

LSB INDUSTRIES INC
Form 10-Q
August 08, 2011

Table of Contents

**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 **June 30, 2011**

OR

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

For the transition period from _____ to _____

Commission file number 1-7677

LSB Industries, Inc.

Exact name of Registrant as specified in its charter

Delaware

73-1015226

State or other jurisdiction of incorporation or organization

I.R.S. Employer Identification No.

**16 South Pennsylvania Avenue, Oklahoma City,
Oklahoma**

73107

Address of principal executive offices

Zip Code

(405) 235-4546

Registrant's telephone number, including area code

None

Former name, former address and former fiscal year, if changed since last report.

Indicate by check mark whether the Registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the Registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes No

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

Indicate by check mark whether the Registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See definitions of "large accelerated filer", "accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer

Accelerated filer

Non-accelerated filer

Smaller reporting company

(Do not check if a smaller reporting company)

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

Edgar Filing: LSB INDUSTRIES INC - Form 10-Q

The number of shares outstanding of the Registrant's voting common stock, as of July 29, 2011 was 22,254,188 shares, excluding 4,320,462 shares held as treasury stock.

FORM 10-Q OF LSB INDUSTRIES, INC.
TABLE OF CONTENTS

	Page
<u>PART I Financial Information</u>	
<u>Item 1. Financial Statements</u>	3
<u>Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations</u>	30
<u>Item 3. Quantitative and Qualitative Disclosures About Market Risk</u>	48
<u>Item 4. Controls and Procedures</u>	49
Special Note Regarding Forward-Looking Statements	50
<u>PART II Other Information</u>	
<u>Item 1. Legal Proceedings</u>	51
<u>Item 1A. Risk Factors</u>	51
<u>Item 2. Unregistered Sales of Equity Securities and Use of Proceeds</u>	52
<u>Item 3. Defaults Upon Senior Securities</u>	52
<u>Item 4. (Reserved)</u>	52
<u>Item 5. Other Information</u>	52
<u>Item 6. Exhibits</u>	53
<u>EX-31.1</u>	
<u>EX-31.2</u>	
<u>EX-32.1</u>	
<u>EX-32.2</u>	
<u>EX-101 INSTANCE DOCUMENT</u>	
<u>EX-101 SCHEMA DOCUMENT</u>	
<u>EX-101 CALCULATION LINKBASE DOCUMENT</u>	
<u>EX-101 LABELS LINKBASE DOCUMENT</u>	
<u>EX-101 PRESENTATION LINKBASE DOCUMENT</u>	
<u>EX-101 DEFINITION LINKBASE DOCUMENT</u>	

Table of Contents

**PART I
FINANCIAL INFORMATION**

Item 1. Financial Statements

**LSB INDUSTRIES, INC.
CONDENSED CONSOLIDATED BALANCE SHEETS
(Information at June 30, 2011 is unaudited)**

	June 30, 2011	December 31, 2010
	(In Thousands)	
Assets		
Current assets:		
Cash and cash equivalents	\$ 115,998	\$ 66,946
Restricted cash	83	31
Short-term investments		10,003
Accounts receivable, net	101,689	74,259
Inventories:		
Finished goods	28,052	32,072
Work in process	4,227	2,981
Raw materials	27,372	25,053
Total inventories	59,651	60,106
Supplies, prepaid items and other:		
Prepaid insurance	1,965	4,449
Precious metals	14,639	12,048
Supplies	7,614	6,802
Fair value of derivatives and other	9	1,454
Other	2,321	1,174
Total supplies, prepaid items and other	26,548	25,927
Deferred income taxes	5,490	5,396
Total current assets	309,459	242,668
Property, plant and equipment, net	144,299	135,755
Other assets:		
Debt issuance costs, net	1,243	1,023
Investment in affiliate	3,398	4,016
Goodwill	1,724	1,724
Other, net	3,687	2,795
Total other assets	10,052	9,558
	\$ 463,810	\$ 387,981

(Continued on following page)

Table of Contents

LSB INDUSTRIES, INC.
CONDENSED CONSOLIDATED BALANCE SHEETS (continued)
(Information at June 30, 2011 is unaudited)

	June 30, 2011	December 31, 2010
	(In Thousands)	
Liabilities and Stockholders Equity		
Current liabilities:		
Accounts payable	\$ 53,817	\$ 51,025
Short-term financing	1,537	3,821
Accrued and other liabilities	36,534	31,507
Current portion of long-term debt	5,579	2,328
 Total current liabilities	 97,467	 88,681
 Long-term debt	 81,250	 93,064
 Noncurrent accrued and other liabilities	 13,583	 12,605
 Deferred income taxes	 15,921	 14,261
 Commitments and contingencies (Note 10)		
 Stockholders equity:		
Series B 12% cumulative, convertible preferred stock, \$100 par value; 20,000 shares issued and outstanding	2,000	2,000
Series D 6% cumulative, convertible Class C preferred stock, no par value; 1,000,000 shares issued and outstanding	1,000	1,000
Common stock, \$.10 par value; 75,000,000 shares authorized, 26,496,670 shares issued (25,476,534 at December 31, 2010)	2,650	2,548
Capital in excess of par value	158,719	131,845
Retained earnings	119,594	70,351
	283,963	207,744
 Less treasury stock at cost:		
Common stock, 4,320,462 shares	28,374	28,374
 Total stockholders equity	 255,589	 179,370
	\$ 463,810	\$ 387,981

See accompanying notes.

Table of Contents

LSB INDUSTRIES, INC.
CONDENSED CONSOLIDATED STATEMENTS OF INCOME
(Unaudited)
Six and Three Months Ended June 30, 2011 and 2010

	Six Months		Three Months	
	2011	2010	2011	2010
	(In Thousands, Except Per Share Amounts)			
Net sales	\$ 413,112	\$ 298,802	\$ 235,619	\$ 168,392
Cost of sales	287,172	235,388	163,533	133,244
Gross profit	125,940	63,414	72,086	35,148
Selling, general and administrative expense	43,102	46,827	22,517	22,238
Provision for (recoveries of) losses on accounts receivable	121	(35)	79	(44)
Other expense	2,383	302	2,321	244
Other income	(1,977)	(906)	(1,105)	(100)
Operating income	82,311	17,226	48,274	12,810
Interest expense	3,580	4,079	1,868	1,999
Losses on extinguishment of debt	136	52	136	52
Non-operating other expense (income), net	(5)	(38)	2	
Income from continuing operations before provisions for income taxes and equity in earnings and losses of affiliate	78,600	13,133	46,268	10,759
Provisions for income taxes	29,149	5,891	17,492	4,979
Equity in losses (earnings) of affiliate	(207)	(528)	78	(267)
Income from continuing operations	49,658	7,770	28,698	6,047
Net loss from discontinued operations	110	43	53	38
Net income	49,548	7,727	28,645	6,009
Dividends on preferred stocks	305	305		
Net income applicable to common stock	\$ 49,243	\$ 7,422	\$ 28,645	\$ 6,009
Weighted-average common shares:				
Basic	21,657	21,227	22,133	21,229
Diluted	23,485	21,692	23,526	22,377

Edgar Filing: LSB INDUSTRIES INC - Form 10-Q

Income per common share:

Basic	\$	2.27	\$.35	\$	1.29	\$.28
-------	----	------	----	-----	----	------	----	-----

Diluted	\$	2.12	\$.35	\$	1.22	\$.27
---------	----	------	----	-----	----	------	----	-----

See accompanying notes.

Table of Contents

LSB INDUSTRIES, INC.
CONDENSED CONSOLIDATED STATEMENT OF STOCKHOLDERS EQUITY
(Unaudited)
Six Months Ended June 30, 2011

	Common Stock Shares	Non- Redeemable Preferred Stock	Common Stock Par Value	Capital in Excess of Par Value (In Thousands)	Retained Earnings	Treasury Stock- Common	Total
Balance at December 31, 2010	25,477	\$ 3,000	\$ 2,548	\$ 131,845	\$ 70,351	\$ (28,374)	\$ 179,370
Net income and comprehensive income					49,548		49,548
Dividends paid on preferred stocks					(305)		(305)
Stock-based compensation				519			519
Conversion of debentures to common stock	888		89	24,319			24,408
Exercise of stock options	132		13	927			940
Excess income tax benefit associated with stock-based compensation				1,109			1,109
Balance at June 30, 2011	26,497	\$ 3,000	\$ 2,650	\$ 158,719	\$ 119,594	\$ (28,374)	\$ 255,589

See accompanying notes.

Note: For the six and three months ended June 30, 2011 and 2010, there were no differences between net income and comprehensive income.

Table of Contents

LSB INDUSTRIES, INC.
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
(Unaudited)
Six Months Ended June 30, 2011 and 2010

	2011	2010
	(In Thousands)	
Cash flows from continuing operating activities:		
Net income	\$ 49,548	\$ 7,727
Adjustments to reconcile net income to net cash provided by continuing operating activities:		
Net loss from discontinued operations	110	43
Deferred income taxes	1,566	244
Losses on extinguishment of debt	136	52
Expense associated with modification of secured term loan	387	
Expense associated with induced conversion of 5.5% convertible debentures	558	
Net gain on carbon credits	(94)	
Losses on sales and disposals of property and equipment	895	259
Gain on property insurance recoveries associated with property, plant and equipment		(495)
Depreciation of property, plant and equipment	9,184	8,626
Amortization	267	311
Stock-based compensation	519	500
Provision for (recovery of) losses on accounts receivable	121	(35)
Provision for (realization of) losses on inventory	279	(324)
Realization of losses on firm sales commitments		(371)
Equity in earnings of affiliate	(207)	(528)
Distributions received from affiliate	825	240
Changes in fair value of commodities contracts	52	246
Changes in fair value of interest rate contracts	240	348
Other		(10)
Cash provided (used) by changes in assets and liabilities:		
Accounts receivable	(27,549)	(16,585)
Inventories	226	4,128
Other supplies, prepaid items and other	(1,256)	1,948
Accounts payable	(1,356)	2,700
Accrued payroll and benefits	(835)	(1,054)
Accrued and prepaid income taxes	1,791	2,392
Accrued contractual profit-sharing obligation	1,637	
Deferred revenue on product sales	1,472	263
Customer deposits	1,399	(77)
Other current and noncurrent liabilities	1,248	1,980
Net cash provided by continuing operating activities	41,163	12,528
Cash flows from continuing investing activities:		
Capital expenditures	(14,556)	(10,861)
Proceeds from property insurance recoveries associated with property, plant and equipment		1,670
Proceeds from sales of property and equipment	31	11

Edgar Filing: LSB INDUSTRIES INC - Form 10-Q

Proceeds from short-term investments	10,012	20,053
Purchase of short-term investments	(9)	(10,002)
Deposits of restricted cash	(52)	(246)
Proceeds from sales of carbon credits	1,665	
Payments on contractual obligations carbon credits	(1,573)	
Other assets	(914)	(326)
Net cash provided (used) by continuing investing activities	(5,396)	299

(Continued on following page)

Table of Contents

LSB INDUSTRIES, INC.
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS (continued)
(Unaudited)
Six Months Ended June 30, 2011 and 2010

	2011	2010
	(In Thousands)	
Cash flows from continuing financing activities:		
Proceeds from revolving debt facility	\$ 329,797	\$ 263,064
Payments on revolving debt facility	(329,797)	(263,064)
Proceeds from modification of secured term loan, net of fees	10,347	
Proceeds from secured term loan, net of fees	14,766	
Proceeds from other long-term debt, net of fees		47
Payments associated with induced conversion of 5.5% convertible debentures	(558)	
Acquisition of 5.5% convertible debentures		(2,494)
Payments on other long-term debt	(10,484)	(2,386)
Payments of debt issuance costs	(108)	
Payments on short-term financing	(2,284)	(2,062)
Proceeds from exercise of stock options	940	296
Purchase of treasury stock		(2,421)
Excess income tax benefit associated with stock-based compensation	1,109	189
Dividends paid on preferred stocks	(305)	(305)
Net cash provided (used) by continuing financing activities	13,423	(9,136)
Cash flows of discontinued operations:		
Operating cash flows	(138)	(145)
Net increase in cash and cash equivalents	49,052	3,546
Cash and cash equivalents at beginning of period	66,946	61,739
Cash and cash equivalents at end of period	\$ 115,998	\$ 65,285
Supplemental cash flow information:		
Cash payments for income taxes, net of refunds	\$ 24,619	\$ 3,093
Noncash investing and financing activities:		
Receivable associated with a property insurance claim	\$	\$ 560
Current other assets, accounts payable and long-term debt associated with property, plant and equipment	\$ 5,662	\$ 5,548
Debt issuance costs incurred associated with secured term loan	\$ 835	\$
Debt issuance costs written off associated with 5.5% debentures	\$ 328	\$ 58
Accrued liabilities extinguished associated with 5.5% debentures	\$ 336	\$
5.5% debentures converted to common stock	\$ 24,400	\$

See accompanying notes.

Table of Contents

LSB INDUSTRIES, INC.
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited)

Note 1: Summary of Significant Accounting Policies

For a complete discussion of our significant accounting policies, refer to the notes to our audited consolidated financial statements included in our Form 10-K for the year ended December 31, 2010 (2010 Form 10-K), filed with the Securities and Exchange Commission (SEC) on March 3, 2011.

Basis of Consolidation and Presentation LSB Industries, Inc. (LSB) and its subsidiaries (the Company , We , Us

Our) are consolidated in the accompanying condensed consolidated financial statements. We are involved in manufacturing, marketing and engineering operations. We are primarily engaged in the manufacture and sale of geothermal and water source heat pumps and air handling products (the Climate Control Business) and the manufacture and sale of chemical products (the Chemical Business). LSB is a holding company with no significant operations or assets other than cash, cash equivalents, and investments in its subsidiaries. Entities that are 20% to 50% owned and for which we have significant influence are accounted for on the equity method. All material intercompany accounts and transactions have been eliminated.

In the opinion of management, the unaudited condensed consolidated financial statements of the Company as of June 30, 2011 and for the six and three-month periods ended June 30, 2011 and 2010 include all adjustments and accruals, consisting of normal, recurring accrual adjustments which are necessary for a fair presentation of the results for the interim periods. These interim results are not necessarily indicative of results for a full year due, in part, to the seasonality of our sales of agricultural products and the timing of performing our major plant maintenance activities. Our selling seasons for agricultural products are primarily during the spring and fall planting seasons, which typically extend from March through June and from September through November.

Certain information and footnote disclosures normally included in financial statements prepared in accordance with United States generally accepted accounting principles (GAAP) have been condensed or omitted in this Form 10-Q pursuant to the rules and regulations of the SEC. These condensed consolidated financial statements should be read in connection with our audited consolidated financial statements and notes thereto included in our 2010 Form 10-K.

Reclassifications Certain reclassifications have been made in our condensed consolidated statement of cash flows for the six months ended June 30, 2010 to conform to our condensed consolidated statement of cash flows presentation for the six months ended June 30, 2011, which reclassifications expanded and eliminated certain of our continuing operating activity line items. These reclassifications did not impact the total amount of net cash provided by continuing operating activities for the six months ended June 30, 2010.

Use of Estimates The preparation of condensed consolidated financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

Income per Common Share Net income applicable to common stock is computed by adjusting net income by the amount of preferred stock dividends and dividend requirements, if applicable. Basic income per common share is based upon net income applicable to common stock and the weighted-average number of common shares outstanding during each year. Diluted income per share is based on net income applicable to common stock plus preferred stock dividends and dividend requirements on preferred stock assumed to be converted, if dilutive, and interest expense including amortization of debt issuance cost, net of income taxes, on convertible debt assumed to be converted, if dilutive, and the weighted-average number of common shares and dilutive common equivalent shares outstanding, and the assumed conversion of dilutive convertible securities outstanding.

Short-Term Investments Investments, which consisted of certificates of deposit with an original maturity of 13 weeks, are considered short-term investments. These investments are carried at cost which approximates fair value. All of these investments were held by financial institutions within the United States (U.S.) and none of these investments were in excess of the federally insured limits.

Accounts Receivable Our accounts receivable are stated at net realizable value. This value includes an appropriate allowance for estimated uncollectible accounts to reflect any loss anticipated on accounts receivable balances. Our

estimate is based on historical experience and periodic assessment of outstanding accounts receivable, particularly those accounts which are past due (based upon the terms of the sale). Our periodic assessment of our accounts receivable is based on our best estimate of amounts that are not recoverable.

Table of Contents

LSB INDUSTRIES, INC.
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (continued)
(Unaudited)

Note 1: Summary of Significant Accounting Policies (continued)

Inventories Inventories are stated at the lower of cost (determined using the first-in, first-out (FIFO) basis) or market (net realizable value). Finished goods and work-in-process inventories include material, labor, and manufacturing overhead costs. Additionally, we review inventories and record inventory reserves for slow-moving inventory items.

Precious Metals Precious metals are used as a catalyst in the Chemical Business manufacturing process. Precious metals are carried at cost, with cost being determined using the FIFO basis. Because some of the catalyst consumed in the production process cannot be readily recovered and the amount and timing of recoveries are not predictable, we follow the practice of expensing precious metals as they are consumed. Occasionally, during major maintenance or capital projects, we may be able to perform procedures to recover precious metals (previously expensed) which have accumulated over time within the manufacturing equipment. Recoveries of precious metals are recognized at historical FIFO costs. When we accumulate precious metals in excess of our production requirements, we may sell a portion of the excess metals.

Product Warranty Our Climate Control Business sells equipment that has an expected life, under normal circumstances and use, which extends over several years. As such, we provide warranties after equipment shipment/start up covering defects in materials and workmanship.

Our accounting policy and methodology for warranty arrangements is to measure and recognize the expense and liability for such warranty obligations at the time of sale using a percentage of sales and cost per unit of equipment, based upon our historical and estimated future warranty costs. We also recognize the additional warranty expense and liability to cover atypical costs associated with a specific product, or component thereof, or project installation, when such costs are probable and reasonably estimable. It is reasonably possible that our estimated accrued warranty costs could change in the near term.

Contingencies Certain conditions may exist which may result in a loss, but which will only be resolved when future events occur. We and our legal counsel assess such contingent liabilities, and such assessment inherently involves an exercise of judgment. If the assessment of a contingency indicates that it is probable that a loss has been incurred, we would accrue for such contingent losses when such losses can be reasonably estimated. If the assessment indicates that a potentially material loss contingency is not probable but reasonably possible, or is probable but cannot be estimated, the nature of the contingent liability, together with an estimate of the range of possible loss if determinable and material, would be disclosed. Estimates of potential legal fees and other directly related costs associated with contingencies are not accrued but rather are expensed as incurred. Loss contingency liabilities are included in current and noncurrent accrued and other liabilities and are based on current estimates that may be revised in the