Vulcan Materials CO
Form 10-Q
November 02, 2016
UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

FORM 10-Q

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

For the quarterly period ended September 30, 2016

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

For the transition period from to

Commission File Number 001-33841

VULCAN MATERIALS COMPANY
(Exact name of registrant as specified in its charter)

New Jersey (State or other jurisdiction of incorporation)	20-8579133 (I.R.S. Employer Identification No.)
1200 Urban Center Drive, Birmingham, Alabama (Address of principal executive offices)	35242 (zip code)

(205) 298-3000 (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 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 registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See the definitions of "large accelerated filer," "accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act. (Check one):

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

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

Class	Shares outstanding at October 28, 2016
Common Stock, $1 Par Value	132,309,274

VULCAN MATERIALS COMPANY

FORM 10-Q

QUARTER ENDED SEPTEMBER 30, 2016

Contents

Unless otherwise stated or the context otherwise requires, references in this report to "Vulcan," the "Company," "we," "our," or "us" refer to Vulcan Materials Company and its consolidated subsidiaries.

part I financial information

ITEM 1

FINANCIAL STATEMENTS

VULCAN MATERIALS COMPANY AND SUBSIDIARY COMPANIES

CONDENSED CONSOLIDATED BALANCE SHEETS

Unaudited, except for December 31 in thousands	September 30 2016	December 31 2015	September 30 2015
Assets			
Cash and cash equivalents	$ 135,365	$ 284,060	$ 168,681
Restricted cash	0	1,150	0
Accounts and notes receivable			
Accounts and notes receivable, gross	536,242	423,600	558,755
Less: Allowance for doubtful accounts	(4,260)	(5,576)	(5,770)
Accounts and notes receivable, net	531,982	418,024	552,985
Inventories			
Finished products	283,266	297,925	275,717
Raw materials	25,411	21,765	21,680
Products in process	2,753	1,008	1,161
Operating supplies and other	26,612	26,375	28,148
Inventories	338,042	347,073	326,706
Current deferred income taxes	0	0	39,301
Prepaid expenses	71,370	34,284	56,017
Total current assets	1,076,759	1,084,591	1,143,690
Investments and long-term receivables	38,914	40,558	40,516
Property, plant & equipment			
Property, plant & equipment, cost	7,105,036	6,891,287	6,803,588
Reserve for depreciation, depletion & amortization	(3,876,743)	(3,734,997)	(3,683,961)
Property, plant & equipment, net	3,228,293	3,156,290	3,119,627
Goodwill	3,094,824	3,094,824	3,094,824
Other intangible assets, net	753,314	766,579	766,695
Other noncurrent assets	165,981	158,790	151,514
Total assets	$ 8,358,085	$ 8,301,632	$ 8,316,866
Liabilities			
Current maturities of long-term debt	131	130	130

Trade payables and accruals	163,139	175,729	195,536
Other current liabilities	197,642	177,620	216,411
Total current liabilities	360,912	353,479	412,077
Long-term debt	1,983,639	1,980,334	1,979,493
Noncurrent deferred income taxes	706,715	681,096	692,643
Deferred revenue	201,732	207,660	209,651
Other noncurrent liabilities	601,117	624,875	659,725
Total liabilities	$ 3,854,115	$ 3,847,444	$ 3,953,589
Other commitments and contingencies (Note 8)			
Equity			
Common stock, $1 par value, Authorized 480,000 shares,			
Outstanding 132,309, 133,172 and 133,315 shares, respectively	132,309	133,172	133,315
Capital in excess of par value	2,829,806	2,822,578	2,812,593
Retained earnings	1,660,961	1,618,507	1,564,215
Accumulated other comprehensive loss	(119,106)	(120,069)	(146,846)
Total equity	$ 4,503,970	$ 4,454,188	$ 4,363,277
Total liabilities and equity	$ 8,358,085	$ 8,301,632	$ 8,316,866

The accompanying Notes to the Condensed Consolidated Financial Statements are an integral part of these statements.

VULCAN MATERIALS COMPANY AND SUBSIDIARY COMPANIES

CONDENSED CONSOLIDATED STATEMENTS OF
COMPREHENSIVE INCOME

	Three Months Ended		Nine Months Ended	
Unaudited		September 30		September 30
in thousands, except per share data	2016	2015	2016	2015
Total revenues	$ 1,008,140	$ 1,038,460	$ 2,719,693	$ 2,564,896
Cost of revenues	703,931	747,170	1,958,581	1,961,292
Gross profit	304,209	291,290	761,112	603,604
Selling, administrative and general expenses	76,311	71,390	235,460	207,350
Gain on sale of property, plant & equipment and businesses	2,023	799	2,934	7,423
Business interruption claims recovery	690	0	11,652	0
Impairment of long-lived assets	0	0	(10,506)	(5,190)
Restructuring charges	0	(448)	(320)	(4,546)
Other operating expense, net	(3,535)	(8,045)	(23,629)	(17,201)
Operating earnings	227,076	212,206	505,783	376,740
Other nonoperating income (expense), net	990	(2,818)	325	(2,277)
Interest expense, net	33,126	37,800	100,192	183,931
Earnings from continuing operations before income taxes	194,940	171,588	405,916	190,532
Provision for income taxes	52,062	45,386	116,026	51,177
Earnings from continuing operations	142,878	126,202	289,890	139,355
Loss on discontinued operations, net of tax	(3,113)	(2,397)	(7,451)	(7,066)
Net earnings	$ 139,765	$ 123,805	$ 282,439	$ 132,289
Other comprehensive income, net of tax				
Reclassification adjustment for cash flow hedges	307	282	902	5,607
Amortization of actuarial loss and prior service cost for benefit plans	20	3,883	61	9,261
Other comprehensive income	327	4,165	963	14,868
Comprehensive income	$ 140,092	$ 127,970	$ 283,402	$ 147,157
Basic earnings (loss) per share				
Continuing operations	$ 1.07	$ 0.95	$ 2.17	$ 1.05
Discontinued operations	(0.02)	(0.02)	(0.05)	(0.06)
Net earnings	$ 1.05	$ 0.93	$ 2.12	$ 0.99
Diluted earnings (loss) per share				
Continuing operations	$ 1.06	$ 0.93	$ 2.14	$ 1.03
Discontinued operations	(0.02)	(0.02)	(0.05)	(0.05)
Net earnings	$ 1.04	$ 0.91	$ 2.09	$ 0.98
Weighted-average common shares outstanding				

Basic	133,019	133,474	133,418	133,082
Assuming dilution	135,033	135,558	135,192	134,942
Cash dividends per share of common stock	$ 0.20	$ 0.10	$ 0.60	$ 0.30
Depreciation, depletion, accretion and amortization	$ 72,049	$ 69,662	$ 213,362	$ 204,770
Effective tax rate from continuing operations	26.7%	26.5%	28.6%	26.9%

The accompanying Notes to the Condensed Consolidated Financial Statements are an integral part of these statements.

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VULCAN MATERIALS COMPANY AND SUBSIDIARY COMPANIES

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

Unaudited in thousands	Nine Months Ended 2016	September 30 2015
Operating Activities		
Net earnings	$ 282,439	$ 132,289
Adjustments to reconcile net earnings to net cash provided by operating activities		
Depreciation, depletion, accretion and amortization	213,362	204,770
Net gain on sale of property, plant & equipment and businesses	(2,934)	(7,423)
Contributions to pension plans	(7,126)	(11,337)
Share-based compensation expense	15,645	14,020
Excess tax benefits from share-based compensation	(26,747)	(16,950)
Deferred tax provision (benefit)	25,094	(7,640)
Cost of debt purchase	0	67,075
Changes in assets and liabilities before initial effects of business acquisitions and dispositions	(121,097)	(79,000)
Other, net	(33,188)	(14,467)
Net cash provided by operating activities	$ 345,448	$ 281,337
Investing Activities		
Purchases of property, plant & equipment	(287,440)	(214,815)
Proceeds from sale of property, plant & equipment	5,865	4,464
Payment for businesses acquired, net of acquired cash	(1,611)	(20,801)
Decrease in restricted cash	1,150	0
Other, net	2,488	(301)
Net cash used for investing activities	$ (279,548)	$ (231,453)
Financing Activities		
Proceeds from line of credit	3,000	291,000
Payments of line of credit	(3,000)	(206,000)
Payments of current maturities and long-term debt	(14)	(545,056)
Proceeds from issuance of long-term debt	0	400,000
Debt and line of credit issuance costs	0	(7,382)
Purchases of common stock	(161,463)	0
Dividends paid	(79,865)	(39,878)
Proceeds from exercise of stock options	0	67,888
Excess tax benefits from share-based compensation	26,747	16,950
Other, net	0	2
Net cash used for financing activities	$ (214,595)	$ (22,476)
Net increase (decrease) in cash and cash equivalents	(148,695)	27,408
Cash and cash equivalents at beginning of year	284,060	141,273
Cash and cash equivalents at end of period	$ 135,365	$ 168,681

The accompanying Notes to the Condensed Consolidated Financial Statements are an integral part of the statements.

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notes to condensed consolidated financial statements

Note 1: summary of significant accounting policies

NATURE OF OPERATIONS

Vulcan Materials Company (the “Company,” “Vulcan,” “we,” “our”), a New Jersey corporation, is the nation's largest producer of construction aggregates (primarily crushed stone, sand and gravel) and a major producer of asphalt mix and ready-mixed concrete.

We operate primarily in the United States and our principal product — aggregates — is used in virtually all types of public and private construction projects and in the production of asphalt mix and ready-mixed concrete. We serve markets in twenty states, Washington D.C., and the local markets surrounding our operations in Mexico and the Bahamas. Our primary focus is serving states in metropolitan markets in the United States that are expected to experience the most significant growth in population, households and employment. These three demographic factors are significant drivers of demand for aggregates. While aggregates is our focus and primary business, we produce and sell asphalt mix and/or ready-mixed concrete in our mid-Atlantic, Georgia, Southwestern and Western markets.

BASIS OF PRESENTATION

Our accompanying unaudited condensed consolidated financial statements were prepared in compliance with the instructions to Form 10-Q and Article 10 of Regulation S-X and thus do not include all of the information and footnotes required by accounting principles generally accepted in the United States of America for complete financial statements. Our Condensed Consolidated Balance Sheet as of December 31, 2015 was derived from the audited financial statement, but it does not include all disclosures required by accounting principles generally accepted in the United States of America. In the opinion of our management, the statements reflect all adjustments, including those of a normal recurring nature, necessary to present fairly the results of the reported interim periods. Operating results for the three and nine month periods ended September 30, 2016 are not necessarily indicative of the results that may be expected for the year ending December 31, 2016. For further information, refer to the consolidated financial statements and footnotes included in our most recent Annual Report on Form 10-K.

Due to the 2005 sale of our Chemicals business as described in Note 2, the results of the Chemicals business are presented as discontinued operations in the accompanying Condensed Consolidated Statements of Comprehensive Income.

RECLASSIFICATIONS

Certain items previously reported in specific financial statement captions have been reclassified to conform with the 2016 presentation.

RESTRUCTURING CHARGES

In 2014, we announced changes to our executive management team, and a new divisional organization structure that was effective January 1, 2015. During the nine months ended September 30, 2016 and September 30, 2015, we incurred $320,000 and $4,546,000, respectively, of costs related to these initiatives. We do not expect to incur any future charges related to this initiative.

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EARNINGS PER SHARE (EPS)

Earnings per share are computed by dividing net earnings by the weighted-average common shares outstanding (basic EPS) or weighted-average common shares outstanding assuming dilution (diluted EPS), as set forth below:

	Three Months Ended September 30		Nine Months Ended September 30	
in thousands	2016	2015	2016	2015
Weighted-average common shares outstanding	133,019	133,474	133,418	133,082
Dilutive effect of				
Stock-Only Stock Appreciation Rights	961	919	957	1,024
Other stock compensation plans	1,053	1,165	817	836
Weighted-average common shares outstanding, assuming dilution	135,033	135,558	135,192	134,942

All dilutive common stock equivalents are reflected in our earnings per share calculations. Antidilutive common stock equivalents are not included in our earnings per share calculations. In periods of loss, shares that otherwise would have been included in our diluted weighted-average common shares outstanding computation are excluded. There were no excluded shares for the periods presented.

The number of antidilutive common stock equivalents for which the exercise price exceeds the weighted-average market price is as follows:

	Three Months Ended September 30		Nine Months Ended September 30	
in thousands	2016	2015	2016	2015
Antidilutive common stock equivalents	2	545	234	555

Note 2: Discontinued Operations

In 2005, we sold substantially all the assets of our Chemicals business to Basic Chemicals, a subsidiary of Occidental Chemical Corporation. The financial results of the Chemicals business are classified as discontinued operations in the accompanying Condensed Consolidated Statements of Comprehensive Income for all periods presented. There were no revenues from discontinued operations for the periods presented. Results from discontinued operations are as follows:

	Three Months Ended September 30		Nine Months Ended September 30	
in thousands	2016	2015	2016	2015
Discontinued Operations				
Pretax loss	$ (5,135)	$ (3,974)	$ (12,312)	$ (11,627)
Income tax benefit	2,022	1,577	4,861	4,561
Loss on discontinued operations, net of tax	$ (3,113)	$ (2,397)	$ (7,451)	$ (7,066)

The losses from discontinued operations noted above include charges related to general and product liability costs, including legal defense costs, and environmental remediation costs associated with our former Chemicals business. These losses resulted primarily from charges associated with the Lower Passaic and Texas Brine matters as further discussed in Note 8.

Note 3: Income Taxes

Our estimated annual effective tax rate (EAETR) is based on full-year expectations of pretax earnings, statutory tax rates, permanent differences between book and tax accounting such as percentage depletion, and tax planning alternatives available in the various jurisdictions in which we operate. For interim financial reporting, we calculate our quarterly income tax provision in accordance with the EAETR. Each quarter, we update our EAETR based on our revised full-year expectation of pretax earnings and calculate the income tax provision so that the year-to-date income tax provision reflects the EAETR. Significant judgment is required in determining our EAETR.

In the third quarter of 2016, we recorded income tax expense from continuing operations of $52,062,000 compared to $45,386,000 in the third quarter of 2015. The increase in our income tax expense resulted largely from applying the statutory rate to the increase in our pretax earnings.

For the first nine months of 2016, we recorded income tax expense from continuing operations of $116,026,000 compared to $51,177,000 for the first nine months of 2015. The increase in our income tax expense resulted largely from applying the statutory rate to the increase in our pretax earnings.

We recognize deferred tax assets and liabilities (which reflect our best assessment of the future taxes we will pay) based on the differences between the book basis and tax basis of assets and liabilities. Deferred tax assets represent items to be used as a tax deduction or credit in future tax returns while deferred tax liabilities represent items that will result in additional tax in future tax returns. With our adoption of Accounting Standards Update 2015-17, “Balance Sheet Classification of Deferred Taxes” as of December 31, 2015, all deferred tax assets and liabilities are presented as noncurrent. We adopted this standard prospectively and as a result, we did not restate periods prior to adoption.

Each quarter we analyze the likelihood that our deferred tax assets will be realized. Realization of the deferred tax assets ultimately depends on the existence of sufficient taxable income of the appropriate character in either the carryback or carryforward period. A valuation allowance is recorded if, based on the weight of all available positive and negative evidence, it is more likely than not (a likelihood of more than 50%) that some portion, or all, of a deferred tax asset will not be realized.

Based on our third quarter 2016 analysis, we believe it is more likely than not that we will realize the benefit of all our deferred tax assets with the exception of certain state net operating loss carryforwards. For December 31, 2016, we project deferred tax assets related to state net operating loss carryforwards of $55,318,000, of which $52,995,000 relates to Alabama. The Alabama net operating loss carryforward, if not utilized, would expire in years 2022 – 2029. Prior to 2015, we carried a full valuation allowance against this Alabama deferred tax asset as we did not expect to utilize any portion of it. During 2015, we restructured our legal entities which, among other benefits, resulted in a partial release of the valuation allowance in the amount of $4,655,000 during the third quarter of 2015. Our analyses over the last four quarters have confirmed our third quarter 2015 conclusion but resulted in no further reductions of the valuation allowance. We expect to further reduce, or possibly eliminate, this valuation allowance once we have returned to sustained profitability (as defined in our most recent Annual Report on Form 10-K), which we project could occur in the fourth quarter of 2016.

We recognize a tax benefit associated with a tax position when, in our judgment, it is more likely than not that the position will be sustained based upon the technical merits of the position. For a tax position that meets the more likely than not recognition threshold, we measure the income tax benefit as the largest amount that we judge to have a greater than 50% likelihood of being realized. A liability is established for the unrecognized portion of any tax benefit. Our liability for unrecognized tax benefits is adjusted periodically due to changing circumstances, such as the progress of tax audits, case law developments and new or emerging legislation.

A summary of our deferred tax assets is included in Note 9 “Income Taxes” in our Annual Report on Form 10-K for the year ended December 31, 2015.

Note 4: deferred revenue

In 2013 and 2012, we sold a percentage interest in future production structured as volumetric production payments (VPPs).

The VPPs:

- § relate to eight quarries in Georgia and South Carolina
- § provide the purchaser solely with a nonoperating percentage interest in the subject quarries’ future production from aggregates reserves
- § are both time and volume limited
- § contain no minimum annual or cumulative guarantees for production or sales volume, nor minimum sales price

Our consolidated total revenues exclude the sales of aggregates owned by the VPP purchaser.

We received net cash proceeds from the sale of the VPPs of $153,282,000 and $73,644,000 for the 2013 and 2012 transactions, respectively. These proceeds were recorded as deferred revenue on the balance sheet and are amortized to revenue on a unit-of-sales basis over the terms of the VPPs (expected to be approximately 25 years, limited by volume rather than time).

Reconciliation of the deferred revenue balances (current and noncurrent) is as follows:

	Three Months Ended September 30		Nine Months Ended September 30	
in thousands	2016	2015	2016	2015
Deferred Revenue				
Balance at beginning of period	$ 210,200	$ 217,429	$ 214,060	$ 219,968
Amortization of deferred revenue	(2,068)	(1,778)	(5,928)	(4,317)
Balance at end of period	$ 208,132	$ 215,651	$ 208,132	$ 215,651

Based on expected sales from the specified quarries, we expect to recognize approximately $6,400,000 of deferred revenue as income during the 12-month period ending September 30, 2017 (reflected in other current liabilities in our 2016 Condensed Consolidated Balance Sheet).

Note 5: Fair Value Measurements

Fair value is defined as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. The fair value hierarchy prioritizes the inputs to valuation techniques used to measure fair value into three broad levels as described below:

Level 1: Quoted prices in active markets for identical assets or liabilities

Level 2: Inputs that are derived principally from or corroborated by observable market data

Level 3: Inputs that are unobservable and significant to the overall fair value measurement

Our assets subject to fair value measurement on a recurring basis are summarized below:

	Level 1 Fair Value		
in thousands	September 30 2016	December 31 2015	September 30 2015
Fair Value Recurring			
Rabbi Trust			
Mutual funds	$ 6,601	$ 11,472	$ 12,081
Equities	8,574	8,992	8,778
Total	$ 15,175	$ 20,464	$ 20,859

	Level 2 Fair Value		
in thousands	September 30 2016	December 31 2015	September 30 2015
Fair Value Recurring			
Rabbi Trust			
Money market mutual fund	$ 2,144	$ 2,124	$ 1,464
Total	$ 2,144	$ 2,124	$ 1,464

We have established two Rabbi Trusts for the purpose of providing a level of security for the employee nonqualified retirement and deferred compensation plans and for the directors' nonqualified deferred compensation plans. The fair values of these investments are estimated using a market approach. The Level 1 investments include mutual funds and equity securities for which quoted prices in active markets are available. Level 2 investments are stated at estimated fair value based on the underlying investments in the fund (short-term, highly liquid assets in commercial paper, short-term bonds and certificates of deposit).

Net gains (losses) of the Rabbi Trust investments were $1,379,000 and $(1,964,000) for the nine months ended September 30, 2016 and 2015, respectively. The portions of the net gains (losses) related to investments still held by the Rabbi Trusts at September 30, 2016 and 2015 were $273,000 and $(2,068,000), respectively.

The year-to-date decrease of $5,269,000 in total Rabbi Trust asset fair values at September 30, 2016 is primarily attributable to the elections by several retired executives to receive their distributions from the nonqualified retirement and deferred compensation plans.

The carrying values of our cash equivalents, restricted cash, accounts and notes receivable, short-term debt, trade payables and accruals, and other current liabilities approximate their fair values because of the short-term nature of these instruments. Additional disclosures for derivative instruments and interest-bearing debt are presented in Notes 6 and 7, respectively.

Assets subject to fair value measurement on a nonrecurring basis are summarized below:

	Period ending September 30, 2016		Period ending September 30, 2015	
in thousands	Level 2	Impairment Charges	Level 2	Impairment Charges
Fair Value Nonrecurring				
Property, plant & equipment, net	$ 0	$ 1,359	$ 0	$ 2,176
Other intangible assets, net	0	8,180	0	2,858
Other assets	0	967	0	156
Total	$ 0	$ 10,506	$ 0	$ 5,190

We recorded $10,506,000 and $5,190,000 of losses on impairment of long-lived assets for the nine months ended September 30, 2016 and 2015, respectively, reducing the carrying value of these Aggregates segment assets to their estimated fair values of $0 and $0. Fair value was estimated using a market approach (observed transactions involving comparable assets in similar locations).

Note 6: Derivative Instruments

During the normal course of operations, we are exposed to market risks including interest rates, foreign currency exchange rates and commodity prices. From time to time, and consistent with our risk management policies, we use derivative instruments to balance the cost and risk of such expenses. We do not utilize derivative instruments for trading or other speculative purposes.

The accounting for gains and losses that result from changes in the fair value of derivative instruments depends on whether the derivatives have been designated and qualify as hedging instruments and the type of hedging relationship. The interest rate swap agreements described below were designated as either cash flow hedges or fair value hedges. The changes in fair value of our interest rate swap cash flow hedges are recorded in accumulated other comprehensive income (AOCI) and are reclassified into interest expense in the same period the hedged items affect earnings. The changes in fair value of our interest rate swap fair value hedges are recorded as interest expense consistent with the change in the fair value of the hedged items attributable to the risk being hedged.

CASH FLOW HEDGES

During 2007, we entered into fifteen forward starting interest rate locks on $1,500,000,000 of future debt issuances in order to hedge the risk of higher interest rates. Upon the 2007 and 2008 issuances of the related fixed-rate debt, underlying interest rates were lower than the rate locks and we terminated and settled these forward starting locks for cash payments of $89,777,000. This amount was booked to AOCI and is being amortized to interest expense over the term of the related debt.

This amortization was reflected in the accompanying Condensed Consolidated Statements of Comprehensive Income as follows:

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