STEPAN CO
Form 10-Q
August 03, 2012

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

(MARK ONE)

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

FOR THE QUARTERLY PERIOD ENDED JUNE 30, 2012

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

FOR THE TRANSITION PERIOD FROM TO

1-4462

Commission File Number

STEPAN COMPANY

(Exact name of registrant as specified in its charter)

Delaware	**36-1823834**
(State or other jurisdiction of	**(I.R.S. Employer**
incorporation or organization)	**Identification Number)**

Edens and Winnetka Road, Northfield, Illinois 60093

(Address of principal executive offices)

Registrant s telephone number (847) 446-7500

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 x 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 (§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 x 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	x
Non-accelerated filer	¨	Smaller reporting company	¨

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

Indicate the number of shares outstanding of each of the issuer s classes of common stock, as of the latest practicable date.

Class	**Outstanding at July 31, 2012**
Common Stock, $1 par value	10,369,660 Shares

Part I **FINANCIAL INFORMATION**

Item 1 - Financial Statements

STEPAN COMPANY

CONDENSED CONSOLIDATED STATEMENTS OF INCOME

Unaudited

(In thousands, except per share amounts)	Three Months Ended June 30 2012	Three Months Ended June 30 2011	Six Months Ended June 30 2012	Six Months Ended June 30 2011
Net Sales	$ 470,231	$ 476,989	$ 935,500	$ 899,587
Cost of Sales	396,835	407,404	785,320	768,216
Gross Profit	73,396	69,585	150,180	131,371
Operating Expenses:				
Selling	12,985	12,171	26,636	23,001
Administrative	14,086	12,680	31,038	23,554
Research, development and technical services	11,504	10,656	22,285	20,887
	38,575	35,507	79,959	67,442
Operating Income	34,821	34,078	70,221	63,929
Other Income (Expense):				
Interest, net	(2,086)	(2,194)	(4,690)	(4,257)
Loss from equity in joint ventures	(1,300)	(805)	(2,441)	(1,770)
Other, net (Note 12)	83	253	1,148	565
	(3,303)	(2,746)	(5,983)	(5,462)
Income Before Provision for Income Taxes	31,518	31,332	64,238	58,467
Provision for Income Taxes	10,007	10,326	20,363	18,645
Net Income	21,511	21,006	43,875	39,822
Net Income Attributable to Noncontrolling Interests (Note 2)	(86)	(139)	(148)	(194)
Net Income Attributable to Stepan Company	$ 21,425	$ 20,867	$ 43,727	$ 39,628
Net Income Per Common Share Attributable to Stepan Company (Note 9):				
Basic	$ 2.01	$ 2.00	$ 4.12	$ 3.80
Diluted	$ 1.89	$ 1.87	$ 3.85	$ 3.55
Shares Used to Compute Net Income Per Common Share Attributable to Stepan Company (Note 9):				
Basic	10,550	10,345	10,537	10,335

Diluted		11,357		11,178		11,345		11,175
Dividends Declared Per Common Share	$	0.28	$	0.26	$	0.56	$	0.52

The accompanying Notes to Condensed Consolidated Financial Statements are an integral part of these financial statements.

STEPAN COMPANY

CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME

Unaudited

(In thousands)	Three Months Ended June 30		Six Months Ended June 30	
	2012	2011	2012	2011
Net income	$ 21,511	$ 21,006	$ 43,875	$ 39,822
Other comprehensive income (loss):				
Foreign currency translation adjustments	(10,554)	3,964	(2,020)	10,081
Pension liability adjustment, net of tax	582	521	1,164	1,044
Derivative instrument activity, net of tax	(43)	315	64	389
Other comprehensive income (loss)	(10,015)	4,800	(792)	11,514
Comprehensive income	11,496	25,806	43,083	51,336
Less: Comprehensive income attributable to noncontrolling interests	(65)	(167)	(202)	(236)
Comprehensive income attributable to Stepan Company	$ 11,431	$ 25,639	$ 42,881	$ 51,100

The accompanying Notes to Condensed Consolidated Financial Statements are an integral part of these financial statements.

STEPAN COMPANY

CONDENSED CONSOLIDATED BALANCE SHEETS

Unaudited

(In thousands)	June 30, 2012	December 31, 2011
Assets		
Current Assets:		
Cash and cash equivalents	$ 69,523	$ 84,099
Receivables, net	278,184	260,784
Inventories (Note 6)	137,852	111,175
Deferred income taxes	9,055	8,769
Other current assets	16,183	14,915
Total current assets	510,797	479,742
Property, Plant and Equipment:		
Cost	1,152,600	1,119,897
Less: accumulated depreciation	756,661	735,914
Property, plant and equipment, net	395,939	383,983
Goodwill, net	7,038	7,000
Other intangible assets, net	9,940	11,181
Long-term investments (Note 3)	13,445	12,464
Other non-current assets	6,138	6,748
Total assets	$ 943,297	$ 901,118
Liabilities and Equity		
Current Liabilities:		
Current maturities of long-term debt (Note 11)	$ 33,294	$ 34,487
Accounts payable	140,604	137,764
Accrued liabilities	61,615	60,975
Total current liabilities	235,513	233,226
Deferred income taxes	9,990	8,644
Long-term debt, less current maturities (Note 11)	162,049	164,967
Other non-current liabilities	90,878	88,816
Commitments and Contingencies (Note 7)		
Equity:		
5-1/2% convertible preferred stock, cumulative, voting, without par value; authorized 2,000,000 shares; issued and outstanding 518,293 shares in 2012 and in 2011	12,957	12,957
Common stock, $1 par value; authorized 30,000,000 shares; Issued 11,831,942 shares in 2012 and 11,709,312 shares in 2011	11,832	11,709
Additional paid-in capital	101,564	94,932
Accumulated other comprehensive loss	(42,134)	(41,485)

Retained earnings	403,872	366,293
Less: Common treasury stock, at cost, 1,482,657 shares in 2012 and 1,462,980 shares in 2011	(44,932)	(43,195)
Total Stepan Company stockholders equity	443,159	401,211
Noncontrolling interests (Note 2)	1,708	4,254
Total equity	444,867	405,465
Total liabilities and equity	$ 943,297	$ 901,118

The accompanying Notes to Condensed Consolidated Financial Statements are an integral part of these financial statements.

STEPAN COMPANY

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

Unaudited

(In thousands)	Six Months Ended June 30 2012	2011
Cash Flows From Operating Activities		
Net income	$ 43,875	$ 39,822
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	25,217	23,007
Deferred compensation	4,957	(709)
Realized and unrealized gain on long-term investments	(1,010)	(438)
Stock-based compensation	1,591	1,777
Deferred income taxes	538	4,846
Other non-cash items	2,669	1,083
Changes in assets and liabilities:		
Receivables, net	(19,725)	(83,875)
Inventories	(27,978)	(55,088)
Other current assets	(1,150)	(3,586)
Accounts payable and accrued liabilities	12,303	55,151
Pension liabilities	(1,646)	(895)
Environmental and legal liabilities	(143)	(412)
Deferred revenues	(662)	(890)
Excess tax benefit from stock options and awards	(2,070)	(1,113)
Net Cash Provided By (Used In) Operating Activities	36,766	(21,320)
Cash Flows From Investing Activities		
Expenditures for property, plant and equipment	(40,798)	(40,400)
Business acquisition		(13,562)
Sale of mutual funds	537	1,613
Other, net	(1,662)	(2,136)
Net Cash Used In Investing Activities	(41,923)	(54,485)
Cash Flows From Financing Activities		
Revolving debt and bank overdrafts, net	(810)	9,738
Build-to-suit obligation buyout		(12,206)
Other debt repayments	(2,827)	(2,291)
Dividends paid	(6,148)	(5,638)
Company stock repurchased	(500)	(1,000)
Stock option exercises	2,320	889
Payment to noncontrolling interest (Note 13)	(2,000)	
Excess tax benefit from stock options and awards	2,070	1,113
Other, net	(1,256)	(1,265)
Net Cash Used In Financing Activities	(9,151)	(10,660)
Effect of Exchange Rate Changes on Cash	(268)	866
Net Decrease in Cash and Cash Equivalents	(14,576)	(85,599)
Cash and Cash Equivalents at Beginning of Period	84,099	111,198

Cash and Cash Equivalents at End of Period	$ 69,523	$ 25,599
Supplemental Cash Flow Information		
Cash payments of income taxes, net of refunds	$ 15,121	$ 9,832
Cash payments of interest	$ 5,216	$ 4,122

The accompanying Notes to Condensed Consolidated Financial Statements are an integral part of these financial statements.

STEPAN COMPANY

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

June 30, 2012

Unaudited

1. CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

The condensed consolidated financial statements included herein have been prepared by Stepan Company (Company), without audit, pursuant to the rules and regulations of the Securities and Exchange Commission (SEC). Certain information and footnote disclosures normally included in financial statements prepared in accordance with accounting principles generally accepted in the United States of America have been condensed or omitted pursuant to such rules and regulations, although management believes that the disclosures are adequate and make the information presented not misleading. In the opinion of management, all adjustments, consisting only of normal recurring accruals, necessary to present fairly the Company s financial position as of June 30, 2012 and its results of operations for the three and six months ended June 30, 2012 and 2011, and cash flows for the six months ended June 30, 2012 and 2011, have been included. These financial statements and related footnotes should be read in conjunction with the financial statements and related footnotes included in the Company s 2011 Form 10-K.

2. RECONCILIATIONS OF EQUITY

Below are reconciliations of total equity, Company equity and equity attributable to the noncontrolling interests for the six months ended June 30, 2012 and 2011:

(In thousands)	Total Equity	Stepan Company Equity	Noncontrolling Interests Equity (3)
Balance at January 1, 2012	$ 405,465	$ 401,211	$ 4,254
Net income	43,875	43,727	148
Purchase of remaining interest in Stepan Philippines, Inc. from noncontrolling interest	(2,000)	748	(2,748)
Dividends	(6,148)	(6,148)	
Common stock purchases (1)	(1,761)	(1,761)	
Stock option exercises	2,320	2,320	
Defined benefit pension adjustments, net of tax	1,164	1,164	
Translation adjustments	(2,020)	(2,074)	54
Derivative instrument activity, net of tax	64	64	
Other (2)	3,908	3,908	
Balance at June 30, 2012	$ 444,867	$ 443,159	$ 1,708

(In thousands)	Total Equity	Stepan Company Equity	Noncontrolling Interests Equity [3]
Balance at January 1, 2011	$ 353,071	$ 349,491	$ 3,580
Net income	39,822	39,628	194
Dividends	(5,638)	(5,638)	
Common stock purchases [1]	(2,274)	(2,274)	
Stock option exercises	889	889	
Defined benefit pension adjustments, net of tax	1,044	1,044	
Translation adjustments	10,081	10,039	42
Derivative instrument gain, net of tax	389	389	
Other [2]	3,603	3,603	
Balance at June 30, 2011	$ 400,987	$ 397,171	$ 3,816

(1) Includes the value of Company shares purchased in the open market and the value of Company common shares tendered by employees to settle minimum statutory withholding taxes related to the receipt of performance awards and deferred compensation distributions.

(2) Primarily comprised of activity related to stock-based compensation, deferred compensation and excess tax benefits.

(3) Includes partners noncontrolling interests in the Company s China and Philippines joint ventures. See Note 13 for information regarding the Company s purchase of the remaining ownership interest in the Philippine joint venture.

3. FINANCIAL INSTRUMENTS

The following are the financial instruments held by the Company at June 30, 2012 and December 31, 2011, and descriptions of the methods and assumptions used to estimate the instruments fair values:

Cash and cash equivalents

Carrying value approximates fair value because of the short maturity of the instruments.

Derivative assets and liabilities

Derivative assets and liabilities relate to the foreign currency exchange and interest rate contracts discussed in Note 4. Fair value and carrying value were the same because the contracts were recorded at fair value. The fair values of the foreign currency contracts were calculated as the difference between the applicable forward foreign exchange rates at the reporting date and the contracted foreign exchange rates multiplied by the contracted notional amounts. The fair values of the interest rate swaps were calculated as the difference between the contracted swap rate and the current market replacement swap rate multiplied by the present value of one basis point for the notional amount of the contract. See the table that follows these financial instrument descriptions for the reported fair values of derivative assets and liabilities.

Long-term investments

Long-term investments are the mutual fund assets the Company holds to fund a portion of its deferred compensation liabilities and all of its non-qualified supplemental executive defined contribution obligations (see the defined contribution plans section of Note 8). Fair value and carrying value were the same because the mutual fund assets were recorded at fair value in accordance with the fair value option rules set forth in the Financial Accounting Standards Board (FASB) Accounting Standards Codification (ASC) Topic 825, *Financial Instruments*. Fair values for the mutual funds were calculated using the published market price per unit at the reporting date multiplied by the number of units held at the reporting date. See the table that follows these financial instrument descriptions for the reported fair value of long-term investments.

Debt obligations

The fair value of debt with original maturities greater than one year comprised the combined present values of scheduled principal and interest payments for each of the various loans, individually discounted at rates equivalent to those which could be obtained by the Company for new debt issues with durations equal to the average life to maturity of each loan. The fair values of the remaining Company debt obligations approximated their carrying values due to the short-term nature of the debt. The Company s fair value measurements for debt fall in level 2 of the fair value hierarchy.

At June 30, 2012, and December 31, 2011, the fair value of debt and the related carrying values, including current maturities, were as follows:

(In thousands)	June 30, 2012	December 31, 2011
Fair value	$ 206,391	$ 206,789
Carrying value	195,343	199,454

The following tables present financial assets and liabilities measured on a recurring basis at fair value as of June 30, 2012, and December 31, 2011, and the level within the fair value hierarchy in which the fair value measurements fall:

(In thousands)	June 2012	Level 1	Level 2	Level 3
Mutual fund assets	$ 13,445	$ 13,445	$	$
Derivative assets:				
Foreign currency contracts	30		30	
Total assets at fair value	$ 13,475	$ 13,445	$ 30	$
Derivative liabilities:				
Foreign currency contracts	$ 3	$	$ 3	$
Interest rate contracts	55		55	
Total liabilities at fair value	$ 58	$	$ 58	$

(In thousands)	December 2011	Level 1	Level 2	Level 3
Mutual fund assets	$ 12,464	$ 12,464	$	$
Derivative assets:				
Foreign currency contracts	100		100	
Total assets at fair value	$ 12,564	$ 12,464	$ 100	$
Derivative liabilities:				
Foreign currency contracts	$ 52	$	$ 52	$
Interest rate contracts	36		36	
Total liabilities at fair value	$ 88	$	$ 88	$

4. DERIVATIVE INSTRUMENTS

The Company is exposed to certain risks relating to its ongoing business operations. The primary risk managed by the use of derivative instruments is foreign currency exchange risk. The Company holds forward foreign currency exchange contracts that are not designated as any type of accounting hedge as defined by U.S. generally accepted accounting principles (although they are effectively economic hedges). The Company uses these contracts to manage its exposure to exchange rate fluctuations on certain Company subsidiary accounts receivable, accounts payable and other obligation balances that are denominated in currencies other than the entities functional currencies. The forward foreign exchange contracts are recognized on the balance sheet as either an asset or a liability measured at fair value. Gains and losses arising from recording the foreign exchange contracts at fair value are reported in earnings as offsets to the losses and gains reported in earnings arising from the re-measurement of the receivable and payable balances into the applicable functional currencies. At June 30, 2012, the Company had open forward foreign currency exchange contracts, with settlement dates of about one month, to buy or sell foreign currencies with a U.S. dollar equivalent of $15,458,000. At

December 31, 2011, the Company had open forward foreign currency exchange contracts, all with settlement dates of about one month, to buy or sell foreign currencies with a U.S. dollar equivalent of $26,627,000.

The Company also holds forward foreign currency exchange contracts that are designated as a cash flow hedge. The Company uses these contracts to manage the risks and related cash flow variability resulting from exposure to exchange rate fluctuations on forecasted progress payments related to a construction project undertaken in Singapore. The progress payments are denominated in a currency other than the Singapore location s functional currency. The latest date through which the Company expects to hedge its exposure to the variability in cash flows for the progress payments is December 31, 2013. The forward foreign exchange contracts are recognized on the balance sheet as either an asset or a liability measured at fair value. Period-to-period changes in the fair value of the hedging instruments are recognized as gains or losses in other comprehensive income, to the extent effective. Once the constructed asset is complete and placed into service, the accumulated gains or losses will be reclassified out of accumulated other comprehensive income (AOCI) into earnings in the periods over which the asset is being depreciated. The amount in AOCI at June 30, 2012, that is expected to be reclassified into earnings in the next 12 months is insignificant. The Company had open forward foreign currency exchange contracts designated as cash flow hedges with U.S. dollar equivalent amounts of $1,508,000 and $5,266,000 at June 30, 2012, and December 31, 2011, respectively.

The Company is exposed to volatility in short-term interest rates and mitigates certain portions of that risk by using interest rate swaps. The interest rate swaps are recognized on the balance sheet as either an asset or a liability measured at fair value. The Company held interest rate swap contracts with notional values of $3,229,000 at June 30, 2012, and $3,694,000 at December 31, 2011, which were designated as cash flow hedges. Period-to-period changes in the fair value of interest rate swap contracts are recognized as gains or losses in other comprehensive income, to the extent effective. As each interest rate swap hedge contract is settled, the corresponding gain or loss is reclassified out of AOCI into earnings in that settlement period. The latest date through which the Company expects to hedge its exposure to the volatility of short-term interest rates is June 30, 2014.

The fair values of the derivative instruments held by the Company on June 30, 2012, and December 31, 2011, and derivative instrument gains and losses and amounts reclassified out of AOCI into earnings for the three and six month periods ended June 30, 2012 and 2011, were immaterial.

5. STOCK-BASED COMPENSATION

On June 30, 2012, the Company had stock options outstanding under its 2000 Stock Option Plan, stock options and stock awards outstanding under its 2006 Incentive Compensation Plan and stock options, stock awards and stock appreciation rights (SARs) outstanding under its 2011 Incentive Compensation Plan. SARs, which were granted for the first time in 2012, cliff vest after two years of continuous service, settle in cash and expire ten years from the grant date. Because SARs are cash-settled, they are accounted for as liabilities that must be re-measured at fair value at the end of every reporting period until settlement. The Company uses the Black-Scholes option pricing model for determining the fair value of SARs. Compensation expense for each reporting period is based on the period-to-period change (or portion of the change, depending on the proportion of the vesting period that has been completed at the reporting date) in the fair value of the SARs

Compensation expense charged against income for all stock options, stock awards and SARs was as follows:

(In thousands)

Three Months Ended June 30		Six Months Ended June 30	
2012	2011	2012	2011
$ 963	$ 928	$ 1,591	$ 1,777

Unrecognized compensation costs for stock options, stock awards and SARs was as follows:

(In thousands)

	June 30, 2012	December 31, 2011
Stock options	$ 1,269	$ 974
Stock awards	3,220	2,109
SARs	910	

The increase in unrecognized compensation costs for stock options, SARs and stock awards reflected the first quarter 2012 grants of 32,623 stock options, 29,729 stock awards and 32,623 SARs. The unrecognized compensation costs at June 30, 2012, are expected to be recognized over weighted-average periods of 1.2 years, 2.1 years and 1.6 years for stock options, stock awards and SARs, respectively.

6. INVENTORIES

The composition of inventories was as follows:

(In thousands)	June 30, 2012	December 31, 2011
Finished products	$ 88,586	$ 73,076
Raw materials	49,266	38,099
Total inventories	$ 137,852	$ 111,175

Inventories are primarily priced using the last-in, first-out inventory valuation method. If the first-in, first-out inventory valuation method had been used for all inventories, inventory balances would have been approximately $42,614,000 and $43,954,000 higher than reported at June 30, 2012, and December 31, 2011, respectively.

7. CONTINGENCIES

There are a variety of legal proceedings pending or threatened against the Company. Some of these proceedings may result in fines, penalties, judgments or costs being assessed against the Company at some future time. The Company s operations are subject to extensive local, state and federal regulations, including the U.S. Comprehensive Environmental Response, Compensation and Liability Act of 1980 (CERCLA) and the Superfund amendments of 1986 (Superfund). Over the years, the Company has received requests for information related to or has been named by the government as a potentially responsible party (PRP) at a number of waste disposal sites where clean up costs have been or may be incurred under CERCLA and similar state statutes. In addition, damages are being claimed against the Company in general liability actions for alleged personal injury or property damage in the case of some disposal and plant sites. The Company believes that it has made adequate provisions for the costs it may incur with respect to these sites.

At June 30, 2012, the Company has estimated a range of possible environmental and legal losses of $9.1 million to $28.9 million. At June 30, 2012, and December 31, 2011, the Company s accrued liability for such losses, which represented the Company s best estimate within the estimated range of possible environmental and legal losses, was $14.9 million and $14.6 million, respectively. During the first six months of 2012 cash outlays related to legal and environmental matters approximated $1.5 million compared to $2.7 million in the first six months of 2011.

For certain sites, the Company has responded to information requests made by federal, state or local government agencies but has received no response confirming or denying the Company s stated positions. As such, estimates of the total costs, or range of possible costs, of remediation, if any, or the Company s share of such costs, if any, cannot be determined with respect to these sites. Consequently, the Company is unable to predict the effect thereof on the Company s financial position, cash flows and results of operations. Given the information available, management believes the Company has no liability at these sites. However, in the event of one or more adverse determinations with respect to such sites in any annual or interim period, the effect on the Company s cash flows and results of operations for those periods could be material. Based upon the Company s present knowledge with respect to its involvement at these sites, the possibility of other viable entities responsibilities for cleanup, and the extended period over which any costs would be incurred, the Company believes that these matters, individually and in the aggregate, will not have a material effect on the Company s financial position.

Following are summaries of the material contingencies at June 30, 2012:

Maywood, New Jersey Site

The Company s property in Maywood, New Jersey, and property formerly owned by the Company adjacent to its current site and other nearby properties (Maywood site) were listed on the National Priorities List in September 1993 pursuant to the provisions of CERCLA because of certain alleged chemical contamination. Pursuant to an Administrative Order on Consent entered into between USEPA and the Company for property formerly owned by the Company and the issuance of an order by USEPA to the Company for property currently owned by the Company, the Company has completed various Remedial Investigation Feasibility Studies (RI/FS) and is awaiting the issuance of a Record of Decision (ROD) from USEPA.

The Company believes its recorded liability for claims associated with the remediation of chemical contamination at the Maywood site is adequate. However, depending on the results of the ongoing discussions with USEPA, the final cost of such remediation could differ from the current estimates.

In addition, under the terms of a settlement agreement reached on November 12, 2004, the United States Department of Justice and the Company agreed to fulfill the terms of a Cooperative Agreement reached in 1985 under which the United States will take title to and responsibility for radioactive waste removal at the Maywood site, including past and future remediation costs incurred by the United States. As such, the Company recorded no liability related to this settlement agreement.

D Imperio Property Site

During the mid-1970 s, Jerome Lightman and the Lightman Drum Company disposed of hazardous substances at several sites in New Jersey. The Company was named as a potentially responsible party (PRP) in the case *United States v. Lightman* (1:92-cv-4710 D.N.J.), which involved the D Imperio Property Site located in New Jersey. In 2007, the Company reached an agreement with respect to the past costs and future allocation percentage in said litigation for costs related to the D Imperio site, including costs to comply with USEPA s Unilateral Administrative Orders. The resolution of the Company s liability for this litigation did not have a material impact on the financial position, results of operations or cash flows of the Company. In the first quarter of 2012, the PRPs approved certain changes to remediation cost estimates, which were considered in the Company s determination of its range of estimated possible losses and liability balance. The changes in range of possible losses and liability balance were immaterial.

Remediation work is continuing at this site. Based on current information, the Company believes that its recorded liability for claims associated with the D Imperio site is adequate. However, actual costs could differ from current estimates.

Wilmington Site

The Company is currently contractually obligated to contribute to the response costs associated with the Company s formerly-owned site at 51 Eames Street, Wilmington, Massachusetts. Remediation at this site is being managed by its current owner to whom the Company sold the property in 1980. Under the agreement, once total site remediation costs exceed certain levels, the Company is obligated to contribute up to five percent of future response costs associated with this site with no limitation on the ultimate amount of contributions. To date, the Company has paid the current owner $2.0 million for the Company s portion of environmental response costs through the first quarter of 2012 (the current owner of the site bills the Company one calendar quarter in arrears). The Company has recorded a liability for its portion of the estimated remediation costs for the site. Depending on the ultimate cost of the remediation at this site, the amount for which the Company is liable could differ from the current estimates.

The Company and other prior owners also entered into an agreement in April 2004 waiving certain statute of limitations defenses for claims which may be filed by the Town of Wilmington, Massachusetts, in connection with this site. While the Company has denied any liability for any such claims, the Company agreed to this waiver while the parties continue to discuss the resolution of any potential claim which may be filed.

The Company believes that based on current information its recorded liability for the claims related to this site is adequate. However, actual costs could differ from current estimates.

8. POSTRETIREMENT BENEFIT PLANS

Defined Benefit Pension Plans

The Company sponsors various funded qualified and unfunded non-qualified defined benefit pension plans, the most significant of which cover employees in the U.S. and U.K. locations. The U.S. and U.K. defined benefit pension plans are frozen and service benefits are no longer being accrued.

Components of Net Periodic Benefit Cost

	UNITED STATES			
(In thousands)	Three Months Ended June 30		Six Months Ended June 30	
	2012	2011	2012	2011
Interest cost	$ 1,735	$ 1,761	$ 3,471	$ 3,523
Expected return on plan assets	(2,103)	(2,013)	(4,205)	(4,025)
Amortization of net loss	932	786	1,863	1,571
Net periodic benefit cost	$ 564	$ 534	$ 1,129	$ 1,069

	UNITED KINGDOM			
(In thousands)	Three Months Ended June 30		Six Months Ended June 30	
	2012	2011	2012	2011
Interest cost	$ 210	$ 279	$ 419	$ 555
Expected return on plan assets	(221)	(264)	(441)	(525)
Amortization of net loss	11	52	22	103
Net periodic benefit cost	$	$ 67	$	$ 133

Employer Contributions

U.S. Plans

The Company expects to contribute approximately $6,698,000 to its U.S. qualified defined benefit pension plans in 2012 and to pay $268,000 in 2012 related to its unfunded non-qualified plans. As of June 30, 2012, $2,120,000 had been contributed to the qualified plans and $152,000 had been paid related to the non-qualified plans.

U.K. Plan

The Company s United Kingdom subsidiary expects to contribute approximately $940,000 to its defined benefit pension plan in 2012. As of June 30, 2012, $507,000 had been contributed to the plan.

Defined Contribution Plans

The Company sponsors retirement savings defined contribution plans that cover U.S. and U.K. employees. The Company also sponsors a qualified profit sharing plan for its U.S. employees. The retirement savings and profit sharing defined contribution plans include a qualified plan and a non-qualified supplemental executive plan.

Defined contribution plan expenses for the Company s retirement savings plan were $1,058,000 and $2,112,000, respectively, for the three and six months ended June 30, 2012, compared to $1,005,000 and $1,955,000, respectively, for three and six months ended June 30, 2011.

Expenses related to the Company s profit sharing plan were $1,352,000 and $2,881,000, respectively, for the three and six months ended June 30, 20112 compared to $1,510,000 and $2,660,000, respectively, for the three and six months ended June 30, 2011.

In July 2011, the Company established a rabbi trust to fund the obligations of its previously unfunded non-qualified supplemental executive defined contribution plans (supplemental plans). The trust comprises various mutual fund investments selected by the participants of the supplemental plans. In accordance with the accounting guidance for rabbi trust arrangements, the assets of the trust and the obligations of the supplemental plans are reported on the Company s consolidated balance sheets. The Company elected the fair value option for the mutual fund investment assets so that offsetting changes in the mutual fund values and defined contribution plan obligations would be recorded in earnings in the same period. Therefore, the mutual funds are reported at fair value with any subsequent changes in fair value recorded in the statements of income. The liabilities related to the supplemental plans increase (i.e., supplemental plan expense is recognized) when the value of the trust assets appreciates and decrease when the value of the trust assets declines (i.e., supplemental plan income is recognized). At June 30, 2012, the balance of the trust assets was $1,429,000, which equaled the balance of the supplemental plan liabilities (see the long-term investments section in Note 3 for further information regarding the Company s mutual fund assets).

9. EARNINGS PER SHARE

Below is the computation of basic and diluted earnings per share for the three and six months ended June 30, 2012 and 2011.

(In thousands, except per share amounts)	Three Months Ended June 30 2012	Three Months Ended June 30 2011	Six Months Ended June 30 2012	Six Months Ended June 30 2011
Computation of Basic Earnings per Share				
Net income attributable to Stepan Company	$ 21,425	$ 20,867	$ 43,727	$ 39,628
Deduct dividends on preferred stock	177	179	355	358
Income applicable to common stock	$ 21,248	$ 20,688	$ 43,372	$ 39,270
Weighted-average number of common shares outstanding	10,550	10,345	10,537	10,335
Basic earnings per share	$ 2.01	$ 2.00	$ 4.12	$ 3.80
Computation of Diluted Earnings per Share				
Net income attributable to Stepan Company	$ 21,425	$ 20,867	$ 43,727	$ 39,628
Weighted-average number of shares outstanding	10,550	10,345	10,537	10,335
Add weighted-average net shares issuable from assumed exercise of options (under treasury stock method) [(1)]	212	237	213	244
Add weighted-average net shares related to unvested stock awards (under treasury stock method)	3	2	3	2
Add weighted-average shares issuable from assumed conversion of convertible preferred stock	592	594	592	594
Weighted-average shares applicable to diluted earnings	11,357	11,178	11,345	11,175
Diluted earnings per share	$ 1.89	$ 1.87	$ 3.85	$ 3.55

(1) Options to purchase 255 and 16,444 shares of common stock were not included in the computations of diluted earnings per share for the three and six months ended June 30, 2012, respectively. Options to purchase 63,167 and 61,516 shares of common stock were not included in the computations of diluted earnings per share for the three and six months ended June 30, 2011, respectively. The options exercise prices were greater than the average market price for the common stock and their effect would have been antidilutive.

10. SEGMENT REPORTING

The Company has three reportable segments: surfactants, polymers and specialty products. Segment operating results for the three and six months ended June 30, 2012 and 2011 are summarized below:

(In thousands)	Surfactants	Polymers	Specialty Products	Segment Totals
For the three months ended June 30, 2012				
Net sales	$ 335,114	$ 113,923	$ 21,194	$ 470,231
Operating income	31,024	11,775	3,395	46,194
For the three months ended June 30, 2011				
Net sales	$ 343,767	$ 120,854	$ 12,368	$ 476,989
Operating income	24,693	15,064	3,485	43,242
For the six months ended June 30, 2012				
Net sales	$ 682,270	$ 210,672	$ 42,558	$ 935,500
Operating income	64,016	23,526	7,290	94,832
For the six months ended June 30, 2011				
Net sales	$ 668,652	$ 207,253	$ 23,682	$ 899,587
Operating income	52,857	21,429	6,749	81,035

Below are reconciliations of segment operating income to consolidated income before income taxes:

(In thousands)	Three Months Ended June 30		Six Months Ended June 30	
	2012	2011	2012	2011
Operating income segment totals	$ 46,194	$ 43,242	$ 94,832	$ 81,035
Unallocated corporate expenses [1]	(11,373)	(9,164)	(24,611)	(17,106)
Total operating income	34,821	34,078	70,221	63,929
Interest expense, net	(2,086)	(2,194)	(4,690)	(4,257)
Loss from equity in joint ventures	(1,300)	(805)	(2,441)	(1,770)
Other, net	83	253	1,148	565
Consolidated income before income taxes	$ 31,518	$ 31,332	$ 64,238	$ 58,467

[1] Unallocated corporate expenses primarily comprise corporate administrative expenses (e.g., corporate finance, legal, human resources, information systems and deferred compensation) that are not included in segment operating income and not used to evaluate segment performance.

11. DEBT

At June 30, 2012, and December 31, 2011, debt comprised the following:

(In thousands)	Maturity Dates	June 30, 2012	December 31, 2011
Unsecured private placement notes			
4.86%	2017-2023	$ 65,000	$ 65,000
5.88%	2016-2022	40,000	40,000
5.69%	2012-2018	40,000	