

ARMSTRONG WORLD INDUSTRIES INC

Form 10-Q

July 30, 2012

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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 June 30, 2012

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 1-2116

ARMSTRONG WORLD INDUSTRIES, INC.

(Exact name of registrant as specified in its charter)

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Pennsylvania
(State or other jurisdiction of
incorporation or organization)

23-0366390
(I.R.S. Employer
Identification No.)

2500 Columbia Avenue, Lancaster, Pennsylvania
(Address of principal executive offices)

17603
(Zip Code)

Registrant's telephone number, including area code (717) 397-0611

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 Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter time 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 (Check one):

Large accelerated filer Accelerated filer
Non-accelerated filer 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

Number of shares of Armstrong World Industries, Inc.'s common stock outstanding as of July 24, 2012 58,812,970.

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Cautionary Note Regarding Forward-Looking Statements

Certain information included in this report and in our other materials we have filed or will file with the Securities and Exchange Commission (SEC), as well as information included in oral statements or other written statements made or to be made by us, contains or may contain forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995 (the PSLRA). Those statements provide our future expectations or forecasts and can be identified by our use of words such as anticipate, estimate, expect, project, intend, plan, outlook, and other words or phrases of similar meaning in connection with any discussion of future operating or financial performance or the outcome of contingencies such as liabilities or legal proceedings.

Forward-looking statements, by their nature, address matters that are uncertain and involve risks (such as those referenced in Part II, Item 1A, Risk Factors of this report) because they relate to events and depend on circumstances that may or may not occur in the future. The risks and uncertainties identified in the forward-looking statements contained in this report, together with those previously disclosed in our SEC filings, or those that are presently unforeseen, could result in significant adverse effects on our financial condition, results of operations and cash flows, and cause our actual results to differ materially from our expectations and from those expressed in our forward-looking statements.

We try to reduce the likelihood that these and other risks will significantly affect our businesses, as well as their potential impact. However, no matter how accurate our foresight, how well we evaluate risks, and how effective we are at mitigating them, one or more of these risks could have serious consequences for us, and could cause a material adverse effect on our business. See the related discussions in this document and our other SEC filings and other public documents for more details relating to the risks and uncertainties impacting our businesses. Forward-looking statements speak only as of the date they are made. We undertake no obligation to update any forward-looking statements beyond what is required under applicable securities law.

This discussion is provided as permitted by the PSLRA, and all of our forward-looking statements are expressly qualified in their entirety by the cautionary statements contained or referenced in this section.

Table of Contents**PART I****ITEM 1. FINANCIAL STATEMENTS**

Armstrong World Industries, Inc., and Subsidiaries

Condensed Consolidated Statements of Earnings and Comprehensive Income

(amounts in millions, except per share data)

Unaudited

	Three Months Ended June 30, 2012	Three Months Ended June 30, 2011	Six Months Ended June 30, 2012	Six Months Ended June 30, 2011
Net sales	\$ 709.9	\$ 748.6	\$ 1,377.9	\$ 1,433.8
Cost of goods sold	533.7	563.9	1,056.9	1,088.4
Gross profit	176.2	184.7	321.0	345.4
Selling, general and administrative expenses	114.2	122.2	230.8	242.3
Restructuring charges, net		2.4	0.2	7.3
Equity earnings from joint venture	(14.9)	(12.6)	(28.5)	(29.0)
Operating income	76.9	72.7	118.5	124.8
Interest expense	14.4	11.5	25.6	26.3
Other non-operating expense	0.3	0.8	0.3	1.1
Other non-operating (income)	(0.7)	(0.8)	(1.5)	(1.4)
Earnings before income taxes	62.9	61.2	94.1	98.8
Income tax expense	21.1	23.3	34.1	47.4
Earnings	\$ 41.8	\$ 37.9	\$ 60.0	\$ 51.4
Other comprehensive income (loss), net of tax:				
Foreign currency translation adjustments	(8.6)	4.0	(3.3)	15.4
Derivative (loss)	(2.0)	(3.5)	(4.3)	(2.4)
Pension and postretirement adjustments	2.5	3.2	4.9	6.5
Total other comprehensive (loss) income	(8.1)	3.7	(2.7)	19.5
Total comprehensive income	\$ 33.7	\$ 41.6	\$ 57.3	\$ 70.9
Earnings per share of common stock:				
Basic	\$ 0.71	\$ 0.64	\$ 1.02	\$ 0.88
Diluted	\$ 0.70	\$ 0.64	\$ 1.01	\$ 0.87
Average number of common shares outstanding:				
Basic	58.8	58.3	58.7	58.2
Diluted	59.4	58.9	59.3	58.8
Dividend declared per common share			\$ 8.55	

See accompanying notes to Condensed Consolidated Financial Statements beginning on page 8.

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Armstrong World Industries, Inc., and Subsidiaries

Condensed Consolidated Balance Sheets

(amounts in millions, except share data)

	Unaudited June 30, 2012	December 31, 2011
<u>Assets</u>		
Current assets:		
Cash and cash equivalents	\$ 217.3	\$ 480.6
Accounts and notes receivable, net	281.3	232.5
Inventories, net	403.4	388.9
Deferred income taxes	21.3	45.3
Income tax receivable	23.4	23.4
Other current assets	46.8	38.6
Total current assets	993.5	1,209.3
Property, plant, and equipment, less accumulated depreciation and amortization of \$548.0 and \$506.4, respectively	918.4	902.9
Prepaid pension costs	76.1	58.0
Investment in joint venture	135.9	141.0
Intangible assets, net	538.0	545.1
Restricted cash		1.5
Deferred income taxes	43.3	46.4
Other noncurrent assets	98.2	90.5
Total assets	\$ 2,803.4	\$ 2,994.7
<u>Liabilities and Shareholders' Equity</u>		
Current liabilities:		
Short-term debt	\$ 6.2	\$ 2.0
Current installments of long-term debt	34.9	18.1
Accounts payable and accrued expenses	347.9	359.6
Dividends payable	4.9	
Income tax payable	11.0	4.0
Deferred income taxes	2.4	2.4
Total current liabilities	407.3	386.1
Long-term debt, less current installments	1,054.5	822.9
Postretirement benefit liabilities	265.1	272.2
Pension benefit liabilities	195.0	206.7
Other long-term liabilities	89.1	78.9
Income taxes payable	38.7	36.7
Deferred income taxes	58.2	61.0
Total noncurrent liabilities	1,700.6	1,478.4
Shareholders' equity:		
Common stock, \$0.01 par value per share, authorized 200 million shares; issued 58,812,184 shares in 2012 and 58,424,691 shares in 2011	0.6	0.6
Capital in excess of par value	1,070.8	1,467.5
Retained earnings	41.8	77.1
Accumulated other comprehensive (loss)	(417.7)	(415.0)

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Total shareholders' equity	695.5	1,130.2
Total liabilities and shareholders' equity	\$ 2,803.4	\$ 2,994.7

See accompanying notes to Condensed Consolidated Financial Statements beginning on page 8.

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Armstrong World Industries, Inc., and Subsidiaries

Condensed Consolidated Statements of Shareholders' Equity

(amounts in millions)

Unaudited

	Common Stock		Six Months Ended June 30, 2012			
	Shares	Amount	Additional Paid-In Capital	Retained Earnings	Accumulated	Total
					Other Comprehensive (Loss)	
Balance at beginning of year	58,424,691	\$ 0.6	\$ 1,467.5	\$ 77.1	(\$ 415.0)	\$ 1,130.2
Stock issuance	387,493					
Share-based employee compensation			16.2			16.2
Earnings				60.0		60.0
Dividends			(412.9)	(95.3)		(508.2)
Other comprehensive loss					(2.7)	(2.7)
Balance at June 30	58,812,184	\$ 0.6	\$ 1,070.8	\$ 41.8	(\$ 417.7)	\$ 695.5

	Common Stock		Six Months Ended June 30, 2011			
	Shares	Amount	Additional Paid-In Capital	Retained	Accumulated	Total
				Earnings (Accumulated Deficit)	Other Comprehensive Income (Loss)	
Balance at beginning of year	58,070,807	\$ 0.6	\$ 1,451.2	(\$ 35.3)	(\$ 325.7)	\$ 1,090.8
Stock issuance	304,760					
Share-based employee compensation			10.5			10.5
Earnings				51.4		51.4
Other comprehensive income					19.5	19.5
Balance at June 30	58,375,567	\$ 0.6	\$ 1,461.7	\$ 16.1	(\$ 306.2)	\$ 1,172.2

See accompanying notes to Condensed Consolidated Financial Statements beginning on page 8.

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Armstrong World Industries, Inc., and Subsidiaries

Condensed Consolidated Statements of Cash Flows

(amounts in millions)

Unaudited

	Six Months Ended June 30,	
	2012	2011
Cash flows from operating activities:		
Earnings	\$ 60.0	\$ 51.4
Adjustments to reconcile earnings to net cash provided by operating activities:		
Depreciation and amortization	60.3	61.8
Fixed asset impairment	4.6	
Deferred income taxes	23.8	39.0
Share-based compensation	8.0	6.0
Equity earnings from joint venture	(28.5)	(29.0)
U.S. pension credit	(6.1)	(13.0)
Restructuring charges, net	0.2	7.3
Restructuring payments	(2.6)	(14.0)
Changes in operating assets and liabilities:		
Receivables	(52.3)	(71.8)
Inventories	(19.4)	(29.5)
Other current assets	(8.6)	(8.3)
Other noncurrent assets	(0.1)	4.8
Accounts payable and accrued expenses	(8.5)	43.9
Income taxes payable	9.1	(8.4)
Other long-term liabilities	(14.8)	(2.9)
Other, net	4.5	(5.2)
Net cash provided by operating activities	29.6	32.1
Cash flows from investing activities:		
Purchases of property, plant and equipment	(77.4)	(49.7)
Restricted cash	1.5	3.6
Return of investment from joint venture	33.7	23.0
Proceeds from the sale of assets		0.4
Net cash (used for) investing activities	(42.2)	(22.7)
Cash flows from financing activities:		
Proceeds from revolving credit facility and other debt	4.5	0.1
Payments on revolving credit facility and other debt		(25.0)
Proceeds from long-term debt	251.9	
Payments of long-term debt	(3.5)	(3.8)
Financing costs	(8.1)	(7.8)
Special dividends paid	(503.2)	
Proceeds from exercised stock options	9.3	6.8
Net cash (used for) financing activities	(249.1)	(29.7)
Effect of exchange rate changes on cash and cash equivalents	(1.6)	9.1

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Net (decrease) in cash and cash equivalents	(263.3)	(11.2)
Cash and cash equivalents at beginning of year	480.6	315.8
Cash and cash equivalents at end of period	\$ 217.3	\$ 304.6
Supplemental Cash Flow Disclosures:		
Interest paid	\$ 22.0	\$ 21.7
Income taxes paid, net	1.2	16.7
Amounts in accounts payable for capital expenditures	14.5	
See accompanying notes to Condensed Consolidated Financial Statements beginning on page 8.		

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Armstrong World Industries, Inc., and Subsidiaries

Notes to Condensed Consolidated Financial Statements (Unaudited)

(dollar amounts in millions)

NOTE 1. BUSINESS AND BASIS OF PRESENTATION

Armstrong World Industries, Inc. (AWI) is a Pennsylvania corporation incorporated in 1891. When we refer to we, our and us in these notes, we are referring to AWI and its subsidiaries. We use the term AWI when we are referring solely to Armstrong World Industries, Inc.

In December 2000, AWI filed a voluntary petition for relief (the Filing) under Chapter 11 of the U.S. Bankruptcy Code (the Bankruptcy Code) in the United States Bankruptcy Court for the District of Delaware (the Bankruptcy Court) in order to use the court-supervised reorganization process to achieve a resolution of AWI's asbestos-related liability. On October 2, 2006, AWI's court-approved plan of reorganization (POR) became effective and AWI emerged from Chapter 11. All claims in AWI's Chapter 11 case have been resolved and closed.

On October 2, 2006, the Armstrong World Industries, Inc. Asbestos Personal Injury Settlement Trust (Asbestos PI Trust) was created to address AWI's personal injury (including wrongful death) asbestos-related liability. All present and future asbestos-related personal injury claims against AWI, including contribution claims of co-defendants but excluding certain foreign claims against subsidiaries, arising directly or indirectly out of AWI's pre-filing use of, or other activities involving, asbestos are channeled to the Asbestos PI Trust.

In August 2009, Armor TPG Holdings LLC (TPG) and the Asbestos PI Trust entered into agreements whereby TPG purchased 7,000,000 shares of AWI common stock from the Asbestos PI Trust and acquired an economic interest in an additional 1,039,777 shares from the Asbestos PI Trust. The Asbestos PI Trust and TPG together hold more than 60% of AWI's outstanding shares and have entered into a shareholders agreement, pursuant to which the Asbestos PI Trust and TPG have agreed to vote their shares together on certain matters.

The accounting policies used in preparing the Condensed Consolidated Financial Statements in this Form 10-Q are the same as those used in preparing the Consolidated Financial Statements for the year ended December 31, 2011. These statements should therefore be read in conjunction with the Consolidated Financial Statements and notes that are included in the Form 10-K for the fiscal year ended December 31, 2011. In the opinion of management, all adjustments of a normal recurring nature have been included to provide a fair statement of the results for the reporting periods presented. Quarterly results are not necessarily indicative of annual earnings, primarily due to the different level of sales in each quarter of the year and the possibility of changes in general economic conditions.

Certain amounts in the prior year's Condensed Consolidated Financial Statements have been recast to conform to the 2012 presentation.

These Condensed Consolidated Financial Statements are prepared in accordance with U.S. generally accepted accounting principles (U.S. GAAP). The statements include management estimates and judgments, where appropriate. Management utilizes estimates to record many items including certain asset values, allowances for bad debts, inventory obsolescence and lower of cost or market charges, warranty, workers compensation, general liability and environmental claims and income taxes. When preparing an estimate, management determines the amount based upon the consideration of relevant information. Management may confer with outside parties, including outside counsel. Actual results may differ from these estimates.

In June 2011, the Financial Accounting Standards Board (FASB) issued new guidance that is now part of ASC 220: *Presentation of Comprehensive Income*. The guidance requires companies to present the components of net income and other comprehensive income either as one continuous statement or as two consecutive statements. It eliminates the option to present components of other comprehensive income as part of the statement of changes in stockholder's equity. The standard does not change the items which must be reported in other comprehensive income. These provisions are to be applied retrospectively and were effective for us as of January 1, 2012. There was no impact on our financial condition, results of operations or cash flows as a result of this presentation.

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Armstrong World Industries, Inc., and Subsidiaries

Notes to Condensed Consolidated Financial Statements (Unaudited)

(dollar amounts in millions)

Operating results for the second quarter and first six months of 2012 and the corresponding periods of 2011 included in this report are unaudited. However, these Condensed Consolidated Financial Statements have been reviewed by an independent registered public accounting firm in accordance with standards of the Public Company Accounting Oversight Board (United States) for a limited review of interim financial information.

NOTE 2. SEGMENT RESULTS

	Three Months Ended June 30,		Six Months Ended June 30,	
	2012	2011	2012	2011
<u>Net sales to external customers</u>				
Building Products	\$ 297.0	\$ 305.0	\$ 600.1	\$ 611.9
Resilient Flooring	253.5	274.7	480.8	509.4
Wood Flooring	124.8	133.6	230.4	244.6
Cabinets	34.6	35.3	66.6	67.9
Total net sales to external customers	\$ 709.9	\$ 748.6	\$ 1,377.9	\$ 1,433.8

	Three Months Ended June 30,		Six Months Ended June 30,	
	2012	2011	2012	2011
<u>Segment operating income (loss)</u>				
Building Products	\$ 53.5	\$ 57.1	\$ 96.8	\$ 118.6
Resilient Flooring	21.9	11.3	32.6	10.0
Wood Flooring	13.8	13.4	16.3	16.9
Cabinets	(0.7)	0.8	(1.8)	
Unallocated Corporate (expense)	(11.6)	(9.9)	(25.4)	(20.7)
Total consolidated operating income	\$ 76.9	\$ 72.7	\$ 118.5	\$ 124.8

	Three Months Ended June 30,		Six Months Ended June 30,	
	2012	2011	2012	2011
Total consolidated operating income	\$ 76.9	\$ 72.7	\$ 118.5	\$ 124.8
Interest expense	14.4	11.5	25.6	26.3
Other non-operating expense	0.3	0.8	0.3	1.1
Other non-operating income	(0.7)	(0.8)	(1.5)	(1.4)
Earnings before income taxes	\$ 62.9	\$ 61.2	\$ 94.1	\$ 98.8

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	June 30, 2012	December 31, 2011
<u>Segment assets</u>		
Building Products	\$ 946.0	\$ 935.6
Resilient Flooring	623.1	575.9
Wood Flooring	335.3	329.5
Cabinets	51.5	46.3
Total segment assets	1,955.9	1,887.3
Assets not assigned to segments	847.5	1,107.4
Total consolidated assets	\$ 2,803.4	\$ 2,994.7

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Armstrong World Industries, Inc., and Subsidiaries

Notes to Condensed Consolidated Financial Statements (Unaudited)

(dollar amounts in millions)

Impairment testing of our tangible assets occurs whenever events or changes in circumstances indicate that the carrying amount of the assets may not be recoverable. During the second quarter of 2012 we performed an impairment test of our Cabinets business due to losses incurred during the first six months of 2012. The carrying amount of the tangible assets was determined to be recoverable as the projected undiscounted cash flows exceeded the carrying value.

In March 2012, we made the decision to permanently close a previously idled ceiling tile plant in Mobile, AL. As a result, during the first quarter we recorded accelerated depreciation of \$9.3 million for machinery and equipment and a \$4.6 million impairment charge for buildings in cost of goods sold. The preliminary fair values were determined by management estimates and an independent valuation based on information available at that time (considered Level 2 inputs in the fair value hierarchy).

During the first quarter of 2011, we announced the idling of our Statesville, NC engineered wood production facility. As a result, we evaluated the impairment implications of this decision and determined no impairment charge was necessary.

NOTE 3. ACCOUNTS AND NOTES RECEIVABLE

	June 30, 2012	December 31, 2011
Customer receivables	\$ 311.8	\$ 263.3
Customer notes	2.2	1.7
Miscellaneous receivables	7.0	7.9
Less allowance for warranties, discounts and losses	(39.7)	(40.4)
Accounts and notes receivable, net	\$ 281.3	\$ 232.5

Generally, we sell our products to select, pre-approved customers whose businesses are affected by changes in economic and market conditions. We consider these factors and the financial condition of each customer when establishing our allowance for losses from doubtful accounts.

NOTE 4. INVENTORIES

	June 30, 2012	December 31, 2011
Finished goods	\$ 292.6	\$ 271.5
Goods in process	28.3	25.7
Raw materials and supplies	118.1	118.1
Less LIFO and other reserves	(35.6)	(26.4)
Total inventories, net	\$ 403.4	\$ 388.9

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Armstrong World Industries, Inc., and Subsidiaries

Notes to Condensed Consolidated Financial Statements (Unaudited)

(dollar amounts in millions)

NOTE 5. OTHER CURRENT ASSETS

	June 30, 2012	December 31, 2011
Prepaid expenses	\$ 30.2	\$ 27.7
Assets held for sale	6.1	6.2
Fair value of derivative assets	3.2	2.4
Other	7.3	2.3
Total other current assets	\$ 46.8	\$ 38.6

NOTE 6. EQUITY INVESTMENT

Investment in joint venture at June 30, 2012 reflected our 50% equity interest in our Worthington Armstrong Venture (WAVE) joint venture with Worthington Industries, Inc. Condensed income statement data for WAVE is summarized below:

	Three Months Ended June 30,		Six Months Ended June 30,	
	2012	2011	2012	2011
Net sales	\$ 95.2	\$ 86.6	\$ 186.0	\$ 185.1
Gross profit	42.4	36.8	82.6	80.1
Net earnings	32.5	28.5	63.1	63.9

NOTE 7. INTANGIBLE ASSETS

The following table details amounts related to our intangible assets as of June 30, 2012 and December 31, 2011.

		June 30, 2012		December 31, 2011	
	Estimated Useful Life	Gross Carrying Amount	Accumulated Amortization	Gross Carrying Amount	Accumulated Amortization
<u>Amortizing intangible assets</u>					
Customer relationships	20 years	\$ 170.7	\$ 49.1	\$ 170.7	\$ 44.8
Developed technology	15 years	81.1	31.0	81.1	28.3
Other	Various	14.6	1.2	14.6	1.0
Total		\$ 266.4	\$ 81.3	\$ 266.4	\$ 74.1
<u>Non-amortizing intangible assets</u>					
Trademarks and brand names	Indefinite	352.9		352.8	

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Total other intangible assets	\$ 619.3	\$ 619.2
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	Six Months Ended June 30,	
	2012	2011
Amortization expense	\$ 7.2	\$ 7.1

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Armstrong World Industries, Inc., and Subsidiaries

Notes to Condensed Consolidated Financial Statements (Unaudited)

(dollar amounts in millions)

NOTE 8. SEVERANCES AND RELATED COSTS

See Note 9 to the Condensed Consolidated Financial Statements for a discussion of severance charges associated with restructuring actions.

In the second quarter of 2012, we recorded \$3.4 million for severance and related costs in selling, general, and administrative (SG&A) expense (\$3.2M) and cost of goods sold (\$0.2M) to reflect approximately 35 position eliminations in our European Building Products business, primarily as a result of streamlining SG&A functions.

In the first quarter of 2011, we recorded \$3.0 million in cost of goods sold for severance and related costs to reflect position eliminations in our European Resilient Flooring business as a result of improved manufacturing productivity. In addition, we recorded \$0.5 million in SG&A expense for severance and related costs to reflect the separation costs for our former Senior Vice President, General Counsel and Secretary.

NOTE 9. RESTRUCTURING ACTIONS

During the third quarter of 2010, management made several significant decisions to address our cost structure. Given the materiality to our financial statements and impact to our operations, we decided to classify charges related to these actions as restructuring charges. The following table summarizes the restructuring charges recorded in the second quarters and first six months of 2012 and 2011:

<u>Action Title</u>	<u>Three Months Ended</u>		<u>Six Months Ended</u>		<u>Segment</u>
	<u>June 30,</u>	<u>June 30,</u>	<u>June 30,</u>	<u>June 30,</u>	
	<u>2012</u>	<u>2011</u>	<u>2012</u>	<u>2011</u>	
Floor Products Europe	\$ 2.2	\$ 0.2	\$ 5.3		Resilient Flooring
Beaver Falls plant		(0.3)	1.3		Building Products
North America SG&A		0.5	0.9		Unallocated Corporate, Resilient
Other initiatives			(0.2)		Flooring, Building Products Wood Flooring
Total	\$ 2.4	\$ 0.2	\$ 7.3		

Floor Products Europe: In the third quarter of 2010, we announced our intent to focus our European flooring strategy on products and regions in which we believe we can be a market leader, and to streamline our product range and sales organization accordingly. During the fourth quarter of 2010, we withdrew from the residential market and, as a result, we sold our Teesside, UK manufacturing facility. In addition, during the second quarter of 2011, we ceased production at our heterogeneous vinyl flooring plant in Holmsund, Sweden.

In addition to the restructuring costs reflected in the above table, we also recorded \$2.7 million in the second quarter and \$4.8 million in the first six months of 2011 of other related costs in cost of goods sold (\$2.4 million in the second quarter and \$4.1 million in the first six months) and SG&A expense (\$0.3 million in the second quarter and \$0.7 million in the first six months). These costs are primarily related to inventory obsolescence, accelerated depreciation and plant closure costs.

Through June 30, 2012, we have incurred expenses of \$30.1 million related to this initiative. We do not expect to incur further material restructuring costs related to this initiative.

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Beaver Falls Plant: Production at the Beaver Falls, PA facility ended March 31, 2011, and production requirements have been transitioned to other facilities. The decision to close the plant was driven by the location and layout of the plant, technology limitations and the continued limited demand for the products we made at the plant.

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Armstrong World Industries, Inc., and Subsidiaries

Notes to Condensed Consolidated Financial Statements (Unaudited)

(dollar amounts in millions)

In addition to the restructuring costs reflected in the table above, we also recorded \$1.8 million in the second quarter and \$6.5 million in the first six months of 2011 of accelerated depreciation and \$2.8 million of closure-related costs in cost of goods sold in the second quarter and first six months of 2011.

Through June 30, 2012, we have incurred expense of \$25.1 million related to this initiative. We do not expect to incur additional costs in the future as the plant was sold in 2011. The sale resulted in a net gain of \$0.7 million which was recorded in SG&A in the third quarter of 2011.

North America SG&A: We are committed to augmenting margin expansion through the aggressive adoption of projects to standardize, simplify or eliminate SG&A activities. As a result, in the third quarter of 2010, we began to restructure our North American SG&A operations. The first six months of 2011 restructuring expense related to this initiative was recorded in the Unallocated Corporate (\$0.6 million) and Resilient Flooring (\$0.2 million) and Building Products (\$0.1 million) segments.

Through June 30, 2012, we have incurred restructuring expense of \$7.2 million related to this initiative. In total, we expect to incur restructuring expenses of up to \$8 million related to this initiative through 2012 as we further streamline North American SG&A functions.

The following table summarizes activity in the restructuring accruals.

	Floor Products Europe	Severance and Related Costs		Total
		North America SG&A	Beaver Falls Plant	
December 31, 2011	\$ 3.2	\$ 0.5	\$ 0.1	\$ 3.8
Net charges	0.2			0.2
Cash payments	(2.2)	(0.4)		(2.6)
June 30, 2012	\$ 1.2	\$ 0.1	\$ 0.1	\$ 1.4

Most of the accrual balance as of June 30, 2012 is expected to be paid by March 31, 2013.

NOTE 10. INCOME TAX EXPENSE

	Three Months Ended June 30,		Six Months Ended June 30,	
	2012	2011	2012	2011
Earnings before income taxes	\$ 62.9	\$ 61.2	\$ 94.1	\$ 98.8
Income tax expense	21.1	23.3	34.1	47.4
Effective tax rate	33.5%	38.1%	36.2%	48.0%

The effective tax rate for the second quarter of 2012 was lower than the comparable period in 2011, primarily due to the favorable tax impact from our mix of income from international operations.

The effective tax rate for the first six months of 2012 was lower than the first six months of 2011 primarily due to the favorable tax impact from our mix of income from international operations. Additionally, the effective tax rate was lower in the first six months of 2012 due to a decrease in the valuation allowance for foreign tax credits based on our projected ability to utilize these credits to offset future taxable income.

We do not expect to record any material changes during 2012 to unrecognized tax benefits that were claimed on tax returns covering tax years ending on or before December 31, 2011.

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As of June 30, 2012 we consider foreign unremitted earnings to be permanently reinvested.

NOTE 11. DEBT

On March 22, 2012, we amended our \$1.05 billion senior credit facility arranged by Merrill Lynch, Pierce, Fenner & Smith, Inc., J.P. Morgan Securities, Inc. and Barclays Capital. We added \$250 million to our existing Term Loan B facility. The amended \$1.3 billion facility is made up of a \$250 million revolving credit facility (with a \$150 million sublimit for letters of credit), a \$250 million Term Loan A and an \$800 million Term Loan B. The facility is secured by U.S. personal property, the capital stock of material U.S. subsidiaries, and a pledge of 65% of the stock of our material first tier foreign subsidiaries. The only significant change to existing terms, conditions and covenants related to the consolidated leverage ratio covenant. Under the revised covenant, threshold ratios are as follow: 4.5 to 1.0 through December 31, 2013, 4.0 to 1.0 through March 31, 2015, and 3.75 to 1.0 thereafter. During the first six months of 2012, we were in compliance with all covenants of the previous and amended credit agreements.

In connection with the additional \$250 million Term Loan B borrowings, we paid \$8.1 million for bank, legal and other fees. This amount was capitalized and is being amortized into interest expense over the life of the loan.

NOTE 12. PENSIONS AND OTHER BENEFIT PROGRAMS

Following are the components of net periodic benefit costs (credits):

	Three Months Ended June 30,		Six Months Ended June 30,	
	2012	2011	2012	2011
<u>U.S. defined-benefit plans:</u>				
<u>Pension benefits</u>				
Service cost of benefits earned during the period	\$ 4.0	\$ 3.9	\$ 7.9	\$ 7.8
Interest cost on projected benefit obligation	22.6	23.1	45.3	46.1
Expected return on plan assets	(35.0)	(38.1)	(70.0)	(76.2)
Amortization of prior service cost	0.4	0.4	0.9	0.9
Amortization of net actuarial loss	5.9	4.8	11.7	9.6
Net periodic pension (credit)	(\$ 2.1)	(\$ 5.9)	(\$ 4.2)	(\$ 11.8)
<u>Retiree health and life insurance benefits</u>				
Service cost of benefits earned during the period	\$ 0.3	\$ 0.6	\$ 0.6	\$ 1.2
Interest cost on projected benefit obligation	3.1	3.6	5.5	7.2
Amortization of prior service cost	(0.2)		(0.3)	
Amortization of net actuarial gain	(1.3)	(0.7)	(4.3)	(1.4)
Net periodic postretirement benefit cost	\$ 1.9	\$ 3.5	\$ 1.5	\$ 7.0
<u>Non-U.S. defined-benefit pension plans</u>				
Service cost of benefits earned during the period	\$ 0.5	\$ 1.0	\$ 1.0	\$ 1.8
Interest cost on projected benefit obligation	3.9	4.5	7.8	8.9
Expected return on plan assets	(2.6)	(3.3)	(5.1)	(6.6)

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Amortization of net actuarial loss	0.4		0.7	0.1
Net periodic pension cost	\$ 2.2	\$ 2.2	\$ 4.4	\$ 4.2

We currently estimate that the 2012 net periodic postretirement benefit cost for our U.S. retiree health and life insurance plans will total approximately \$5 million.

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NOTE 13. FINANCIAL INSTRUMENTS

We do not hold or issue financial instruments for trading purposes. The estimated fair values of our financial instruments are as follows:

	June 30, 2012		December 31, 2011	
	Carrying amount	Estimated fair value	Carrying amount	Estimated fair value
Assets/(Liabilities), net:				
Total debt, including current portion	(\$ 1,095.6)	(\$ 1,089.3)	(\$ 843.0)	(\$ 835.2)
Foreign currency contract obligations	1.8	1.8	1.1	1.1
Natural gas contracts	(7.1)	(7.1)	(9.3)	(9.3)
Interest rate swap contracts	(24.2)	(24.2)	(14.0)	(14.0)

The carrying amounts of cash and cash equivalents of \$217.3 million at June 30, 2012 (made up of bank deposits), receivables, accounts payable and accrued expenses, short-term debt and current installments of long-term debt approximate fair value because of the short-term maturity of these instruments. The fair value estimates of long-term debt were based upon quotes from a major financial institution of recently observed trading levels of our Term Loan B debt. The fair value estimates of foreign currency contract obligations are estimated from market quotes provided by a well recognized national market data provider. The fair value estimates of natural gas contracts are estimated using internal valuation models with verification by obtaining quotes from major financial institutions. For natural gas swap transactions, fair value is calculated using NYMEX market quotes provided by a well recognized national market data provider. For natural gas option based strategies, fair value is calculated using an industry standard Black-Scholes model with market based inputs, including but not limited to, underlying asset price, strike price, implied volatility, discounted risk free rate and time to expiration, provided by a well recognized national market data provider. The fair value estimates for interest rate swap contracts are estimated by obtaining quotes from major financial institutions with verification by internal valuation models.

As of June 30, 2012 we had no restricted cash on our balance sheet. As of December 31, 2011, we had \$1.5 million of restricted cash held by a trustee related to the construction of our Millwood, WV mineral wool plant. These funds were released during the first six months of 2012.

Fair value is defined as the exchange price that would be received for an asset or paid to transfer a liability (an exit price) in the principal or most advantageous market for the asset or liability in an orderly transaction between market participants at the measurement date. U.S. GAAP establishes a three-level fair value hierarchy that prioritizes the inputs used to measure fair value. The three levels of inputs used to measure fair value are as follows:

Level 1 Quoted prices in active markets for identical assets or liabilities.

Level 2 Observable inputs other than quoted prices 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 markets that are not active; or other inputs that are observable or can be corroborated by observable market data.

Level 3 Unobservable inputs that are supported by little or no market activity and that are significant to the fair value of the assets or liabilities. This includes certain pricing models, discounted cash flow methodologies and similar techniques that use significant unobservable inputs.

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Assets and liabilities are summarized below:

	June 30, 2012		December 31, 2011	
	Fair value based on		Fair value based on	
	Quoted, active markets Level 1	Other observable inputs Level 2	Quoted, active markets Level 1	Other observable inputs Level 2
Assets/(Liabilities), net:				
Total debt, including current portion	(\$ 787.5)	(\$ 301.8)	(\$ 545.9)	(\$ 289.3)
Foreign currency contract obligations	1.8		1.1	
Natural gas contracts		(7.1)		(9.3)
Interest rate swap contracts		(24.2)		(14.0)

We do not have any financial assets or liabilities that are valued using Level 3 (unobservable) inputs.

NOTE 14. DERIVATIVE FINANCIAL INSTRUMENTS

We are exposed to market risk from changes in foreign exchange rates, interest rates and commodity prices that could impact our results of operations and financial condition. We use forward swaps and option contracts to hedge certain of these exposures. Exposure to individual counterparties is controlled and derivative financial instruments are entered into with a diversified group of major financial institutions. Forward swaps and option contracts are entered into for periods consistent with underlying exposure and do not constitute positions independent of those exposures. At inception, hedges that we designate as hedging instruments are formally documented as either (1) a hedge of a forecasted transaction or cash flow hedge, or (2) a hedge of the fair value of a recognized liability or asset or fair value hedge. We also formally assess both at inception and at least quarterly thereafter, whether the derivatives that are used in hedging transactions are highly effective in offsetting changes in either the fair value or cash flows of the hedged item. If it is determined that a derivative ceases to be a highly effective hedge, or if the anticipated transaction is no longer probable of occurring, we discontinue hedge accounting, and any future mark to market adjustments are recognized in earnings. We use derivative financial instruments as risk management tools and not for speculative trading purposes.

Counterparty Risk

We only enter into derivative transactions with established counterparties having a credit rating of BBB or better. We monitor counterparty credit default swap levels and credit ratings on a regular basis. All of our derivative transactions with counterparties are governed by master International Swap and Derivatives Association agreements (ISDAs) with netting arrangements. These agreements can limit our exposure in situations where we have gain and loss positions outstanding with a single counterparty. We generally do not post nor do we receive cash collateral with any counterparty for our derivative transactions. As of June 30, 2012, we had no cash collateral posted or received for any of our derivative transactions. These ISDAs do not have any credit contingent features; however, a default under our bank credit facility would trigger a default under these agreements. Exposure to individual counterparties is controlled, and thus we consider the risk of counterparty default to be negligible.

Commodity Price Risk

We purchase natural gas for use in the manufacture of ceiling tiles and other products, and to heat many of our facilities. As a result, we are exposed to fluctuations in the price of natural gas. We have a policy to reduce cost volatility for North American natural gas purchases by purchasing natural gas forward contracts and swaps, purchased call options, and zero-cost collars up to 24 months forward to reduce our overall exposure to natural gas price movements. There is a high correlation between the hedged item and the hedged instrument. The gains and losses on these transactions offset gains and losses on the transactions being hedged. These instruments are designated as cash flow hedges. At June 30,

2012 and December 31, 2011, the notional

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amount of these hedges was \$36.6 million and \$47.2 million, respectively. The mark-to-market gain or loss on qualifying hedges is included in other comprehensive income to the extent effective, and reclassified into cost of goods sold in the period during which the underlying gas is consumed. The mark-to-market gains or losses on ineffective portions of hedges are recognized in cost of goods sold immediately. The earnings impact of the ineffective portion of these hedges was not material for the second quarter or first six months of 2012 or 2011. The contracts are based on forecasted usage of natural gas measured in mmBtu s.

Currency Rate Risk – Sales and Purchases

We manufacture and sell our products in a number of countries throughout the world and, as a result, we are exposed to movements in foreign currency exchange rates. To a large extent, our global manufacturing and sales provide a natural hedge of foreign currency exchange rate movement, as foreign currency expenses generally offset foreign currency revenues. We manage our cash flow exposures on a net basis and use derivatives to hedge the majority of our unmatched foreign currency cash inflows and outflows. As of June 30, 2012, our major foreign currency exposures are to the Canadian dollar, the Australian dollar, and the Euro.

We use foreign currency forward exchange contracts to reduce our exposure to the risk that the eventual net cash inflows and outflows resulting from the sale of products to foreign customers and purchases from foreign suppliers will be adversely affected by changes in exchange rates. These derivative instruments are used for forecasted transactions and are classified as cash flow hedges. Cash flow hedges are executed quarterly, generally up to 15 months forward, and allow us to further reduce our overall exposure to exchange rate movements, since gains and losses on these contracts offset gains and losses on the transactions being hedged. The notional amount of these hedges was \$137.0 million and \$128.3 million at June 30, 2012 and December 31, 2011, respectively. Gains and losses on these instruments are recorded in other comprehensive income, to the extent effective, until the underlying transaction is recognized in earnings. The earnings impact of the ineffective portion of these hedges was not material for the second quarter or first six months of 2012 or 2011.

Currency Rate Risk – Intercompany Loans and Dividends

We also use foreign currency forward exchange contracts to hedge exposures created by cross-currency intercompany loans and dividends. The translation adjustments related to these loans are recorded in other non-operating income or expense. The offsetting gains or losses on the related derivative contracts are also recorded in other non-operating income or expense. These contracts are decreased or increased as repayments are made or additional intercompany loans are extended or adjusted for intercompany dividend activity as necessary. The notional amount of these hedges was \$21.8 million at December 31, 2011. We did not have any open hedges related to intercompany loans and dividends as of June 30, 2012.

Interest Rate Risk

We utilize interest rate swaps to minimize the fluctuations in earnings caused by interest rate volatility. Interest expense on variable-rate liabilities increases or decreases as a result of interest rate fluctuations. On March 31, 2011 we entered into two interest rate swaps, on our Term Loan A and Term Loan B, with notional amounts of \$100 million and \$200 million, respectively, which mature in November 2015. Under the terms of the Term Loan A swap, we receive 3-month LIBOR and pay a fixed rate over the hedged period. Under the terms of the Term Loan B swap, we receive the greater of 3-month LIBOR or the 1% LIBOR Floor and pay a fixed rate over the hedged period. On March 27, 2012 we entered into an additional interest rate swap agreement with a notional amount of \$250 million, maturing in March 2018, under the terms of which we pay a fixed rate of 1.9275% over the hedged period. We also entered into a forward starting interest rate swap of \$200 million from November 2015 to March 2018, under the terms of which we pay a fixed rate of 2.810% over the hedged period. These swaps are designated as cash flow hedges against changes in LIBOR for a portion of our variable rate debt.

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Financial Statement Impacts

The following tables detail amounts related to our derivatives as of June 30, 2012 and December 31, 2011. Our derivative assets and liabilities not designated as hedging instruments were not material as of June 30, 2012 and December 31, 2011.

	Asset Derivatives			Derivative Liabilities		
	Balance Sheet Location	Fair Value		Balance Sheet Location	Fair Value	
		June 30, 2012	December 31, 2011		June 30, 2012	December 31, 2011
Derivatives designated as hedging instruments						
Natural gas commodity contracts	Other current assets			Accounts payable and accrued expenses	\$ 7.1	\$ 7.2
Natural gas commodity contracts	Other non-current assets			Other long-term liabilities		2.1
Foreign exchange contracts	Other current assets	\$ 3.2	\$ 2.4	Accounts payable and accrued expenses	1.4	1.3
Interest rate swap contracts	Other current assets			Other long-term liabilities	24.2	14.0
Total derivatives designated as hedging instruments		\$ 3.2	\$ 2.4		\$ 32.7	\$ 24.6

	Amount of Gain (Loss) Recognized in Accumulated Other Comprehensive Income (AOCI) (Effective Portion)(a)		Location of (Loss) Reclassified from AOCI into Income (Effective Portion)	(Loss) Reclassified from AOCI into Income (Effective Portion)			
	Six Months Ended June 30,			Three Months Ended		Six Months Ended	
	2012	2011		Ended June 30, 2012	2011	2012	2011
Derivatives in Cash Flow Hedging Relationships							
Natural gas commodity contracts	(\$ 7.0)	(\$ 2.9)	Cost of goods sold	(\$ 2.4)	(\$ 1.3)	(\$ 5.1)	(\$ 3.8)
Foreign exchange contracts purchases and sales	1.8	(1.9)	Cost of goods sold	(0.3)	(1.3)	(0.8)	(2.1)
Interest rate swap contracts	(24.2)	(6.7)	Interest Expense				
Total	(\$ 29.4)	(\$ 11.5)		(\$ 2.7)	(\$ 2.6)	(\$ 5.9)	(\$ 5.9)

(a) As of June 30, 2012 the amount of existing (loss) in Accumulated OCI expected to be recognized in earnings over the next twelve months is \$(5.3) million.

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	Location of Gain (Loss) Recognized in Income on Derivative (Ineffective Portion) (a)
<u>Derivatives in Cash Flow Hedging Relationships</u>	
Natural gas commodity contracts	Cost of goods sold
Foreign exchange contracts purchases and sales	SG&A expense
Interest rate swap contracts	Interest expense

(a) The amount of gain (loss) recognized in income related to the ineffective portion of the hedging relationships was immaterial for the three months and six months ended June 30, 2012 and June 30, 2011. No gains or losses are excluded from the assessment of the hedge effectiveness.

The gain (loss) recognized in income for derivative instruments not designated as hedging instruments was \$0.6 million for the second quarter and zero for the first six months of 2012 and \$(0.2) million and \$4.3 million for the second quarter and first six months of 2011, respectively.

NOTE 15. PRODUCT WARRANTIES

We provide direct customer and end-user warranties for our products. These warranties cover manufacturing defects that would prevent the product from performing in line with its intended and marketed use. The terms of these warranties vary by product and generally provide for the repair or replacement of the defective product. We collect and analyze warranty claims data with a focus on the historic amount of claims, the products involved, the amount of time between the warranty claims and their respective sales and the amount of current sales. The following table summarizes the activity for the accrual of product warranties for the first six months of 2012 and 2011:

	2012	2011
Balance at January 1,	\$ 12.1	\$ 11.9
Reductions for payments	(9.4)	(7.4)
Current year warranty accruals	10.1	8.1
Preexisting warranty accrual changes	(0.3)	(0.1)
Effects of foreign exchange translation	(0.2)	0.3
Balance at June 30,	\$ 12.3	\$ 12.8

The warranty provision and related reserve are recorded as a reduction of sales and accounts receivable.

NOTE 16. LITIGATION AND RELATED MATTERS

ENVIRONMENTAL MATTERS

Environmental Expenditures

Our manufacturing and research facilities are affected by various federal, state and local requirements relating to the discharge of materials and the protection of the environment. We make expenditures necessary for compliance with applicable environmental requirements at each of our operating facilities. These regulatory requirements continually change, therefore we cannot predict with certainty future expenditures associated

with compliance with environmental requirements.

Environmental Remediation

Summary

We are actively involved in the investigation and/or remediation of environmental contamination under the Comprehensive Environmental Response, Compensation and Liability Act (CERCLA), and state or international Superfund and similar type laws at several domestically- and internationally-owned, formerly owned and non-owned locations allegedly resulting from past industrial activity. In a few cases, we are one of

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several potentially responsible parties (PRPs) and have agreed to jointly fund the required investigation and remediation, while preserving our defenses to the liability. We may also have rights of contribution or reimbursement from other parties or coverage under applicable insurance policies.

Estimates of our future liability at the environmental sites are based on evaluations of currently available facts regarding each individual site. We consider factors such as our activities associated with the site, existing technology, presently enacted laws and regulations and prior company experience in remediating contaminated sites. Although current law imposes joint and several liability on all parties at Superfund sites, our contribution to the remediation of these sites is expected to be limited by the number of other companies potentially liable for site remediation. As a result, our estimated liability reflects only our expected share. In determining the probability of contribution, we consider the solvency of other parties, whether liability is being disputed, the terms of any existing agreements and experience with similar matters, and the effect of our Chapter 11 reorganization upon the validity of the claim.

Specific Material Events

In August 2010, we entered into a Consent Order with the Oregon Department of Environmental Quality (ODEQ), along with Kaiser Gypsum Company, Inc. (Kaiser), and Owens Corning Sales LLC (OC), with respect to our St. Helens, OR Building Products facility, which was previously owned by Kaiser and then OC. The Consent Order, which replaces a previous order of the ODEQ requiring us to investigate and remediate hazardous substances present at the facility, requires that we and Kaiser complete a remedial investigation and feasibility study (RI/FS) on the portion of the site owned by us. The Consent Order further requires us, Kaiser and OC to conduct an RI/FS in the adjacent Scappoose Bay. Our current estimate of our future liability at the site relates to the investigation work required by the Consent Order and to the currently projected cost of possible remedies for certain portions of the site. However, neither the RI/FS for the portion of the property owned by us nor the Scappoose Bay is complete. At this time, we have determined that it is probable that additional corrective action for the portion of the property owned by us will be required. Such corrective action could result in additional costs greater than currently estimated and, consequently, those costs may be material. At this time, it is not possible to reasonably estimate the total costs that we may ultimately incur with respect to the Scappoose Bay, although such amounts may be material.

Costs and responsibilities for the RI/FS for certain portions of the St. Helens property owned by us continue to be shared with Kaiser pursuant to an agreement with Kaiser. Limited contributions are also being made by ODEQ pursuant to its settlement with OC for OC s liabilities for the property, although we anticipate that the settlement funds will likely be depleted this year. Contemporaneously with the execution of the Consent Order, we, Kaiser and OC also entered into a cost allocation agreement for the investigation and possible remediation of the Scappoose Bay.

The U.S. Environmental Protection Agency (EPA) has listed two landfills located on a portion of our Building Products facility in Macon, GA, along with the former Macon Naval Ordnance Plant landfill adjacent to our property, and portions of Rocky Creek (collectively, the Macon Site) as a Superfund site on the National Priorities List due to the presence of contaminants, most notably PCBs. In September 2010, we entered into an Administrative Order on Consent for a Removal Action with the EPA to investigate PCB contamination in one of the landfills on our property that is a portion of the Superfund Site. Our current estimate of future liability includes costs for investigative work that we agreed to perform under the EPA order as well as remedial work associated with this landfill which became probable and estimable in the second quarter of 2012. Additionally, it is probable that we will incur field investigation, engineering and oversight costs associated with an RI/FS with respect to the remainder of the Superfund site, including Rocky Creek. We, along with other parties, may also ultimately incur costs in remedying contamination discovered during the RI/FS. At this time, we are able to estimate only a portion of the amounts probable to occur with respect to these activities. It is anticipated that significant investigative work may be required that is not currently possible to reasonably estimate, although such amounts may be material.

In the second quarter of 2012, we recorded a liability for probable and estimable costs associated with the clean closure of a non-hazardous containment pond located on the property of our previously idled Mobile, AL Building Products plant. We anticipate that this work could start in the fourth quarter of 2012. At that time,

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additional closure actions may become known and reasonably estimable. We are unable to anticipate all of the closure actions that will be required by the Alabama Department of Environmental Management, although amounts associated with such actions may be material.

Summary of Financial Position

Liabilities of \$11.1 million at June 30, 2012 and \$7.3 million at December 31, 2011 were recorded for potential environmental liabilities, on a global basis, that we consider probable and for which a reasonable estimate of the probable liability could be made. Where existing data is sufficient to estimate the liability, that estimate has been used; where only a range of probable liabilities is available and no amount within that range is more likely than any other, the lower end of the range has been used. As assessments and remediation activities progress at each site, these liabilities are reviewed to reflect new information as it becomes available. These liabilities are undiscounted.

The estimated liabilities above do not take into account any claims for recoveries from insurance or third parties. It is our policy to record probable recoveries that are either available through settlement or anticipated to be recovered through negotiation or litigation as assets in the Condensed Consolidated Balance Sheets. No amounts were recorded for probable recoveries at June 30, 2012 or December 31, 2011.

Actual costs to be incurred at identified sites may vary from our estimates. Based on our current knowledge of the identified sites, it is not possible to reasonably estimate future costs which may exceed amounts already recognized.

OTHER CLAIMS

We are involved in various lawsuits, claims, investigations and other legal matters from time to time that arise in the ordinary course of conducting business, including matters involving our products, intellectual property, relationships with suppliers, distributors, relationships with competitors, employees and other matters. While complete assurance cannot be given to the outcome of these proceedings, we do not currently believe that any of these matters, individually or in the aggregate, will have a material adverse effect on our financial condition, liquidity or results of operations.

NOTE 17. SPECIAL CASH DIVIDEND AND STOCK OPTION ADJUSTMENTS

On March 23, 2012, our Board of Directors declared a special cash dividend in the amount of \$8.55 per share, or \$508.2 million in the aggregate, of which \$502.9 million was paid on April 10, 2012 to the shareholders of record as of April 3, 2012. The unpaid portion of the dividend relates to unvested employee shares and is reflected in current liabilities (\$1.8 million) and other long term liabilities (\$3.5 million) and will be paid when the underlying employee shares vest. The dividend was funded in part by existing cash and in part by the proceeds of additional debt issued under our Term Loan B. The dividend was recorded as a reduction of retained earnings to the extent that retained earnings were available at the dividend declaration date. Dividends in excess of retained earnings were recorded as a reduction of capital in excess of par value.

Under the terms of the 2011 Long Term Incentive Plan (the "Plan"), the Management Development and Compensation Committee of our Board of Directors is required to make equitable adjustments to stock option grants if there is a change in our capital structure. The special cash dividend qualified as a change to our capital structure under the terms of the Plan. We used the Black-Scholes option pricing model to determine the fair value of the awards before and after the special cash dividend, using consistent assumptions for the risk free rate of return, expected term, expected volatility and expected dividend yield. The stock prices used in the before and after calculations were \$57.38 (the New York Stock Exchange Volume Weighted Average Price (NYSE VWAP)) on March 29, 2012, the day before the ex-dividend date) and \$49.21 (NYSE VWAP on March 30, 2012, the ex-dividend date), respectively. For all option grants, the fair value of the award before and after the dividend remained the same. Therefore there was no incremental cost recognized in our financial statements due to the resulting award adjustments described in the table below.

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The following adjustments were made to the options outstanding as a result of this analysis:

Year Granted	Pre-Dividend Grant Terms		Post-Dividend Grant Terms	
	Number of Shares	Exercise Price	Number of Shares	Exercise Price
2006	262,418	\$ 22.55	305,992	\$ 19.34
2007	83,452	30.62	97,306	26.26
2008	171,792	21.85	200,318	18.74
2009	100,209	10.34	116,851	8.87
2010	608,278	26.21 29.23	709,309	22.48 25.07
2011	434,674	38.65 47.47	506,873	33.15 40.71
2012	403,750	50.38	470,805	43.21

NOTE 18. EARNINGS PER SHARE

Earnings per share (EPS) components may not add due to rounding.

The following table is a reconciliation of earnings to earnings attributable to common shares used in our basic and diluted EPS calculations for the three month and six month periods ended June 30, 2012 and 2011:

	Three Months Ended June 30,		Six Months Ended June 30,	
	2012	2011	2012	2011
Earnings	\$ 41.8	\$ 37.9	\$ 60.0	\$ 51.4
Earnings allocated to participating non-vested share awards	(0.3)	(0.3)	(0.4)	(0.4)
Earnings attributable to common shares	\$ 41.5	\$ 37.6	\$ 59.6	\$ 51.0

The following table is a reconciliation of basic shares outstanding to diluted shares outstanding for the three month and six month periods ended June 30, 2012 and 2011 (shares in millions):

	Three Months Ended June 30,		Six Months Ended June 30,	
	2012	2011	2012	2011
Basic shares outstanding	58.8	58.3	58.7	58.2
Dilutive effect of stock option awards	0.6	0.6	0.6	0.6
Diluted shares outstanding	59.4	58.9	59.3	58.8