BORGWARNER INC
Form 10-Q
April 30, 2009

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UNITED STATES SECURITIES AND EXCHANGE COMMISSION
Washington D.C. 20549
FORM 10-Q
QUARTERLY REPORT

(Mark One)

þ **Quarterly Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934**
For the quarterly period ended March 31, 2009

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 þ 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 þ 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 þ 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 þ

On March 31, 2009, the registrant had 116,527,045 shares of Common Stock outstanding.

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PART I. FINANCIAL INFORMATION
BORGWARNER INC. AND CONSOLIDATED SUBSIDIARIES
CONDENSED CONSOLIDATED BALANCE SHEETS
(millions of dollars)

	March 31, 2009 (Unaudited)	December 31, 2008
ASSETS		
Cash	$ 90.8	$ 103.4
Receivables, net	622.1	607.1
Inventories, net	352.4	451.2
Deferred income taxes	61.7	67.5
Prepayments and other current assets	61.4	79.0
Total current assets	1,188.4	1,308.2
Property, plant and equipment, net	1,510.1	1,586.2
Investments and advances	243.0	266.5
Goodwill	1,038.1	1,052.4
Other non-current assets	374.1	430.7
Total assets	$ 4,353.7	$ 4,644.0
LIABILITIES AND STOCKHOLDERS EQUITY		
Notes payable	$ 250.4	$ 183.8
Current portion of long-term debt		136.9
Accounts payable and accrued expenses	851.4	923.0
Income taxes payable	9.2	6.3
Total current liabilities	1,111.0	1,250.0
Long-term debt	466.5	459.6
Other non-current liabilities:		
Retirement-related liabilities	467.8	543.8
Other	321.5	353.1
Total other non-current liabilities	789.3	896.9
Common stock	1.2	1.2
Capital in excess of par value	984.7	977.6
Retained earnings	1,179.6	1,200.5
Accumulated other comprehensive loss	(117.5)	(85.9)
Treasury stock	(87.0)	(87.4)
Total BorgWarner Inc. stockholders equity	1,961.0	2,006.0

Noncontrolling interest	25.9	31.5
Total stockholders equity	1,986.9	2,037.5
Total liabilities and stockholders equity	$ 4,353.7	$ 4,644.0

See accompanying Notes to Condensed Consolidated Financial Statements

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BORGWARNER INC. AND CONSOLIDATED SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS (UNAUDITED)
(millions of dollars, except share and per share data)

	Three Months Ended March 31,	
	2009	**2008**
Net sales	$ 819.5	$ 1,498.9
Cost of sales	739.9	1,215.4
Gross profit	79.6	283.5
Selling, general and administrative expenses	74.1	155.7
Other expense		3.0
Operating income	5.5	124.8
Equity in affiliates earnings, net of tax	(0.2)	(9.1)
Interest income	(0.5)	(1.9)
Interest expense and finance charges	19.1	6.5
Earnings (loss) before income taxes and noncontrolling interest	(12.9)	129.3
Provision (benefit) for income taxes	(6.6)	33.6
Net earnings (loss)	(6.3)	95.7
Net earnings attributable to the noncontrolling interest	0.7	7.0
Net earnings (loss) attributable to BorgWarner Inc.	$ (7.0)	$ 88.7
Earnings (loss) per share basic	$ (0.06)*	$ 0.76
Earnings (loss) per share diluted	$ (0.06)*	$ 0.75
Weighted average shares outstanding (thousands):		
Basic	116,029	116,247
Diluted	116,029*	118,466
Dividends declared per share	$ 0.12	$ 0.11

* The Company had a loss for the quarter ended

March 31, 2009. As a result, diluted loss per share is the same as basic in the period, as any dilutive securities would reduce the loss per share. Therefore, diluted shares are equal to basic shares outstanding for the three months ended March 31, 2009.

See accompanying Notes to Condensed Consolidated Financial Statements

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

	Three Months Ended March 31, 2009	Three Months Ended March 31, 2008
OPERATING		
Net earnings (loss) attributable to BorgWarner Inc.	$ (7.0)	$ 88.7
Adjustments to reconcile net earnings (loss) to net cash flows from operations:		
Non-cash charges (credits) to operations:		
Depreciation and tooling amortization	57.3	66.8
Amortization of intangible assets and other	5.8	5.4
Stock based compensation expense	5.2	5.5
Deferred income tax loss (benefit)	(12.1)	4.0
Equity in affiliates earnings, net of dividends received, noncontrolling interest and other	45.1	4.4
Net earnings adjusted for non-cash charges to operations	94.3	174.8
Changes in assets and liabilities:		
Receivables	(37.6)	(111.2)
Inventories	83.4	(5.3)
Prepayments and other current assets	14.9	8.0
Accounts payable and accrued expenses	(54.3)	22.2
Income taxes payable	3.8	(11.4)
Other non-current assets and liabilities	(36.5)	(2.6)
Net cash provided by operating activities	68.0	74.5
INVESTING		
Capital expenditures, including tooling outlays	(38.6)	(75.4)
Net proceeds from asset disposals	5.2	0.3
Payments for business acquired, net of cash acquired	(12.2)	
Proceeds from sales of marketable securities		3.7
Net cash used in investing activities	(45.6)	(71.4)
FINANCING		
Increase in notes payable	70.2	79.0
Additions to long-term debt	20.0	
Repayments of long-term debt, including current portion	(136.7)	(5.1)
Payment for purchase of treasury stock		(13.5)
Proceeds from interest rate swap termination	30.0	
Proceeds from stock options exercised, including the tax benefit	0.5	2.7
Dividends paid to BorgWarner stockholders	(13.8)	(12.8)
Dividends paid to noncontrolling stockholders	(4.6)	(8.2)
Net cash provided by (used in) financing activities	(34.4)	42.1
Effect of exchange rate changes on cash	(0.6)	(30.3)

Net increase (decrease) in cash	(12.6)	14.9
Cash at beginning of year	103.4	188.5
Cash at end of period	$ 90.8	$ 203.4
SUPPLEMENTAL CASH FLOW INFORMATION		
Net cash paid (refunded) during the period for:		
Interest	$ 11.4	$ 11.7
Income taxes	(0.9)	45.3
Non-cash financing transactions:		
Stock Performance Plans	1.5	1.5

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 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 months ended March 31, 2009 are not necessarily indicative of the results that may be expected for the year ending December 31, 2009. The balance sheet as of December 31, 2008 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, 2008.

We have reclassified certain 2008 amounts to conform to the presentation of our 2009 Condensed Consolidated Statement of Operations. The financial statements and Management s Discussion and Analysis of Financial Condition and Results of Operations should be read in conjunction with the Company s Annual Report on Form 10-K for the fiscal year ended December 31, 2008. The Company s presentation of the Condensed Consolidated Balance Sheets, Condensed Consolidated Statements of Operations, Reporting Segments Note and Comprehensive Income (Loss) Note have been adjusted to conform with the requirements of Statement of Financial Accounting Standard No. 160, Non-controlling Interest in Consolidated Financial Statements, (FAS 160). See Note 18 to the Condensed Consolidated Financial Statements for more information regarding the Company s first quarter 2009 adoption of FAS 160.

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.

(2) Research and Development

The following table presents the Company s gross and net expenditures on research and development (R&D) activities:

(millions)		
Three months ended March 31,	**2009**	**2008**
Gross R&D expenditures	$ 48.5	$ 67.0
Customer reimbursements	(16.0)	(9.5)
Net R&D expenditures	$ 32.5	$ 57.5

The Company s net R&D expenditures are included in the selling, general and administrative expenses of the Condensed Consolidated Statements of Operations. Customer reimbursements are netted against gross R&D expenditures upon billing of services performed. The Company has contracts with several customers at the Company s various R&D locations. No such contract exceeded $6 million in any of the periods presented.

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(3) Income Taxes

The Company s provision for income taxes is normally based on an estimated tax rate for the year applied to the year-to-date federal, state and foreign income. However, due to unprecedented depressed global economic conditions there is a significant amount of uncertainty regarding industry production volumes for the remainder of the year. This precludes us from making a reliable estimate of the annual effective tax rate for the year. Accordingly, we have made our income tax provision in the first quarter pursuant to Financial Accounting Standards Board (FASB) Interpretation No. 18, Accounting for Income Taxes in interim Periods, which provides that tax (or benefit) in each foreign jurisdiction that is not subject to a valuation allowance be separately computed as ordinary income/(loss) occurs within the jurisdiction for the quarter. The actual global effective tax rate for the quarter is calculated to be a benefit of (51.3%). This represents an income tax benefit of ($6.6) million on the loss of ($12.9) million for the first quarter of 2009.

As of March 31, 2009, the balance of gross unrecognized tax benefits is $61.1 million. Included in the balance at March 31, 2009 are $50.9 million of tax positions that are permanent in nature and, if recognized, would reduce the global effective tax rate.

During the first quarter of 2008, the Company made a $6.6 million cash payment to the Internal Revenue Service (IRS) to resolve agreed upon issues of the ongoing IRS examination of the Company s 2002-2004 tax years. Also, there was a reduction in the first quarter of 2008 of $6.7 million related to the Company s unrecognized tax benefits balance due to settlement of the agreed upon issues primarily related to the Extraterritorial Income Exclusion for the 2002-2004 tax years. The Company is currently in the appeals process on disputed issues related to the 2002-2004 IRS audit, which is not expected to be resolved by December 31, 2009. Other possible changes in the unrecognized tax benefits balance related to other examinations cannot be reasonably estimated within the next 12 months.

The Company recognizes interest and penalties related to unrecognized tax benefits in income tax expense. The Company had approximately $11.4 million for the payment of interest and penalties accrued at December 31, 2008. The Company had approximately $11.9 million for the payment of interest and penalties accrued at March 31, 2009.

The Company or one of its subsidiaries files income tax returns in the U.S. federal jurisdiction, and various states and foreign jurisdictions. The Company is no longer subject to income tax examinations by tax authorities in its major tax jurisdictions as follows:

Tax Jurisdiction	Years No Longer Subject to Audit
U.S. Federal	2001 and prior
Brazil	2002 and prior
France	2006 and prior
Germany	2003 and prior
Hungary	2004 and prior
Italy	2002 and prior
Japan	2006 and prior
South Korea	2004 and prior
United Kingdom	2006 and prior

In certain tax jurisdictions the Company may have more than one taxpayer. The table above reflects the status of the major taxpayer in each major tax jurisdiction.

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(4) Sales of Receivables

The Company securitizes and sells certain receivables through third party financial institutions without recourse. The amount sold can vary each month based on the amount of underlying receivables. The Company continues to administer the collection of these receivables on behalf of the third party. The maximum size of the facility has been set at $50 million since fourth quarter of 2003.

At both March 31, 2009 and December 31, 2008, the Company had sold $50 million of receivables under a Receivables Transfer Agreement for face value without recourse. During both of the three-month periods ended March 31, 2009 and 2008, total cash proceeds from sales of accounts receivable were $150 million. The Company paid servicing fees related to these receivables for the three months ended March 31, 2009 and 2008 of $0.3 million and $0.6 million, respectively. These amounts are recorded in interest expense and finance charges in the Condensed Consolidated Statements of Operations.

On April 24, 2009 the $50 million receivables securitization matured and was not renewed. The impact of this maturity will be an increase in receivables of $50 million and a decrease in cash of $50 million in the second quarter of 2009.

(5) Inventories

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)	March 31, 2009	December 31, 2008
Raw material and supplies	$ 212.7	$ 260.7
Work in progress	72.7	95.7
Finished goods	82.7	111.4
FIFO inventories	368.1	467.8
LIFO reserve	(15.7)	(16.6)
Inventories, net	$ 352.4	$ 451.2

(6) Property, Plant and Equipment

(millions)	March 31, 2009	December 31, 2008
Land and buildings	$ 608.4	$ 619.8
Machinery and equipment	1,705.8	1,756.1
Capital leases	1.1	1.1
Construction in progress	148.7	160.0
Total property, plant and equipment	2,464.0	2,537.0
Less accumulated depreciation	(1,046.2)	(1,047.4)
	1,417.8	1,489.6
Tooling, net of amortization	92.3	96.6
Property, plant and equipment, net	$ 1,510.1	$ 1,586.2

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Interest costs capitalized during the three-month periods ended March 31, 2009 and March 31, 2008 were $2.7 million and $1.8 million, respectively.

As of March 31, 2009 and December 31, 2008, accounts payable of $42.3 million and $43.2 million, respectively, were related to property, plant and equipment purchases.

As of March 31, 2009 and December 31, 2008, specific assets of $7.0 million and $7.4 million, respectively, were pledged as collateral under certain of the Company s long-term debt agreements.

During the first quarter of 2009, based on current market conditions and asset utilization rates, the Company elected to extend the useful lives of certain machinery and equipment. As a result of this change in estimate, depreciation expense was reduced by approximately $4 million. As a result of the impairment charges recorded in the third and fourth quarters of 2008, depreciation expense was further reduced by approximately $3 million.

(7) Product Warranty

The Company provides warranties on some 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 claims. Management actively studies trends of warranty claims and takes action to improve product quality and minimize warranty claims. While management believes that the warranty accrual is appropriate, actual claims incurred could differ from the original estimates, requiring adjustments to the accrual. The accrual is recorded in both long-term and short-term liabilities on the balance sheet. The following table summarizes the activity in the warranty accrual accounts:

	Three months ended March 31,	
(millions)	**2009**	**2008**
Beginning balance	$ 82.1	$ 70.1
Provision	0.2	10.1
Payments	(15.3)	(6.7)
Currency translation	(2.9)	3.3
Ending balance	$ 64.1	$ 76.8

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(8) Notes Payable and Long-Term Debt

Following is a summary of notes payable and long-term debt, including the current portion. The weighted average interest rate on all borrowings outstanding as of March 31, 2009 and December 31, 2008 was 4.3% and 5.0%, respectively.

	March 31, 2009		December 31, 2008	
(millions)	Current	Long-Term	Current	Long-Term
Bank borrowings and other	$197.7	$ 0.5	$130.7	$ 1.0
Term loans due through 2015 (at an average rate of 5.9% in 2009 and 4.9% in 2008)	52.7	29.6	53.1	12.9
6.50% Senior Notes due 02/17/09, net of unamortized discount (a)			136.7	
5.75% Senior Notes due 11/01/16, net of unamortized discount (a)		149.2		149.2
8.00% Senior Notes due 10/01/19, net of unamortized discount (a)		133.9		133.9
7.125% Senior Notes due 02/15/29, net of unamortized discount		119.2		119.2
Carrying amount of notes payable and long-term debt	250.4	432.4	320.5	416.2
Impact of derivatives on debt (a)		34.1	0.2	43.4
Total notes payable and long-term debt	$250.4	$466.5	$320.7	$459.6

(a) In 2006, the Company entered into several interest rate swaps that had the effect of converting $325.0 million of fixed rate notes to variable rates. The weighted average effective interest rate of these borrowings, including the effects of outstanding swaps as noted in Note 10 was 5.3% as of December 31,

2008. In the first quarter of 2009, $100 million in interest rate swaps related to the Company s 2009 fixed rate debt matured and the Company terminated $150 million in interest rate swap agreements related to the Company s 2016 fixed rate debt and $75 million of interest rate swap agreements related to the Company s 2019 fixed rate debt. As a result of the first quarter 2009 swap terminations, a $34.5 million gain remained in debt to be amortized over the remaining lives of the respective 2016 and 2019 debt. As of March 31, 2009, the unamortized portion was $34.1 million.

The Company has a multi-currency revolving credit facility, which provides for borrowings up to $600 million through July 22, 2009. Subsequent to the end of the first quarter of 2009, the Company extended its revolving credit facility for eighteen months, maturing January 22, 2011. The facility will be reduced to $250 million beginning July 23, 2009. At March 31, 2009 and December 31, 2008 there were no outstanding borrowings under the facility. The credit agreement is subject to the usual terms and conditions applied by banks to an investment grade company. The three key covenants of the credit agreement are a net worth test, a debt compared to EBITDA (Earnings Before Interest, Taxes, Depreciation and Amortization) test, and an interest coverage test. The Company was in compliance with all covenants at March 31, 2009 and expects to remain compliant in future periods. The Company s 6.5% Senior Notes of $136.7 million matured on February 17, 2009. The Company had outstanding letters of credit at March 31, 2009 and December 31, 2008 of $16.8 million and $21.4 million, respectively. The letters of credit typically act as a guarantee of payment to certain third parties in accordance with specified terms and conditions.

As of March 31, 2009 and December 31, 2008, the estimated fair values of the Company s senior unsecured notes totaled $270.5 million and $532.3 million, respectively. The estimated fair values were $131.8 million lower at March 31, 2009 and $6.7 million higher at December 31, 2008 than their respective carrying values. Fair market values are developed by the use of estimates obtained from brokers and other appropriate valuation techniques based on information available as of quarter-end and year-end. The fair value estimates do not necessarily reflect the values the Company could realize in the current markets.

(9) Fair Value Measurements

On January 1, 2009, the Company fully adopted as required, Statement of Financial Accounting Standards No. 157 Fair Value Measurements (SFAS 157) which expands the disclosure of fair value measurements and its impact on the Company s financial statements.

Statement No. 157 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

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participants would use in pricing an asset or liability. As a basis for considering market participant assumptions in fair value measurements, SFAS 157 establishes a fair value hierarchy, which prioritizes the inputs used in measuring fair values as follows:

Level 1: Observable inputs such as quoted prices 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 SFAS 157:

A. Market approach: Prices and other relevant information generated by market transactions involving identical or comparable assets or liabilities.

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 during the period ended March 31, 2009:

		Basis of Fair Value Measurements			
(millions)	**Balance at March 31, 2009**	**Quoted Prices in Active Markets for Identical Items (Level 1)**	**Significant Other Observable Inputs (Level 2)**	**Significant Unobservable Inputs (Level 3)**	**Valuation Technique**
Assets:					
Commodity contracts	$ 1.0	$	$ 1.0	$	A
Foreign exchange contracts	9.9		9.9		A
	$ 10.9	$	$ 10.9	$	
Liabilities:					
Commodity contracts	$ 10.0	$	$ 10.0	$	A
Foreign exchange contracts	50.6		50.6		A
Net investment hedge contracts	40.8		40.8		A