

ARMSTRONG WORLD INDUSTRIES INC

Form 10-Q

April 28, 2014

Table of Contents

**UNITED STATES**

**SECURITIES AND EXCHANGE COMMISSION**

**Washington, D.C. 20549**

**FORM 10-Q**

(Mark One)

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

**For the quarterly period ended March 31, 2014**

**OR**

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

**For the transition period from \_\_\_\_\_ to \_\_\_\_\_**

**Commission File Number 1-2116**

**ARMSTRONG WORLD INDUSTRIES, INC.**

**(Exact name of registrant as specified in its charter)**

**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 April 22, 2014 54,808,061.

Table of Contents

TABLE OF CONTENTS

	PAGE
<u>Cautionary Note Regarding Forward-Looking Statements</u>	3
<u>PART I FINANCIAL INFORMATION</u>	
Item 1. <u>Financial Statements</u>	5
Item 2. <u>Management's Discussion and Analysis of Financial Condition and Results of Operations</u>	27
Item 3. <u>Quantitative and Qualitative Disclosures About Market Risk</u>	35
Item 4. <u>Controls and Procedures</u>	35
<u>PART II OTHER INFORMATION</u>	
Item 1. <u>Legal Proceedings</u>	36
Item 1A. <u>Risk Factors</u>	36
Item 2. <u>Unregistered Sales of Equity Securities and Use of Proceeds</u>	36
Item 3. <u>Defaults Upon Senior Securities</u>	36
Item 4. <u>Mine Safety Disclosures</u>	36
Item 5. <u>Other Information</u>	36
Item 6. <u>Exhibits</u>	37
<u>Signatures</u>	38

**Table of Contents**

**CAUTIONARY NOTE REGARDING FORWARD-LOOKING STATEMENTS**

Certain statements in this Quarterly Report on Form 10-Q and the documents incorporated by reference may constitute forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995. Those forward-looking statements are subject to various risks and uncertainties and include all statements that are not historical statements of fact and those regarding our intent, belief or expectations, including, but not limited to, our expectations concerning our residential and commercial markets and their effect on our operating results; our expectations regarding the payment of dividends, and our ability to increase revenues, earnings and EBITDA (as such terms are defined by documents incorporated by reference herein). Words such as anticipate, expect, intend, plan, target, project, predict, believe, may, will, would, could, should, seek, estimate and similar expressions identify such forward-looking statements. These statements are based on management's current expectations and beliefs and are subject to a number of factors that could lead to actual results materially different from those described in the forward-looking statements. Although we believe that the assumptions underlying the forward-looking statements are reasonable, we can give no assurance that our expectations will be attained. Factors that could have a material adverse effect on our financial condition, liquidity, results of operations or future prospects or which could cause actual results to differ materially from our expectations include, but are not limited to:

global economic conditions;

construction activity;

availability and costs of raw materials and energy;

our liquidity;

covenants in our debt agreements;

our indebtedness;

competition;

key customers;

labor;

plant construction projects;

our WAVE joint venture;

environmental matters;

availability of deferred tax assets;

strategic transactions;

negative tax consequences;

international operations;

our intellectual property rights;

outsourcing;

**Table of Contents**

costs savings and productivity initiatives;

claims and litigation;

concentration of share ownership and voting control;

anti-takeover provisions; and

other risks detailed from time to time in our filings with the Securities and Exchange Commission (the "SEC"), press releases and other communications, including those set forth herein, and under "Risk Factors" included in our Annual Report on Form 10-K and in the documents incorporated by reference.

Such forward-looking statements speak only as of the date they are made. We expressly disclaim any obligation to release publicly any updates or revisions to any forward-looking statements to reflect any change in our expectations with regard thereto or change in events, conditions or circumstances on which any statement is based.

Table of ContentsPART I FINANCIAL INFORMATIONITEM 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 March 31, 2014	Three Months Ended March 31, 2013
Net sales	\$ 634.4	\$ 622.3
Cost of goods sold	479.4	477.8
Gross profit	155.0	144.5
Selling, general and administrative expenses	117.3	112.7
Equity earnings from joint venture	(14.8)	(15.2)
Operating income	52.5	47.0
Interest expense	11.6	33.2
Other non-operating expense	5.3	
Other non-operating (income)	(0.6)	(1.3)
Earnings from continuing operations before income taxes	36.2	15.1
Income tax expense	19.3	11.9
Earnings from continuing operations	16.9	3.2
Loss on sale of discontinued business, net of tax benefit of \$ and (\$0.1)		(0.2)
Net loss from discontinued operations		(0.2)
Net earnings	\$ 16.9	\$ 3.0
Other comprehensive income (loss), net of tax:		
Foreign currency translation adjustments	(0.4)	(6.2)
Derivative (loss) gain	(0.6)	4.3
Pension and postretirement adjustments	7.1	8.9
Total other comprehensive income	6.1	7.0
Total comprehensive income	\$ 23.0	\$ 10.0

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Earnings per share of common stock, continuing operations:

Basic	\$	0.31	\$	0.05
Diluted	\$	0.30	\$	0.05

Loss per share of common stock, discontinued operations:

Basic				
Diluted				

Net earnings per share of common stock:

Basic	\$	0.31	\$	0.05
Diluted	\$	0.30	\$	0.05

Average number of common shares outstanding:

Basic		54.8		59.2
Diluted		55.3		59.8

See accompanying notes to Condensed Consolidated Financial Statements beginning on page 9.



**Table of Contents**

## Armstrong World Industries, Inc., and Subsidiaries

## Condensed Consolidated Balance Sheets

(amounts in millions, except share data)

	Unaudited March 31, 2014	December 31, 2013
<u>Assets</u>		
Current assets:		
Cash and cash equivalents	\$ 131.0	\$ 135.2
Accounts and notes receivable, net	244.3	222.2
Inventories, net	428.5	381.7
Deferred income taxes	70.3	72.0
Income tax receivable	12.9	17.4
Other current assets	66.5	55.5
<b>Total current assets</b>	<b>953.5</b>	<b>884.0</b>
Property, plant, and equipment, less accumulated depreciation and amortization of \$663.7 and \$639.7, respectively	1,113.2	1,107.2
Prepaid pension costs	178.0	167.0
Investment in joint venture	128.6	132.0
Intangible assets, net	519.5	522.9
Deferred income taxes	25.5	30.1
Other non-current assets	73.2	73.4
<b>Total assets</b>	<b>\$ 2,991.5</b>	<b>\$ 2,916.6</b>
<u>Liabilities and Shareholders' Equity</u>		
Current liabilities:		
Short-term debt	\$ 42.7	
Current installments of long-term debt	30.3	\$ 23.9
Accounts payable and accrued expenses	379.4	383.6
Income tax payable	2.9	2.7
Deferred income taxes	0.7	0.7
<b>Total current liabilities</b>	<b>456.0</b>	<b>410.9</b>
Long-term debt, less current installments	1,035.0	1,042.6
Postretirement benefit liabilities	233.5	234.2
Pension benefit liabilities	223.4	225.5
Other long-term liabilities	64.1	67.5
Income taxes payable	39.9	81.7
Deferred income taxes	229.4	181.0
<b>Total noncurrent liabilities</b>	<b>1,825.3</b>	<b>1,832.5</b>
Shareholders' equity:		

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Common stock, \$0.01 par value per share, authorized 200 million shares; issued 59,864,407 shares, outstanding 54,807,025 shares in 2014 and 59,464,309 shares issued, outstanding 54,406,927 shares in 2013	0.6	0.6
Capital in excess of par value	1,112.4	1,098.4
Retained earnings	224.1	207.2
Treasury stock, at cost, 5,057,382 shares	(261.4)	(261.4)
Accumulated other comprehensive loss	(365.5)	(371.6)
Total shareholders equity	710.2	673.2
Total liabilities and shareholders equity	\$ 2,991.5	\$ 2,916.6

See accompanying notes to Condensed Consolidated Financial Statements beginning on page 9.

**Table of Contents**

## Armstrong World Industries, Inc., and Subsidiaries

## Condensed Consolidated Statements of Shareholders Equity

(amounts in millions, except share data)

Unaudited

	Three Months Ended March 31, 2014								
	Common Stock				Treasury Stock		Accumulated Other Comprehensive		Total
	Shares	Amount	Additional Paid-In Capital	Retained Earnings	Shares	Amount	Loss		
Balance at beginning of period	54,406,927	\$ 0.6	\$ 1,098.4	\$ 207.2	5,057,382	(\$ 261.4)	(\$ 371.6)	\$ 673.2	
Stock issuance	400,098								
Share-based employee compensation			14.0					14.0	
Net earnings				16.9				16.9	
Other comprehensive income							6.1	6.1	
Balance at end of period	54,807,025	\$ 0.6	\$ 1,112.4	\$ 224.1	5,057,382	(\$ 261.4)	(\$ 365.5)	\$ 710.2	

	Three Months Ended March 31, 2013								
	Common Stock				Treasury Stock		Accumulated Other Comprehensive		Total
	Shares	Amount	Additional Paid-In Capital	Retained Earnings	Shares	Amount	Loss		
Balance at beginning of period	58,934,050	\$ 0.6	\$ 1,076.8	\$ 113.1			(\$ 471.4)	\$ 719.1	
Stock issuance	212,198								
Share-based employee compensation			5.7					5.7	
Net earnings				3.0				3.0	
Other comprehensive income							7.0	7.0	
Balance at end of period	59,146,248	\$ 0.6	\$ 1,082.5	\$ 116.1			(\$ 464.4)	\$ 734.8	

See accompanying notes to Condensed Consolidated Financial Statements beginning on page 9.



**Table of Contents**

Armstrong World Industries, Inc., and Subsidiaries

Condensed Consolidated Statements of Cash Flows

(amounts in millions)

Unaudited

	Three Months Ended March 31,	
	2014	2013
Cash flows from operating activities:		
Net earnings	\$ 16.9	\$ 3.0
Adjustments to reconcile net earnings to net cash (used for) operating activities:		
Depreciation and amortization	30.0	25.4
Write off of debt financing costs		18.9
Deferred income taxes	11.8	2.4
Share-based compensation	5.1	5.1
Equity earnings from joint venture	(14.8)	(15.2)
Other non-cash adjustments, net	6.8	(0.3)
Changes in operating assets and liabilities:		
Receivables	(22.9)	(35.2)
Inventories	(47.2)	(29.6)
Other current assets	(9.9)	(3.5)
Other non-current assets	(2.6)	(6.0)
Accounts payable and accrued expenses	(6.1)	16.5
Income taxes payable	5.8	6.7
Other long-term liabilities	(7.0)	(5.2)
Other, net	1.2	3.0
Net cash (used for) operating activities	(32.9)	(14.0)
Cash flows from investing activities:		
Purchases of property, plant and equipment	(40.9)	(52.3)
Return of investment from joint venture	18.2	14.9
(Payment of) proceeds from company owned life insurance, net	(0.2)	0.1
Proceeds from the sale of assets	0.9	
Net cash (used for) investing activities	(22.0)	(37.3)
Cash flows from financing activities:		
Proceeds from revolving credit facility and other short-term debt	67.8	
Payments of revolving credit facility and other short-term debt	(25.0)	
Proceeds from long-term debt		1,025.0
Payments of long-term debt	(1.2)	(1,026.0)
Financing costs		(7.2)

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Special dividends paid	(1.2)	(0.7)
Proceeds from exercised stock options	8.8	2.7
Excess tax benefit from share-based awards	2.7	
Net cash provided by (used for) financing activities	51.9	(6.2)
Effect of exchange rate changes on cash and cash equivalents	(1.2)	(0.9)
Net (decrease) in cash and cash equivalents	(4.2)	(58.4)
Cash and cash equivalents at beginning of year	135.2	336.4
Cash and cash equivalents at end of period	\$ 131.0	\$ 278.0

Supplemental Cash Flow Disclosures:

Interest paid	\$ 10.0	\$ 11.1
Income taxes paid, net	1.7	2.6
Amounts in accounts payable for capital expenditures	16.8	14.9

See accompanying notes to Condensed Consolidated Financial Statements beginning on page 9.

**Table of Contents**

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 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 (the 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 pursuant to which TPG purchased from the Asbestos PI Trust 7,000,000 shares of our common stock and acquired an economic interest in an additional 1,039,777 shares pursuant to a forward sales contract. During the fourth quarter of 2012, the Asbestos PI Trust and TPG together sold 5,980,000 shares in a secondary public offering. In the third quarter of 2013, the Asbestos PI Trust and TPG together sold 12,057,382 shares in another secondary public offering. Contemporaneously with this secondary public offering, we paid \$261.4 million, including associated fees, to buy back 5,057,382 shares, which we currently hold in treasury. The treasury share purchase was funded by existing cash and borrowings under our credit and securitization facilities. In November 2013, the Asbestos PI Trust physically settled the 2009 forward sales contract by delivering to TPG the 1,039,777 shares in which TPG previously held an economic interest. Additionally, during the fourth quarter of 2013, the Asbestos PI Trust and TPG together sold an additional 6,000,000 shares. In March 2014, the Asbestos PI Trust and TPG together sold an additional 3,900,000 shares, which consisted of the last remaining 2,054,977 shares owned by TPG and an additional 1,845,023 shares owned by the Asbestos PI Trust. We did not sell any shares and did not receive any proceeds from these offerings. As a result of these transactions the Asbestos PI Trust now holds approximately 17% of our outstanding shares and TPG no longer owns any of our common stock.

In September 2012, we entered into a definitive agreement to sell our cabinets business for \$27 million. The sale was completed in October 2012. The transaction was subject to working capital adjustments which were completed in the second quarter of 2013. The financial results of the cabinets business, which were previously shown as a separate reporting segment, have been reclassified as discontinued operations for all periods presented. See Note 3 to the Condensed Consolidated Financial Statements for additional financial information related to discontinued operations.

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, 2013. 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, 2013. 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 2014 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



**Table of Contents**

## Armstrong World Industries, Inc., and Subsidiaries

## Notes to Condensed Consolidated Financial Statements (Unaudited)

(dollar amounts in millions)

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 February 2013, the Financial Accounting Standards Board ( FASB ) issued Accounting Standards Update ( ASU ) 2013-04 *Obligations Resulting from Joint and Several Liability Arrangements for Which the Total Amount of the Obligation Is Fixed at the Reporting Date* which is part of ASC 405: Liabilities. The guidance requires an entity to measure obligations resulting from joint and several liability arrangements, within the scope of this ASU, as the amount the reporting entity agreed to pay on the basis of its arrangement among its co-obligors and any additional amount the reporting entity expects to pay on behalf of its co-obligors. The guidance requires an entity to disclose the nature and amount of the obligation. The guidance is to be applied retrospectively and was effective for us beginning January 1, 2014. There was no impact on our financial condition, results of operations or cash flows as a result of the adoption of this guidance.

In July 2013, the FASB issued ASU 2013-11 *Income Taxes - Presentation of an Unrecognized Tax Benefit When a Net Operating Loss Carryforward, a Similar Tax Loss, or a Tax Credit Carryforward Exists* which is part of ASC 740: Income Taxes. The guidance requires an entity to present an unrecognized tax benefit and a net operating loss ( NOL ) carryforward, a similar tax loss, or a tax credit carryforward on a net basis as part of a deferred tax asset, unless the unrecognized tax benefit is not available to reduce the deferred tax asset component or would not be utilized for that purpose, then a liability would be recognized. The guidance was applied prospectively and was effective for us beginning January 1, 2014. As a result of adopting this guidance, we recorded a reduction to noncurrent income taxes payable and a corresponding increase to noncurrent deferred tax liabilities of approximately \$40 million. There was no impact on results of operations or cash flows as a result of the adoption of this guidance.

Operating results for the first quarter of 2014 and 2013 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 March 31,	
	2014	2013
<b><u>Net sales to external customers</u></b>		
Building Products	\$ 308.2	\$ 292.8
Resilient Flooring	208.1	214.8

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Wood Flooring	118.1	114.7
<b>Total net sales to external customers</b>	<b>\$ 634.4</b>	<b>\$ 622.3</b>
	Three Months Ended March 31,	
	2014	2013
<u>Segment operating income (loss)</u>		
Building Products	\$ 57.8	\$ 59.3
Resilient Flooring	9.4	6.4
Wood Flooring	5.1	0.5
Unallocated Corporate (expense)	(19.8)	(19.2)
<b>Total consolidated operating income</b>	<b>\$ 52.5</b>	<b>\$ 47.0</b>

**Table of Contents**

## Armstrong World Industries, Inc., and Subsidiaries

## Notes to Condensed Consolidated Financial Statements (Unaudited)

(dollar amounts in millions)

	Three Months Ended March 31,	
	2014	2013
Total consolidated operating income	\$ 52.5	\$ 47.0
Interest expense	11.6	33.2
Other non-operating expense	5.3	
Other non-operating income	(0.6)	(1.3)
Earnings from continuing operations before income taxes	\$ 36.2	\$ 15.1

	March 31, 2014	December 31, 2013
<b>Segment assets</b>		
Building Products	\$ 1,087.3	\$ 1,071.9
Resilient Flooring	680.2	635.2
Wood Flooring	354.6	335.2
Unallocated Corporate	869.4	874.3
Total consolidated assets	\$ 2,991.5	\$ 2,916.6

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.

**NOTE 3. DISCONTINUED OPERATIONS**

In September 2012, we entered into a definitive agreement to sell our cabinets business to American Industrial Partners ( AIP ) for \$27 million in cash. During the third quarter of 2012, we recorded an impairment charge of \$17.5 million on the cabinets assets to reflect the expected proceeds from the sale. The sale was completed in October 2012. The transaction was subject to working capital adjustments which were completed in the second quarter of 2013.

The operating results of the cabinets business (previously shown as the Cabinets reporting segment), for the first quarter of 2013 was a pre-tax loss of \$0.3 million (\$0.2 million net of tax benefit). The financial results of the cabinets business have been classified as discontinued operations for all periods presented. The Condensed Consolidated Statement of Cash Flows does not separately report the cash flows of the discontinued operation.

During the third quarter of 2013, we recorded an estimated liability of \$7.5 million for a potential withdrawal liability related to a multi-employer pension plan. See Note 17 to the Condensed Consolidated Financial Statements for further information.



**Table of Contents**

## Armstrong World Industries, Inc., and Subsidiaries

## Notes to Condensed Consolidated Financial Statements (Unaudited)

(dollar amounts in millions)

**NOTE 4. ACCOUNTS AND NOTES RECEIVABLE**

	March 31, 2014	December 31, 2013
Customer receivables	\$ 263.1	\$ 242.7
Customer notes	1.3	1.6
Miscellaneous receivables	7.3	5.9
Less allowance for warranties, discounts and losses	(27.4)	(28.0)
Accounts and notes receivable, net	\$ 244.3	\$ 222.2

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 5. INVENTORIES**

	March 31, 2014	December 31, 2013
Finished goods	\$ 317.3	\$ 292.8
Goods in process	34.9	29.2
Raw materials and supplies	133.2	118.6
Less LIFO and other reserves	(56.9)	(58.9)
Total inventories, net	\$ 428.5	\$ 381.7

**NOTE 6. OTHER CURRENT ASSETS**

	March 31, 2014	December 31, 2013
Prepaid expenses	\$ 49.5	\$ 46.0
Fair value of derivative assets	7.4	5.9
Other	9.6	3.6

Total other current assets	\$ 66.5	\$ 55.5
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NOTE 7. EQUITY INVESTMENT

Investment in joint venture at March 31, 2014 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 March 31,	
	2014	2013
Net sales	\$ 92.3	\$ 91.9
Gross profit	43.5	43.3
Net earnings	32.2	33.8

**Table of Contents**

## Armstrong World Industries, Inc., and Subsidiaries

## Notes to Condensed Consolidated Financial Statements (Unaudited)

(dollar amounts in millions)

**NOTE 8. INTANGIBLE ASSETS**

The following table details amounts related to our intangible assets as of March 31, 2014 and December 31, 2013.

	Estimated Useful Life	March 31, 2014 Gross Carrying Amount	Accumulated Amortization	December 31, 2013 Gross Carrying Amount	Accumulated Amortization
<b><u>Amortizing intangible assets</u></b>					
Customer relationships	20 years	\$ 165.5	\$ 62.2	\$ 165.5	\$ 60.2
Developed technology	15 years	83.3	40.9	83.1	39.4
Other	Various	21.2	2.0	21.5	1.9
<b>Total</b>		<b>\$ 270.0</b>	<b>\$ 105.1</b>	<b>\$ 270.1</b>	<b>\$ 101.5</b>
<b><u>Non-amortizing intangible assets</u></b>					
Trademarks and brand names	Indefinite	354.6		354.3	
<b>Total intangible assets</b>		<b>\$ 624.6</b>		<b>\$ 624.4</b>	

	Three Months Ended March 31,	
	2014	2013
Amortization expense	\$ 3.6	\$ 3.6

**NOTE 9. SEVERANCES AND RELATED COSTS**

In the first quarter of 2013, we recorded \$5.2 million for severance and related costs to reflect approximately 40 position eliminations in our European Resilient Flooring business (\$1.8 million in cost of goods sold and \$1.0 million in selling, general and administrative ( SG&A ) expense) and approximately 40 position eliminations in our Resilient Flooring business in Australia (\$2.4 million in cost of goods sold).

**NOTE 10. INCOME TAX EXPENSE**

	Three Months Ended	
	March 31,	
	2014	2013
Earnings from continuing operations before income taxes	\$ 36.2	\$ 15.1
Income tax expense	19.3	11.9
Effective tax rate	53.3%	78.8%

The effective tax rate for the first quarter of 2014 was lower than the comparable period of 2013 primarily due to mix of income and a lower rate impact of unbenefitted foreign losses. First quarter 2013 income was lower as a result of the write-off of unamortized debt financing costs related to our previous credit facility to interest expense.

We do not expect to record any material changes during 2014 to unrecognized tax benefits that were claimed on tax returns covering tax years ending on or before December 31, 2013.

As of March 31, 2014, we consider foreign unremitted earnings to be permanently reinvested.



**Table of Contents**

## Armstrong World Industries, Inc., and Subsidiaries

## Notes to Condensed Consolidated Financial Statements (Unaudited)

(dollar amounts in millions)

**NOTE 11. DEBT**

On March 15, 2013, we refinanced our \$1.3 billion senior credit facility and amended the underlying credit agreement. The amended facility is composed of a \$250 million revolving credit facility (with a \$150 million sublimit for letters of credit), a \$550 million Term Loan A and a \$475 million Term Loan B. The terms of the facility resulted in a lower interest rate spread (2.5% vs. 3.0%) than our previous facility. We also extended the maturity of Term Loan A from November 2015 to March 2018 and of Term Loan B from March 2018 to March 2020. 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. In connection with the refinancing, we incurred \$8.3 million for bank, legal, and other fees, of which \$7.2 million was capitalized and is being amortized into interest expense over the life of the loans. Additionally, we wrote off \$18.9 million of unamortized debt financing costs in the first quarter of 2013 related to our previous credit facility to interest expense (see Liquidity for further information).

As of March 31, 2014, we were in compliance with all covenants of the amended senior credit facility. Our debt agreements include other restrictions, including restrictions pertaining to the acquisition of additional debt, the redemption, repurchase or retirement of our capital stock, payment of dividends, and certain financial transactions as it relates to specified assets. We currently believe that default under these covenants is unlikely. Fully borrowing under our revolving credit facility would not violate these covenants.

On March 28, 2013, we amended our \$100 million Accounts Receivable Securitization Facility with the Bank of Nova Scotia. We decreased the facility to \$75 million to reduce commitment fees on unused capacity. The maturity was extended to March 2016.

As of March 31, 2014, outstanding balances on the revolving credit facility and accounts receivable securitization facility were \$20.0 million and \$17.8 million respectively and are classified as short-term debt. There was no outstanding balance on either facility as of December 31, 2013.

**NOTE 12. PENSIONS AND OTHER BENEFIT PROGRAMS**

Following are the components of net periodic benefit costs:

	Three Months Ended March 31,	
	2014	2013
<b><u>U.S. defined-benefit plans:</u></b>		
<b><u>Pension benefits</u></b>		
Service cost of benefits earned during the period	\$ 3.6	\$ 4.2
Interest cost on projected benefit obligation	21.4	19.9

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Expected return on plan assets	(34.8)	(34.1)
Amortization of prior service cost	0.5	0.5
Amortization of net actuarial loss	10.6	10.2
Net periodic pension cost	\$ 1.3	\$ 0.7
<u>Retiree health and life insurance benefits</u>		
Service cost of benefits earned during the period	\$ 0.2	\$ 0.3
Interest cost on projected benefit obligation	2.7	2.4
Amortization of prior service credit	(0.1)	(0.2)
Amortization of net actuarial gain	(1.0)	(0.9)
Net periodic postretirement benefit cost	\$ 1.8	\$ 1.6
<u>Non-U.S. defined-benefit pension plans</u>		
Service cost of benefits earned during the period	\$ 0.8	\$ 0.7
Interest cost on projected benefit obligation	3.5	3.3
Expected return on plan assets	(2.9)	(2.4)
Amortization of net actuarial loss	0.5	0.7
Net periodic pension cost	\$ 1.9	\$ 2.3

**Table of Contents**

## Armstrong World Industries, Inc., and Subsidiaries

## Notes to Condensed Consolidated Financial Statements (Unaudited)

(dollar amounts in millions)

**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:

	March 31, 2014		December 31, 2013	
	Carrying amount	Estimated fair value	Carrying amount	Estimated fair value
<b>Assets (Liabilities), net:</b>				
Total long-term debt, including current portion	(\$ 1,065.3)	(\$ 1,066.5)	(\$ 1,066.5)	(\$ 1,065.2)
Foreign currency contract obligations	6.4	6.4	5.2	5.2
Natural gas contracts	0.6	0.6	0.5	0.5
Interest rate swap contracts	(7.9)	(7.9)	(7.9)	(7.9)

The carrying amounts of cash and cash equivalents, receivables, accounts payable, accrued expenses, and short-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.

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.

**Table of Contents**

## Armstrong World Industries, Inc., and Subsidiaries

## Notes to Condensed Consolidated Financial Statements (Unaudited)

(dollar amounts in millions)

Assets and liabilities are summarized below:

	March 31, 2014		December 31, 2013	
	Quoted, active markets Level 1	Other observable inputs Level 2	Quoted, active markets Level 1	Other observable inputs Level 2
Assets (Liabilities), net:				
Total long-term debt, including current portion	(\$ 470.8)	(\$ 595.7)	(\$ 470.9)	(\$ 594.3)
Foreign currency contract obligations	6.4		5.2	
Natural gas contracts		0.6		0.5
Interest rate swap contracts		(7.9)		