3M CO
Form 10-Q
April 30, 2015
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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

FORM 10-Q

QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE

SECURITIES EXCHANGE ACT OF 1934

For the quarterly period ended March 31, 2015

Commission file number: 1-3285

3M COMPANY

(Exact name of registrant as specified in its charter)

DELAWARE	**41-0417775**
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)
3M Center, St. Paul, Minnesota	**55144**
(Address of principal executive offices)	(Zip Code)

(651) 733-1110

(Registrant s telephone number, including area code)

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 x No o

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes x No o

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See the definitions of large accelerated filer, accelerated filer and smaller reporting company in Rule 12b-2 of the Exchange Act.

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

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

Indicate the number of shares outstanding of each of the issuer s classes of common stock, as of the latest practicable date.

Class	**Outstanding at March 31, 2015**
Common Stock, $0.01 par value per share	634,340,975 shares

This document (excluding exhibits) contains 70 pages.

The table of contents is set forth on page 2.

The exhibit index begins on page 67.

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FORM 10-Q

For the Quarterly Period Ended March 31, 2015

PART I. Financial Information

Item 1. Financial Statements.

3M Company and Subsidiaries

Consolidated Statement of Income

(Unaudited)

(Millions, except per share amounts)		**Three months ended March 31, 2015**		**2014**
Net sales	**$**	**7,578**	$	7,831
Operating expenses				
Cost of sales		**3,821**		4,031
Selling, general and administrative expenses		**1,564**		1,632
Research, development and related expenses		**463**		452
Total operating expenses		**5,848**		6,115
Operating income		**1,730**		1,716
Interest expense and income				
Interest expense		**31**		37
Interest income		**(4)**		(9)
Total interest expense net		**27**		28
Income before income taxes		**1,703**		1,688
Provision for income taxes		**502**		463
Net income including noncontrolling interest	**$**	**1,201**	$	1,225
Less: Net income attributable to noncontrolling interest		**2**		18
Net income attributable to 3M	**$**	**1,199**	$	1,207
Weighted average 3M common shares outstanding basic		**636.2**		661.5
Earnings per share attributable to 3M common shareholders basic	**$**	**1.88**	$	1.83
Weighted average 3M common shares outstanding diluted		**649.2**		674.5
Earnings per share attributable to 3M common shareholders diluted	**$**	**1.85**	$	1.79
Cash dividends paid per 3M common share	**$**	**1.025**	$	0.855

The accompanying Notes to Consolidated Financial Statements are an integral part of this statement.

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3M Company and Subsidiaries

Consolidated Statement of Comprehensive Income

(Unaudited)

	Three months ended March 31,	
(Millions)	**2015**	**2014**
Net income including noncontrolling interest	**$ 1,201**	$ 1,225
Other comprehensive income (loss), net of tax:		
Cumulative translation adjustment	**(193)**	20
Defined benefit pension and postretirement plans adjustment	**91**	61
Debt and equity securities, unrealized gain (loss)		1
Cash flow hedging instruments, unrealized gain (loss)	**70**	2
Total other comprehensive income (loss), net of tax	**(32)**	84
Comprehensive income (loss) including noncontrolling interest	**1,169**	1,309
Comprehensive (income) loss attributable to noncontrolling interest	**(2)**	(30)
Comprehensive income (loss) attributable to 3M	**$ 1,167**	$ 1,279

The accompanying Notes to Consolidated Financial Statements are an integral part of this statement.

3M Company and Subsidiaries

Consolidated Balance Sheet

(Unaudited)

(Dollars in millions, except per share amount)		March 31, 2015		December 31, 2014
Assets				
Current assets				
Cash and cash equivalents	$	1,791	$	1,897
Marketable securities current		1,018		626
Accounts receivable net		4,408		4,238
Inventories				
Finished goods		1,713		1,723
Work in process		1,116		1,081
Raw materials and supplies		875		902
Total inventories		3,704		3,706
Other current assets		1,597		1,298
Total current assets		12,518		11,765
Marketable securities non-current		13		828
Investments		102		102
Property, plant and equipment		22,473		22,841
Less: Accumulated depreciation		(14,187)		(14,352)
Property, plant and equipment net		8,286		8,489
Goodwill		6,934		7,050
Intangible assets net		1,396		1,435
Prepaid pension benefits		56		46
Other assets		1,338		1,554
Total assets	$	30,643	$	31,269
Liabilities				
Current liabilities				
Short-term borrowings and current portion of long-term debt	$	132	$	106
Accounts payable		1,801		1,807
Accrued payroll		446		732
Accrued income taxes		464		435
Other current liabilities		2,239		2,918
Total current liabilities		5,082		5,998
Long-term debt		6,459		6,731
Pension and postretirement benefits		3,764		3,843
Other liabilities		1,386		1,555
Total liabilities	$	16,691	$	18,127
Commitments and contingencies (Note 10)				
Equity				
3M Company shareholders equity:				
Common stock par value, $.01 par value, 944,033,056 shares issued	$	9	$	9
Additional paid-in capital		4,607		4,379
Retained earnings		35,080		34,317
Treasury stock, at cost: 309,692,081 shares at March 31, 2015; 308,898,462 shares at December 31, 2014		(19,458)		(19,307)
Accumulated other comprehensive income (loss)		(6,321)		(6,289)

Total 3M Company shareholders equity		**13,917**		13,109
Noncontrolling interest		**35**		33
Total equity	**$**	**13,952**	$	13,142
Total liabilities and equity	**$**	**30,643**	$	31,269

The accompanying Notes to Consolidated Financial Statements are an integral part of this statement.

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3M Company and Subsidiaries

Consolidated Statement of Cash Flows

(Unaudited)

(Millions)	Three months ended March 31, 2015	2014
Cash Flows from Operating Activities		
Net income including noncontrolling interest	$ **1,201**	$ 1,225
Adjustments to reconcile net income including noncontrolling interest to net cash provided by operating activities		
Depreciation and amortization	**339**	350
Company pension and postretirement contributions	**(91)**	(42)
Company pension and postretirement expense	**134**	98
Stock-based compensation expense	**138**	122
Deferred income taxes	**44**	(83)
Excess tax benefits from stock-based compensation	**(101)**	(51)
Changes in assets and liabilities		
Accounts receivable	**(296)**	(347)
Inventories	**(131)**	(131)
Accounts payable	**56**	84
Accrued income taxes (current and long-term)	**100**	135
Other net	**(313)**	(268)
Net cash provided by operating activities	**1,080**	1,092
Cash Flows from Investing Activities		
Purchases of property, plant and equipment (PP&E)	**(291)**	(293)
Proceeds from sale of PP&E and other assets	**4**	3
Acquisitions, net of cash acquired	**(150)**	
Purchases of marketable securities and investments	**(191)**	(601)
Proceeds from maturities and sale of marketable securities and investments	**605**	599
Proceeds from sale of businesses	**19**	
Other investing	**4**	5
Net cash used in investing activities		(287)
Cash Flows from Financing Activities		
Change in short-term debt net	**(4)**	466
Repayment of debt (maturities greater than 90 days)		(64)
Proceeds from debt (maturities greater than 90 days)		172
Purchases of treasury stock	**(886)**	(1,708)
Proceeds from issuance of treasury stock pursuant to stock option and benefit plans	**309**	267
Dividends paid to shareholders	**(652)**	(566)
Excess tax benefits from stock-based compensation	**101**	51
Other net	**(22)**	(17)
Net cash used in financing activities	**(1,154)**	(1,399)
Effect of exchange rate changes on cash and cash equivalents	**(32)**	(33)
Net increase (decrease) in cash and cash equivalents	**(106)**	(627)
Cash and cash equivalents at beginning of year	**1,897**	2,581
Cash and cash equivalents at end of period	$ **1,791**	$ 1,954

The accompanying Notes to Consolidated Financial Statements are an integral part of this statement.

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3M Company and Subsidiaries

Notes to Consolidated Financial Statements

(Unaudited)

NOTE 1. Significant Accounting Policies

Basis of Presentation

The interim consolidated financial statements are unaudited but, in the opinion of management, reflect all adjustments necessary for a fair statement of the Company s consolidated financial position, results of operations and cash flows for the periods presented. These adjustments consist of normal, recurring items. The results of operations for any interim period are not necessarily indicative of results for the full year. The interim consolidated financial statements and notes are presented as permitted by the requirements for Quarterly Reports on Form 10-Q. This Quarterly Report on Form 10-Q should be read in conjunction with the Company s consolidated financial statements and notes included in its 2014 Annual Report on Form 10-K.

Foreign Currency Translation

Local currencies generally are considered the functional currencies outside the United States. Assets and liabilities for operations in local-currency environments are translated at month-end exchange rates of the period reported. Income and expense items are translated at month-end exchange rates of each applicable month. Cumulative translation adjustments are recorded as a component of accumulated other comprehensive income (loss) in shareholders equity.

Although local currencies are typically considered as the functional currencies outside the United States, under Accounting Standards Codification (ASC) 830, *Foreign Currency Matters*, the reporting currency of a foreign entity s parent is assumed to be that entity s functional currency when the economic environment of a foreign entity is highly inflationary generally when its cumulative inflation is approximately 100 percent or more for the three years that precede the beginning of a reporting period. 3M has a subsidiary in Venezuela with operating income representing less than 1.0 percent of 3M s consolidated operating income for 2014. 3M has determined that the applicable cumulative inflation rate of Venezuela has exceeded, and continues to exceed, 100 percent since November 2009. Accordingly, since January 1, 2010, the financial statements of the Venezuelan subsidiary have been remeasured as if its functional currency were that of its parent.

The Venezuelan government sets official rates of exchange and conditions precedent to purchase foreign currency at these rates with local currency. Such rates and conditions are subject to change. In January 2014, the Venezuelan government announced that a new agency, the National Center for Foreign Commerce (CENCOEX), had assumed the role with respect to the continuation of the existing official exchange rate; significantly expanded the use of a second foreign exchange mechanism called the Complementary System for Foreign Currency Acquirement (or SICAD1); and issued exchange regulations indicating the SICAD1 rate of exchange would be used for payments related to international investments. The SICAD1 exchange mechanism, a complementary currency auction system, had previously been created for purchases of foreign currency by only certain eligible importers and tourists. In late March 2014, the Venezuelan government launched a third foreign exchange mechanism, SICAD2, which relied on U.S. dollar cash and U.S. dollar denominated bonds offered by the Venezuelan Central Bank, PDVSA (the Venezuelan national oil and gas company) and certain private companies. SICAD2 was announced as being available to all industry sectors and that its use would not be restricted as to purpose. In February 2015, the Venezuelan government introduced another foreign currency exchange platform called the Marginal System of Foreign Currency (SIMADI), resulting in the elimination and replacement of the SICAD2 rate. The SIMADI rate was described as being derived from daily private bidders and buyers exchanging offers through authorized agents and approved and published by the Venezuelan Central Bank.

Since January 1, 2010, as discussed above, the financial statements of 3M s Venezuelan subsidiary have been remeasured as if its functional currency were that of its parent. For the periods presented, this remeasurement utilized the official CENCOEX rate into March 2014, the SICAD1 rate beginning in late March 2014, the SICAD2 rate beginning in June 2014, and the SIMADI rate beginning in February 2015. 3M s uses of these applicable exchange rates were based upon evaluation of a number of factors including, but not limited to, the exchange rate the Company s Venezuelan subsidiary may legally use to convert currency, settle transactions or pay dividends; the probability of accessing and obtaining currency by use of a particular rate or mechanism; and the Company s intent and ability to use a particular exchange mechanism. Other factors notwithstanding, the remeasurement impacts as a result of the changes in use of these exchange rates did not have material impacts on 3M s consolidated results of operations or financial condition.

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The Company continues to monitor circumstances relative to its Venezuelan subsidiary. Changes in applicable exchange rates or exchange mechanisms may continue in the future. These changes could impact the rate of exchange applicable to remeasure the Company s net monetary assets (liabilities) denominated in Venezuelan Bolivars (VEF). As March 31, 2015, the Company had a balance of net monetary assets denominated in VEF of less than 100 million VEF and the CENCOEX, SICAD (formerly SICAD1), and SIMADI exchange rates were approximately 6 VEF, 12 VEF, and 190 VEF per U.S. dollar, respectively.

A need to deconsolidate the Company s Venezuelan subsidiary s operations may result from a lack of exchangeability of VEF-denominated cash coupled with an acute degradation in the ability to make key operational decisions due to government regulations in Venezuela. 3M monitors factors such as its ability to access various exchange mechanisms; the impact of government regulations on the Company s ability to manage its Venezuelan subsidiary s capital structure, purchasing, product pricing, and labor relations; and the current political and economic situation within Venezuela. Based upon such factors as of March 31, 2015, the Company continues to consolidate its Venezuelan subsidiary. As of March 31, 2015, the balance of intercompany receivables due from this subsidiary is less than $20 million and its equity balance is not significant.

Earnings Per Share

The difference in the weighted average 3M shares outstanding for calculating basic and diluted earnings per share attributable to 3M common shareholders is a result of the dilution associated with the Company s stock-based compensation plans. Certain options outstanding under these stock-based compensation plans were not included in the computation of diluted earnings per share attributable to 3M common shareholders because they would not have had a dilutive effect (3.5 million average options for the three months ended March 31, 2015 and 2.3 million average options for the three months ended March 31, 2014). The computations for basic and diluted earnings per share follow:

Earnings Per Share Computations

	Three months ended March 31,			
(Amounts in millions, except per share amounts)	**2015**		**2014**	
Numerator:				
Net income attributable to 3M	**$**	**1,199**	$	1,207
Denominator:				
Denominator for weighted average 3M common shares outstanding basic		**636.2**		661.5
Dilution associated with the Company s stock-based compensation plans		**13.0**		13.0
Denominator for weighted average 3M common shares outstanding diluted		**649.2**		674.5
Earnings per share attributable to 3M common shareholders basic	**$**	**1.88**	$	1.83
Earnings per share attributable to 3M common shareholders diluted	**$**	**1.85**	$	1.79

New Accounting Pronouncements

In April 2014, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update (ASU) No. 2014-08, *Reporting Discontinued Operations and Disclosures of Disposals of Components of an Entity*, which changed the criteria for determining which disposals can be presented as discontinued operations and modified related disclosure requirements. This standard has the impact of reducing the frequency of disposals reported as discontinued operations, by requiring such a disposal to represent a strategic shift that has or will have a major effect on an entity s operations and financial results. However, existing provisions that prohibited an entity from reporting a discontinued operation if it had certain continuing cash flows or involvement with the component after disposal were eliminated by this standard. The ASU also expands the disclosures for discontinued operations and requires new disclosures related to individually significant disposals that do not qualify as discontinued operations. For 3M, this ASU was effective prospectively beginning January 1, 2015. This ASU was applied to the 2015 divestiture discussed in Note 2 and had no material impact on consolidated results of operations and financial condition.

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In May 2014, the FASB issued ASU No. 2014-09, *Revenue from Contracts with Customers*, which provides a single comprehensive model to be used in the accounting for revenue arising from contracts with customers and supersedes most current revenue recognition guidance, including industry-specific guidance. The standard s stated core principle is that an entity should 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. To achieve this core principle the ASU includes provisions within a five step model that includes identifying the contract with a customer, identifying the performance obligations in the contract, determining the transaction price, allocating the transaction price to the performance obligations, and recognizing revenue when (or as) an entity satisfies a performance obligation. The standard also specifies the accounting for some costs to obtain or fulfill a contract with a customer and requires expanded disclosures about revenue recognition. The standard provides for either full retrospective adoption or a modified retrospective adoption by which it is applied only to the most current period presented. For 3M, this ASU is effective January 1, 2017. The Company is currently assessing this ASU s impact on 3M s consolidated results of operations and financial condition.

In February 2015, the FASB issued ASU No. 2015-02, *Amendments to the Consolidation Analysis*, which changes guidance related to both the variable interest entity (VIE) and voting interest entity (VOE) consolidation models. With respect to the VIE model, the standard changes, among other things, the identification of variable interests associated with fees paid to a decision maker or service provider, the VIE characteristics for a limited partner or similar entity, and the primary beneficiary determination. With respect to the VOE model, the ASU eliminates the presumption that a general partner controls a limited partnership or similar entity unless the presumption can otherwise be overcome. Under the new guidance, a general partner would largely not consolidate a partnership or similar entity under the VOE model. For 3M, this ASU is effective January 1, 2016, with early adoption permitted. 3M does not have significant involvement with entities subject to consolidation considerations impacted by the VIE model changes or with limited partnerships potentially impacted by the VOE model changes. As a result, 3M does not expect this ASU to have a material impact on the Company s consolidated results of operations and financial condition.

In April 2015, the FASB issued ASU No. 2015-03, *Simplifying the Presentation of Debt Issuance Costs*. Under this new standard, debt issuance costs reported on the consolidated balance sheet would be reflected as a direct deduction from the related debt liability rather than as an asset. For 3M, this ASU is effective January 1, 2016, with early adoption permitted. Retrospective application to prior periods is required. As this standard impacts only the classification of certain amounts within the consolidated balance sheet, 3M does not expect this ASU to have a material impact on the Company s consolidated results of operations and financial condition.

In April 2015, the FASB issued ASU No. 2015-05, *Customer s Accounting for Fees Paid in a Cloud Arrangement*, which requires a customer to determine whether a cloud computing arrangement contains a software license. If the arrangement contains a software license, the customer would account for fees related to the software license element in a manner consistent with how the acquisition of other acquired software licenses is accounted. If the arrangement does not contain a software license, the customer would account for the arrangement as a service contract. An arrangement would contain a software license element if both (1) the customer has the contractual right to take possession of the software at any time during the hosting period without significant penalty and (2) it is feasible for the customer to either run the software on its own hardware or contract with another party unrelated to the vendor to host the software. For 3M, this ASU is effective January 1, 2016, with early adoption permitted. The standard provides for adoption either fully retrospectively or prospectively to arrangements entered into, or materially modified, after the effective date. The Company is currently assessing this ASU s impact on 3M s consolidated results of operations and financial condition.

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NOTE 2. Acquisitions and Divestitures

3M makes acquisitions of certain businesses from time to time that the Company feels align with its strategic intent with respect to, among other factors, growth markets and adjacent product lines or technologies. Goodwill resulting from business combinations is largely attributable to the existing workforce of the acquired businesses and synergies expected to arise after 3M s acquisition of these businesses. In addition to business combinations, 3M periodically acquires certain tangible and/or intangible assets and purchases interests in certain enterprises that do not otherwise qualify for accounting as business combinations. These transactions are largely reflected as additional asset purchase and investment activity.

During the three months ended March 31, 2015, the purchase price paid for business combinations (net of cash acquired) was $150 million, which primarily related to 3M s acquisition of Ivera Medical Corp. (discussed below).

In March 2015, 3M (Health Care Business) purchased all of the outstanding shares of Ivera Medical Corp., headquartered in San Diego, California. Ivera Medical Corp., with annual sales of approximately $30 million, is a manufacturer of health care products that disinfect and protect devices used for access into a patient s bloodstream. The allocation of purchase price related to this acquisition is considered preliminary, largely with respect to intangible assets, and tax-related assets and liabilities. In addition, in the first quarter of 2015, 3M (Industrial Business) purchased the remaining interest in a former equity method investment for an immaterial amount.

Purchased identifiable finite-lived intangible assets related to the Ivera Medical Corp. acquisition which closed in the three months ended March 31, 2015 totaled $52 million. The associated finite-lived intangible assets acquired will be amortized on a systematic and rational basis (generally straight line) over a weighted-average life of 13 years (lives ranging from two to 16 years). Acquired in-process research and development and identifiable intangible assets for which significant assumed renewals or extensions of underlying arrangements impacted the determination of their useful lives were not material. Pro forma information related to acquisitions was not included because the impact on the Company s consolidated results of operations was not considered to be material.

In February 2015, 3M announced that it had entered into a definitive agreement with Polypore International Inc., headquartered in Charlotte, North Carolina, to acquire the assets and liabilities associated with Polypore s Separations Media business for a total purchase price of approximately $1.0 billion. Polypore s Separations Media business is a leading provider of microporous membranes and modules for filtration in the life sciences, industrial and specialty segments with annual sales of approximately $208 million for the 2014 fiscal year ended January 3, 2015. Separately, Asahi Kasei, a leading diversified chemical manufacturer based in Tokyo, Japan, announced that it entered into a definitive merger agreement to acquire Polypore s Energy Storage business. Both transactions are subject to regulatory approvals and customary closing conditions. In addition, both transactions are conditioned on 3M s transaction with Polypore closing immediately prior to the closing of Asahi Kasei s transaction with Polypore.

In January 2015, 3M (Electronics and Energy Business) completed the sale of its global static control business to Desco Industries Inc., based in Chino, California. 2014 sales of this business were $46 million. This transaction was not considered material.

Refer to Note 2 in 3M s 2014 Annual Report on Form 10-K for more information on 3M s acquisitions and divestitures.

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NOTE 3. Goodwill and Intangible Assets

Purchased goodwill from acquisitions totaled $96 million during the first three months of 2015, none of which is deductible for tax purposes. The amounts in the Translation and other column in the following table primarily relate to changes in foreign currency exchange rates. The goodwill balances by business segment as of December 31, 2014 and March 31, 2015, follow:

Goodwill

(Millions)	December 31, 2014 Balance	Acquisition activity	Translation and other	March 31, 2015 Balance
Industrial	$ 2,037	$ 1	$ (66)	$ 1,972
Safety and Graphics	1,650		(46)	1,604
Electronics and Energy	1,559		(35)	1,524
Health Care	1,589	95	(58)	1,626
Consumer	215		(7)	208
Total Company	$ 7,050	$ 96	$ (212)	$ 6,934

Acquired Intangible Assets

For the three months ended March 31, 2015, changes in foreign currency exchange rates decreased the gross carrying amount of intangible assets, with this impact partially offset by gross intangible assets (excluding goodwill) acquired through business combinations. The carrying amount and accumulated amortization of acquired finite-lived intangible assets, in addition to the balance of non-amortizable intangible assets, as of March 31, 2015, and December 31, 2014, follow:

(Millions)	March 31, 2015	December 31, 2014
Customer related intangible assets	$ 1,339	$ 1,348
Patents	561	581
Other technology-based intangible assets	400	407
Definite-lived tradenames	396	401
Other amortizable intangible assets	224	221
Total gross carrying amount	$ 2,920	$ 2,958
Accumulated amortization customer related	(599)	(597)
Accumulated amortization patents	(457)	(472)
Accumulated amortization other technology-based	(218)	(215)
Accumulated amortization definite-lived tradenames	(197)	(195)
Accumulated amortization other	(168)	(167)
Total accumulated amortization	$ (1,639)	$ (1,646)
Total finite-lived intangible assets net	$ 1,281	$ 1,312
Non-amortizable intangible assets (primarily tradenames)	115	123

Total intangible assets net	**$**	**1,396**	$	1,435

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Amortization expense for acquired intangible assets for the three months ended March 31, 2015 and 2014 follows:

	Three months ended March 31,	
(Millions)	**2015**	**2014**
Amortization expense	**$ 53**	$ 57

The table below shows expected amortization expense for acquired amortizable intangible assets recorded as of March 31, 2015:

(Millions)	**Remainder of 2015**	**2016**	**2017**	**2018**	**2019**	**2020**	**After 2020**
Amortization expense	$ 150	$ 177	$ 155	$ 139	$ 127	$ 117	$ 416

The preceding expected amortization expense is an estimate. Actual amounts of amortization expense may differ from estimated amounts due to additional intangible asset acquisitions, changes in foreign currency exchange rates, impairment of intangible assets, accelerated amortization of intangible assets and other events. 3M expenses the costs incurred to renew or extend the term of intangible assets.

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NOTE 4. Supplemental Equity and Comprehensive Income Information

Consolidated Statement of Changes in Equity

Three months ended March 31, 2015

		3M Company Shareholders				
(Millions)	Total	Common Stock and Additional Paid-in Capital	Retained Earnings	Treasury Stock	Accumulated Other Comprehensive Income (Loss)	Non-controlling Interest
Balance at December 31, 2014	$ 13,142	$ 4,388	$ 34,317	$ (19,307)	$ (6,289)	$ 33
Net income	1,201		1,199			2
Other comprehensive income (loss), net of tax:						
Cumulative translation adjustment	(193)				(193)	
Defined benefit pension and post-retirement plans adjustment	91				91	
Debt and equity securities - unrealized gain (loss)						
Cash flow hedging instruments - unrealized gain (loss)	70				70	
Total other comprehensive income (loss), net of tax	(32)					
Dividends declared	(3)		(3)			
Stock-based compensation, net of tax impacts	228	228				
Reacquired stock	(896)			(896)		
Issuances pursuant to stock option and benefit plans	312		(433)	745		
Balance at March 31, 2015	$ 13,952	$ 4,616	$ 35,080	$ (19,458)	$ (6,321)	$ 35

Three months ended March 31, 2014

		3M Company Shareholders				
(Millions)	Total	Common Stock and Additional Paid-in Capital	Retained Earnings	Treasury Stock	Accumulated Other Comprehensive Income (Loss)	Non-controlling Interest
Balance at December 31, 2013	$ 17,948	$ 4,384	$ 32,416	$ (15,385)	$ (3,913)	$ 446
Net income	1,225		1,207			18
Other comprehensive income (loss), net of tax:						
Cumulative translation adjustment	20				8	12
	61				61	

Defined benefit pension and post-retirement plans adjustment						
Debt and equity securities - unrealized gain (loss)	1				1	
Cash flow hedging instruments - unrealized gain (loss)	2				2	
Total other comprehensive income (loss), net of tax	84					
Dividends declared	1		1			
Stock-based compensation, net of tax impacts	170	170				
Reacquired stock	(1,773)			(1,773)		
Issuances pursuant to stock option and benefit plans	269		(312)	581		
Balance at March 31, 2014	$ 17,924	$ 4,554	$ 33,312	$ (16,577)	$ (3,841)	$ 476

In December 2014, 3M s Board of Directors declared a first-quarter 2015 dividend of $1.025 per share (paid in March 2015). In December 2013, 3M s Board of Directors declared a first-quarter 2014 dividend of $0.855 per share (paid in March 2014). This reduced 3M s stockholder equity and increased other current liabilities as of both December 31, 2014 and December 31, 2013, by approximately $0.6 billion.

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Changes in Accumulated Other Comprehensive Income (Loss) Attributable to 3M by Component

Three months ended March 31, 2015

(Millions)	Cumulative Translation Adjustment	Defined Benefit Pension and Postretirement Plans Adjustment	Debt and Equity Securities, Unrealized Gain (Loss)	Cash Flow Hedging Instruments, Unrealized Gain (Loss)	Total Accumulated Other Comprehensive Income (Loss)
Balance at December 31, 2014, net of tax	$ (1,095)	$ (5,293)	$	$ 99	$ (6,289)
Other comprehensive income (loss), before tax:					
Amounts before reclassifications	(44)	24		136	116
Amounts reclassified out		124		(27)	97
Total other comprehensive income (loss), before tax	(44)	148		109	213
Tax effect	(149)	(57)		(39)	(245)
Total other comprehensive income (loss), net of tax	(193)	91		70	(32)
Balance at March 31, 2015, net of tax	$ (1,288)	$ (5,202)	$	$ 169	$ (6,321)

Three months ended March 31, 2014

(Millions)	Cumulative Translation Adjustment	Defined Benefit Pension and Postretirement Plans Adjustment	Debt and Equity Securities, Unrealized Gain (Loss)	Cash Flow Hedging Instruments, Unrealized Gain (Loss)	Total Accumulated Other Comprehensive Income (Loss)
Balance at December 31, 2013, net of tax	$ (188)	$ (3,715)	$ (2)	$ (8)	$ (3,913)
Other comprehensive income (loss), before tax:					
Amounts before reclassifications	5		2	9	16
Amounts reclassified out		91		(6)	85
Total other comprehensive income (loss), before tax	5	91	2	3	101
Tax effect	3	(30)	(1)	(1)	(29)
Total other comprehensive income (loss), net of tax	8	61	1	2	72
Balance at March 31, 2014, net of tax	$ (180)	$ (3,654)	$ (1)	$ (6)	$ (3,841)

Income taxes are not provided for foreign translation relating to permanent investments in international subsidiaries, but tax effects within cumulative translation does include impacts from items such as net investment hedge transactions. Reclassification adjustments are made to avoid double counting in comprehensive income items that are also recorded as part of net income.

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Reclassifications out of Accumulated Other Comprehensive Income Attributable to 3M

(Millions) Details about Accumulated Other Comprehensive Income Components	Amount Reclassified from Accumulated Other Comprehensive Income Three months ended March 31, 2015	 Three months ended March 31, 2014	Location on Income Statement
Gains (losses) associated with, defined benefit pension and postretirement plans amortization			
Transition asset	**$**	$	See Note 7
Prior service benefit	**18**	15	See Note 7
Net actuarial loss	**(159)**	(106)	See Note 7
Curtailments/Settlements	**17**		See Note 7
Total before tax	**(124)**	(91)	
Tax effect	**46**	30	Provision for income taxes
Net of tax	**$ (78)**	$ (61)	
Debt and equity security gains (losses)			
Sales or impairments of securities	**$**	$	Selling, general and administrative expenses
Total before tax			
Tax effect			Provision for income taxes
Net of tax	**$**	$	
Cash flow hedging instruments gains (losses)			
Foreign currency forward/option contracts	**$ 30**	$ 4	Cost of sales
Commodity price swap contracts	**(2)**	2	Cost of sales
Interest rate swap contracts	**(1)**		Interest expense
Total before tax	**27**	6	
Tax effect	**(10)**	(2)	Provision for income taxes
Net of tax	**$ 17**	$ 4	
Total reclassifications for the period, net of tax	**$ (61)**	$ (57)	

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NOTE 5. Income Taxes

The Company files income tax returns in the U.S. federal jurisdiction, and various states and foreign jurisdictions. With few exceptions, the Company is no longer subject to U.S. federal, state and local, or non-U.S. income tax examinations by tax authorities for years before 2005.

The IRS has completed its field examination of the Company s U.S. federal income tax returns for the years 2005 through 2013. The Company protested certain IRS positions within these tax years and entered into the administrative appeals process with the IRS. In December 2012, the Company received a statutory notice of deficiency for the 2006 year. The Company filed a petition in Tax Court in the first quarter of 2013 relating to the 2006 tax year.

Currently, the Company is under examination by the IRS for its U.S. federal income tax returns for the years 2014 and 2015. It is anticipated that the IRS will complete its examination of the Company for 2014 by the end of the first quarter of 2016 and for 2015 by the end of the first quarter of 2017. As of March 31, 2015, the IRS has not proposed any significant adjustments to the Company s tax positions for which the Company is not adequately reserved.

Payments relating to other proposed assessments arising from the 2005 through 2015 examinations may not be made until a final agreement is reached between the Company and the IRS on such assessments or upon a final resolution resulting from the administrative appeals process or judicial action. In addition to the U.S. federal examination, there is also audit activity in several U.S. state and foreign jurisdictions.

3M anticipates changes to the Company s uncertain tax positions due to the closing of various audit years mentioned above and closure of statutes. Currently, the Company is not estimating a significant increase or decrease in unrecognized tax benefits as of March 31, 2015, during the next 12 months. The total amounts of unrecognized tax benefits that, if recognized, would affect the effective tax rate as of March 31, 2015 and December 31, 2014 are $268 million and $265 million, respectively.

The Company recognizes interest and penalties accrued related to unrecognized tax benefits in tax expense. The Company recognized in the consolidated statement of income on a gross basis approximately $2 million of expense and $15 million of benefit for the three months ended March 31, 2015 and March 31, 2014, respectively. At March 31, 2015, and December 31, 2014, accrued interest and penalties in the consolidated balance sheet on a gross basis were $46 million and $44 million, respectively. Included in these interest and penalty amounts are interest and penalties related to tax positions for which the ultimate deductibility is highly certain but for which there is uncertainty about the timing of such deductibility. Because of the impact of deferred tax accounting, other than interest and penalties, the disallowance of the shorter deductibility period would not affect the annual effective tax rate but would accelerate the payment of cash to the taxing authority to an earlier period.

The effective tax rate for the first quarter of 2015 was 29.5 percent, compared to 27.4 percent in the first quarter of 2014, an increase of 2.1 percentage points. Primary factors that increased the Company s effective tax rate on a combined basis by 2.1 percentage points year-on-year included the 2014 restoration of tax basis on certain assets for which depreciation deductions were previously limited, adjustments to 3M s income tax reserves for the first quarter of 2015 when compared to the same period in 2014, and international taxes, including changes in foreign currency rates and changes to the geographic mix of income before taxes.

The provision for income taxes is determined using the asset and liability approach. Under this approach, deferred income taxes represent the expected future tax consequences of temporary differences between the carrying amounts and tax basis of assets and liabilities. The Company records a valuation allowance to reduce its deferred tax assets when uncertainty regarding their realizability exits. As of both March 31, 2015 and December 31, 2014, the Company had valuation allowances of $22 million on its deferred tax assets.

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NOTE 6. Marketable Securities

The Company invests in agency securities, corporate securities, asset-backed securities, treasury securities and other securities. The following is a summary of amounts recorded on the Consolidated Balance Sheet for marketable securities (current and non-current).

(Millions)	March 31, 2015	December 31, 2014
U.S. government agency securities	**$ 67**	$ 67
Foreign government agency securities	**60**	75
Corporate debt securities	**551**	241
Commercial paper	**27**	
Certificates of deposit/time deposits	**24**	41
U.S. municipal securities	**3**	
Asset-backed securities:		
Automobile loan related	**167**	122
Credit card related	**66**	59
Equipment lease related	**7**	21
Other	**46**	
Asset-backed securities total	**286**	202
Current marketable securities	**$ 1,018**	$ 626
U.S. government agency securities	**$ 1**	$ 41
Foreign government agency securities		20
Corporate debt securities		378
U.S. treasury securities		38
U.S. municipal securities	**12**	15
Asset-backed securities:		
Automobile loan related		160
Credit card related		103
Equipment lease related		27
Other		46
Asset-backed securities total		336
Non-current marketable securities	**$ 13**	$ 828
Total marketable securities	**$ 1,031**	$ 1,454

Classification of marketable securities as current or non-current is dependent upon management s intended holding period, the security s maturity date and liquidity considerations based on market conditions. If management intends to hold the securities for longer than one year as of the balance sheet date, they are classified as non-current. The classification as of March 31, 2015, was impacted by the February 2015 announcement that 3M has entered into a definitive agreement with Polypore International Inc. to acquire Polypore s Separations Media business (discussed in Note 2).

At March 31, 2015, gross unrealized losses were immaterial, while gross unrealized gains totaled approximately $1 million (pre-tax). At December 31, 2014, gross unrealized losses totaled approximately $1 million (pre-tax), while gross unrealized gains totaled approximately $1 million (pre-tax). Refer to Note 4 for a table that provides the net realized gains (losses) related to sales or impairments of debt and equity securities, which includes marketable securities. The gross amounts of the realized gains or losses were not material. Cost of securities sold use the first in, first out (FIFO) method. Since these marketable securities are classified as available-for-sale securities, changes in fair value will flow through other comprehensive income, with amounts reclassified out of other comprehensive income into earnings upon sale or other-than-temporary impairment.

3M reviews impairments associated with its marketable securities in accordance with the measurement guidance provided by ASC 320, *Investments-Debt and Equity Securities*, when determining the classification of the impairment as temporary or other-than-temporary . A temporary impairment charge results in an unrealized loss being recorded in the other comprehensive income component of shareholders equity. Such an unrealized loss does not reduce net income

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attributable to 3M for the applicable accounting period because the loss is not viewed as other-than-temporary. The factors evaluated to differentiate between temporary and other-than-temporary include the projected future cash flows, credit ratings actions, and assessment of the credit quality of the underlying collateral, as well as other factors.

The balances at March 31, 2015 for marketable securities by contractual maturity are shown below. Actual maturities may differ from contractual maturities because the issuers of the securities may have the right to prepay obligations without prepayment penalties.

(Millions)		**March 31, 2015**
Due in one year or less	$	357
Due after one year through five years		654
Due after five years through ten years		5
Due after ten years		15
Total marketable securities	$	1,031

3M has a diversified marketable securities portfolio of $1.031 billion as of March 31, 2015. Within this portfolio, current and long-term asset-backed securities (estimated fair value of $286 million) primarily include interests in automobile loans, credit cards and equipment leases. 3M s investment policy allows investments in asset-backed securities with minimum credit ratings of Aa2 by Moody s Investors Service or AA by Standard & Poor s or Fitch Ratings or DBRS. Asset-backed securities must be rated by at least two of the aforementioned rating agencies, one of which must be Moody s Investors Service or Standard & Poor s. At March 31, 2015, all asset-backed security investments were in compliance with this policy. Approximately 92.2 percent of all asset-backed security investments were rated AAA or A-1+ by Standard & Poor s and/or Aaa or P-1 by Moody s Investors Service and/or AAA or F1+ by Fitch Ratings. Interest rate risk and credit risk related to the underlying collateral may impact the value of investments in asset-backed securities, while factors such as general conditions in the overall credit market and the nature of the underlying collateral may affect the liquidity of investments in asset-backed securities. 3M does not currently expect risk related to its holding in asset-backed securities to materially impact its financial condition or liquidity.

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NOTE 7. Pension and Postretirement Benefit Plans

Net periodic benefit cost is recorded in cost of sales, selling, general and administrative expenses, and research, development and related expenses. Components of net periodic benefit cost and other supplemental information for the three months ended March 31, 2015 and 2014 follow:

Benefit Plan Information

	Three months ended March 31,					
	Qualified and Non-qualified Pension Benefits				Postretirement Benefits	
	United States		International			
(Millions)	2015	2014	2015	2014	2015	2014
Net periodic benefit cost (benefit)						
Service cost	**$ 73**	$ 60	**$ 42**	$ 36	**$ 21**	$ 16
Interest cost	**164**	169	**55**	64	**25**	24
Expected return on plan assets	**(267)**	(261)	**(81)**	(79)	**(22)**	(22)
Amortization of transition (asset) obligation						
Amortization of prior service cost (benefit)	**(6)**	1	**(4)**	(4)	**(8)**	(12)
Amortization of net actuarial (gain) loss	**102**	61	**38**	31	**19**	14
Net periodic benefit cost (benefit)	**$ 66**	$ 30	**$ 50**	$ 48	**$ 35**	$ 20
Settlements, curtailments, special termination benefits and other			**(17)**			
Net periodic benefit cost (benefit) after settlements, curtailments, special termination benefits and other	**$ 66**	$ 30	**$ 33**	$ 48	**$ 35**	$ 20

For the three months ended March 31, 2015, contributions totaling $90 million were made to the Company s U.S. and international pension plans and $1 million to its postretirement plans. For total year 2015, the Company expects to contribute approximately $200 million of cash to its global defined benefit pension and postretirement plans. The Company does not have a required minimum cash pension contribution obligation for its U.S. plans in 2015. Future contributions will depend on market conditions, interest rates and other factors. 3M s annual measurement date for pension and postretirement assets and liabilities is December 31 each year, which is also the date used for the related annual measurement assumptions.

3M was informed during the first quarter of 2009, that the general partners of WG Trading Company, in which 3M s benefit plans hold limited partnership interests, are the subject of a criminal investigation as well as civil proceedings by the SEC and CFTC (Commodity Futures Trading Commission). In March 2011, over the objections of 3M and six other limited partners of WG Trading Company, the district court judge ruled in favor of the court appointed receiver s proposed distribution plan (and in April 2013, the United States Court of Appeals for the Second Circuit affirmed the district court s ruling). The benefit plan trustee holdings of WG Trading Company interests were adjusted to reflect the decreased estimated fair market value, inclusive of estimated insurance proceeds, as of the annual measurement dates. The Company has insurance that it believes, based on what is currently known, will result in the probable recovery of a portion of the decrease in original asset value. In the first quarter of 2014, 3M and certain 3M benefit plans filed a lawsuit in the U.S. District Court for the District of Minnesota against five insurers seeking insurance coverage for the WG Trading Company claim. As of the 2014 measurement date, these holdings represented less than one half of one percent of 3M s fair value of total plan assets for the 3M pension plan. 3M currently believes that the resolution of these events will not have a material adverse effect on the consolidated financial position of the Company.

In March 2015, 3M Japan modified the Japan Limited Defined Benefit Corporate Pension Plan (DBCPP). Beginning July 1, 2015, eligible employees will receive a company provided contribution match of 6.12% of their eligible salary to their defined contribution plan. Employees will no longer earn additional service towards their defined benefit pension plans after July 1, 2015, except for eligible salaries above the statutory defined contribution limits. As a result of this plan modification, the Company re-measured the DBCPP, which resulted in a $17 million pre-tax curtailment gain for the period ended March 31, 2015.

In addition, the Company also sponsors employee savings plans under Section 401(k) of the Internal Revenue Code, as discussed in Note 10 in 3M s 2014 Annual Report on Form 10-K.

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NOTE 8. Derivatives

The Company uses interest rate swaps, currency swaps, commodity price swaps, and forward and option contracts to manage risks generally associated with foreign exchange rate, interest rate and commodity price fluctuations. The information that follows explains the various types of derivatives and financial instruments used by 3M, how and why 3M uses such instruments, how such instruments are accounted for, and how such instruments impact 3M s financial position and performance.

Additional information with respect to the impacts on other comprehensive income of nonderivative hedging and derivative instruments is included in Note 4. Additional information with respect to the fair value of derivative instruments is included in Note 9. References to information regarding derivatives and/or hedging instruments associated with the Company s long-term debt are also made in Note 9 in 3M s 2014 Annual Report on Form 10-K.

Types of Derivatives/Hedging Instruments and Inclusion in Income/Other Comprehensive Income

Cash Flow Hedges:

For derivative instruments that are designated and qualify as cash flow hedges, the effective portion of the gain or loss on the derivative is reported as a component of other comprehensive income and reclassified into earnings in the same period during which the hedged transaction affects earnings. Gains and losses on the derivative representing either hedge ineffectiveness or hedge components excluded from the assessment of effectiveness are recognized in current earnings.

Cash Flow Hedging - Foreign Currency Forward and Option Contracts: The Company enters into foreign exchange forward and option contracts to hedge against the effect of exchange rate fluctuations on cash flows denominated in foreign currencies. These transactions are designated as cash flow hedges. The settlement or extension of these derivatives will result in reclassifications (from accumulated other comprehensive income) to earnings in the period during which the hedged transactions affect earnings. 3M may dedesignate these cash flow hedge relationships in advance of the occurrence of the forecasted transaction. The portion of gains or losses on the derivative instrument previously accumulated in other comprehensive income for dedesignated hedges remains in accumulated other comprehensive income until the forecasted transaction occurs. Changes in the value of derivative instruments after dedesignation are recorded in earnings and are included in the Derivatives Not Designated as Hedging Instruments section below. Hedge ineffectiveness and the amount excluded from effectiveness testing recognized in income on cash flow hedges were not material for the three months ended March 31, 2015 and 2014. Beginning in the second quarter of 2014 3M began extending the maximum length of time over which it hedges its exposure to the variability in future cash flows of the forecasted transactions from a previous term of 12 months to a longer term of 24 months, with certain currencies being extended further to 36 months starting in the first quarter of 2015. The dollar equivalent gross notional amount of the Company s foreign exchange forward and option contracts designated as cash flow hedges at March 31, 2015 was approximately $2.8 billion.

Cash Flow Hedging - Commodity Price Management: The Company manages commodity price risks through negotiated supply contracts, price protection agreements and forward contracts. 3M discontinued the use of commodity price swaps as cash flow hedges of forecasted commodity transactions in the first quarter of 2015. The Company used commodity price swaps as cash flow hedges of forecasted commodity transactions to manage price volatility. The related mark-to-market gain or loss on qualifying hedges was included in other comprehensive income to the extent effective, and reclassified into cost of sales in the period during which the hedged transaction affected earnings.

Cash Flow Hedging Interest Rate Contracts: In August 2011, in anticipation of the September 2011 issuance of $1 billion in five-year fixed rate notes, 3M executed a pre-issuance cash flow hedge on a notional amount of $400 million by entering into a forward-starting five-year floating-to-fixed interest rate swap. Upon debt issuance in September 2011, 3M terminated the floating-to-fixed interest rate swap. The termination of the swap resulted in a $7 million pre-tax loss ($4 million after-tax) that will be amortized over the five-year life of the note.

In the third and fourth quarters of 2014, the Company entered into forward starting interest rate swaps with notional amounts totaling 500 million Euros as a hedge against interest rate volatility associated with the forecasted issuance of fixed rate debt. Upon issuance in November 2014 of 750 million Euros aggregate principal amount of twelve-year fixed rate notes, 3M terminated these interest rate swaps. The termination resulted in a $8 million pre-tax ($5 million after-tax) loss within accumulated other comprehensive income that will be amortized over the twelve-year life of the notes.

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The amortization of losses referenced in the two preceding paragraphs is included in the tables below as part of the loss recognized in income on the effective portion of derivatives as a result of reclassification from accumulated other comprehensive income.

As of March 31, 2015, the Company had a balance of $169 million (as shown in Note 4) associated with the after-tax net unrealized gain associated with cash flow hedging instruments recorded in accumulated other comprehensive income. This includes a remaining balance of $6 million (loss) related to the forward starting interest rate swaps (discussed in the preceding paragraphs), which will be amortized over the respective lives of the notes. Based on exchange rates as of March 31, 2015, 3M expects to reclassify approximately $116 million of the after-tax net unrealized foreign exchange cash flow hedging gains to earnings over the next 12 months, of which 3M expects to reclassify approximately $91 million over the remainder of 2015. 3M expects to reclassify approximately $70 million of the after-tax net unrealized foreign exchange cash flow hedging gains to earnings in 2016. This impact will be offset by cash flows from underlying hedged items.

The location in the consolidated statements of income and comprehensive income and amounts of gains and losses related to derivative instruments designated as cash flow hedges are provided in the following table. Reclassifications of amounts from accumulated other comprehensive income into income include accumulated gains (losses) on dedesignated hedges at the time earnings are impacted by the forecasted transaction.

Three months ended March 31, 2015

(Millions)	Pretax Gain (Loss) Recognized in Other Comprehensive Income on Effective Portion of Derivative		Pretax Gain (Loss) Recognized in Income on Effective Portion of Derivative as a Result of Reclassification from Accumulated Other Comprehensive Income			Ineffective Portion of Gain (Loss) on Derivative and Amount Excluded from Effectiveness Testing Recognized in Income		
Derivatives in Cash Flow Hedging Relationships	**Amount**		**Location**	**Amount**		**Location**	**Amount**	
Foreign currency forward/option contracts	$	136	Cost of sales	$	30	Cost of sales	$	—
Commodity price swap contracts		—	Cost of sales		(2)	Cost of sales		—
Interest rate swap contracts		—	Interest expense		(1)	Interest expense		—
Total	$	136		$	27		$	—

Three months ended March 31, 2014

(Millions)	Pretax Gain (Loss) Recognized in Other Comprehensive Income on Effective Portion of Derivative		Pretax Gain (Loss) Recognized in Income on Effective Portion of Derivative as a Result of Reclassification from Accumulated Other Comprehensive Income			Ineffective Portion of Gain (Loss) on Derivative and Amount Excluded from Effectiveness Testing Recognized in Income		
Derivatives in Cash Flow Hedging Relationships	**Amount**		**Location**	**Amount**		**Location**	**Amount**	
Foreign currency forward/option contracts	$	7	Cost of sales	$	4	Cost of sales	$	—
Commodity price swap contracts		2	Cost of sales		2	Cost of sales		—
Total	$	9		$	6		$	—

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Fair Value Hedges:

For derivative instruments that are designated and qualify as fair value hedges, the gain or loss on the derivatives as well as the offsetting loss or gain on the hedged item attributable to the hedged risk are recognized in current earnings.

Fair Value Hedging - Interest Rate Swaps: The Company manages interest expense using a mix of fixed and floating rate debt. To help manage borrowing costs, the Company may enter into interest rate swaps. Under these arrangements, the Company agrees to exchange, at specified intervals, the difference between fixed and floating interest amounts calculated by reference to an agreed-upon notional principal amount. The mark-to-market of these fair value hedges is recorded as gains or losses in interest expense and is offset by the gain or loss of the underlying debt instrument, which also is recorded in interest expense. These fair value hedges are highly effective and, thus, there is no impact on earnings due to hedge ineffectiveness. The dollar equivalent (based on inception date foreign currency exchange rates) gross notional amount of the Company s interest rate swaps at March 31, 2015 was $1 billion.

At March 31, 2015, the Company had interest rate swaps designated as fair value hedges of underlying fixed rate obligations. In July 2007, in connection with the issuance of a seven-year Eurobond for an amount of 750 million Euros, the Company completed a fixed-to-floating interest rate swap on a notional amount of 400 million Euros as a fair value hedge of a portion of the fixed interest rate Eurobond obligation. In August 2010, the Company terminated 150 million Euros of the notional amount of this swap. As a result, a gain of 18 million Euros, recorded as part of the balance of the underlying debt, was amortized as an offset to interest expense over this debt s remaining life. Prior to termination of the applicable portion of the interest rate swap, the mark-to-market of the hedge instrument was recorded as gains or losses in interest expense and was offset by the gain or loss on carrying value of the underlying debt instrument. Consequently, the subsequent amortization of the 18 million Euros recorded as part of the underlying debt balance was not part of gains on hedged items recognized in income in the tables below. The remaining interest rate swap of 250 million Euros (notional amount) matured in July 2014.

In November 2013, 3M issued an eight-year 1.875% fixed rate Eurobond for a face amount of 600 million Euros. Upon debt issuance, 3M completed a fixed-to-floating interest rate swap on a notional amount of 300 million Euros as a fair value hedge of a portion of the fixed interest rate Eurobond obligation.

In June 2014, 3M issued a five-year 1.625% fixed rate medium-term note for a face amount of $625 million. Upon debt issuance, 3M completed a fixed-to-floating interest rate swap on a notional amount of $600 million as a fair value hedge of a portion of the fixed interest rate medium-term note obligation.

The location in the consolidated statements of income and amounts of gains and losses related to derivative instruments designated as fair value hedges and similar information relative to the hedged items are as follows:

Three months ended March 31, 2015

	Gain (Loss) on Derivative	Gain (Loss) on Hedged Item

(Millions) Derivatives in Fair Value Hedging Relationships	Recognized in Income Location	 Amount	Recognized in Income Location	 Amount
Interest rate swap contracts	Interest expense	$ 6	Interest expense	$ (6)
Total		$ 6		$ (6)

Three months ended March 31, 2014

(Millions) Derivatives in Fair Value Hedging Relationships	Gain (Loss) on Derivative Recognized in Income Location	 Amount	Gain (Loss) on Hedged Item Recognized in Income Location	 Amount
Interest rate swap contracts	Interest expense	$ 7	Interest expense	$ (7)
Total		$ 7		$ (7)

Net Investment Hedges:

The Company may use non-derivative (foreign currency denominated debt) and derivative (foreign exchange forward contracts) instruments to hedge portions of the Company s investment in foreign subsidiaries and manage foreign exchange risk. The extent of 3M s use of forward contracts may depend on the volume of foreign currency denominated debt already designated in net investment hedges. For instruments that are designated and qualify as hedges of net investments in foreign operations and that meet the effectiveness requirements, the net gains or losses attributable to changes in spot exchange rates are recorded in cumulative translation within other comprehensive income. The remainder of the change in value of such instruments is recorded in earnings. Recognition in earnings of amounts previously recorded in cumulative translation is limited to circumstances such as complete or substantially complete liquidation of the net investment in the hedged foreign operation. To the extent foreign currency denominated debt is not

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designated in or is dedesignated from a net investment hedge relationship, changes in value of that portion of foreign currency denominated debt due to exchange rate changes are recorded in earnings through their maturity date.

3M s use of foreign exchange forward contracts designated in hedges of the Company s net investment in European subsidiaries can vary by time period depending on when foreign currency denominated debt balances designated in such relationships are dedesignated, matured, or are newly issued and designated. Additionally, variation can occur in connection with the extent of the Company s desired exchange risk coverage.

3M also began using foreign exchange forward contracts designated in hedges of the Company s net investment in Korean subsidiaries during the first quarter of 2015.

At March 31, 2015, the total notional amount of foreign exchange forward contracts designated in net investment hedges was 2.45 billion Euros and approximately 275 billion South Korean Won along with a principal amount of long-term debt instruments designated in net investment hedges totaling 1.85 billion Euros (as discussed in Note 9 in 3M s 2014 Annual Report on Form 10-K, specifically items C, D1, D2, and H). The maturity dates of these derivative and nonderivative instruments designated in net investment hedges range from 2015 to 2026.

The Company revised amounts previously presented in the tables below for the pretax gain (loss) recognized as cumulative translation within other comprehensive income on effective portion of instrument (Gain Recognized as CTA) for three months March 31, 2014 relative to foreign currency denominated debt and in total. These immaterial corrections increased the previously presented amounts of the Gain recognized as CTA in the disclosure tables below by $18 million for three months March 31, 2014. The revisions had no impact on the Company s consolidated results of operations, financial condition, or cash flows.

The location in the consolidated statements of income and comprehensive income and amounts of gains and losses related to derivative and nonderivative instruments designated as net investment hedges are as follows. There were no reclassifications of the effective portion of net investment hedges out of accumulated other comprehensive income into income for the periods presented in the table below.

Three months ended March 31, 2015

Derivative and Nonderivative Instruments in Net Investment Hedging Relationships (Millions)	**Pretax Gain (Loss) Recognized as Cumulative Translation within Other Comprehensive Income on Effective Portion of Instrument**		**Ineffective Portion of Gain (Loss) on Instrument and Amount Excluded from Effectiveness Testing Recognized in Income**		
		Amount	**Location**		**Amount**
Foreign currency denominated debt	$	240	N/A	$	
Foreign currency forward contracts		157	Cost of Sales		
Total	$	397		$	

Three months ended March 31, 2014

Derivative and Nonderivative Instruments in Net Investment Hedging Relationships (Millions)	Pretax Gain (Loss) Recognized as Cumulative Translation within Other Comprehensive Income on Effective Portion of Instrument		Ineffective Portion of Gain (Loss) on Instrument and Amount Excluded from Effectiveness Testing Recognized in Income	
	Amount		Location	Amount
Foreign currency denominated debt	$	9	N/A	$
Total	$	9		$

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Derivatives Not Designated as Hedging Instruments:

Derivatives not designated as hedging instruments include dedesignated foreign currency forward and option contracts that formerly were designated in cash flow hedging relationships (as referenced in the Cash Flow Hedges section above). In addition, 3M enters into foreign currency forward contracts to offset, in part, the impacts of certain intercompany activities (primarily associated with intercompany licensing arrangements) and enters into commodity price swaps to offset, in part, fluctuations in costs associated with the use of certain commodities and precious metals. These derivative instruments are not designated in hedging relationships; therefore, fair value gains and losses on these contracts are recorded in earnings. The dollar equivalent gross notional amount of these forward, option and swap contracts not designated as hedging instruments totaled $7.1 billion as of March 31, 2015. The Company does not hold or issue derivative financial instruments for trading purposes.

The location in the consolidated statements of income and amounts of gains and losses related to derivative instruments not designated as hedging instruments are as follows:

	Three months ended March 31, 2015		
Derivatives Not Designated as Hedging Instruments	**Gain (Loss) on Derivative Recognized in Income**		
(Millions)	**Location**		**Amount**
Foreign currency forward/option contracts	Cost of sales	$	4
Foreign currency forward contracts	Interest expense		89
Commodity price swap contracts	Cost of sales		(4)
Total		$	89

	Three months ended March 31, 2014		
Derivatives Not Designated as Hedging Instruments	**Gain (Loss) on Derivative Recognized in Income**		
(Millions)	**Location**		**Amount**
Foreign currency forward/option contracts	Cost of sales	$	(1)
Foreign currency forward contracts	Interest expense		33
Total		$	32

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Location and Fair Value Amount of Derivative Instruments

The following tables summarize the fair value of 3M s derivative instruments, excluding nonderivative instruments used as hedging instruments, and their location in the consolidated balance sheet. Additional information with respect to the fair value of derivative instruments is included in Note 9.

March 31, 2015

(Millions)	**Assets**			**Liabilities**		
Fair Value of Derivative Instruments	**Location**		**Amount**	**Location**		**Amount**
Derivatives designated as hedging instruments						
Foreign currency forward/option contracts	Other current assets	$	310	Other current liabilities	$	6
Foreign currency forward/option contracts	Other assets		100	Other liabilities		
Interest rate swap contracts	Other assets		31	Other liabilities		
Total derivatives designated as hedging instruments		$	441		$	6
Derivatives not designated as hedging instruments						
Foreign currency forward/option contracts	Other current assets	$	118	Other current liabilities	$	62
Foreign currency forward/option contracts	Other assets		1	Other liabilities		1
Commodity price swap contracts	Other current assets		1	Other current liabilities		4
Total derivatives not designated as hedging instruments		$	120		$	67
Total derivative instruments		$	561		$	73

December 31, 2014

(Millions)	**Assets**			**Liabilities**		
Fair Value of Derivative Instruments	**Location**		**Amount**	**Location**		**Amount**
Derivatives designated as hedging instruments						
Foreign currency forward/option contracts	Other current assets	$	116	Other current liabilities	$	2
Foreign currency forward/option contracts	Other assets		47	Other liabilities		1
Commodity price swap contracts	Other current assets			Other current liabilities		4
Interest rate swap contracts	Other assets		27	Other liabilities		3
Total derivatives designated as hedging instruments		$	190		$	10

Derivatives not designated as hedging instruments						
Foreign currency forward/option contracts	Other current assets	$	66	Other current liabilities	$	33
Total derivatives not designated as hedging instruments		$	66		$	33
Total derivative instruments		$	256		$	43

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Credit Risk and Offsetting of Assets and Liabilities of Derivative Instruments

The Company is exposed to credit loss in the event of nonperformance by counterparties in interest rate swaps, currency swaps, commodity price swaps, and forward and option contracts. However, the Company s risk is limited to the fair value of the instruments. The Company actively monitors its exposure to credit risk through the use of credit approvals and credit limits, and by selecting major international banks and financial institutions as counterparties. 3M enters into master netting arrangements with counterparties when possible to mitigate credit risk in derivative transactions. A master netting arrangement may allow each counterparty to net settle amounts owed between a 3M entity and the counterparty as a result of multiple, separate derivative transactions. As of March 31, 2015, 3M has International Swaps and Derivatives Association (ISDA) agreements with 16 applicable banks and financial institutions which contain netting provisions. In addition to a master agreement with 3M supported by a primary counterparty s parent guarantee, 3M also has associated credit support agreements in place with 15 of its primary derivative counterparties which, among other things, provide the circumstances under which either party is required to post eligible collateral (when the market value of transactions covered by these agreements exceeds specified thresholds or if a counterparty s credit rating has been downgraded to a predetermined rating). The Company does not anticipate nonperformance by any of these counterparties.

3M has elected to present the fair value of derivative assets and liabilities within the Company s consolidated balance sheet on a gross basis even when derivative transactions are subject to master netting arrangements and may otherwise qualify for net presentation. However, the following tables provide information as if the Company had elected to offset the asset and liability balances of derivative instruments, netted in accordance with various criteria in the event of default or termination as stipulated by the terms of netting arrangements with each of the counterparties. For each counterparty, if netted, the Company would offset the asset and liability balances of all derivatives at the end of the reporting period based on the 3M entity that is a party to the transactions. Derivatives not subject to master netting agreements are not eligible for net presentation. As of the applicable dates presented below, no collateral had been received or pledged related to these derivative instruments.

Offsetting of Financial Assets/Liabilities under Master Netting Agreements with Derivative Counterparties

March 31, 2015

		Gross Amounts not Offset in the Consolidated Balance Sheet that are Subject to Master Netting Agreements		
(Millions)	**Gross Amount of Derivative Assets Presented in the Consolidated Balance Sheet**	**Gross Amount of Eligible Offsetting Recognized Derivative Liabilities**	**Cash Collateral Received**	**Net Amount of Derivative Assets**
Derivatives subject to master netting agreements	$ 561	$ 38	$	$ 523
Derivatives not subject to master netting agreements				
Total	$ 561			$ 523

March 31, 2015

(Millions)	Gross Amount of Derivative Liabilities Presented in the Consolidated Balance Sheet	Gross Amounts not Offset in the Consolidated Balance Sheet that are Subject to Master Netting Agreements: Gross Amount of Eligible Offsetting Recognized Derivative Assets	Cash Collateral Pledged	Net Amount of Derivative Liabilities
Derivatives subject to master netting agreements	$ 68	$ 38	$	$ 30
Derivatives not subject to master netting agreements	5			5
Total	$ 73			$ 35

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December 31, 2014

(Millions)	Gross Amount of Derivative Assets Presented in the Consolidated Balance Sheet	Gross Amounts not Offset in the Consolidated Balance Sheet that are Subject to Master Netting Agreements: Gross Amount of Eligible Offsetting Recognized Derivative Liabilities	Gross Amounts not Offset in the Consolidated Balance Sheet that are Subject to Master Netting Agreements: Cash Collateral Received	Net Amount of Derivative Assets
Derivatives subject to master netting agreements	$ 256	$ 20	$	$ 236
Derivatives not subject to master netting agreements				
Total	$ 256			$ 236

December 31, 2014

(Millions)	Gross Amount of Derivative Liabilities Presented in the Consolidated Balance Sheet	Gross Amounts not Offset in the Consolidated Balance Sheet that are Subject to Master Netting Agreements: Gross Amount of Eligible Offsetting Recognized Derivative Assets	Gross Amounts not Offset in the Consolidated Balance Sheet that are Subject to Master Netting Agreements: Cash Collateral Pledged	Net Amount of Derivative Liabilities
Derivatives subject to master netting agreements	$ 36	$ 20	$	$ 16
Derivatives not subject to master netting agreements	7			7
Total	$ 43			$ 23

Currency Effects

3M estimates that year-on-year currency effects, including hedging impacts, decreased pre-tax income by approximately $90 million for the three months ended March 31, 2015. This estimate includes the effect of translating profits from local currencies into U.S. dollars; the impact of currency fluctuations on the transfer of goods between 3M operations in the United States and abroad; and transaction gains and losses, including derivative instruments designed to reduce foreign currency exchange rate risks. 3M estimates that year-on-year derivative and other transaction gains and losses increased pre-tax income by approximately $40 million for the three months ended March 31, 2015.

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NOTE 9. Fair Value Measurements

3M follows ASC 820, *Fair Value Measurements and Disclosures*, with respect to assets and liabilities that are measured at fair value on a recurring basis and nonrecurring basis. Under the standard, fair value is defined as the exit price, or the amount that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants as of the measurement date. The standard also establishes a hierarchy for inputs used in measuring fair value that maximizes the use of observable inputs and minimizes the use of unobservable inputs by requiring that the most observable inputs be used when available. Observable inputs are inputs market participants would use in valuing the asset or liability developed based on market data obtained from sources independent of the Company. Unobservable inputs are inputs that reflect the Company s assumptions about the factors market participants would use in valuing the asset or liability developed based upon the best information available in the circumstances. The hierarchy is broken down into three levels. Level 1 inputs are quoted prices (unadjusted) in active markets for identical assets or liabilities. Level 2 inputs include quoted prices for similar assets or liabilities in active markets, quoted prices for identical or similar assets or liabilities in markets that are not active, and inputs (other than quoted prices) that are observable for the asset or liability, either directly or indirectly. Level 3 inputs are unobservable inputs for the asset or liability. Categorization within the valuation hierarchy is based upon the lowest level of input that is significant to the fair value measurement.

Assets and Liabilities that are Measured at Fair Value on a Recurring Basis:

For 3M, assets and liabilities that are measured at fair value on a recurring basis primarily relate to available-for-sale marketable securities, available-for-sale investments (included as part of investments in the Consolidated Balance Sheet) and certain derivative instruments. Derivatives include cash flow hedges, interest rate swaps and most net investment hedges. The information in the following paragraphs and tables primarily addresses matters relative to these financial assets and liabilities. Separately, there were no material fair value measurements with respect to nonfinancial assets or liabilities that are recognized or disclosed at fair value in the Company s financial statements on a recurring basis for the three month periods ended March 31, 2015 and 2014.

3M uses various valuation techniques, which are primarily based upon the market and income approaches, with respect to financial assets and liabilities. Following is a description of the valuation methodologies used for the respective financial assets and liabilities measured at fair value.

Available-for-sale marketable securities except certain U.S. municipal securities:

Marketable securities, except certain U.S. municipal securities, are valued utilizing multiple sources. A weighted average price is used for these securities. Market prices are obtained for these securities from a variety of industry standard data providers, security master files from large financial institutions, and other third-party sources. These multiple prices are used as inputs into a distribution-curve-based algorithm to determine the daily fair value to be used. 3M classifies U.S. treasury securities as level 1, while all other marketable securities (excluding certain U.S. municipal securities) are classified as level 2. Marketable securities are discussed further in Note 6.

Available-for-sale marketable securities certain U.S. municipal securities only:

In the fourth quarter 2014, 3M obtained a municipal bond with the City of Nevada, Missouri, which represent 3M s only U.S. municipal securities holding as of March 31, 2015 and December 31, 2014. Due to the nature of this security, the valuation method utilized will include the financial health of the City of Nevada, any recent municipal bond issuances by Nevada, and macroeconomic considerations related to the direction of interest rates and the health of the overall municipal bond market, and as such will be classified as a level 3 security.

Available-for-sale investments:

Investments include equity securities that are traded in an active market. Closing stock prices are readily available from active markets and are used as being representative of fair value. 3M classifies these securities as level 1.

Derivative instruments:

The Company s derivative assets and liabilities within the scope of ASC 815, *Derivatives and Hedging*, are required to be recorded at fair value. The Company s derivatives that are recorded at fair value include foreign currency forward and option contracts, commodity price swaps, interest rate swaps, and net investment hedges where the hedging instrument is recorded at fair value. Net investment hedges that use foreign currency denominated debt to hedge 3M s net investment are not impacted by the fair value measurement standard under ASC 820, as the debt used as the hedging instrument is

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marked to a value with respect to changes in spot foreign currency exchange rates and not with respect to other factors that may impact fair value.

3M has determined that foreign currency forwards, commodity price swaps, currency swaps, foreign currency options, interest rate swaps and cross-currency swaps will be considered level 2 measurements. 3M uses inputs other than quoted prices that are observable for the asset. These inputs include foreign currency exchange rates, volatilities, and interest rates. Derivative positions are primarily valued using standard calculations/models that use as their basis readily observable market parameters. Industry standard data providers are 3M s primary source for forward and spot rate information for both interest rates and currency rates, with resulting valuations periodically validated through third-party or counterparty quotes and a net present value stream of cash flows model.

The following tables provide information by level for assets and liabilities that are measured at fair value on a recurring basis.

(Millions) Description	Fair Value at March 31, 2015	Level 1	Fair Value Measurements Using Inputs Considered as Level 2	Level 3
Assets:				
Available-for-sale:				
Marketable securities:				
U.S. government agency securities	$ 68	$	$ 68	$
Foreign government agency securities	60		60	
Corporate debt securities	551		551	
Certificates of deposit/time deposits	24		24	
Commercial paper	27		27	
Asset-backed securities:				
Automobile loan related	167		167	
Credit card related	66		66	
Equipment lease related	7		7	
Other	46		46	
U.S. municipal securities	15			15
Investments	1	1		
Derivative instruments assets:				
Foreign currency forward/option contracts	529		529	
Commodity price swap contracts	1		1	
Interest rate swap contracts	31		31	
Liabilities:				
Derivative instruments liabilities:				
Foreign currency forward/option contracts	69		69	
Commodity price swap contracts	4		4	

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(Millions) Description	Fair Value at December 31, 2014	Fair Value Measurements Using Inputs Considered as Level 1	Level 2	Level 3
Assets:				
Available-for-sale:				
Marketable securities:				
U.S. government agency securities	$ 108	$	$ 108	$
Foreign government agency securities	95		95	
Corporate debt securities	619		619	
Certificates of deposit/time deposits	41		41	
Asset-backed securities:				
Automobile loan related	282		282	
Credit card related	162		162	
Equipment lease related	48		48	
Other	46		46	
U.S. treasury securities	38	38		
U.S. municipal securities	15			15
Investments	1	1		
Derivative instruments assets:				
Foreign currency forward/option contracts	229		229	
Interest rate swap contracts	27		27	
Liabilities:				
Derivative instruments liabilities:				
Foreign currency forward/option contracts	36		36	
Commodity price swap contracts	4		4	
Interest rate swap contracts	3		3	

The following table provides a reconciliation of the beginning and ending balances of items measured at fair value on a recurring basis in the table above that used significant unobservable inputs (Level 3).

(Millions) Marketable securities auction rate securities and certain U.S. municipal securities only	Three months ended March 31, 2015	2014
Beginning balance	**$ 15**	$ 11
Total gains or losses:		
Included in earnings		
Included in other comprehensive income		1
Purchases and issuances		
Sales and settlements		
Transfers in and/or out of Level 3		
Ending balance (March 31)	**15**	12
Change in unrealized gains or losses for the period included in earnings for securities held at the end of the reporting period		

In addition, the plan assets of 3M s pension and postretirement benefit plans are measured at fair value on a recurring basis (at least annually). Refer to Note 10 in 3M s 2014 Annual Report on Form 10-K.

Assets and Liabilities that are Measured at Fair Value on a Nonrecurring Basis:

Disclosures are required for certain assets and liabilities that are measured at fair value, but are recognized and disclosed at fair value on a nonrecurring basis in periods subsequent to initial recognition. For 3M, such measurements of fair value relate primarily to long-lived asset impairments. There were no material long-lived asset impairments for the three months ended March 31, 2015 and 2014.

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Fair Value of Financial Instruments:

The Company s financial instruments include cash and cash equivalents, marketable securities, accounts receivable, certain investments, accounts payable, borrowings, and derivative contracts. The fair values of cash and cash equivalents, accounts receivable, accounts payable, and short-term borrowings and current portion of long-term debt approximated carrying values because of the short-term nature of these instruments. Available-for-sale marketable securities and investments, in addition to certain derivative instruments, are recorded at fair values as indicated in the preceding disclosures. For its long-term debt the Company utilized third-party quotes to estimate fair values (classified as level 2). Information with respect to the carrying amounts and estimated fair values of these financial instruments follow:

	March 31, 2015		December 31, 2014	
(Millions)	Carrying Value	Fair Value	Carrying Value	Fair Value
Long-term debt, excluding current portion	**$ 6,459**	**$ 6,938**	$ 6,731	$ 7,203

The fair values reflected above consider the terms of the related debt absent the impacts of derivative/hedging activity. The carrying amount of long-term debt referenced above is impacted by certain fixed-to-floating interest rate swaps that are designated as fair value hedges and by the designation of fixed rate Eurobond securities issued by the Company as hedging instruments of the Company s net investment in its European subsidiaries. Many of 3M s fixed-rate bonds were trading at a premium at March 31, 2015 and December 31, 2014 due to the low interest rates and tightening of 3M s credit spreads.

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NOTE 10. Commitments and Contingencies

Legal Proceedings:

The Company and some of its subsidiaries are involved in numerous claims and lawsuits, principally in the United States, and regulatory proceedings worldwide. These include various products liability (involving products that the Company now or formerly manufactured and sold), intellectual property, and commercial claims and lawsuits, including those brought under the antitrust laws, and environmental proceedings. Unless otherwise stated, the Company is vigorously defending all such litigation. Additional information about the Company s process for disclosure and recording of liabilities and insurance receivables related to legal proceedings can be found in Note 13 Commitments and Contingencies in the Company s Annual Report on Form 10-K for the year ended December 31, 2014.

The following sections first describe the significant legal proceedings in which the Company is involved, and then describe the liabilities and associated insurance receivables the Company has accrued relating to its significant legal proceedings.

Respirator Mask/Asbestos Litigation

As of March 31, 2015, the Company is a named defendant, with multiple co-defendants, in numerous lawsuits in various courts that purport to represent approximately 2,150 individual claimants, compared to approximately 2,220 individual claimants with actions pending at December 31, 2014.

The vast majority of the lawsuits and claims resolved by and currently pending against the Company allege use of some of the Company s mask and respirator products and seek damages from the Company and other defendants for alleged personal injury from workplace exposures to asbestos, silica, coal mine dust or other occupational dusts found in products manufactured by other defendants or generally in the workplace. A minority of the lawsuits and claims resolved by and currently pending against the Company generally allege personal injury from occupational exposure to asbestos from products previously manufactured by the Company, which are often unspecified, as well as products manufactured by other defendants, or occasionally at Company premises.

The Company s current volume of new and pending matters is substantially lower than it experienced at the peak of filings in 2003. The Company expects that filing of claims by unimpaired claimants in the future will continue to be at much lower levels than in the past. Accordingly, the number of claims alleging more serious injuries, including mesothelioma and other malignancies, will represent a greater percentage of total claims than in the past. The Company has prevailed in all nine cases taken to trial, including seven of the eight cases tried to verdict (such trials occurred in 1999, 2000, 2001, 2003, 2004, and 2007), and an appellate reversal in 2005 of the 2001 jury verdict adverse to the Company. The ninth case, tried in 2009, was dismissed by the court at the close of plaintiff s evidence, based on the court s legal finding that the plaintiff had not presented sufficient evidence to support a jury verdict.

The Company has demonstrated in these past trial proceedings that its respiratory protection products are effective as claimed when used in the intended manner and in the intended circumstances. Consequently the Company believes that claimants are unable to establish that their medical conditions, even if significant, are attributable to the Company s respiratory protection products. Nonetheless the Company s litigation experience indicates that claims of persons with malignant conditions are costlier to resolve than the claims of unimpaired persons, and it therefore believes the average cost of resolving pending and future claims on a per-claim basis will continue to be higher than it experienced in prior periods when the vast majority of claims were asserted by the unimpaired.

As previously reported, the State of West Virginia, through its Attorney General, filed a complaint in 2003 against the Company and two other manufacturers of respiratory protection products in the Circuit Court of Lincoln County, West Virginia and amended its complaint in 2005. The amended complaint seeks substantial, but unspecified, compensatory damages primarily for reimbursement of the costs allegedly incurred by the State for worker s compensation and healthcare benefits provided to all workers with occupational pneumoconiosis and unspecified punitive damages. The case has been inactive since the fourth quarter of 2007, other than a case management conference in March 2011. In November 2013, the State filed a motion to bifurcate the lawsuit into separate liability and damages proceedings. At the hearing on the motion, the Court declined to bifurcate, and set a status conference during the second quarter of 2015. No liability has been recorded for this matter because the Company believes that liability is not probable and estimable at this time. In addition, the Company is not able to estimate a possible loss or range of loss given the lack of any meaningful discovery responses by the State of West Virginia, the otherwise minimal activity in this case and the fact that the complaint asserts claims against two other manufacturers where a defendant s share of liability may turn on the law of joint and several liability and by the amount of fault, if any, a jury might allocate to each defendant if the case is ultimately tried.

Respirator Mask/Asbestos Liabilities and Insurance Receivables: The Company estimates its respirator mask/asbestos liabilities, including the cost to resolve the claims and defense costs, by examining: (i) the Company s experience in

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resolving claims, (ii) apparent trends, (iii) the apparent quality of claims (*e.g.,* whether the claim has been asserted on behalf of asymptomatic claimants), (iv) changes in the nature and mix of claims (*e.g.,* the proportion of claims asserting usage of the Company s mask or respirator products and alleging exposure to each of asbestos, silica, coal or other occupational dusts, and claims pleading use of asbestos-containing products allegedly manufactured by the Company), (v) the number of current claims and a projection of the number of future asbestos and other claims that may be filed against the Company, (vi) the cost to resolve recently settled claims, and (vii) an estimate of the cost to resolve and defend against current and future claims.

Developments may occur that could affect the Company s estimate of its liabilities. These developments include, but are not limited to, significant changes in (i) the number of future claims, (ii) the average cost of resolving claims, (iii) the legal costs of defending these claims and in maintaining trial readiness, (iv) changes in the mix and nature of claims received, (v) trial and appellate outcomes, (vi) changes in the law and procedure applicable to these claims, and (vii) the financial viability of other co-defendants and insurers.

As a result of the Company s cost of resolving claims of persons who claim more serious injuries, including mesothelioma and other malignancies, the Company increased its accruals in the first quarter of 2015 for respirator mask/asbestos liabilities by $14 million. In the first quarter of 2015, the Company made payments for fees and settlements of $10 million related to the respirator mask/asbestos litigation. As of March 31, 2015, the Company had accruals for respirator mask/asbestos liabilities of $144 million (excluding Aearo accruals). This accrual represents the low end in a range of loss. The Company cannot estimate the amount or upper end of the range of amounts by which the liability may exceed the accrual the Company has established because of the (i) inherent difficulty in projecting the number of claims that have not yet been asserted or the time period in which future claims may be asserted, (ii) the complaints nearly always assert claims against multiple defendants where the damages alleged are typically not attributed to individual defendants so that a defendant s share of liability may turn on the law of joint and several liability, which can vary by state, (iii) the multiple factors described above that the Company considers in estimating its liabilities, and (iv) the several possible developments described above that may occur that could affect the Company s estimate of liabilities.

As of March 31, 2015, the Company s receivable for insurance recoveries related to the respirator mask/asbestos litigation was $41 million. The Company estimates insurance receivables based on an analysis of its policies, including their exclusions, pertinent case law interpreting comparable policies, its experience with similar claims, and assessment of the nature of each claim and remaining coverage, and then records an amount it has concluded is likely to be recovered. Various factors could affect the timing and amount of recovery of this receivable, including (i) delays in or avoidance of payment by insurers; (ii) the extent to which insurers may become insolvent in the future, and (iii) the outcome of negotiations with insurers and legal proceedings with respect to respirator mask/asbestos liability insurance coverage.

The Company has unresolved coverage with claims-made carriers for respirator mask claims. The Company is also seeking coverage under the policies of certain insolvent insurers. Once those claims for coverage are resolved, the Company will have collected substantially all of its remaining insurance coverage for respirator mask/asbestos claims.

Respirator Mask/Asbestos Litigation Aearo Technologies

On April 1, 2008, a subsidiary of the Company purchased the stock of Aearo Holding Corp., the parent of Aearo Technologies (Aearo). Aearo manufactured and sold various products, including personal protection equipment, such as eye, ear, head, face, fall and certain respiratory protection products.

As of March 31, 2015, Aearo and/or other companies that previously owned and operated Aearo s respirator business (American Optical Corporation, Warner-Lambert LLC, AO Corp. and Cabot Corporation (Cabot)) are named defendants, with multiple co-defendants, including the Company, in numerous lawsuits in various courts in which plaintiffs allege use of mask and respirator products and seek damages from Aearo and other defendants for alleged personal injury from workplace exposures to asbestos, silica-related, or other occupational dusts found in products manufactured by other defendants or generally in the workplace.

As of March 31, 2015, the Company, through its Aearo subsidiary, had accruals of $23 million for product liabilities and defense costs related to current and future Aearo-related asbestos and silica-related claims. Responsibility for legal costs, as well as for settlements and judgments, is currently shared in an informal arrangement among Aearo, Cabot, American Optical Corporation and a subsidiary of Warner Lambert and their insurers (the Payor Group). Liability is allocated among the parties based on the number of years each company sold respiratory products under the AO Safety brand and/or owned the AO Safety Division of American Optical Corporation and the alleged years of exposure of the individual plaintiff. Aearo s share of the contingent liability is further limited by an agreement entered into between Aearo and Cabot on July 11, 1995. This agreement provides that, so long as Aearo pays to Cabot a quarterly fee of $100,000, Cabot will retain responsibility and liability for, and indemnify Aearo against, any product liability claims involving exposure to asbestos, silica, or silica products for respirators sold prior to July 11, 1995. Because of the difficulty in determining how long a particular respirator remains in the stream of commerce after being sold, Aearo and Cabot have applied the agreement to claims arising out of the alleged use of respirators involving exposure to asbestos, silica or silica products prior to January 1, 1997.

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With these arrangements in place, Aearo s potential liability is limited to exposures alleged to have arisen from the use of respirators involving exposure to asbestos, silica, or silica products on or after January 1, 1997. To date, Aearo has elected to pay the quarterly fee. Aearo could potentially be exposed to additional claims for some part of the pre-July 11, 1995 period covered by its agreement with Cabot if Aearo elects to discontinue its participation in this arrangement, or if Cabot is no longer able to meet its obligations in these matters.

In March 2012, Cabot CSC Corporation and Cabot Corporation filed a lawsuit against Aearo in the Superior Court of Suffolk County, Massachusetts seeking declaratory relief as to the scope of Cabot s indemnity obligations under the July 11, 1995 agreement, including whether Cabot has retained liability for coal workers pneumoconiosis claims, and seeking damages for breach of contract. In June 2014, the court granted Aearo s motion for summary judgment on all claims. Cabot filed a motion for reconsideration, and Aearo filed a motion for clarification of the court s order granting Aearo summary judgment. In October 2014, the court denied Aearo s motion for clarification. The court also denied, in part, Cabot s motion for reconsideration and reaffirmed its ruling that Cabot retained liability for claims involving exposure to silica in coal mine dust. The court granted Cabot s motion, in part, ruling that Aearo was not entitled to summary judgment on Cabot s claim for equitable allocation, and on whether the 258 underlying claims were Cabot s responsibility. These two issues remain in the case for further proceedings and the parties have engaged in discovery related to them. New motions for summary judgment will be presented to the court in the third quarter of 2015.

Developments may occur that could affect the estimate of Aearo s liabilities. These developments include, but are not limited to: (i) significant changes in the number of future claims, (ii) significant changes in the average cost of resolving claims, (iii) significant changes in the legal costs of defending these claims, (iv) significant changes in the mix and nature of claims received, (v) trial and appellate outcomes, (vi) significant changes in the law and procedure applicable to these claims, (vii) significant changes in the liability allocation among the co-defendants, (viii) the financial viability of members of the Payor Group including exhaustion of available coverage limits, and/or (ix) a determination that the interpretation of the contractual obligations on which Aearo has estimated its share of liability is inaccurate. The Company cannot determine the impact of these potential developments on its current estimate of Aearo s share of liability for these existing and future claims. If any of the developments described above were to occur, the actual amount of these liabilities for existing and future claims could be significantly larger than the amount accrued.

Because of the inherent difficulty in projecting the number of claims that have not yet been asserted, the complexity of allocating responsibility for future claims among the Payor Group, and the several possible developments that may occur that could affect the estimate of Aearo s liabilities, the Company cannot estimate the amount or range of amounts by which Aearo s liability may exceed the accrual the Company has established.

Environmental Matters and Litigation

The Company s operations are subject to environmental laws and regulations including those pertaining to air emissions, wastewater discharges, toxic substances, and the handling and disposal of solid and hazardous wastes enforceable by national, state, and local authorities around the world, and private parties in the United States and abroad. These laws and regulations provide, under certain circumstances, a basis for the remediation of contamination, for restoration of or compensation for damages to natural resources, and for personal injury and property damage claims. The Company has incurred, and will continue to incur, costs and capital expenditures in complying with these laws and regulations, defending personal injury and property damage claims, and modifying its business operations in light of its environmental responsibilities. In its effort to satisfy its environmental responsibilities and comply with environmental laws and regulations, the Company has established, and periodically updates, policies relating to environmental standards of performance for its operations worldwide.

Under certain environmental laws, including the United States Comprehensive Environmental Response, Compensation and Liability Act of 1980 and similar state laws, the Company may be jointly and severally liable, typically with other companies, for the costs of remediation of environmental contamination at current or former facilities and at off-site locations. The Company has identified numerous locations, most of which are in the United States, at which it may have some liability. Please refer to the section entitled *Environmental Liabilities and Insurance Receivables* that follows for information on the amount of the accrual.