NL INDUSTRIES INC
Form 10-Q
November 07, 2016

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF

THE SECURITIES EXCHANGE ACT OF 1934

For the quarter ended September 30, 2016

Commission file number 1-640

NL INDUSTRIES, INC.

(Exact name of Registrant as specified in its charter)

| | |
|---|---|
| New Jersey | 13-5267260 |
| (State or other jurisdiction of incorporation or organization) | (IRS Employer Identification No.) |

5430 LBJ Freeway, Suite 1700

Dallas, Texas 75240-2697

(Address of principal executive offices)

Registrant’s telephone number, including area code: (972) 233-1700

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 and (2) has been subject to such filing requirements for the past 90 days.    Yes        No

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

Indicate by check mark whether the Registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer or a smaller reporting company (as defined in Rule 12b-2 of the Securities Exchange Act of 1934).    Large accelerated filer        Accelerated filer        Non-accelerated filer        Smaller reporting company

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

Number of shares of the Registrant's common stock outstanding on October 28, 2016:  48,705,884.

NL INDUSTRIES, INC. AND SUBSIDIARIES

INDEX



Items 2, 3, 4 and 5 of Part II are omitted because there is no information to report.

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NL INDUSTRIES, INC. AND SUBSIDIARIES

CONDENSED CONSOLIDATED BALANCE SHEETS

(In thousands)

| | December 31, 2015 | September 30, 2016 (unaudited) |
|---|---|---|
| ASSETS | | |
| Current assets: | | |
| Cash and cash equivalents | $ 96,462 | $ 100,995 |
| Restricted cash and cash equivalents | 3,246 | 3,336 |
| Accounts and other receivables, net | 8,977 | 13,282 |
| Inventories, net | 15,098 | 14,638 |
| Prepaid expenses and other | 981 | 856 |
| Total current assets | 124,764 | 133,107 |
| Other assets: | | |
| Notes receivable from affiliate | — | 10,700 |
| Marketable securities | 19,260 | 33,058 |
| Investment in Kronos Worldwide, Inc. | 140,695 | 138,550 |
| Goodwill | 27,156 | 27,156 |
| Other assets, net | 3,331 | 3,658 |
| Deferred income taxes | 11 | 11 |
| Total other assets | 190,453 | 213,133 |
| Property and equipment: | | |
| Land | 5,138 | 5,146 |
| Buildings | 21,502 | 22,812 |
| Equipment | 64,051 | 65,443 |
| Construction in progress | 1,567 | 873 |
| | 92,258 | 94,274 |
| Less accumulated depreciation | 58,152 | 60,657 |
| Net property and equipment | 34,106 | 33,617 |
| Total assets | $ 349,323 | $ 379,857 |

NL INDUSTRIES, INC. AND SUBSIDIARIES

CONDENSED CONSOLIDATED BALANCE SHEETS (CONTINUED)

(In thousands)

| | December 31, 2015 | September 30, 2016 (unaudited) |
|---|---|---|
| LIABILITIES AND EQUITY | | |
| Current liabilities: | | |
| Accounts payable | $4,557 | $5,387 |
| Accrued and other current liabilities | 10,783 | 10,091 |
| Accrued environmental remediation and related costs | 8,668 | 13,361 |
| Total current liabilities | 24,008 | 28,839 |
| Noncurrent liabilities: | | |
| Accrued pension costs | 14,155 | 13,586 |
| Accrued postretirement benefits (OPEB) costs | 2,773 | 2,595 |
| Accrued environmental remediation and related costs | 104,465 | 103,450 |
| Deferred income taxes | 25,035 | 31,651 |
| Other | 13,636 | 13,567 |
| Total noncurrent liabilities | 160,064 | 164,849 |
| Equity: | | |
| NL stockholders' equity: | | |
| Common stock | 6,086 | 6,088 |
| Additional paid-in capital | 300,543 | 300,674 |
| Retained earnings | 88,679 | 94,427 |
| Accumulated other comprehensive loss | (245,358) | (231,080) |
| Total NL stockholders' equity | 149,950 | 170,109 |
| Noncontrolling interest in subsidiary | 15,301 | 16,060 |
| Total equity | 165,251 | 186,169 |
| Total liabilities and equity | $349,323 | $379,857 |

Commitments and contingencies (Notes 11 and 13)

See accompanying notes to Condensed Consolidated Financial Statements.

NL INDUSTRIES, INC. AND SUBSIDIARIES

CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS

(In thousands, except per share data)

| | Three months ended September 30, | | Nine months ended September 30, | |
|---|---|---|---|---|
| | 2015 | 2016 | 2015 | 2016 |
| | (unaudited) | | | |
| Net sales | $26,505 | $28,404 | $83,314 | $82,586 |
| Cost of sales | 18,387 | 19,005 | 57,471 | 56,496 |
| Gross margin | 8,118 | 9,399 | 25,843 | 26,090 |
| Selling, general and administrative expense | 4,684 | 4,926 | 14,402 | 14,547 |
| Other operating income (expense): | | | | |
| Insurance recoveries | 113 | 76 | 3,480 | 399 |
| Other income | 74 | — | 91 | 5 |
| Corporate expense | (2,659 ) | (4,555 ) | (12,146) | (13,538) |
| Income (loss) from operations | 962 | (6 ) | 2,866 | (1,591 ) |
| Equity in earnings (losses) of Kronos Worldwide, Inc. | (3,600 ) | 6,776 | (46,584) | 6,123 |
| Other income - interest and dividend income | 294 | 430 | 878 | 1,160 |
| Income (loss) before income taxes | (2,344 ) | 7,200 | (42,840) | 5,692 |
| Income tax benefit | (3,581 ) | (560 ) | (25,534) | (1,052 ) |
| Net income (loss) | 1,237 | 7,760 | (17,306) | 6,744 |
| Noncontrolling interest in net income of subsidiary | 294 | 388 | 976 | 996 |
| Net income (loss) attributable to NL stockholders | $943 | $7,372 | $(18,282) | $5,748 |
| Amounts attributable to NL stockholders: | | | | |
| Basic and diluted net income (loss) per share | $.02 | $.15 | $(.38 ) | $.12 |
| Weighted average shares used in the calculation | | | | |
| of net income (loss) per share | 48,692 | 48,706 | 48,687 | 48,699 |

See accompanying notes to Condensed Consolidated Financial Statements.

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NL INDUSTRIES, INC. AND SUBSIDIARIES

CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME (LOSS)

(In thousands)

| | Three months ended September 30, | | Nine months ended September 30, | |
|---|---|---|---|---|
| | 2015 | 2016 | 2015 | 2016 |
| | (unaudited) | | | |
| Net income (loss) | $1,237 | $7,760 | $(17,306) | $6,744 |
| Other comprehensive income (loss), net of tax: | | | | |
| Marketable securities | (34,513) | 6,983 | (41,657) | 9,182 |
| Currency translation | (3,538) | 1,777 | (15,309) | 3,628 |
| Interest rate swap | (733) | 145 | (733) | (583) |
| Defined benefit pension plans | 902 | 817 | 2,723 | 2,447 |
| Other postretirement benefit plans | (137) | (132) | (410) | (396) |
| Total other comprehensive income (loss), net | (38,019) | 9,590 | (55,386) | 14,278 |
| Comprehensive income (loss) | (36,782) | 17,350 | (72,692) | 21,022 |
| Comprehensive income attributable to noncontrolling interest | 294 | 388 | 976 | 996 |
| Comprehensive income (loss) attributable to NL stockholders | $(37,076) | $16,962 | $(73,668) | $20,026 |

See accompanying notes to Condensed Consolidated Financial Statements.

NL INDUSTRIES, INC. AND SUBSIDIARIES

CONDENSED CONSOLIDATED STATEMENT OF EQUITY

Nine months ended September 30, 2016

(In thousands)

| | Common stock | Additional paid—in capital | Retained earnings | Accumulated other comprehensive income (loss) | Noncontrolling interest in subsidiary | Total equity |
|---|---|---|---|---|---|---|
| | (unaudited) | | | | | |
| Balance at December 31, 2015 | $6,086 | $300,543 | $88,679 | $(245,358) | $15,301 | $165,251 |
| Net income | — | — | 5,748 | — | 996 | 6,744 |
| Other comprehensive income, net of tax | — | — | — | 14,278 | — | 14,278 |
| Issuance of NL common stock | 2 | 35 | — | — | — | 37 |
| Dividends | — | — | — | — | (249) | (249) |
| Other, net | — | 96 | — | — | 12 | 108 |
| Balance at September 30, 2016 | $6,088 | $300,674 | $94,427 | $(231,080) | $16,060 | $186,169 |

See accompanying notes to Condensed Consolidated Financial Statements.

NL INDUSTRIES, INC. AND SUBSIDIARIES

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

(In thousands)

| | Nine months ended September 30, | |
|---|---|---|
| | 2015 | 2016 |
| | (unaudited) | |
| Cash flows from operating activities: | | |
| Net income (loss) | $(17,306) | $6,744 |
| Depreciation and amortization | 2,699 | 2,847 |
| Deferred income taxes | (20,978) | (1,080) |
| Equity in earnings of Kronos Worldwide, Inc. | 46,584 | (6,123) |
| Dividends received from Kronos Worldwide, Inc. | 15,849 | 15,849 |
| Cash funding of benefit plans in excess of net benefit plan expense | (1,116) | (267) |
| Other, net | 348 | 385 |
| Change in assets and liabilities: | | |
| Accounts and other receivables, net | (2,583) | (4,303) |
| Inventories, net | 1,246 | 280 |
| Prepaid expenses and other | (40) | 125 |
| Accounts payable and accrued liabilities | (1,805) | 50 |
| Income taxes | — | (4) |
| Accounts with affiliates | (1,497) | (34) |
| Accrued environmental remediation and related costs | 1,596 | 3,679 |
| Other noncurrent assets and liabilities, net | (4,700) | (259) |
| Net cash provided by operating activities | 18,297 | 17,889 |
| Cash flows from investing activities: | | |
| Capital expenditures | (2,570) | (2,354) |
| Change in restricted cash equivalents, net | 348 | (53) |
| Notes receivable from affiliate: | | |
| Loans | — | (15,100) |
| Proceeds from collection | — | 4,400 |
| Proceeds from the sale of marketable securities | 255 | — |
| Purchase of marketable securities | (251) | — |
| Net cash used in investing activities | (2,218) | (13,107) |
| Cash flows from financing activities — | | |
| Distributions to noncontrolling interests in subsidiary | (247) | (249) |
| Cash and cash equivalents — net change from: | | |
| Operating, investing and financing activities | 15,832 | 4,533 |
| Cash and cash equivalents at beginning of period | 72,560 | 96,462 |

| | | |
|---|---|---|
| Cash and cash equivalents at end of period | $88,392 | $100,995 |
| | | |
| Supplemental disclosure — cash paid for: | | |
| Income taxes, net | $1,587 | $61 |

See accompanying notes to Condensed Consolidated Financial Statements.

NL INDUSTRIES, INC. AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

September 30, 2016

(unaudited)

Note 1 – Organization and basis of presentation:

Organization – At September 30, 2016, Valhi, Inc. (NYSE: VHI) held approximately 83% of our outstanding common stock and a wholly-owned subsidiary of Contran Corporation held approximately 93% of Valhi's outstanding common stock. All of Contran's outstanding voting stock is held by a family trust established for the benefit of Lisa K. Simmons and Serena Simmons Connelly and their children for which Ms. Simmons and Ms. Connelly are co-trustees, or is held directly by Ms. Simmons and Ms. Connelly or entities related to them. Consequently, Ms. Simmons and Ms. Connelly may be deemed to control Contran, Valhi and us.

Basis of presentation – Consolidated in this Quarterly Report are the results of our majority-owned subsidiary, CompX International Inc. We also own 30% of Kronos Worldwide, Inc. (Kronos). CompX (NYSE MKT: CIX) and Kronos (NYSE: KRO); each file periodic reports with the Securities and Exchange Commission (SEC).

The unaudited Condensed Consolidated Financial Statements contained in this Quarterly Report have been prepared on the same basis as the audited Consolidated Financial Statements in our Annual Report on Form 10-K for the year ended December 31, 2015 that we filed with the SEC on March 10, 2016 (the 2015 Annual Report). In our opinion, we have made all necessary adjustments (which include only normal recurring adjustments) in order to state fairly, in all material respects, our consolidated financial position, results of operations and cash flows as of the dates and for the periods presented. We have condensed the Consolidated Balance Sheet at December 31, 2015 contained in this Quarterly Report as compared to our audited Consolidated Financial Statements at that date, and we have omitted certain information and footnote disclosures (including those related to the Consolidated Balance Sheet at December 31, 2015) normally included in financial statements prepared in accordance with accounting principles generally accepted in the United States of America (GAAP). Our results of operations for the interim periods ended September 30, 2016 may not be indicative of our operating results for the full year. The Condensed Consolidated Financial Statements contained in this Quarterly Report should be read in conjunction with our 2015 Consolidated Financial Statements contained in our 2015 Annual Report.

Unless otherwise indicated, references in this report to "NL," "we," "us" or "our" refer to NL Industries, Inc. and its subsidiaries and affiliate, Kronos, taken as a whole.

Note 2 – Accounts and other receivables, net:

| | December 31, 2015 | September 30, 2016 |
|---|---|---|
| | (In thousands) | |
| Trade receivables — CompX | $8,847 | $ 13,110 |

| | | |
|---|---|---|
| Accrued insurance recoveries | 138 | 92 |
| Other receivables | 79 | 150 |
| Allowance for doubtful accounts | (87 ) | (70 ) |
| | | |
| Total | $ 8,977 | $ 13,282 |

Accrued insurance recoveries are discussed in Note 13.

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Note 3 – Inventories, net:

| | December 31, 2015 | September 30, 2016 |
|---|---|---|
| | (In thousands) | |
| Raw materials | $2,807 | $ 2,739 |
| Work in process | 9,346 | 9,143 |
| Finished products | 2,945 | 2,756 |
| | | |
| Total | $15,098 | $ 14,638 |

Note 4 – Marketable securities:

| | Fair value measurement level | Market value | Cost basis | Unrealized gain (loss) |
|---|---|---|---|---|
| | | (In thousands) | | |
| December 31, 2015 | | | | |
| Valhi common stock | 1 | $19,260 | $24,347 | $ (5,087 ) |
| | | | | |
| September 30, 2016 | | | | |
| Valhi common stock | 1 | $33,058 | $24,347 | $ 8,711 |

At December 31, 2015 and September 30, 2016, we held approximately 14.4 million shares of common stock of our immediate parent company, Valhi.  See Note 1.  We account for our investment in Valhi common stock as available-for-sale marketable equity securities and any unrealized gains or losses on the securities are recognized through other comprehensive income, net of deferred income taxes.  Our shares of Valhi common stock are carried at fair value based on quoted market prices, representing a Level 1 input within the fair value hierarchy.  At December 31, 2015 and September 30, 2016, the quoted per share market price of Valhi common stock was $1.34 and $2.30, respectively.

The Valhi common stock we own is subject to the restrictions on resale pursuant to certain provisions of the SEC Rule 144.  In addition, as a majority-owned subsidiary of Valhi, we cannot vote our shares of Valhi common stock under Delaware General Corporation Law, but we do receive dividends from Valhi on these shares, when declared and paid.

Note 5 – Investment in Kronos Worldwide, Inc.:

At December 31, 2015 and September 30, 2016, we owned approximately 35.2 million shares of Kronos common stock.  At September 30, 2016, the quoted market price of Kronos' common stock was $8.29 per share, or an aggregate market value of $292.0 million.  At December 31, 2015, the quoted market price was $5.64 per share, or an aggregate market value of $198.6 million.

The change in the carrying value of our investment in Kronos during the first nine months of 2016 is summarized below.

| | Amount (In millions) |
|---|---|
| Balance at the beginning of the period | $ 140.7 |
| Equity in earnings of Kronos | 6.1 |
| Dividends received from Kronos | (15.8 ) |
| Equity in Kronos' other comprehensive income (loss): | |
| Marketable securities | .3 |
| Currency translation | 5.6 |
| Interest rate swap | (.9 ) |
| Defined benefit pension plans | 2.6 |
| | |
| Balance at the end of the period | $ 138.6 |

Selected financial information of Kronos is summarized below:

| | December 31, 2015 | September 30, 2016 |
|---|---|---|
| | (In millions) | |
| Current assets | $710.8 | $ 690.5 |
| Property and equipment, net | 429.5 | 446.6 |
| Investment in $TiO_2$ joint venture | 82.9 | 79.8 |
| Other noncurrent assets | 19.5 | 24.6 |
| | | |
| Total assets | $1,242.7 | $ 1,241.5 |
| | | |
| Current liabilities | $201.7 | $ 206.5 |
| Long-term debt | 337.2 | 336.0 |
| Accrued pension and postretirement benefits | 209.4 | 210.3 |
| Other noncurrent liabilities | 32.5 | 33.8 |
| Stockholders' equity | 461.9 | 454.9 |
| | | |
| Total liabilities and stockholders' equity | $1,242.7 | $ 1,241.5 |

| | Three months ended September 30, | | Nine months ended September 30, | |
|---|---|---|---|---|
| | 2015 | 2016 | 2015 | 2016 |
| | (In millions) | | | |

| | | | | |
|---|---|---|---|---|
| Net sales | $336.5 | $356.1 | $1,061.8 | $1,030.6 |
| Cost of sales | 293.3 | 280.6 | 894.7 | 859.2 |
| Income (loss) from operations | (3.2 ) | 28.0 | 18.6 | 38.2 |
| Income tax expense (benefit) | (7.4 ) | 0.7 | 147.1 | 3.2 |
| Net income (loss) | (11.8 ) | 22.2 | (153.2 ) | 20.1 |

Note 6 – Other noncurrent assets, net:

| | December 31, 2015 | September 30, 2016 |
|---|---|---|
| | (In thousands) | |
| Pension asset | $1,303 | 1,434 |
| Restricted cash | 1,273 | $ 1,279 |
| Other | 755 | 945 |
| Total | $3,331 | $ 3,658 |

Note 7 – Accrued and other current liabilities:

| | December 31, 2015 | September 30, 2016 |
|---|---|---|
| | (In thousands) | |
| Employee benefits | $8,438 | $ 7,457 |
| Professional fees | 698 | 290 |
| Payables to affiliates: | | |
| Income taxes - Valhi | 40 | 11 |
| Other | 180 | 179 |
| Income taxes | 5 | 7 |
| Other | 1,422 | 2,147 |
| Total | $10,783 | $ 10,091 |

Note 8 – Other noncurrent liabilities:

| | December 31, 2015 | September 30, 2016 |
|---|---|---|
| | (In thousands) | |
| Reserve for uncertain tax positions | $12,186 | $ 12,186 |
| Insurance claims and expenses | 663 | 639 |
| Other | 787 | 742 |
| Total | $13,636 | $ 13,567 |

Our reserve for uncertain tax positions is discussed in Note 11.

Note 9 – Long-term debt:

During the first nine months of 2016, we had no borrowing under our promissory note with Valhi, and at September 30, 2016, the full $40 million was available for borrowing under this facility. The amount of any such loan Valhi would make to us is at Valhi’s discretion.

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Note 10 – Accumulated other comprehensive income (loss):

Changes in accumulated other comprehensive income (loss) attributable to NL stockholders, including amounts resulting from our investment in Kronos Worldwide (see Note 5), are presented in the table below.

| | Three months ended September 30, | | Nine months ended September 30, | |
|---|---|---|---|---|
| | 2015 | 2016 | 2015 | 2016 |
| | (In thousands) | | | |
| Accumulated other comprehensive loss, net of tax: | | | | |
| Marketable securities: | | | | |
| Balance at beginning of period | $39,968 | $2,394 | $47,112 | $195 |
| Other comprehensive income - unrealized gains (losses) arising during the year | (34,513 ) | 6,983 | (41,657 ) | 9,182 |
| Balance at end of period | $5,455 | $9,377 | $5,455 | $9,377 |
| Currency translation: | | | | |
| Balance at beginning of period | $(165,944) | $(170,533) | $(154,173) | $(172,384) |
| Other comprehensive income (loss) | (3,538 ) | 1,777 | (15,309 ) | 3,628 |
| Balance at end of period | $(169,482) | $(168,756) | $(169,482) | $(168,756) |
| Interest rate swap: | | | | |
| Balance at beginning of period | $— | $(1,173 ) | $— | $(445 ) |
| Other comprehensive loss: | | | | |
| Unrealized gains (losses) arising during the year | $(733 ) | $32 | $(733 ) | $(920 ) |
| Less reclassification adjustment for amounts included in interest expense | — | 113 | — | 337 |
| Balance at end of period | $(733 ) | $(1,028 ) | $(733 ) | $(1,028 ) |
| Defined benefit pension plans: | | | | |
| Balance at beginning of period | $(73,439 ) | $(71,082 ) | $(75,260 ) | $(72,712 ) |
| Other comprehensive income - amortization of net losses included in net periodic pension cost | 902 | 817 | 2,723 | 2,447 |
| Balance at end of period | $(72,537 ) | $(70,265 ) | $(72,537 ) | $(70,265 ) |
| OPEB plans: | | | | |

| | | | | |
|---|---|---|---|---|
| Balance at beginning of period | $9 | $(276) | $282 | $(12) |
| Other comprehensive loss - amortization of prior service credit and net gains included in net periodic OPEB cost | (137) | (132) | (410) | (396) |
| Balance at end of period | $(128) | $(408) | $(128) | $(408) |
| Total accumulated other comprehensive loss: | | | | |
| Balance at beginning of period | $(199,406) | $(240,670) | $(182,039) | $(245,358) |
| Other comprehensive income (loss) | (38,019) | 9,590 | (55,386) | 14,278 |
| Balance at end of period | $(237,425) | $(231,080) | $(237,425) | $(231,080) |

See Note 12 for amounts related to our defined benefit pension plans and OPEB plans.

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Note 11 – Income taxes:

| | Three months ended September 30, | | Nine months ended September 30, | |
|---|---|---|---|---|
| | 2015 | 2016 | 2015 | 2016 |
| | (In millions) | | | |
| Expected tax expense (benefit), at U.S. federal statutory income tax rate of 35% | $(.8) | $2.5 | $(15.0) | $2.0 |
| Rate differences on equity in earnings (losses) of Kronos | (2.7) | (3.0) | (7.4) | (2.8) |
| Adjustment to the reserve for uncertain tax positions, net | — | — | (3.0) | — |
| Nontaxable income | (.1) | (.2) | (.3) | (.4) |
| U.S. state income taxes and other, net | .1 | .1 | .2 | .1 |
| Income tax expense (benefit) | $(3.5) | $(.6) | $(25.5) | $(1.1) |
| Comprehensive provision for income taxes (benefit) allocable to: | | | | |
| Net income (loss) | $(3.5) | $(.6) | $(25.5) | $(1.1) |
| Other comprehensive income (loss): | | | | |
| Marketable securities | (18.6) | 3.7 | (22.4) | 4.9 |
| Currency translation | (2.0) | 1.0 | (8.3) | 2.0 |
| Interest rate swap | (.4) | .1 | (.4) | (.3) |
| Pension plans | .5 | .4 | 1.5 | 1.3 |
| OPEB plans | — | (.1) | (.2) | (.2) |
| Total | $(24.0) | $4.5 | $(55.3) | $6.6 |

In accordance with GAAP, we recognize deferred income taxes on our undistributed equity in earnings (losses) of Kronos. Because we and Kronos are part of the same U.S. federal income tax group, any dividends we receive from Kronos are nontaxable to us. Accordingly, we do not recognize and we are not required to pay income taxes on dividends from Kronos. We received aggregate dividends from Kronos of $15.8 million in the first nine months of 2015 and 2016. The amounts shown in the above table of our income tax rate reconciliation for rate differences on equity in earnings (losses) of Kronos represents the net tax (benefit) associated with such non-taxability of the dividends we receive from Kronos, as it relates to the amount of deferred income taxes we recognize on our undistributed equity in earnings (losses) of Kronos.

Kronos has substantial net operating losses in Germany and Belgium, the benefit of which Kronos had previously recognized under the more-likely-than-not recognition criteria. In the second quarter of 2015, Kronos determined that such losses did not meet the more-likely-than-not recognition criteria, and as a result Kronos recognized a non-cash deferred income tax expense of $150.3 million in the second quarter of 2015 as a valuation allowance against Kronos' net deferred income tax assets in such jurisdictions. Kronos recognized an additional $2.3 million non-cash deferred income tax asset valuation allowance during the third quarter of 2015 and recognized an aggregate $2.1 million non-cash deferred income tax asset valuation allowance in the first nine months of 2016 (mostly in the second quarter) as additional valuation allowance against additional losses in such jurisdictions. The rate difference related to our equity in losses of Kronos in the third quarter and first nine months of 2015 and 2016 includes our equity in such non-cash deferred income tax expense recognized by Kronos.

Tax authorities are examining certain of our U.S. and non-U.S. tax returns, including those of Kronos, and tax authorities have or may propose tax deficiencies, including penalties and interest. Because of the inherent uncertainties involved in settlement initiatives and court and tax proceedings, we cannot guarantee that these matters will be resolved in our favor, and therefore our potential exposure, if any, is also uncertain. As a result of ongoing audits in in certain jurisdictions, in 2008 Kronos filed Advance Pricing Agreement Requests with the tax authorities in the U.S., Canada and Germany. These requests have been under review with the respective tax authorities since 2008 and prior to the third quarter of 2016, it was uncertain whether an agreement would be reached between the tax authorities and whether Kronos would agree to execute and finalize such agreements. During the third quarter of 2016, Contran, as the ultimate parent of our U.S. Consolidated income tax group, executed and finalized an Advance Pricing Agreement with the U.S. Internal Revenue Service and Kronos' Canadian subsidiary executed and finalized an Advance Pricing Agreement with the Competent Authority for Canada (collectively, the "U.S.-Canada APA") effective for tax years 2005 - 2015. Pursuant to the terms of the U.S.-Canada APA, the U.S. and Canadian tax authorities agreed to certain prior year changes to taxable income of the U.S. and Canadian subsidiaries. As a result of such agreed-upon changes, Kronos recognized a $5.6 million current U.S. income tax benefit in the third quarter of 2016. In addition, Kronos' Canadian subsidiary will incur a cash income tax payment of approximately CAD $3 million (USD $2.3 million) as a result of the U.S.-Canada APA, but such payment was fully offset by previously provided accruals. Kronos currently expects the Advance Pricing Agreement between Canada and Germany (collectively, the "Canada-Germany APA") to be executed and finalized within the next twelve months. Kronos believes it has adequate accruals to cover any cash income tax payment which might result from the finalization of the Canada-Germany APA, and accordingly does not expect the execution of such APA to have a material adverse effect on its consolidated financial position, results of operations or liquidity. We believe we have adequate accruals for additional taxes and related interest expense which could ultimately result from tax examinations. We believe the ultimate disposition of tax examinations should not have a material adverse effect on our consolidated financial position, results of operations or liquidity. The rate difference related to our equity in losses of Kronos in the third quarter and first nine months of 2016 includes our equity in such current tax benefit recognized by Kronos.

In the first nine months of 2015, we recognized a first quarter non-cash income tax benefit of $3.0 million related to the release of a portion of our reserve for uncertain tax positions due to the expiration of the applicable statute of limitations. We currently estimate that our unrecognized tax benefits will not change materially during the next twelve months.

Note 12 – Employee benefit plans:

Defined benefit plans – The components of net periodic defined benefit pension cost (income) are presented in the table below.

| | Three months ended September 30, | | Nine months ended September 30, | |
|---|---|---|---|---|
| | 2015 | 2016 | 2015 | 2016 |
| | (In thousands) | | | |
| Interest cost | $597 | $585 | $1,801 | $1,778 |
| Expected return on plan assets | (840) | (723) | (2,516) | (2,194) |
| Recognized actuarial losses | 349 | 406 | 1,025 | 1,314 |
| Total | $106 | $268 | $310 | $898 |

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Postretirement benefits – The components of net periodic postretirement benefits other than pension (OPEB) income are presented in the table below.

| | Three months ended September 30, | | Nine months ended September 30, | |
|---|---|---|---|---|
| | 2015 | 2016 | 2015 | 2016 |
| | (In thousands) | | | |
| Interest cost | $27 | $24 | $81 | $72 |
| Amortization of prior service credit | (155) | (135) | (466) | (406) |
| Recognized actuarial gains | (25) | (38) | (76) | (114) |
| Total | $(153) | $(149) | $(461) | $(448) |

Contributions – We currently expect our 2016 contributions to our defined benefit pension plans and other postretirement plans to be approximately $1 million.

Note 13 – Commitments and contingencies:

General

We are involved in various environmental, contractual, product liability, patent (or intellectual property), employment and other claims and disputes incidental to our current and former businesses. At least quarterly our management discusses and evaluates the status of any pending litigation or claim to which we are a party or which has been asserted against us. The factors considered in such evaluation include, among other things, the nature of such pending cases and claims, the status of such pending cases and claims, the advice of legal counsel and our experience in similar cases and claims (if any). Based on such evaluation, we make a determination as to whether we believe (i) it is probable a loss has been incurred, and if so if the amount of such loss (or a range of loss) is reasonably estimable, or (ii) it is reasonably possible but not probable a loss has been incurred, and if so if the amount of such loss (or a range of loss) is reasonably estimable, or (iii) the probability a loss has been incurred is remote.

Lead pigment litigation

Our former operations included the manufacture of lead pigments for use in paint and lead-based paint. We, other former manufacturers of lead pigments for use in paint and lead-based paint (together, the "former pigment manufacturers"), and the Lead Industries Association (LIA), which discontinued business operations in 2002, have been named as defendants in various legal proceedings seeking damages for personal injury, property damage and governmental expenditures allegedly caused by the use of lead-based paints. Certain of these actions have been filed by or on behalf of states, counties, cities or their public housing authorities and school districts, and certain others have been asserted as class actions. These lawsuits seek recovery under a variety of theories, including public and private nuisance, negligent product design, negligent failure to warn, strict liability, breach of warranty, conspiracy/concert of action, aiding and abetting, enterprise liability, market share or risk contribution liability, intentional tort, fraud and misrepresentation, violations of state consumer protection statutes, supplier negligence and similar claims.

The plaintiffs in these actions generally seek to impose on the defendants responsibility for lead paint abatement and health concerns associated with the use of lead-based paints, including damages for personal injury, contribution and/or indemnification for medical expenses, medical monitoring expenses and costs for educational programs. To the extent the plaintiffs seek compensatory or punitive damages in these actions, such damages are generally unspecified. In some cases, the damages are unspecified pursuant to the requirements of applicable state law. A number of cases are inactive or have been dismissed or withdrawn. Most of the remaining cases are in various pre-trial stages. Some are on appeal following dismissal or summary judgment rulings or a trial verdict in favor of either the defendants or the plaintiffs.

We believe that these actions are without merit, and we intend to continue to deny all allegations of wrongdoing and liability and to defend against all actions vigorously. We do not believe it is probable that we have incurred any liability with respect to all of the lead pigment litigation cases to which we are a party, and liability to us that may result, if any, in this regard cannot be reasonably estimated, because:

- we have never settled any of the market share, intentional tort, fraud, nuisance, supplier negligence, breach of warranty, conspiracy, misrepresentation, aiding and abetting, enterprise liability, or statutory cases,
- no final, non-appealable adverse verdicts have ever been entered against us, and
- we have never ultimately been found liable with respect to any such litigation matters, including over 100 cases over a twenty-year period for which we were previously a party and for which we have been dismissed without any finding of liability.

Accordingly, we have not accrued any amounts for any of the pending lead pigment and lead—based paint litigation cases filed by or on behalf of states, counties, cities or their public housing authorities and school districts, or those asserted as class actions. In addition, we have determined that liability to us which may result, if any, cannot be reasonably estimated because there is no prior history of a loss of this nature on which an estimate could be made and there is no substantive information available upon which an estimate could be based.

In one of these lead pigment cases, in April 2000 we were served with a complaint in County of Santa Clara v. Atlantic Richfield Company, et al. (Superior Court of the State of California, County of Santa Clara, Case No. 1-00-CV-788657) brought by a number of California government entities against the former pigment manufacturers, the LIA and certain paint manufacturers. The County of Santa Clara sought to recover compensatory damages for funds the plaintiffs have expended or would in the future expend for medical treatment, educational expenses, abatement or other costs due to exposure to, or potential exposure to, lead paint, disgorgement of profit, and punitive damages. In July 2003, the trial judge granted defendants’ motion to dismiss all remaining claims. Plaintiffs appealed and the intermediate appellate court reinstated public nuisance, negligence, strict liability, and fraud claims in March 2006. A fourth amended complaint was filed in March 2011 on behalf of The People of California by the County Attorneys of Alameda, Ventura, Solano, San Mateo, Los Angeles and Santa Clara, and the City Attorneys of San Francisco, San Diego and Oakland. That complaint alleged that the presence of lead paint created a public nuisance in each of the prosecuting jurisdictions and sought its abatement. In July and August 2013, the case was tried. In January 2014, the Judge issued a judgment finding us, The Sherwin Williams Company and ConAgra Grocery Products Company jointly and severally liable for the abatement of lead paint in pre-1980 homes, and ordered the defendants to pay an aggregate $1.15 billion to the people of the State of California to fund such abatement. In February 2014, we filed a motion for a new trial, and in March 2014 the court denied the motion. Subsequently in March 2014, we filed a notice of appeal with the Sixth District Court of Appeal for the State of California and the appeal is proceeding with the appellate court. NL believes that this judgment is inconsistent with California law and is unsupported by the evidence, and we will defend vigorously against all claims.

The Santa Clara case is unusual in that this is the second time that an adverse verdict in the lead pigment litigation has been entered against NL (the first adverse verdict against NL was ultimately overturned on appeal). We have concluded that the likelihood of a loss in this case has not reached a standard of “probable” as contemplated by ASC 450, given (i) the substantive, substantial and meritorious grounds on which the adverse verdict in the Santa Clara case will be appealed, (ii) the uniqueness of the Santa Clara verdict (i.e. no final, non-appealable verdicts have ever been rendered against us, or any of the other former lead pigment manufacturers, based on the public nuisance theory of liability or otherwise), and (iii) the rejection of the public nuisance theory of liability as it relates to lead pigment matters in many other jurisdictions (no jurisdiction in which a plaintiff has asserted a public nuisance theory of liability has ever successfully been upheld). In addition, liability that may result, if any, cannot be reasonably estimated, as NL continues to have no basis on which an estimate of liability could be made, as discussed above.

However, as with any legal proceeding, there is no assurance that any appeal would be successful, and it is reasonably possible, based on the outcome of the appeals process, that NL may in the future incur some liability resulting in the recognition of a loss contingency accrual that could have a material adverse impact on our results of operations, financial position and liquidity.



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New cases may continue to be filed against us. We do not know if we will incur liability in the future in respect of any of the pending or possible litigation in view of the inherent uncertainties involved in court and jury rulings. In the future, if new information regarding such matters becomes available to us (such as a final, non-appealable adverse verdict against us or otherwise ultimately being found liable with respect to such matters), at that time we would consider such information in evaluating any remaining cases then-pending against us as to whether it might then have become probable we have incurred liability with respect to these matters, and whether such liability, if any, could have become reasonably estimable. The resolution of any of these cases could result in the recognition of a loss contingency accrual that could have a material adverse impact on our net income for the interim or annual period during which such liability is recognized and a material adverse impact on our consolidated financial condition and liquidity.

Environmental matters and litigation

Our operations are governed by various environmental laws and regulations. Certain of our businesses are and have been engaged in the handling, manufacture or use of substances or compounds that may be considered toxic or hazardous within the meaning of applicable environmental laws and regulations. As with other companies engaged in similar businesses, certain of our past and current operations and products have the potential to cause environmental or other damage. We have implemented and continue to implement various policies and programs in an effort to minimize these risks. Our policy is to maintain compliance with applicable environmental laws and regulations at all of our plants and to strive to improve environmental performance. From time to time, we may be subject to environmental regulatory enforcement under U.S. and non-U.S. statutes, the resolution of which typically involves the establishment of compliance programs. It is possible that future developments, such as stricter requirements of environmental laws and enforcement policies, could adversely affect our production, handling, use, storage, transportation, sale or disposal of such substances. We believe that all of our facilities are in substantial compliance with applicable environmental laws.

Certain properties and facilities used in our former operations, including divested primary and secondary lead smelters and former mining locations, are the subject of civil litigation, administrative proceedings or investigations arising under federal and state environmental laws and common law. Additionally, in connection with past operating practices, we are currently involved as a defendant, potentially responsible party (PRP) or both, pursuant to the Comprehensive Environmental Response, Compensation and Liability Act, as amended by the Superfund Amendments and Reauthorization Act (CERCLA), and similar state laws in various governmental and private actions associated with waste disposal sites, mining locations, and facilities that we or our predecessors, our subsidiaries or their predecessors currently or previously owned, operated or used, certain of which are on the United States Environmental Protection Agency’s (EPA) Superfund National Priorities List or similar state lists. These proceedings seek cleanup costs, damages for personal injury or property damage and/or damages for injury to natural resources. Certain of these proceedings involve claims for substantial amounts. Although we may be jointly and severally liable for these costs, in most cases we are only one of a number of PRPs who may also be jointly and severally liable, and among whom costs may be shared or allocated. In addition, we are occasionally named as a party in a number of personal injury lawsuits filed in various jurisdictions alleging claims related to environmental conditions alleged to have resulted from our operations.

Obligations associated with environmental remediation and related matters are difficult to assess and estimate for numerous reasons including the:

- complexity and differing interpretations of governmental regulations,
- number of PRPs and their ability or willingness to fund such allocation of costs,
- financial capabilities of the PRPs and the allocation of costs among them,
- solvency of other PRPs,

- multiplicity of possible solutions,
- number of years of investigatory, remedial and monitoring activity required,

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- uncertainty over the extent, if any, to which our former operations might have contributed to the conditions allegedly giving rise to such personal injury, property damage, natural resource and related claims, and
- number of years between former operations and notice of claims and lack of information and documents about the former operations.

In addition, the imposition of more stringent standards or requirements under environmental laws or regulations, new developments or changes regarding site cleanup costs or the allocation of costs among PRPs, solvency of other PRPs, the results of future testing and analysis undertaken with respect to certain sites or a determination that we are potentially responsible for the release of hazardous substances at other sites, could cause our expenditures to exceed our current estimates. We do not know if actual costs will exceed accrued amounts or the upper end of the range for sites for which estimates have been made, and we do not know if costs will be incurred for sites where no estimates presently can be made. Further, additional environmental and related matters may arise in the future. If we were to incur any future liability, this could have a material adverse effect on our consolidated financial statements, results of operations and liquidity.

We record liabilities related to environmental remediation and related matters (including costs associated with damages for personal injury or property damage and/or damages for injury to natural resources) when estimated future expenditures are probable and reasonably estimable. We adjust such accruals as further information becomes available to us or as circumstances change. Unless the amounts and timing of such estimated future expenditures are fixed and reasonably determinable, we generally do not discount estimated future expenditures to their present value due to the uncertainty of the timing of the payout. We recognize recoveries of costs from other parties, if any, as assets when their receipt is deemed probable. At December 31, 2015 and September 30, 2016, we have not recognized any receivables for recoveries.

We do not know and cannot estimate the exact time frame over which we will make payments for our accrued environmental and related costs. The timing of payments depends upon a number of factors, including but not limited to the timing of the actual remediation process; which in turn depends on factors outside of our control. At each balance sheet date, we estimate the amount of our accrued environmental and related costs which we expect to pay within the next twelve months, and we classify this estimate as a current liability. We classify the remaining accrued environmental costs as a noncurrent liability.

Changes in the accrued environmental remediation and related costs during the first nine months of 2016 are as follows:

| | Amount (In thousands) |
|---|---|
| Balance at the beginning of the period | $ 113,133 |
| Additions charged to expense, net | 5,090 |
| Payments, net | (1,412 ) |
| Balance at the end of the period | $ 116,811 |
| Amounts recognized in the Condensed Consolidated Balance Sheet at the end of the period: | |
| Current liability | $ 13,361 |
| Noncurrent liability | 103,450 |
| Balance at the end of the period | $ 116,811 |

On a quarterly basis, we evaluate the potential range of our liability for environmental remediation and related costs at sites where we have been named as a PRP or defendant, including sites for which our wholly-owned environmental management subsidiary, NL Environmental Management Services, Inc. (EMS), has contractually assumed our obligations. At September 30, 2016, we had accrued approximately $117 million related to approximately 42 sites associated with remediation and related matters that we believe are at the present time and/or in their current phase reasonably estimable. The upper end of the range of reasonably possible costs to us for remediation and related matters for which we believe it is possible to estimate costs is approximately $160 million, including the amount currently accrued.

We believe that it is not reasonably possible to estimate the range of costs for certain sites. At September 30, 2016, there were approximately 5 sites for which we are not currently able to reasonably estimate a range of costs. For these sites, generally the investigation is in the early stages, and we are unable to determine whether or not we actually had any association with the site, the nature of our responsibility for the contamination at the site, if any, and the extent of contamination at and cost to remediate the site. The timing and availability of information on these sites is dependent on events outside of our control, such as when the party alleging liability provides information to us. At certain of these previously inactive sites, we have received general and special notices of liability from the EPA and/or state agencies alleging that we, sometimes with other PRPs, are liable for past and future costs of remediating environmental contamination allegedly caused by former operations. These notifications may assert that we, along with any other alleged PRPs, are liable for past and/or future clean-up costs. As further information becomes available to us for any of these sites, which would allow us to estimate a range of costs, we would at that time adjust our accruals. Any such adjustment could result in the recognition of an accrual that would have a material effect on our consolidated financial statements, results of operations and liquidity.

Insurance coverage claims

We are involved in certain legal proceedings with a number of our former insurance carriers regarding the nature and extent of the carriers' obligations to us under insurance policies with respect to certain lead pigment and asbestos lawsuits. The issue of whether insurance coverage for defense costs or indemnity or both will be found to exist for our lead pigment and asbestos litigation depends upon a variety of factors and we cannot assure you that such insurance coverage will be available.

We have agreements with certain of our former insurance carriers pursuant to which the carriers reimburse us for a portion of our future lead pigment litigation defense costs, and one such carrier reimburses us for a portion of our future asbestos litigation defense costs. We are not able to determine how much we will ultimately recover from these carriers for defense costs incurred by us because of certain issues that arise regarding which defense costs qualify for reimbursement. While we continue to seek additional insurance recoveries, we do not know if we will be successful in obtaining reimbursement for either defense costs or indemnity. Accordingly, we recognize insurance recoveries in income only when receipt of the recovery is probable and we are able to reasonably estimate the amount of the recovery.

For a complete discussion of certain litigation involving us and certain of our former insurance carriers, refer to our 2015 Annual Report.

Other litigation

We have been named as a defendant in various lawsuits in several jurisdictions, alleging personal injuries as a result of occupational exposure primarily to products manufactured by our former operations containing asbestos, silica and/or mixed dust. In addition, some plaintiffs allege exposure to asbestos from working in various facilities previously owned and/or operated by us. There are 103 of these types of cases pending, involving a total of approximately 588 plaintiffs.  In addition, the claims of approximately 8,692 plaintiffs have been administratively dismissed or placed on the inactive docket in Ohio state court.  We do not expect these claims will be re-opened unless the plaintiffs meet the courts' medical criteria for asbestos-related claims.  We have not accrued any amounts for this litigation because of the uncertainty of liability and inability to reasonably estimate the liability, if any.  To date, we have not been adjudicated liable in any of these matters.

Based on information available to us, including:

- facts concerning historical operations,
- the rate of new claims,
- the number of claims from which we have been dismissed, and
- our prior experience in the defense of these matters,

we believe that the range of reasonably possible outcomes of these matters will be consistent with our historical costs (which are not material). Furthermore, we do not expect any reasonably possible outcome would involve amounts material to our consolidated financial position, results of operations or liquidity. We have sought and will continue to vigorously seek, dismissal and/or a finding of no liability from each claim. In addition, from time to time, we have received notices regarding asbestos or silica claims purporting to be brought against former subsidiaries, including notices provided to insurers with which we have entered into settlements extinguishing certain insurance policies. These insurers may seek indemnification from us. For a discussion of other legal proceedings to which we are a party, refer to our 2015 Annual Report.

In addition to the litigation described above, we and our affiliates are also involved in various other environmental, contractual, product liability, patent (or intellectual property), employment and other claims and disputes incidental to present and former businesses. In certain cases, we have insurance coverage for these items, although we do not expect additional material insurance coverage for environmental matters.

We currently believe the disposition of all of these various other claims and disputes, individually and in the aggregate, should not have a material adverse effect on our consolidated financial position, results of operations or liquidity beyond the accruals already provided.

Note 14 – Related party transactions:

From time to time, we may have loans and advances outstanding between us and various related parties pursuant to term and demand notes. We generally enter into these loans and advances for cash management purposes. When we loan funds to related parties, we are generally able to earn a higher rate of return on the loan than we would earn if we invested the funds in other instruments, and when we borrow from related parties, we are generally able to pay a lower rate of interest than we would pay if we had incurred third-party indebtedness. While certain of these loans to affiliates may be of a lesser credit quality than cash equivalent instruments otherwise available to us, we believe we have considered the credit risks in the terms of the applicable loans. In this regard, on August 3, 2016 CompX entered into an unsecured revolving demand promissory note with Valhi whereby CompX has agreed to loan Valhi up to $40 million. CompX's loan to Valhi bears interest at prime plus 1.00%, payable quarterly, with all principal due on demand, but in any event no earlier than December 31, 2017. The amount of CompX's outstanding loans to Valhi at any time is at its discretion. At September 30, 2016, the outstanding principal balance receivable from Valhi under the promissory note was $10.7 million.

Note 15 – Financial instruments and fair value measurements:

See Note 4 for information on how we determine fair value of our marketable securities.

The following table presents the financial instruments that are not carried at fair value but which require fair value disclosure at December 31, 2015 and September 30, 2016:

| | December 31, 2015 | September 30, 2016 |
|---|---|---|

| | Carrying amount | Fair value | Carrying amount | Fair value |
|---|---|---|---|---|
| | (In thousands) | | | |
| Cash, cash equivalents and restricted cash | $100,981 | $100,981 | $105,611 | $105,611 |
| Note receivable from affiliate | — | — | 10,700 | 10,700 |
| Noncontrolling interest in CompX common stock | 15,301 | 18,878 | 16,060 | 19,269 |

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The fair value of our noncontrolling interest in CompX stockholders' equity is based upon its quoted market price at each balance sheet date, which represents a Level 1 input. The fair value of our variable-rate promissory note receivable from affiliate is deemed to approximate book value using Level 2 inputs. Due to their near-term maturities, the carrying amounts of accounts receivable and accounts payable are considered equivalent to fair value.

Note 16 – Recent accounting pronouncements not yet adopted:

In May 2014, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update (ASU) No. 2014-09, Revenue from Contracts with Customers (Topic 606). This standard replaces existing revenue recognition guidance, which in many cases was tailored for specific industries, with a uniform accounting standard applicable to all industries and transactions. The new standard, as amended, is currently effective for us beginning with the first quarter of 2018. Entities may elect to adopt ASU No. 2014-09 retrospectively for all periods for all contracts and transactions which occurred during the period (with a few exceptions for practical expediency) or retrospectively with a cumulative effect recognized as of the date of adoption. ASU No. 2014-09 is a fundamental rewriting of existing GAAP with respect to revenue recognition, and we are still evaluating the effect the Standard will have on our Consolidated Financial Statements. We currently expect to adopt the standard in the first quarter of 2018. In addition, we have not yet determined the method we will use to adopt the Standard.

In January 2016, the FASB issued ASU 2016-01, Financial Instruments—Overall (Subtopic 825-10): Recognition and Measurement of Financial Assets and Financial Liabilities, which addresses certain aspects related to the recognition, measurement, presentation and disclosure of financial instruments. The ASU requires equity investments (except for those accounted for under the equity method of accounting or those that result in the consolidation of the investee) to generally be measured at fair value with changes in fair value recognized in net income. The amendment also requires a number of other changes, including among others: simplifying the impairment assessment for equity instruments without readily determinable fair values; eliminating the requirement for public business entities to disclose method and assumptions used to determine fair value for financial instruments measured at amortized cost; requiring an exit price notion when measuring the fair value of financial instruments for disclosure purposes; and requiring separate presentation of financial assets and liabilities by measurement category and form of asset. The changes indicated above will be effective for us beginning in the first quarter of 2018, with prospective application required, and early adoption is not permitted. The most significant aspect of adopting this ASU will be the requirement to recognize changes in fair value of our available-for-sale marketable equity securities in net income (currently changes in fair value of such securities are recognized in other comprehensive income).

In August 2016, the FASB issued ASU No. 2016-15, Statement of Cash Flows (Topic 230): Classification of Certain Cash Receipts and Cash Payments. This standard provides guidance on eight specific cash flow issues including: debt prepayment or debt extinguishment costs, proceeds from the settlement of insurance claims, distributions from equity method investees and separately identifiable cash flows and application of the predominance principle. The new standard is effective for us beginning with the first quarter of 2018. ASU 2016-15 is to be adopted with retrospective presentation and early adoption is permitted provided all provisions are adopted. We have not yet determined when we will adopt ASU 2016-15. The adoption of the standard will not have a material effect on our Consolidated Financial Statements.

In October 2016, the FASB issued ASU 2016-16, Income Taxes (Topic 740) Intra-Entity Transfers of Assets Other Than Inventory. Currently an entity would not recognize the income tax consequences of an intra-entity transfer of assets other than inventory until final disposition to a third—party. Under the new guidance an entity should recognize the income tax consequences of an intra-entity transfer of an asset other than inventory when the transfer occurs. No additional disclosures are required under this pronouncement. This standard is effective for us in the first quarter of 2018 and early adoption is permitted. From time to time we engage in intra-entity asset transfers that may fall under the new guidance but we do not expect the adoption of this standard to have a material effect on our Consolidated

Financial Statements.

ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

RESULTS OF OPERATIONS:

Business overview

We are primarily a holding company. We operate in the component products industry through our majority-owned subsidiary, CompX International Inc. We also own a non-controlling interest in Kronos Worldwide, Inc. Both CompX (NYSE MKT: CIX) and Kronos (NYSE: KRO) file periodic reports with the Securities and Exchange Commission (SEC).

CompX is a leading manufacturer of engineered components utilized in a variety of applications and industries. Through its Security Products operations, CompX manufactures mechanical and electronic cabinet locks and other locking mechanisms used in recreational transportation, postal, office and institutional furniture, cabinetry, tool storage and healthcare applications. CompX also manufactures stainless steel exhaust systems, gauges, throttle controls and trim tabs for the recreational marine and other industries through its Marine Components operations.

We account for our 30% non-controlling interest in Kronos by the equity method. Kronos is a leading global producer and marketer of value-added titanium dioxide pigments ($TiO_2$). $TiO_2$ is used for a variety of manufacturing applications including paints, plastics, paper and other industrial and specialty products.

Forward-looking information

This report contains forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995, as amended. Statements in this Quarterly Report on Form 10-Q that are not historical facts are forward-looking in nature and represent management's beliefs and assumptions based on currently available information. Statements in this report including, but not limited to, statements found in Item 2 — "Management's Discussion and Analysis of Financial Condition and Results of Operations," are forward-looking statements that represent our management's beliefs and assumptions based on currently available information. In some cases you can identify forward-looking statements by the use of words such as "believes," "intends," "may," "should," "could," "anticipates," "expects" or comparable terminolog by discussions of strategies or trends. Although we believe the expectations reflected in forward-looking statements are reasonable, we do not know if these expectations will be correct. Such statements by their nature involve substantial risks and uncertainties that could significantly impact expected results. Actual future results could differ materially from those predicted. The factors that could cause our actual future results to differ materially from those described herein are the risks and uncertainties discussed in this Quarterly Report and those described from time to time in our other filings with the SEC including, but are not limited to, the following:

- Future supply and demand for our products
- The extent of the dependence of certain of our businesses on certain market sectors
- The cyclicality of our businesses (such as Kronos' $TiO_2$ operations)
- Customer and producer inventory levels
- Unexpected or earlier-than-expected industry capacity expansion (such as the $TiO_2$ industry)
- Changes in raw material and other operating costs (such as energy, ore, zinc and brass costs) and our ability to pass those costs on to our customers or offset them with reductions in other operating costs
- Changes in the availability of raw material (such as ore)
- General global economic and political conditions (such as changes in the level of gross domestic product in various regions of the world and the impact of such changes on demand for, among other things, $TiO_2$ and component products)
- Competitive products and substitute products

- Price and product competition from low-cost manufacturing sources (such as China)

- Customer and competitor strategies
- Potential consolidation of Kronos' competitors
- Potential consolidation of Kronos' customers
- The impact of pricing and production decisions
- Competitive technology positions
- Potential difficulties in integrating future acquisitions
- Potential difficulties in upgrading or implementing new accounting and manufacturing software systems
- The introduction of trade barriers
- Possible disruption of Kronos' or CompX's business, or increases in our cost of doing business resulting from terrorist activities or global conflicts
- The impact of current or future government regulations (including employee healthcare benefit related regulations)
- Fluctuations in currency exchange rates (such as changes in the exchange rate between the U.S. dollar and each of the euro, the Norwegian krone and the Canadian dollar), or possible disruptions to our business resulting from potential instability resulting from uncertainties associated with the euro or other currencies
- Operating interruptions (including, but not limited to, labor disputes, leaks, natural disasters, fires, explosions, unscheduled or unplanned downtime, transportation interruptions and cyber attacks)
- Decisions to sell operating assets other than in the ordinary course of business
- Kronos' ability to renew or refinance credit facilities
- Our ability to maintain sufficient liquidity
- The timing and amounts of insurance recoveries
- The extent to which our subsidiaries or affiliates were to become unable to pay us dividends
- The ultimate outcome of income tax audits, tax settlement initiatives or other tax matters
- Uncertainties associated with CompX's development of new product features
- Our ability to utilize income tax attributes or changes in income tax rates related to such attributes, the benefits of which may not have been recognized under the more-likely-than-not recognition criteria
- Environmental matters (such as those requiring compliance with emission and discharge standards for existing and new facilities or new developments regarding environmental remediation at sites related to our former operations)
- Government laws and regulations and possible changes therein (such as changes in government regulations which might impose various obligations on former manufacturers of lead pigment and lead-based paint, including us, with respect to asserted health concerns associated with the use of such products)
- The ultimate resolution of pending litigation (such as our lead pigment and environmental matters)
- Possible future litigation.

Should one or more of these risks materialize (or if the consequences of such a development worsen), or should the underlying assumptions prove incorrect, actual results could differ materially from those currently forecasted or expected. We disclaim any intention or obligation to update or revise any forward-looking statement whether as a result of changes in information, future events or otherwise.

Results of operations

Net income (loss) overview

Quarter ended September 30, 2016 compared to the quarter ended September 30, 2015

Our net income attributable to NL stockholders was $7.4 million, or $.15 per share, in the third quarter of 2016 compared to $.9 million, or $.02 per share, in the third quarter of 2015. As more fully described below, the increase in our earnings per share from 2015 to 2016 is primarily due to the net effects of:

- equity in earnings from Kronos in 2016 of $6.8 million compared to equity in losses from Kronos in 2015 of $3.6 million,
- higher income from operations attributable to CompX of $1.1 million, and
- higher environmental remediation and related costs in 2016 of $2.1 million.

Our 2015 net income attributable to NL stockholders includes:

- loss of $.03 per share, net of income taxes, included in our equity in losses of Kronos related to Kronos' recognition of an other-than-temporary impairment charge in a marketable equity security.

Our 2016 net income attributable to NL stockholders includes:

- income of $.02 per share, net of income taxes, included in our equity in earnings of Kronos related to Kronos' current income tax benefit related to the execution and finalization of an Advance Pricing Agreement between the U.S. and Canada.

Nine months ended September 30, 2016 compared to nine months ended September 30, 2015

Our net income attributable to NL stockholders was $5.7 million, or $.12 per share, in the first nine months of 2016 compared to net loss attributable to NL stockholders of $18.3 million, or $.38 per share, in the first nine months of 2015. As more fully described below, the increase in our earnings per share from 2015 to 2016 is primarily due to the net effects of:

- equity in earnings from Kronos in 2016 of $6.1 million compared to equity in losses from Kronos in 2015 of $46.6 million,
- lower insurance recoveries in 2016 of $3.1 million primarily related to an insurance recovery settlement for certain past lead pigment litigation defense costs in the first quarter of 2015,
- a first quarter non-cash income tax benefit in 2015 related to a net reduction in our reserve for uncertain tax positions of $3.0 million,
- higher environmental remediation and related costs in 2016 of $2.5 million, and
- lower litigation fees and related costs in 2016 of $1.4 million.

Our 2016 net income attributable to NL stockholders includes:

- income of $.02 per share, net of income taxes, included in our equity in earnings of Kronos related to Kronos' current income tax benefit related to the execution and finalization of an Advance Pricing Agreement between the U.S. and Canada.
- income of $.01 per share, net of income taxes, included in our equity in earnings of Kronos related to Kronos' insurance settlement gain related to a 2014 business interruption claim, and
- loss of $.01 per share, net of income taxes, included in our equity in earnings of Kronos related to Kronos' recognition of a deferred income tax asset valuation allowance related to its German and Belgian operations.

Our 2015 net loss attributable to NL stockholders includes:

- loss of $.62 per share, net of income taxes, included in our equity in losses of Kronos related to Kronos' recognition of a deferred income tax asset valuation allowance related to its German and Belgian operations,
- loss of $.07 per share, net of income taxes, included in our equity in losses of Kronos related to certain workforce reduction charges recognized by Kronos,
- income of $.06 per share related to a net reduction of our reserve for uncertain tax positions,
- income of $.05 per share, net of income taxes, related to insurance recoveries we recognized, and
- loss of $.03 per share, net of income taxes, included in our equity in losses of Kronos related to Kronos' recognition of an other-than-temporary impairment charge in a marketable equity security.

Income (loss) from operations

The following table shows the components of our income (loss) from operations.

| | Three months ended | | | Nine months ended | | |
|---|---|---|---|---|---|---|
| | September 30, | | % | September 30, | | % |
| | 2015 | 2016 | Change | 2015 | 2016 | Change |
| | (In millions) | | | (In millions) | | |
| CompX | $ 3.4 | $ 4.5 | 32 % | $ 11.4 | $ 11.5 | 1 % |
| Insurance recoveries | .1 | .1 | - | 3.5 | 0.4 | (89 ) |
| Other income, net | .1 | - | (100 ) | .1 | — | (100 ) |