

RPM INTERNATIONAL INC/DE/  
Form 10-Q  
October 08, 2014  
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**UNITED STATES**  
**SECURITIES AND EXCHANGE COMMISSION**

Washington, D.C. 20549

**Form 10-Q**

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

For the quarterly period ended August 31, 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 No. 1-14187

**RPM International Inc.**

(Exact name of Registrant as specified in its charter)

**DELAWARE**  
(State or other jurisdiction of

incorporation or organization)

**P.O. BOX 777;**

**2628 PEARL ROAD;**

**MEDINA, OHIO**  
(Address of principal executive offices)

**02-0642224**  
(IRS Employer

Identification No.)

**44258**  
(Zip Code)

**(330) 273-5090**

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(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 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 ☒ 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	<input checked="" type="checkbox"/>	Accelerated filer	<input type="checkbox"/>
Non-accelerated filer	<input type="checkbox"/>	Smaller reporting company	<input type="checkbox"/>

(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 ☒.

As of October 6, 2014

133,476,101 Shares of RPM International Inc. Common Stock were outstanding.

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**RPM INTERNATIONAL INC. AND SUBSIDIARIES\***

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\* As used herein, the terms "RPM" and the "Company" refer to RPM International Inc. and its subsidiaries, unless the context indicates otherwise.

**Table of Contents****PART I. FINANCIAL INFORMATION****ITEM 1. FINANCIAL STATEMENTS****RPM INTERNATIONAL INC. AND SUBSIDIARIES****CONSOLIDATED BALANCE SHEETS***(In thousands, except per share amounts)*

	August 31, 2014 (Unaudited)	May 31, 2014
<b>Assets</b>		
<b>Current Assets</b>		
Cash and cash equivalents	\$ 225,025	\$ 332,868
Trade accounts receivable (less allowances of \$29,197 and \$27,641, respectively)	946,887	873,946
Inventories	628,463	613,644
Deferred income taxes	22,251	22,281
Prepaid expenses and other current assets	216,848	219,556
<b>Total current assets</b>	2,039,474	2,062,295
<b>Property, Plant and Equipment, at Cost</b>	1,193,599	1,191,676
Allowance for depreciation and amortization	(664,064)	(658,871)
<b>Property, plant and equipment, net</b>	529,535	532,805
<b>Other Assets</b>		
Goodwill	1,152,318	1,147,374
Other intangible assets, net of amortization	460,579	459,536
Deferred income taxes, non-current	7,882	7,943
Other	156,934	168,412
<b>Total other assets</b>	1,777,713	1,783,265
<b>Total Assets</b>	\$ 4,346,722	\$ 4,378,365
<b>Liabilities and Stockholders' Equity</b>		
<b>Current Liabilities</b>		
Accounts payable	\$ 408,961	\$ 525,680
Current portion of long-term debt	1,677	5,662
Accrued compensation and benefits	102,335	173,846
Accrued loss reserves	19,016	27,487
Other accrued liabilities	223,012	204,411
<b>Total current liabilities</b>	755,001	937,086
<b>Long-Term Liabilities</b>		
Long-term debt, less current maturities	1,476,349	1,345,965
Other long-term liabilities	428,576	466,659
Deferred income taxes	52,428	50,061
<b>Total long-term liabilities</b>	1,957,353	1,862,685

**Stockholders' Equity**

Preferred stock, par value \$0.01; authorized 50,000 shares; none issued		
Common stock, par value \$0.01; authorized 300,000 shares; issued 138,386 and outstanding 133,511 as of August 2014; issued 138,039 and outstanding 133,273 as of May 2014	1,335	1,333
Paid-in capital	796,041	790,102
Treasury stock, at cost	(90,095)	(85,400)
Accumulated other comprehensive (loss)	(171,829)	(156,882)
Retained earnings	900,782	833,691
<b>Total RPM International Inc. stockholders' equity</b>	<b>1,436,234</b>	<b>1,382,844</b>
Noncontrolling Interest	198,134	195,750
<b>Total equity</b>	<b>1,634,368</b>	<b>1,578,594</b>
<b>Total Liabilities and Stockholders' Equity</b>	<b>\$ 4,346,722</b>	<b>\$ 4,378,365</b>

The accompanying notes to Consolidated Financial Statements are an integral part of these statements.

**Table of Contents****RPM INTERNATIONAL INC. AND SUBSIDIARIES****CONSOLIDATED STATEMENTS OF INCOME****(Unaudited)***(In thousands, except per share amounts)*

	Three Months Ended August 31,	
	2014	2013
Net Sales	\$ 1,203,896	\$ 1,164,674
Cost of Sales	695,503	665,602
Gross Profit	508,393	499,072
Selling, General and Administrative Expenses	346,525	335,459
Interest Expense	19,415	20,725
Investment (Income), Net	(3,803)	(3,894)
Other (Income), Net	(1,822)	(434)
Income Before Income Taxes	148,078	147,216
Provision for Income Taxes	43,239	40,327
Net Income	104,839	106,889
Less: Net Income Attributable to Noncontrolling Interests	5,760	3,791
Net Income Attributable to RPM International Inc. Stockholders	\$ 99,079	\$ 103,098
Average Number of Shares of Common Stock Outstanding:		
Basic	130,094	129,344
Diluted	135,032	130,294
Earnings per Share of Common Stock Attributable to RPM International Inc. Stockholders		
Basic	\$ 0.74	\$ 0.78
Diluted	\$ 0.73	\$ 0.77
Cash Dividends Declared per Share of Common Stock	\$ 0.240	\$ 0.225

The accompanying notes to consolidated financial statements are an integral part of these statements.

**Table of Contents****RPM INTERNATIONAL INC. AND SUBSIDIARIES****CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME****(Unaudited)****(In thousands)**

	<b>Three Months Ended August 31,</b>	
	<b>2014</b>	<b>2013</b>
<b>Net Income</b>	<b>\$ 104,839</b>	<b>\$ 106,889</b>
Other comprehensive income, net of tax:		
Foreign currency translation adjustments	(21,266)	(13,414)
Pension and other postretirement benefit liability adjustments (net of tax of \$1,455 and \$1,586, respectively)	2,929	2,924
Unrealized gain (loss) on securities (net of tax of \$114 and \$(815), respectively)	76	(1,439)
Unrealized gain (loss) on derivatives (net of tax of \$(42) and \$45, respectively)	(66)	109
<b>Total other comprehensive income</b>	<b>(18,327)</b>	<b>(11,820)</b>
<b>Total Comprehensive Income</b>	<b>86,512</b>	<b>95,069</b>
<b>Less: Comprehensive Income Attributable to Noncontrolling Interests</b>	<b>2,380</b>	<b>7,627</b>
<b>Comprehensive Income Attributable to RPM International Inc. Stockholders</b>	<b>\$ 84,132</b>	<b>\$ 87,442</b>

The accompanying notes to consolidated financial statements are an integral part of these statements.

**Table of Contents****RPM INTERNATIONAL INC. AND SUBSIDIARIES****CONSOLIDATED STATEMENTS OF CASH FLOWS****(Unaudited)****(In thousands)**

	<b>Three Months Ended August 31,</b>	
	<b>2014</b>	<b>2013</b>
<b>Cash Flows From Operating Activities:</b>		
<b>Net income</b>	<b>\$ 104,839</b>	<b>\$ 106,889</b>
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation	15,048	14,431
Amortization	8,246	7,882
Deferred income taxes	1,984	(11,505)
Stock-based compensation expense	5,700	4,826
Other	(605)	(701)
Changes in assets and liabilities, net of effect from purchases and sales of businesses:		
(Increase) in receivables	(72,292)	(76,455)
(Increase) in inventory	(17,338)	(23,439)
(Increase) in prepaid expenses and other current and long-term assets	(2,307)	(7,201)
(Decrease) in accounts payable	(115,686)	(83,264)
(Decrease) in accrued compensation and benefits	(70,880)	(46,001)
(Decrease) in accrued loss reserves	(8,311)	(499)
Increase in other accrued liabilities	29,911	47,701
(Decrease) in contingent payment		(61,894)
Other	(3,542)	(232)
<b>Cash (Used For) Operating Activities</b>	<b>(125,233)</b>	<b>(129,462)</b>
<b>Cash Flows From Investing Activities:</b>		
Capital expenditures	(12,050)	(10,696)
Acquisition of businesses, net of cash acquired	(33,472)	(12,328)
Purchase of marketable securities	(5,034)	(20,152)
Proceeds from sales of marketable securities	7,512	17,786
Other	(319)	3,092
<b>Cash (Used For) Investing Activities</b>	<b>(43,363)</b>	<b>(22,298)</b>
<b>Cash Flows From Financing Activities:</b>		
Additions to long-term and short-term debt	131,907	53,218
Reductions of long-term and short-term debt	(5,468)	(1,936)
Cash dividends	(31,987)	(29,836)
Repurchase of stock	(4,695)	(4,004)
Payments of acquisition-related contingent consideration	(24,750)	
Other	244	(2,388)
<b>Cash Provided By Financing Activities</b>	<b>65,251</b>	<b>15,054</b>
<b>Effect of Exchange Rate Changes on Cash and Cash Equivalents</b>	<b>(4,498)</b>	<b>(1,945)</b>
<b>Net Change in Cash and Cash Equivalents</b>	<b>(107,843)</b>	<b>(138,651)</b>



<b>Cash and Cash Equivalents at Beginning of Period</b>	<b>332,868</b>	<b>343,554</b>
<b>Cash and Cash Equivalents at End of Period</b>	<b>\$ 225,025</b>	<b>\$ 204,903</b>

The accompanying notes to consolidated financial statements are an integral part of these statements.

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**RPM INTERNATIONAL INC. AND SUBSIDIARIES**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**August 31, 2014**

**(Unaudited)**

**NOTE 1 CONSOLIDATION, NONCONTROLLING INTERESTS AND BASIS OF PRESENTATION**

Our financial statements include all of our majority-owned subsidiaries, except for certain subsidiaries that were deconsolidated on May 31, 2010 (please refer to Note 2). We account for our investments in less-than-majority-owned joint ventures, for which we have the ability to exercise significant influence, under the equity method. Effects of transactions between related companies, except for certain subsidiaries that were deconsolidated, are eliminated in consolidation.

Noncontrolling interests are presented in our Consolidated Financial Statements as if parent company investors (controlling interests) and other minority investors (noncontrolling interests) in partially-owned subsidiaries have similar economic interests in a single entity. As a result, investments in noncontrolling interests are reported as equity in our consolidated financial statements. Additionally, our Consolidated Financial Statements include 100% of a controlled subsidiary's earnings, rather than only our share. Transactions between the parent company and noncontrolling interests are reported in equity as transactions between stockholders provided that these transactions do not create a change in control.

The accompanying unaudited consolidated financial statements have been prepared in accordance with the instructions to Form 10-Q and do not include all of the information and notes required by Generally Accepted Accounting Principles in the U.S. ( GAAP ) for complete financial statements. In our opinion, all adjustments (consisting of normal, recurring accruals) considered necessary for a fair presentation have been included for the three month periods ended August 31, 2014 and 2013. For further information, refer to the Consolidated Financial Statements and Notes included in our Annual Report on Form 10-K for the year ended May 31, 2014.

Our business is dependent on external weather factors. Historically, we have experienced strong sales and net income in our first, second and fourth fiscal quarters comprising the three month periods ending August 31, November 30 and May 31, respectively, with weaker performance in our third fiscal quarter (December through February).

**NOTE 2 DECONSOLIDATION OF SPECIALTY PRODUCTS HOLDING CORP. ( SPHC )**

On May 31, 2010, Bondex International, Inc. ( Bondex ) and its parent, SPHC, filed Chapter 11 reorganization proceedings in the United States Bankruptcy Court for the District of Delaware. SPHC is our wholly owned subsidiary. In accordance with ASC 810, when a subsidiary becomes subject to the control of a government, court, administrator, or regulator, deconsolidation of that subsidiary is generally required. We therefore deconsolidated SPHC and its subsidiaries from our balance sheet as of May 31, 2010, and eliminated the results of SPHC's operations from our results of operations beginning on that date. As a result of the Chapter 11 reorganization proceedings, on a prospective basis we will continue to account for our investment in SPHC under the cost method. See Note 13 for a description of an agreement in principle that we have entered into that would resolve all present and future asbestos personal injury claims related to Bondex and other related entities.

We had a net receivable from SPHC at May 31, 2010, that we expect may change before the bankruptcy proceedings have been finalized. The potential change relates to our indemnification of an insurer on appeal bonds pertaining to Bondex's appeal of two asbestos cases that had been underway prior to the bankruptcy filing, neither of which are material in amount. During our fiscal 2012, one of the appeal bonds was satisfied, and during fiscal 2013, the remaining appeal bond was satisfied. Included in the net amount due from SPHC are receivables and payables, which we concluded we have the right to report as a net amount based on several

**Table of Contents****RPM INTERNATIONAL INC. AND SUBSIDIARIES****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

factors, including the fact that all amounts are determinable, the balances are due to and from our subsidiaries, and we have been given reasonable assurance that netting the applicable receivables and payables would remain legally enforceable. We analyzed our net investment in SPHC as of May 31, 2010, which included a review of our advances to SPHC, an assessment of the collectibility of our net receivables due from SPHC, and a computation of the gain to be recorded upon deconsolidation based on the carrying amount of our investment in SPHC. In accordance with GAAP, the gain on deconsolidation related to the carrying amount of net assets of SPHC at May 31, 2010, was calculated in accordance with ASC 810-10-40-5, as follows:

- a) the aggregate of (1) the fair value of consideration received, (2) the fair value of any retained noncontrolling investment in the former subsidiary at the date the subsidiary is deconsolidated, and (3) the carrying amount of any noncontrolling interest in the former subsidiary; less

- b) the carrying amount of the former subsidiary's assets and liabilities.

In determining the carrying value of any retained noncontrolling investment in SPHC at the date of deconsolidation we considered several factors, including analyses of cash flows combined with various assumptions relating to the future performance of this entity and a discounted value of SPHC's recorded asbestos-related contingent obligations based on information available to us as of the date of deconsolidation. The discounted cash flow approach relies primarily on Level 3 unobservable inputs, whereby expected future cash flows are discounted using a rate that includes assumptions regarding an entity's average cost of debt and equity, incorporates expected future cash flows based on internal business plans, and applies certain assumptions about risk and uncertainties due to the bankruptcy filing. Our estimates are based upon assumptions we believe to be reasonable, but which by nature are uncertain and unpredictable. As a result of this analysis, we determined that the carrying value of our retained interest in SPHC approximated zero.

As a result of the combined analyses of each of the components of our net investment in SPHC, we recorded a net loss of approximately \$7.9 million, which was reflected in Other Expense, Net, during the fourth fiscal quarter of the year ended May 31, 2010. No changes have been made to these amounts through August 31, 2014.

**NOTE 3 NEW ACCOUNTING PRONOUNCEMENTS**

In May 2014, the FASB issued ASU 2014-09, Revenue from Contracts with Customers, which establishes a comprehensive revenue recognition standard for virtually all industries in U.S. GAAP. The new standard will apply for annual periods beginning after December 15, 2016, including interim periods therein. Early adoption is prohibited. We have not yet determined the effects, if any, adoption of this pronouncement may have on our consolidated financial statements.

**NOTE 4 INVESTMENT (INCOME), NET**

Investment (income), net, consists of the following components:

(In thousands)

**Three Months Ended**  
**August 31,**  
**2014                      2013**

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Interest (income)	\$ (1,404)	\$ (1,503)
(Gain) on sale of marketable securities	(2,116)	(2,197)
Other-than-temporary impairment on securities		51
Dividend (income)	(283)	(245)
Investment (income), net	\$ (3,803)	\$ (3,894)

**Table of Contents****RPM INTERNATIONAL INC. AND SUBSIDIARIES****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)****NOTE 5 OTHER (INCOME), NET**

Other (income), net, consists of the following components:

<i>(In thousands)</i>	<b>Three Months Ended August 31,</b>	
	<b>2014</b>	<b>2013</b>
Royalty (income) expense, net	\$ (1,217)	\$ 318
(Income) related to unconsolidated equity affiliates	(605)	(752)
Other (income), net	\$ (1,822)	\$ (434)

**NOTE 6 PENSION PLANS**

We offer defined benefit pension plans, defined contribution pension plans, as well as several unfunded health care benefit plans primarily for certain of our retired employees. The following tables provide the retirement-related benefit plans' impact on income before income taxes for the three month periods ended August 31, 2014 and 2013:

<b>Pension Benefits</b> <i>(In thousands)</i>	<b>U.S. Plans Three Months Ended August 31,</b>		<b>Non-U.S. Plans Three Months Ended August 31,</b>	
	<b>2014</b>	<b>2013</b>	<b>2014</b>	<b>2013</b>
Service cost	\$ 7,564	\$ 6,764	\$ 1,231	\$ 1,109
Interest cost	5,002	4,510	1,891	1,800
Expected return on plan assets	(6,034)	(5,190)	(2,296)	(2,095)
Amortization of:				
Prior service cost	74	83	10	1
Net actuarial losses recognized	3,472	3,306	487	623
<b>Net Periodic Benefit Cost</b>	<b>\$ 10,078</b>	<b>\$ 9,473</b>	<b>\$ 1,323</b>	<b>\$ 1,438</b>

<b>Postretirement Benefits</b> <i>(In thousands)</i>	<b>U.S. Plans Three Months Ended August 31,</b>		<b>Non-U.S. Plans Three Months Ended August 31,</b>	
	<b>2014</b>	<b>2013</b>	<b>2014</b>	<b>2013</b>
Service cost	\$ 66	\$ 81	\$ 313	\$ 327
Interest cost			308	317

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Amortization of:				
Prior service (credit)	(62)	(22)		
Net actuarial (gains) losses recognized	(34)	(29)	104	133
<b>Net Periodic Benefit Cost</b>	<b>\$ (30)</b>	<b>\$ 30</b>	<b>\$ 725</b>	<b>\$ 777</b>

We previously disclosed in our financial statements for the fiscal year ended May 31, 2014 that we expected to contribute approximately \$53.1 million to our retirement plans in the U.S. and approximately \$6.3 million to plans outside the U.S. during the current fiscal year. As of August 31, 2014, this has not changed.

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**RPM INTERNATIONAL INC. AND SUBSIDIARIES**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

We have determined that our postretirement medical plan provides prescription drug benefits that will qualify for the federal subsidy provided by the Medicare Prescription Drug, Improvement and Modernization Act of 2003. For all groups of retirees, we have assumed that the subsidy will continue indefinitely. However, effective January 1, 2014, we changed our retiree medical offering to a Medicare Advantage Plan. Under the Medicare Advantage Plan, any Part D subsidy belongs to the insurance carrier. Our results reflect this change.

**NOTE 7 INCOME TAXES**

The effective income tax rate was 29.2% for the three month period ended August 31, 2014 compared to an effective income tax rate of 27.4% for the three month period ended August 31, 2013.

The effective tax rate for the three month period ended August 31, 2014 reflects variances from the 35% federal statutory rate primarily due to the lower effective tax rate of certain of our foreign subsidiaries and the benefit of the domestic manufacturing deduction. These favorable variances from the statutory rate were partially offset by the impact of state and local income taxes.

The effective tax rate for three month period ended August 31, 2013 reflects variances from the 35% federal statutory rate primarily due to the lower effective tax rate of certain of our foreign subsidiaries and the benefit of the domestic manufacturing deduction. These favorable variances were partially offset by the impact of state and local income taxes and the net impact of valuation allowances associated with certain foreign net operating losses. Additionally, the effective tax rate for this period includes a discrete benefit related to the recognition of a foreign deferred income tax asset resulting from the merger of certain foreign subsidiaries. This one-time benefit was partially offset by the discrete impact of the enactment of a Canadian tax law change, Canada Bill C-48, Technical Tax Amendments Act, 2012, which was enacted on June 26, 2013.

As of August 31, 2014 we had unrecognized tax benefits of approximately \$15.7, of which approximately \$15.0 would impact the effective tax rate, if recognized. We recognize interest and penalties related to unrecognized benefits in income tax expense. As of August 31, 2014 the accrual for interest and penalties was approximately \$5.2 million. Unrecognized tax benefits, including interest and penalties, have been classified as other long-term liabilities unless expected to be paid in one year. We do not anticipate changes to the total unrecognized tax benefits within the next 12 months.

We, or our subsidiaries, file income tax returns in the U.S. and in various states, local and foreign jurisdictions. The Internal Revenue Service is performing a limited scope examination of fiscal year 2012 and has informed us that they may perform a limited scope examination of fiscal year 2013. In addition, with limited exceptions, we, or our subsidiaries, are generally subject to state, local and non-US income tax examinations by tax authorities for the fiscal years 2008 through 2014.

We are currently under examination, or have been notified of a planned income tax examination for various non-US, state and local jurisdictions. Although it is possible that certain income tax examinations could be resolved during the next twelve months, the timing and outcomes are uncertain.

As of August 31, 2014, we have determined, based on the available evidence, that it is uncertain whether we will be able to recognize certain deferred tax assets. Therefore, we intend to maintain the valuation allowances recorded at August 31, 2014 for those deferred tax assets until sufficient positive evidence (for example, cumulative positive foreign earnings or additional foreign source income) exists to support their reversal. These valuation allowances relate to U.S. foreign tax credit carryforwards, capital loss carryforwards, unrealized losses on securities, certain foreign net operating losses and net foreign deferred tax assets.

**Table of Contents****RPM INTERNATIONAL INC. AND SUBSIDIARIES****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)****NOTE 8 EARNINGS PER SHARE**

The following table sets forth the reconciliation of the numerator and denominator of basic and diluted earnings per share, as calculated using the two-class method, for the three month periods ended August 31, 2014 and 2013:

	<b>Three Months Ended August 31,</b>	
<i>(In thousands, except per share amounts)</i>	<b>2014</b>	<b>2013</b>
<b>Numerator for earnings per share:</b>		
Net income attributable to RPM International Inc. stockholders	\$ 99,079	\$ 103,098
Less: Allocation of earnings and dividends to participating securities	(2,179)	(2,285)
Net income available to common shareholders basic	96,900	100,813
Add: Undistributed earnings reallocated to unvested shareholders	12	12
Add: Income effect of contingently issuable shares	1,339	
Net income available to common shareholders diluted	\$ 98,251	\$ 100,825
<b>Denominator for basic and diluted earnings per share:</b>		
Basic weighted average common shares	130,094	129,344
Average diluted options	1,065	950
Net issuable common share equivalents (2)	3,873	
Total shares for diluted earnings per share	135,032	130,294
<b>Earnings Per Share of Common Stock Attributable to RPM International Inc. Stockholders:</b>		
Basic	\$ 0.74	\$ 0.78
Diluted (1)	\$ 0.73	\$ 0.77

- (1) For the quarters ended August 31, 2014 and 2013, approximately 3,034,000 and 3,097,000 shares of stock, respectively, granted under stock-based compensation plans were excluded from the calculation of diluted earnings per share, as the effect would have been anti-dilutive.
- (2) For the quarter ended August 31, 2014, represents the number of shares that would be issued if our contingently convertible notes were converted. We include these shares in the calculation of diluted EPS as the conversion of the notes may be settled, at our election, in cash, shares of our common stock, or a combination of cash and shares of our common stock.

**NOTE 9 INVENTORIES**

Inventories were composed of the following major classes:



	August 31, 2014	May 31, 2014
<i>(In thousands)</i>		
Raw material and supplies	\$ 211,650	\$ 213,981
Finished goods	416,813	399,663
<b>Total Inventory</b>	<b>\$ 628,463</b>	<b>\$ 613,644</b>

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We record restructuring charges associated with management-approved restructuring plans to either reorganize one or more of our business segments, or to remove duplicative headcount and infrastructure associated with our businesses. Restructuring charges can include severance costs to eliminate a specified number of employees, infrastructure charges to vacate facilities and consolidate operations, and contract cancellation costs. Restructuring charges are recorded based upon planned employee termination dates and site closure and consolidation plans. The timing of associated cash payments is dependent upon the type of restructuring charge and can extend over a multi-year period. We record the short-term portion of our restructuring liability in Other accrued liabilities and the long-term portion, if any, in Other long-term liabilities in our Consolidated Balance Sheets.

***Fiscal 2013 Plans***

In May 2013, we approved a restructuring plan for one of our consumer operating segments designed to eliminate duplicative processes and overhead and to exit certain processes and product lines. This restructuring plan allows management to refocus its attention on faster growing brands within the consumer operating segment. In connection with this plan, we recorded aggregate charges of approximately \$15.6 million during the year ended May 31, 2013, of which approximately \$8.2 million related to the elimination of 133 positions and approximately \$7.4 million resulted from the shutdown of two manufacturing facilities. The facilities have been closed and are awaiting sale. Related severance payments will be paid in full by approximately the third quarter of fiscal 2015. In addition, there were approximately \$3.9 million of inventory markdowns, which were reflected in Cost of Sales in our Consolidated Statements of Income during the year ended May 31, 2013.

Additionally, one of our industrial operating businesses adopted a restructuring plan designed to simplify business processes, accelerate innovation and deliver better results for customers, employees and stockholders. This plan eliminated approximately 34 positions. Severance payments will be paid out in full generally by the first half of fiscal 2015. In connection with the plan, we recorded aggregate charges of approximately \$4.5 million during the year ended May 31, 2013, all of which relates to workforce reductions.

The following table includes the changes in our accrued restructuring balances:

<i>(In thousands)</i>	<b>Employee Severance</b>	<b>Other</b>	<b>Total</b>
<b>Balance at May 31, 2014</b>	\$ 2,082	\$ 381	\$ 2,463
Cash payments	(492)	(126)	(618)
Noncash and foreign exchange impacts	(35)	(14)	(49)
<b>Balance at August 31, 2014</b>	\$ 1,555	\$ 241	\$ 1,796

**Table of Contents****RPM INTERNATIONAL INC. AND SUBSIDIARIES****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)****NOTE 11 MARKETABLE SECURITIES**

The following tables summarize marketable securities held at August 31, 2014 and May 31, 2014 by asset type:

	Available-For-Sale Securities			Fair Value (Net Carrying Amount)
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	
<i>(In thousands)</i>				
<b>August 31, 2014</b>				
Equity securities:				
Stocks foreign	\$ 2,315	\$ 887	\$ (25)	\$ 3,177
Stocks domestic	30,867	7,704	(153)	38,418
Mutual funds foreign	30,443	2,285		32,728
Mutual funds domestic	43,701	1,783	(1,001)	44,483
Total equity securities	107,326	12,659	(1,179)	118,806
Fixed maturity:				
U.S. treasury and other government	20,494	127	(228)	20,393
Corporate bonds	1,474	219	(4)	1,689
Foreign bonds	38	1		39
Mortgage-backed securities	84	53		137
Total fixed maturity securities	22,090	400	(232)	22,258
Total	\$ 129,416	\$ 13,059	\$ (1,411)	\$ 141,064

	Available-For-Sale Securities			Fair Value (Net Carrying Amount)
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	
<i>(In thousands)</i>				
<b>May 31, 2014</b>				
Equity securities:				
Stocks foreign	\$ 984	\$ 669	\$ (20)	\$ 1,633
Stocks domestic	31,071	8,965	(132)	39,904
Mutual funds foreign	30,541	2,799		33,340
Mutual funds domestic	44,242	1,790	(1,109)	44,923
Total equity securities	106,838	14,223	(1,261)	119,800
Fixed maturity:				

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U.S. treasury and other government	21,156	152	(164)	21,144
Corporate bonds	1,544	212		1,756
Foreign bonds	37	3		40
Mortgage-backed securities	85	55		140
<b>Total fixed maturity securities</b>	<b>22,822</b>	<b>422</b>	<b>(164)</b>	<b>23,080</b>
<b>Total</b>	<b>\$ 129,660</b>	<b>\$ 14,645</b>	<b>\$ (1,425)</b>	<b>\$ 142,880</b>

Marketable securities, included in other current and long-term assets totaling \$76.9 million and \$64.2 million at August 31, 2014, respectively, and included in other current and long-term assets totaling \$71.9 million and \$71.0 million at May 31, 2014, respectively, are composed of available-for-sale securities and are reported at fair value. We carry a portion of our marketable securities portfolio in long-term assets since they are generally held for the settlement of our general and product liability insurance claims processed through our wholly owned captive insurance subsidiaries.

**Table of Contents****RPM INTERNATIONAL INC. AND SUBSIDIARIES****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

Marketable securities are composed of available-for-sale securities and are reported at fair value. Realized gains and losses on sales of investments are recognized in net income on the specific identification basis. Changes in the fair values of securities that are considered temporary are recorded as unrealized gains and losses, net of applicable taxes, in accumulated other comprehensive income (loss) within stockholders' equity. Other-than-temporary declines in market value from original cost are reflected in operating income in the period in which the unrealized losses are deemed other than temporary. In order to determine whether other-than-temporary declines in market value have occurred, the duration of the decline in value and our ability to hold the investment are considered in conjunction with an evaluation of the strength of the underlying collateral and the extent to which the investment's amortized cost or cost, as appropriate, exceeds its related market value.

Gross gains realized on sales of investments were \$2.1 million and \$2.2 million, respectively, for the quarters ended August 31, 2014 and 2013, respectively. During the first quarter of fiscal 2014, we recognized losses of approximately \$0.1 million for securities deemed to have other-than-temporary impairments, while we recognized no such losses during the first quarter of fiscal 2015. These amounts are included in investment (income), net in the Consolidated Statements of Income.

Summarized below are the securities we held at August 31, 2014 and 2013 that were in an unrealized loss position and that were included in accumulated other comprehensive income, aggregated by the length of time the investments had been in that position:

	<b>August 31, 2014</b>		<b>May 31, 2014</b>	
	<b>Fair Value</b>	<b>Gross Unrealized Losses</b>	<b>Fair Value</b>	<b>Gross Unrealized Losses</b>
<i>(In thousands)</i>				
Total investments with unrealized losses	\$ 41,958	\$ (1,411)	\$ 35,465	\$ (1,425)
Unrealized losses with a loss position for less than 12 months	26,504	(952)	16,611	(845)
Unrealized losses with a loss position for more than 12 months	15,454	(459)	18,854	(580)

We have reviewed all of the securities included in the table above and have concluded that we have the ability and intent to hold these investments until their cost can be recovered, based upon the severity and duration of the decline. Therefore, we did not recognize any other-than-temporary impairment losses on these investments. The unrealized losses generally relate to investments whose fair values at August 31, 2014 were less than 15% below their original cost. From time to time, we may experience significant volatility in general economic and market conditions. If we were to experience unrealized losses that were to continue for longer periods of time, or arise to more significant levels of unrealized losses within our portfolio of investments in marketable securities in the future, we may recognize additional other-than-temporary impairment losses. Such potential losses could have a material impact on our results of operations in any given reporting period. As such, we continue to closely evaluate the status of our investments and our ability and intent to hold these investments.

**Table of Contents****RPM INTERNATIONAL INC. AND SUBSIDIARIES****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

The net carrying values of debt securities at August 31, 2014, by contractual maturity, are shown below. Expected maturities may differ from contractual maturities because the issuers of the securities may have the right to prepay obligations without prepayment penalties.

<i>(In thousands)</i>	<b>Amortized Cost</b>	<b>Fair Value</b>
<b>Due:</b>		
Less than one year	\$ 2,995	\$ 2,998
One year through five years	14,715	14,638
Six years through ten years	3,261	3,292
After ten years	1,119	1,330
	<b>\$ 22,090</b>	<b>\$ 22,258</b>

**NOTE 12 FAIR VALUE MEASUREMENTS**

Financial instruments recorded on the balance sheet include cash and cash equivalents, trade accounts receivable, marketable securities, notes and accounts payable, and debt.

An allowance for anticipated uncollectible trade receivable amounts is established using a combination of specifically identified accounts to be reserved, and a reserve covering trends in collectibility. These estimates are based on an analysis of trends in collectability and past experience, but are primarily made up of individual account balances identified as doubtful based on specific facts and conditions. Receivable losses are charged against the allowance when we confirm uncollectibility.

All derivative instruments are recognized on our Consolidated Balance Sheet and measured at fair value. Changes in the fair values of derivative instruments that do not qualify as hedges and/or any ineffective portion of hedges are recognized as a gain or (loss) in our Consolidated Statement of Income in the current period. Changes in the fair value of derivative instruments used effectively as cash flow hedges are recognized in other comprehensive income (loss), along with the change in the value of the hedged item. We do not hold or issue derivative instruments for speculative purposes.

The valuation techniques utilized for establishing the fair values of assets and liabilities are based on observable and unobservable inputs. Observable inputs reflect readily obtainable data from independent sources, while unobservable inputs reflect management's market assumptions. The fair value hierarchy has three levels based on the reliability of the inputs used to determine fair value, as follows:

Level 1 Inputs Quoted prices for identical instruments in active markets.

Level 2 Inputs Quoted prices for similar instruments in active markets; quoted prices for identical or similar instruments in markets that are not active; and model-derived valuations whose inputs are observable or whose significant value drivers are observable.

Level 3 Inputs Instruments with primarily unobservable value drivers.



**Table of Contents****RPM INTERNATIONAL INC. AND SUBSIDIARIES****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

The following tables present our assets and liabilities that are measured at fair value on a recurring basis and are categorized using the fair value hierarchy.

<i>(In thousands)</i>	<b>Quoted Prices in Active Markets for Identical Assets (Level 1)</b>	<b>Significant Other Observable Inputs (Level 2)</b>	<b>Significant Unobservable Inputs (Level 3)</b>	<b>Fair Value at August 31, 2014</b>
U.S. Treasury and other government	\$	\$ 20,393	\$	\$ 20,393
Foreign bonds		39		39
Mortgage-backed securities		137		137
Corporate bonds		1,689		1,689
Stocks foreign	3,177			3,177
Stocks domestic	38,418			38,418
Mutual funds foreign		32,728		32,728
Mutual funds domestic		44,483		44,483
Foreign currency forward contract		(492)		(492)
Cross-currency swap		(13,415)		(13,415)
Contingent consideration			(55,466)	(55,466)
Total	\$ 41,595	\$ 85,562	\$ (55,466)	\$ 71,691

<i>(In thousands)</i>	<b>Quoted Prices in Active Markets for Identical Assets (Level 1)</b>	<b>Significant Other Observable Inputs (Level 2)</b>	<b>Significant Unobservable Inputs (Level 3)</b>	<b>Fair Value at May 31, 2014</b>
U.S. Treasury and other government	\$	\$ 21,144	\$	\$ 21,144
Foreign bonds		40		40
Mortgage-backed securities		140		140
Corporate bonds		1,756		1,756
Stocks foreign	1,633			1,633
Stocks domestic	39,904			39,904
Mutual funds foreign		33,340		33,340
Mutual funds domestic		44,923		44,923
Foreign currency forward contract		2,582		2,582
Cross-currency swap		(19,550)		(19,550)
Contingent consideration			(81,296)	(81,296)
Total	\$ 41,537	\$ 84,375	\$ (81,296)	\$ 44,616



Our marketable securities are composed of mainly available-for-sale securities, and are valued using a market approach. The availability of inputs observable in the market varies from instrument to instrument and depends on a variety of factors including the type of instrument, whether the instrument is actively traded, and other characteristics particular to the transaction. For most of our financial instruments, pricing inputs are readily observable in the market, the valuation methodology used is widely accepted by market participants, and the valuation does not require significant management discretion. For other financial instruments, pricing inputs are less observable in the market and may require management judgment.

Our cross-currency swap is a liability that has a fair value of \$13.4 million at August 31, 2014, which was originally designed to fix our interest and principal payments in euros for the life of our unsecured 6.70% senior notes due November 1, 2015, which resulted in an effective euro fixed-rate borrowing of 5.31%. The basis for determining the rates for this swap included three legs at the inception of the agreement: the U.S. dollar (USD) fixed rate to a USD floating rate; the euro floating to euro fixed rate; and the dollar to euro basis fixed rate at

**Table of Contents****RPM INTERNATIONAL INC. AND SUBSIDIARIES****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

inception. Therefore, we essentially exchanged fixed payments denominated in USD for fixed payments denominated in euros, paying fixed euros at 5.31% and receiving fixed USD at 6.70%. The ultimate payments are based on the notional principal amounts of \$150 million and approximately 125 million euros. There will be an exchange of the notional amounts at maturity. The rates included in this swap are based upon observable market data, but are not quoted market prices, and therefore, the cross-currency swap is considered a Level 2 liability on the fair value hierarchy. Additionally, this cross-currency swap has been designated as a hedging instrument, and is classified as other long-term liabilities in our Consolidated Balance Sheets.

At August 31, 2014, we had a foreign currency forward contract with a fair value of approximately \$0.5 million, which is classified in other accrued liabilities in our Consolidated Balance Sheets. At May 31, 2014, we had a foreign currency forward contract with a fair value of approximately \$2.6 million, which is classified in other current assets in our Consolidated Balance Sheets. Our foreign currency forward contract, which has not been designated as a hedge, was designed to reduce our exposure to the changes in the cash flows of intercompany foreign-currency-denominated loans related to changes in foreign currency exchange rates by fixing the functional currency cash flows. The foreign exchange rates included in the forward contract are based upon observable market data, but are not quoted market prices, and therefore, the forward currency forward contract is considered a Level 2 liability on the fair value hierarchy.

The contingent consideration represents the estimated fair value of the additional variable cash consideration payable in connection with recent acquisitions that is contingent upon the achievement of certain performance milestones. We estimated the fair value using expected future cash flows over the period in which the obligation is expected to be settled, and applied a discount rate that appropriately captures a market participant's view of the risk associated with the obligation, which are considered to be Level 3 inputs. During the quarter ended August 31, 2014, we reversed approximately \$1.0 million for contingent earnout targets that were not met, and we paid approximately \$24.8 million for settlements of contingent consideration obligations relating to certain performance milestones that were established in prior periods and achieved during the current period.

The carrying value of our current financial instruments, which include cash and cash equivalents, marketable securities, trade accounts receivable, accounts payable and short-term debt approximates fair value because of the short-term maturity of these financial instruments. At August 31, 2014 and May 31, 2014, the fair value of our long-term debt was estimated using active market quotes, based on our current incremental borrowing rates for similar types of borrowing arrangements, which are considered to be Level 2 inputs. Based on the analysis performed, the fair value and the carrying value of our financial instruments and long-term debt as of August 31, 2014 and May 31, 2014 are as follows:

	At August 31, 2014	
	Carrying Value	Fair Value
(In thousands)		
Cash and cash equivalents	\$ 225,025	\$ 225,025
Marketable equity securities	118,806	118,806
Marketable debt securities	22,258	22,258
Long-term debt, including current portion	1,478,026	1,575,909

  

	At May 31, 2014	
	Carrying Value	Fair Value
(In thousands)		
Cash and cash equivalents	\$ 332,868	\$ 332,868
Marketable equity securities	119,800	119,800
Marketable debt securities	23,080	23,080

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Long-term debt, including current portion	1,351,627	1,516,062
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**RPM INTERNATIONAL INC. AND SUBSIDIARIES**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

**NOTE 13 REORGANIZATION PROCEEDINGS OF CERTAIN SUBSIDIARIES**

*General* Prior to May 31, 2010, Bondex and SPHC were defendants in various asbestos-related bodily injury lawsuits filed in various state courts. These cases generally sought unspecified damages for asbestos-related diseases based on alleged exposures to asbestos-containing products.

On May 31, 2010, Bondex and its parent, SPHC, filed voluntary petitions in the U.S. Bankruptcy Court in Delaware (the Bankruptcy Court) to reorganize under chapter 11 of the Bankruptcy Code. SPHC and Bondex took this action in an effort to permanently and comprehensively resolve all pending and future asbestos-related liability claims associated with Bondex and SPHC. As a result of the filing, all litigation related to Bondex and SPHC asbestos personal injury claims has been stayed, with the exception of the cases referenced in Note 3 with respect to which the stay was lifted. The objective of the bankruptcy proceedings is to enable the filing entities to establish a section 524(g) trust accompanied by a court order that will direct all existing and future SPHC-related and Bondex-related claims to such trust, which will then compensate asbestos claimants based upon factors set forth in an approved plan of reorganization. Since the date of the filing, and in accordance with GAAP, the financial results of SPHC and Bondex have been deconsolidated from our financial results.

We have entered into an agreement in principle with the official representatives of current and future claimants that would resolve all present and future asbestos personal injury claims related to Bondex and other related entities. The agreement contemplates the filing of a plan or plans of reorganization and related documents (the Plan) with the Bankruptcy Court. A Plan was filed on September 26, 2014. The Plan is subject to approval of the claimants, as well as the Bankruptcy Court and U.S. District Court.

In addition to Bondex and SPHC, the settlement resolves all present and future asbestos personal injury claims related to Republic Powdered Metals, Inc. (Republic) and NMBFiL, Inc. (NMBFiL), both of which are indirect wholly-owned subsidiaries of RPM, that filed for Chapter 11 bankruptcy in August 2014. Both Republic and NMBFiL will remain consolidated subsidiaries, considering the short-term nature of the bankruptcy and as long as RPM maintains control, from a participating rights perspective, of the subsidiaries.

Under the terms of the agreement in principle, a trust or trusts (the Trust) will be established under Section 524(g) of the Bankruptcy Code for the benefit of current and future asbestos personal injury claimants. Upon effectiveness of the Plan (the Effective Date), the Trust will be funded with \$450 million in cash and one or more promissory notes, bearing no interest and maturing on or before the fourth anniversary of the Effective Date. The Plan shall provide for the following contributions to the Trust:

On or before the second anniversary of the Effective Date, an additional \$102.5 million in cash, RPM International stock or a combination thereof (at our discretion in this and all subsequent cases) will be deposited into the Trust;

On or before the third anniversary of the Effective Date, an additional \$120 million in cash, RPM International stock or a combination thereof will be deposited into the Trust; and

On or before the fourth anniversary of the Effective Date, a final payment of \$125 million in cash, RPM International stock or a combination thereof will be deposited into the Trust.

Of the first \$450 million payment, \$2.5 million relates to the resolution of all present and future asbestos personal injury claims related to NMBFiL. A portion of the payments due under the promissory note(s) will be secured by a right to the equity of Bondex and related chapter 11

debtor entities. All present and future asbestos personal injury claims against Bondex and the other related entities would be channeled to and paid by the Trust.

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**RPM INTERNATIONAL INC. AND SUBSIDIARIES**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

Pursuant to the terms of the agreement, the Plan must be confirmed and effective no later than October 31, 2015, otherwise simple interest at the rate of 3.45% will begin to accrue on the aggregate funding amount of the trust through the effective date of the Plan. A confirmation hearing is scheduled for December 10, 2014.

There is no guaranty that the Plan will be confirmed. If the Plan is not confirmed, the interests of SPHC, Bondex and RPM International may be significantly and adversely affected, SPHC and Bondex will remain in chapter 11, the amount of the asbestos liabilities of SPHC and Bondex will remain unresolved and the terms, timing and impact of any plan of reorganization ultimately confirmed in the cases will be unknown. If the Plan is not confirmed, the amount of SPHC's and Bondex's asbestos-related personal injury liabilities will not be resolved and will continue to be subject to substantial dispute and uncertainty as the appeals process with respect to the estimation ruling will then move forward. If the Plan is not confirmed, the amount of the asbestos personal injury liabilities could ultimately be determined to be significantly different from the amount agreed to by the parties in the agreement. This difference could be material to our financial position, cash flows and results of operations. In the event the Plan is not confirmed it is unclear whether any channeling injunction entered in connection with a plan of reorganization will extend to all non-filing affiliates of the filing entities, including RPM International.

At a hearing held on November 13, 2013, the Bankruptcy Court granted the motion of the Official Committee of Asbestos Personal Injury Claimants and the Future Claimants' Representative (collectively, the ACC/FCR) for standing to pursue SPHC estate claims against us, certain of our current and former directors and executive officers, and third party advisors. As previously disclosed, we anticipated that the ACC/FCR might be permitted to pursue claims on behalf of the SPHC and Bondex estates against us. We believe that the alleged SPHC estate claims are without merit and, if such claims are made, intend to contest them vigorously. The ACC/FCR have agreed not to proceed with any such claims unless the Plan is not confirmed.

At August 31, 2014, no amounts have been accrued for the funding of the Trust, as the Plan is subject to the approval of the claimants, as well as the Bankruptcy Court and the U.S. District Court. Once approved, the funding of the Trust will be accounted for as a business combination and will allow us to regain control of SPHC. The portion of the funding related to NMBFiL Inc. will be recognized as a charge to the consolidated income statement at the time the Plan is approved.

As previously disclosed, the Bankruptcy Court issued an opinion in May 2013 estimating the current and future asbestos claims associated with Bondex and SPHC at approximately \$1.17 billion, which represented one step in the legal process in helping to determine the amount of potential funding for a 524(g) asbestos trust. The Debtors firmly believe that the opinion substantially overstates the amount of their liability and is not supported by the facts or the law, and we and the Debtors have appealed the ruling. Those appeals have been consolidated by the District Court and, on February 7, 2014, were certified by the District Court for direct review by the U.S. Court of Appeals for the Third Circuit, but the Third Circuit declined to accept the certification. The appeals remain pending before the District Court. The ACC/FCR have also filed a motion with the District Court to dismiss the appeal on the ground that the estimation decision was not a final, appealable order. Briefing of the appeal, and the motion to dismiss the appeal, at the District Court level have been stayed pending confirmation of the Plan.

Prior to the bankruptcy filing, the filing entities had litigated and, on many occasions, settled asbestos products liability claims brought against them. The debtors paid \$92.6 million during the year ended May 31, 2010, prior to the bankruptcy filing, in connection with the litigation and settlement of asbestos claims, \$42.6 million of which consisted of defense costs. With the exception of the appeal bonds described in Note A, no claims have been paid since the bankruptcy filing and it is not contemplated that any claims will be paid until a plan of reorganization is confirmed and an asbestos trust is established and operating.

Prior to the chapter 11 bankruptcy filing, we recorded asbestos contingent liabilities that included estimations of future costs. Such estimates by their nature are subject to many uncertainties that may change over time,



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**RPM INTERNATIONAL INC. AND SUBSIDIARIES**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

including (i) the ultimate number of claims filed; (ii) the amounts required to resolve both currently known and future unknown claims; (iii) the amount of insurance, if any, available to cover such claims, including the outcome of coverage litigation against the filing entities' third-party insurers; (iv) future earnings and cash flow of the filing entities; (v) the impact of bankruptcies of other companies whose share of liability may be imposed on the filing entities under certain state liability laws; (vi) the unpredictable aspects of the litigation process including a changing trial docket and the jurisdictions in which trials are scheduled; (vii) the outcome of any such trials, including potential judgments or jury verdicts, as a result of the strategy of Bondex and SPHC to take selective cases to verdict; (viii) the lack of specific information in many cases concerning exposure to products for which Bondex, SPHC, or another of our subsidiaries is allegedly responsible, and the claimants' alleged diseases resulting from such exposure; (ix) potential changes in applicable federal and/or state tort liability law; and (x) the potential impact of various proposed structured settlement transactions. All these factors may have a material effect upon future asbestos-related liability estimates.

As a result of their bankruptcy filing, SPHC and Bondex are precluded from paying dividends to shareholders and from making payments on any pre-bankruptcy filing accounts or notes payable that are due and owing to any other entity within the RPM group of companies (the Pre-Petition Intercompany Payables) or other pre-petition creditors during the pendency of the bankruptcy case, without the Bankruptcy Court's approval. Moreover, no assurances can be given that any of the Pre-Petition Intercompany Payables will ever be paid or otherwise satisfied.

When SPHC emerges from the jurisdiction of the Bankruptcy Court, the subsequent accounting will be determined based upon the applicable circumstances and facts at such time, including the terms of any plan of reorganization.

SPHC has assessed its liquidity position as a result of the bankruptcy filing and believes that it can continue to fund its and its subsidiaries' operating activities and meet its debt and capital requirements for the foreseeable future.

*Historical Asbestos Liability Reserve* In fiscal 2006, management retained Crawford & Winiarski (C&W), an independent, third-party consulting firm with expertise in the area of asbestos valuation work, to assist it in calculating an estimate of Bondex's liability for unasserted-potential-future-asbestos-related claims. C&W's methodology to project Bondex's liability for unasserted-potential-future-asbestos-related claims included an analysis of: (a) a widely accepted forecast of the population likely to have been exposed to asbestos; (b) epidemiological studies estimating the number of people likely to develop asbestos-related diseases; (c) the historical rate at which mesothelioma incidences resulted in the payment of claims by Bondex; (d) the historical settlement averages to value the projected number of future compensable mesothelioma claims; (e) the historical ratio of mesothelioma-related indemnity payments to non-mesothelioma indemnity payments; and (f) the historical defense costs and their relationship with total indemnity payments. Based upon the results of this analysis, Bondex recorded an accrued liability for asbestos claims through 2016 as of May 31, 2006 of \$421.3 million. This amount was calculated on a pretax basis and was not discounted for the time value of money.

During the fiscal year ended May 31, 2008, the ten-year asbestos liability established as of May 31, 2006 was reviewed and evaluated. As part of that process, the credibility of epidemiological studies of Bondex's mesothelioma claims, first introduced to management by C&W some two-and-one-half years earlier, was validated. At the core of the evaluation process, and the basis of C&W's actuarial work on behalf of Bondex, is the Nicholson Study. The Nicholson Study is the most widely recognized reference in bankruptcy trust valuations, global settlement negotiations and the Congressional Budget Office's work done on the proposed FAIR Act in 2006. Based on our ongoing comparison of the Nicholson Study projections and Bondex's specific actual experience, which at that time continued to bear an extremely close correlation to the study's projections, the asbestos liability projection was extended out to the year 2028. C&W assisted in calculating an estimate of



**Table of Contents****RPM INTERNATIONAL INC. AND SUBSIDIARIES****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

our liability for unasserted-potential-future-asbestos-related claims out to 2028. C&W projected that the cost of extending the asbestos liability to 2028, coupled with an updated evaluation of Bondex's current known claims to reflect its most recent actual experience, would be \$288.1 million. Therefore, management added \$288.1 million to the existing asbestos liability, which brought Bondex's total asbestos-related balance sheet liabilities at May 31, 2008 to \$559.7 million. On May 30, 2010, the day prior to the bankruptcy filing, Bondex had recorded an asbestos related product liability of \$397.7 million.

**NOTE 14 CONTINGENCIES AND OTHER ACCRUED LOSSES**

We provide, through our wholly owned insurance subsidiaries, certain insurance coverage, primarily product liability coverage, to our other subsidiaries. Excess coverage is provided by third-party insurers. Our reserves provide for these potential losses as well as other uninsured claims. Product liability reserves are established based upon actuarial calculations of potential liability using industry experience, actual historical experience and actuarial assumptions developed for similar types of product liability claims, including development factors and lag times. To the extent there is a reasonable possibility that potential losses could exceed the amounts already accrued, we believe that the amount of any such additional loss would be immaterial to our results of operations, liquidity and consolidated financial position.

We also offer warranty programs at several of our industrial businesses and have established a product warranty liability. We review this liability for adequacy on a quarterly basis and adjust it as necessary. The primary factors that could affect this liability may include changes in the historical system performance rate as well as the costs of replacement. Provision for estimated warranty costs is recorded at the time of sale and periodically adjusted, as required, to reflect actual experience. It is probable that we will incur future losses related to warranty claims we have received but that have not been fully investigated and related to claims not yet received. While our warranty liability represents our best estimate at August 31, 2014, we can provide no assurances that we will not experience material claims in the future or that we will not incur significant costs to resolve such claims beyond the amounts accrued or beyond what we may recover from our suppliers. Product warranty expense is recorded within selling, general and administrative expense.

Also, due to the nature of our roofing business, the amount of claims paid can fluctuate from one period to the next. While our warranty liability represents our best estimate of our expected losses at any given time, from time-to-time we may revise our estimates based on our experience relating to factors such as weather conditions, specific circumstances surrounding product installations and other factors.

The following table includes the changes in our accrued warranty balances:

<i>(In thousands)</i>	Quarter Ended August 31,	
	2014	2013
Beginning Balance	\$ 14,741	\$ 9,330
Deductions (1)	(14,675)	(4,796)
Provision charged to SG&A expense	7,355	5,308
Ending Balance	\$ 7,421	\$ 9,842

(1) Primarily claims paid during the year.

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In addition, like other companies participating in similar lines of business, some of our subsidiaries are involved in several proceedings relating to environmental matters. It is our policy to accrue remediation costs when it is probable that such efforts will be required and the related costs can be reasonably estimated. These liabilities are undiscounted and are not material to our financial statements during any of the periods presented.

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**RPM INTERNATIONAL INC. AND SUBSIDIARIES**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

As previously disclosed, we recorded a \$65.1 million accrual during the year ended May 31, 2013 associated with settlement discussions with the DOJ and the GSA Office of Inspector General aimed at resolving an existing investigation. Since first receiving a broad request for documents from the GSA in March 2011, we cooperated with that investigation, which involved our compliance with certain pricing terms and conditions of our GSA Multiple Award Schedule contracts under which the roofing division of our Tremco Group sold products and services to the federal government. A substantial majority of the transactions as to which potential compliance issues were raised took place during the period from 2002 to 2008. In August 2013, we entered into a final agreement with the DOJ and the GSA Office of Inspector General regarding this matter. During the year ended May 31, 2014, we paid the GSA Office of Inspector General \$61.9 million and made other payments for miscellaneous legal expenses for approximately \$1.1 million. We expect to pay approximately \$2.1 million more in legal fees and other related costs arising out of this investigation. The accrual for this contingency is classified in other accrued liabilities in our Consolidated Balance Sheets.

We were notified by the SEC on June 24, 2014 that we are the subject of a formal investigation pertaining to the timing of our disclosure and accrual of loss reserves in fiscal 2013 with respect to the previously disclosed GSA and DOJ investigation into compliance issues relating to Tremco Roofing Division's GSA contracts. We are cooperating with the SEC in its ongoing investigation. At this time, we are unable to predict the outcome of this matter or provide any quantification of how the final resolution of this matter may impact our future consolidated financial condition, results of operations or cash flows.

In January 2013, we entered into a Voluntary Self-Disclosure Agreement ( VSDA ) with the State of Delaware relating to certain property that may be held by us, including securities, payments, and refunds to employees, vendors and customers, that has been unclaimed for a specified period of time. Delaware's Abandoned Property Law, like other state and federal escheat laws, generally requires companies to report and remit unclaimed property to the state. Although we believe we have procedures in place to comply with these laws, we entered into the VSDA so that we may identify any previously unreported abandoned property and remit any such property to the State of Delaware. We cannot estimate the amount or range of any such potential loss. However, we do not expect the outcome of this review to have a material impact on our results of operations or financial position.

During the first quarter of fiscal 2015, two complaints were filed against Rust-Oleum and RPM International both seeking to have a class certified and alleging breach of warranty, breach of contract and other claims regarding certain deck coating products of Rust-Oleum. RPM International has since been dismissed from both actions, but they remain pending against Rust-Oleum. Rust-Oleum plans to vigorously defend these actions, including any attempts at class certification. At this time, we are unable to predict the outcome of this matter or provide any quantification of how the final resolution of these matters may impact our future consolidated financial condition, results of operations or cash flows.

**NOTE 15 STOCK REPURCHASE PROGRAM**

On January 8, 2008, we announced our authorization of a stock repurchase program under which we may repurchase shares of RPM International Inc. common stock at management's discretion for general corporate purposes. Our current intent is to limit our repurchases only to amounts required to offset dilution created by stock issued in connection with our equity-based compensation plans, or approximately one to two million shares per year. As a result of this authorization, we may repurchase shares from time to time in the open market or in private transactions at various times and in amounts and for prices that our management deems appropriate, subject to insider trading rules and other securities law restrictions. The timing of our purchases will depend upon prevailing market conditions, alternative uses of capital and other factors. We may limit or terminate the repurchase program at any time. During the three months ended August 31, 2014, we did not repurchase any shares of our common stock under this program.



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## RPM INTERNATIONAL INC. AND SUBSIDIARIES

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

## NOTE 16 EQUITY

The following tables illustrate the components of total equity and comprehensive income for the three months ended August 31, 2014 and 2013:

<i>(In thousands)</i>	Total RPM International Inc. Equity	Noncontrolling Interest	Total Equity
<b>Total equity at May 31, 2014</b>	<b>\$ 1,382,844</b>	<b>\$ 195,750</b>	<b>\$ 1,578,594</b>
Net income	99,079	5,760	104,839
Other Comprehensive Income:			
Foreign currency translation adjustments	(17,738)	(3,528)	(21,266)
Pension and other postretirement benefit liability adjustments, net of tax	2,760	169	2,929
Unrealized (loss) on securities, net of tax	83	(7)	76
Unrealized gain on derivatives, net of tax	(52)	(14)	(66)
Total Other Comprehensive Income, net of tax	(14,947)	(3,380)	(18,327)
<b>Comprehensive Income</b>	<b>84,132</b>	<b>2,380</b>	<b>86,512</b>
Dividends paid	(31,987)		(31,987)
Other noncontrolling interest activity	(4)	4	
Stock option exercises, net	(4,451)		(4,451)
Stock based compensation expense	5,700		5,700
<b>Total Equity at August 31, 2014</b>	<b>\$ 1,436,234</b>	<b>\$ 198,134</b>	<b>\$ 1,634,368</b>

<i>(In thousands)</i>	Total RPM International Inc. Equity	Noncontrolling Interest	Total Equity
<b>Total equity at May 31, 2013</b>	<b>\$ 1,200,858</b>	<b>\$ 154,075</b>	<b>\$ 1,354,933</b>
Net income	103,098	3,791	106,889
Other Comprehensive Income:			
Foreign currency translation adjustments	(17,071)	3,657	(13,414)
Pension and other postretirement benefit liability adjustments, net of tax	2,761	163	2,924
Unrealized (loss) gain on securities, net of tax	(1,432)	(7)	(1,439)
Unrealized gain on derivatives, net of tax	86	23	109
Total Other Comprehensive Income, net of tax	(15,656)	3,836	(11,820)
<b>Comprehensive Income</b>	<b>87,442</b>	<b>7,627</b>	<b>95,069</b>
Dividends paid	(29,836)		(29,836)

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Other noncontrolling interest activity	(341)	341	
Stock option exercises, net	2,401		2,401
Stock based compensation expense	709		709
Restricted awards, net	451		451
<b>Total Equity at August 31, 2013</b>	<b>\$ 1,261,684</b>	<b>\$ 162,043</b>	<b>\$ 1,423,727</b>

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**RPM INTERNATIONAL INC. AND SUBSIDIARIES**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

**NOTE 17 SEGMENT INFORMATION**

We operate a portfolio of businesses and product lines that manufacture and sell a variety of specialty paints, protective coatings and roofing systems, sealants and adhesives. We manage our portfolio by organizing our businesses and product lines into two reportable segments: the industrial reportable segment and the consumer reportable segment. Within each reportable segment, we aggregate several operating segments that consist of individual groups of companies and product lines, which generally address common markets, share similar economic characteristics, utilize similar technologies and can share manufacturing or distribution capabilities. Our seven operating segments represent components of our business for which separate financial information is available that is utilized on a regular basis by our chief executive officer in determining how to allocate the assets of the company and evaluate performance. These seven operating segments are each managed by an operating segment manager, who is responsible for the day-to-day operating decisions and performance evaluation of the operating segments underlying businesses.

Our industrial reportable segment products are sold throughout North America and also account for the majority of our international sales. Our industrial product lines are sold directly to contractors, distributors and end-users, such as industrial manufacturing facilities, public institutions and other commercial customers. This reportable segment comprises four separate operating segments – Tremco Group, Tremco illbruck Group, Performance Coatings Group and RPM2-Industrial Group. Products and services within this reportable segment include construction chemicals; roofing systems; weatherproofing and other sealants; polymer flooring; edible coatings and specialty glazes for pharmaceutical, cosmetic and food industries; and other specialty chemicals.

Our consumer reportable segment manufactures and markets professional use and do-it-yourself (DIY) products for a variety of mainly consumer applications, including home improvement and personal leisure activities. Our consumer segment's major manufacturing and distribution operations are located primarily in North America, along with a few locations in Europe. Consumer segment products are primarily sold directly to mass merchandisers, home improvement centers, hardware stores, paint stores, craft shops, cosmetic companies and to other smaller customers through distributors. This reportable segment comprises three operating segments – DAP Group, RPM2-Consumer Group and Rust-Oleum Group. Products within this reportable segment include specialty, hobby and professional paints; nail care enamels; caulks; adhesives; silicone sealants and wood stains.

In addition to our two reportable segments, there is a category of certain business activities and expenses, referred to as corporate/other, that does not constitute an operating segment. This category includes our corporate headquarters and related administrative expenses, results of our captive insurance companies, gains or losses on the sales of certain assets and other expenses not directly associated with either reportable segment. Assets related to the corporate/other category consist primarily of investments, prepaid expenses and headquarters' property and equipment. These corporate and other assets and expenses reconcile reportable segment data to total consolidated income before income taxes, interest expense and earnings before interest and taxes; as well as identifiable assets, capital expenditures and depreciation and amortization.

We reflect income from our joint ventures on the equity method, and receive royalties from our licensees.

**Table of Contents****RPM INTERNATIONAL INC. AND SUBSIDIARIES****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

The following tables reflect the results of our reportable segments consistent with our management philosophy, and represent the information we utilize, in conjunction with various strategic, operational and other financial performance criteria, in evaluating the performance of our portfolio of businesses.

	<b>Three Months Ended</b>	
	<b>August 31, 2014</b>	<b>August 31, 2013</b>
	<i>(In thousands)</i>	
<b>Net Sales</b>		
Industrial Segment	\$ 773,886	\$ 731,226
Consumer Segment	430,010	433,448
<b>Consolidated</b>	<b>\$ 1,203,896</b>	<b>\$ 1,164,674</b>
<b>Income (Loss) Before Income Taxes</b>		
Industrial Segment	\$ 102,464	\$ 97,581
Consumer Segment	76,669	82,717
Corporate/Other	(31,055)	(33,082)
<b>Consolidated</b>	<b>\$ 148,078</b>	<b>\$ 147,216</b>
	<b>August 31, 2014</b>	<b>May 31, 2014</b>
<b>Identifiable Assets</b>		
Industrial Segment	\$ 2,418,189	\$ 2,507,257
Consumer Segment	1,734,551	1,648,272
Corporate/Other	193,982	222,836
<b>Consolidated</b>	<b>\$ 4,346,722</b>	<b>\$ 4,378,365</b>



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### **MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS**

### **CRITICAL ACCOUNTING POLICIES AND ESTIMATES**

Our Consolidated Financial Statements include the accounts of RPM International Inc. and its majority-owned subsidiaries, except for certain subsidiaries that were deconsolidated on May 31, 2010 (please refer to Note 1 to the Consolidated Financial Statements for further information). Investments in less-than-majority-owned joint ventures for which we have the ability to exercise significant influence over are accounted for under the equity method. Preparation of our financial statements requires the use of estimates and assumptions that affect the reported amounts of our assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. We continually evaluate these estimates, including those related to our allowances for doubtful accounts; inventories; allowances for recoverable taxes; uncertain tax positions; useful lives of property, plant and equipment; goodwill and other intangible assets; environmental, warranties and other contingent liabilities; income tax valuation allowances; pension plans; and the fair value of financial instruments. We base our estimates on historical experience, our most recent facts, and other assumptions that we believe to be reasonable under the circumstances. These estimates form the basis for making judgments about the carrying values of our assets and liabilities. Actual results, which are shaped by actual market conditions, may differ materially from our estimates.

We have identified below the accounting policies and estimates that are the most critical to our financial statements.

#### **Revenue Recognition**

Revenues are recognized when realized or realizable, and when earned. In general, this is when title and risk of loss pass to the customer. Further, revenues are realizable when we have persuasive evidence of a sales arrangement, the product has been shipped or the services have been provided to the customer, the sales price is fixed or determinable and collectability is reasonably assured. We reduce our revenues for estimated customer returns and allowances, certain rebates, sales incentives and promotions in the same period the related sales are recorded.

We also record revenues generated under long-term construction contracts, mainly in connection with the installation of specialized roofing and flooring systems, and related services. In general, we account for long-term construction contracts under the percentage-of-completion method, and therefore record contract revenues and related costs as our contracts progress. This method recognizes the economic results of contract performance on a timelier basis than does the completed-contract method; however, application of this method requires reasonably dependable estimates of progress toward completion, as well as other dependable estimates. When reasonably dependable estimates cannot be made, or if other factors make estimates doubtful, the completed-contract method is applied. Under the completed-contract method, billings and costs are accumulated on the balance sheet as the contract progresses, but no revenue is recognized until the contract is complete or substantially complete.

#### **Translation of Foreign Currency Financial Statements and Foreign Currency Transactions**

Our reporting currency is the U.S. dollar. However, the functional currency for each of our foreign subsidiaries is its principal operating currency. We translate the amounts included in our Consolidated Statements of Income from our foreign subsidiaries into U.S. dollars at weighted-average exchange rates, which we believe are representative of the actual exchange rates on the dates of the transactions. Our foreign subsidiaries' assets and liabilities are translated into U.S. dollars from local currency at the actual exchange rates as of the end of each reporting date, and we record the resulting foreign exchange translation adjustments in our Consolidated Balance Sheets as a component of accumulated other comprehensive income (loss). If the U.S. dollar strengthens, we reflect the resulting losses as a component of accumulated other comprehensive income (loss). Conversely, if the U.S. dollar weakens, foreign exchange translation gains result, which favorably impact accumulated other

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comprehensive income (loss). Translation adjustments may be included in net earnings in the event of a sale or liquidation of certain of our underlying foreign investments. If we determine that the functional currency of any of our foreign subsidiaries should be the U.S. dollar, our financial statements will be affected. Should this occur, we will adjust our reporting to appropriately account for any such changes.

As appropriate, we use permanently invested intercompany loans as a source of capital to reduce exposure to foreign currency fluctuations at our foreign subsidiaries. These loans, on a consolidated basis, are treated as being analogous to equity for accounting purposes. Therefore, foreign exchange gains or losses on these intercompany loans are recorded in accumulated other comprehensive income (loss).

### **Goodwill**

We test our goodwill balances at least annually, or more frequently as impairment indicators arise, at the reporting unit level. Our reporting units have been identified at the component level, which is the operating segment level or one level below our operating segments.

In the fourth quarter of our fiscal year ended May 31, 2012, we early adopted new Financial Accounting Standards Board ( FASB ) guidance that simplifies how an entity tests goodwill for impairment. It provides an option to first assess qualitative factors to determine whether it is more likely than not that the fair value of a reporting unit is less than its carrying amount, and whether it is necessary to perform the two-step goodwill impairment test.

We assess qualitative factors in each of our reporting units that carry goodwill. Among other relevant events and circumstances that affect the fair value of our reporting units, we assess individual factors such as:

a significant adverse change in legal factors or the business climate;

an adverse action or assessment by a regulator;

unanticipated competition;

a loss of key personnel; and

a more-likely-than-not expectation that a reporting unit or a significant portion of a reporting unit will be sold or otherwise disposed of. We assess these qualitative factors to determine whether it is necessary to perform the two-step quantitative goodwill impairment test. Under the new guidance, this quantitative test is required only if we conclude that it is more likely than not that a reporting unit's fair value is less than its carrying amount.

In applying the first step of the quantitative test, we compare the fair value of a reporting unit to its carrying value. Calculating the fair market value of a reporting unit requires our use of estimates and assumptions. We use significant judgment in determining the most appropriate method to establish the fair value of a reporting unit. We estimate the fair value of a reporting unit by employing various valuation techniques, depending on the availability and reliability of comparable market value indicators, and employ methods and assumptions that include the application of third-party market value indicators and the computation of discounted future cash flows for a reporting unit's annual projected earnings before interest, taxes, depreciation and amortization ( EBITDA ).

We evaluate discounted future cash flows for a reporting unit's projected EBITDA. Under this approach, we calculate the fair value of a reporting unit based on the present value of estimated future cash flows. If the fair value of the reporting unit exceeds the carrying value of the net assets of the reporting unit, goodwill is not impaired. An indication that goodwill may be impaired results when the carrying value of the net assets of a reporting unit exceeds the fair value of the reporting unit. At that point, the second step of the impairment test is performed, which requires a fair value estimate of each tangible and intangible asset in order to determine the



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implied fair value of the reporting unit's goodwill. If the carrying value of a reporting unit's goodwill exceeds its implied fair value, then we record an impairment loss equal to the difference.

In applying the discounted cash flow methodology, we rely on a number of factors, including future business plans, actual and forecasted operating results, and market data. The significant assumptions employed under this method include discount rates; revenue growth rates, including assumed terminal growth rates; and operating margins used to project future cash flows for a reporting unit. The discount rates utilized reflect market-based estimates of capital costs and discount rates adjusted for management's assessment of a market participant's view with respect to other risks associated with the projected cash flows of the individual reporting unit. Our estimates are based upon assumptions we believe to be reasonable, but which by nature are uncertain and unpredictable. We believe we incorporate ample sensitivity ranges into our analysis of goodwill impairment testing for a reporting unit, such that actual experience would need to be materially out of the range of expected assumptions in order for an impairment to remain undetected.

Our annual goodwill impairment analysis for fiscal 2014 did not result in any indicators of impairment. Should the future earnings and cash flows at our reporting units decline and/or discount rates increase, future impairment charges to goodwill and other intangible assets may be required.

### **Other Long-Lived Assets**

We assess identifiable, amortizable intangibles and other long-lived assets for impairment whenever events or changes in facts and circumstances indicate the possibility that the carrying values of these assets may not be recoverable over their estimated remaining useful lives. Factors considered important in our assessment, which might trigger an impairment evaluation, include the following:

significant under-performance relative to historical or projected future operating results;

significant changes in the manner of our use of the acquired assets;

significant changes in the strategy for our overall business; and

significant negative industry or economic trends.

Measuring a potential impairment of amortizable intangibles and other long-lived assets requires the use of various estimates and assumptions, including the determination of which cash flows are directly related to the assets being evaluated, the respective useful lives over which those cash flows will occur and potential residual values, if any. If we determine that the carrying values of these assets may not be recoverable based upon the existence of one or more of the above-described indicators or other factors, any impairment amounts would be measured based on the projected net cash flows expected from these assets, including any net cash flows related to eventual disposition activities. The determination of any impairment losses would be based on the best information available, including internal estimates of discounted cash flows; market participant assumptions; quoted market prices, when available; and independent appraisals, as appropriate, to determine fair values. Cash flow estimates would be based on our historical experience and our internal business plans, with appropriate discount rates applied.

Additionally, we test all indefinite-lived intangible assets for impairment at least annually during our fiscal fourth quarter. In the fourth quarter of our fiscal year ended May 31, 2013, we adopted new FASB guidance that simplifies how an entity tests indefinite-lived intangible assets for impairment. It provides an option to first assess qualitative factors to determine whether it is more likely than not that the fair value of an indefinite-lived intangible asset is less than its carrying amount. Our fiscal 2014 annual impairment tests of each of our indefinite-lived intangible assets did not result in any impairment loss.

### **Income Taxes**

Our provision for income taxes is calculated using the liability method, which requires the recognition of deferred income taxes. Deferred income taxes reflect the net tax effect of temporary differences between the



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carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for income tax purposes and certain changes in valuation allowances. We provide valuation allowances against deferred tax assets if, based on available evidence, it is more likely than not that some portion or all of the deferred tax assets will not be realized.

In determining the adequacy of valuation allowances, we consider cumulative and anticipated amounts of domestic and international earnings or losses, anticipated amounts of foreign source income, as well as the anticipated taxable income resulting from the reversal of future taxable temporary differences. We intend to maintain any recorded valuation allowances until sufficient positive evidence (for example, cumulative positive foreign earnings or additional foreign source income) exists to support a reversal of the tax valuation allowances.

Further, at each interim reporting period, we estimate an effective income tax rate that is expected to be applicable for the full year. Significant judgment is involved regarding the application of global income tax laws and regulations and when projecting the jurisdictional mix of income. Additionally, interpretation of tax laws, court decisions or other guidance provided by taxing authorities influences our estimate of the effective income tax rates. As a result, our actual effective income tax rates and related income tax liabilities may differ materially from our estimated effective tax rates and related income tax liabilities. Any resulting differences are recorded in the period they become known.

## **Contingencies**

We are party to various claims and lawsuits arising in the normal course of business. Although we cannot precisely predict the amount of any liability that may ultimately arise with respect to any of these matters, we record provisions when we consider the liability probable and estimable. Our provisions are based on historical experience and legal advice, reviewed quarterly and adjusted according to developments. In general, our accruals, including our accruals for environmental, warranty and tax liabilities, discussed further below, represent the best estimate of a range of probable losses. Estimating probable losses requires the analysis of multiple forecasted factors that often depend on judgments about potential actions by third parties, such as regulators, courts, and state and federal legislatures. Changes in the amounts of our loss provisions, which can be material, affect our Consolidated Statements of Income. To the extent there is a reasonable possibility that potential losses could exceed the amounts already accrued, we believe that the amount of any such additional loss would be immaterial to our results of operations, liquidity and consolidated financial position. We evaluate our accruals at the end of each quarter, or sometimes more frequently, based on available facts, and may revise our estimates in the future based on any new information becoming available.

Our environmental-related accruals are similarly established and/or adjusted as more information becomes available upon which costs can be reasonably estimated. Actual costs may vary from these estimates because of the inherent uncertainties involved, including the identification of new sites and the development of new information about contamination. Certain sites are still being investigated; therefore, we have been unable to fully evaluate the ultimate costs for those sites. As a result, accruals have not been estimated for certain of these sites and costs may ultimately exceed existing estimated accruals for other sites. We have received indemnities for potential environmental issues from purchasers of certain of our properties and businesses and from sellers of some of the properties or businesses we have acquired. We also have purchased insurance to cover potential environmental liabilities at certain sites. If the indemnifying or insuring party fails to, or becomes unable to, fulfill its obligations under those agreements or policies, we may incur environmental costs in addition to any amounts accrued, which may have a material adverse effect on our financial condition, results of operations or cash flows.

Several of our industrial businesses offer extended warranty terms and related programs, and thus have established a corresponding warranty liability. Warranty expense is impacted by variations in local construction practices and installation conditions, including geographic and climate differences. Although we believe that appropriate liabilities have been recorded for our warranty expense, actual results may differ materially from our estimates.

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Additionally, our operations are subject to various federal, state, local and foreign tax laws and regulations that govern, among other things, taxes on worldwide income. The calculation of our income tax expense is based on the best information available, including the application of currently enacted income tax laws and regulations, and involves our significant judgment. The actual income tax liability for each jurisdiction in any year can ultimately be determined, in some instances, several years after the financial statements have been published.

We also maintain accruals for estimated income tax exposures for many different jurisdictions. Tax exposures are settled primarily through the resolution of audits within each tax jurisdiction or the closing of a statute of limitation. Tax exposures and actual income tax liabilities can also be affected by changes in applicable tax laws, retroactive tax law changes, or other factors, which may cause us to believe revisions of past estimates are appropriate. Although we believe that appropriate liabilities have been recorded for our income tax expense and income tax exposures, actual results may differ materially from our estimates.

### **Allowance for Doubtful Accounts Receivable**

An allowance for anticipated uncollectible trade receivable amounts is established using a combination of specifically identified accounts to be reserved and a reserve covering trends in collectability. These estimates are based on an analysis of trends in collectability and past experience, but are primarily made up of individual account balances identified as doubtful based on specific facts and conditions. Receivable losses are charged against the allowance when we confirm uncollectability. Actual collections of trade receivables could differ from our estimates due to changes in future economic or industry conditions or specific customer's financial conditions.

### **Inventories**

Inventories are stated at the lower of cost or market, cost being determined on a first-in, first-out (FIFO) basis and market being determined on the basis of replacement cost or net realizable value. Inventory costs include raw materials, labor and manufacturing overhead. We review the net realizable value of our inventory in detail on an on-going basis, with consideration given to various factors, which include our estimated reserves for excess, obsolete, slow moving or distressed inventories. If actual market conditions differ from our projections, and our estimates prove to be inaccurate, write-downs of inventory values and adjustments to cost of sales may be required. Historically, our inventory reserves have approximated actual experience.

### **Marketable Securities**

Marketable securities, included in other current and long-term assets, are composed of available-for-sale securities and are reported at fair value. Realized gains and losses on sales of investments are recognized in net income on the specific identification basis. Changes in fair values of securities that are considered temporary are recorded as unrealized gains and losses, net of applicable taxes, in accumulated other comprehensive income (loss) within stockholders' equity. Other-than-temporary declines in market value from original cost are reflected in operating income in the period in which the unrealized losses are deemed other than temporary. In order to determine whether an other-than-temporary decline in market value has occurred, the duration of the decline in value and our ability to hold the investment to recovery are considered in conjunction with an evaluation of the strength of the underlying collateral and the extent to which the investment's amortized cost or cost, as appropriate, exceeds its related market value.

### **Pension and Postretirement Plans**

We sponsor qualified defined benefit pension plans and various other nonqualified postretirement plans. The qualified defined benefit pension plans are funded with trust assets invested in a diversified portfolio of debt and equity securities and other investments. Among other factors, changes in interest rates, investment returns and the market value of plan assets can (i) affect the level of plan funding, (ii) cause volatility in the net periodic pension cost, and (iii) increase our future contribution requirements. A significant decrease in investment returns or the market value of plan assets or a significant decrease in interest rates could increase our net periodic pension costs.

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and adversely affect our results of operations. A significant increase in our contribution requirements with respect to our qualified defined benefit pension plans could have an adverse impact on our cash flow.

Changes in our key plan assumptions would impact net periodic benefit expense and the projected benefit obligation for our defined benefit and various postretirement benefit plans. Based upon May 31, 2014 information, the following tables reflect the impact of a 1% change in the key assumptions applied to our defined benefit pension plans in the U.S. and internationally:

	U.S.		International	
	1% Increase	1% Decrease	1% Increase	1% Decrease
<i>(In millions)</i>				
<b>Discount Rate</b>				
Increase (decrease) in expense in FY 2014	\$ (5.4)	\$ 6.5	\$ (1.8)	\$ 2.2
Increase (decrease) in obligation as of May 31, 2014	\$ (53.2)	\$ 65.9	\$ (29.9)	\$ 37.7
<b>Expected Return on Plan Assets</b>				
Increase (decrease) in expense in FY 2014	\$ (2.4)	\$ 2.4	\$ (1.6)	\$ 1.6
Increase (decrease) in obligation as of May 31, 2014	N/A	N/A	N/A	N/A
<b>Compensation Increase</b>				
Increase (decrease) in expense in FY 2014	\$ 4.1	\$ (3.6)	\$ 1.3	\$ (0.8)
Increase (decrease) in obligation as of May 31, 2014	\$ 21.3	\$ (19.2)	\$ 5.2	\$ (4.7)

Based upon May 31, 2014 information, the following table reflects the impact of a 1% change in the key assumptions applied to our various postretirement health care plans:

	U.S.		International	
	1% Increase	1% Decrease	1% Increase	1% Decrease
<i>(In millions)</i>				
<b>Discount Rate</b>				
Increase (decrease) in expense in FY 2014	\$	\$	\$ (0.7)	\$ 0.8
Increase (decrease) in obligation as of May 31, 2014	\$ (0.6)	\$ 0.7	\$ (4.7)	\$ 6.0
<b>Healthcare Cost Trend Rate</b>				
Increase (decrease) in expense in FY 2014	\$	\$	\$ 0.7	\$ (0.5)
Increase (decrease) in obligation as of May 31, 2014	\$ 0.2	\$ (0.2)	\$ 6.5	\$ (5.0)

**BUSINESS SEGMENT INFORMATION**

Our business is divided into two reportable segments: the industrial reportable segment and the consumer reportable segment. Within each reportable segment, we aggregate several operating segments that consist of individual groups of companies and product lines, which generally address common markets, share similar economic characteristics, utilize similar technologies and can share manufacturing or distribution capabilities. Our seven operating segments represent components of our business for which separate financial information is available that is utilized on a regular basis by our chief executive officer in determining how to allocate the assets of the company and evaluate performance. These seven operating segments are each managed by an operating segment manager who is responsible for the day-to-day operating decisions and performance evaluation of the operating segment's underlying businesses. We evaluate the profit performance of our segments primarily based on income before income taxes, but also look to earnings (loss) before interest and taxes (EBIT) as a performance evaluation measure because interest expense is essentially related to corporate acquisitions, as opposed to segment operations.

Our industrial reportable segment's products are sold throughout North America and also account for the majority of our international sales. Our industrial product lines are sold directly to contractors, distributors and end-users, such as industrial manufacturing facilities, public institutions and other commercial customers. This reportable segment comprises four separate operating segments—Tremco Group, tremco illbruck Group, Performance Coatings Group and RPM2-Industrial Group. Products and services within this reportable segment



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include construction chemicals; roofing systems; weatherproofing and other sealants; polymer flooring; edible coatings and specialty glazes for pharmaceutical, cosmetic and food industries; and other specialty chemicals.

Our consumer reportable segment manufactures and markets professional use and do-it-yourself (DIY) products for a variety of mainly consumer applications, including home improvement and personal leisure activities. Our consumer reportable segment's major manufacturing and distribution operations are located primarily in North America, along with a few locations in Europe. Our consumer reportable segment's products are sold throughout North America primarily to mass merchants, home improvement centers, hardware stores, paint stores, craft shops, cosmetic companies and to other smaller customers through distributors. This reportable segment comprises three operating segments—DAP Group, RPM2-Consumer Group and Rust-Oleum Group. Products within this reportable segment include specialty, hobby and professional paints; nail care enamels; caulks; adhesives; silicone sealants and wood stains.

In addition to our two reportable segments, there is a category of certain business activities and expenses, referred to as corporate/other, that does not constitute an operating segment. This category includes our corporate headquarters and related administrative expenses, results of our captive insurance companies, gains or losses on the sales of certain assets and other expenses not directly associated with either reportable segment. Assets related to the corporate/other category consist primarily of investments, prepaid expenses and headquarters property and equipment. These corporate and other assets and expenses reconcile reportable segment data to total consolidated income before income taxes, interest expense and earnings before interest and taxes.

The following table reflects the results of our reportable segments consistent with our management philosophy, and represents the information we utilize, in conjunction with various strategic, operational and other financial performance criteria, in evaluating the performance of our portfolio of product lines.

	<b>Three Months Ended</b>	
	<b>August 31, 2014</b>	<b>August 31, 2013</b>
	<i>(In thousands)</i>	
<b>Net Sales</b>		
Industrial Segment	\$ 773,886	\$ 731,226
Consumer Segment	430,010	433,448
<b>Consolidated</b>	<b>\$ 1,203,896</b>	<b>\$ 1,164,674</b>
<b>Income (Loss) Before Income Taxes (a)</b>		
Industrial Segment		
Income Before Income Taxes (a)	\$ 102,464	\$ 97,581
Interest (Expense), Net (b)	(2,633)	(2,534)
<b>EBIT (c)</b>	<b>\$ 105,097</b>	<b>\$ 100,115</b>
Consumer Segment		
Income Before Income Taxes (a)	\$ 76,669	\$ 82,717
Interest (Expense), Net (b)	(8)	39
<b>EBIT (c)</b>	<b>\$ 76,677</b>	<b>\$ 82,678</b>
Corporate/Other		
(Expense) Before Income Taxes (a)	\$ (31,055)	\$ (33,082)
Interest (Expense), Net (b)	(12,971)	(14,336)
<b>EBIT (c)</b>	<b>\$ (18,084)</b>	<b>\$ (18,746)</b>
<b>Consolidated</b>		
Income (Loss) Before Income Taxes (a)	\$ 148,078	\$ 147,216
Interest (Expense), Net (b)	(15,612)	(16,831)

EBIT (c)	\$ 163,690	\$ 164,047
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- (a) The presentation includes a reconciliation of Income (Loss) Before Income Taxes, a measure defined by Generally Accepted Accounting Principles (GAAP) in the United States, to EBIT.
- (b) Interest (expense), net includes the combination of interest (expense) and investment income/(expense), net.
- (c) EBIT is defined as earnings (loss) before interest and taxes. We evaluate the profit performance of our segments based on income before income taxes, but also look to EBIT as a performance evaluation measure because interest expense is essentially related to corporate acquisitions, as opposed to segment operations. We believe EBIT is useful to investors for this purpose as well, using EBIT as a metric in their investment decisions. EBIT should not be considered an alternative to, or more meaningful than, operating income as determined in accordance with GAAP, since EBIT omits the impact of interest and taxes in determining operating performance, which represent items necessary to our continued operations, given our level of indebtedness and ongoing tax obligations. Nonetheless, EBIT is a key measure expected by and useful to our fixed income investors, rating agencies and the banking community all of whom believe, and we concur, that this measure is critical to the capital markets analysis of our segments core operating performance. We also evaluate EBIT because it is clear that movements in EBIT impact our impact our ability to attract financing. Our underwriters and bankers consistently require inclusion of this measure in offering memoranda in conjunction with any debt underwriting or bank financing. EBIT may not be indicative of our historical operating results, nor is it meant to be predictive of potential future results.

## **RESULTS OF OPERATIONS**

### ***Three Months Ended August 31, 2014***

**Net Sales** Consolidated net sales increased 3.4% to \$1,203.9 million for the quarter ended August 31, 2014 due to organic growth of 2.1%, including a favorable foreign exchange impact of 0.1%, and acquisition growth of 1.3%. Industrial segment net sales for the current quarter were up 5.8% to \$773.9 million due to organic growth of 4.5%, including a favorable foreign exchange impact of 0.1%, and acquisition growth of 1.3%. The consumer segment generated net sales of \$430.0 million, or a decline of 0.8% in net sales during the current quarter versus the same period a year ago, due to decline in organic sales of 2.0%, including a favorable foreign exchange impact of 0.1%, offset slightly by the growth contributed from acquisitions of 1.2%. The decline in organic sales in the consumer segment resulted from exceptional sales from two consumer-segment product lines in the prior year first quarter, due to a new product launch for one and load-in sales to additional distribution channels for the other, that did not repeat at similar levels this year.

**Gross Profit Margin** Our consolidated gross profit margin declined to 42.2% of net sales for the first quarter of fiscal 2015 versus a consolidated gross profit margin of 42.9% for the comparable period a year ago, primarily reflecting the unfavorable impact of the mix of product sold during the current quarter versus the same period last year, and to a lesser extent, raw material inflation.

**Selling, General and Administrative Expenses ( SG&A )** Our consolidated SG&A expense increased by \$11.0 million during the current period versus the last year, but remained flat at 28.8% of net sales for both the current and prior year quarter. The current quarter SG&A expense includes \$5.6 million of higher legal and professional expense related to: the SEC and audit committee investigation of timing of the previously disclosed GSA accrual; the proposed SPHC settlement agreement; and our voluntary self-disclosure agreement with the State of Delaware for unclaimed property reviews. During the current quarter, there was also an increase in distribution and freight expense. Warranty expense for the quarter ended August 31, 2014 increased by approximately \$2.0 million from the amount recorded during the comparable prior year period, and it is typical that warranty expense will fluctuate from period to period.

Our industrial segment SG&A was approximately \$7.6 million higher during the first quarter of fiscal 2015 versus the comparable prior year period, but lower as a percentage of net sales, reflecting the favorable impact of lower transactional foreign exchange expense and lower legal and professional expense, which more than offset higher warranty and distribution expense versus the comparable prior year period.

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Our consumer segment SG&A was approximately \$4.1 million higher during the first quarter of fiscal 2015 versus the comparable prior year period, and higher as a percentage of net sales in the first quarter of fiscal 2015 as compared with the same period a year ago. SG&A expense for this segment reflects higher warranty and distribution expense during the current quarter of fiscal 2015 versus the comparable prior year period, partially offset by lower advertising expense.

SG&A expenses in our corporate/other category decreased by \$0.7 million during the first quarter of fiscal 2015 to \$18.1 million. The higher professional and legal fees discussed above were offset by lower employee benefits expenses, acquisition-related expenses and lower transactional foreign exchange losses during the current quarter versus the same period a year ago.

We recorded total net periodic pension and postretirement benefit costs of \$12.1 million and \$11.7 million for the first quarter of fiscal 2015 and 2014, respectively. The \$0.4 million increase in pension expense was primarily the result of higher service and interest cost of \$1.5 million during the first quarter of fiscal 2015 versus the comparable prior year period, offset partially by a favorable impact of \$1.1 million due to larger returns on higher plan asset levels. We expect that pension expense will fluctuate on a year-to-year basis, depending primarily upon the investment performance of plan assets and potential changes in interest rates, but such changes are not expected to be material to our consolidated financial results. See Note 6, Pension Plans, for additional information regarding these benefits.

**Interest Expense** Interest expense was \$19.4 million for the first quarter of fiscal 2015 versus \$20.7 million for the same period a year ago. Higher average borrowings, related to recent acquisitions, increased interest expense during this year's first quarter by approximately \$0.3 million versus the same period a year ago. Excluding acquisition-related borrowings, lower average borrowings year-over-year decreased interest expense by approximately \$0.9 million. Lower interest rates, which averaged 4.75% overall for the first quarter of fiscal 2015 compared with 5.06% for the same period of fiscal 2014, decreased interest expense by approximately \$0.7 million during the current quarter versus the same period last year.

**Investment (Income), Net** Net investment income of \$3.8 million during the first quarter of fiscal 2015 compares to net investment income of \$3.9 million during the same period last year. Dividend and interest income totaled \$1.7 million for the current quarter and \$1.8 million for the prior year quarter. Net realized gains on the sales of investments totaled \$2.1 million during the first quarter of fiscal 2015, while those gains were \$2.2 million during the same period a year ago. There were no impairments recognized on securities that management has determined are other-than-temporary declines in value during the current quarter versus \$0.1 million of losses recognized during the prior year period.

**Other Expense (Income), Net** Other income of \$1.8 million for the first quarter of fiscal 2015 compared with other income of \$0.4 million for the same period a year ago. Items reflected in this balance include net royalty income of \$1.2 million for the current quarter of fiscal 2015 and royalty expense of \$0.3 million for the first quarter of fiscal 2014. Also included in this balance is our equity in earnings of unconsolidated affiliates totaling approximately \$0.6 million and \$0.7 million for the first quarter of fiscal 2015 and 2014, respectively.

**Income Before Income Taxes ( IBT )** Our consolidated pretax income for the first quarter of fiscal 2015 of \$148.1 million compares with \$147.2 million for the same period a year ago.

Our industrial segment had pretax income of \$102.5 million, or 13.2% of net sales, for the quarter ended August 31, 2014, versus pretax income of \$97.6 million, or 13.3% of net sales, for the same period a year ago. Our consumer segment IBT decreased to \$76.7 million, or 17.8% of net sales for the first quarter of fiscal 2015, from the prior year first quarter result of \$82.6 million, or 19.1% of net sales. This was driven primarily by the decline in organic net sales for the consumer segment in the first quarter of fiscal 2015 from the comparable prior year period.

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**Income Tax Rate** The effective income tax rate was 29.2% for the three months ended August 31, 2014 compared to an effective income tax rate of 27.4% for the three month ended August 31, 2013. The quarter over quarter increase in the effective income tax rate is primarily due to a non-recurring net tax benefit recorded in the three month period ended August 31, 2013. This net tax benefit was primarily comprised of the benefit associated with recognition of a foreign deferred income tax asset resulting from the merger of certain foreign subsidiaries partially offset by the impact of the enactment of a Canadian tax law change, Canada Bill C-48, Technical Tax Amendments Act, 2012, which was enacted on of June 26, 2013.

**Net Income** Net income of \$104.9 million for the quarter ended August 31, 2014 compares to \$106.9 million for the comparable prior year period, which results in a net margin on sales of 8.7% and 9.2%, respectively, for the first quarter of fiscal 2015 and 2014. During the quarter ended August 31, 2014, we had net income from noncontrolling interests of \$5.8 million versus \$3.8 million during the comparable prior year period. Net income attributable to RPM International Inc. stockholders for the first quarter of fiscal 2015 was \$99.1 million, or an adjusted \$103.1 million, which compared to \$103.1 million for the comparable prior year period.

Diluted earnings per share of common stock for the quarter ended August 31, 2014 of \$0.73 compares with diluted earnings per share of common stock of \$0.77 for the quarter ended August 31, 2013. Excluding the impact of the convertible note, diluted earnings per share of common stock would have been \$0.74 for the quarter ended August 31, 2014.

## **LIQUIDITY AND CAPITAL RESOURCES**

### **Operating Activities**

Approximately \$125.2 million of cash was used for operating activities during fiscal 2015, compared with \$129.5 million during fiscal 2014, resulting in \$4.3 million less cash used during the current period versus the same period a year ago.

The net change in cash from operations includes the change in net income, which decreased by \$2.1 million during fiscal 2015 versus fiscal 2014. Other items impacting the net change in cash from operations included items adjusting net income for non-cash expenses and income, which increased cash flows by approximately \$15.4 million more during fiscal 2015 versus fiscal 2014. Changes in working capital accounts and all other accruals, combined with a payment on a contingency during fiscal 2014, decreased cash flows by \$260.4 million and \$251.3 million, respectively, during fiscal 2015 versus fiscal 2014.

The change in accounts receivable during fiscal 2015 used cash of \$72.3 million versus the \$76.5 million of cash used for accounts receivable during fiscal 2014, or approximately \$4.2 million less cash used year over year. This resulted from the geographical mix of sales and from the timing of sales and collections on accounts receivable. Days sales outstanding at August 31, 2014 increased to 67.4 days from 63.4 days sales outstanding at August 31, 2013.

Inventory balances used \$17.3 million of cash during fiscal 2015, compared with a use of \$23.4 million in cash during fiscal 2014, or \$6.1 million less cash used year over year. Days of inventory outstanding at August 31, 2014 increased to 81.3 days from 77.4 days of inventory outstanding at August 31, 2013.

The current year-to-date change in accounts payable used \$32.4 million more cash during fiscal 2015 compared to fiscal 2014, resulting from a change in the timing of certain payments. Accrued compensation and benefits used approximately \$24.9 million more cash during fiscal 2015 versus fiscal 2014, due to higher bonus payments for fiscal 2014 versus fiscal 2013. Other accruals and prepaids, including those for other short-term and long-term items and changes, used \$20.7 million more cash during fiscal 2015 versus fiscal 2014, due to changes in the timing of such payments. Lastly, during the prior year period, cash provided from operations was impacted by a payment on a contingency for \$61.9 million.

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Cash provided from operations, along with the use of available credit lines, as required, remain our primary sources of liquidity.

### **Investing Activities**

Capital expenditures, other than for ordinary repairs and replacements, are made to accommodate our continued growth to achieve production and distribution efficiencies, expand capacity, introduce new technology, improve environmental health and safety capabilities, improve information systems, and enhance our administration capabilities. Capital expenditures of \$12.1 million during the first quarter of fiscal 2015 compare with depreciation of \$15.0 million. We believe our current production capacity, along with moderate plant modifications or additions will be adequate to meet our immediate needs based on anticipated growth rates. We anticipate that additional shifts at our production facilities, coupled with the capacity added through acquisition activity and our planned increase in future capital spending levels, will enable us to meet increased demand throughout fiscal 2015.

Our captive insurance companies invest their excess cash in marketable securities in the ordinary course of conducting their operations, and this activity will continue. Differences in the amounts related to these activities on a year-over-year basis are primarily attributable to differences in the timing and performance of their investments balanced against amounts required to satisfy claims. At August 31, 2014, the fair value of our investments in marketable securities totaled \$141.1 million, of which investments with a fair value of \$42.0 million were in an unrealized loss position. At May 31, 2014, the fair value of our investments in marketable securities totaled \$142.9 million, of which investments with a fair value of \$35.5 million were in an unrealized loss position. The fair value of our portfolio of marketable securities is based on quoted market prices for identical, or similar, instruments in active or non-active markets or model-derived-valuations with observable inputs. We have no marketable securities whose fair value is subject to unobservable inputs. Total pretax unrealized losses recorded in accumulated other comprehensive income at August 31, 2014 and May 31, 2014 were \$1.4 million and \$1.4 million, respectively.

We regularly review our marketable securities in unrealized loss positions in order to determine whether or not we have the ability and intent to hold these investments. That determination is based upon the severity and duration of the decline, in addition to our evaluation of the cash flow requirements of our businesses. Unrealized losses at August 31, 2014 were generally related to the normal volatility in valuations over the past several months for a portion of our portfolio of investments in marketable securities. The unrealized losses generally relate to investments whose fair values at August 31, 2014 were less than 15% below their original cost or that have been in a loss position for less than six consecutive months. From time to time, we may experience significant volatility in general economic and market conditions. If we were to experience unrealized losses that were to continue for longer periods of time, or arise to more significant levels of unrealized losses within our portfolio of investments in marketable securities in the future, we may recognize additional other-than-temporary impairment losses. Such potential losses could have a material impact on our results of operations in any given reporting period. As such, we continue to closely evaluate the status of our investments and our ability and intent to hold these investments.

As of August 31, 2014, approximately \$198.0 million of our consolidated cash and cash equivalents were held at various foreign subsidiaries. At this time, we continue to believe it is possible that we could repatriate approximately \$50.0 million of undistributed foreign earnings in the foreseeable future. Accordingly, the estimated deferred tax impact of this potential repatriation is reflected in our balance sheet. These earnings have been previously subject to U.S. taxation and as such, the estimated net tax impact of such remittance is estimated to be minimal.

Other than as noted above, the funds held at our foreign subsidiaries are considered permanently reinvested to be used, for instance, to expand operations organically or for acquisitions in foreign jurisdictions. Our operations in the U.S. generate sufficient cash flow to satisfy U.S. operating requirements. As such, we do not intend to repatriate any significant amounts of these cash balances to the U.S. in the foreseeable future. Any repatriation of

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these balances could be subject to U.S. and foreign taxes. However, a portion of these remaining foreign earnings have also been previously subject to U.S. taxation and could be repatriated to the U.S. with little or no residual tax impact. We believe that the tax impact of repatriating these previously taxed earnings to the U.S. would not have a material impact on our financial results. Furthermore, any repatriation could be subject to government or other local restrictions or limitations such as local minimum capital reserve requirements or exchange controls, etc.

As previously stated, we intend to permanently reinvest the certain cash and cash equivalents held at our various foreign subsidiaries for foreign expansion and other uses. Due to the uncertainties and complexities involved in the various options for repatriation of foreign cash, including any associated governmental or other local restrictions, it is not practicable to calculate the deferred taxes associated with the remittance of these cash balances.

## **Financing Activities**

As a result of the Specialty Products Holding Corp. ( SPHC ) bankruptcy filing, our access to the cash flows of SPHC and its subsidiaries has been restricted. However, the bankruptcy filing has not resulted in any reductions in our credit ratings by Moody's Investor Service, Standard & Poor's or Fitch Ratings. Therefore, we feel this has not adversely impacted our ability to gain access to capital.

Our available liquidity, including our cash and cash equivalents and amounts available under our committed credit facilities, stood at \$892.7 million at August 31, 2014. Our debt-to-capital ratio was 50.72% at August 31, 2014, compared with 49.4% at May 31, 2014.

### ***2.25% Convertible Senior Notes due 2020***

On December 9, 2013, we issued \$205 million of 2.25% convertible senior notes due 2020 (the Convertible Notes ). We will pay interest on the Convertible Notes semi-annually on June 15<sup>th</sup> and December 15<sup>th</sup> of each year, and began doing so on June 15, 2014. Net proceeds of approximately \$200.1 million from the sale were used to refinance \$200 million in principal amount of unsecured senior notes due December 15, 2013, which bear interest at 6.25%.

The Convertible Notes will be convertible under certain circumstances and during certain periods at an initial conversion rate of 18.8905 shares of RPM common stock per \$1,000 principal amount of notes (representing an initial conversion price of approximately \$52.94 per share of common stock), subject to adjustment in certain circumstances. The initial conversion price represents a conversion premium of approximately 37% over the last reported sale price of RPM common stock of \$38.64 on December 3, 2013. Prior to June 15, 2020, the Convertible Notes may be converted only upon specified events, and, thereafter, at any time. Upon conversion, the Convertible Notes may be settled, at RPM's election, in cash, shares of RPM's common stock, or a combination of cash and shares of RPM's common stock.

We account for the liability and equity components of the Convertible Notes separately, and in a manner that will reflect our nonconvertible debt borrowing rate when interest cost is recognized in subsequent periods. The effective interest rate on the liability component is 3.92%. Contractual interest was \$1.1 million for the first quarter of fiscal 2015, and amortization of the debt discount was \$0.7 million for the first quarter of fiscal 2015. At August 31, 2014, the remaining period over which the debt discount will be amortized was 6.5 years, the unamortized debt discount was \$18.9 million, and the carrying amount of the equity component was \$20.7 million.

### ***6.25% Notes due 2013***

On December 15, 2013, our \$200 million 6.25% senior notes matured. In December 2013, we refinanced this debt with proceeds received from our issuance of \$205 million of Convertible Notes.

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### ***3.45% Notes due 2022***

On October 23, 2012, we sold \$300 million aggregated principal amount of 3.45% Notes due 2022 (the *New Notes* ). The net proceeds of \$297.7 million from the offering of the New Notes were used to repay short-term borrowings outstanding under our \$600 million revolving credit facility.

### ***Revolving Credit Agreement***

On June 29, 2012, we entered into an unsecured syndicated revolving credit facility (the *Credit Facility* ) with a group of banks. The Credit Facility expires on June 29, 2017 and provides for a five-year \$600.0 million revolving credit facility, which includes sublimits for the issuance of \$50.0 million in swingline loans, which are comparatively short-term loans used for working capital purposes, and letters of credit. The aggregate maximum principal amount of the commitments under the Credit Facility may be expanded upon our request, subject to certain conditions, to \$800.0 million. The Credit Facility is available to refinance existing indebtedness, to finance working capital and capital expenditure needs, and for general corporate purposes.

The Credit Facility requires us to comply with various customary affirmative and negative covenants, including a leverage covenant and interest coverage ratio. Under the terms of the leverage covenant, we may not permit our consolidated indebtedness as of any fiscal quarter end to exceed 60% of the sum of such indebtedness and our consolidated shareholders' equity on such date. The minimum required consolidated interest coverage ratio for EBITDA to interest expense is 3.50 to 1. The interest coverage ratio is calculated at the end of each fiscal quarter for the four fiscal quarters then ended.

As of August 31, 2014, we were in compliance with all covenants contained in our Credit Facility, including the leverage and interest coverage ratio covenants. At that date, our leverage ratio was 50.82%, while our interest coverage ratio was 7.96 to 1.

Our access to funds under our Credit Facility is dependent on the ability of the financial institutions that are parties to the Credit Facility to meet their funding commitments. Those financial institutions may not be able to meet their funding commitments if they experience shortages of capital and liquidity or if they experience excessive volumes of borrowing requests within a short period of time. Moreover, the obligations of the financial institutions under our Credit Facility are several and not joint and, as a result, a funding default by one or more institutions does not need to be made up by the others.

### ***Accounts Receivable Securitization Program***

On May 9, 2014, we replaced our existing \$150.0 million accounts receivable securitization program (which immediately prior to such replacement was assigned from Wells Fargo Bank, National Association to PNC Bank, National Association, as administrative agent) with a new, three-year, \$200.0 million accounts receivable securitization facility (the *New Facility* ). The New Facility was entered into pursuant to (1) a second amended and restated receivables sale agreement, dated as of May 9, 2014 (the *Sale Agreement* ), among certain of our subsidiaries (the *Originators* ), and RPM Funding Corporation, a special purpose entity (the *SPE* ) whose voting interests are wholly owned by us, and (2) an amended and restated receivables purchase agreement, dated as of May 9, 2014 (the *Purchase Agreement* ), among the SPE, certain purchasers from time to time party thereto (the *Purchasers* ), and PNC Bank, National Association as administrative agent.

Under the Sale Agreement, the Originators may, during the term thereof, sell specified accounts receivable to the SPE, which may in turn, pursuant to the Purchase Agreement, transfer an undivided interest in such accounts receivable to the Purchasers. Once transferred to the SPE, such receivables are owned in their entirety by the SPE and are not available to satisfy claims of our creditors or creditors of the originating subsidiaries until the obligations owing to the participating banks have been paid in full. We indirectly hold a 100% economic interest



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in the SPE and will, along with our subsidiaries, receive the economic benefit of the New Facility. The transactions contemplated by the New Facility do not constitute a form of off-balance sheet financing, and will be fully reflected in our financial statements.

The maximum availability under the New Facility is \$200.0 million. Availability is further subject to changes in the credit ratings of the Originator's customers, customer concentration levels or certain characteristics of the accounts receivable being transferred and therefore at certain times we may not be able to fully access the \$200.0 million of funding available under the New Facility. The interest rate under the Purchase Agreement is based on the Alternate Base Rate, LIBOR Market Index Rate, one-month LIBOR or LIBOR for a specified tranche period, as selected by the SPE, at its option, plus in each case, a margin of 0.70%. In addition, as set forth in an Amended and Restated Fee Letter, dated May 9, 2014 (the "Fee Letter"), the SPE is obligated to pay a monthly unused commitment fee to the Purchasers based on the daily amount of unused commitments under the Agreement which fee ranges from 0.30% to 0.50% based on usage.

The New Facility contains various customary affirmative and negative covenants and also contains customary default and termination provisions, which provide for acceleration of amounts owed under the New Facility upon the occurrence of certain specified events, including, but not limited to, failure by the SPE to pay interest and other amounts due, defaults on certain indebtedness, certain judgments, change in control, certain events negatively affecting the overall credit quality of transferred accounts receivable, bankruptcy and insolvency events, and failure by us to meet financial tests requiring maintenance of an interest coverage ratio, if applicable. If we do not maintain an investment grade public debt rating with at least two specified rating agencies, we must comply with the interest coverage ratio which requires us not to permit the ratio, calculated at the end of each fiscal quarter for the four fiscal quarters then ended, of EBITDA, as defined in the New Facility, for such period to interest expense for such period, to be less than 3.5:1. This financial test, to the extent applicable, is substantively identical to a similar covenant already contained in our revolving credit facility. As of August 31, 2014, there was approximately \$50.0 million in outstanding borrowings under the New Facility.

Our failure to comply with the covenants described above and other covenants contained in the Credit Facility could result in an event of default under that agreement, entitling the lenders to, among other things, declare the entire amount outstanding under the Credit Facility to be due and payable. The instruments governing our other outstanding indebtedness generally include cross-default provisions that provide that under certain circumstances, an event of default that results in acceleration of our indebtedness under the Credit Facility will entitle the holders of such other indebtedness to declare amounts outstanding immediately due and payable.

We are exposed to market risk associated with interest rates. We do not use financial derivative instruments for trading purposes, nor do we engage in foreign currency, commodity or interest rate speculation. Concurrent with the issuance of our 6.7% Senior Unsecured Notes, RPM United Kingdom G.P. entered into a cross currency swap, which fixed the interest and principal payments in euros for the life of the 6.7% Senior Unsecured Notes and resulted in an effective euro fixed rate borrowing of 5.31%.

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The following table summarizes our financial obligations and their expected maturities at August 31, 2014 and the effect such obligations are expected to have on our liquidity and cash flow in the periods indicated.

**Contractual Obligations**

	Total Contractual Payment Stream	Payments Due In			
		2015	2016-17 <i>(In thousands)</i>	2018-19	After 2019
Long-term debt obligations	\$ 1,478,026	\$ 1,677	\$ 283,519	\$ 248,864	\$ 943,966
Capital lease obligations	1,369	553	526	225	65
Operating lease obligations	210,371	47,493	65,448	33,825	63,605
Other long-term liabilities (1):					
Interest payments on long-term debt obligations	341,313	67,499	121,912	101,300	50,602
Contributions to pension and postretirement plans (2)	370,800	60,300	84,300	88,900	137,300
<b>Total</b>	<b>\$ 2,401,879</b>	<b>\$ 177,522</b>	<b>\$ 555,705</b>	<b>\$ 473,114</b>	<b>\$ 1,195,538</b>

- (1) Excluded from other long-term liabilities are our gross long-term liabilities for unrecognized tax benefits, which totaled \$20.2 million at August 31, 2014. Currently, we cannot predict with reasonable reliability the timing of cash settlements to the respective taxing authorities related to these liabilities.
- (2) These amounts represent our estimated cash contributions to be made in the periods indicated for our pension and postretirement plans, assuming no actuarial gains or losses, assumption changes or plan changes occur in any period. The projection results assume the required minimum contribution will be contributed.

**Off-Balance Sheet Arrangements**

We do not have any off-balance sheet financings, other than the minimum operating lease commitments included in the above Contractual Obligations table. We have no subsidiaries that are not included in our financial statements, nor do we have any interests in, or relationships with, any special purpose entities that are not reflected in our financial statements. At the end of fiscal 2010, we deconsolidated our wholly owned subsidiary, SPHC, and its subsidiaries, from our balance sheet and eliminated the results of SPHC's operations from our operations beginning on May 31, 2010. We account for our investment in SPHC, which had no value at August 31, 2014 and May 31, 2014, under the cost method (refer to Note 3 to the Consolidated Financial Statements).

**OTHER MATTERS****Environmental Matters**

Environmental obligations continue to be appropriately addressed and, based upon the latest available information, it is not anticipated that the outcome of such matters will materially affect our results of operations or financial condition. Our critical accounting policies and estimates set forth above describe our method of establishing and adjusting environmental-related accruals and should be read in conjunction with this disclosure. For additional information, refer to Part II, Item 1. Legal Proceedings.

**FORWARD-LOOKING STATEMENTS**

The foregoing discussion includes forward-looking statements relating to our business. These forward-looking statements, or other statements made by us, are made based on our expectations and beliefs concerning future events impacting us and are subject to uncertainties and factors (including those specified below), which are



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difficult to predict and, in many instances, are beyond our control. As a result, our actual results could differ materially from those expressed in or implied by any such forward-looking statements. These uncertainties and factors include (a) global markets and general economic conditions, including uncertainties surrounding the volatility in financial markets, the availability of capital and the effect of changes in interest rates, and the viability of banks and other financial institutions; (b) the prices, supply and capacity of raw materials, including assorted pigments, resins, solvents, and other natural gas- and oil-based materials; packaging, including plastic containers; and transportation services, including fuel surcharges; (c) continued growth in demand for our products; (d) legal, environmental and litigation risks inherent in our construction and chemicals businesses and risks related to the adequacy of our insurance coverage for such matters; (e) the effect of changes in interest rates; (f) the effect of fluctuations in currency exchange rates upon our foreign operations; (g) the effect of non-currency risks of investing in and conducting operations in foreign countries, including those relating to domestic and international political, social, economic and regulatory factors; (h) risks and uncertainties associated with our ongoing acquisition and divestiture activities; (i) risks related to the adequacy of our contingent liability reserves; (j) risks and uncertainties associated with the SPHC bankruptcy proceedings; and (k) other risks detailed in our filings with the Securities and Exchange Commission, including the risk factors set forth in our Annual Report on Form 10-K for the year ended May 31, 2014, as the same may be updated from time to time. We do not undertake any obligation to publicly update or revise any forward-looking statements to reflect future events, information or circumstances that arise after the filing date of this document.

### **ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK**

We are exposed to market risk from changes in raw materials costs, interest rates and foreign exchange rates since we fund our operations through long- and short-term borrowings and conduct our business in a variety of foreign currencies. There were no material potential changes in our exposure to these market risks since May 31, 2014.

### **ITEM 4. CONTROLS AND PROCEDURES**

#### **(a) EVALUATION OF DISCLOSURE CONTROLS AND PROCEDURES.**

Our Chief Executive Officer and Chief Financial Officer, after evaluating the effectiveness of our disclosure controls and procedures (as defined in Exchange Act Rule 13a-15(e)) as of August 31, 2014 (the Evaluation Date), have concluded that as of the Evaluation Date, our disclosure controls and procedures were effective in ensuring that information required to be disclosed by us in the reports we file or submit under the Exchange Act (1) is recorded, processed, summarized and reported, within the time periods specified in the Commission's rules and forms, and (2) is accumulated and communicated to our management, including the Chief Executive Officer and the Chief Financial Officer, as appropriate to allow for timely decisions regarding required disclosure.

#### **(b) CHANGES IN INTERNAL CONTROL.**

There were no changes in our internal control over financial reporting that occurred during the fiscal quarter ended August 31, 2014 that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

**Table of Contents****PART II OTHER INFORMATION****ITEM 1. LEGAL PROCEEDINGS*****Asbestos Litigation and the Bankruptcy Filings by SPHC and Bondex***

For information regarding asbestos litigation involving SPHC and Bondex, see Note 2 to the Consolidated Financial Statements. On May 31, 2010, Bondex and its parent, SPHC, filed voluntary petitions in the United States Bankruptcy Court for the District of Delaware to reorganize under Chapter 11 of the Bankruptcy Code.

***Environmental Proceedings***

As previously reported, several of our subsidiaries are, from time to time, identified as a potentially responsible party under the Federal Comprehensive Environmental Response, Compensation and Liability Act and similar state environmental statutes. In some cases, our subsidiaries are participating in the cost of certain clean-up efforts or other remedial actions. Our share of such costs, however, has not been material and we believe that these environmental proceedings will not have a material adverse effect on our consolidated financial condition or results of operations. See Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations Other Matters, in Part I of this Quarterly Report on Form 10-Q.

**ITEM 1A. RISK FACTORS**

In addition to the other information set forth in this report, you should carefully consider the risk factors disclosed in Item 1A of our Annual Report on Form 10-K for the fiscal year ended May 31, 2014.

**ITEM 2. UNREGISTERED SALE OF EQUITY SECURITIES AND USE OF PROCEEDS**

(c) The following table presents information about repurchases of common stock we made during the first quarter of fiscal 2015:

Period	Total Number of Shares Purchased (1)	Average Price Paid Per Share	Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs	Maximum Number of Shares that May Yet be Purchased Under the Plans or Programs (2)
June 1, 2014 through June 30, 2014		\$		
July 1, 2014 through July 31, 2014	101,571	\$ 44.79		
August 1, 2014 through August 31, 2014	3,127	\$ 46.71		
Total First Quarter	104,698	\$ 44.85		

(1) All of the shares of common stock reported as purchased are attributable to shares of common stock that were disposed of back to us in satisfaction of tax obligations related to the vesting of restricted stock which was granted under RPM International Inc.'s Amended and Restated 2004 Omnibus Equity and Incentive Plan.

(2) Refer to Note 15 of the Notes to Consolidated Financial Statements for further information regarding our stock repurchase program.

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**ITEM 6. EXHIBITS**

Exhibit	
Number	Description
10.1	Settlement Term Sheet, dated July 26, 2014, by and among the Company, Bondex, SPHC, Republic, the Asbestos Claimants Committee, counsel for each member of the Asbestos Claimants Committee in its individual capacity and on behalf of such member, and Eric Green, in his capacity as the Future Claimants Representative, which is incorporated by reference to Exhibit 10.1 to the Company's Current Report on Form 8-K, as filed with the Securities and Exchange Commission on July 31, 2014 (File No. 1-14187).
12	Computation of Ratio of Earnings to Fixed Charges. (x)
31.1	Rule 13a-14(a) Certification of the Company's Chief Executive Officer.(x)
31.2	Rule 13a-14(a) Certification of the Company's Chief Financial Officer.(x)
32.1	Section 1350 Certification of the Company's Chief Executive Officer.(x)
32.2	Section 1350 Certification of the Company's Chief Financial Officer.(x)
101.INS	XBRL Instance Document.
101.SCH	XBRL Taxonomy Extension Schema Document.
101.PRE	XBRL Taxonomy Extension Presentation Linkbase Document.
101.DEF	XBRL Taxonomy Extension Definition Linkbase Document.
101.CAL	XBRL Taxonomy Extension Calculation Linkbase Document.
101.LAB	XBRL Taxonomy Extension Label Linkbase Document.

(x) Filed herewith.

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**SIGNATURES**

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

**RPM International Inc.**

By: /s/ Frank C. Sullivan  
Frank C. Sullivan  
Chairman and Chief Executive Officer

By: /s/ Russell L. Gordon  
Russell L. Gordon  
Vice President and  
Chief Financial Officer

Dated: October 8, 2014