes with an aggregate principal amount of 300 million British pounds in July 2016. Interest on these notes will accrue at a rate of 2.60% and be paid annually. As of October 31, 2016, the carrying amount of these notes was $360 million ($365 million principal, less unamortized discounts and issuance costs). These notes are due on July 7, 2028.

As of April 30, 2016, our short-term borrowings of $271 million included $269 million of commercial paper, with an average interest rate of 0.53% and a remaining maturity of 26 days. As of October 31, 2016, our short-term borrowings of $337 million included $335 million of commercial paper, with an average interest rate of 0.60% and a remaining maturity of 10 days.

7. Pension and Other Postretirement Benefits

The following table shows the components of the pension and other postretirement benefit cost recognized for our U.S. benefit plans. Information about similar international plans is not presented due to immateriality.

	Three Months Ended October 31,		Six Months Ended October 31,	
(Dollars in millions)	2015	2016	2015	2016
Pension Benefits:				
Service cost	$6	$6	$13	$13
Interest cost	9	9	17	18
Expected return on plan assets	(10)	(10)	(20)	(21)
Amortization of net actuarial loss	7	6	14	13
Net cost	$12	$11	$24	$23
Other Postretirement Benefits:				
Service cost	$—	$—	$1	$1
Interest cost	1	1	1	1
Amortization of prior service cost (credit)	(1)	(1)	(1)	(1)
Net cost	$—	$—	$1	$1

8. Fair Value Measurements

Fair value is defined as the exchange price that would be received for an asset or paid to transfer a liability in the principal or most advantageous market for the asset or liability in an orderly transaction between market participants at the measurement date. We categorize the fair values of assets and liabilities into three levels based upon the assumptions (inputs) used to determine those values. Level 1 provides the most reliable measure of fair value, while Level 3 generally requires significant management judgment. The three levels are:

- Level 1 – Quoted prices (unadjusted) in active markets for identical assets or liabilities.
- Level 2 – Observable inputs other than those included in Level 1, such as quoted prices for similar assets and liabilities in active markets; quoted prices for identical or similar assets and liabilities in inactive markets; or other inputs that are observable or can be derived from or corroborated by observable market data.
- Level 3 – Unobservable inputs that are supported by little or no market activity.

The following table summarizes the assets and liabilities measured or disclosed at fair value on a recurring basis:

(Dollars in millions)	Level 1	Level 2	Level 3	Total
April 30, 2016:				
Assets:				
Currency derivatives	$ —	$ 19	$ —	$ 19
Liabilities:				
Currency derivatives	—	10	—	10
Short-term borrowings	—	271	—	271
Long-term debt	—	1,293	—	1,293
October 31, 2016:				
Assets:				
Currency derivatives	—	50	—	50
Liabilities:				
Currency derivatives	—	6	—	6
Short-term borrowings	—	337	—	337
Long-term debt	—	2,011	—	2,011

We determine the fair values of our currency derivatives (forward contracts) using standard valuation models. The significant inputs used in these models, which are readily available in public markets or can be derived from observable market transactions, include the applicable exchange rates, forward rates, and discount rates. The discount rates are based on the historical U.S. Treasury rates.

The fair value of short-term borrowings approximates their carrying amount. We determine the fair value of long-term debt primarily based on the prices at which similar debt has recently traded in the market and also considering the overall market conditions on the date of valuation.

We measure some assets and liabilities at fair value on a nonrecurring basis. That is, we do not measure them at fair value on an ongoing basis, but we do adjust them to fair value in some circumstances (for example, when we determine that an asset is impaired). No material nonrecurring fair value measurements were required during the periods presented in these financial statements.

9. Fair Value of Financial Instruments

The fair value of cash, cash equivalents, and short-term borrowings approximate the carrying amounts due to the short maturities of these instruments. We determine the fair value of currency derivatives and long-term debt as discussed in Note 8.

Below is a comparison of the fair values and carrying amounts of these instruments:

	April 30, 2016		October 31, 2016	
(Dollars in millions)	Carrying Amount	Fair Value	Carrying Amount	Fair Value
Assets:				
Cash and cash equivalents	$263	$263	$211	$211
Currency derivatives	19	19	50	50
Liabilities:				
Currency derivatives	10	10	6	6
Short-term borrowings	271	271	337	337
Long-term debt	1,230	1,293	1,917	2,011

10. Derivative Financial Instruments and Hedging Activities

Our multinational business exposes us to global market risks, including the effect of fluctuations in currency exchange rates, commodity prices, and interest rates. We use derivatives to help manage financial exposures that occur in the normal course of business. We formally document the purpose of each derivative contract, which includes linking the contract to the financial exposure it is designed to mitigate. We do not hold or issue derivatives for trading or speculative purposes.

We use currency derivative contracts to limit our exposure to the currency exchange risk that we cannot mitigate internally by using netting strategies. We designate most of these contracts as cash flow hedges of forecasted transactions (expected to occur within three years). We record all changes in the fair value of cash flow hedges (except any ineffective portion) in accumulated other comprehensive income (AOCI) until the underlying hedged transaction occurs, at which time we reclassify that amount into earnings. We assess the effectiveness of these hedges based on changes in forward exchange rates. The ineffective portion of the changes in fair value of our hedges (recognized immediately in earnings) during the periods presented in this report was not material.

We had outstanding currency derivatives, related primarily to our euro, British pound, and Australian dollar exposures, with notional amounts totaling $1,265 million at April 30, 2016 and $1,176 million at October 31, 2016.

During the six months ended October 31, 2016, we used some currency derivative forward contracts and foreign currency-denominated long-term debt as after-tax net investment hedges of our investments in certain foreign subsidiaries. Any change in value of the designated portion of the hedging instruments is recorded in AOCI, offsetting the foreign currency translation adjustment of the related net investments that is also recorded in AOCI. As of October 31, 2016, $515 million of our foreign currency-denominated debt was designated as a net investment hedge. Our net investment hedges are intended to mitigate foreign exchange exposure related to non-U.S. dollar net investments in certain foreign subsidiaries against changes in foreign exchange rates. There was no ineffectiveness related to our net investment hedges during the periods presented in this report.

We do not designate some of our currency derivatives and foreign currency-denominated debt as hedges because we use them to at least partially offset the immediate earnings impact of changes in foreign exchange rates on existing assets or liabilities. We immediately recognize the change in fair value of these instruments in earnings.

We use forward purchase contracts with suppliers to protect against corn price volatility. We expect to physically take delivery of the corn underlying each contract and use it for production over a reasonable period of time. Accordingly, we account for these contracts as normal purchases rather than derivative instruments.

During May 2015, we entered into interest rate derivative contracts (U.S. Treasury lock agreements) to manage the interest rate risk related to the anticipated issuance of fixed-rate senior, unsecured notes. We designated the contracts as cash flow hedges of the future interest payments associated with the anticipated notes. Upon issuance in June 2015 of an aggregate principal amount of $500 million of the 4.50% notes, due July 15, 2045, we settled the contracts for a gain of $8 million. The entire gain was recorded to AOCI and will be amortized as a reduction of interest expense over the life of the notes.

The following tables present the pre-tax impact that changes in the fair value of our derivative instruments and non-derivative hedging instruments had on AOCI and earnings:

(Dollars in millions)	Classification	Three Months Ended October 31, 2015	2016
Derivative Instruments			
Currency derivatives designated as cash flow hedges:			
Net gain (loss) recognized in AOCI	n/a	$9	$23
Net gain (loss) reclassified from AOCI into income	Net sales	17	9
Interest rate derivatives designated as cash flow hedges:			
Net gain (loss) recognized in AOCI	n/a	—	—
Currency derivatives designated as net investment hedge:			
Net gain (loss) recognized in AOCI	n/a	—	—
Currency derivatives not designated as hedging instruments:			
Net gain (loss) recognized in income	Net sales	—	2
Net gain (loss) recognized in income	Other income	—	(3)
Non-Derivative Hedging Instruments			
Foreign currency-denominated debt designated as net investment hedge:			
Net gain (loss) recognized in AOCI	n/a	—	34
Foreign currency-denominated debt not designated as hedging instrument:			
Net gain (loss) recognized in income	Other income	—	3

(Dollars in millions)	Classification	Six Months Ended October 31, 2015	2016
Derivative Instruments			
Currency derivatives designated as cash flow hedges:			
Net gain (loss) recognized in AOCI	n/a	$38	$52
Net gain (loss) reclassified from AOCI into income	Net sales	30	19
Interest rate derivatives designated as cash flow hedges:			
Net gain (loss) recognized in AOCI	n/a	8	—
Currency derivatives designated as net investment hedge:			
Net gain (loss) recognized in AOCI	n/a	—	8
Currency derivatives not designated as hedging instruments:			
Net gain (loss) recognized in income	Net sales	3	3
Net gain (loss) recognized in income	Other income	4	(8)
Non-Derivative Hedging Instruments			
Foreign currency-denominated debt designated as net investment hedge:			
Net gain (loss) recognized in AOCI	n/a	—	24
Foreign currency-denominated debt not designated as hedging instrument:			
Net gain (loss) recognized in income	Other income	—	2

We expect to reclassify $27 million of deferred net gains on cash flow hedges recorded in AOCI as of October 31, 2016, to earnings during the next 12 months. This reclassification would offset the anticipated earnings impact of the underlying hedged exposures. The actual amounts that we ultimately reclassify to earnings will depend on the exchange rates in effect when the underlying hedged transactions occur. As of October 31, 2016, the maximum term of our outstanding derivative contracts was 36 months.

The following table presents the fair values of our derivative instruments:

(Dollars in millions)	Classification	Fair value of derivatives in a gain position	Fair value of derivatives in a loss position
April 30, 2016:			
Designated as cash flow hedges:			
Currency derivatives	Other current assets	$ 23	$ (2)
Currency derivatives	Other assets	3	(2)
Currency derivatives	Accrued expenses	4	(8)
Currency derivatives	Other liabilities	3	(9)
Not designated as hedges:			
Currency derivatives	Other current assets	1	(4)
October 31, 2016:			
Designated as cash flow hedges:			
Currency derivatives	Other current assets	35	(3)
Currency derivatives	Other assets	24	(5)
Currency derivatives	Accrued expenses	5	(5)
Currency derivatives	Other liabilities	—	(1)
Not designated as hedges:			
Currency derivatives	Other current assets	1	(2)
Currency derivatives	Accrued expenses	—	(5)

The fair values reflected in the above table are presented on a gross basis. However, as discussed further below, the fair values of those instruments that are subject to net settlement agreements are presented in our balance sheets on a net basis.

In our statement of cash flows, we classify cash flows related to cash flow hedges in the same category as the cash flows from the hedged items.

Credit risk. We are exposed to credit-related losses if the counterparties to our derivative contracts default. This credit risk is limited to the fair value of the contracts. To manage this risk, we contract only with major financial institutions that have earned investment-grade credit ratings and with whom we have standard International Swaps and Derivatives Association (ISDA) agreements that allow for net settlement of the derivative contracts. Also, we have established counterparty credit guidelines that are regularly monitored and that provide for reports to senior management according to prescribed guidelines, and we monetize contracts when we believe it is warranted. Because of these safeguards, we believe we have no derivative positions that warrant credit valuation adjustments.

Some of our derivative instruments require us to maintain a specific level of creditworthiness, which we have maintained. If our creditworthiness were to fall below that level, then the counterparties to our derivative instruments could request immediate payment or collateralization for derivative instruments in net liability positions. The aggregate fair value of all derivatives with creditworthiness requirements that were in a net liability position was $8 million at April 30, 2016 and $6 million at October 31, 2016.

Offsetting. As noted above, our derivative contracts are governed by ISDA agreements that allow for net settlement of derivative contracts with the same counterparty. It is our policy to present the fair values of current derivatives (i.e., those with a remaining term of 12 months or less) with the same counterparty on a net basis in the balance sheet. Similarly, we present the fair values of noncurrent derivatives with the same counterparty on a net basis. Current derivatives are not netted with noncurrent derivatives in the balance sheet. The following table summarizes the gross and net amounts of our derivative contracts:

(Dollars in millions)	Gross Amounts of Recognized Assets (Liabilities)	Gross Amounts Offset in Balance Sheet	Net Amounts Presented in Balance Sheet	Gross Amounts Not Offset in Balance Sheet	Net Amounts
April 30, 2016:					
Derivative assets	$ 34	$ (15)	$ 19	$ (6)	$ 13
Derivative liabilities	(25)	15	(10)	6	(4)
October 31, 2016:					
Derivative assets	65	(15)	50	—	50
Derivative liabilities	(21)	15	(6)	—	(6)

No cash collateral was received or pledged related to our derivative contracts as of April 30, 2016 and October 31, 2016.

11. Goodwill and Other Intangible Assets

The following table summarizes the changes in goodwill and other intangible assets during the six months ended October 31, 2016:

(Dollars in millions)	Goodwill	Other Intangible Assets
Balance at April 30, 2016	$ 590	$ 595
Acquisitions (Note 14)	182	65
Foreign currency translation adjustment	(29)	(20)
Balance at October 31, 2016	$ 743	$ 640

Our other intangible assets consist of trademarks and brand names, all with indefinite useful lives.

12. Stockholders' Equity

The following table summarizes the changes in stockholders' equity during the six months ended October 31, 2016:

(Dollars in millions)	Class A Common Stock	Class B Common Stock	Additional Paid-in Capital	Retained Earnings	AOCI	Treasury Stock	Total
Balance at April 30, 2016	$ 13	$ 21	$ 114	$ 4,065	$ (350)	$ (2,301)	$ 1,562
Cumulative effect of change in accounting principle (Note 1)				10			10
Net income				342			342
Net other comprehensive income (loss)					(57)		(57)
Cash dividends				(134)			(134)
Acquisition of treasury stock						(442)	(442)
Stock-based compensation expense			7				7
Stock issued under compensation plans						8	8
Loss on issuance of treasury stock issued under compensation plans			(13)				(13)
Stock split	12	22	(34)				—
Balance at October 31, 2016	$ 25	$ 43	$ 74	$ 4,283	$ (407)	$ (2,735)	$ 1,283

15

Stock split. On May 26, 2016, our Board of Directors approved a two-for-one stock split for our Class A and Class B common stock, subject to stockholder approval of an amendment to our Restated Certificate of Incorporation. The amendment, which was approved by stockholders on July 28, 2016, increased the number of authorized shares of Class A common stock from 85,000,000 to 170,000,000. The amendment did not change the number of authorized Class B common shares, which remains at 400,000,000.

The stock split, which was effected as a stock dividend, resulted in the issuance of one new share of Class A common stock for each share of Class A common stock outstanding and one new share of Class B common stock for each share of Class B common stock outstanding. The stock split was also applied to our treasury shares. Thus, the stock split increased the number of Class A shares issued from 85,000,000 to 170,000,000, and increased the number of Class B shares issued from 142,313,000 to 284,626,000. The new shares were distributed on August 18, 2016, to shareholders of record as of August 8, 2016.

As a result of the stock split, we reclassified approximately $34 million from additional paid-in capital to common stock during the quarter ended July 31, 2016. The $34 million represents the $0.15 par value per share of the new shares issued in the stock split.

All share and per share amounts reported in the accompanying financial statements and related notes are presented on a split-adjusted basis.

Dividends. The following table summarizes the cash dividends declared per share on our Class A and Class B common stock during the six months ended October 31, 2016:

Declaration Date	Record Date	Payable Date	Amount per Share
May 26, 2016	June 6, 2016	July 1, 2016	$0.17
July 28, 2016	September 1, 2016	October 3, 2016	$0.17

As announced on November 17, 2016, our Board of Directors increased the quarterly cash dividend on our Class A and Class B common stock from $0.17 per share to $0.1825 per share. Stockholders of record on December 2, 2016, will receive the cash dividend on January 3, 2017.

Accumulated Other Comprehensive Income. The following table summarizes the changes in each component of AOCI, net of tax, during the six months ended October 31, 2016:

(Dollars in millions)	Currency Translation Adjustments	Cash Flow Hedge Adjustments	Postretirement Benefits Adjustments	Total AOCI
Balance at April 30, 2016	$ (131)	$ 11	$ (230)	$(350)
Net other comprehensive income (loss)	(85)	21	7	(57)
Balance at October 31, 2016	$ (216)	$ 32	$ (223)	$(407)

16

13. Other Comprehensive Income

The following tables present the components of net other comprehensive income (loss):

	Three Months Ended October 31, 2015			Three Months Ended October 31, 2016		
(Dollars in millions)	Pre-Tax	Tax	Net	Pre-Tax	Tax	Net
Currency translation adjustments:						
Net gain (loss) on currency translation	$(4)	$ —	$(4)	$(4)	$(14)	$(18)
Reclassification to earnings	—	—	—	—	—	—
Other comprehensive income (loss), net	(4)	—	(4)	(4)	(14)	(18)
Cash flow hedge adjustments:						
Net gain (loss) on hedging instruments	9	(3)	6	23	(9)	14
Reclassification to earnings[1]	(17)	7	(10)	(9)	4	(5)
Other comprehensive income (loss), net	(8)	4	(4)	14		