AIR PRODUCTS & CHEMICALS INC /DE/
Form 10-Q
July 24, 2014
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UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

FORM 10-Q

(Mark One)

x QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the quarterly period ended 30 June 2014

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	23-1274455
(State or Other Jurisdiction of Incorporation or Organization)	(I.R.S. Employer Identification No.)
7201 Hamilton Boulevard, Allentown, Pennsylvania	18195-1501
(Address of Principal Executive Offices)	(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 _ü_ 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 (§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 _ü_ 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 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 _ü_ 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 Exchange Act). YES ___ NO _ü_

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 30 June 2014
Common Stock, $1 par value	213,015,723

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AIR PRODUCTS AND CHEMICALS, INC. and Subsidiaries

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AIR PRODUCTS AND CHEMICALS, INC. and Subsidiaries

CONSOLIDATED INCOME STATEMENTS

(Unaudited)

	Three Months Ended 30 June		Nine Months Ended 30 June	
(Millions of dollars, except for share data)	2014	2013	2014	2013
Sales	$ 2,634.6	$ 2,547.3	$ 7,762.0	$ 7,593.9
Cost of sales	1,918.7	1,875.5	5,702.2	5,589.2
Selling and administrative	272.0	271.3	816.3	806.1
Research and development	33.8	33.5	100.5	99.1
Other income (expense), net	3.7	16.1	41.1	45.7
Operating Income	413.8	383.1	1,184.1	1,145.2
Equity affiliates income	43.1	44.2	111.7	125.4
Interest expense	31.3	35.4	96.1	106.4
Income from Continuing Operations before Taxes	425.6	391.9	1,199.7	1,164.2
Income tax provision	102.1	94.1	288.7	282.1
Income from Continuing Operations	323.5	297.8	911.0	882.1
Income from Discontinued Operations, net of tax		.6	3.1	3.1
Net Income	323.5	298.4	914.1	885.2
Less: Net Income Attributable to Noncontrolling Interests	9.5	10.0	26.4	28.1
Net Income Attributable to Air Products	$ 314.0	$ 288.4	$ 887.7	$ 857.1
Net Income Attributable to Air Products				
Income from continuing operations	$ 314.0	$ 287.8	$ 884.6	$ 854.0
Income from discontinued operations		.6	3.1	3.1
Net Income Attributable to Air Products	$ 314.0	$ 288.4	$ 887.7	$ 857.1
Basic Earnings Per Common Share Attributable to Air Products				
Income from continuing operations	$ 1.47	$ 1.38	$ 4.17	$ 4.08
Income from discontinued operations			.01	.02
Net Income Attributable to Air Products	$ 1.47	$ 1.38	$ 4.18	$ 4.10
Diluted Earnings Per Common Share Attributable to Air Products				
Income from continuing operations	$ 1.46	$ 1.36	$ 4.12	$ 4.03
Income from discontinued operations			.01	.01
Net Income Attributable to Air Products	$ 1.46	$ 1.36	$ 4.13	$ 4.04
Weighted Average Common Shares Basic (in millions)	212.9	209.4	212.4	209.3
Weighted Average Common Shares Diluted (in millions)	215.4	211.9	214.9	211.9
Dividends Declared Per Common Share Cash	$ .77	$ .71	$ 2.25	$ 2.06

The accompanying notes are an integral part of these statements.

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AIR PRODUCTS AND CHEMICALS, INC. and Subsidiaries

CONSOLIDATED COMPREHENSIVE INCOME STATEMENTS

(Unaudited)

	Three Months Ended 30 June	
(Millions of dollars)	2014	2013
Net Income	$ 323.5	$ 298.4
Other Comprehensive Income, net of tax:		
Translation adjustments, net of tax of $4.0 and ($6.8)	108.0	(99.8)
Net (loss) gain on derivatives, net of tax of ($8.2) and $5.5	(16.9)	12.0
Pension and postretirement benefits, net of tax of $3.5		5.8
Reclassification adjustments:		
Currency translation adjustment		(.6)
Derivatives, net of tax of $.2 and ($.1)	.9	(2.1)
Pension and postretirement benefits, net of tax of $9.5 and $14.6	20.3	27.1
Total Other Comprehensive Income (Loss)	112.3	(57.6)
Comprehensive Income	435.8	240.8
Net Income Attributable to Noncontrolling Interests	9.5	10.0
Other Comprehensive Income (Loss) Attributable to Noncontrolling Interests	2.2	(1.4)
Comprehensive Income Attributable to Air Products	$ 424.1	$ 232.2

	Nine Months Ended 30 June	
(Millions of dollars)	2014	2013
Net Income	$ 914.1	$ 885.2
Other Comprehensive Income, net of tax:		
Translation adjustments, net of tax of ($17.7) and ($7.1)	53.8	(184.2)
Net gain on derivatives, net of tax of ($2.9) and $10.9	.8	25.5
Pension and postretirement benefits, net of tax of $3.5		5.8
Reclassification adjustments:		
Currency translation adjustment		(.6)
Derivatives, net of tax of ($7.8) and ($2.3)	(21.8)	(9.8)
Pension and postretirement benefits, net of tax of $28.7 and $40.4	60.9	75.7
Total Other Comprehensive Income (Loss)	93.7	(87.6)
Comprehensive Income	1,007.8	797.6
Net Income Attributable to Noncontrolling Interests	26.4	28.1
Other Comprehensive Loss Attributable to Noncontrolling Interests	(2.4)	(3.1)
Comprehensive Income Attributable to Air Products	$ 983.8	$ 772.6

The accompanying notes are an integral part of these statements.

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AIR PRODUCTS AND CHEMICALS, INC. and Subsidiaries

CONSOLIDATED BALANCE SHEETS

(Unaudited)

(Millions of dollars, except for share data)	30 June 2014	30 September 2013
Assets		
Current Assets		
Cash and cash items	$ 337.6	$ 450.4
Trade receivables, net	1,612.7	1,544.3
Inventories	690.2	706.1
Contracts in progress, less progress billings	157.5	182.3
Prepaid expenses	115.6	121.1
Other receivables and current assets	426.2	432.4
Current assets of discontinued operations		2.5
Total Current Assets	3,339.8	3,439.1
Investment in net assets of and advances to equity affiliates	1,256.3	1,195.5
Plant and equipment, at cost	20,447.3	19,529.9
Less: accumulated depreciation	10,868.2	10,555.9
Plant and equipment, net	9,579.1	8,974.0
Goodwill	1,612.5	1,653.8
Intangible assets, net	665.6	717.3
Noncurrent capital lease receivables	1,436.6	1,476.9
Other noncurrent assets	426.3	393.5
Total Noncurrent Assets	14,976.4	14,411.0
Total Assets	$ 18,316.2	$ 17,850.1
Liabilities and Equity		
Current Liabilities		
Payables and accrued liabilities	$ 1,892.3	$ 1,944.9
Accrued income taxes	78.8	63.0
Short-term borrowings	1,115.2	709.9
Current portion of long-term debt	69.8	507.4
Current liabilities of discontinued operations		2.4
Total Current Liabilities	3,156.1	3,227.6
Long-term debt	4,951.0	5,056.3
Other noncurrent liabilities	1,153.2	1,164.3
Deferred income taxes	858.3	827.2
Total Noncurrent Liabilities	6,962.5	7,047.8
Total Liabilities	10,118.6	10,275.4
Commitments and Contingencies See Note 11		
Redeemable Noncontrolling Interest	341.4	375.8
Air Products Shareholders Equity		
Common stock (par value $1 per share; issued 2014 and 2013 249,455,584 shares)	249.4	249.4
Capital in excess of par value	828.8	799.2
Retained earnings	10,053.5	9,646.4
Accumulated other comprehensive loss	(924.5)	(1,020.6)
Treasury stock, at cost (2014 36,439,861 shares; 2013 38,276,327 shares)	(2,510.5)	(2,632.3)
Total Air Products Shareholders Equity	7,696.7	7,042.1
Noncontrolling Interests	159.5	156.8
Total Equity	7,856.2	7,198.9
Total Liabilities and Equity	$ 18,316.2	$ 17,850.1

The accompanying notes are an integral part of these statements.

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AIR PRODUCTS AND CHEMICALS, INC. and Subsidiaries

CONSOLIDATED STATEMENTS OF CASH FLOWS

(Unaudited)

	Nine Months Ended 30 June	
(Millions of dollars)	2014	2013
Operating Activities		
Net Income	$ 914.1	$ 885.2
Less: Net income attributable to noncontrolling interests	26.4	28.1
Net income attributable to Air Products	887.7	857.1
Income from discontinued operations	(3.1)	(3.1)
Income from continuing operations attributable to Air Products	884.6	854.0
Adjustments to reconcile income to cash provided by operating activities:		
Depreciation and amortization	702.3	674.4
Deferred income taxes	69.8	8.4
Undistributed earnings of unconsolidated affiliates	(36.7)	(47.6)
Share-based compensation	32.5	33.0
Noncurrent capital lease receivables	11.8	(124.2)
Other adjustments	102.8	(96.9)
Working capital changes that provided (used) cash, excluding effects of acquisitions and divestitures:		
Trade receivables	(77.1)	(88.9)
Inventories	12.6	68.5
Contracts in progress, less progress billings	(1.1)	(3.9)
Other receivables	(3.1)	(65.9)
Payables and accrued liabilities	(125.6)	(139.8)
Other working capital	11.2	(19.9)
Cash Provided by Operating Activities	1,584.0	1,051.2
Investing Activities		
Additions to plant and equipment	(1,264.9)	(1,115.4)
Acquisitions, less cash acquired		(125.6)
Proceeds from sale of assets and investments	34.0	25.4
Other investing activities	.8	(2.6)
Cash Used for Investing Activities	(1,230.1)	(1,218.2)
Financing Activities		
Long-term debt proceeds	57.3	522.1
Payments on long-term debt	(591.7)	(415.7)
Net increase in commercial paper and short-term borrowings	422.7	780.8
Dividends paid to shareholders	(463.7)	(416.8)
Purchase of treasury shares		(461.6)
Proceeds from stock option exercises	106.5	133.1
Excess tax benefit from share-based compensation	22.5	24.6
Payment for subsidiary shares from noncontrolling interests	(.5)	(12.6)
Other financing activities	(35.8)	(28.8)
Cash (Used for) Provided by Financing Activities	(482.7)	125.1
Discontinued Operations		
Cash provided by operating activities	.7	13.3
Cash provided by (used for) investing activities	9.8	(1.2)
Cash provided by financing activities		
Cash Provided by Discontinued Operations	10.5	12.1
Effect of Exchange Rate Changes on Cash	5.5	(5.8)
(Decrease) in Cash and Cash Items	(112.8)	(35.6)
Cash and Cash Items Beginning of Year	450.4	454.4

Cash and Cash Items End of Period	$ 337.6	$ 418.8

The accompanying notes are an integral part of these statements.

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AIR PRODUCTS AND CHEMICALS, INC. and Subsidiaries

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(Millions of dollars unless otherwise indicated, except for share data)

1. BASIS OF PRESENTATION AND MAJOR ACCOUNTING POLICIES

Refer to our 2013 Form 10-K for a description of major accounting policies. There have been no material changes to these accounting policies during the first nine months of fiscal year 2014.

The consolidated financial statements of Air Products and Chemicals, Inc. and its subsidiaries (we, our, us, the Company, Air Products, or registrant) included herein have been prepared by us, without audit, pursuant to the rules and regulations of the Securities and Exchange Commission (SEC). Certain information and footnote disclosures normally included in financial statements prepared in accordance with U.S. generally accepted accounting principles (U.S. GAAP) have been condensed or omitted pursuant to such rules and regulations. In our opinion, 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. The interim results for the periods indicated herein, however, do not reflect certain adjustments, such as the valuation of inventories on the last-in, first-out (LIFO) cost basis, which are only finally determined on an annual basis. The consolidated financial statements and related Notes included herein should be read in conjunction with the financial statements and Notes thereto included in our latest 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.

2. NEW ACCOUNTING GUIDANCE

Accounting Guidance Implemented in 2014

Amounts Reclassified out of Accumulated Other Comprehensive Income

In February 2013, the Financial Accounting Standards Board (FASB) issued disclosure guidance to improve the transparency of items reclassified out of accumulated other comprehensive income to net income. The guidance requires an entity to present, in a single location, information about the amounts reclassified out of accumulated other comprehensive income, by component, including the income statement line items affected by the reclassification. This disclosure guidance was effective for us beginning in the first quarter of fiscal year 2014 and did not have a material impact on our consolidated financial statements. Refer to Note 14, Accumulated Other Comprehensive Loss, for the required disclosures.

Cumulative Translation Adjustment

In March 2013, the FASB issued an update to clarify existing guidance for the release of cumulative translation adjustments into net income when a parent sells all or a part of its investment in a foreign entity or achieves a business combination of a foreign entity in stages. We adopted this guidance, which is to be applied prospectively, at the beginning of fiscal year 2014. This guidance did not have an impact on our consolidated financial statements.

New Accounting Guidance to be Implemented

Unrecognized Tax Benefits

In July 2013, the FASB issued guidance to require standard presentation of an unrecognized tax benefit when a carryforward related to net operating losses or tax credits exists. This guidance will be applied prospectively and is effective for us beginning in the first quarter of fiscal year 2015, with early adoption permitted. We do not expect this guidance to have a material impact on our consolidated financial statements.

Discontinued Operations

In April 2014, the FASB issued an update to change the criteria for determining which disposals qualify as a discontinued operation and to expand related disclosure requirements. Under the new guidance, a disposal is required to be reported in discontinued operations if the disposal represents a strategic shift that has or will have a major effect on operations and financial results. This guidance will be effective prospectively for new disposals and new disposal groups classified as held for sale beginning in fiscal year 2016, with early adoption permitted.

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Revenue Recognition

In May 2014, the FASB issued guidance based on the principle that revenue is recognized in an amount which the entity expects to be entitled in exchange for the transfer of goods or services. This guidance is effective for us beginning in fiscal year 2018 and can be adopted either retrospectively or as a cumulative-effect adjustment as of the date of adoption. Early adoption is not permitted. We are currently evaluating the adoption alternatives and impact that this update will have on our consolidated financial statements.

Share-based Compensation

In June 2014, the FASB issued guidance clarifying that share-based compensation performance targets that could be achieved after the requisite service period should be treated as a performance condition that affects vesting, rather than a condition that affects the grant-date fair value of the award. This guidance is effective for us beginning in fiscal year 2017, with early adoption permitted. We do not expect this guidance to have a material impact on our consolidated financial statements.

3. DISCONTINUED OPERATIONS

During the second quarter of 2012, the Board of Directors authorized the sale of our Homecare business, which had previously been reported as part of the Merchant Gases operating segment.

In the third quarter of 2012, we sold the majority of our Homecare business to The Linde Group for total sale proceeds of 590 million ($777). This amount included contingent proceeds of 110 million ($144) related to the outcome of certain retender arrangements. As of 30 June 2014, this liability is reflected in payables and accrued liabilities on our consolidated balance sheet. Based on the outcome of the retenders, the Company was contractually required to return the proceeds to The Linde Group. We settled this liability on 17 July 2014.

In the first quarter of 2014, we sold the remaining portion of the Homecare business, which was primarily in the United Kingdom and Ireland, for £6.1 million ($9.8) and recorded a gain on sale of $2.4. We entered into an operations guarantee related to the obligations under certain homecare contracts assigned in connection with the transaction. Our maximum potential payment under the guarantee is £20 million (approximately $34 at 30 June 2014), and our exposure will be extinguished by 2020. The fair value of the guarantee is not material.

The results of discontinued operations are summarized below:

	Three Months Ended 30 June		Nine Months Ended 30 June	
	2014	2013	2014	2013
Sales	$	$ 12.7	$ 8.5	$ 40.0
Income before taxes	$	$ .5	$ .7	$ 3.3
Income tax provision		(.1)		.2
Income from operations of discontinued operations		.6	.7	3.1
Gain on sale of business, net of tax			2.4	
Income from Discontinued Operations, net of tax	$	$ .6	$ 3.1	$ 3.1

The assets and liabilities classified as discontinued operations for the Homecare business at 30 September 2013 consisted of $2.5 in trade receivables, net, and $2.4 in payables and accrued liabilities. As of 30 June 2014, no assets or liabilities were classified as discontinued operations.

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4. BUSINESS RESTRUCTURING AND COST REDUCTION PLANS

2013 Plan

During the fourth quarter of 2013, we recorded an expense of $231.6 ($157.9 after-tax, or $.74 per share) reflecting actions to better align our cost structure with current market conditions. The asset and contract actions primarily impacted the Electronics business due to continued weakness in the photovoltaic (PV) and light-emitting diode (LED) markets. The severance and other contractual benefits primarily impacted our Merchant Gases business and corporate functions in response to weaker than expected business conditions in Europe and Asia, reorganization of our operations and functional areas, and previously announced senior executive changes. The planned actions are expected to be completed by the end of fiscal year 2014.

The following table summarizes the carrying amount of the accrual for the 2013 plan at 30 June 2014:

	Severance and Other Benefits	Asset Actions	Contract Actions/Other	Total
2013 Charge	$ 71.9	$ 100.4	$ 59.3	$ 231.6
Amount reflected in pension liability	(6.9)			(6.9)
Noncash expenses		(100.4)		(100.4)
Cash expenditures	(3.0)		(58.5)	(61.5)
Currency translation adjustment	.4			.4
30 September 2013	$ 62.4	$	$ .8	$ 63.2
Cash expenditures	(31.3)		(.8)	(32.1)
Currency translation adjustment	.1			.1
Accrued balance	$ 31.2	$	$	$ 31.2

2012 Plans

In 2012, we recorded an expense of $327.4 ($222.4 after-tax, or $1.03 per share) for business restructuring and cost reduction plans in our Polyurethane Intermediates, Electronics, and European Merchant businesses. As of 30 September 2013, the planned actions were substantially complete.

5. BUSINESS COMBINATIONS

2013 Business Combinations

We completed two acquisitions during the third quarter of 2013. The acquisitions were accounted for as business combinations, and their results of operations were consolidated within their respective segments after the acquisition dates. The aggregate purchase price, net of cash acquired, for these acquisitions was $134.

On 31 May 2013, we acquired EPCO Carbondioxide Products, Inc. (EPCO), the largest independent U.S. producer of liquid carbon dioxide (CO_2). This acquisition expanded our North American offerings of bulk industrial process gases in the Merchant Gases segment. In addition, we acquired Wuxi Chem-Gas Company, Ltd. (WCG) on 1 April 2013. This acquisition provided our Merchant Gases segment with additional gases presence in the Jiangsu Province of China.

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6. INVENTORIES

The components of inventories are as follows:

	30 June 2014	30 September 2013
Finished goods	$ 514.5	$ 527.3
Work in process	37.9	38.7
Raw materials, supplies and other	234.3	234.9
	$ 786.7	$ 800.9
Less: Excess of FIFO cost over LIFO cost	(96.5)	(94.8)
	$ 690.2	$ 706.1

First-in, first-out (FIFO) cost approximates replacement cost. Our inventories generally have a high turnover, and as a result, there is little difference between the original cost of an item and its current replacement cost.

7. GOODWILL

Changes to the carrying amount of consolidated goodwill by segment for the nine months ended 30 June 2014 are as follows:

	Merchant Gases	Tonnage Gases	Electronics and Performance Materials	Total
Balance at 30 September 2013	$ 1,192.0	$ 15.2	$ 446.6	$ 1,653.8
Currency translation and other	(48.7)	.7	6.7	(41.3)
Balance at 30 June 2014	$ 1,143.3	$ 15.9	$ 453.3	$ 1,612.5

Goodwill is subject to impairment testing at least annually. In addition, goodwill is tested more frequently if a change in circumstances or the occurrence of events indicates that potential impairment exists.

8. FINANCIAL INSTRUMENTS

Currency Price Risk Management

Our earnings, cash flows, and financial position are exposed to foreign currency risk from foreign currency denominated transactions and net investments in foreign operations. It is our policy to minimize our cash flow volatility from changes in currency exchange rates. This is accomplished by identifying and evaluating the risk that our cash flows will change in value due to changes in exchange rates and by executing the appropriate strategies necessary to manage such exposures. Our objective is to maintain economically balanced currency risk management strategies that provide adequate downside protection.

Forward Exchange Contracts

We enter into forward exchange contracts to reduce the cash flow exposure to foreign currency fluctuations associated with highly anticipated cash flows and certain firm commitments such as the purchase of plant and equipment. We also enter into forward exchange contracts to hedge the cash flow exposure on intercompany loans. This portfolio of forward exchange contracts consists primarily of Euros and British Pound Sterling as well as Euros and U.S. dollars. The maximum remaining term of any forward exchange contract currently outstanding and designated as a cash flow hedge at 30 June 2014 is 3.6 years.

Forward exchange contracts are also used to hedge the value of investments in certain foreign subsidiaries and affiliates by creating a liability in a currency in which we have a net equity position. The primary currency pair in this portfolio of forward exchange contracts is the Euro and U.S. dollar.

In addition to the forward exchange contracts that are designated as hedges, we utilize forward exchange contracts that are not designated as hedges. These contracts are used to economically hedge foreign currency-denominated monetary assets and liabilities, primarily working capital. The primary objective of these forward exchange contracts is to protect the value of foreign currency-denominated monetary assets and liabilities from the effects of volatility in foreign exchange rates that might occur prior to their receipt or settlement. This portfolio of forward exchange contracts comprises many different foreign currency pairs, with a profile that changes from time to time depending on business activity and sourcing decisions.

The table below summarizes our outstanding currency price risk management instruments:

	30 June 2014		30 September 2013	
	US$ Notional	Years Average Maturity	US$ Notional	Years Average Maturity
Forward exchange contracts:				
Cash flow hedges	$ 2,456.6	.4	$ 2,653.4	.6
Net investment hedges	742.4	3.1	1,231.8	2.4
Not designated	431.1	.1	751.9	.1
Total Forward Exchange Contracts	$ 3,630.1	.9	$ 4,637.1	1.0

In addition to the above, we use foreign currency-denominated debt to hedge the foreign currency exposures of our net investment in certain foreign subsidiaries. The designated foreign currency denominated debt and related accrued interest included 892.5 million ($1,222.0) and Chinese Renminbi 748.5 million ($120.7) at 30 June 2014 and 908.3 million ($1,228.4) at 30 September 2013.

Debt Portfolio Management

It is our policy to identify on a continuing basis the need for debt capital and evaluate the financial risks inherent in funding the Company with debt capital. Reflecting the result of this ongoing review, the debt portfolio and hedging program are managed with the objectives and intent to (1) reduce funding risk with respect to borrowings made by us to preserve our access to debt capital and provide debt capital as required for funding and liquidity purposes, and (2) manage the aggregate interest rate risk and the debt portfolio in accordance with certain debt management parameters.

Interest Rate Management Contracts

We enter into interest rate swaps to change the fixed/variable interest rate mix of our debt portfolio in order to maintain the percentage of fixed- and variable-rate debt within the parameters set by management. In accordance with these parameters, the agreements are used to manage interest rate risks and costs inherent in our debt portfolio. Our interest rate management portfolio generally consists of fixed to floating interest rate swaps (which are designated as fair value hedges), pre-issuance interest rate swaps and treasury locks (which hedge the interest rate risk associated with anticipated fixed-rate debt issuances and are designated as cash flow hedges), and floating to fixed interest rate swaps (which are designated as cash flow hedges). At 30 June 2014, the outstanding interest rate swaps were denominated in U.S. dollars, Euros, and Chilean Pesos. The maximum remaining term of any interest rate swap designated as a cash flow hedge is .7 years. The notional amount of the interest rate swap agreements is equal to or less than the designated debt being hedged. When interest rate swaps are used to hedge variable-rate debt, the indices of the swaps and the debt to which they are designated are the same. It is our policy not to enter into any interest rate management contracts which lever a move in interest rates on a greater than one-to-one basis.

Cross Currency Interest Rate Swap Contracts

We enter into cross currency interest rate swap contracts when our risk management function deems necessary. These contracts may entail both the exchange of fixed- and floating-rate interest payments periodically over the life of the agreement and the exchange of one currency for another currency at inception and at a specified future date. These contracts effectively convert the currency denomination of a debt instrument into another currency in which we have a net equity position while changing the interest rate characteristics of the instrument. The contracts are used to hedge either certain net investments in foreign operations or non-functional currency cash flows related to intercompany loans. The current cross currency interest rate swap portfolio consists of fixed-to-fixed swaps between U.S. dollars and Chilean Pesos, U.S. dollars and offshore Chinese Renminbi, U.S. dollars and British Pound Sterling, as well as U.S. dollars and Euros.

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The following table summarizes our outstanding interest rate management contracts and cross currency interest rate swaps:

	30 June 2014				30 September 2013			
	US$ Notional	Average Pay %	Average Receive %	Years Average Maturity	US$ Notional	Average Pay %	Average Receive %	Years Average Maturity
Interest rate swaps (fair value hedge)	$ 400.0	LIBOR	3.25%	5.1	$ 300.0	LIBOR	3.61%	5.9
Cross currency interest rate swaps (net investment hedge)	$ 371.2	3.62%	.82%	2.4	$ 310.8	3.87%	.72%	2.4
Interest rate swaps (cash flow hedge)	$ 863.6	2.70%	.53%	.5	$ 52.8	6.84%	5.64%	1.4
Cross currency interest rate swaps (cash flow hedge)	$ 446.3	3.39%	2.86%	4.3	$ 169.3	3.48%	2.53%	4.8

The table below summarizes the fair value and balance sheet location of our outstanding derivatives:

	Balance Sheet Location	30 June 2014	30 September 2013	Balance Sheet Location	30 June 2014	30 September 2013
Derivatives Designated as Hedging Instruments:						
Forward exchange contracts	Other receivables	$ 64.9	$ 52.2	Accrued liabilities	$ 42.9	$ 22.5
Interest rate management contracts	Other receivables			Accrued liabilities	19.6	3.5
Forward exchange contracts	Other noncurrent assets	.9	28.7	Other noncurrent liabilities	27.6	7.7
Interest rate management contracts	Other noncurrent assets	56.2	35.4	Other noncurrent liabilities	5.6	6.1
Total Derivatives Designated as Hedging Instruments		$ 122.0	$ 116.3		$ 95.7	$ 39.8
Derivatives Not Designated as Hedging Instruments:						
Forward exchange contracts	Other receivables	$ 1.0	$ 9.6	Accrued liabilities	$ 2.2	$ 1.5
Total Derivatives		$ 123.0	$ 125.9		$ 97.9	$ 41.3

Refer to Note 9, Fair Value Measurements, which defines fair value, describes the method for measuring fair value, and provides additional disclosures regarding fair value measurements.

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The table below summarizes the gain or loss related to our cash flow hedges, fair value hedges, net investment hedges, and derivatives not designated as hedging instruments:

	Three Months Ended 30 June							
	Foreign Currency							
	Forward Exchange Contracts		Debt		Other [A]		Total	
	2014	2013	2014	2013	2014	2013	2014	2013
Cash Flow Hedges, net of tax:								
Net gain (loss) recognized in OCI (effective portion)	$ (8.7)	$ 5.9	$	$	$ (8.2)	$ 6.1	$ (16.9)	$ 12.0
Net (gain) loss reclassified from OCI to sales/cost of sales (effective portion)	(1.2)						(1.2)	
Net (gain) loss reclassified from OCI to other income, net (effective portion)	3.0	(4.4)			(.5)	1.9	2.5	(2.5)
Net (gain) loss reclassified from OCI to interest expense (effective portion)	(.6)	.2				.2	(.6)	.4
Net (gain) loss reclassified from OCI to other income, net (ineffective portion)	.2						.2	
Fair Value Hedges:								
Net gain (loss) recognized in interest expense [B]	$	$	$	$	$ 2.8	$ (13.0)	$ 2.8	$ (13.0)
Net Investment Hedges, net of tax:								
Net gain (loss) recognized in OCI	$ 1.5	$ (4.9)	$ 4.6	$ (8.6)	$ (.9)	$ 6.0	$ 5.2	$ (7.5)
Derivatives Not Designated as Hedging Instruments:								
Net gain (loss) recognized in other income, net [C]	$ (4.7)	$ (2.1)	$	$	$	$	$ (4.7)	$ (2.1)

	Nine Months Ended 30 June							
	Foreign Currency							
	Forward Exchange Contracts		Debt		Other [A]		Total	
	2014	2013	2014	2013	2014	2013	2014	2013
Cash Flow Hedges, net of tax:								
Net gain (loss) recognized in OCI (effective portion)	$ 10.7	$ 13.6	$	$	$ (9.9)	$ 11.9	$ .8	$ 25.5
Net (gain) loss reclassified from OCI to sales/cost of sales (effective portion)	(.2)	.7					(.2)	.7
Net (gain) loss reclassified from OCI to other income, net (effective portion)	(15.6)	(12.7)			(4.2)	1.9	(19.8)	(10.8)
Net (gain) loss reclassified from OCI to interest expense (effective portion)	(1.4)	(.8)			.1	.8	(1.3)	
Net (gain) loss reclassified from OCI to other income, net (ineffective portion)	(.5)	.3					(.5)	.3
Fair Value Hedges:								
Net gain (loss) recognized in interest expense [B]	$	$	$	$	$ (.6)	$ (20.0)	$ (.6)	$ (20.0)
Net Investment Hedges, net of tax:								
Net gain (loss) recognized in OCI	$ (15.1)	$ (4.7)	$ (7.1)	$ (9.1)	$ 6.7	$ 3.7	$ (15.5)	$ (10.1)
Derivatives Not Designated as Hedging Instruments:								
Net gain (loss) recognized in other income, net [C]	$ (4.9)	$ (2.9)	$	$	$ .2	$	$ (4.7)	$ (2.9)

(A) Other includes the impact on other comprehensive income (OCI) and earnings primarily related to interest rate and cross currency interest rate swaps.

(B) The impact of fair value hedges noted above was largely offset by gains and losses resulting from the impact of changes in related interest rates on recognized outstanding debt.

(C) The impact of the non-designated hedges noted above was largely offset by gains and losses, respectively, resulting from the impact of changes in exchange rates on recognized assets and liabilities denominated in nonfunctional currencies.

The amount of cash flow hedges unrealized gains and losses at 30 June 2014 that are expected to be reclassified to earnings in the next twelve months is not material.

The cash flows related to all derivative contracts are reported in the operating activities section of the consolidated statements of cash flows.

Credit Risk-Related Contingent Features

Certain derivative instruments are executed under agreements that require us to maintain a minimum credit rating with both Standard & Poor s and Moody s. If our credit rating falls below this threshold, the counterparty to the derivative instruments has the right to request full collateralization on the derivatives net liability position. The net liability position of derivatives with credit risk-related contingent features was $19.2 as of 30 June 2014 and $10.0 as of 30 September 2013. Because our current credit rating is above the various pre-established thresholds, no collateral has been posted on these liability positions.

Counterparty Credit Risk Management

We execute all financial derivative transactions with counterparties that are highly rated financial institutions, all of which are investment grade at this time. Some of our underlying derivative agreements give us the right to require the institution to post collateral if its credit rating falls below the pre-established thresholds with Standard & Poor s or Moody s. These are the same agreements referenced in Credit Risk-Related Contingent Features above. The collateral that the counterparties would be required to post was $55.4 as of 30 June 2014 and $80.6 as of 30 September 2013. No financial institution is required to post collateral at this time, as all have credit ratings at or above the threshold.

9. FAIR VALUE MEASUREMENTS

Fair value is defined as an exit price, i.e., 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 follows:

Level 1 Quoted prices (unadjusted) in active markets for identical assets or liabilities.

Level 2 Inputs that are observable for the asset or liability, either directly or indirectly through market corroboration, for substantially the full term of the asset or liability.

Level 3 Inputs that are unobservable for the asset or liability based on our own assumptions (about the assumptions market participants would use in pricing the asset or liability).

The methods and assumptions used to measure the fair value of financial instruments are as follows:

Derivatives

The fair value of our interest rate management contracts and forward exchange contracts are quantified using the income approach and are based on estimates using standard pricing models. These models take into account the value of future cash flows as of the balance sheet date, discounted to a present value using discount factors that match both the time to maturity and currency of the underlying instruments. The computation of the fair values of these instruments is generally performed by the Company. These standard pricing models utilize inputs which are derived from or corroborated by observable market data such as interest rate yield curves and currency spot and forward rates. In addition, on an ongoing basis, we randomly test a subset of our valuations against valuations received from the transaction s counterparty to validate the accuracy of our standard pricing models. Counterparties to these derivative contracts are highly rated financial institutions.

Refer to Note 8, Financial Instruments, for a description of derivative instruments, including details on the balance sheet line classifications.

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Long-term Debt

The fair value of our debt is based on estimates using standard pricing models that take into account the value of future cash flows as of the balance sheet date, discounted to a present value using discount factors that match both the time to maturity and currency of the underlying instruments. These standard valuation models utilize observable market data such as interest rate yield curves and currency spot rates. Therefore, the fair value of our debt is classified as a level 2 measurement. We generally perform the computation of the fair value of these instruments.

The carrying values and fair values of financial instruments were as follows:

	30 June 2014		30 September 2013	
	Carrying Value	Fair Value	Carrying Value	Fair Value
Assets				
Derivatives				
Forward exchange contracts	$ 66.8	$ 66.8	$ 90.5	$ 90.5
Interest rate management contracts	56.2	56.2	35.4	35.4
Liabilities				
Derivatives				
Forward exchange contracts	$ 72.7	$ 72.7	$ 31.7	$ 31.7
Interest rate management contracts	25.2	25.2	9.6	9.6
Long-term debt, including current portion	5,020.8	5,258.0	5,563.7	5,804.1

The carrying amounts reported in the balance sheet for cash and cash items, trade receivables, payables and accrued liabilities, accrued income taxes, and short-term borrowings approximate fair value due to the short-term nature of these instruments. Accordingly, these items have been excluded from the above table.

The following table summarizes assets and liabilities measured at fair value on a recurring basis in the consolidated balance sheets:

	30 June 2014				30 September 2013			
	Total	Level 1	Level 2	Level 3	Total	Level 1	Level 2	Level 3
Assets at Fair Value								
Derivatives								
Forward exchange contracts	$ 66.8	$	$ 66.8	$	$ 90.5	$	$ 90.5	$
Interest rate management contracts	56.2		56.2		35.4		35.4	
Total Assets at Fair Value	$ 123.0	$	$ 123.0	$	$ 125.9	$	$ 125.9	$

Liabilities at Fair Value