

CENTURY ALUMINUM CO
Form 10-Q
November 08, 2016

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549

FORM 10-Q

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

For the quarterly period ended September 30, 2016

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 1-34474

Century Aluminum Company

(Exact name of registrant as specified in its charter)

Delaware

13-3070826

(State or other jurisdiction of incorporation or organization) (IRS Employer Identification No.)

One South Wacker Drive

Suite 1000

60606

Chicago, Illinois

(Zip Code)

(Address of principal executive offices)

Registrant's telephone number, including area code: (312) 696-3101

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 website, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§ 232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes No

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer or a smaller reporting company. See the definitions of "large accelerated filer," "accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer

Accelerated filer

Non-accelerated filer

Smaller reporting company

(Do not check if a smaller reporting company)

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).

Yes No

The registrant had 87,075,587 shares of common stock outstanding at October 31, 2016.

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PART I – FINANCIAL INFORMATION

Item 1. Financial Statements.

CENTURY ALUMINUM COMPANY
CONSOLIDATED STATEMENTS OF OPERATIONS

(in thousands, except per share amounts)

(Unaudited)

	Three months ended		Nine months ended	
	September 30,		September 30,	
	2016	2015	2016	2015
NET SALES:				
Related parties	\$301,111	\$428,018	\$871,771	\$1,517,428
Third-party customers	32,539	26,522	107,487	48,514
Total net sales	333,650	454,540	979,258	1,565,942
Cost of goods sold	351,262	496,963	995,357	1,505,928
Gross profit (loss)	(17,612)	(42,423)	(16,099)	60,014
Selling, general and administrative expenses	9,733	11,566	29,303	33,549
Ravenswood charges	26,830	—	26,830	30,850
Other operating expense - net	878	1,537	2,337	6,217
Operating loss	(55,053)	(55,526)	(74,569)	(10,602)
Interest expense	(5,531)	(5,418)	(16,521)	(16,542)
Interest income	190	45	475	248
Net gain on forward and derivative contracts	1,275	285	2,998	1,204
Unrealized gain on fair value of contingent consideration	—	1,523	—	18,337
Other income (expense) - net	(157)	114	(462)	1,261
Loss before income taxes and equity in earnings of joint ventures	(59,276)	(58,977)	(88,079)	(6,094)
Income tax benefit (expense)	848	2,161	3,237	(12,205)
Loss before equity in earnings of joint ventures	(58,428)	(56,816)	(84,842)	(18,299)
Equity in earnings of joint ventures	155	704	891	2,069
Net loss	\$(58,273)	\$(56,112)	\$(83,951)	\$(16,230)
Net loss allocated to common stockholders	\$(58,273)	\$(56,112)	\$(83,951)	\$(16,230)
LOSS PER COMMON SHARE:				
Basic and diluted	\$(0.67)	\$(0.65)	\$(0.96)	\$(0.19)
WEIGHTED AVERAGE COMMON SHARES OUTSTANDING:				
Basic and diluted	87,076	86,907	87,059	87,524

See condensed notes to consolidated financial statements

CENTURY ALUMINUM COMPANY
CONSOLIDATED STATEMENTS OF COMPREHENSIVE LOSS
(in thousands)
(Unaudited)

	Three months ended September 30,		Nine months ended September 30,	
	2016	2015	2016	2015
Comprehensive loss:				
Net loss	\$(58,273)	\$(56,112)	\$(83,951)	\$(16,230)
Other comprehensive income (loss) before income tax effect:				
Net loss on foreign currency cash flow hedges reclassified as income	(46)	(46)	(139)	(139)
Defined benefit plans and other postretirement benefits:				
Net gain (loss) arising during the period	—	(4,115)	—	12,145
Prior service benefit arising during the period	—	—	—	1,782
Amortization of prior service benefit during the period	(667)	(979)	(2,001)	(2,846)
Amortization of net loss during the period	1,919	1,899	5,758	6,022
Other comprehensive income (loss) before income tax effect	1,206	(3,241)	3,618	16,964
Income tax effect	(382)	(383)	(1,147)	(1,148)
Other comprehensive income (loss)	824	(3,624)	2,471	15,816
Total comprehensive loss	\$(57,449)	\$(59,736)	\$(81,480)	\$(414)

See condensed notes to consolidated financial statements

CENTURY ALUMINUM COMPANY
CONSOLIDATED BALANCE SHEETS

(in thousands)

(Unaudited)

	September 30, 2016	December 31, 2015
ASSETS		
Cash and cash equivalents	\$ 117,593	\$ 115,393
Restricted cash	1,046	791
Accounts receivable - net	11,187	9,475
Due from affiliates	14,271	17,417
Inventories	233,288	231,872
Prepaid and other current assets	31,828	42,412
Assets held for sale	23,239	30,697
Total current assets	432,452	448,057
Property, plant and equipment - net	1,185,101	1,232,256
Other assets	71,163	72,155
TOTAL	\$ 1,688,716	\$ 1,752,468
LIABILITIES AND SHAREHOLDERS' EQUITY		
LIABILITIES:		
Accounts payable, trade	\$ 85,314	\$ 90,489
Due to affiliates	13,105	10,045
Accrued and other current liabilities	59,382	48,822
Accrued employee benefits costs	9,284	10,148
Industrial revenue bonds	7,815	7,815
Total current liabilities	174,900	167,319
Senior notes payable	247,590	247,278
Accrued pension benefits costs - less current portion	42,433	43,999
Accrued postretirement benefits costs - less current portion	125,490	125,999
Other liabilities	72,330	53,009
Deferred taxes	88,449	96,994
Total noncurrent liabilities	576,292	567,279
COMMITMENTS AND CONTINGENCIES (NOTE 11)		
SHAREHOLDERS' EQUITY:		
Preferred stock (Note 7)	1	1
Common stock (Note 7)	942	942
Additional paid-in capital	2,514,765	2,513,631
Treasury stock, at cost	(86,276)	(86,276)
Accumulated other comprehensive loss	(110,179)	(112,650)
Accumulated deficit	(1,381,729)	(1,297,778)
Total shareholders' equity	937,524	1,017,870
TOTAL	\$ 1,688,716	\$ 1,752,468

See condensed notes to consolidated financial statements

CENTURY ALUMINUM COMPANY
CONSOLIDATED STATEMENTS OF CASH FLOWS
(in thousands)
(Unaudited)

	Nine months ended September 30,	
	2016	2015
CASH FLOWS FROM OPERATING ACTIVITIES:		
Net loss	\$(83,951)	\$(16,230)
Adjustments to reconcile net loss to net cash provided by operating activities:		
Unrealized gain on fair value of contingent consideration	—	(18,337)
Unrealized gain on E.ON contingent obligation	(1,059)	(1,059)
Lower of cost or market inventory adjustment	1,499	31,013
Depreciation and amortization	63,306	55,815
Ravenswood impairment	3,830	30,850
Pension and other postretirement benefits	1,682	(298)
Deferred income taxes	(8,520)	1,215
Stock-based compensation	1,134	1,381
Equity in earnings of joint ventures	(891)	(2,069)
Change in operating assets and liabilities:		
Accounts receivable - net	(1,712)	69,055
Due from affiliates	3,146	2,406
Inventories	(1,265)	(46,392)
Prepaid and other current assets	9,016	3,435
Accounts payable, trade	(5,028)	(43,485)
Due to affiliates	4,628	11,395
Accrued and other current liabilities	4,769	(8,418)
Pension contribution - Mt. Holly	—	(34,595)
Ravenswood retiree legal settlement	23,000	—
Other - net	1,998	(3,173)
Net cash provided by operating activities	15,582	32,509
CASH FLOWS FROM INVESTING ACTIVITIES:		
Purchase of property, plant and equipment	(13,127)	(47,595)
Purchase of remaining interest in Mt. Holly smelter	—	11,313
Restricted and other cash deposits	(255)	(141)
Net cash used in investing activities	(13,382)	(36,423)
CASH FLOWS FROM FINANCING ACTIVITIES:		
Borrowings under revolving credit facilities	900	1,414
Repayments under revolving credit facilities	(900)	(1,414)
Repurchase of common stock	—	(36,352)
Net cash used in financing activities	—	(36,352)
CHANGE IN CASH AND CASH EQUIVALENTS	2,200	(40,266)
Cash and cash equivalents, beginning of period	115,393	163,242
Cash and cash equivalents, end of period	\$117,593	\$122,976

See condensed notes to consolidated financial statements

CENTURY ALUMINUM COMPANY

Condensed Notes to the Consolidated Financial Statements

Three and nine months ended September 30, 2016 and 2015

(amounts in thousands, except share and per share amounts)

(Unaudited)

1. General

The accompanying unaudited interim consolidated financial statements of Century Aluminum Company should be read in conjunction with the audited consolidated financial statements for the year ended December 31, 2015. In management's opinion, the unaudited interim consolidated financial statements reflect all adjustments, which are of a normal and recurring nature, that are necessary for a fair presentation of financial results for the interim periods presented. Operating results for the first nine months of 2016 are not necessarily indicative of the results that may be expected for the year ending December 31, 2016. Throughout this Form 10-Q, and unless expressly stated otherwise or as the context otherwise requires, "Century Aluminum," "Century," the "Company", "we," "us," "our" and "ours" refer to Century Aluminum Company and its consolidated subsidiaries.

2. Related party transactions

Our significant related party transactions occurring during the three and nine months ended September 30, 2016 and 2015 are described below. We believe that all of the transactions with our related parties were at prices that approximate market.

Glencore ownership

As of September 30, 2016, Glencore plc and its affiliates (together "Glencore") owned 42.9% of Century's outstanding common stock and all of our outstanding Series A Convertible Preferred stock resulting in 47.5% ownership in Century Aluminum.

Sales to Glencore

We are party to an agreement with Glencore pursuant to which we agreed to sell, and Glencore agreed to purchase, substantially all of our primary aluminum production in North America for 2015 and 2016 on a take-or-pay basis at prices determined by reference to the Midwest Transaction Price plus additional negotiated product premiums. The current term of the agreement continues through December 31, 2016. In addition, we have agreed to sell approximately 24,500 tonnes of molten aluminum to Glencore during 2017 at prices based on the Midwest Transaction Price.

We sell primary aluminum produced at our Grundartangi, Iceland smelter ("Grundartangi") under a long-term sales contract through 2017 with Glencore at prices based on the London Metal Exchange ("LME") price for primary aluminum plus the European Duty Paid premium and any applicable product premiums. We also received tolling fees from Glencore under a tolling agreement that provided for delivery of primary aluminum produced at our Grundartangi facility through June 2016. The fee paid by Glencore under this tolling agreement was based on the LME price for primary aluminum plus a portion of the European Duty Paid premium.

Glencore purchases the aluminum we produce for resale.

Purchases from Glencore

We purchase alumina from Glencore under a long-term supply agreement and on a spot basis. Pursuant to our current agreement, Glencore has agreed to supply us with alumina through 2017 at prices indexed to the LME price of primary aluminum. In 2015 and 2016, upon mutual agreement, all of our purchases from Glencore under this agreement were priced based on a published alumina index.

Financial contracts with Glencore

During 2016, we entered into certain financial contracts with Glencore. Refer to Note 15 Derivative instruments to the consolidated financial statements included herein. Settlements of financial contracts with Glencore are not material to the consolidated financial statements for all periods presented.

CENTURY ALUMINUM COMPANY

Condensed Notes to the Consolidated Financial Statements (continued)

(amounts in thousands, except share and per share amounts)

(Unaudited)

Transactions with Baise Haohai Carbon Co., Ltd. ("BHH")

We own a 40% stake in BHH, a joint venture that owns a carbon anode and cathode facility located in the Guangxi Zhuang Autonomous Region of south China. We purchase carbon anodes from BHH. In the fourth quarter of 2015, we completed the construction of a second furnace at our carbon anode facility in Vlissingen, Netherlands. This investment increased our capacity to produce carbon anodes and significantly reduced the quantity of carbon anodes that we source from BHH. As a result, in the fourth quarter of 2015, we made the decision to pursue an exit from our investment in BHH and recorded an \$11,584 impairment loss.

Summary

A summary of the aforementioned significant related party transactions for the three and nine months ended September 30, 2016 and 2015 is as follows:

	Three months ended September 30,		Nine months ended September 30,	
	2016	2015	2016	2015
Net sales to Glencore	\$301,111	\$428,018	\$871,771	\$1,517,428
Purchases from Glencore	62,317	86,664	156,507	328,120
Purchases from BHH	2,568	13,515	7,666	41,768

3. Ravenswood impairment

On July 27, 2015, we announced the immediate and permanent closure of our Ravenswood, West Virginia aluminum smelter ("Ravenswood"). Ravenswood has been idled since February 2009. The decision to permanently close Ravenswood was based on the inability to secure a competitive power contract for the smelter, compounded by challenging aluminum market conditions largely driven by increased exports of aluminum from China.

At June 30, 2015, we recorded an impairment charge of \$30,850 related to Ravenswood. Based on a tentative agreement for the sale of the assets, we recorded an additional impairment charge of \$3,830, included in Ravenswood charges in the consolidated statements of operations for the quarter ended September 30, 2016.

We classified the estimated salvage value of the property, plant and equipment within Level 3 of the fair value hierarchy as its fair value was determined based on recent comparable transactions with inputs that are not readily observable in the market.

4. Business acquisitions

Acquisition of Mt. Holly aluminum smelter

On October 23, 2014, our wholly-owned subsidiary, Berkeley Aluminum Inc. ("Berkeley") entered into a stock purchase agreement (the "Stock Purchase Agreement") with Alumax Inc. ("Alumax"), a wholly-owned subsidiary of Alcoa Inc. ("Alcoa"), pursuant to which Berkeley acquired all of the issued and outstanding shares of Alumax of South Carolina, Inc. ("Alumax of SC") and thereby acquired Alcoa's 50.3% stake in Mt. Holly. Berkeley had previously owned 49.7% of Mt. Holly. Immediately following the consummation of the transaction on December 1, 2014, Berkeley merged with and into Alumax of SC with Alumax of SC surviving and changing its name to Century Aluminum of South Carolina, Inc. ("CASC"). Following the consummation of the transaction, CASC owned 100% of Mt. Holly. Mt. Holly, located in Goose Creek, South Carolina, employed approximately 600 people and had an annual production capacity of 231,000 tonnes of primary aluminum as of the acquisition date.

Pursuant to the terms of the Stock Purchase Agreement, Berkeley acquired all of the issued and outstanding shares of capital stock of Alumax of SC for \$67,500 in cash subject to a contingent earn-out payment, working capital and other similar adjustments. The acquisition was funded with available cash on hand.

CENTURY ALUMINUM COMPANY

Condensed Notes to the Consolidated Financial Statements (continued)

(amounts in thousands, except share and per share amounts)

(Unaudited)

We accounted for this transaction as a step acquisition and this resulted in a non-cash pre-tax gain of \$15,955 at closing. Acquisition-related costs for Mt. Holly of \$1,539 were expensed to selling, general and administrative expenses in the period that they were incurred.

The following table summarizes all of the elements of purchase consideration for the transaction as of December 1, 2014.

Purchase price	\$67,500
Contingent consideration	13,780
Economic, working capital and other closing adjustments	(13,513)
Total consideration	\$67,767

We received payments from Alcoa of \$12,500 in settlement of the contingent consideration in March 2016, \$11,313 for economic and working capital adjustments in April 2015 and \$2,400 at closing which was primarily for post-employment benefits.

We recognized gains on contingent consideration of \$1,523 and \$18,337, respectively, during the three and nine month periods ended September 30, 2015.

The total net cash consideration paid to Alcoa after final resolution of all post-closing adjustments, including the earn-out provision, was \$41,487.

5. Fair value measurements

The following section describes the valuation methodology used to measure our financial assets and liabilities that were accounted for at fair value and are categorized based on the fair value hierarchy described in Accounting Standards Codification ("ASC") 820, "Fair Value Measurements and Disclosures."

Overview of Century's valuation methodology

	Level	Significant inputs
Cash equivalents	1	Quoted market prices
Trust assets (1)	1	Quoted market prices
Surety bonds	1	Quoted market prices
Forward sales contracts	2	Quoted LME forward market
Fixed for floating swaps	3	Quoted LME forward market, management's estimates of future U.S. Midwest premium
E.ON contingent obligation	3	Quoted LME forward market, management's estimates of the LME forward market prices for periods beyond the quoted periods and management's estimate of future level of operations
(1)		Trust assets are currently invested in money market funds. These trust assets are held to fund the non-qualified supplemental executive pension benefit obligations for certain of our officers. The trust has sole authority to invest the funds in secure interest producing investments consisting of short-term securities issued or guaranteed by the United States government or cash and cash equivalents.

Our fair value measurements include the consideration of market risks that other market participants might consider in pricing the particular asset or liability, specifically non-performance risk and counterparty credit risk. Considerations of the non-performance risk and counterparty credit risk are used to establish the appropriate risk-adjusted discount rates used in our fair value measurements.

CENTURY ALUMINUM COMPANY

Condensed Notes to the Consolidated Financial Statements (continued)

(amounts in thousands, except share and per share amounts)

(Unaudited)

Financial assets and liabilities are classified in their entirety based on the lowest level of input that is significant to the fair value measurement. Our assessment of the significance of a particular input to the fair value measurement requires judgment, and may affect the valuation of fair value assets and liabilities and the placement within the fair value hierarchy levels. There were no transfers between Level 1 and 2 during the periods presented. There were no transfers into or out of Level 3 during the periods presented. It is our policy to recognize transfers into and transfers out of Level 3 as of the date of the event or change in circumstances that caused the transfer.

The following table sets forth our financial assets and liabilities that were accounted for at fair value on a recurring basis by the level of input within the ASC 820 fair value hierarchy.

	Recurring Fair Value Measurements As of September 30, 2016			
	Level 1	Level 2	Level 3	Total
ASSETS:				
Cash equivalents	\$104,730	\$—	\$—	\$104,730
Trust assets	3,664	—	—	3,664
Surety bonds	1,874	—	—	1,874
Derivative contracts	—	330	574	904
TOTAL	\$110,268	\$330	\$574	\$111,172

LIABILITIES:

E.ON contingent obligation - net	\$—	\$—	\$—	\$—
Derivative contracts	—	—	574	574
TOTAL	\$—	\$—	\$574	\$574

Recurring Fair Value Measurements As of December 31, 2015

	Recurring Fair Value Measurements As of December 31, 2015			
	Level 1	Level 2	Level 3	Total
ASSETS:				
Cash equivalents	\$102,675	\$—	\$—	\$102,675
Trust assets	5,226	—	—	5,226
Surety bonds	1,870	—	—	1,870
TOTAL	\$109,771	\$—	\$—	\$109,771
LIABILITIES:				
E.ON contingent obligation - net	\$—	\$—	\$—	\$—
TOTAL	\$—	\$—	\$—	\$—

CENTURY ALUMINUM COMPANY

Condensed Notes to the Consolidated Financial Statements (continued)

(amounts in thousands, except share and per share amounts)

(Unaudited)

6. Earnings (loss) per share

Basic earnings (loss) per share ("EPS") amounts are calculated by dividing net income (loss) allocated to common stockholders by the weighted average number of common shares outstanding. Diluted EPS amounts assume the issuance of common stock for all potentially dilutive common shares.

In periods when we report a net loss, all share-based compensation awards are excluded from the calculation of diluted weighted average shares outstanding because of their antidilutive effect on loss per share. In periods when we report net income, certain share-based compensation awards may be excluded from the calculation of diluted EPS if the exercise price was greater than the average market price of the underlying common stock.

The following table shows the basic and diluted earnings (loss) per share for the three and nine months ended September 30, 2016 and 2015:

	For the three months ended September 30,					
	2016			2015		
	Loss	Shares (000)	Per-Share	Loss	Shares (000)	Per-Share
Net loss	\$(58,273)			\$(56,112)		
Amount allocated to common stockholders	100.00	%		100.00	%	
Basic and diluted EPS:						
Net loss allocated to common stockholders	\$(58,273)	87,076	\$(0.67)	\$(56,112)	86,907	\$(0.65)

	For the nine months ended September 30,					
	2016			2015		
	Loss	Shares (000)	Per-Share	Income	Shares (000)	Per-Share
Net loss	\$(83,951)			\$(16,230)		
Amount allocated to common stockholders	100.00	%		100.00	%	