

CRANE CO /DE/  
Form 10-Q  
May 08, 2014  
UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION  
Washington, D.C. 20549  
FORM 10-Q

Mark One:

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

For the Quarterly Period Ended March 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 Number: 1-1657

CRANE CO.

(Exact name of registrant as specified in its charter)

Delaware 13-1952290  
(State or other jurisdiction of (I.R.S. Employer  
incorporation or organization) Identification No.)  
100 First Stamford Place, Stamford, CT 06902  
(Address of principal executive offices) (Zip Code)

Registrant's telephone number, including area code: 203-363-7300

(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 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 definitions of "large accelerated filer", "accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act.

(check one):

Large accelerated filer  Accelerated filer

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

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

The number of shares outstanding of the issuer's classes of common stock, as of April 30, 2014

Common stock, \$1.00 Par Value - 58,840,757 shares

PART I: FINANCIAL INFORMATION  
ITEM 1: FINANCIAL STATEMENTS  
CRANE CO. AND SUBSIDIARIES  
CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS  
(IN THOUSANDS, EXCEPT PER SHARE DATA)  
(UNAUDITED)

	Three Months Ended	
	March 31,	
	2014	2013
Net sales	\$716,830	\$627,571
Operating costs and expenses:		
Cost of sales	462,734	409,819
Selling, general and administrative	157,946	130,852
Restructuring charges	10,037	—
Acquisition integration related charges	4,727	—
Operating profit	81,386	86,900
Other income (expense):		
Interest income	388	632
Interest expense	(9,809)	) (6,718)
Miscellaneous - net	(204)	) (120)
	(9,625)	) (6,206)
Income before income taxes	71,761	80,694
Provision for income taxes	22,889	22,752
Net income before allocation to noncontrolling interests	48,872	57,942
Less: Noncontrolling interest in subsidiaries' earnings	188	151
Net income attributable to common shareholders	\$48,684	\$57,791
Earnings per basic share	\$0.83	\$1.01
Earnings per diluted share	\$0.82	\$0.99
Average basic shares outstanding	58,516	57,479
Average diluted shares outstanding	59,514	58,389
Dividends per share	\$0.30	\$0.28

See Notes to Condensed Consolidated Financial Statements

CRANE CO. AND SUBSIDIARIES  
 CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME  
 (IN THOUSANDS)  
 (UNAUDITED)

	Three Months Ended	
	March 31,	
	2014	2013
Net income before allocation to noncontrolling interests	\$48,872	\$57,942
Other comprehensive (loss) income, net of tax		
Currency translation adjustment	(2,536	) (19,901
Changes in pension and postretirement plan assets and benefit obligation, net of tax	1,508	2,104
Other comprehensive (loss) income	(1,028	) (17,797
Comprehensive income before allocation to noncontrolling interests	47,844	40,145
Less: Noncontrolling interests in comprehensive (loss) income	163	161
Comprehensive income attributable to common shareholders	\$47,681	\$39,984
See Notes to Condensed Consolidated Financial Statements.		

CRANE CO. AND SUBSIDIARIES  
 CONDENSED CONSOLIDATED BALANCE SHEETS  
 (IN THOUSANDS)  
 (UNAUDITED)

	March 31, 2014	December 31, 2013
Assets		
Current assets:		
Cash and cash equivalents	\$250,274	\$270,643
Accounts receivable, net	457,180	437,541
Current insurance receivable - asbestos	22,783	22,783
Inventories, net:		
Finished goods	124,917	108,409
Finished parts and subassemblies	36,840	36,645
Work in process	58,093	55,434
Raw materials	169,451	168,398
Inventories, net	389,301	368,886
Current deferred tax asset	31,834	31,651
Other current assets	18,713	17,588
Total current assets	1,170,085	1,149,092
Property, plant and equipment:		
Cost	843,618	841,231
Less: accumulated depreciation	539,840	536,176
Property, plant and equipment, net	303,778	305,055
Long-term insurance receivable - asbestos	143,044	148,222
Long-term deferred tax assets	179,992	186,734
Other assets	111,009	112,265
Intangible assets, net	398,337	408,923
Goodwill	1,247,100	1,249,316
Total assets	\$3,553,345	\$3,559,607

See Notes to Condensed Consolidated Financial Statements.

CRANE CO. AND SUBSIDIARIES  
CONDENSED CONSOLIDATED BALANCE SHEETS  
(IN THOUSANDS, EXCEPT SHARE AND PER SHARE DATA)  
(UNAUDITED)

	March 31, 2014	December 31, 2013	
Liabilities and equity			
Current liabilities:			
Short-term borrowings	\$ 143,804	\$ 125,826	
Accounts payable	214,108	229,828	
Current asbestos liability	88,038	88,038	
Accrued liabilities	233,504	223,148	
U.S. and foreign taxes on income	1,519	2,062	
Total current liabilities	680,973	668,902	
Long-term debt	749,181	749,170	
Accrued pension and postretirement benefits	146,352	151,133	
Long-term deferred tax liability	50,907	76,041	
Long-term asbestos liability	592,428	610,530	
Other liabilities	74,059	89,158	
Total liabilities	2,293,900	2,344,934	
Commitments and contingencies (Note 9)			
Equity:			
Preferred shares, par value \$.01; 5,000,000 shares authorized	—	—	
Common stock, par value \$1.00; 200,000,000 shares authorized, 72,426,139 shares issued	72,426	72,426	
Capital surplus	234,782	228,537	
Retained earnings	1,434,270	1,403,202	
Accumulated other comprehensive loss	(49,654	) (48,651	)
Treasury stock	(442,896	) (451,195	)
Total shareholders' equity	1,248,928	1,204,319	
Noncontrolling interests	10,517	10,354	
Total equity	1,259,445	1,214,673	
Total liabilities and equity	\$3,553,345	\$3,559,607	
Common stock issued	72,426,139	72,426,139	
Less: Common stock held in treasury	(13,605,026	) (14,240,852	)
Common stock outstanding	58,821,113	58,185,287	

See Notes to Condensed Consolidated Financial Statements.

CRANE CO. AND SUBSIDIARIES  
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS  
(IN THOUSANDS)  
(UNAUDITED)

	Three Months Ended		
	March 31,		
	2014	2013	
Operating activities:			
Net income attributable to common shareholders	\$48,684	\$57,791	
Noncontrolling interests in subsidiaries' earnings	188	151	
Net income before allocation to noncontrolling interests	48,872	57,942	
Restructuring - non-cash	366	—	
Depreciation and amortization	21,775	12,710	
Stock-based compensation expense	5,647	5,379	
Defined benefit plans and postretirement (benefit) expense	(2,908)	) 943	
Deferred income taxes	4,738	8,200	
Cash used for working capital	(69,322)	) (98,534	)
Defined benefit plans and postretirement contributions	(4,761)	) (2,816	)
Environmental payments, net of reimbursements	(2,683)	) (3,505	)
Payments for asbestos-related fees and costs, net of insurance recoveries	(12,925)	) (10,493	)
Other	(7,709)	) 9,771	
Total used for operating activities	(18,910)	) (20,403	)
Investing activities:			
Capital expenditures	(9,393)	) (5,473	)
Proceeds from disposition of capital assets	231	196	
Total used for investing activities	(9,162)	) (5,277	)
Financing activities:			
Equity:			
Dividends paid	(17,616)	) (16,144	)
Stock options exercised - net of shares reacquired	3,752	10,389	
Excess tax benefit from stock-based compensation	5,145	2,928	
Debt:			
Proceeds received from credit facility	18,000	—	
Total provided by (used for) financing activities	9,281	(2,827	)
Effect of exchange rates on cash and cash equivalents	(1,578)	) (10,801	)
Decrease in cash and cash equivalents	(20,369)	) (39,308	)
Cash and cash equivalents at beginning of period	270,643	423,947	
Cash and cash equivalents at end of period	\$250,274	\$384,639	
Detail of cash used for working capital:			
Accounts receivable	\$(17,427	) \$(39,425	)
Inventories	(22,089	) (13,026	)
Other current assets	(1,381	) (1,096	)
Accounts payable	(15,066	) (5,287	)
Accrued liabilities	(14,198	) (39,618	)
U.S. and foreign taxes on income	839	(82	)
Total	\$(69,322	) \$(98,534	)
Supplemental disclosure of cash flow information:			
Interest paid	\$1,578	\$6,013	
Income taxes paid	\$12,167	\$11,706	
See Notes to Condensed Consolidated Financial Statements.			



Note 1 - Basis of Presentation

The accompanying unaudited condensed consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America for interim financial reporting and the instructions to Form 10-Q and, therefore, reflect all adjustments which are, in the opinion of management, necessary for a fair statement of the results for the interim periods presented. These interim condensed consolidated financial statements should be read in conjunction with the Consolidated Financial Statements and Notes to Consolidated Financial Statements in the Company's Annual Report on Form 10-K for the year ended December 31, 2013.

Recent Accounting Pronouncements

In April 2014, the Financial Accounting Standards Board ("FASB") issued amended guidance to change the reporting of discontinued operations. Under the previous guidance, any component of an entity that was a reportable segment, an operating segment, a reporting unit, a subsidiary, or an asset group was eligible for discontinued operations presentation. The amendment only allows disposals of components of an entity that represent a strategic shift and that have a major effect on a reporting entity's operations and financial results to be reported as discontinued operations. The amendment requires expanded disclosure in the financial statements for discontinued operations as well as for disposals of significant components of an entity that do not qualify for discontinued operations presentation. The amendment is effective for annual periods beginning on or after December 15, 2014 with early adoption permitted. The adoption of this guidance is not expected to have a material impact on the Company's consolidated financial position, results of operations and cash flows.

Note 2 - Segment Results

The Company's segments are reported on the same basis used internally for evaluating performance and for allocating resources. The Company has four reportable segments: Fluid Handling, Payment & Merchandising Technologies (formerly known as Merchandising Systems segment), Aerospace & Electronics and Engineered Materials. Assets of the reportable segments exclude general corporate assets, which principally consist of cash, deferred tax assets, insurance receivables, certain property, plant and equipment, and certain other assets. Furthermore, Corporate consists of corporate office expenses including compensation, benefits, occupancy, depreciation, and other administrative costs.

Financial information by reportable segment is set forth below:

(in thousands)	Three Months Ended	
	March 31, 2014	2013
Net sales		
Fluid Handling	\$310,837	\$312,998
Payment & Merchandising Technologies	169,092	89,461
Aerospace & Electronics	168,960	164,882
Engineered Materials	67,941	60,230
Total	\$716,830	\$627,571
Operating profit (loss)		
Fluid Handling <sup>a</sup>	\$44,501	\$45,891
Payment & Merchandising Technologies <sup>b</sup>	7,447	10,165
Aerospace & Electronics <sup>c</sup>	32,557	40,111
Engineered Materials	10,793	8,574
Corporate <sup>d</sup>	(13,912)	(17,841)
Total	81,386	86,900
Interest income	388	632
Interest expense	(9,809)	(6,718)
Miscellaneous - net	(204)	(120)
Income before income taxes	\$71,761	\$80,694

<sup>a</sup> Includes \$3,231 of restructuring and related charges for the three months ended March 31, 2014.

<sup>b</sup> Includes \$3,988 of restructuring and related charges, \$3,584 of acquisition integration related costs and \$4,790 of acquisition related inventory step up and backlog amortization for the three months ended March 31, 2014.

<sup>c</sup> Includes \$2,818 of restructuring and related charges for the three months ended March 31, 2014.

<sup>d</sup> Includes \$1,143 of acquisition integration related costs for the three months ended March 31, 2014 and \$2,888 of acquisition transaction costs for the three months ended March 31, 2013.

(in thousands)	As of	
	March 31, 2014	December 31, 2013
Assets		
Fluid Handling	\$998,998	\$996,101
Payment & Merchandising Technologies	1,369,024	1,383,007
Aerospace & Electronics	515,514	511,676
Engineered Materials	241,591	233,214
Corporate	428,218	435,609
Total	\$3,553,345	\$3,559,607

(in thousands)	As of	
	March 31, 2014	December 31, 2013
Goodwill		
Fluid Handling	\$239,351	\$239,205
Payment & Merchandising Technologies	633,381	635,759
Aerospace & Electronics	202,809	202,799
Engineered Materials	171,559	171,553
Total	\$1,247,100	\$1,249,316



## Note 3 - Earnings Per Share

The Company's basic earnings per share calculations are based on the weighted average number of common shares outstanding during the year. Shares of restricted stock are included in the computation of both basic and diluted earnings per share. Potentially dilutive securities include outstanding stock options, restricted share units, deferred stock units and performance-based restricted share units. The dilutive effect of potentially dilutive securities is reflected in diluted earnings per common share by application of the treasury method. Diluted earnings per share gives effect to all potentially dilutive common shares outstanding during the year.

(in thousands, except per share data)	Three Months Ended	
	March 31,	
	2014	2013
Net income attributable to common shareholders	\$48,684	\$57,791
Average basic shares outstanding	58,516	57,479
Effect of dilutive stock options	998	910
Average diluted shares outstanding	59,514	58,389
Earnings per basic share	\$0.83	\$1.01
Earnings per diluted share	\$0.82	\$0.99

The computation of diluted earnings per share excludes the effect of the potential exercise of stock options when the average market price of the common stock is lower than the exercise price of the related stock options during the period (0.5 million and 1.7 million average options were excluded for the first quarter of 2014 and 2013, respectively).

## Note 4 - Changes in Equity and Comprehensive Income

A summary of the changes in equity for the three months ended March 31, 2014 and 2013 is provided below:

(in thousands)	Three Months Ended March 31,			2013		
	2014 Total Shareholders' Equity	Noncontrolling Interests	Total Equity	Total Shareholders' Equity	Noncontrolling Interests	Total Equity
Balance, beginning of period	\$ 1,204,319	\$ 10,354	\$ 1,214,673	\$ 918,383	\$ 8,993	\$ 927,376
Dividends	(17,616 )	—	(17,616 )	(16,144 )	—	(16,144 )
Reacquisition on open market	—	—	—	—	—	—
Exercise of stock options, net of shares reacquired	3,752	—	3,752	13,609	—	13,609
Stock compensation expense	5,647	—	5,647	5,379	—	5,379
Excess tax benefit from stock based compensation	5,145	—	5,145	2,928	—	2,928
Net income	48,684	188	48,872	57,791	151	57,942
Other comprehensive income (loss)	(1,003 )	(25 )	(1,028 )	(17,807 )	10	(17,797 )
Comprehensive income	47,681	163	47,844	39,984	161	40,145
Balance, end of period	\$ 1,248,928	\$ 10,517	\$ 1,259,445	\$ 964,139	\$ 9,154	\$ 973,293

The table below provides the accumulated balances for each classification of accumulated other comprehensive income (loss), as reflected on the Condensed Consolidated Balance Sheets.

(in thousands)	Defined Benefit Pension and Other Postretirement Items*		Currency Translation Adjustment	Total
	Balance as of December 31, 2013	\$(121,318 )	\$72,667	\$(48,651 )
Other comprehensive income (loss) before reclassifications	—	(2,511 )	(2,511 )	
Amounts reclassified from accumulated other comprehensive income	1,508	—	1,508	
Net current-period other comprehensive income (loss)	1,508	(2,511 )	(1,003 )	
Balance as of March 31, 2014	\$(119,810 )	\$70,156	\$(49,654 )	

\* Net of tax benefit of \$52,286 and \$53,373 for March 31, 2014 and December 31, 2013, respectively.

The table below illustrates the amounts reclassified out of each component of accumulated other comprehensive income for the period ended March 31, 2014.

Details of Accumulated Other Comprehensive Income Components (in thousands)	Amounts Reclassified from Accumulated Other Comprehensive Income	Affected Line Item in the Statement of Operations
Amortization of defined benefit pension items:		
Prior-service costs	\$ 30	\$40 and (\$11) has been recorded within Cost of Sales and Selling, General & Administrative, respectively
Net loss (gain)	1,257	\$1,704 and (\$447) has been recorded within Cost of Sales and Selling, General & Administrative, respectively
Amortization of other postretirement items:		
Prior-service costs	(59	) Recorded within Selling, General & Administrative
Net loss (gain)	(33	) Recorded within Selling, General & Administrative
	\$ 1,195	Total before tax
	387	Tax benefit
Total reclassifications for the period	\$ 808	Net of tax

The table below illustrates the amounts reclassified out of each component of accumulated other comprehensive income for the period ended March 31, 2013.

Details of Accumulated Other Comprehensive Income Components (in thousands)	Amounts Reclassified from Accumulated Other Comprehensive Income	Affected Line Item in the Statement of Operations
Amortization of defined benefit pension items:		
Prior-service costs	\$ (6	) Prior-service costs
Net loss (gain)	3,164	Net loss (gain)
Amortization of other postretirement items:		
Prior-service costs	(59	) Prior-service costs
Net loss (gain)	(35	) Net loss (gain)
	\$ 3,064	
	960	
Total reclassifications for the period	\$ 2,104	Total reclassifications for the period

#### Note 5 - Acquisitions

Acquisitions are accounted for in accordance with the guidance for business combinations. Accordingly, the Company makes an initial allocation of the purchase price at the date of acquisition based upon its understanding of the fair value of the acquired assets and assumed liabilities. The Company obtains this information during due diligence and through other sources. In the months after closing, as the Company obtains additional information about these assets

and liabilities, including through tangible and intangible asset appraisals, it is able to refine the estimates of fair value and more accurately allocate the purchase price. Only items identified as of the acquisition date are considered for subsequent adjustment. The Company will make appropriate adjustments to the purchase price allocation prior to completion of the measurement period, as required.

On December 11, 2013, the Company completed the acquisition of MEI Conlux Holdings (U.S.), Inc. and its affiliate MEI Conlux Holdings (Japan), Inc. (together, "MEI"), a leading provider of payment solutions for unattended transaction systems serving customers in the transportation, gaming, retail, financial services and vending markets. The purchase price was \$804 million for all of the outstanding equity interests of MEI. MEI had sales of \$399 million in 2012 and has been integrated into the Company's Crane Payment Innovations business within its Payment & Merchandising Technologies segment. The amount allocated to goodwill reflects the benefits the Company expects to realize from the acquisition, as the acquisition is expected to strengthen and broaden the Company's product offering and will allow the Company to strengthen its global position in all sectors of the market, including self checkout applications. Goodwill from this acquisition is not deductible for tax purposes.

To finance the cash consideration for the MEI acquisition, the Company issued \$250 million of 2.75% Senior Notes due 2018 and \$300 million of 4.45% Senior Notes due 2023. For the remainder of the cash consideration, the Company utilized cash and cash equivalents generated from operating activities.

#### Allocation of Consideration Transferred to Net Assets Acquired

The following amounts represent the preliminary determination of the fair value of identifiable assets acquired and liabilities assumed from the Company's acquisition of MEI. The final determination of the fair value of certain assets and liabilities will be completed within the one year measurement period as required by Accounting Standards Codification ("ASC") Topic 805, "Business Combinations." The size and breadth of the MEI acquisition will necessitate the use of this measurement period to adequately analyze and assess a number of the factors used in establishing the asset and liability fair values as of the acquisition date, including the significant contractual and operational factors underlying the customer relationship intangible asset and the assumptions underpinning the related tax impacts of any changes made. Any potential adjustments made could be material in relation to the preliminary values presented below:

#### Preliminary net assets acquired (in millions)

Total current assets	\$173
Property, plant and equipment	45
Other assets	7
Intangible assets	302
Goodwill	442
Total assets acquired	\$969
Assumed liabilities	120
Net assets acquired	\$849

The amounts allocated to acquired intangible assets, and their associated weighted- average useful lives which were determined based on the period which the assets are expected to contribute directly or indirectly to our future cash flows, consist of the following:

Intangible Assets (dollars in millions)	Intangible Fair Value	Weighted Average Life
Trademarks/trade names	\$7	6.7
Customer relationships	277	16.6
Backlog	5	0.3
Product technology	13	5.7
Total acquired Intangible assets	\$302	

In order to allocate the consideration transferred for MEI, the fair values of all identifiable assets and liabilities must be established. For accounting and financial reporting purposes, fair value is defined under ASC Topic 820, "Fair Value Measurement and Disclosure" as the price that would be received upon sale of an asset or the amount paid to transfer a liability in an orderly transaction between market participants at the measurement date. Market participants are assumed to be buyers and sellers in the principal (most advantageous) market for the asset or liability.

Additionally, fair value measurements for an asset assume the highest and best use of that asset by market participants. Use of different estimates and judgments could yield different results.

The fair values of the trademark and trade name intangible assets were determined by using an “income approach”, specifically the relief-from-royalty approach, which is a commonly accepted valuation approach. This approach is based on the assumption that in lieu of ownership, a firm would be willing to pay a royalty in order to exploit the related benefits of this asset. Therefore, a portion of MEI’s earnings, equal to the after-tax royalty that would have been paid for the use of the asset, can be attributed to the firm’s ownership. The trademark and trade names are being amortized on a straight-line basis (which approximates the economic pattern of benefits) over the estimated economic life of five to ten years.

The fair values of the product technology intangible assets were also determined by the relief-from-royalty approach. Similarly, this approach is based on the assumption that in lieu of ownership, a firm would be willing to pay a royalty in order to exploit the related benefits of the technology. Therefore, a portion of MEI’s earnings, equal to the after-tax royalty that would have been paid for the use of the technology, can be attributed to the firm’s ownership of the technology. The technology assets are being amortized on a straight-line basis (which approximates the economic pattern of benefits) over the estimated economic life of three to six years.

The fair values of the customer relationships and backlog intangible assets, were determined by using an “income approach” which is a commonly accepted valuation approach. Under this approach, the net earnings attributable to the asset or liability being measured are isolated using the discounted projected net cash flows. These projected cash flows are isolated from the projected cash flows of the combined asset group over the remaining economic life of the intangible asset or liability being measured. Both the amount and the duration of the cash flows are considered from a market participant perspective. Our estimates of market participant net cash flows considered historical and projected pricing, operational performance including market participant synergies, aftermarket retention, product life cycles, material and labor pricing, and other relevant customer, contractual and market factors. Where appropriate, the net cash flows were adjusted to reflect the potential attrition of existing customers in the future, as existing customers are a “wasting” asset and are expected to decline over time. The attrition-adjusted future cash flows are then discounted to present value using an appropriate discount rate. The customer relationship is being amortized on a straight-line basis (which approximates the economic pattern of benefits) over the estimated economic life of 13 to 18 years.

#### Acquisition-Related Costs

Acquisition-related costs are being expensed as incurred. For the quarter ended March 31, 2014, the Company recorded \$4.7 million of acquisition integration related charges, \$4.8 million of inventory step-up and backlog amortization and \$4.0 million of restructuring costs (see additional discussion in Note 14). For the quarter ended March 31, 2013, the Company recorded \$2.9 million of transaction costs within the selling, general and administrative line on the Condensed Consolidated Statement of Operations.

#### Supplemental Pro Forma Data

MEI's results of operations have been included in the Company's financial statements for the period subsequent to the completion of the acquisition on December 11, 2013. The following unaudited supplemental pro forma data for the quarter ended March 31, 2013 presents consolidated information as if the acquisition had been completed on January 1, 2011. There were no significant pro forma adjustments required for the three months ended March 31, 2014. The pro forma results were calculated by combining the results of Crane Co. with the stand-alone results of MEI for the pre-acquisition periods, which were adjusted to account for certain costs which would have been incurred during this pre-acquisition period:

(in millions, except per share data)

For the three months ended March 31,	2013
Net sales	\$717
Net income attributable to common shareholders	\$57
Basic earnings per share from continuing operations	\$1.00
Diluted earnings per share from continuing operations	\$0.98

The unaudited supplemental pro forma data above includes adjustments for inventory step up, depreciation and amortization related to acquired MEI property, plant & equipment and intangible assets, transaction costs, interest expense related to financing directly associated with the acquisition and the effect of required dispositions to meet regulatory approval.

Note 6 - Goodwill and Intangible Assets

The Company's business acquisitions have typically resulted in the recognition of goodwill and other intangible assets. The Company follows the provisions of ASC Topic 350, "Intangibles – Goodwill and Other" ("ASC 350") as it relates to the

accounting for goodwill in the Condensed Consolidated Financial Statements. These provisions require that the Company, on at least an annual basis, evaluate the fair value of the reporting units to which goodwill is assigned and attributed and compare that fair value to the carrying value of the reporting unit to determine if an impairment has occurred. The Company performs its annual impairment testing during the fourth quarter. Impairment testing takes place more often than annually if events or circumstances indicate a change in status that would indicate a potential impairment. The Company believes that there have been no events or circumstances which would more likely than not reduce the fair value for its reporting units below its carrying value. A reporting unit is an operating segment unless discrete financial information is prepared and reviewed by segment management for businesses one level below that operating segment (a "component"), in which case the component would be the reporting unit. In certain instances, the Company has aggregated components of an operating segment into a single reporting unit based on similar economic characteristics. At March 31, 2014, the Company had eight reporting units.

When performing its annual impairment assessment, the Company compares the fair value of each of its reporting units to its respective carrying value. Goodwill is considered to be potentially impaired when the net book value of the reporting unit exceeds its estimated fair value. Fair values are established primarily by discounting estimated future cash flows at an estimated cost of capital which varies for each reporting unit and which, as of the Company's most recent annual impairment assessment, ranged between 10% and 13% (a weighted average of 11%), reflecting the respective inherent business risk of each of the reporting units tested. This methodology for valuing the Company's reporting units (commonly referred to as the Income Method) has not changed since the adoption of the provisions under ASC 350. The determination of discounted cash flows is based on the businesses' strategic plans and long-range planning forecasts, which change from year to year. The revenue growth rates included in the forecasts represent best estimates based on current and forecasted market conditions. Profit margin assumptions are projected by each reporting unit based on the current cost structure and anticipated net cost increases/reductions. There are inherent uncertainties related to these assumptions, including changes in market conditions, and management's judgment in applying them to the analysis of goodwill impairment. In addition to the foregoing, for each reporting unit, market multiples are used to corroborate its discounted cash flow results where fair value is estimated based on earnings multiples determined by available public information of comparable businesses. While the Company believes it has made reasonable estimates and assumptions to calculate the fair value of its reporting units, it is possible a material change could occur. If actual results are not consistent with management's estimates and assumptions, goodwill and other intangible assets may then be determined to be overstated and a charge would need to be taken against net earnings. Furthermore, in order to evaluate the sensitivity of the fair value calculations on the goodwill impairment test performed during the fourth quarter of 2013, the Company applied a hypothetical, reasonably possible 10% decrease to the fair values of each reporting unit. The effects of this hypothetical 10% decrease would still result in the fair value calculation exceeding the carrying value for each reporting unit.

Changes to goodwill are as follows:

(in thousands)	Three Months Ended March 31, 2014	Year Ended December 31, 2013
Balance at beginning of period	\$1,249,316	\$813,792
Additions	—	442,170
Disposals	—	(2,834 )
Currency translation and other	(2,216 )	(3,812 )
Balance at end of period	\$1,247,100	\$1,249,316

For the year ended December 31, 2013, the additions to goodwill represent the initial purchase price allocation related to the December 2013 acquisition of MEI and the disposals represent the goodwill associated with the Company's sale of a product line as part of the execution of regulatory remedies associated with the MEI acquisition. See discussion in Note 5, "Acquisitions" for further details.

Changes to intangible assets are as follows:

(in thousands)	Three Months Ended March 31, 2014	Year Ended December 31, 2013
Balance at beginning of period, net of accumulated amortization	\$408,923	\$125,913
Additions	—	301,800
Disposals	—	(311)
Amortization expense	(12,441)	(18,795)
Currency translation and other	1,855	316
Balance at end of period, net of accumulated amortization	\$398,337	\$408,923

For the year ended December 31, 2013, the additions represent the initial purchase price allocation related to the December 2013 acquisition of MEI and the disposals represent the intangible assets associated with the Company's sale of a product line as part of the execution of regulatory remedies associated with the MEI acquisition. See discussion in Note 5, "Acquisitions" for further details.

As of March 31, 2014, the Company had \$398.3 million of net intangible assets, of which \$30.8 million were intangibles with indefinite useful lives, consisting of trade names. The Company amortizes the cost of other intangibles over their estimated useful lives unless such lives are deemed indefinite. Intangibles with indefinite useful lives are tested annually for impairment, or when events or changes in circumstances indicate the potential for impairment. If the carrying amount of an intangible asset with an indefinite useful life exceeds the fair value, the intangible asset is written down to its fair value. Fair value is calculated using discounted cash flows.

In addition to annual testing for impairment of indefinite-lived intangible assets, the Company reviews all of its long-lived assets, including intangible assets subject to amortization, for impairment whenever events or changes in circumstances indicate the carrying amount of an asset may not be recoverable. Examples of events or changes in circumstances could include, but are not limited to, a prolonged economic downturn, current period operating or cash flow losses combined with a history of losses or a forecast of continuing losses associated with the use of an asset or asset group, or a current expectation that an asset or asset group will be sold or disposed of before the end of its previously estimated useful life. Recoverability is based upon projections of anticipated future undiscounted cash flows associated with the use and eventual disposal of the long-lived asset (or asset group), as well as specific appraisal in certain instances. Reviews occur at the lowest level for which identifiable cash flows are largely independent of cash flows associated with other long-lived assets or asset groups and include estimated future revenues, gross profit margins, operating profit margins and capital expenditures which are based on the businesses' strategic plans and long-range planning forecasts, which change from year to year. The revenue growth rates included in the forecasts represent our best estimates based on current and forecasted market conditions, and the profit margin assumptions are based on the current cost structure and anticipated net cost increases/reductions. There are inherent uncertainties related to these assumptions, including changes in market conditions, and management's judgment in applying them to the analysis. If the future undiscounted cash flows are less than the carrying value, then the long-lived asset is considered impaired and a charge would be taken against net earnings based on the amount by which the carrying amount exceeds the estimated fair value. Judgments that the Company makes which impact these assessments relate to the expected useful lives of long-lived assets and its ability to realize any undiscounted cash flows in excess of the carrying amounts of such assets, and are affected primarily by changes in the expected use of the assets, changes in technology or development of alternative assets, changes in economic conditions, changes in operating performance and changes in expected future cash flows. Since judgment is involved in determining the fair value of long-lived assets, there is risk that the carrying value of our long-lived assets may require adjustment in future periods. Historical results to date have generally approximated expected cash flows for the identifiable cash flow generating level. The Company believes that there have been no events or circumstances which would more likely than not reduce the fair value of its indefinite-lived and amortizing intangible assets.

A summary of intangible assets follows:

(in thousands)	Weighted Average Amortization Period of Finite Lived Assets (in years)	March 31, 2014			December 31, 2013		
		Gross Asset	Accumulated Amortization	Net	Gross Asset	Accumulated Amortization	Net
Intellectual property rights	16.5	\$94,858	\$ 49,598	\$45,260	\$95,052	\$ 48,960	\$46,092
Customer relationships and backlog	13.9	422,404	96,473	325,931	420,951	86,556	334,395
Drawings	37.9	11,149	9,976	1,173	11,149	9,951	1,198
Other	12.7	64,831	38,858	25,973	64,800	37,562	27,238
Total	14.4	\$593,242	\$ 194,905	\$398,337	\$591,952	\$ 183,029	\$408,923

Amortization expense for these intangible assets is currently estimated to be approximately \$34.1 million in total for the remainder of 2014, \$38.7 million in 2015, \$37.9 million in 2016, \$37.0 million in 2017, \$34.1 million in 2018 and \$185.8 million in 2019 and thereafter.

#### Note 7 - Accrued Liabilities

Accrued liabilities consist of:

(in thousands)	March 31, 2014	December 31, 2013
Employee related expenses	\$69,409	\$91,984
Warranty	18,197	18,923
Other	145,898	112,241
Total	\$233,504	\$223,148

The Company accrues warranty liabilities when it is probable that an asset has been impaired or a liability has been incurred and the amount of the loss can be reasonably estimated. Warranty provision is included in cost of sales in the Condensed Consolidated Statements of Operations.

A summary of the warranty liabilities is as follows:

(in thousands)	Three Months Ended		Year Ended
	March 31, 2014		December 31, 2013
Balance at beginning of period	\$ 18,923		\$ 10,718
Expense	3,711		10,230
Changes due to acquisitions/divestitures	—		10,211
Payments / deductions	(4,501		) (12,464
Currency translation	64		228
Balance at end of period	\$ 18,197		\$ 18,923

#### Note 8 - Commitments and Contingencies

##### Asbestos Liability

##### Information Regarding Claims and Costs in the Tort System

As of March 31, 2014, the Company was a defendant in cases filed in numerous state and federal courts alleging injury or death as a result of exposure to asbestos. Activity related to asbestos claims during the periods indicated was as follows:

	Three Months Ended		Year Ended
	March 31,		December 31,
	2014	2013	2013
Beginning claims	51,490	56,442	56,442
New claims	680	792	2,950
Settlements	(303	) (237	) (1,142
Dismissals	(968	) (789	) (6,762
MARDOC claims*	—	—	2
Ending claims	50,899	56,208	51,490

\* As of January 1, 2010, the Company was named in 36,448 maritime actions which had been administratively dismissed by the United States District Court for the Eastern District of Pennsylvania ("MARDOC claims"), and therefore were not classified as active claims. In addition, the Company was named in 8 new maritime actions in 2010 (also not classified as active claims). By settlement agreement of December 30, 2013, the Company resolved all of the remaining MARDOC claims with plaintiffs' counsel. The agreement resulted in the dismissal of all MARDOC claims against the Company.

Of the 50,899 pending claims as of March 31, 2014, approximately 19,000 claims were pending in New York, approximately 9,700 claims were pending in Texas, approximately 5,300 claims were pending in Mississippi, and approximately 400 claims were pending in Ohio, all jurisdictions in which legislation or judicial orders restrict the types of claims that can proceed to trial on the merits.

Substantially all of the claims the Company resolves are either dismissed or concluded through settlements. To date, the Company has paid two judgments arising from adverse jury verdicts in asbestos matters. The first payment, in the amount of \$2.54 million, was made on July 14, 2008, approximately two years after the adverse verdict in the Joseph Norris matter in California, after the Company had exhausted all post-trial and appellate remedies. The second payment, in the amount of \$0.02 million, was made in June 2009 after an adverse verdict in the Earl Haupt case in Los Angeles, California on April 21, 2009.

The Company has tried several cases resulting in defense verdicts by the jury or directed verdicts for the defense by the court. The Company further has pursued appeals of certain adverse jury verdicts that have resulted in reversals in favor of the defense.

On March 23, 2010, a Philadelphia, Pennsylvania, state court jury found the Company responsible for a 1/11th share of a \$14.5 million verdict in the James Nelson claim, and for a 1/20th share of a \$3.5 million verdict in the Larry Bell

claim. On February 23, 2011, the court entered judgment on the verdicts in the amount of \$0.2 million against the Company, only, in Bell, and in the amount of \$4.0 million, jointly, against the Company and two other defendants in Nelson, with additional interest in the amount of \$0.01 million being assessed against the Company, only, in Nelson. All defendants, including the Company, and the plaintiffs took timely appeals of certain aspects of those judgments. The Company resolved the Bell appeal by settlement, which is reflected in the settled claims for 2012. On September 5, 2013, a panel of the Pennsylvania Superior Court, in a 2-1 decision, vacated the Nelson verdict against all defendants, reversing and remanding for a new trial. Plaintiffs have requested a rehearing in the Superior Court, which the defendants, including the Company, have opposed. By order dated November 18, 2013, the Superior Court vacated the panel opinion, and granted en banc reargument at a date to be scheduled.

On August 17, 2011, a New York City state court jury found the Company responsible for a 99% share of a \$32 million verdict on the Ronald Dummitt claim. The Company filed post-trial motions seeking to overturn the verdict, to grant a new trial, or to reduce the damages, which the Company argued were excessive under New York appellate case law governing awards for non-economic losses. The Court held oral argument on these motions on October 18, 2011 and issued a written decision on August 21, 2012 confirming the jury's liability findings but reducing the award of damages to \$8 million. At plaintiffs' request, the Court entered a judgment in the amount of \$4.9 million against the Company, taking into account settlement offsets and accrued interest under New York law. The Company has appealed.

On March 9, 2012, a Philadelphia, Pennsylvania, state court jury found the Company responsible for a 1/8th share of a \$123,000 verdict in the Frank Paasch claim. The Company and plaintiffs filed post-trial motions. On May 31, 2012, on plaintiffs' motion, the Court entered an order dismissing the claim against the Company, with prejudice, and without any payment.

On August 29, 2012, the Company received an adverse verdict in the William Paulus claim in Los Angeles, California. The jury found that the Company was responsible for ten percent (10%) of plaintiffs' non-economic damages of \$6.5 million, plus a portion of plaintiffs' economic damages of \$0.4 million. Based on California court rules regarding allocation of damages, judgment was entered in the amount of \$0.8 million against the Company. The Company filed post-trial motions requesting judgment in the Company's favor notwithstanding the jury's verdict, which were denied. The Company appealed, and the judgment was affirmed by order dated February 21, 2014. The Company will seek review of certain aspects of the ruling before the California Supreme Court.

On October 23, 2012, the Company received an adverse verdict in the Gerald Suttner claim in Buffalo, New York. The jury found that the Company was responsible for four percent (4%) of plaintiffs' damages of \$3 million. The Company filed post-trial motions requesting judgment in the Company's favor notwithstanding the jury's verdict, which were denied. The court entered a judgment of \$0.1 million against the Company. The Company appealed, and the judgment was affirmed by order dated March 21, 2014. The Company is seeking reargument of this decision.

On November 28, 2012, the Company received an adverse verdict in the James Hellam claim in Oakland, CA. The jury found that the Company was responsible for seven percent (7%) of plaintiffs' non-economic damages of \$4.5 million, plus a portion of their economic damages of \$0.9 million. Based on California court rules regarding allocation of damages, judgment was entered against the Company in the amount of \$1.282 million. The Company filed post-trial motions requesting judgment in the Company's favor notwithstanding the jury's verdict and also requesting that settlement offsets be applied to reduce the judgment in accordance with California law. On January 31, 2013, the court entered an order disposing partially of that motion. On March 1, 2013, the Company filed an appeal regarding the portions of the motion that were denied. The court entered judgment against the Company in the amount of \$1.1 million. The Company appealed. By opinion dated April 16, 2014, the Court of Appeal affirmed the finding of liability against the Company, but reserved the arguments relating to recoverable damages to a subsequent appeal that remains pending.

On February 25, 2013, a Philadelphia, Pennsylvania, state court jury found the Company responsible for a 1/10th share of a \$2.5 million verdict in the Thomas Amato claim and a 1/5th share of a \$2.3 million verdict in the Frank Vinciguerra claim, which were consolidated for trial. The Company filed post-trial motions requesting judgments in the Company's favor notwithstanding the jury's verdicts or new trials, and also requesting that settlement offsets be applied to reduce the judgment in accordance with Pennsylvania law. These motions were denied. The Company has appealed.

On March 1, 2013, a New York City state court jury entered a \$35 million verdict against the Company in the Ivo Peraica claim. The Company filed post-trial motions seeking to overturn the verdict, to grant a new trial, or to reduce the damages, which the Company argues were excessive under New York appellate case law governing awards for non-economic losses and further were subject to settlement offsets. After the trial court remitted the verdict to \$18 million, but otherwise denied the Company's post-trial motion, judgment also entered against the Company in the amount of \$10.6 million (including interest). The Company has appealed. The Company has taken a separate appeal of the trial court's denial of its summary judgment motion. The Court has consolidated the appeals, which are scheduled to be heard in third quarter of 2014.

On July 31, 2013, a Buffalo, New York state court jury entered a \$3.1 million verdict against the Company in the Lee Holdsworth claim. The Company plans to file post-trial motions seeking to overturn the verdict, to grant a new trial, or to reduce the damages, which the Company argues were excessive under New York appellate case law governing awards for non-economic losses and further were subject to settlement offsets. Plaintiffs have requested judgment in the amount of \$1.1 million. Post-trial motions remain pending. The Company plans to pursue an appeal if necessary. On September 11, 2013, a Columbia, South Carolina state court jury in the Lloyd Garvin claim entered an \$11 million verdict for compensatory damages against the Company and two other defendants jointly, and also awarded exemplary damages

against the Company in the amount of \$11 million. The jury also awarded exemplary damages against both other defendants. The Company has filed post-trial motions seeking to overturn the verdict, to grant a new trial, or to reduce the damages. The Company plans to pursue an appeal if necessary.

On September 17, 2013, a Fort Lauderdale, Florida state court jury in the Richard DeLisle claim found the Company responsible for 16 percent of an \$8 million verdict. The trial court denied all parties' post-trial motions, and entered judgment against the Company in the amount of \$1.3 million. The Company has appealed.

Such judgment amounts are not included in the Company's incurred costs until all available appeals are exhausted and the final payment amount is determined.

The gross settlement and defense costs incurred (before insurance recoveries and tax effects) for the Company for the three-month periods ended March 31, 2014 and 2013 totaled \$20.5 million. In contrast to the recognition of settlement and defense costs, which reflect the current level of activity in the tort system, cash payments and receipts generally lag the tort system activity by several months or more, and may show some fluctuation from quarter to quarter. Cash payments of settlement amounts are not made until all releases and other required documentation are received by the Company, and reimbursements of both settlement amounts and defense costs by insurers may be uneven due to insurer payment practices, transitions from one insurance layer to the next excess layer and the payment terms of certain reimbursement agreements. The Company's total pre-tax payments for settlement and defense costs, net of funds received from insurers, for the three-month periods ended March 31, 2014 and 2013 totaled \$12.9 million and \$10.5 million, respectively. Detailed below are the comparable amounts for the periods indicated.

(in millions)	Three Months Ended		Year Ended
	March 31,		December 31,
	2014	2013	2013
Settlement / indemnity costs incurred (1)	\$7.7	\$6.8	\$ 31.6
Defense costs incurred (1)	12.9	13.7	59.1
Total costs incurred	\$20.5	\$20.5	\$ 90.8
Settlement / indemnity payments	\$6.7	\$9.6	\$ 37.8
Defense payments	11.4	13.0	59.5
Insurance receipts	(5.2	) (12.1	) (34.5
Pre-tax cash payments	\$ 12.9	\$ 10.5	\$ 62.8

(1) Before insurance recoveries and tax effects.

The amounts shown for settlement and defense costs incurred, and cash payments, are not necessarily indicative of future period amounts, which may be higher or lower than those reported.

Cumulatively through March 31, 2014, the Company has resolved (by settlement or dismissal) approximately 101,000 claims, not including the MARDOC claims referred to above. The related settlement cost incurred by the Company and its insurance carriers is approximately \$407 million, for an average settlement cost per resolved claim of approximately \$4,000. The average settlement cost per claim resolved during the years ended December 31, 2013, 2012 and 2011 was \$3,300, \$6,300 and \$4,123, respectively. Because claims are sometimes dismissed in large groups, the average cost per resolved claim, as well as the number of open claims, can fluctuate significantly from period to period. In addition to large group dismissals, the nature of the disease and corresponding settlement amounts for each claim resolved will also drive changes from period to period in the average settlement cost per claim. Accordingly, the average cost per resolved claim is not considered in the Company's periodic review of its estimated asbestos liability. For a discussion regarding the four most significant factors affecting the liability estimate, see "Effects on the Condensed Consolidated Financial Statements".

Effects on the Condensed Consolidated Financial Statements

The Company has retained the firm of Hamilton, Rabinovitz & Associates, Inc. ("HR&A"), a nationally recognized expert in the field, to assist management in estimating the Company's asbestos liability in the tort system. HR&A reviews information provided by the Company concerning claims filed, settled and dismissed, amounts paid in settlements and relevant claim information such as the nature of the asbestos-related disease asserted by the claimant,

the jurisdiction where filed and the time lag from filing to disposition of the claim. The methodology used by HR&A to project future asbestos costs is based largely on

the Company's experience during a base reference period of eleven quarterly periods (consisting of the two full preceding calendar years and three additional quarterly periods to the estimate date) for claims filed, settled and dismissed. The Company's experience is then compared to the results of widely used previously conducted epidemiological studies estimating the number of individuals likely to develop asbestos-related diseases. Those studies were undertaken in connection with national analyses of the population of workers believed to have been exposed to asbestos. Using that information, HR&A estimates the number of future claims that would be filed against the Company and estimates the aggregate settlement or indemnity costs that would be incurred to resolve both pending and future claims based upon the average settlement costs by disease during the reference period. This methodology has been accepted by numerous courts. After discussions with the Company, HR&A augments its liability estimate for the costs of defending asbestos claims in the tort system using a forecast from the Company which is based upon discussions with its defense counsel. Based on this information, HR&A compiles an estimate of the Company's asbestos liability for pending and future claims, based on claim experience during the reference period and covering claims expected to be filed through the indicated forecast period. The most significant factors affecting the liability estimate are (1) the number of new mesothelioma claims filed against the Company, (2) the average settlement costs for mesothelioma claims, (3) the percentage of mesothelioma claims dismissed against the Company and (4) the aggregate defense costs incurred by the Company. These factors are interdependent, and no one factor predominates in determining the liability estimate. Although the methodology used by HR&A can be applied to show claims and costs for periods subsequent to the indicated period (up to and including the endpoint of the asbestos studies referred to above), management believes that the level of uncertainty regarding the various factors used in estimating future asbestos costs is too great to provide for reasonable estimation of the number of future claims, the nature of such claims or the cost to resolve them for years beyond the indicated estimate.

In the Company's view, the forecast period used to provide the best estimate for asbestos claims and related liabilities and costs is a judgment based upon a number of trend factors, including the number and type of claims being filed each year; the jurisdictions where such claims are filed, and the effect of any legislation or judicial orders in such jurisdictions restricting the types of claims that can proceed to trial on the merits; and the likelihood of any comprehensive asbestos legislation at the federal level. In addition, the dynamics of asbestos litigation in the tort system have been significantly affected over the past five to ten years by the substantial number of companies that have filed for bankruptcy protection, thereby staying any asbestos claims against them until the conclusion of such proceedings, and the establishment of a number of post-bankruptcy trusts for asbestos claimants, which are estimated to provide \$36 billion for payments to current and future claimants. These trend factors have both positive and negative effects on the dynamics of asbestos litigation in the tort system and the related best estimate of the Company's asbestos liability, and these effects do not move in a linear fashion but rather change over multi-year periods. Accordingly, the Company's management continues to monitor these trend factors over time and periodically assesses whether an alternative forecast period is appropriate.

Each quarter, HR&A compiles an update based upon the Company's experience in claims filed, settled and dismissed during the updated reference period (consisting of the preceding eleven quarterly periods) as well as average settlement costs by disease category (mesothelioma, lung cancer, other cancer and non-malignant conditions including asbestosis) during that period. In addition to this claims experience, the Company also considers additional quantitative and qualitative factors such as the nature of the aging of pending claims, significant appellate rulings and legislative developments, and their respective effects on expected future settlement values. As part of this process, the Company also takes into account trends in the tort system such as those enumerated above. Management considers all these factors in conjunction with the liability estimate of HR&A and determines whether a change in the estimate is warranted.

**Liability Estimate.** With the assistance of HR&A, effective as of December 31, 2011, the Company updated and extended its estimate of the asbestos liability, including the costs of settlement or indemnity payments and defense costs relating to currently pending claims and future claims projected to be filed against the Company through 2021. The Company's previous estimate was for asbestos claims filed or projected to be filed through 2017. As a result of this updated estimate, the Company recorded an additional liability of \$285 million as of December 31, 2011. The Company's decision to take this action at such date was based on several factors which contribute to the Company's ability to reasonably estimate this liability for the additional period noted. First, the number of mesothelioma claims

(which although constituting approximately 8% of the Company's total pending asbestos claims, have accounted for approximately 90% of the Company's aggregate settlement and defense costs) being filed against the Company and associated settlement costs have recently stabilized. In the Company's opinion, the outlook for mesothelioma claims expected to be filed and resolved in the forecast period is reasonably stable. Second, there have been favorable developments in the trend of case law which has been a contributing factor in stabilizing the asbestos claims activity and related settlement costs. Third, there have been significant actions taken by certain state legislatures and courts over the past several years that have reduced the number and types of claims that can proceed to trial, which has been a significant factor in stabilizing the asbestos claims activity. Fourth, the Company has now entered into coverage-in-place agreements with almost all of its excess insurers, which enables the Company to project a more stable relationship between settlement and defense costs paid by the Company and reimbursements from its insurers. Taking all of these factors into

account, the Company believes that it can reasonably estimate the asbestos liability for pending claims and future claims to be filed through 2021. While it is probable that the Company will incur additional charges for asbestos liabilities and defense costs in excess of the amounts currently provided, the Company does not believe that any such amount can be reasonably estimated beyond 2021. Accordingly, no accrual has been recorded for any costs which may be incurred for claims which may be made subsequent to 2021.

Management has made its best estimate of the costs through 2021 based on the analysis by HR&A completed in January 2012. Through March 31, 2014, the Company's actual experience during the updated reference period for mesothelioma claims filed and dismissed generally approximated the assumptions in the Company's liability estimate. In addition to this claims experience, the Company considered additional quantitative and qualitative factors such as the nature of the aging of pending claims, significant appellate rulings and legislative developments, and their respective effects on expected future settlement values. Based on this evaluation, the Company determined that no change in the estimate was warranted for the period ended March 31, 2014. Nevertheless, if certain factors show a pattern of sustained increase or decrease, the liability could change materially; however, all the assumptions used in estimating the asbestos liability are interdependent and no single factor predominates in determining the liability estimate. Because of the uncertainty with regard to and the interdependency of such factors used in the calculation of its asbestos liability, and since no one factor predominates, the Company believes that a range of potential liability estimates beyond the indicated forecast period cannot be reasonably estimated.

A liability of \$894 million was recorded as of December 31, 2011 to cover the estimated cost of asbestos claims now pending or subsequently asserted through 2021, of which approximately 80% is attributable to settlement and defense costs for future claims projected to be filed through 2021. The liability is reduced when cash payments are made in respect of settled claims and defense costs. The liability was \$680 million as of March 31, 2014. It is not possible to forecast when cash payments related to the asbestos liability will be fully expended; however, it is expected such cash payments will continue for a number of years past 2021, due to the significant proportion of future claims included in the estimated asbestos liability and the lag time between the date a claim is filed and when it is resolved. None of these estimated costs have been discounted to present value due to the inability to reliably forecast the timing of payments. The current portion of the total estimated liability at March 31, 2014 was \$88 million and represents the Company's best estimate of total asbestos costs expected to be paid during the twelve-month period. Such amount is based upon the HR&A model together with the Company's prior year payment experience for both settlement and defense costs.

**Insurance Coverage and Receivables.** Prior to 2005, a significant portion of the Company's settlement and defense costs were paid by its primary insurers. With the exhaustion of that primary coverage, the Company began negotiations with its excess insurers to reimburse the Company for a portion of its settlement and/or defense costs as incurred. To date, the Company has entered into agreements providing for such reimbursements, known as "coverage-in-place", with eleven of its excess insurer groups. Under such coverage-in-place agreements, an insurer's policies remain in force and the insurer undertakes to provide coverage for the Company's present and future asbestos claims on specified terms and conditions that address, among other things, the share of asbestos claims costs to be paid by the insurer, payment terms, claims handling procedures and the expiration of the insurer's obligations. Similarly, under a variant of coverage-in-place, the Company has entered into an agreement with a group of insurers confirming the aggregate amount of available coverage under the subject policies and setting forth a schedule for future reimbursement payments to the Company based on aggregate indemnity and defense payments made. In addition, with ten of its excess insurer groups, the Company entered into policy buyout agreements, settling all asbestos and other coverage obligations for an agreed sum, totaling \$82.5 million in aggregate. Reimbursements from insurers for past and ongoing settlement and defense costs allocable to their policies have been made in accordance with these coverage-in-place and other agreements. All of these agreements include provisions for mutual releases, indemnification of the insurer and, for coverage-in-place, claims handling procedures. With the agreements referenced above, the Company has concluded settlements with all but one of its solvent excess insurers whose policies are expected to respond to the aggregate costs included in the updated liability estimate. That insurer, which issued a single applicable policy, has been paying the shares of defense and indemnity costs the Company has allocated to it, subject to a reservation of rights. There are no pending legal proceedings between the Company and any insurer contesting the Company's asbestos claims under its insurance policies.

In conjunction with developing the aggregate liability estimate referenced above, the Company also developed an estimate of probable insurance recoveries for its asbestos liabilities. In developing this estimate, the Company considered its coverage-in-place and other settlement agreements described above, as well as a number of additional factors. These additional factors include the financial viability of the insurance companies, the method by which losses will be allocated to the various insurance policies and the years covered by those policies, how settlement and defense costs will be covered by the insurance policies and interpretation of the effect on coverage of various policy terms and limits and their interrelationships. In addition, the timing and amount of reimbursements will vary because the Company's insurance coverage for asbestos claims involves multiple insurers, with different policy terms and certain gaps in coverage. In addition to consulting with legal counsel on these insurance matters, the Company retained insurance consultants to assist management in the estimation of probable insurance

recoveries based upon the aggregate liability estimate described above and assuming the continued viability of all solvent insurance carriers. Based upon the analysis of policy terms and other factors noted above by the Company's legal counsel, and incorporating risk mitigation judgments by the Company where policy terms or other factors were not certain, the Company's insurance consultants compiled a model indicating how the Company's historical insurance policies would respond to varying levels of asbestos settlement and defense costs and the allocation of such costs between such insurers and the Company. Using the estimated liability as of December 31, 2011 (for claims filed or expected to be filed through 2021), the insurance consultant's model forecasted that approximately 25% of the liability would be reimbursed by the Company's insurers. While there are overall limits on the aggregate amount of insurance available to the Company with respect to asbestos claims, those overall limits were not reached by the total estimated liability currently recorded by the Company, and such overall limits did not influence the Company in its determination of the asset amount to record. The proportion of the asbestos liability that is allocated to certain insurance coverage years, however, exceeds the limits of available insurance in those years. The Company allocates to itself the amount of the asbestos liability (for claims filed or expected to be filed through 2021) that is in excess of available insurance coverage allocated to such years. An asset of \$225 million was recorded as of December 31, 2011 representing the probable insurance reimbursement for such claims expected through 2021. The asset is reduced as reimbursements and other payments from insurers are received. The asset was \$166 million as of March 31, 2014. The Company reviews the aforementioned estimated reimbursement rate with its insurance consultants on a periodic basis in order to confirm its overall consistency with the Company's established reserves. The reviews encompass consideration of the performance of the insurers under coverage-in-place agreements and the effect of any additional lump-sum payments under policy buyout agreements. Since December 2011, there have been no developments that have caused the Company to change the estimated 25% rate, although actual insurance reimbursements vary from period to period, and will decline over time, for the reasons cited above.

Uncertainties. Estimation of the Company's ultimate exposure for asbestos-related claims is subject to significant uncertainties, as there are multiple variables that can affect the timing, severity and quantity of claims and the manner of their resolution. The Company cautions that its estimated liability is based on assumptions with respect to future claims, settlement and defense costs based on past experience that may not prove reliable as predictors. A significant upward or downward trend in the number of claims filed, depending on the nature of the alleged injury, the jurisdiction where filed and the quality of the product identification, or a significant upward or downward trend in the costs of defending claims, could change the estimated liability, as would substantial adverse verdicts at trial that withstand appeal. A legislative solution, structured settlement transaction, or significant change in relevant case law could also change the estimated liability.

The same factors that affect developing estimates of probable settlement and defense costs for asbestos-related liabilities also affect estimates of the probable insurance reimbursements, as do a number of additional factors. These additional factors include the financial viability of the insurance companies, the method by which losses will be allocated to the various insurance policies and the years covered by those policies, how settlement and defense costs will be covered by the insurance policies and interpretation of the effect on coverage of various policy terms and limits and their interrelationships. In addition, due to the uncertainties inherent in litigation matters, no assurances can be given regarding the outcome of any litigation, if necessary, to enforce the Company's rights under its insurance policies or settlement agreements.

Many uncertainties exist surrounding asbestos litigation, and the Company will continue to evaluate its estimated asbestos-related liability and corresponding estimated insurance reimbursement as well as the underlying assumptions and process used to derive these amounts. These uncertainties may result in the Company incurring future charges or increases to income to adjust the carrying value of recorded liabilities and assets, particularly if the number of claims and settlement and defense costs change significantly, or if there are significant developments in the trend of case law or court procedures, or if legislation or another alternative solution is implemented; however, the Company is currently unable to estimate such future changes and, accordingly, while it is probable that the Company will incur additional charges for asbestos liabilities and defense costs in excess of the amounts currently provided, the Company does not believe that any such amount can be reasonably determined beyond 2021. Although the resolution of these claims may take many years, the effect on the results of operations, financial position and cash flow in any given period from a revision to these estimates could be material.

Other Contingencies

Environmental Matters

For environmental matters, the Company records a liability for estimated remediation costs when it is probable that the Company will be responsible for such costs and they can be reasonably estimated. Generally, third party specialists assist in the estimation of remediation costs. The environmental remediation liability as of March 31, 2014 is substantially related to the former manufacturing site in Goodyear, Arizona (the “Goodyear Site”) discussed below.

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The Goodyear Site was operated by UniDynamics/Phoenix, Inc. (“UPI”), which became an indirect subsidiary of the Company in 1985 when the Company acquired UPI’s parent company, UniDynamics Corporation. UPI manufactured explosive and pyrotechnic compounds, including components for critical military programs, for the U.S. government at the Goodyear Site from 1962 to 1993, under contracts with the Department of Defense and other government agencies and certain of their prime contractors. No manufacturing operations have been conducted at the Goodyear Site since 1994. The Goodyear Site was placed on the National Priorities List in 1983, and is now part of the Phoenix-Goodyear Airport North Superfund Site. In 1990, the U.S. Environmental Protection Agency (“EPA”) issued administrative orders requiring UPI to design and carry out certain remedial actions, which UPI has done. Groundwater extraction and treatment systems have been in operation at the Goodyear Site since 1994. A soil vapor extraction system was in operation from 1994 to 1998, was restarted in 2004, and is currently in operation. The Company recorded a liability in 2004 for estimated costs to remediate the Goodyear Site. On July 26, 2006, the Company entered into a consent decree with the EPA with respect to the Goodyear Site providing for, among other things, a work plan for further investigation and remediation activities (inclusive of a supplemental remediation investigation and feasibility study). During the fourth quarter of 2007, the Company and its technical advisors determined that changing groundwater flow rates and contaminant plume direction at the Goodyear Site required additional extraction systems as well as modifications and upgrades of the existing systems. In consultation with its technical advisors, the Company prepared a forecast of the expenditures required for these new and upgraded systems as well as the costs of operation over the forecast period through 2014. Taking these additional costs into consideration, the Company estimated its liability for the costs of such activities through 2014 to be \$41.5 million as of December 31, 2007. During the fourth quarter of 2008, based on further consultation with the Company’s advisors and the EPA and in response to groundwater monitoring results that reflected a continuing migration in contaminant plume direction during the year, the Company revised its forecast of remedial activities to increase the level of extraction systems and the number of monitoring wells in and around the Goodyear Site, among other things. As of December 31, 2008, the revised liability estimate was \$65.2 million which resulted in an additional charge of \$24.3 million during the fourth quarter of 2008. During the fourth quarter of 2011, additional remediation activities were determined to be required, in consultation with the Company’s advisors, to further address the migration of the contaminant plume. As a result, the Company recorded a charge of \$30.3 million during the fourth quarter of 2011, extending the accrued costs through 2016. The total estimated gross liability was \$28.6 million as of March 31, 2014, and as described below, a portion is reimbursable by the U.S. Government. The current portion of the total estimated liability was approximately \$12.2 million and represents the Company’s best estimate, in consultation with its technical advisors, of total remediation costs expected to be paid during the twelve-month period.

Estimates of the Company’s environmental liabilities at the Goodyear Site are based on currently available facts, present laws and regulations and current technology available for remediation, and are recorded on an undiscounted basis. These estimates consider the Company’s prior experience in the Goodyear Site investigation and remediation, as well as available data from, and in consultation with, the Company’s environmental specialists. Estimates at the Goodyear Site are subject to significant uncertainties caused primarily by the dynamic nature of the Goodyear Site conditions, the range of remediation alternatives available, together with the corresponding estimates of cleanup methodology and costs, as well as ongoing, required regulatory approvals, primarily from the EPA. Accordingly, it is likely that upon completing the supplemental remediation investigation and feasibility study and reaching a final work plan in or before 2016, an adjustment to the Company’s liability estimate may be necessary to account for the agreed upon additional work as further information and circumstances regarding the Goodyear Site characterization develop. While actual remediation cost therefore may be more than amounts accrued, the Company believes it has established adequate reserves for all probable and reasonably estimable costs.

It is not possible at this point to reasonably estimate the amount of any obligation in excess of the Company’s current accruals through the 2016 forecast period because of the aforementioned uncertainties, in particular, the continued significant changes in the Goodyear Site conditions and additional expectations of remediation activities experienced in recent years.

On July 31, 2006, the Company entered into a consent decree with the U.S. Department of Justice on behalf of the Department of Defense and the Department of Energy pursuant to which, among other things, the U.S. Government

reimburses the Company for 21% of qualifying costs of investigation and remediation activities at the Goodyear Site. As of March 31, 2014, the Company has recorded a receivable of \$7.8 million for the expected reimbursements from the U.S. Government in respect of the aggregate liability as at that date. The receivable is reduced as reimbursements and other payments from the U.S. Government are received.

The Company has been identified as a potentially responsible party (“PRP”) with respect to environmental contamination at the Crab Orchard National Wildlife Refuge Superfund Site (the “Crab Orchard Site”). The Crab Orchard Site is located near Marion, Illinois, and consists of approximately 55,000 acres. Beginning in 1941, the United States used the Crab Orchard Site for the production of ordnance and other related products for use in World War II. In 1947, the Crab Orchard Site was transferred to the United States Fish and Wildlife Service (“FWS”), and about half of the Crab Orchard Site was leased to a variety of industrial tenants whose activities (which continue to this day) included manufacturing ordnance and explosives. A

predecessor to the Company formerly leased portions of the Crab Orchard Site, and conducted manufacturing operations at the Crab Orchard Site from 1952 until 1964. General Dynamics Ordnance and Tactical Systems, Inc. ("GD-OTS") is in the process of conducting a remedial investigation and feasibility study for the Additional and Uncharacterized Sites Operable Unit ("AUS-OU") at the Crab Orchard Site, pursuant to an Administrative Order on Consent between GD-OTS and the FWS, the EPA and the Illinois Environmental Protection Agency. The Company is not a party to that agreement, and has not been asked by any agency of the United States Government or the State of Illinois to participate in any investigative or remedial activity relative to the Crab Orchard Site. The Company has been informed that GD-OTS completed a Phase I remedial investigation in 2008, and a Phase II remedial investigation in 2010. Additionally, FWS completed its human health and baseline ecological risk assessments in 2010, and submitted a revised human health risk assessment in December 2011. GD-OTS is in the process of responding to agency comments on a revised draft remedial investigation report, and expects to submit the revised remedial investigation report after July 1, 2014. Further, based on discussions with FWS, GD-OTS contemplates performing a remedial investigation "addendum" in Spring 2014 to address potential data gaps, which is anticipated to include additional groundwater sampling in bedrock in certain areas of the Crab Orchard Site. Work on interim deliverables for the feasibility study is reportedly underway, with submission of the draft feasibility study report projected for early to mid-2016. It is unclear when a final Record of Decision may be issued.

GD-OTS has asked the Company to participate in a voluntary cost allocation/mediation exercise with respect to response costs it has incurred or will incur with respect to the AUS-OU. To date, the Company, along with a number of other PRPs that were contacted, have declined, citing the absence of certain necessary parties as well as an underdeveloped environmental record. In light of the ongoing investigative activities, and the apparent willingness of the U.S. government to participate in a mediation proceeding, it is possible that an allocation or mediation proceeding may go forward, and may commence in 2014. The Company at present cannot predict when any determination of the allocable share of the various PRPs, including the U.S. Government, is likely to be completed. Although a loss is probable, it is not possible at this time to reasonably estimate the amount of any obligation for remediation of the Crab Orchard Site because the extent of the environmental impact, allocation among PRPs, remediation alternatives, and concurrence of regulatory authorities have not yet advanced to the stage where a reasonable estimate can be made. The Company has notified its insurers of this potential liability and will seek coverage under its insurance policies. On a related matter, the United States has brought suit against GD-OTS and Schlumberger Technology Corporation ("Schlumberger"), seeking to recover response costs that the United States has allegedly incurred in connection with alleged environmental contamination at a portion of the Crab Orchard Site known as "Site 36," which is within the Site's Miscellaneous Areas Operable Unit. This area, reported to be the wastewater treatment plant formerly serving the Crab Orchard Site, is not a part of the AUS-OU, as discussed above. On June 1, 2012, GD-OTS and Schlumberger filed a third-party complaint against the Company and seven other third-party defendants, seeking to shift a portion of any costs that GD-OTS and Schlumberger are held liable to pay to other entities formerly conducting activities at Site 36. GD-OTS and Schlumberger have also counterclaimed against the United States, seeking to compel the United States to bear a share of the response costs the United States allegedly has incurred. The United States, GD-OTS, Schlumberger, the Company, and all remaining third-party defendants have resolved their claims against each other and have finalized the terms of a consent decree, which was entered by the Court on April 1, 2014. Pursuant to the parties' agreement, the Company paid \$166,667 to resolve all past and future claims for response costs relating to Site 36. The Company notified its insurers of this liability and has obtained an agreement for coverage for the settlement amount referenced above.

#### Other Proceedings

In 2009, at the request of the New Jersey Department of Environmental Protection, the Company performed certain tests of the indoor air quality of approximately 40 homes in a residential area surrounding a former manufacturing facility in Roseland, New Jersey (the "Site"), where the Company had performed soil and groundwater remediation activities after the manufacturing facility was closed in the mid-1980s, to determine if any contaminants (volatile organic compound vapors from groundwater) from the Site were present in those homes. The test results showed that three homes had volatile organic compound vapors above NJ DEP's recommended concentration levels, and the Company installed vapor mitigation equipment in those homes. On April 15, 2011, those three homeowners, and the tenants in one of those homes, filed separate suits against the Company seeking unspecified compensatory and

punitive damages for their lost property value and nuisance. In addition, a homeowner in the testing area, whose home tested negative for the presence of contaminants, filed a class action suit against the Company on behalf of himself and 141 other homeowners in the surrounding area, claiming damages in the nature of loss of value on their homes due to their proximity to the Site. The plaintiffs in these cases recently amended their complaints to assert claims under New Jersey's Environmental Rights Act for the Company's alleged failure to properly report its waste discharge practices in the late 1960s and early 1970s, and for natural resource damages. In late December 2013, the plaintiffs moved to have a class of 139 homeowners certified, and the motion was granted in early February 2014. At the same time the

Court also entered partial summary judgment on liability for the three homes where the Company had installed vapor mitigation equipment. It is not possible at this time to reasonably estimate the amount of a loss and therefore, no loss amount has been accrued for the claims because, among other things, the number of homes potentially affected, the extent of the environmental impact, and consideration of other factors affecting value have not yet advanced to the stage where a reasonable estimate can be made.

A number of other lawsuits, claims and proceedings have been or may be asserted against the Company relating to the conduct of its business, including those pertaining to product liability, patent infringement, commercial, employment, employee benefits, environmental and stockholder matters. While the outcome of litigation cannot be predicted with certainty, and some of these other lawsuits, claims or proceedings may be determined adversely to the Company, the Company does not believe that the disposition of any such other pending matters is likely to have a material impact on its financial condition or liquidity, although the resolution in any reporting period of one or more of these matters could have a significant impact on the Company's results of operations and cash flows for that period.

#### Other Commitments

The Company entered into a five year operating lease for an airplane in the first quarter of 2014 which included a maximum residual value guarantee of \$7.8 million by the Company if the fair value of the airplane was less than \$9.5 million at the end of the lease term.

Note 9 - Pension and Other Postretirement Benefit Plans

The components of net periodic cost are as follows:

(in thousands)	Three Months Ended March 31, 2014			
	Pension Benefits		Other Postretirement Benefits	
	2014	2013	2014	2013
Service cost	\$1,258	\$1,529	\$17	\$27
Interest cost	10,234	9,410	101	125
Expected return on plan assets	(15,713 )	(13,212 )	—	—