BORGWARNER INC
Form 10-Q
July 26, 2012
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UNITED STATES SECURITIES AND EXCHANGE COMMISSION
Washington D.C. 20549
FORM 10-Q
QUARTERLY REPORT
(Mark One)

R	Quarterly Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934 For the quarterly period ended June 30, 2012
OR	
o	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: 1-12162
BORGWARNER INC.

(Exact name of registrant as specified in its charter)

Delaware	13-3404508
State or other jurisdiction of Incorporation or organization	(I.R.S. Employer Identification No.)
3850 Hamlin Road, Auburn Hills, Michigan	48326
(Address of principal executive offices)	(Zip Code)

Registrant's telephone number, including area code: (248) 754-9200
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 R NO o
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 R NO o
Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See the definitions of "large accelerated filer," "accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act. (Check one):
Large accelerated filer R Accelerated filer o Non-accelerated filer o Smaller reporting company o
Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).
YES o NO R
As of July 20, 2012, the registrant had 114,441,115 shares of voting common stock outstanding.

BORGWARNER INC.
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THREE AND SIX MONTHS ENDED JUNE 30, 2012
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PART I. FINANCIAL INFORMATION
Item 1. Financial Information
BORGWARNER INC. AND CONSOLIDATED SUBSIDIARIES
CONDENSED CONSOLIDATED BALANCE SHEETS (UNAUDITED)

(millions of dollars)	June 30, 2012	December 31, 2011
ASSETS		
Cash	$481.9	$359.6
Receivables, net	1,327.7	1,183.0
Inventories, net	472.7	454.3
Deferred income taxes	37.5	58.5
Prepayments and other current assets	100.7	82.4
Total current assets	2,420.5	2,137.8
Property, plant and equipment, net	1,672.7	1,664.3
Investments and advances	363.7	345.3
Goodwill	1,161.8	1,186.2
Other non-current assets	602.0	625.0
Total assets	$6,220.7	$5,958.6
LIABILITIES AND EQUITY		
Notes payable and other short-term debt	$186.8	$196.3
Current portion of long-term debt	10.2	381.5
Accounts payable and accrued expenses	1,279.3	1,297.8
Income taxes payable	37.0	29.8
Total current liabilities	1,513.3	1,905.4
Long-term debt	956.2	751.3
Other non-current liabilities:		
Retirement-related liabilities	451.1	457.0
Other	365.6	391.9
Total other non-current liabilities	816.7	848.9
Common stock	1.2	1.2
Capital in excess of par value	1,477.8	1,134.3
Retained earnings	2,388.9	2,110.3
Accumulated other comprehensive loss	(182.6)	(150.8)
Common stock held in treasury	(811.6)	(707.1)
Total BorgWarner Inc. stockholders' equity	2,873.7	2,387.9
Noncontrolling interest	60.8	65.1
Total equity	2,934.5	2,453.0
Total liabilities and equity	$6,220.7	$5,958.6

See accompanying Notes to Condensed Consolidated Financial Statements.

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BORGWARNER INC. AND CONSOLIDATED SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS (UNAUDITED)

	Three Months Ended June 30,		Six Months Ended June 30,	
(in millions, except per share amounts)	2012	2011	2012	2011
Net sales	$1,856.4	$1,818.8	$3,768.9	$3,549.2
Cost of sales	1,473.2	1,461.7	2,989.9	2,849.3
Gross profit	383.2	357.1	779.0	699.9
Selling, general and administrative expenses	153.1	157.7	322.1	322.8
Other (income) expense	36.6	(28.9)	37.7	(30.5)
Operating income	193.5	228.3	419.2	407.6
Equity in affiliates' earnings, net of tax	(12.5)	(8.1)	(21.7)	(16.5)
Interest income	(1.3)	(1.2)	(2.7)	(2.2)
Interest expense and finance charges	12.6	20.5	27.7	38.9
Earnings before income taxes and noncontrolling interest	194.7	217.1	415.9	387.4
Provision for income taxes	68.5	49.8	126.0	90.7
Net earnings	126.2	167.3	289.9	296.7
Net earnings attributable to the noncontrolling interest, net of tax	5.6	5.3	11.3	10.2
Net earnings attributable to BorgWarner Inc.	$120.6	$162.0	$278.6	$286.5
Earnings per share — basic	$1.08	$1.49	$2.53	$2.61
Earnings per share — diluted	$1.00	$1.31	$2.28	$2.30
Weighted average shares outstanding:				
Basic	112.139	108.761	110.280	109.697
Diluted	121.473	128.142	124.608	129.183

See accompanying Notes to Condensed Consolidated Financial Statements.

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BORGWARNER INC. AND CONSOLIDATED SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME (UNAUDITED)

	Three Months Ended June 30,		Six Months Ended June 30,	
(millions of dollars)	2012	2011	2012	2011
Net earnings attributable to BorgWarner Inc.	$120.6	$162.0	$278.6	$286.5
Foreign currency translation adjustments	(90.7)	40.1	(45.9)	131.3
Hedge instrument adjustments				
Market value change of hedge instruments	(0.5)	(10.8)	13.7	(15.3)
Income taxes associated with the market value change of hedge instruments	0.8	3.7	(4.3)	4.4
Loss reclassified into net earnings	1.9	0.6	2.6	0.8
Income taxes reclassified into net earnings	(0.8)	(0.3)	(1.0)	(0.5)
Net change in hedge instruments	1.4	(6.8)	11.0	(10.6)
Defined benefit post employment plans				
Net unrecognized loss arising during the period	(0.7)	—	(0.7)	—
Income taxes associated with net unrecognized loss arising during the period	0.3	—	0.3	—
Amortization of prior service benefit and unrecognized loss into net earnings	2.2	1.8	4.4	3.8
Income taxes reclassified into net earnings	(0.8)	(0.7)	(1.4)	(1.3)
Acquisition	—	—	—	(5.4)
Income taxes associated with acquisition	—	—	—	1.4
Net change in defined benefit post employment plans	1.0	1.1	2.6	(1.5)
Other changes in OCI, net of tax	0.5	0.2	0.5	0.2
Comprehensive income	32.8	196.6	246.8	405.9
Comprehensive income attributable to the noncontrolling interest	(0.8)	1.3	0.1	2.7
Comprehensive income attributable to BorgWarner Inc.	$32.0	$197.9	$246.9	$408.6

See accompanying Notes to Condensed Consolidated Financial Statements.

BORGWARNER INC. AND CONSOLIDATED SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS (UNAUDITED)

	Six Months Ended June 30,	
(millions of dollars)	2012	2011
OPERATING		
Net earnings	$289.9	$296.7
Adjustments to reconcile net earnings to net cash flows from operations:		
Non-cash charges (credits) to operations:		
Depreciation and tooling amortization	126.8	125.0
Amortization of intangible assets and other	14.7	15.1
Loss from disposal activities, net of cash paid	34.8	—
Bond amortization	5.3	9.8
Stock-based compensation expense	31.1	11.2
Deferred income tax benefit	(5.6)	(14.6)
Equity in affiliates’ earnings, net of dividends received, and other	(7.9)	(20.3)
Net earnings adjusted for non-cash charges to operations	489.1	422.9
Changes in assets and liabilities:		
Receivables	(162.2)	(156.3)
Inventories	(27.3)	(31.0)
Prepayments and other current assets	(15.2)	(5.7)
Accounts payable and accrued expenses	25.9	25.3
Income taxes payable	8.3	(2.7)
Other non-current assets and liabilities	(8.5)	(2.9)
Net cash provided by operating activities	310.1	249.6
INVESTING		
Capital expenditures, including tooling outlays	(188.4)	(159.9)
Net proceeds from asset disposals	2.5	5.5
Payments for business acquired, net of cash acquired	—	(203.7)
Net proceeds from sale of business	1.6	2.1
Net cash used in investing activities	(184.3)	(356.0)
FINANCING		
Net (decrease) increase in notes payable	(9.4)	37.0
Additions to long-term debt, net of debt issuance costs	300.0	353.9
Repayments of long-term debt, including current portion	(96.2)	(139.7)
Payments for purchase of treasury stock	(200.3)	(268.8)
Proceeds from stock options exercised, including the tax benefit	48.2	38.2
Taxes paid on employees' restricted stock award vestings	(17.6)	(14.4)
Capital contribution from noncontrolling interest	—	19.5
Dividends paid to noncontrolling stockholders	(14.4)	(9.2)
Net cash provided by financing activities	10.3	16.5
Effect of exchange rate changes on cash	(13.8)	12.4
Net increase (decrease) in cash	122.3	(77.5)
Cash at beginning of year	359.6	449.9
Cash at end of period	$481.9	$372.4

SUPPLEMENTAL CASH FLOW INFORMATION

Net cash paid during the period for:		
Interest	$31.9	$36.3
Income taxes	87.3	78.0
Non-cash investing transactions:		
Liabilities assumed from business acquired	—	5.3
Non-cash financing transactions:		
Debt assumed from business acquired	—	5.9

See accompanying Notes to Condensed Consolidated Financial Statements.

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BORGWARNER INC. AND CONSOLIDATED SUBSIDIARIES
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(UNAUDITED)

(1) Basis of Presentation

The accompanying unaudited Condensed Consolidated Financial Statements of BorgWarner Inc. and Consolidated Subsidiaries (the “Company”) have been prepared in accordance with accounting principles generally accepted in the United States of America (“GAAP”) for interim financial information and with the instructions to Form 10-Q and Rule 10-01 of Regulation S-X. Accordingly, they do not include all of the information and footnotes necessary for a comprehensive presentation of financial position, results of operations and cash flow activity required by GAAP for complete financial statements. In the opinion of management, all normal recurring adjustments necessary for a fair presentation of results have been included. Operating results for the three and six months ended June 30, 2012 are not necessarily indicative of the results that may be expected for the year ending December 31, 2012. The balance sheet as of December 31, 2011 was derived from the audited financial statements as of that date. For further information, refer to the Consolidated Financial Statements and Footnotes thereto included in the Company’s Annual Report on Form 10-K for the year ended December 31, 2011.

Management makes estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities as of the date of the financial statements and accompanying notes, as well as, the amounts of revenues and expenses reported during the periods covered by those financial statements and accompanying notes. Actual results could differ from these estimates.

The Company retrospectively adopted the amendment to Accounting Standards Codification ("ASC") Topic 220, "Comprehensive Income," which requires companies to separately disclose reclassifications from other comprehensive income into net income on the face of the financial statements. Prior year balances within the Condensed Consolidated Statements of Comprehensive Income conform to this requirement.

(2) Research and Development

The Company's net Research & Development ("R&D") expenditures are included in selling, general and administrative expenses of the Condensed Consolidated Statements of Operations. Customer reimbursements are netted against gross R&D expenditures as they are considered a recovery of cost. Customer reimbursements for prototypes are recorded net of prototype costs based on customer contracts, typically either when the prototype is shipped or when it is accepted by the customer. Customer reimbursements for engineering services are recorded when performance obligations are satisfied in accordance with the contract and accepted by the customer. Financial risks and rewards transfer upon shipment, acceptance of a prototype component by the customer or upon completion of the performance obligation as stated in the respective customer agreement.

The following table presents the Company’s gross and net expenditures on R&D activities:

	Three Months Ended June 30,		Six Months Ended June 30,	
(millions of dollars)	2012	2011	2012	2011
Gross R&D expenditures	$76.7	$76.1	$152.9	$145.2
Customer reimbursements	(10.1)	(11.4)	(18.6)	(19.5)
Net R&D expenditures	$66.6	$64.7	$134.3	$125.7

The Company has contracts with several customers at the Company's various R&D locations. No such contract exceeded 5% of annual net R&D expenditures in any of the periods presented.

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(3) Other (Income) Expense

Items included in other (income) expense consist of:

(millions of dollars)	Three Months Ended June 30, 2012	Three Months Ended June 30, 2011	Six Months Ended June 30, 2012	Six Months Ended June 30, 2011
Loss from disposal activities	$37.9	$—	$37.9	$—
Patent infringement settlement, net of legal costs incurred	—	(29.1)	—	(29.1)
Other	(1.3)	0.2	(0.2)	(1.4)
Other (income) expense	$36.6	$(28.9)	$37.7	$(30.5)

During the second quarter of 2012, the Company signed a Master Purchase Agreement to sell its spark plug business to Federal-Mogul Corporation. As a result, the Company recorded expense of $37.9 million primarily to write-down prior purchase price accounting adjustments included within the disposal group. These purchase price accounting adjustments were originally recorded in the Engine segment and related to the BERU acquisition.

On May 16, 2011, BorgWarner and Honeywell settled a lawsuit resolving BorgWarner's patent infringement claims. As a result of the settlement, Honeywell paid $32.5 million for a paid up license to use the asserted BorgWarner patents. During 2011, the Company incurred $3.4 million in legal costs related to this lawsuit and after deducting these costs, the Company recorded a net gain of $29.1 million.

(4) Income Taxes

The Company's provision for income taxes is based upon an estimated annual tax rate for the year applied to federal, state and foreign income. On a quarterly basis, the annual effective tax rate is adjusted, as appropriate, based upon changed facts and circumstances, if any, as compared to those forecasted at the beginning of the fiscal year and each interim period thereafter.

At June 30, 2012, the Company estimated its U.S. GAAP effective tax rate to be approximately 29% for the year ending December 31, 2012. This rate includes a tax benefit of $5.5 million associated with the $37.9 million loss from disposal activities recorded in the second quarter of 2012 and an expense of $9.0 million associated with the Company's decision to change its cash repatriation assertion for some of its foreign subsidiaries. Primarily as a result of the change in the Company's cash repatriation assumptions, the Company also increased its estimated annual effective tax rate for on-going business operations from 26% to 27%.

The Company is not required to provide U.S. federal or state income taxes on cumulative undistributed earnings of foreign subsidiaries when such earnings are considered permanently reinvested. At December 31, 2011, the Company considered most of its foreign unremitted earnings to be permanently reinvested. The Company's policy is to evaluate this assertion on a quarterly basis. During the second quarter of 2012, the Company changed the assertion for some of its foreign subsidiaries to provide management additional financial flexibility.

At June 30, 2011, the Company estimated its U.S. GAAP effective tax rate to be approximately 24% for the year ending December 31, 2011. This rate included $11.0 million of additional tax expense associated with the Company's patent infringement settlement and a tax benefit of $6.2 million resulting from other tax adjustments. These other tax adjustments related to a change in state corporate income tax legislation as well as an adjustment of the Company's tax accounts as a result of the closure of certain tax audits.

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The annual effective tax rates differ from the U.S. statutory rate primarily due to foreign rates which differ from those in the U.S., the realization of certain business tax credits, including foreign tax credits, and favorable permanent differences between book and tax treatment for certain items, including equity in affiliates' earnings. The estimated annual effective tax rate for 2012 is higher than the annual effective tax rate for 2011 primarily due to the Company's projected increased profitability in higher taxed jurisdictions and the items discussed above.

(5) Inventories, net

Inventories are valued at the lower of cost or market. The cost of U.S. inventories is determined by the last-in, first-out (“LIFO”) method, while the operations outside the U.S. use the first-in, first-out (“FIFO”) or average-cost methods. Inventories consisted of the following:

(millions of dollars)	June 30 2012	December 31, 2011
Raw material and supplies	$273.3	$254.4
Work in progress	89.7	90.9
Finished goods	128.2	124.3
FIFO inventories	491.2	469.6
LIFO reserve	(18.5)	(15.3)
Inventories, net	$472.7	$454.3

(6) Property, Plant and Equipment, net

(millions of dollars)	June 30, 2012	December 31, 2011
Land and buildings	$691.4	$687.9
Machinery and equipment	2,141.8	2,006.9
Capital leases	2.3	2.3
Construction in progress	201.4	206.8
Total property, plant and equipment, gross	3,036.9	2,903.9
Less: accumulated depreciation	(1,466.7)	(1,343.9)
Property, plant and equipment, net, excluding tooling	1,570.2	1,560.0
Tooling, net of amortization	102.5	104.3
Property, plant and equipment, net	$1,672.7	$1,664.3

As of June 30, 2012 and December 31, 2011, accounts payable of $18.1 million and $48.9 million, respectively, were related to property, plant and equipment purchases.

Interest costs capitalized for the six months ended June 30, 2012 and 2011 were $9.0 million and $6.0 million, respectively.

(7) Product Warranty

The Company provides warranties on some, but not all, of its products. The warranty terms are typically from one to three years. Provisions for estimated expenses related to product warranty are made at the time products are sold. These estimates are established using historical information about the nature, frequency and average cost of warranty claim settlements as well as product manufacturing and industry developments and recoveries from third parties. Management actively studies trends of warranty claims and takes action to improve product quality and minimize warranty claims. Management believes that the warranty accrual is appropriate, however, actual claims incurred could differ from the original estimates, requiring adjustments to the accrual.

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The following table summarizes the activity in the product warranty accrual accounts:

(millions of dollars)	2012	2011
Beginning balance, January 1	$72.7	$66.8
Acquisition	—	4.5
Provisions	17.1	24.1
Payments	(16.5)	(25.4)
Translation adjustment	(0.9)	3.7
Ending balance, June 30	$72.4	$73.7

The product warranty liability is classified in the Condensed Consolidated Balance Sheets as follows:

(millions of dollars)	June 30, 2012	December 31, 2011
Accounts payable and accrued expenses	$38.6	$38.6
Other non-current liabilities	33.8	34.1
Total product warranty liability	$72.4	$72.7

(8) Notes Payable and Long-Term Debt

As of June 30, 2012 and December 31, 2011, the Company had short-term and long-term debt outstanding as follows:

(millions of dollars)	June 30, 2012	December 31, 2011
Short-term debt		
Short-term borrowings	$106.8	$116.3
Receivables securitization	80.0	80.0
Total short-term debt	$186.8	$196.3
Long-term debt		
3.50% Convertible senior notes due 04/15/12	$—	$368.5
5.75% Senior notes due 11/01/16 ($150 million par value)	149.5	149.5
8.00% Senior notes due 10/01/19 ($134 million par value)	133.9	133.9
4.625% Senior notes due 09/15/20 ($250 million par value)	247.7	247.7
7.125% Senior notes due 02/15/29 ($121 million par value)	119.4	119.3
Multi-currency revolving credit facility	280.0	70.0
Term loan facilities and other	13.8	19.8
Unamortized portion of debt derivatives	22.1	24.1
Total long-term debt	966.4	1,132.8
Less: current portion	10.2	381.5
Long-term debt, net of current portion	$956.2	$751.3

The weighted average interest rate on all borrowings outstanding as of June 30, 2012 and December 31, 2011 was 3.9% and 5.9%, respectively.

The Company's $650 million multi-currency revolving credit facility, which includes a feature that allows the Company's borrowings to be increased to $1 billion, provides for borrowings through June 30, 2016 and is guaranteed by the Company's material domestic subsidiaries. The Company has two key financial covenants as part of the credit agreement. These covenants are a debt compared to EBITDA (“Earnings

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Before Interest, Taxes, Depreciation and Amortization") test and an interest coverage test. The Company was in compliance with all covenants at June 30, 2012 and expects to remain compliant in future periods. At June 30, 2012 and December 31, 2011, the Company had outstanding borrowings of $280.0 million and $70.0 million, respectively, under this facility.

On April 9, 2009, the Company issued $373.8 million in convertible senior notes, which were settled in April 2012. The Company settled its convertible senior notes by delivering approximately 11.4 million shares of common stock held in treasury to the note holders. The settlement resulted in a reduction in the current portion of long-term debt of $373.8 million, a reduction in common stock held in treasury of $617.3 million and a reduction in capital in excess of par value of $243.5 million in the second quarter of 2012. Prior to the settlement, the Company accreted the discounted carrying value of the convertible notes to their face value over the term of the notes.

The total interest expense related to the convertible senior notes in the Company's Condensed Consolidated Statements of Operations for the three and six months ended June 30, 2012 and 2011 is as follows:

	Three Months Ended June 30,		Six Months Ended June 30,	
(millions of dollars)	2012	2011	2012	2011
Interest expense	$1.4	$8.3	$9.0	$16.3
Non-cash portion	$0.9	$5.0	$5.3	$9.8

In conjunction with the convertible senior note offering, the Company entered into a bond hedge overlay, including both call options and warrants, at a net pre-tax cost of $25.2 million, effectively raising the conversion premium to 50.0%, or approximately $38.61 per share. On April 16, 2012, the Company settled the call option portion of the bond hedge overlay, receiving approximately 6.5 million shares of its common stock. The settlement resulted in an increase to common stock held in treasury of $503.9 million offset by an increase to capital in excess of par value of $503.9 million in the second quarter of 2012.

Subsequent to the Balance Sheet date, on July 13, 2012, the Company settled half of the outstanding warrants included in the bond hedge overlay, delivering approximately 2.3 million shares of its common stock held in treasury. The settlement will result in a decrease to common stock held in treasury of $148.7 million offset by a decrease to capital in excess of par value of $148.7 million in the third quarter of 2012. The remaining warrants are scheduled to mature through October 9, 2012.

As of June 30, 2012 and December 31, 2011, the estimated fair values of the Company's senior unsecured notes totaled $777.0 million and $1,454.4 million, respectively. The estimated fair values were $126.5 million and $435.5 million higher at June 30, 2012 and December 31, 2011, respectively, than their carrying values. The carrying value of the Company's multi-currency revolving credit facility is equal to its fair value. Fair market values are developed using observable values for similar debt instruments, which are considered Level 2 inputs as defined by ASC Topic 820. The fair value estimates do not necessarily reflect the values the Company could realize in the current markets.

The Company had outstanding letters of credit of $50.0 million at both June 30, 2012 and December 31, 2011. The letters of credit typically act as guarantees of payment to certain third parties in accordance with specified terms and conditions.

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(9) Fair Value Measurements

ASC Topic 820 emphasizes that fair value is a market-based measurement, not an entity specific measurement. Therefore, a fair value measurement should be determined based on assumptions that market participants would use in pricing an asset or liability. As a basis for considering market participant assumptions in fair value measurements, ASC Topic 820 establishes a fair value hierarchy, which prioritizes the inputs used in measuring fair values as follows:

Level 1: Observable inputs such as quoted prices for identical assets or liabilities in active markets;
Level 2: Inputs, other than quoted prices in active markets, that are observable either directly or indirectly; and
Level 3: Unobservable inputs in which there is little or no market data, which require the reporting entity to develop its own assumptions.

Assets and liabilities measured at fair value are based on one or more of the following three valuation techniques noted in ASC Topic 820:

A. Market approach: Prices and other relevant information generated by market transactions involving identical or comparable assets, liabilities or a group and assets or liabilities, such as a business.
B. Cost approach: Amount that would be required to replace the service capacity of an asset (replacement cost).
C. Income approach: Techniques to convert future amounts to a single present amount based upon market expectations (including present value techniques, option-pricing and excess earnings models).

The following table classifies the assets and liabilities measured at fair value on a recurring basis as of June 30, 2012:

		Basis of fair value measurements			
(millions of dollars)	Balance at June 30, 2012	Quoted prices in active markets for identical items (Level 1)	Significant other observable inputs (Level 2)	Significant unobservable inputs (Level 3)	Valuation technique
Assets:					
Foreign currency contracts	$6.7	$—	$6.7	$—	A
Other non-current assets (insurance settlement agreement note receivable)	$11.7	$—	$11.7	$—	C
Liabilities:					
Foreign currency contracts	$0.5	$—	$0.5	$—	A
Commodity contracts	$—	$—	$—	$—	A
Net investment hedge contracts	$77.1	$—	$77.1	$—	A

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The following table classifies the assets and liabilities measured at fair value on a recurring basis as of December 31, 2011:

(millions of dollars)	Balance at December 31, 2011	Basis of fair value measurements Quoted prices in active markets for identical items (Level 1)	Significant other observable inputs (Level 2)	Significant unobservable inputs (Level 3)	Valuation technique
Assets:					
Foreign currency contracts	$2.7	$—	$2.7	$—	A
Other non-current assets (insurance settlement agreement note receivable)	$21.3	$—	$21.3	$—	C
Liabilities:					
Foreign currency contracts	$2.9	$—	$2.9	$—	A
Net investment hedge contracts	$85.0	$—	$85.0	$—	A

(10) Financial Instruments

The Company’s financial instruments include cash and marketable securities. Due to the short-term nature of these instruments, their book value approximates their fair value. The Company’s financial instruments also include long-term debt, interest rate and cross-currency swaps, commodity derivative contracts and foreign currency derivatives. All derivative contracts are placed with counterparties that have an S&P, or equivalent, investment grade credit rating at the time of the contracts’ placement. At June 30, 2012, the Company had no derivative contracts that contained credit risk related contingent features.

The Company selectively uses cross-currency swaps to hedge the foreign currency exposure associated with our net investment in certain foreign operations (net investment hedges). At June 30, 2012 and December 31, 2011, the following cross-currency swaps were outstanding: