MCCORMICK & CO INC
Form 10-Q
March 28, 2017
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 Quarter Ended February 28, 2017
Commission File Number 001-14920

McCORMICK & COMPANY, INCORPORATED
(Exact name of registrant as specified in its charter)

MARYLAND	52-0408290
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)

18 Loveton Circle, P. O. Box 6000, Sparks, MD	21152-6000
(Address of principal executive offices)	(Zip Code)

Registrant's telephone number, including area code (410) 771-7301

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 filing requirements for the past 90 days. Yes x No ¨
Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (Section 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 ¨
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 definition of "accelerated filer," "large accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act.

Large Accelerated Filer	x	Accelerated Filer	¨
Non-Accelerated Filer	¨	Smaller Reporting Company	¨

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes ¨ No x
Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date.

	Shares Outstanding February 28, 2017
Common Stock	11,451,748
Common Stock Non-Voting	113,226,723

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PART I - FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS

McCORMICK & COMPANY, INCORPORATED
CONDENSED CONSOLIDATED INCOME STATEMENT (UNAUDITED)
(in millions except per share amounts)

	Three months ended	
	February 28, 2017	February 29, 2016
Net sales	$1,043.7	$ 1,030.2
Cost of goods sold	630.7	625.2
Gross profit	413.0	405.0
Selling, general and administrative expense	275.2	274.3
Special charges	3.6	1.6
Operating income	134.2	129.1
Interest expense	14.5	13.9
Other income, net	0.1	1.1
Income from consolidated operations before income taxes	119.8	116.3
Income taxes	33.3	31.3
Net income from consolidated operations	86.5	85.0
Income from unconsolidated operations	7.0	8.4
Net income	$93.5	$ 93.4
Earnings per share – basic	$0.75	$ 0.73
Average shares outstanding – basic	125.1	127.1
Earnings per share – diluted	$0.74	$ 0.73
Average shares outstanding – diluted	126.9	128.3
Cash dividends paid per share	$0.47	$ 0.43

See notes to condensed consolidated financial statements (unaudited).

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McCORMICK & COMPANY, INCORPORATED
CONDENSED CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME (UNAUDITED)
(in millions)

	Three months ended	
	February 28, 2017	February 29, 2016
Net income	$93.5	$ 93.4
Net income attributable to non-controlling interest	1.1	0.7
Other comprehensive income (loss):		
Unrealized components of pension plans (including curtailment gains of $76.7 for 2017)	86.5	7.7
Currency translation adjustments	15.1	(25.2)
Change in derivative financial instruments	(2.6)	1.6
Deferred taxes	(29.6)	(1.7)
Comprehensive income	$164.0	$ 76.5

See notes to condensed consolidated financial statements (unaudited).

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McCORMICK & COMPANY, INCORPORATED
CONDENSED CONSOLIDATED BALANCE SHEET
(in millions)

	February 28, 2017 (unaudited)	February 29, 2016 (unaudited)	November 30, 2016
ASSETS			
Current Assets			
Cash and cash equivalents	$ 125.7	$ 111.8	$ 118.4
Trade accounts receivables, net	404.4	371.2	465.2
Inventories, net			
Finished products	351.4	320.0	336.3
Raw materials and work-in-process	415.8	382.2	420.0
	767.2	702.2	756.3
Prepaid expenses and other current assets	87.8	72.9	81.9
Total current assets	1,385.1	1,258.1	1,421.8
Property, plant and equipment	1,665.2	1,533.3	1,630.2
Less: accumulated depreciation	(982.4)	(924.2)	(960.8)
Property, plant and equipment, net	682.8	609.1	669.4
Goodwill	1,857.6	1,764.0	1,771.4
Intangible assets, net	473.9	370.1	424.9
Investments and other assets	351.7	363.7	348.4
Total assets	$ 4,751.1	$ 4,365.0	$ 4,635.9
LIABILITIES AND SHAREHOLDERS' EQUITY			
Current Liabilities			
Short-term borrowings	$ 638.9	$ 389.6	$ 390.3
Current portion of long-term debt	250.7	0.6	2.9
Trade accounts payable	448.4	336.7	450.8
Other accrued liabilities	400.4	363.7	578.7
Total current liabilities	1,738.4	1,090.6	1,422.7
Long-term debt	803.5	1,055.0	1,054.0
Other long-term liabilities	477.6	492.5	521.1
Total liabilities	3,019.5	2,638.1	2,997.8
Shareholders' Equity			
Common stock	413.1	386.5	409.7
Common stock non-voting	678.0	661.1	674.5
Retained earnings	1,073.1	1,086.3	1,056.8
Accumulated other comprehensive loss	(445.0)	(423.7)	(514.4)
Non-controlling interests	12.4	16.7	11.5
Total shareholders' equity	1,731.6	1,726.9	1,638.1
Total liabilities and shareholders' equity	$ 4,751.1	$ 4,365.0	$ 4,635.9

See notes to condensed consolidated financial statements (unaudited).

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McCORMICK & COMPANY, INCORPORATED
CONDENSED CONSOLIDATED CASH FLOW STATEMENT (UNAUDITED)
(in millions)

	Three months ended February 28, 2017	February 29, 2016
Operating activities		
Net income	$93.5	$93.4
Adjustments to reconcile net income to net cash flow provided by operating activities:		
Depreciation and amortization	28.3	26.4
Stock-based compensation	4.1	3.0
Income from unconsolidated operations	(7.0)	(8.4)
Changes in operating assets and liabilities	(80.2)	(43.7)
Dividends from unconsolidated affiliates	5.6	7.9
Net cash flow provided by operating activities	44.3	78.6
Investing activities		
Acquisition of businesses (net of cash acquired)	(124.0)	—
Capital expenditures	(29.6)	(22.4)
Proceeds from sale of property, plant and equipment	0.9	0.2
Net cash flow used in investing activities	(152.7)	(22.2)
Financing activities		
Short-term borrowings, net	247.8	250.8
Long-term debt repayments	(2.5)	(201.7)
Proceeds from exercised stock options	8.2	7.8
Taxes withheld and paid on employee stock awards	(1.7)	(0.7)
Common stock acquired by purchase	(82.7)	(47.8)
Dividends paid	(58.9)	(54.6)
Net cash flow provided by (used in) financing activities	110.2	(46.2)
Effect of exchange rate changes on cash and cash equivalents	5.5	(11.0)
Increase (decrease) in cash and cash equivalents	7.3	(0.8)
Cash and cash equivalents at beginning of period	118.4	112.6
Cash and cash equivalents at end of period	$125.7	$111.8

See notes to condensed consolidated financial statements (unaudited).

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McCORMICK & COMPANY, INCORPORATED
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited)

1. ACCOUNTING POLICIES

Basis of Presentation

The accompanying unaudited condensed consolidated financial statements have been prepared in accordance with the instructions to Form 10-Q and do not include all the information and notes required by United States generally accepted accounting principles (U.S. GAAP) for complete financial statements. In our opinion, the accompanying condensed consolidated financial statements contain all adjustments, which are of a normal and recurring nature, necessary to present fairly the financial position and the results of operations for the interim periods presented.

The results of consolidated operations for the three month period ended February 28, 2017 are not necessarily indicative of the results to be expected for the full year. Historically, our net sales, net income and cash flow from operations are lower in the first half of the fiscal year and increase in the second half. The typical increase in net sales, net income and cash flow from operations in the second half of the year is largely due to the consumer business cycle in the U.S., where customers typically purchase more products in the fourth quarter due to the Thanksgiving and Christmas holiday seasons.

For further information, refer to the consolidated financial statements and notes included in our Annual Report on Form 10-K for the year ended November 30, 2016.

As of November 30, 2016, we adopted ASU 2015-03 Simplifying the Presentation of Debt Issuance Costs, which eliminated the prior requirement to recognize debt issuance costs as an asset and instead requires classification as a direct reduction from the carrying amount of the debt liability, and ASU 2015-17 Balance Sheet Classification of Deferred Taxes (Topic 740), which, for entities with a classified balance sheet, eliminated the prior requirement to classify deferred tax assets and liabilities as current and non-current and instead requires the presentation of all deferred tax assets and liabilities as noncurrent. As a result, the accompanying condensed consolidated balance sheet as of February 29, 2016, has been restated to reflect the requirements of these newly adopted standards.

Accounting Pronouncement Adopted in 2017

In March 2016, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update No. 2016-09 Compensation—Stock Compensation (Topic 718): Improvements to Employee Share-Based Payment Accounting, which changes the accounting for certain aspects of share-based payments to employees. The new guidance requires, among its other provisions, that excess tax benefits (which represent the excess of actual tax benefits received at the date of vesting or settlement over the benefits recognized over the vesting period or upon issuance of share-based payments) and tax deficiencies (which represent the amount by which actual tax benefits received at the date of vesting or settlement is lower than the benefits recognized over the vesting period or upon issuance of share-based payments) be recorded in the income statement as an increase or decrease in income taxes when the awards vest or are settled. This is in comparison to the prior requirement that these excess tax benefits be recognized in additional paid-in capital and these tax deficiencies be recognized either as an offset to accumulated excess tax benefits, if any, or in the income statement. The new guidance also requires excess tax benefits to be classified along with other income tax cash flows as an operating activity in the statement of cash flows rather than, as previously required, a financing activity. The new guidance is effective for the first quarter of our fiscal year ending November 30, 2018, with early adoption permitted.

We have elected to early adopt ASU 2016-09 effective December 1, 2016 on a prospective basis where permitted by the new standard. As a result of this adoption:

- We recognized discrete tax benefits of $1.6 million in the income taxes line item of our consolidated income statement for the three months ended February 28, 2017 related to excess tax benefits upon vesting or settlement in that period.
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We elected to adopt the cash flow presentation of the excess tax benefits prospectively, commencing with our cash flow statement for the three months ended February 28, 2017, where these benefits are classified along with other income tax cash flows as an operating activity.

- We have elected to continue to estimate the number of stock-based awards expected to vest, rather than electing to account for forfeitures as they occur to determine the amount of compensation cost to be recognized in each period.

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- At this time, we have not changed our policy on statutory withholding requirements and will continue to allow an employee to withhold at the minimum statutory withholding requirements. Amounts paid by us to taxing authorities when directly withholding shares associated with employees' income tax withholding obligations are classified as a financing activity in our cash flow statement for the three months ended February 28, 2017. ASU 2016-09 requires that this cash flow presentation be made retrospectively and the cash flow statement for the three months ended February 29, 2016 has been restated accordingly.
- We excluded the excess tax benefits from the assumed proceeds available to repurchase shares in the computation of our diluted earnings per share for the three months ended February 28, 2017.

Recently Issued Accounting Pronouncements

In March 2017, the FASB issued Accounting Standards Update No. 2017-07 Compensation-Retirement Benefits (Topic 715)-Improving the Presentation of Net Periodic Pension Cost and Net Periodic Postretirement Benefit Cost. This guidance revises how employers that sponsor defined benefit pension and other postretirement plans present the net periodic benefit cost in their income statement and requires that the service cost component of net periodic benefit cost be presented in the same income statement line items as other employee compensation costs from services rendered during the period. Of the components of net periodic benefit cost, only the service cost component will be eligible for asset capitalization. The other components of the net periodic benefit cost must be presented separately from the line items that include the service cost and outside of any subtotal of operating income on the income statement. The new standard will be effective for the first quarter of our fiscal year ending November 30, 2019. Early adoption is permitted as of the beginning of an annual reporting period for all entities. We have not yet determined the impact from adoption of this new accounting pronouncement on our financial statements.

In January 2017, the FASB issued Accounting Standards Update No. 2017-04 Intangibles-Goodwill and Other Topics (Topic 350)-Simplifying the Test for Goodwill Impairment. This guidance eliminates the requirement to calculate the implied fair value of goodwill of a reporting unit to measure a goodwill impairment charge. Instead, a company will record an impairment charge based on the excess of a reporting unit's carrying amount over its fair value. The new standard will be effective for the first quarter of our fiscal year ending November 30, 2021. Early adoption is permitted for all entities for annual and interim goodwill impairment testing dates after January 1, 2017. We have not yet determined the impact from adoption of this new accounting pronouncement on our financial statements.

In January 2017, the FASB issued Accounting Standards Update No. 2017-01 Business Combinations (Topic 805)-Clarifying the Definition of a Business. This guidance changes the definition of a business to assist entities in evaluating when a set of transferred assets and activities constitutes a business. The guidance requires an entity to evaluate if substantially all of the fair value of the gross assets acquired is concentrated in a single identifiable asset or a group of similar identifiable assets; if so, the set of transferred assets and activities is not a business. The guidance also requires a business to include at least one substantive process and narrows the definition of outputs by more closely aligning it with how outputs are described in Accounting Standards Codification (ASC 606) Revenue from Contracts with Customers. The new standard will be effective for the first quarter of our fiscal year ending November 30, 2019. Early adoption is permitted for all entities. We have not yet determined the impact from adoption of this new accounting pronouncement on our financial statements.

In February 2016, the FASB issued Accounting Standards Update No. 2016-02 Leases (Topic 842). This guidance revises existing practice related to accounting for leases under Accounting Standards Codification Topic 840 Leases (ASC 840) for both lessees and lessors. Our leases as of February 28, 2017 principally relate to: (i) certain real estate, including that related to a number of administrative, distribution and manufacturing locations; (ii) certain machinery and equipment, including a corporate airplane and automobiles; and (iii) certain software. In addition, in 2016, we entered into a 15-year lease for a headquarters building, which is expected to commence upon completion of building construction and fit-out, currently scheduled for the second half of 2018. The new guidance in ASU 2016-02 requires lessees to recognize a right-of-use asset and a lease liability for virtually all of their leases (other than leases that meet the definition of a short-term lease). The lease liability will be equal to the present value of lease payments and the right-of-use asset will be based on the lease liability, subject to adjustment such as for initial direct costs. For income statement purposes, the new standard retains a dual model similar to ASC 840, requiring leases to be classified as either operating or finance. For lessees, operating leases will result in straight-line expense (similar to current accounting by lessees for operating leases under ASC 840) while finance leases will result in a front-loaded expense pattern (similar to current accounting by lessees for capital leases under ASC 840). While the new standard maintains similar accounting for lessors as under ASC 840, the new standard reflects updates to, among other things, align with certain changes to the lessee model. The new standard will be effective for the first quarter of our fiscal year ending November 30, 2020. Early adoption is permitted for all entities. We have not yet determined the impact from adoption of this new accounting pronouncement on our financial statements.

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In July 2015, the FASB issued Accounting Standards Update No. 2015-11 Simplifying the Measurement of Inventory (Topic 330). This guidance is intended to simplify the subsequent measurement of inventories by replacing the current lower of cost or market test with a lower of cost and net realizable value test. It will be effective for the first quarter of our fiscal year ending November 30, 2018, and early adoption is permitted. We have not yet determined the impact from adoption of this new accounting pronouncement on our financial statements.

In May 2014, the FASB issued Accounting Standards Update No. 2014-09 Revenue from Contracts with Customers (Topic 606). This guidance is intended to improve—and converge with international standards—the financial reporting requirements for revenue from contracts with customers. The new standard will be effective for the first quarter of our fiscal year ending November 30, 2019. Early adoption is permitted for all entities, but not before the original effective date for public business entities (that is, annual reporting periods beginning after December 15, 2016 or our fiscal year ending November 30, 2018). We do not expect to early adopt this new accounting pronouncement. In preparation for our adoption of the new standard in our fiscal year ending November 30, 2019, we have obtained representative samples of contracts and other forms of agreements with our customers in the U.S. and international locations and are evaluating the provisions contained therein in light of the five-step model specified by the new guidance. That five-step model includes: (1) determination of whether a contract—an agreement between two or more parties that creates legally enforceable rights and obligations—exists; (2) identification of the performance obligations in the contract; (3) determination of the transaction price; (4) allocation of the transaction price to the performance obligations in the contract; and (5) recognition of revenue when (or as) the performance obligation is satisfied. We are also evaluating the impact of the new standard on certain common practices currently employed by us and by other manufacturers of consumer products, such as slotting fees, co-operative advertising, rebates and other pricing allowances, merchandising funds and consumer coupons. We have not yet determined the impact of the new standard on our financial statements or whether we will adopt on a prospective or retrospective basis in the first quarter of our fiscal year ending November 30, 2019.

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2. ACQUISITIONS

Acquisitions are part of our strategy to increase sales and profits.
On December 15, 2016, we purchased 100% of the shares of Enrico Giotti SpA (Giotti), a leading European flavor manufacturer located in Italy, for a cash payment of $124.0 million (net of cash acquired of $1.2 million), subject to certain post-closing adjustments. The acquisition was funded with cash and short-term borrowings. Giotti is well known in the industry for its innovative beverage, sweet, savory and dairy flavor applications. At the time of the acquisition, annual sales of Giotti were approximately €53 million. Our acquisition of Giotti in fiscal 2017 expands the breadth of value-added products for McCormick's industrial segment, including additional expertise in flavoring health and nutrition products. As of February 28, 2017, a preliminary valuation of the acquired net assets of Giotti resulted in $2.5 million allocated to net tangible assets acquired, $9.8 million allocated to indefinite lived brand asset, $38.0 million allocated to definite lived intangible assets with a weighted-average life of 11.9 years and $74.9 million allocated to goodwill. Goodwill related to the Giotti acquisition, which is not deductible for tax purposes, primarily represents the intangible assets that do not qualify for separate recognition, such as the value of leveraging the customer intimacy and value-added flavor solutions we provide to our industrial customers to Giotti’s relationships with industrial customers of their flavors solutions and extracts, as well as from expected synergies from the combined operations and assembled workforces, and the future development initiatives of the assembled workforces. The preliminary valuation, based on a comparison of acquisitions of similar industrial businesses, provided average percentages of purchase prices assigned to goodwill and other identifiable intangible assets, which we used to initially value the Giotti acquisition. We expect to finalize the determination of the fair value of the acquired net assets of Giotti in the fourth quarter of 2017. Giotti has been included in our industrial segment since its acquisition. During the three months ended February 28, 2017, we recorded $2.1 million in transaction-related expenses associated with this acquisition. Due to the estimated impact of financing, acquisition and integration costs, we do not expect the operating income contribution of Giotti to be significant to our overall results for 2017.

On April 19, 2016, we completed the purchase of 100% of the shares of Botanical Food Company, Pty Ltd, owner of the Gourmet Garden brand of packaged herbs (Gourmet Garden), a privately held company based in Australia. Gourmet Garden is a global market leader in chilled convenient packaged herbs. Gourmet Garden's products complement our existing branded herb portfolio with the addition of chilled convenient herbs located in the perimeter of the grocery store. We plan to drive sales of the Gourmet Garden brand by expanding global distribution and building awareness with increased brand investment. At the time of acquisition, annual sales of Gourmet Garden were approximately 70 million Australian dollars. The purchase price was $116.2 million, net of cash acquired of $3.3 million and after closing adjustments, and was financed with a combination of cash and short-term borrowings. A preliminary valuation of the acquired net assets of Gourmet Garden resulted in $20.4 million allocated to net tangible assets acquired, $20.3 million allocated to indefinite lived brand asset, $14.2 million allocated to definite lived intangible assets with a weighted-average life of 12.0 years and $61.3 million allocated to goodwill. Goodwill related to the Gourmet Garden acquisition, which is not deductible for tax purposes, primarily represents the intangible assets that do not qualify for separate recognition, such as the value of leveraging our brand building expertise, our insights in demand from consumers for herbs, and our supply chain capabilities, as well as expected synergies from the combined operations and assembled workforce. The preliminary valuation, based on a comparison of acquisitions of similar consumer businesses, provided average percentages of purchase prices assigned to goodwill and other identifiable intangible assets, which we used to initially value the Gourmet Garden acquisition. We expect to finalize the determination of the fair value of the acquired net assets of Gourmet Garden in the second quarter of 2017. Gourmet Garden has been included in our consumer segment since its acquisition. While this business has an industrial component, the industrial component was not material to its overall business in 2016. Beginning in 2017, the industrial component of Gourmet Garden is being reflected as a component of our industrial segment.

For the first quarter of 2017, Gourmet Garden and Giotti added $16.6 million and $11.1 million, respectively, to our sales. Due to financing, acquisition and integration costs, the aggregate incremental operating income contributed by Gourmet Garden and Giotti was not significant to our overall results for the three months ended February 28, 2017. Proforma financial information for these acquisitions has not been presented because the financial impact is not material.

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3. SPECIAL CHARGES

We continue to evaluate changes to our organization structure to enable us to reduce fixed costs, simplify or improve processes, and improve our competitiveness.

In our consolidated income statement, we include a separate line item captioned “special charges” in arriving at our consolidated operating income. Special charges consist of expenses associated with certain actions undertaken by the Company to reduce fixed costs, simplify or improve processes, and improve our competitiveness and are of such significance in terms of both up-front costs and organizational/structural impact to require advance approval by our Management Committee, comprised of our senior management, including our Chairman, President and Chief Executive Officer. Upon presentation of any such proposed action (generally including details with respect to estimated costs, which typically consist principally of employee severance and related benefits, together with ancillary costs associated with the action that may include a non-cash component or a component which relates to inventory adjustments that are included in cost of goods sold; impacted employees or operations; expected timing; and expected savings) to the Management Committee and the Committee’s advance approval, expenses associated with the approved action are classified as special charges upon recognition and monitored on an on-going basis through completion.

During the three months ended February 28, 2017, we recorded $3.6 million of special charges, consisting primarily of $1.9 million for severance and other exit costs associated with our Europe, Middle East and Africa (EMEA) region’s closure of its manufacturing plant in Portugal in mid-2017; $1.0 million related to third party expenses incurred associated with our evaluation of organizational streamlining activities; $0.3 million for other exit costs related to the 2015 discontinuance of Kohinoor's non-profitable bulk-packaged and broken basmati rice product lines, and $0.2 million for other exit costs related to the planned exit from our current leased manufacturing facilities in Singapore and Thailand upon construction of a new manufacturing facility in Thailand, which was initiated in 2016. Of the $3.6 million in special charges recorded during the three months ended February 28, 2017, approximately $1.3 million were paid in cash and $0.5 million represented a non-cash asset impairment, with the remaining accrual expected to be substantially paid in 2017.

In addition to the amounts recognized in the first quarter of 2017, we expect to incur additional special charges during the balance of 2017 of $7.4 million, consisting of $1.1 million associated with the plant closure in Portugal and related relocation of manufacturing, $3.3 million of additional third party expenses associated with our evaluation of organizational streamlining activities, and approximately $3 million for other streamlining actions approved by our Management Committee and more fully described in our Annual Report on Form 10-K for the year ended November 30, 2016. These other streamlining actions include: (1) the write-off of the foreign currency translation adjustment, which is included as a component of other comprehensive income, associated with our former consolidated joint venture in South Africa, which we exited in late 2016, upon its liquidation; (2) other costs associated with the planned exit of two leased manufacturing facilities in Singapore and Thailand described above; (3) other exit costs related to our Kohinoor business described above; and (4) other amounts associated with the EMEA reorganization plans initiated in 2015.

During the three months ended February 29, 2016, we recorded $1.6 million of special charges, consisting of $1.1 million related to other exit costs associated with actions undertaken to enhance organization efficiency and streamline processes in our EMEA region (which is more fully described below), $0.3 million for other exit costs related to the discontinuance of Kohinoor's non-profitable bulk-packaged and broken basmati rice product lines, and $0.2 million for employee severance and related costs associated with our North America effectiveness initiative. All of these are a continuation of actions that were initiated in 2015. Substantially all of the $1.6 million of 2016 special charges were paid in cash during the three months ended February 29, 2016.

Of the $3.6 million of special charges recorded in our consolidated financial statements in the first quarter of 2017, $2.5 million related to our consumer segment and $1.1 million related to our industrial segment. Of the $1.6 million of special charges recorded in our consolidated financial statements for the first quarter of 2016, $1.3 million related to our consumer segment and $0.3 million related to our industrial segment. All balances associated with our special charges are included in other accrued liabilities in our consolidated balance sheet.

In 2015, we initiated projects to enhance organization efficiency and streamline processes in EMEA in order to support our competitiveness and long-term growth. These initiatives center on actions intended to reduce fixed costs and improve business processes, as well as continue to drive simplification across the business and supply chain. These actions include the transfer of certain additional activities to our shared services center in Poland. These projects were continued in 2016.

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The following table outlines the major components of accrual balances and activity relating to the special charges associated with the EMEA reorganization plans that were initiated in 2015 for the three months ended February 28, 2017 and February 29, 2016 (in millions):

	Employee severance and related benefits	Other related costs	Total
Balance as of November 30, 2016	$ 10.5	$ 0.5	$ 11.0
Cash paid	(0.9)	—	(0.9)
Balance as of February 28, 2017	$ 9.6	$ 0.5	$ 10.1
Balance as of November 30, 2015	$ 16.2	$ 0.6	$ 16.8
Special charges	—	1.1	1.1
Cash paid	(1.2)	(1.1)	(2.3)
Impact of foreign exchange	0.1	—	0.1
Balance as of February 29, 2016	$ 15.1	$ 0.6	$ 15.7

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4. GOODWILL

The changes in the carrying amount of goodwill by segment for the three months ended February 28, 2017 and February 29, 2016 were as follows (in millions):

	2017		2016	
	Consumer	Industrial	Consumer	Industrial
Beginning of year	$1,608.3	$ 163.1	$1,587.7	$ 171.6
Changes in preliminary purchase price allocation	(0.4)	—	—	—
Increases in goodwill from acquisitions	—	74.9	—	—
Foreign currency fluctuations and other	10.4	1.3	7.6	(2.9)
Balance as of end of February	$1,618.3	$ 239.3	$1,595.3	$ 168.7

5. FINANCING ARRANGEMENTS AND FINANCIAL INSTRUMENTS

In July 2016, we entered into a 15-year lease for a headquarters building in Hunt Valley, Maryland. The lease, which is expected to commence upon completion of building construction and fit-out, currently scheduled for the second half of 2018, requires monthly lease payments of approximately $0.9 million beginning six months after lease commencement. The $0.9 million monthly lease payment is subject to adjustment after an initial 60-month period and thereafter on an annual basis as specified in the lease agreement. In addition, the initial $0.9 million monthly lease payment is subject to increase in the event of agreed-upon changes to specifications related to the headquarters building. We expect to consolidate our Corporate staff and certain non-manufacturing U.S. employees, currently housed in four locations in the Hunt Valley, Maryland area, to the new headquarters building.

We use derivative financial instruments to enhance our ability to manage risk, including foreign currency and interest rate exposures, which exist as part of our ongoing business operations. We do not enter into contracts for trading purposes, nor are we a party to any leveraged derivative instruments. The use of derivative financial instruments is monitored through regular communication with senior management and the use of written guidelines.

During fiscal year 2016, we entered into multiple fair value foreign currency exchange contracts to hedge the currency component of certain intercompany loans between our subsidiaries. At February 28, 2017, the notional value of these contracts was $113.0 million. During the three months ended February 28, 2017, we recognized a $2.7 million loss on the change in fair value of these contracts, which was offset by a $2.5 million gain on the change in the currency component of the underlying loans. Both the loss and the gain were recognized in our consolidated income statement as other income, net.

During the three months ended February 28, 2017, we entered into a total of $75 million of forward starting interest rate swap agreements to manage our interest rate risk associated with the anticipated issuance of at least $75 million of fixed rate notes by December 2017. The weighted average fixed rate of these agreements is 2.49% and is based upon the applicable U.S. LIBOR swap rate at the inception of each agreement. We intend to cash settle these agreements upon issuance of the notes. If the applicable U.S. LIBOR swap rate increases at the time of settlement of the agreements, we will receive a one-time cash payment from the counterparties. If the applicable U.S. LIBOR swap rate decreases at the time of settlement of the agreements, we will make a one-time cash payment to the counterparties.We have designated these forward starting interest rate swap agreements, which expire on December 15, 2017, as cash flow hedges. Amounts associated with these agreements, including the related mark-to-market prior to settlement, will be deferred in other comprehensive income; upon settlement, any gain or loss realized will be amortized over the life of the fixed rate notes as a component of interest expense.

As of February 28, 2017, the maximum time frame for our foreign exchange forward contracts is 9 months.

For all derivatives, the net amount of accumulated other comprehensive income expected to be reclassified in the next 12 months is $2.1 million as an increase to earnings.

All derivatives are recognized at fair value in the balance sheet and recorded in either current or noncurrent other assets or other accrued liabilities or other long-term liabilities depending upon their nature and maturity.
The following table discloses the fair values of derivative instruments on our balance sheet (in millions):

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As of February 28, 2017	Asset Derivatives			Liability Derivatives		
	Balance sheet location	Notional amount	Fair value	Balance sheet location	Notional amount	Fair value
Interest rate contracts	Other current assets	$ —	$ —	Other accrued liabilities	$ 175.0	$ 2.1
Foreign exchange contracts	Other current assets	111.3	3.5	Other accrued liabilities	$ 284.5	8.5
Total			$ 3.5			$ 10.6

As of February 29, 2016	Asset Derivatives			Liability Derivatives		
	Balance sheet location	Notional amount	Fair value	Balance sheet location	Notional amount	Fair value
Interest rate contracts	Other current assets	$ 100.0	$ 4.5	Other accrued liabilities	$ —	$ —
Foreign exchange contracts	Other current assets	150.5	4.4	Other accrued liabilities	119.8	1.8
Total			$ 8.9			$ 1.8

As of November 30, 2016	Asset Derivatives			Liability Derivatives		
	Balance sheet location	Notional amount	Fair value	Balance sheet location	Notional amount	Fair value
Interest rate contracts	Other current assets	$ —	$ —	Other accrued liabilities	$ 100.0	$ 1.2
Foreign exchange contracts	Other current assets	204.3	4.9	Other accrued liabilities	244.9	5.4
Total			$ 4.9			$ 6.6

The following tables disclose the impact of derivative instruments on our other comprehensive income (OCI), accumulated other comprehensive income (AOCI) and our income statement for the three month periods ended February 28, 2017 and February 29, 2016 (in millions):

Fair Value Hedges

Derivative	Income statement location	Income (expense)	
		2017	2016
Interest rate contracts	Interest expense	$ 0.3	$ 0.6

Derivative	Income statement location	Gain (loss) recognized in income		Hedged item	Income statement location	Gain (loss) recognized in income	
		2017	2016			2017	2016
Foreign exchange contracts	Other income, net	$ (2.7)	$ —	Intercompany loans	Other income, net	$ 2.5	$ —

Cash Flow Hedges

Derivative	Gain or (loss)	Income statement location	Gain or (loss) reclassified from

	recognized in OCI			AOCI	
	2017	2016		2017	2016
Interest rate contracts	$(0.2)	$ —	Interest expense	$(0.1)	$(0.1)
Foreign exchange contracts	(0.4)	2.1	Cost of goods sold	1.1	