USG CORP
Form 10-Q
April 21, 2016
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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 March 31, 2016
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 1-8864
USG CORPORATION
(Exact name of registrant as specified in its charter)

Delaware	36-3329400
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)
550 West Adams Street, Chicago, Illinois	60661-3676
(Address of principal executive offices)	(Zip code)

Registrant's telephone number, including area code (312) 436-4000
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 ¨
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 ¨
Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company (as defined in Rule 12b-2 of the Exchange Act).
Large accelerated filer þ 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 o No þ
The number of shares of the registrant's common stock outstanding as of March 31, 2016 was 145,853,372.

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PART I. FINANCIAL INFORMATION
ITEM 1. FINANCIAL STATEMENTS
USG CORPORATION
CONSOLIDATED STATEMENTS OF INCOME
(Unaudited)

(millions, except per-share and share data)	Three months ended March 31,	
	2016	2015
Net sales	$970	$ 909
Cost of products sold	775	756
Gross profit	195	153
Selling and administrative expenses	71	77
Recovery of receivable	(3)	—
Operating profit	127	76
Income from equity method investments	7	8
Interest expense	(40)	(43)
Interest income	2	1
Loss on extinguishment of debt	(2)	(19)
Other income (expense), net	3	(1)
Income before income taxes	97	22
Income tax (expense) benefit	(30)	2
Net income	$67	$ 24
Basic earnings per common share	$0.46	$ 0.16
Diluted earnings per common share	$0.46	$ 0.16
Average common shares	145,819,025	145,381,269
Average diluted common shares	146,986,397	147,176,197

See accompanying Notes to Consolidated Financial Statements.

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USG CORPORATION
CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME (LOSS)
(Unaudited)

(millions)	Three months ended March 31, 2016	2015
Net income	$67	$24
Other comprehensive income (loss), net of tax:		
Derivatives qualifying as cash flow hedges:		
Loss on derivatives qualifying as cash flow hedges, net of tax (benefit) of ($3) and $1, respectively	(8)	(1)
Less: Reclassification adjustment for loss on derivatives included in net income, net of tax (benefit) of ($1) and $0, respectively	(2)	(2)
Net derivatives qualifying as cash flow hedges	(6)	1
Pension and postretirement benefits:		
Changes in pension and postretirement benefits, net of tax (benefit) of ($1) and $1, respectively	(3)	6
Less: Amortization of prior service credit (cost) included in net periodic pension cost, net of tax (benefit) of $0 and ($1), respectively	—	(1)
Net pension and postretirement benefits	(3)	7
Foreign currency translation:		
Changes in foreign currency translation, net of tax of $0 in all periods	24	(34)
Other comprehensive income (loss), net of tax	$15	$(26)
Comprehensive income (loss)	$82	$(2)

See accompanying Notes to Consolidated Financial Statements.

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USG CORPORATION
CONSOLIDATED BALANCE SHEETS

(millions, except share and per share data)	March 31, 2016 (Unaudited)	December 31, 2015
Assets		
Cash and cash equivalents	$ 347	$ 442
Short-term marketable securities	206	194
Restricted cash	—	9
Receivables (net of reserves - $11 and $14)	459	391
Inventories	318	314
Income taxes receivable	4	5
Other current assets	36	45
Total current assets	1,370	1,400
Long-term marketable securities	20	36
Property, plant and equipment (net of accumulated depreciation and depletion - $1,974 and $1,936)	1,770	1,788
Deferred income taxes	698	728
Equity method investments	706	682
Other assets	98	102
Total assets	$ 4,662	$ 4,736
Liabilities and Stockholders' Equity		
Accounts payable	$ 267	$ 259
Accrued expenses	198	214
Current portion of long-term debt	438	500
Income taxes payable	6	9
Litigation settlement accrual	—	9
Total current liabilities	909	991
Long-term debt	1,676	1,675
Deferred income taxes	3	5
Pension and other postretirement benefits	341	392
Other liabilities	215	237
Total liabilities	3,144	3,300
Preferred stock – $1 par value, authorized 36,000,000 shares; outstanding - none	—	—
Common stock – $0.10 par value; authorized 200,000,000 shares; issued: 2016 - 145,853,000 shares; 2015 - 145,667,000 shares	15	15
Additional paid-in capital	3,027	3,027
Accumulated other comprehensive loss	(299)	(314)
Retained earnings (accumulated deficit)	(1,225)	(1,292)
Total stockholders' equity	1,518	1,436
Total liabilities and stockholders' equity	$ 4,662	$ 4,736

See accompanying Notes to Consolidated Financial Statements.

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USG CORPORATION
CONSOLIDATED STATEMENTS OF CASH FLOWS
(Unaudited)

(millions)	Three months ended March 31, 2016	2015
Operating Activities		
Net income	$ 67	$ 24
Adjustments to reconcile net income to net cash:		
Depreciation, depletion and amortization	36	36
Loss on extinguishment of debt	2	19
Recovery of receivable	(3)	—
Share-based compensation expense	4	3
Deferred income taxes	29	1
Income from equity method investments	(7)	(8)
Pension settlement	2	—
(Increase) decrease in working capital:		
Receivables	(65)	(54)
Income taxes receivable	1	(1)
Inventories	(3)	(2)
Other current assets	5	1
Payables	5	(43)
Accrued expenses	(42)	(23)
Decrease in other assets	1	—
(Decrease) increase in pension and other postretirement benefits	(56)	6
Decrease in other liabilities	(1)	(4)
Other, net	(5)	3
Net cash used for operating activities	$ (30)	$ (42)
Investing Activities		
Purchases of marketable securities	(79)	(21)
Sales or maturities of marketable securities	84	87
Capital expenditures	(15)	(29)
Net proceeds from asset dispositions	—	1

Return (deposit) of restricted cash	9			(39		)
Net cash used for investing activities	$	(1	)	$	(1	)
Financing Activities						
Issuance of debt	—			350		
Repayment of debt	(64		)	(368		)
Payment of debt issuance fees	—			(6		)
Issuance of common stock	—			3		
Repurchases of common stock to satisfy employee tax withholding obligations	(1		)	(8		)
Net cash used for financing activities	$	(65	)	$	(29	)
Effect of exchange rate changes on cash	1			(3		)
Net decrease in cash and cash equivalents	$	(95	)	$	(75	)
Cash and cash equivalents at beginning of period	442			228		
Cash and cash equivalents at end of period	$	347		$	153	
Supplemental Cash Flow Disclosures:						
Interest paid, net of capitalized interest	$	47		$	50	
Income taxes paid, net of refunds received	3			1		
Noncash Investing and Financing Activities:						
Amount in accounts payable for capital expenditures	3			8		

See accompanying Notes to Consolidated Financial Statements.

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USG CORPORATION
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited)

In the following Notes to Consolidated Financial Statements, “USG,” “we,” “our” and “us” refer to USG Corporation, a Delaware corporation, and its subsidiaries included in the consolidated financial statements, except as otherwise indicated or as the context otherwise requires.

1. Organization, Consolidation and Presentation of Financial Statements

PREPARATION OF FINANCIAL STATEMENTS

We prepared the accompanying unaudited consolidated financial statements of USG Corporation in accordance with applicable United States Securities and Exchange Commission, or SEC, guidelines pertaining to interim financial information. The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets, liabilities, revenues and expenses. Actual results could differ materially from those estimates. In the opinion of our management, the financial statements reflect all adjustments, which are of a normal recurring nature, necessary for a fair presentation of our financial results for the interim periods. The results of operations for the three months ended March 31, 2016 are not necessarily indicative of the results of operations to be expected for the entire year.

Our segments are structured around our key products and business units: Gypsum, Ceilings, Distribution and USG Boral Building Products, or UBBP.

Our Gypsum reportable segment is an aggregation of the operating segments of the gypsum businesses in the United States, Canada, Mexico, and Latin America, our mining operation in Canada, and our shipping operations, which we exited in the second quarter of 2015. Gypsum manufactures products throughout the United States, Canada, Mexico and Latin America. These products include USG Sheetrock® brand gypsum wallboard, Sheetrock® brand joint compound, Durock® brand cement board, Levelrock® brand gypsum underlayment, Fiberock® brand backerboard, Securock® brand glass mat sheathing used for building exteriors, Securock® brand gypsum fiber and glass mat panels used as roof cover board and structural panel concrete roofing.

Our Ceilings reportable segment is an aggregation of the operating segments of the ceilings businesses in the United States, Canada, Mexico, and Latin America. Ceilings manufactures ceiling tile in the United States and ceiling grid in the United States and Canada.

Our Distribution reportable segment delivers gypsum wallboard, drywall metal, ceilings products, joint compound and other building products throughout the United States.

UBBP is our 50/50 joint ventures with Boral Limited. UBBP manufactures, distributes and sells certain building products, mines raw gypsum and sells natural and synthetic gypsum throughout Asia, Australasia and the Middle East.

These financial statements and notes are to be read in conjunction with the financial statements and notes included in USG’s Annual Report on Form 10-K for the fiscal year ended December 31, 2015, which we filed with the SEC on February 10, 2016.

RECENTLY ISSUED ACCOUNTING PRONOUNCEMENTS

In March 2016, the Financial Accounting Standards Board, or FASB, issued Accounting Standards Update, or ASU, 2016-09, “Improvements to Employee Share-Based Payment Accounting,” which provides for simplification of certain aspects of employee share-based payment accounting including income taxes, classification of awards as either equity or liabilities, and classification on the statement of cash flows. The standard will be effective for us in the first quarter of 2017 and will be applied either prospectively, retrospectively or using a modified retrospective transition approach depending on the area covered in this update. We are currently in the process of assessing the impact of the ASU on our consolidated financial statements and disclosures.

In February 2016, the FASB issued ASU 2016-02, “Leases”, which supersedes existing lease guidance to require lessees to recognize assets and liabilities on the balance sheet for the rights and obligations created by long-term leases and to disclose additional quantitative and qualitative information about leasing arrangements. The standard will be effective for us in the first quarter of 2019, and we will adopt using the modified retrospective approach. While we continue to evaluate the impact of the new standard, we believe the standard will require us to implement new lease accounting systems and processes. Further, we anticipate the adoption of ASU 2016-02 will have a significant impact to our consolidated balance sheets, consolidated statements of income and disclosures.

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In January 2016, the FASB issued ASU 2016-01 “Recognition and Measurement of Financial Assets and Financial Liabilities,” which requires that most equity instruments be measured at fair value, with subsequent changes in fair value recognized in net income. The pronouncement also impacts the financial liabilities under the fair value option and the presentation and disclosure requirements for financial instruments. The ASU does not apply to equity method investments or investments in consolidated subsidiaries. The new standard will be effective for us in the first quarter of 2018 and will be applied as a cumulative-effect adjustment to the balance sheet in the year of adoption. We are currently in the process of assessing the impact of the ASU to our consolidated financial statements and disclosures.

In July 2015, the FASB issued ASU 2015-11, "Simplifying the Measurement of Inventory", which changes the measurement principle for inventory from the lower of cost or market to the lower of cost or net realizable value for entities that measure inventory using the first-in, first-out (FIFO) or average cost method. The ASU defines net realizable value as estimated selling prices in the ordinary course of business, less reasonably predictable costs of completion, disposal, and transportation. The standard will be effective for us in the first quarter of 2017 and will be applied prospectively. We do not expect the adoption of ASU 2015-11 will have a significant impact to our consolidated financial statements or disclosures.

In May 2015, the FASB issued ASU 2015-07, "Disclosures for Investments in Certain Entities That Calculate Net Asset Value per Share (or Its Equivalent)," which updates the disclosure requirements for investments that are measured at net asset value using the practical expedient. These investments are to be removed from the fair value hierarchy and shown as a reconciling item. The standard is effective for us in the first quarter of 2016 and will be applied retrospectively. The update will impact our disclosure for the Annual Report on Form 10-K.

In May 2014, the FASB issued ASU 2014-09, “Revenue from Contracts with Customers,” which supersedes the revenue recognition requirements in “Revenue Recognition (Topic 605),” and requires entities to recognize revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. In March 2016, the FASB issued ASU 2016-08, “Revenue from Contracts with Customers - Principal versus Agent Considerations (Reporting revenue gross versus net),” which clarifies gross versus net revenue reporting when another party is involved in the transaction. In April 2016, the FASB issued ASU 2016-10, “Identifying Performance Obligations and Licensing,” which amends the revenue guidance on identifying performance obligations and accounting for licenses of intellectual property. There are two transition methods available under the new standard, either cumulative effect or retrospective. The standard will be effective for us in the first quarter of 2018, and we will adopt the new standard using the retrospective approach with practical expedients. We do not expect that the adoption of ASU 2014-09, ASU 2016-08, or ASU 2016-10 will have a significant impact to our consolidated financial statements or disclosures.

2. Equity Method Investments

Equity method investments as of March 31, 2016 and December 31, 2015, were as follows:

	March 31, 2016		December 31, 2015	
(dollars in millions)	Carrying Value	Ownership Percentage	Carrying Value	Ownership Percentage
USG Boral Building Products	$ 699	50%	$ 675	50%
Other equity method investments	7	33% - 50%	7	33% - 50%
Total equity method investments	$ 706		$ 682	

Investment in USG Boral Building Products

UBBP is our 50/50 joint ventures with Boral Limited, or Boral, and consists of USG Boral Building Products Pte. Limited, a company organized under the laws of Singapore, and USG Boral Building Products Pty Limited, a company organized under the laws of Australia. It manufactures, distributes and sells certain building products, mines raw gypsum and sells natural and synthetic gypsum throughout Asia, Australasia and the Middle East (the Territory). The products that UBBP manufactures and distributes include products for wall, ceiling, floor lining and exterior systems that utilize gypsum, wallboard, referred to as plasterboard in the Territory, mineral fiber ceiling tiles, steel grid and joint compound. We account for our investment in UBBP using the equity method of accounting. As of

March 31, 2016, the amount of our consolidated retained earnings which represents undistributed earnings from UBBP is $49 million.

We formed the joint ventures with Boral on February 27, 2014. In the event certain performance targets are satisfied by UBBP, we will be obligated to pay Boral scheduled earnout payments in an aggregate amount up to $75 million, comprised first of $25 million based on performance during the first three years after closing and then up to $50 million based on

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performance during the first five years after closing. We recorded a liability representing the present value of the first earnout payment. If our conclusion on the probability were to change, we would reduce the liability with a corresponding reduction to our investment. We have not recorded a liability for the second earnout payment as we have concluded that it is currently not probable that the five-year performance target will be achieved. If our conclusion on the probability of achievement were to change, we will record a liability representing the present value of the second earnout payment with a corresponding increase to our investment. As of both March 31, 2016 and December 31, 2015, our liability for the earnout payments totaled $24 million. On our accompanying consolidated balance sheets, it is included in "Accrued expenses" as of March 31, 2016 and in "Other liabilities" as of December 31, 2015.

All of our investments accounted for under the equity method of accounting are initially recorded at cost, and subsequently adjusted for our share of the net income or loss and cash contributions and distributions to or from these entities. Because the underlying net assets in our investments are denominated in a foreign currency, translation gains or losses will impact the recorded value of our investments. Translation gains or losses recorded in other comprehensive income were as follows:

	Three months ended March 31,	
(in millions)	2016	2015
Translation gain (loss)	$17	$(16)

Summarized financial information for our equity method investments is as follows:

	Three months ended March 31,	
(in millions)	2016	2015
USG Boral Building Products:		
Net sales	$229	$228
Gross profit	65	61
Operating profit	23	23
Income from continuing operations before income taxes	24	26
Net income	15	18
Net income attributable to USG Boral Building Products	14	16
USG share of income from investment accounted for using the equity method	7	8
Other equity method investments:		
USG share of income from investments accounted for using the equity method	—	—
Total income from equity method investments	7	8

Transactions with UBBP

Our Gypsum segment sells products to UBBP. Total sales to UBBP for the three months ended March 31, 2016 and March 31, 2015 were immaterial.

In 2014, in connection with the formation of UBBP, we contributed our ownership interest in a joint venture in China to UBBP, but retained our loan receivable from this joint venture. As of March 31, 2016 and December 31, 2015, the loan receivable, including interest, totaled $14 million and is included in "Other assets" on our accompanying consolidated balance sheets.

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3. Segments

Our operations are organized into four reportable segments: Gypsum, Ceilings, Distribution and UBBP. See Note 2 for segment results for UBBP. Segment results for our Gypsum, Ceilings and Distribution segments were as follows:

	Three months ended March 31,	
(millions)	2016	2015
Net Sales:		
Gypsum	$635	$577
Ceilings	125	123
Distribution	357	334
Eliminations	(147)	(125)
Total	$970	$909
Operating Profit (Loss):		
Gypsum	$111	$68
Ceilings	29	21
Distribution	11	4
Corporate	(21)	(23)
Eliminations	(3)	6
Total	$127	$76

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4. Earning Per Share

Basic earnings per share is based on the weighted average number of common shares outstanding. Diluted earnings per share is based on the weighted average number of common shares outstanding plus the dilutive effect, if any, of market share units, or MSUs, performance shares, restricted stock units, or RSUs, stock options, and deferred shares associated with our deferred compensation program for non-employee directors.

The reconciliation of basic earnings per share to diluted earnings per share is shown in the following table.

	Three months ended March 31,	
(millions, except per-share data)	2016	2015
Net income	$67	$24
Effect of dilutive securities - Deferred compensation program for non-employee directors	—	—
Income available to shareholders	$67	$24
Average common shares	145.8	145.4
Dilutive RSUs, MSUs, performance shares and stock options	1.2	1.6
Deferred shares associated with a deferred compensation program for non-employee directors	—	0.2
Average diluted common shares	147.0	147.2
Earnings per average common share	$0.46	$0.16
Earnings per average diluted common share	$0.46	$0.16

MSUs, performance shares, RSUs, and stock options and deferred shares associated with our deferred compensation program for non-employee directors that were not included in the computation of diluted earnings per share for those periods because their inclusion would be anti-dilutive were as follows:

	Three months ended March 31,	
(millions, common shares)	2016	2015
MSUs, performance shares, RSUs and stock options	1.7	2.0
Deferred shares associated with a deferred compensation program for non-employee directors	0.2	—

5. Marketable Securities

Marketable securities are classified as available-for-sale securities and reported at fair value, with unrealized gains and losses excluded from earnings and reported in accumulated other comprehensive loss on our accompanying consolidated balance sheets. Proceeds received from sales or maturities of marketable securities were $84 million for the three months ended March 31, 2016. Our investments in marketable securities consisted of the following:

	As of March 31, 2016		As of December 31, 2015	
(millions)	Amortized Cost	Fair Value	Amortized Cost	Fair Value
Corporate debt securities	$134	$134	$134	$134
U.S. government and agency debt securities	52	52	57	57
Asset-backed debt securities	13	13	21	21
Certificates of deposit	26	26	15	15
Municipal debt securities	1	1	3	3
Total marketable securities	$226	$226	$230	$230

The realized and unrealized gains and losses for the three months ended March 31, 2016 and 2015 were immaterial. Cost basis for securities sold are determined on a first-in-first-out basis.

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Contractual maturities of marketable securities as of March 31, 2016 were as follows:

(millions)	Amortized Cost	Fair Value
Due in 1 year or less	$ 206	$ 206
Due in 1-5 years	20	20
Total marketable securities	$ 226	$ 226

Actual maturities may differ from the contractual maturities because issuers of the securities may have the right to prepay them.

6. Intangible Assets

Intangible assets are included in other assets on our accompanying consolidated balance sheets. Intangible assets with definite lives are amortized. These assets are summarized as follows:

	As of March 31, 2016			As of December 31, 2015		
(millions)	Gross Carrying Amount	Accumulated Amortization	Net	Gross Carrying Amount	Accumulated Amortization	Net
Intangible Assets with Definite Lives:						
Customer relationships	$ 70	$ (63)	$ 7	$ 70	$ (61)	$ 9
Other	9	(8)	1	9	(8)	1
Total	$ 79	$ (71)	$ 8	$ 79	$ (69)	$ 10

Total amortization expense was $2 million for both of the three months ended March 31, 2016 and 2015. Estimated amortization expense for the remainder of 2016 and for future years is as follows:

(millions)	2016	2017	2018 and thereafter
Estimated future amortization expense	$ 5	$ 2	$ 1

Intangible assets with indefinite lives are not amortized. The gross carrying amount of these assets are as follows:

(millions)	March 31, 2016	December 31, 2015
Intangible Assets with Indefinite Lives:		
Trade names	$ 22	$ 22
Other	8	8
Total	$ 30	$ 30

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7. Debt

Total debt, including the current portion of long-term debt, consisted of the following:

(millions)	March 31, 2016	December 31, 2015
5.5% senior notes due 2025	$ 350	$ 350
5.875% senior notes due 2021	350	350
6.3% senior notes due 2016	438	500
7.75% senior notes due 2018	500	500
7.875% senior notes due 2020, net of discount	249	249
Industrial revenue bonds (due 2028 through 2034)	239	239
Total	$ 2,126	$ 2,188
Less unamortized debt issuance costs	12	13
Total	$ 2,114	$ 2,175

REPURCHASE OF SENIOR NOTES

In the first quarter of 2016, we repurchased $62 million of our 6.3% Senior Notes due in 2016, referred to as the 6.3% Notes, on the open market. The transaction included premiums of $2 million and accrued interest of $1 million for aggregate consideration of $65 million. As a result of the repurchases, we recorded a loss on early extinguishment of debt, before tax, of $2 million including premiums, write-off of deferred financing fees and broker fees.

Subsequent to quarter end, we repurchased an additional $47 million of the 6.3% Notes. The transaction included $2 million for premiums and $1 million for accrued interest for an aggregate consideration of $50 million. These notes are recorded in "Current portion of long-term debt" on our consolidated balance sheets.

In the first quarter of 2015, we repurchased $350 million of our 8.375% Senior Notes due in 2018, referred to as the 2018 Notes, through both a cash tender offer and a subsequent notice of redemption of the remaining 2018 Notes. We completed a cash tender offer pursuant to which we repurchased $126 million of the 2018 Notes for aggregate consideration, including tender offer premium and accrued and unpaid interest, of $135 million. We repurchased the remaining $224 million of the 2018 Notes for aggregate consideration, including premiums and accrued and unpaid interest, of $242 million. As a result of the repurchases, we recorded a loss on early extinguishment of debt of $19 million including premiums and write-off of deferred financing fees.

Also in the first quarter of 2015, we issued $350 million of 5.5% senior notes due March 1, 2025. The net proceeds from the issuance of these notes and cash on hand were used to fund the repurchases of the 2018 Notes and all related costs and expenses. We deferred approximately $6 million of debt issuance costs that are being amortized to interest expense over the term of the notes. As of March 31, 2016, these notes were recorded on the accompanying consolidated balance sheet at $344 million.

CREDIT FACILITY

Taking into account the most recent borrowing base calculation delivered under the credit facility, which reflects trade receivables and inventory as of March 31, 2016, and outstanding letters of credit, borrowings available under the credit facility were approximately $347 million, including $50 million for CGC. As of March 31, 2016 and during the quarter then-ended, there were no borrowings under the facility. Had there been any borrowings as of that date, the applicable interest rate would have been 1.88% for loans in the US and 2.15% for loans in Canada. Outstanding letters of credit totaled $49 million as of March 31, 2016.

The fair value of our debt was approximately $2.251 billion as of March 31, 2016 and $2.295 billion as of December 31, 2015. The fair values were based on quoted prices for identical or similar liabilities in markets that are not active or valuation models in which all significant inputs and value drivers are observable and, as a result, are classified as Level 2 inputs. See Note 9 for further discussion on fair value measurements and classifications.

As of March 31, 2016, we were in compliance with the covenants contained in our credit facilities.

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8. Derivative Instruments

We use derivative instruments to manage selected commodity price and foreign currency exposures as described below. We do not use derivative instruments for speculative trading purposes, and we typically do not hedge beyond three years. Cash flows from derivative instruments are included in net cash used for operating activities in the consolidated statements of cash flows.

COMMODITY DERIVATIVE INSTRUMENTS

As of March 31, 2016, we had outstanding natural gas swap contracts to hedge forecasted purchases with an aggregate notional amount of 18 million mmBTUs (millions of British Thermal Units). All of these contracts mature by December 31, 2017. For contracts designated as cash flow hedges, the pre-tax net unrealized loss that remained in accumulated other comprehensive income (loss), or AOCI, as of March 31, 2016 was $18 million and as of December 31, 2015 was $19 million. No ineffectiveness was recorded on contracts designated as cash flow hedges in the first three months of both 2016 and 2015. Gains and losses on contracts designated as cash flow hedges are reclassified into earnings when the underlying forecasted transactions affect earnings. For contracts designated as cash flow hedges, we reassess the probability of the underlying forecasted transactions occurring on a quarterly basis.

Changes in fair value on contracts not designated as cash flow hedges are recorded to earnings. The fair value of those contracts not designated as cash flow hedges was a $2 million unrealized loss as of March 31, 2016 and December 31, 2015.

FOREIGN EXCHANGE DERIVATIVE INSTRUMENTS

We have foreign exchange forward contracts to hedge forecasted purchases of products and services denominated in foreign currencies. The notional amount of these contracts was $132 million as of March 31, 2016, and they mature by December 31, 2017. These forward contracts are designated as cash flow hedges and no ineffectiveness was recorded in the first three months of both 2016 and 2015. Gains and losses on the contracts are reclassified into earnings when the underlying transactions affect earnings. The fair value of these contracts that remained in AOCI was an unrealized pre-tax loss of $1 million as of March 31, 2016 and an unrealized pre-tax gain of $8 million as of December 31, 2015.

COUNTERPARTY RISK, MASTER NETTING ARRANGEMENTS AND BALANCE SHEET OFFSETTING

We are exposed to credit losses in the event of nonperformance by the counterparties to our derivative instruments. As of March 31, 2016, our derivatives were in a $21 million net liability position. All of our counterparties have investment grade credit ratings; accordingly, we anticipate that they will be able to fully satisfy their obligations under the contracts.

All of our derivative contracts are governed by master netting agreements negotiated between us and the counterparties that reduce our counterparty credit exposure. The agreements outline the conditions (such as credit ratings and net derivative fair values) upon which we, or the counterparties, are required to post collateral. As required by certain of our agreements, we had $21 million of collateral posted with our counterparties related to our derivatives as of March 31, 2016. Amounts paid as cash collateral are included in receivables on our accompanying consolidated balance sheets.

We have not adopted an accounting policy to offset fair value amounts related to derivative contracts under our master netting arrangements; therefore, individual derivative contracts are reflected on a gross basis, as either assets or liabilities, on our consolidated balance sheets, based on their fair value as of the balance sheet date.

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FINANCIAL STATEMENT INFORMATION

The following are the pretax effects of derivative instruments on the consolidated statements of income for the three months ended March 31, 2016 and 2015.

(millions)	Amount of Gain or (Loss) Recognized in Other Comprehensive Income on Derivatives (Effective Portion) 2016	2015	Location of Gain or (Loss) Reclassified from AOCI into Income (Effective Portion)	Amount of Gain or (Loss) Reclassified from AOCI into Income (Effective Portion) 2016	2015
Derivatives in Cash Flow Hedging Relationships					
Commodity contracts	$ (5)	$ (5)	Cost of products sold	$ (5)	$ (3)
Foreign exchange contracts	(6)	5	Cost of products sold	2	1
Total	$ (11)	$ —		$ (3)	$ (2)

(millions)	Location of Gain or (Loss) Recognized in Income on Derivatives	Amount of Gain or (Loss) Recognized in Income on Derivatives 2016	2015
Derivatives Not Designated as Hedging Instruments			
Commodity contracts	Cost of products sold	$ (1)	$ (1)
Total		$ (1)	$ (1)

The following are the fair values of derivative instruments and the location on our accompanying consolidated balance sheets as of March 31, 2016 and December 31, 2015.

(millions)	Balance Sheet Location	Fair Value 3/31/16	12/31/15	Balance Sheet Location	Fair Value 3/31/16	12/31/15
Derivatives in Cash Flow Hedging Relationships						
Commodity contracts	Other current assets	$ 1	$ 1	Accrued expenses	$ 15	$ 15
Commodity contracts	Other assets	—	—	Other liabilities	4	5
Foreign exchange contracts	Other current assets	2				