

AIR PRODUCTS & CHEMICALS INC /DE/

Form 10-Q

January 25, 2008

Table of Contents

**UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549**

FORM 10-Q

(Mark One)

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

For the quarterly period ended 31 December 2007

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 1-4534

AIR PRODUCTS AND CHEMICALS, INC.

(Exact Name of Registrant as Specified in Its Charter)

Delaware
(State or Other Jurisdiction of Incorporation or
Organization)

23-1274455
(I.R.S. Employer Identification No.)

7201 Hamilton Boulevard, Allentown, Pennsylvania
(Address of Principal Executive Offices)

18195-1501
(Zip Code)

610-481-4911
(Registrant's Telephone Number, Including Area Code)

Not Applicable

(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 is a large accelerated filer, an accelerated filer, or a non-accelerated filer. See definition of accelerated filer and large accelerated filer in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer Accelerated filer Non-accelerated filer

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	Outstanding at 21 January 2008
Common Stock, \$1 par value	214,448,095

**AIR PRODUCTS AND CHEMICALS, INC. and Subsidiaries
INDEX**

Page No.

Part I. FINANCIAL INFORMATIONItem 1. Financial Statements

<u>Consolidated Balance Sheets 31 December 2007 and 30 September 2007</u>	3
<u>Consolidated Income Statements Three Months Ended 31 December 2007 and 2006</u>	4
<u>Consolidated Comprehensive Income Statements Three Months Ended 31 December 2007 and 2006</u>	5
<u>Consolidated Statements of Cash Flows Three Months Ended 31 December 2007 and 2006</u>	6
<u>Summary by Business Segments Three Months Ended 31 December 2007 and 2006</u>	8
<u>Summary by Geographic Regions Three Months Ended 31 December 2007 and 2006</u>	9
<u>Notes to Consolidated Financial Statements</u>	10
<u>Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations</u>	17
<u>Item 3. Quantitative and Qualitative Disclosures About Market Risk</u>	27
<u>Item 4. Controls and Procedures</u>	27

Part II. OTHER INFORMATION

<u>Item 1A. Risk Factors</u>	28
<u>Item 2. Unregistered Sales of Equity Securities and Use of Proceeds</u>	32
<u>Item 6. Exhibits</u>	32
<u>Signatures</u>	34
<u>Exhibit Index</u>	35
<u>EX-10.1: FORM OF AWARD AGREEMENT</u>	
<u>EX-10.2: CORPORATE EXECUTIVE COMMITTEE SEPARATION PROGRAM, AS AMENDED AND RESTATED</u>	
<u>EX-12: COMPUTATION OF RATIOS OF EARNINGS TO FIXED CHARGES</u>	
<u>EX-31.1: CERTIFICATION</u>	
<u>EX-31.2: CERTIFICATION</u>	
<u>EX-32: CERTIFICATIONS</u>	

BASIS OF PRESENTATION:

The consolidated financial statements of Air Products and Chemicals, Inc. and its subsidiaries (the Company or registrant) included herein have been prepared by the Company, without audit, pursuant to the rules and regulations of the Securities and Exchange Commission. Certain information and footnote disclosures normally included in financial statements prepared in accordance with U.S. generally accepted accounting principles have been condensed or omitted pursuant to such rules and regulations. In the opinion of the Company, the accompanying statements reflect adjustments necessary to present fairly the financial position, results of operations and cash flows for those periods indicated, and contain adequate disclosure to make the information presented not misleading. Adjustments included herein are of a normal, recurring nature unless otherwise disclosed in the Notes to the consolidated financial statements. However, the interim results for the periods indicated herein do not reflect certain adjustments, such as the valuation of inventories on the LIFO cost basis, which can only be finally determined on an annual basis. The consolidated financial statements included herein should be read in conjunction with the financial statements and Notes thereto included in the Company's latest annual report on Form 10-K in order to fully understand the basis of presentation.

Results of operations for interim periods are not necessarily indicative of the results of operations for a full year. Reference the 2008 Outlook included on pages 23-24 in Management's Discussion and Analysis of Financial Condition and Results of Operations. Risk factors that could impact results are discussed in the Company's latest annual report on Form 10-K and under Forward-Looking Statements on page 27.

Table of Contents**PART I. FINANCIAL INFORMATION****Item 1. Financial Statements**

AIR PRODUCTS AND CHEMICALS, INC. and Subsidiaries
CONSOLIDATED BALANCE SHEETS
(Unaudited)

(Millions of dollars, except for share data)

	31 December 2007	30 September 2007
ASSETS		
CURRENT ASSETS		
Cash and cash items	\$ 96.5	\$ 40.5
Trade receivables, less allowances for doubtful accounts	1,667.5	1,578.5
Inventories	517.3	486.6
Contracts in progress, less progress billings	214.9	259.6
Prepaid expenses	61.3	108.2
Other receivables and current assets	197.8	240.1
Current assets of discontinued operations	108.5	144.9
TOTAL CURRENT ASSETS	2,863.8	2,858.4
INVESTMENT IN NET ASSETS OF AND ADVANCES TO EQUITY		
AFFILIATES	791.6	778.1
PLANT AND EQUIPMENT, at cost	14,910.2	14,600.3
Less accumulated depreciation	8,209.9	7,996.6
PLANT AND EQUIPMENT, net	6,700.3	6,603.7
GOODWILL	1,236.6	1,199.9
INTANGIBLE ASSETS, net	282.4	276.2
OTHER NONCURRENT ASSETS	867.0	638.6
NONCURRENT ASSETS OF DISCONTINUED OPERATIONS	272.6	304.6
TOTAL ASSETS	\$ 13,014.3	\$ 12,659.5
LIABILITIES AND SHAREHOLDERS EQUITY		
CURRENT LIABILITIES		
Payables and accrued liabilities	\$ 1,502.3	\$ 1,550.9
Accrued income taxes	103.6	108.6
Short-term borrowings	463.8	593.3
Current portion of long-term debt	96.0	101.1
Current liabilities of discontinued operations	58.9	68.8
TOTAL CURRENT LIABILITIES	2,224.6	2,422.7

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LONG-TERM DEBT	3,415.6	2,976.5
DEFERRED INCOME & OTHER NONCURRENT LIABILITIES	842.7	872.0
DEFERRED INCOME TAXES	735.3	705.6
NONCURRENT LIABILITIES OF DISCONTINUED OPERATIONS	9.6	9.8
TOTAL LIABILITIES	7,227.8	6,986.6
Minority interest in subsidiary companies	99.3	92.9
Minority interest of discontinued operations	84.2	84.4
TOTAL MINORITY INTEREST	183.5	177.3
COMMITMENTS AND CONTINGENCIES See Note 9		
SHAREHOLDERS EQUITY		
Common stock (par value \$1 per share; 2008 and 2007 249,455,584 shares)	249.4	249.4
Capital in excess of par value	770.2	759.5
Retained earnings	6,625.5	6,458.5
Accumulated other comprehensive loss	(82.9)	(142.9)
Treasury stock, at cost (2008 35,007,489 shares; 2007 34,099,899 shares)	(1,959.2)	(1,828.9)
TOTAL SHAREHOLDERS EQUITY	5,603.0	5,495.6
TOTAL LIABILITIES AND SHAREHOLDERS EQUITY	\$ 13,014.3	\$ 12,659.5

The accompanying notes are an integral part of these statements.

Table of Contents

AIR PRODUCTS AND CHEMICALS, INC. and Subsidiaries
CONSOLIDATED INCOME STATEMENTS
(Unaudited)

(Millions of dollars, except for share data)

	Three Months Ended 31 December	
	2007	2006
SALES	\$2,473.6	\$2,267.8
COSTS AND EXPENSES		
Cost of sales	1,788.5	1,649.7
Selling and administrative	296.8	275.4
Research and development	30.3	32.1
Pension settlement	1.4	
Other (income) expense, net	(15.4)	(6.8)
OPERATING INCOME	372.0	317.4
Equity affiliates income	25.3	27.3
Interest expense	41.0	39.1
INCOME FROM CONTINUING OPERATIONS BEFORE TAXES AND MINORITY INTEREST	356.3	305.6
Income tax provision	93.2	79.5
Minority interest in earnings of subsidiary companies	6.1	5.1
INCOME FROM CONTINUING OPERATIONS	257.0	221.0
INCOME FROM DISCONTINUED OPERATIONS, net of tax	6.7	9.3
NET INCOME	\$ 263.7	\$ 230.3
BASIC EARNINGS PER COMMON SHARE		
Income from continuing operations	\$ 1.20	\$ 1.02
Income from discontinued operations	.03	.04
Net Income	\$ 1.23	\$ 1.06
DILUTED EARNINGS PER COMMON SHARE		
Income from continuing operations	\$ 1.16	\$.99
Income from discontinued operations	.03	.04
Net Income	\$ 1.19	\$ 1.03
WEIGHTED AVERAGE OF COMMON SHARES OUTSTANDING (in millions)	214.8	216.7
WEIGHTED AVERAGE OF COMMON SHARES OUTSTANDING ASSUMING DILUTION (in millions)	222.3	223.4

DIVIDENDS DECLARED PER COMMON SHARE	Cash	\$.38	\$.34
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The accompanying notes are an integral part of these statements.

4

Table of Contents

AIR PRODUCTS AND CHEMICALS, INC. and Subsidiaries
CONSOLIDATED COMPREHENSIVE INCOME STATEMENTS
(Unaudited)

(Millions of dollars)

	Three Months Ended 31 December	
	2007	2006
NET INCOME	\$263.7	\$230.3
OTHER COMPREHENSIVE INCOME, net of tax:		
Net unrealized holding (loss) gain on investments, net of income tax (benefit) of \$(.8) and \$3.4	(1.7)	6.0
Net unrecognized (loss) gain on derivatives qualifying as hedges, net of income tax (benefit) of \$(2.0) and \$1.1	(4.8)	2.6
Foreign currency translation adjustments, net of income tax (benefit) of \$(5.5) and \$(23.3)	55.6	86.0
Change in pension funded status, net of income tax of \$3.6	10.9	
TOTAL OTHER COMPREHENSIVE INCOME	60.0	94.6
COMPREHENSIVE INCOME	\$323.7	\$324.9

Amounts reclassified from other comprehensive income into earnings in 2008 and 2007 were not material.
The accompanying notes are an integral part of these statements.

Table of Contents

AIR PRODUCTS AND CHEMICALS, INC. and Subsidiaries
CONSOLIDATED STATEMENTS OF CASH FLOWS
(Unaudited)

(Millions of dollars)

	Three Months Ended 31 December	
	2007	2006
OPERATING ACTIVITIES FROM CONTINUING OPERATIONS		
Net Income	\$ 263.7	\$ 230.3
Income from discontinued operations, net of tax	(6.7)	(9.3)
Income from Continuing Operations	257.0	221.0
Adjustments to reconcile income to cash provided by operating activities:		
Depreciation and amortization	218.0	192.1
Deferred income taxes	20.8	15.3
Undistributed earnings of unconsolidated affiliates	(7.2)	(13.8)
Gain on sale of assets and investments	(6.2)	(.3)
Share-based compensation	17.1	16.6
Noncurrent capital lease receivables	(47.7)	(47.0)
Other	(30.1)	(21.1)
Working capital changes that provided (used) cash, excluding effects of acquisitions and divestitures:		
Trade receivables	(77.4)	(36.6)
Inventories	(27.3)	(16.0)
Contracts in progress	47.0	52.5
Prepaid expenses	47.0	6.1
Payables and accrued liabilities	(85.9)	(224.9)
Other	42.9	6.5
CASH PROVIDED BY OPERATING ACTIVITIES (a)	368.0	150.4
INVESTING ACTIVITIES FROM CONTINUING OPERATIONS		
Additions to plant and equipment (b)	(271.2)	(232.1)
Acquisitions, less cash acquired	(1.4)	
Investment in and advances to unconsolidated affiliates		(1.5)
Proceeds from sale of assets and investments	9.0	12.5
Proceeds from insurance settlements		14.9
Change in restricted cash	(135.7)	
Other	(.8)	(.4)
CASH USED FOR INVESTING ACTIVITIES	(400.1)	(206.6)
FINANCING ACTIVITIES FROM CONTINUING OPERATIONS		
Long-term debt proceeds	160.5	53.8
Payments on long-term debt	(41.6)	(36.2)
Net increase in commercial paper and short-term borrowings	120.1	226.2

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Dividends paid to shareholders	(81.9)	(73.9)
Purchase of Treasury Stock	(189.7)	(133.5)
Proceeds from stock option exercises	33.0	37.0
Excess tax benefit from share-based compensation/other	21.5	6.7
CASH PROVIDED BY FINANCING ACTIVITIES	21.9	80.1

6

Table of Contents

AIR PRODUCTS AND CHEMICALS, INC. and Subsidiaries
CONSOLIDATED STATEMENTS OF CASH FLOWS (CONTINUED)
(Unaudited)

(Millions of dollars)

	Three Months Ended 31 December	
	2007	2006
DISCONTINUED OPERATIONS		
Cash (used for) provided by operating activities	(1.3)	9.0
Cash provided by (used for) investing activities	65.8	(6.2)
Cash used for financing activities		
CASH PROVIDED BY DISCONTINUED OPERATIONS	64.5	2.8
Effect of Exchange Rate Changes on Cash	1.7	(.4)
Increase in Cash and Cash Items	56.0	26.3
Cash and Cash Items Beginning of Year	40.5	31.0
Cash and Cash Items End of Period	\$96.5	\$57.3

(a) Pension plan contributions in 2008 and 2007 were \$69.8 and \$239.9, respectively.

(b) Excludes capital lease additions of \$.7 and \$.6 in 2008 and 2007, respectively.

The accompanying notes are an integral part of these statements.

Table of Contents

AIR PRODUCTS AND CHEMICALS, INC. and Subsidiaries
SUMMARY BY BUSINESS SEGMENTS
(Unaudited)

(Millions of dollars)

	Three Months Ended 31 December	
	2007	2006
Revenues from external customers		
Merchant Gases	\$ 897.0	\$ 740.0
Tonnage Gases	791.1	689.5
Electronics and Performance Materials	514.3	486.9
Equipment and Energy	100.3	195.6
Healthcare	170.9	155.8
Segment and Consolidated Totals	\$2,473.6	\$2,267.8
Operating income		
Merchant Gases	\$ 175.4	\$ 139.2
Tonnage Gases	111.1	95.4
Electronics and Performance Materials	66.0	49.8
Equipment and Energy	9.3	26.8
Healthcare	13.6	9.4
Segment Totals	375.4	320.6
Other	(3.4)	(3.2)
Consolidated Totals	\$ 372.0	\$ 317.4

(Millions of dollars)

	30 December 2007	30 September 2007
Identifiable assets (a)		
Merchant Gases	\$ 4,175.6	\$ 3,984.4
Tonnage Gases	3,391.4	3,328.4
Electronics and Performance Materials	2,425.0	2,435.3
Equipment and Energy	376.2	362.6
Healthcare	938.1	918.9
Segment Totals	11,306.3	11,029.6
Other	535.3	402.3
Discontinued operations	305.1	381.6

Consolidated Totals	\$12,146.7	\$11,813.5
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(a) Identifiable
assets are equal
to total assets
less investments
in and advances
to equity
affiliates.

Table of Contents

AIR PRODUCTS AND CHEMICALS, INC. and Subsidiaries
SUMMARY BY GEOGRAPHIC REGIONS
(Unaudited)

(Millions of dollars)

	Three Months Ended 31 December	
	2007	2006
Revenues from external customers		
North America	1,212.8	1,223.4
Europe	807.5	664.4
Asia	403.9	341.6
Latin America	49.4	38.4
 Total	 \$ 2,473.6	 \$ 2,267.8

Geographic information is based on country of origin. The Europe segment operates principally in Belgium, France, Germany, the Netherlands, Poland, the U.K., and Spain. The Asia segment operates principally in China, Japan, Korea, and Taiwan.

Table of Contents**AIR PRODUCTS AND CHEMICALS, INC. and Subsidiaries
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

(Millions of dollars, except for share data)

1. MAJOR ACCOUNTING POLICIES

Refer to the Company's 2007 annual report on Form 10-K for a description of major accounting policies. There have been no material changes to these accounting policies during the first quarter of 2008 other than those detailed in Note 2.

2. NEW ACCOUNTING STANDARDS**Uncertainty in Income Taxes**

The Company adopted Financial Accounting Standards Board (FASB) Interpretation No. 48, Accounting for Uncertainty in Income Taxes-an interpretation of FASB Statement No. 109, (FIN No. 48) on 1 October 2007. Upon adoption, the Company recognized a \$25.5 increase to its liability for uncertain tax positions. This increase was recorded as an adjustment to beginning retained earnings for \$13.7 and goodwill for \$11.8.

At 1 October 2007, the Company had \$94.3 of unrecognized tax benefits including \$25.9 for the payment of interest and penalties. The Company classifies interest and penalties related to unrecognized tax benefits as a component of income tax expense. At 1 October 2007, \$48.3 of the liability for unrecognized tax benefits, if recognized, would impact the effective tax rate. The Company does not anticipate any significant changes in the amount of unrecognized income tax benefits over the next twelve months.

The Company remains subject to examination in the following major tax jurisdictions for the years indicated below:

Major Tax Jurisdiction	Open Tax Fiscal Years	
North America		
United States	2005	2007
Canada	2004	2007
Europe		
United Kingdom	2005	2007
Ireland	2007	
Germany	2002	2007
Belgium	2005	2007
France	2007	
Netherlands	2005	2007
Spain	2003	2007
Asia		
Taiwan	2005	2007
Korea	2002	2007

Business Combinations and Noncontrolling Interests

In December 2007, the FASB issued FASB Statements No. 141 (revised 2007), Business Combinations, and No. 160, Noncontrolling Interests in Consolidated Financial Statements. SFAS 141R requires the acquiring entity in a business combination to recognize at full fair value all the assets acquired and liabilities assumed in the transaction; establishes the acquisition-date fair value as the measurement objective for all assets acquired and liabilities assumed; and requires the acquirer to disclose information needed to evaluate and understand the nature and financial effect of the business combination. SFAS No. 160 requires entities to report noncontrolling (minority) interests in subsidiaries as equity in the consolidated financial statements. These Statements are effective for fiscal years beginning after 15 December 2008 and are to be applied prospectively. The Company is currently evaluating the effect of these Statements.

Table of Contents**3. GLOBAL COST REDUCTION PLAN**

The following table summarizes changes to the carrying amount of the accrual for the global cost reduction plan for the three months ended 31 December 2007:

	Severance and Other Benefits
Accrual Balance at 30 September 2007	\$ 8.4
Noncash Expenses	
Cash Expenditures	(4.5)
Accrual Balance at 31 December 2007	\$ 3.9

4. DISCONTINUED OPERATIONS

The High Purity Process Chemicals (HPPC) business and the Polymer Emulsions business have been accounted for as discontinued operations. The results of operations and cash flows of these businesses have been removed from the results of continuing operations for all periods presented. The balance sheet items of discontinued operations have been reclassified and are segregated in the consolidated balance sheets.

HPPC Business

In September 2007, the Company's Board of Directors approved the sale of its HPPC business, which had previously been reported as part of the Electronics and Performance Materials operating segment. The Company's HPPC business consisted of the development, manufacture, and supply of high-purity process chemicals used in the fabrication of integrated circuits in the United States and Europe. The Company wrote down the assets of the HPPC business to net realizable value as of 30 September 2007, resulting in a loss of \$15.3 (\$9.3 after-tax, or \$.04 per share) in the fourth quarter of 2007.

In October 2007, the Company executed an agreement of sale with KMG Chemicals, Inc. The sale closed on 31 December 2007 for cash proceeds of \$69.3 and included manufacturing facilities in the United States and Europe. Certain receivables and inventories will be sold to KMG Chemicals, Inc. subsequent to 31 December 2007. In the first quarter of fiscal 2008, this business generated sales of \$22.9 and income, net of tax, of \$.2. Also, the Company recorded an additional loss of \$.5 (\$.3 after-tax) on the sale of the business. In the first quarter of fiscal 2007, this business generated sales of \$22.9 and income, net of tax, of \$.7.

Assets and liabilities of the discontinued HPPC business are summarized below:

	31 December 2007	30 September 2007
Trade receivables, less allowances	\$ 2.5	\$ 13.1
Inventories	2.1	15.4
Total Current Assets	\$ 4.6	\$ 28.5
Plant and equipment, net	\$	\$ 33.5
Goodwill		5.4
Other noncurrent assets		.9
Total Noncurrent Assets	\$	\$ 39.8
Payables and accrued liabilities	\$ 6.2	\$ 6.9

Total Current Liabilities	\$ 6.2	\$ 6.9
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Polymer Emulsions Business

The Company announced it was exploring the sale of its Polymer Emulsions business in 2006 as part of the Company's ongoing portfolio management activities. In November 2007, the Company's Board of Directors granted the Company the authority to sell this business to its partner based on achieving certain contractual terms

Table of Contents

and conditions. On 11 December 2007, the Company announced it had signed a definitive agreement to sell its interest in its vinyl acetate ethylene (VAE) polymers joint ventures to Wacker Chemie AG, its long-time joint venture partner. As part of the agreement, the Company will receive \$265 and Wacker's interest in the Elkton, Md., and Piedmont, S.C., production facilities and their related businesses. The sale, which is subject to regulatory approvals and customary closing conditions, is expected to close in the second quarter of fiscal year 2008. The Company anticipates a gain on the sale of the Polymer Emulsions business in the range of \$65 to \$85 (\$42 to \$55 after-tax).

The sale consists of the global VAE polymers operations including production facilities located in Calvert City, Ky.; South Brunswick, N.J.; Cologne, Germany; and Ulsan, Korea; and commercial and research capabilities in Allentown, Pa., and Burghausen, Germany. The business produces VAE for use in adhesives, paints and coatings, paper and carpet applications.

Upon completion of the sale, the Company will assume full ownership of the Elkton and Piedmont plants and related North American atmospheric emulsions and global pressure sensitive adhesives business. The Company intends to sell these businesses.

The operating results of the Polymer Emulsions business including the Elkton and Piedmont facilities have been classified as discontinued operations and are summarized below:

	Three Months Ended 31 December 2007	Three Months Ended 31 December 2006
Sales	\$ 151.2	\$ 141.8
Income before taxes	\$ 10.9	\$ 13.8
Income tax provision	4.1	5.2
Income from operations of discontinued operations, net of tax	\$ 6.8	\$ 8.6

Details of balance sheet items for the Polymer Emulsions business including the Elkton and Piedmont facilities are summarized below:

	31 December 2007	30 September 2007
Cash and cash items	\$.7	\$ 1.8
Trade receivables, less allowances	64.5	78.5
Inventories	36.9	30.1
Prepaid expenses	1.6	1.3
Other receivables	.2	4.7
Total Current Assets	\$ 103.9	\$ 116.4
Investment in net assets of and advances to equity affiliates	\$ 76.0	\$ 67.9
Plant and equipment, net	164.3	166.3
Goodwill	30.3	29.7
Other noncurrent assets	2.0	.9
Total Noncurrent Assets	\$ 272.6	\$ 264.8

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Payables and accrued liabilities	\$ 47.7	\$ 53.4
Accrued income taxes	1.9	2.2
Short-term borrowings	\$ 3.1	6.3
Total Current Liabilities	\$ 52.7	\$ 61.9

Table of Contents

	31 December 2007	30 September 2007
Deferred income taxes	\$ 6.9	\$ 6.9
Other noncurrent liabilities	2.7	2.9
Total Noncurrent Liabilities	\$ 9.6	\$ 9.8
Minority Interest	\$ 84.2	\$ 84.4
Cumulative Translation Adjustments (accumulated other comprehensive income)	\$ 52.2	\$ 45.9

5. GOODWILL

Changes to the carrying amount of consolidated goodwill by segment for the quarter ended 31 December 2007 are as follows:

	30 September 2007	Adoption of FIN No. 48	Currency Translation and Other	31 December 2007
Merchant Gases	\$ 475.7	\$ 9.4	\$22.1	\$ 507.2
Tonnage Gases	22.4			