

KMG CHEMICALS INC
Form 10-K
November 27, 2015

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

Form 10-K

(Mark one)

ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the fiscal year ended July 31, 2015

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: 001-35577

KMG CHEMICALS, INC.

(Exact name of registrant as specified in its charter)

Texas 75-2640529
(State or other jurisdiction of (I.R.S. Employer
incorporation or organization) Identification No.)
9555 W. Sam Houston Parkway S., Suite 600

Houston, Texas 77099

(Address of principal executive offices, including zip code)

(713) 600-3800

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(Registrant's telephone number, including area code)

SECURITIES REGISTERED PURSUANT TO SECTION 12(b) OF THE EXCHANGE ACT:

| Title of Each Class | Name of each Exchange on which Registered |
|-------------------------------|---|
| Common Stock, \$.01 par value | The New York Stock Exchange |

SECURITIES REGISTERED PURSUANT TO SECTION 12(g) OF THE EXCHANGE ACT:

| Title of Each Class | Name of each Exchange on which Registered |
|---------------------|---|
|---------------------|---|

None

Indicate by a check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. Yes No

Indicate by a check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act. Yes No

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes No

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulations S-T during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes No

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K.

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

Large Accelerated Filer Accelerated Filer

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

The aggregate market value of the voting and non-voting common equity held by non-affiliates of the registrant computed by reference to the closing price of \$20.92 on The New York Stock Exchange as of the last business day of

our most recently completed second fiscal quarter (January 30, 2015) was \$181.3 million.

As of November 23, 2015, there were 11,715,586 shares of the registrant's common stock, par value \$0.01, per share outstanding.

DOCUMENTS INCORPORATED BY REFERENCE

The proxy statement pertaining to our annual meeting of shareholders is incorporated by reference in Part III of this report.

PART I

ITEM 1. BUSINESS

Company Overview

We were incorporated in 1992 as a Texas corporation. We manufacture, formulate and globally distribute specialty chemicals through our three wholly owned subsidiaries, KMG Electronic Chemicals, Inc. (“KMG EC”), KMG-Bernuth, Inc. (“KMG Bernuth”) and KMG Val-Tex, LLC (“Val-Tex”). We grow primarily by purchasing product lines and businesses that operate in segments of the specialty chemical industry that:

- provide an opportunity to obtain a significant share of the market segment through further acquisitions and organic growth;
- are of a size that larger industry participants generally find too small to be attractive;
- have niche products with well-established and proven commercial uses;
- offer products that have moved well beyond their discovery phase and require little or no on-going research and development expenditures; and
- have significant barriers to entry.

We have acquired and currently operate businesses selling electronic chemicals, industrial wood treating chemicals and industrial valve lubricants and sealants. Our electronic chemicals segment provides high purity and ultra purity, wet process chemicals to the semiconductor industry, primarily to clean and etch silicon wafers in the production of semiconductors. We are the leading supplier of these wet process chemicals to the semiconductor industry in the United States and have a significant presence in Europe and Asia. Our wood treating chemicals, based on pentachlorophenol, or penta, are sold to industrial customers who use these preservatives primarily to extend the useful life of wood utility poles and cross-arms. We are the only supplier of penta in North America. Our industrial valve lubricants and sealants enable optimal valve operation and help prevent costly downtime at oil and gas storage facilities and pipelines. In addition, our lubricants and sealants provide important safety benefits along with preventing fugitive valve emissions. On January 16, 2015, we sold our creosote distribution business, part of our wood treating chemicals business, to Koppers Inc. pursuant to an asset purchase agreement.

For the twelve months ended July 31, 2015, we generated revenues of \$320.5 million and net income of \$12.1 million. On July 31, 2015, we had total long-term debt, net of current maturities, of \$53.0 million, cash and cash equivalents of \$7.5 million and total stockholders' equity of \$123.4 million.

Business Strategy

We seek to build long-term shareholder value through smart and efficient management of our existing operations, and through the rapid integration and optimization of acquired businesses. We favor businesses with stable markets, providing opportunities for harvesting operational synergies and enhancing margins. We focus on mature, specialty chemicals that large companies often ignore. Our actions are guided by our core values, which emphasize a passion for excellence, that we value our people, and that character and teamwork are critical. Three fundamental principles are at the core of our strategy:

- Operate . We seek to maximize cash flow by managing our plants with the best-available technology. We enhance the value of our operations by concentrating on customer satisfaction and efficient management of our resources to increase our profitability and cash flows.

Acquire . The cash flows generated by the businesses that we operate provide us with the ability to pursue further acquisitions in order to build on our existing segments, or to establish a new business platform for future growth. We employ a methodical approach to identify and evaluate potential acquisitions, only pursuing those that meet our financial and strategic criteria. Our discipline throughout the acquisition process maximizes the chances of long-term success.

·Integrate . We have consistently improved our ability as an organization to integrate progressively larger and more complex acquisitions. Our focus is to maintain reliable service to our customers during the integration period, identify and harvest the long-term synergies, and efficiently absorb acquired businesses into our operations. An effective integration strategy is an essential precondition for our operational success.

Business Segments

Electronic Chemicals. Our electronic chemicals business sells high purity and ultra purity wet process chemicals primarily to the semiconductor industry. Our electronic chemicals business accounted for 82.9% of our net sales in fiscal year 2015, 71.8% of our net sales in fiscal year 2014, and 63.0% in fiscal year 2013.

Our electronic chemicals are used to clean and etch silicon wafers in the production of semiconductors. The electronic chemicals business was acquired initially in December 2007 from Air Products and Chemicals, Inc. (“Air Products”), and expanded with our purchases in March 2010 and in May 2013 of similar businesses from General Chemical Performance Products LLP (“General Chemical”) and OM Group, Inc. (“OM Group”), respectively. Our products include sulfuric, phosphoric, and nitric and hydrofluoric acids, ammonium hydroxide, hydrogen peroxide, isopropyl alcohol, other specialty organic solvents and various blends of chemicals. We operate our electronic chemicals business through KMG EC in North America and through KMG Italia, S.r.l. (“KMG Italia”) and KMG Electronic Chemicals Luxembourg Holdings S.a.r.l. (“KMG Lux”) (and its subsidiaries) in Europe and Asia and have facilities in the United States, the United Kingdom, France, Italy and Singapore. Our customers rely on us to provide products with very low levels of contaminants and particles, in some cases at less than 100 parts per trillion levels. We purchase the needed chemicals from various suppliers, and in some cases we purify those chemicals further. We are responsible for product purity levels, for analytical testing, blending and packaging, and for distribution to our customers. Our products are sold in bulk and in containers, including bottles, drums and totes. This purification and distribution process is largely accomplished at our facilities in the United States, Europe and Singapore.

Other Chemicals. Our other chemicals segment includes our wood treating chemicals business and our industrial valve lubricants and sealants business. Our other chemicals segment constituted about 17.1% of our net sales in fiscal year 2015, 28.2% of our net sales in fiscal year 2014, and 37.0% in fiscal year 2013.

In our wood treating chemicals business, we supply penta to industrial customers who use this preservative to pressure treat wood products, primarily utility poles and cross-arms, to extend their useful life by protecting against insect damage and decay. Our penta products include solid blocks and concentrated solutions. We estimate that approximately two million treated utility poles are purchased each year by electric utility companies in the United States and that approximately 45% of those utility poles are treated with penta. We manufacture solid penta blocks at our facility in Matamoros, Mexico through KMG de Mexico (“KMEX”), a Mexican corporation which is a wholly owned subsidiary of KMG Bernuth. We sell solid penta to our customers, or dissolve it to make concentrated solutions of penta which are sold to customers from our Matamoros, Mexico and Tuscaloosa, Alabama facilities. We sell penta products in the United States, Canada and Mexico. We also sell hydrochloric acid, which is a byproduct of penta production for use in the steel and oil well service industries. On January 16, 2015, we sold our creosote distribution business, part of our wood treating chemicals business, to Koppers Inc. pursuant to an asset purchase agreement.

In our industrial valve lubricants and sealants business, we manufacture and distribute industrial sealants, lubricants and related equipment, primarily to the oil and gas storage, pipeline and gas distribution markets, through one facility in the United States. Our industrial valve lubricants and sealants enable optimal valve operation and help prevent costly downtime at oil and gas storage facilities and pipelines. In addition, they provide important safety benefits and prevent fugitive valve emissions. The industrial valve lubricants and sealants business was acquired on May 1, 2015 through the acquisition of Valves Incorporated of Texas, a privately held Texas corporation, pursuant to the terms of an agreement and plan of merger.

Suppliers

In our electronic chemicals segment we rely on a variety of suppliers for our raw materials, some of which we purchase on open account and others which we purchase under supply contracts. The number of suppliers is often limited, particularly as to the specific grade of raw material required by us to supply high purity and ultra purity products to our customers.

In our other chemicals segment, our wood treating chemicals and lubricants depend on outside suppliers for all of the raw materials needed to produce our products, and are subject to fluctuations in the price of those materials. The principal raw materials used are chlorine, phenol and co-solvent for our penta products and castor oil and fumed silica for our lubricants, each of which we purchase from a limited number of suppliers.

No assurance can be given that the loss of a supplier would not have a material adverse effect on our financial position or results of operations.

Customers

We sell our products to approximately 2,500 customers, almost 2,000 of which are customers of our industrial lubricants and sealants business. One of our electronic chemicals customers, Intel Corporation, accounted for 10% or more of our revenues in fiscal years 2015. Intel, along with one of our wood treating chemicals customers, Stella Jones Corporation, prior to the sale of our creosote distribution business, accounted for 10% or more of our revenues in fiscal years 2014 and 2013. No other customer accounted for 10% or more of our revenue in fiscal years 2015, 2014 or 2013. The loss of the Intel business would have a material adverse effect on sales of our electronic chemicals or wood treating chemicals businesses, respectively.

Marketing

We sell to our electronic chemicals customers through a combination of account managers and other sales personnel organized by geographic region. Our other chemicals are sold in the United States, Canada and Mexico through an internal sales force, distributors and independent agents, and sold internationally through distributors and agents.

Geographical Information

Sales made to customers in the United States were 57.2% of total revenues in fiscal year 2015, 60.2% in 2014 and 76.0% in 2013. Sales made outside of the United States were primarily electronic chemicals sold in Europe, Israel and Singapore. As of the end of fiscal year 2015, our property, plant and equipment were allocated, based on net book value, 56.3% in the United States and 43.7% elsewhere.

Competition

There are only a few firms competing with us in the sale of our electronic and wood treating chemical products. In our industrial valve lubricants and sealants business, we compete with many other firms. We compete by selling our products at competitive prices and maintaining a strong commitment to product quality and customer service and training.

In electronic chemicals in North America, we believe that we have a significant market share, and our principal competitors include Honeywell, Kanto Corporation and Avantor (formerly Mallinckrodt Baker). Internationally, we compete in Europe primarily with BASF, Technic and Honeywell, and in Asia with BASF, Kanto Corporation and others. We believe our market share in Europe is comparable to our competitors, and we do not participate materially in the market in Asia outside of Singapore.

In our electronic chemicals business, our customers demand that each of their suppliers and each product used to make their semiconductors go through a rigorous qualification process. Once a customer has qualified one or more suppliers and their products for one of its fabrication facilities, there is often reluctance to switch to suppliers who are not qualified.

The principal wood preserving chemicals for industrial applications are penta, creosote and chromated copper arsenate, or CCA. We supply customers in the United States with penta, but not creosote or CCA. We are the only manufacturer of penta based preservatives in North America. Penta is used primarily to treat electric, telephone and other utility poles, to protect them from insect damage and decay, extending their useful life by many years. We estimate that approximately two million treated utility poles are purchased each year by utility companies in the United States. Of that amount, we estimate approximately 45% are treated with penta. The remaining poles are treated primarily with creosote or CCA.

Our wood treating chemicals must be registered prior to sale under United States law. See “Environmental and Safety Matters — Licenses, Permits and Product Registrations.” As a condition to registration, any company wishing to manufacture and sell these products must provide substantial scientific research and testing data regarding the chemistry and toxicology of the products to the U.S. Environmental Protection Agency (“EPA”). This data must be generated by the applicant, or the applicant must purchase access to the information from other data providers. We believe that the cost of satisfying the data submission requirement serves as an impediment to the entry of new competitors, particularly those with lesser financial resources. While we have no reason to believe that the product registration requirement will be materially modified, we cannot give any assurances as to the effect of such a discontinuation or modification on our competitive position.

In our industrial lubricants business, competitors include about twenty-five other businesses that serve the oil and gas storage, pipeline and gas distribution markets, none of which have a dominant market position. Our principal

competitors include Flowserve Corporation and JetLube, Inc.

Employees

As of the end of fiscal year 2015, we had a total of 657 full-time employees. We employed 514 employees in our electronic chemicals segment, 96 employees in our other chemicals segment, and 47 employees in administration and corporate. Approximately 19.3% of our employees are represented by labor unions, workers councils or comparable organizations, particularly in Mexico and Europe.

Environmental and Safety Matters

Our operations are subject to extensive federal, state and local laws, regulations and ordinances in the United States and abroad relating to the protection of the environment and human health and to safety, including those pertaining to chemical manufacture and distribution, waste generation, storage and disposal, discharges to waterways, and air emissions and various other health and safety matters. Governmental authorities have the power to enforce compliance with their regulations, and violators may be subject to civil,

criminal and administrative penalties, injunctions or both. We devote significant financial resources to ensure compliance with environmental laws.

We anticipate that the regulation of our business operations under federal, state and local environmental laws in the United States and abroad will increase and become more stringent over time. We cannot estimate the impact of increased and more stringent regulation on our operations, future capital expenditure requirements or the cost of compliance.

United States Regulation. Statutory programs relating to protection of the environment and human health and to safety in the United States include, among others, the following.

CERCLA. The Comprehensive Environmental Response, Compensation and Liability Act of 1980, as amended, also known as “CERCLA” and “Superfund”, and comparable state laws generally impose joint and several liability for costs of investigation and remediation and for natural resource damages, without regard to fault or the legality of the original conduct, on certain classes of persons with respect to the release into the environment of specified substances, including under CERCLA those designated as “hazardous substances.” These persons include the present and certain former owners or operators of the site where the release occurred and those that disposed or arranged for the disposal of the hazardous substance at the site. These liabilities can arise in association with the properties where operations were conducted, as well as disposal facilities where wastes were sent. Many states have adopted comparable or more stringent state statutes. In the course of our operations, we generated materials that fall within CERCLA’s definition of hazardous substances. We may be the owner or operator of sites on which hazardous substances have been released and may have generated hazardous substances that have been transported to or otherwise released upon offsite facilities. We may be responsible under CERCLA for all or part of the costs to clean up facilities at which such substances have been released by previous owners or operators, facilities which we previously owned or operations at which such substances were released, and offsite facilities to which our wastes were transported and for associated damages to natural resources.

Resource Conservation and Recovery Act. The federal Resource Conservation and Recovery Act, as amended (“RCRA”) and comparable state laws regulate the treatment, storage, disposal, remediation and transportation of wastes, specifically under RCRA those designated as “hazardous wastes.” The EPA and various state agencies have limited the disposal options for these wastes and impose numerous regulations upon the treatment, storage, disposal, remediation and transportation of them. Our operations generate wastes that are subject to RCRA and comparable state statutes. Furthermore, wastes generated by our operations that are currently exempt from treatment as hazardous wastes may be designated in the future as hazardous wastes under RCRA or other applicable statutes and, therefore, may be subject to more rigorous and costly treatment, storage and disposal requirements. Governmental agencies (and in the case of civil suits, private parties in certain circumstances) can bring actions for failure to comply with RCRA requirements, seeking administrative, civil, or criminal penalties and injunctive relief, to compel us to abate a solid or hazardous waste situation that presents an imminent or substantial endangerment to health or the environment.

Clean Water Act. The federal Clean Water Act imposes restrictions and strict controls regarding the discharge of wastes and fill materials into waters of the United States. Under the Clean Water Act, and comparable state laws, the government (and in the case of civil suits, private parties in certain circumstances) can bring actions for failure to comply with Clean Water Act requirements and enforce compliance through civil, criminal and administrative penalties for unauthorized discharges of hazardous substances and of other pollutants. In the event of an unauthorized discharge of wastes, we may be liable for penalties and subject to injunctive relief.

Clean Air Act. The federal Clean Air Act (CAA), as amended and comparable state and local laws restrict the emission of air pollutants from many sources and also impose various monitoring and reporting requirements. These laws may require us to obtain pre-approval for the construction or modification of certain projects or facilities expected to produce or significantly increase air emissions, obtain and strictly comply with air permit requirements or utilize specific equipment or technologies to control emissions. Governmental agencies (and in the case of civil suits,

private parties in certain circumstances) can bring actions for failure to strictly comply with air pollution regulations or permits and generally enforce compliance through administrative, civil or criminal enforcement actions, resulting in fines, injunctive relief (which could include requiring us to forego construction, modification or operation of sources of air pollutants) and imprisonment. We may be required to incur certain capital expenditures for air pollution control equipment or other air emissions-related issues.

Greenhouse Gas Regulation. More stringent laws and regulations relating to climate change and greenhouse gases (GHGs) may be adopted in the future and could cause us to incur material expenses in complying with them. The EPA has begun to regulate GHGs as pollutants under the CAA. The EPA adopted rules to permit GHG emissions from stationary sources under the Prevention of Significant Deterioration and Title V permitting programs including the “Prevention of Significant Deterioration and Title V Greenhouse Gas Tailoring Rule,” requiring that the largest sources first obtain permits for GHG emissions. The United States Supreme Court, however, ruled that the EPA did not have the authority to require permits for GHG emissions and also did not have the authority to adopt that rule. The Court did hold that if a source required a permit under the program because of other pollutants, the EPA had the authority to require that the source demonstrate that it would use the best available control technology to minimize GHG emissions that exceeded a minimal amount.

Because of the lack of any comprehensive legislation program addressing GHGs, the EPA is using its existing regulatory authority to promulgate regulations requiring reduction in GHG emissions from various categories of sources, starting with fossil fuel-fired power plants. There is a great deal of uncertainty as to how and when additional federal regulation of GHGs might take place. In addition to federal regulation, a number of states, individually and regionally, and localities also are considering implementing or have implemented GHG regulatory programs. These regional and state initiatives may result in so-called cap-and-trade programs, under which overall GHG emissions are limited and GHG emission "allowances" are then allocated and sold to and between persons subject to the program. These and possibly other regulatory requirements could result in our incurring material expenses to comply, for example by being required to purchase or to surrender allowances for GHGs resulting from other operations or otherwise being required to control or reduce emissions.

Occupational Safety. Our operations are also governed by laws and regulations relating to workplace safety and worker health, principally the Occupational Safety and Health Act (OSHA) and its regulations. The OSHA hazard communication standard, the EPA's community right-to-know regulations and similar state programs may require us to organize and/or disclose information about hazardous materials used or produced in our operations.

Foreign Regulation. We are subject to various laws, regulations and ordinances to protect the environment, human health and safety promulgated by the governmental authorities in Mexico, Europe, Singapore, and in other countries where we do business. Each country has laws and regulations concerning waste treatment, storage and disposal, discharges to waterways, air emissions and workplace safety and worker health. Their respective regulatory authorities are given broad authority to enforce compliance with environmental, health and safety laws and regulations, and can require that operations be suspended pending completion of required remedial action.

Licenses, Permits and Product Registrations. Certain licenses, permits and product registrations are required for our products and operations in the United States, Mexico, Europe, Singapore, and in other countries where we do business. The licenses, permits and product registrations are subject to revocation, modification and renewal by governmental authorities. In the United States in particular, producers and distributors of chemicals such as penta are subject to registration and notification requirements under federal law (including under the Federal Insecticide, Fungicide and Rodenticide Act ("FIFRA") and the Toxic Substances Control Act, and comparable state law) in order to sell those products in the United States. Compliance with these laws has had, and in the future will continue to have, a material effect on our business, financial condition and results of operations. Under FIFRA, the law's registration system requires an ongoing submission to the EPA of substantial scientific research and testing data regarding the chemistry and toxicology of pesticide products by manufacturers.

Available Information

We make available free of charge on our Internet web site www.kmgchemicals.com, our Annual Report on Form 10-K, Quarterly Reports on Form 10-Q, Current Reports on Form 8-K and other filings pursuant to Section 13(a) or 15(d) of the Securities Exchange Act of 1934, and amendments to such filings, as soon as reasonably practicable after each are electronically filed with, or furnished to, the United States Securities and Exchange Commission ("SEC"). Information about our members of the Board of Directors, standing committee charters, and our Code of Business Conduct are also available, free of charge, through our website.

The SEC maintains a website that contains reports, proxy and information statements, and other information regarding issuers that file electronically with the SEC, available at www.sec.gov. You may read and copy any materials we file with the SEC at the SEC's Public Reference Room at 100 F Street NE., Washington, DC 20549. You may obtain information on the operation of the Public Reference Room by calling the SEC at 1-800-SEC-0330. Our stock trades under the ticker symbol "KMG" on the New York Stock Exchange. Except for portions of our proxy statement to be filed with the SEC, no information from either the SEC's website or our website is incorporated herein by reference.

ITEM 1A. RISK FACTORS

You should carefully consider the risks described below, together with all of the other information included in this report. We believe the risks and uncertainties described below are the most significant we face. The occurrence of any of the following risks could materially harm our business, financial condition or results of operations. In that case, the trading price of our common stock could decline, and you may lose all or part of your investment.

Risks Relating to Our Business

The industries in which we operate are competitive. This competition may affect our market share or prevent us from raising prices at the same pace as our costs increase, making it difficult for us to maintain existing business and win new business.

We operate in competitive markets. Certain of our competitors have substantially greater financial and technical resources than we do. Additionally, new competitors may enter our markets. We may be required to reduce prices if our competitors reduce prices, or

as a result of any other downward pressure on prices for our products and services, which could have an adverse effect on us. In electronic chemicals, we compete with several very large, international companies. Our customers have regularly requested price decreases and maintaining or raising prices has been difficult over the past several years and will likely continue to be so in the near future. Competition in electronic chemicals is based on a number of factors, including price, freight economics, product quality and technical support. If we are unable to compete successfully, our financial condition and results of operations could be adversely affected.

The industries that we compete in are subject to economic downturns.

An economic downturn in the electronic industry as a whole or other events (e.g., labor disruptions) resulting in significantly reduced production at the manufacturing plants of our customers, could have a material adverse impact on the results of our electronic chemicals segment. Similarly, an economic downturn affecting utilities or the oil and gas industry could have a material adverse effect on demand in our other chemicals segment.

A significant portion of our revenue and operating income are concentrated in a small number of customers.

We derive a significant portion of our revenues and operating income in our electronic chemicals and other chemicals segments from sales of products to a small number of customers. As a result, the loss of Intel, Stella or another significant customer, or a material reduction of demand from any of those customers, could adversely affect our revenues and operating income.

We will continue to pursue new acquisitions or joint ventures, and any such transaction could result in operating or management problems that adversely affect operating results. We remain subject to the ongoing risks of successfully integrating and managing the acquisitions and joint ventures that are completed.

The acquisitions we make expose us to the risk of integrating that acquisition. An integration effort impacts various areas of our business, including our management, production facilities, information systems, accounting and financial reporting, and customer service. Disruption to any of these areas could materially harm our financial condition or results of operations.

In our electronic chemicals segment, we are nearing the completion of our integration of the UPC subsidiaries acquired from OM Group at the end of May 2013. The size and complexity of that effort has been substantial, particularly because of the number of facilities involved, the broad geography of the electronic chemicals footprint, and the detailed coordination required to meet the needs of our customers. We believe that a successful integration allows us to achieve important advantages for our business and financial results, particularly from product sourcing and supply chain optimization. This integration effort is largely complete, and we believe it will generate a substantial improvement in segment operating income. No assurance can be given, however, that the effort will not take longer or be more costly than currently believed, and no assurance can be given that the advantages sought in the integration will be obtained.

We expect to continue to pursue new acquisitions or joint ventures, a pursuit which could consume substantial time and resources. The successful implementation of our operating strategy in current and future acquisitions and joint ventures may require substantial attention from our management team, which could divert management attention from existing businesses. The businesses acquired, or the joint ventures entered into, may not generate the cash flow and earnings, or yield the other benefits anticipated at the time of their acquisition or formation. The risks inherent in any such strategy could have an adverse impact on our results of operation or financial condition.

We are dependent on a limited number of suppliers for certain key raw materials, the loss of any one of which could have a material adverse effect on our financial condition and results of operations.

We depend on a limited number of suppliers for certain key raw materials needed by our businesses, such as sulfuric, hydrofluoric and nitric acids. Those suppliers are subject to a variety of operational and commercial constraints that can adversely impact our supply. If we were to lose suppliers for key raw materials, we might have difficulty securing a replacement supplier at reasonable cost, and no assurance can be given that such loss would not have a material adverse effect on our financial condition and results of operations.

The classification of pentachlorophenol as a Persistent Organic Pollutant under the Stockholm Convention may adversely affect our ability to manufacture or sell our penta products.

The Conference of the Parties (“COP”), comprising representatives from countries that have ratified the treaty known as the Stockholm Convention, met in May 2015 and considered the classification of penta as a persistent organic pollutant (“POP”). The COP accepted the recommendation of the United Nations Persistent Organic Pollutant Review Committee that the use of penta should be banned except that its use for the treatment of utility poles and cross arms could continue for an extended period of six to eleven years. We supply penta to industrial customers who use it primarily to treat utility poles and cross-arms. The United States is not

bound by the determination of the COP because it did not adopt the Stockholm Convention treaty. Canada and Mexico are governed by the treaty. No assurance can be given that the ultimate action of the COP will not have a material adverse effect on our financial condition and results of operation.

If the demand for the wood products on which our chemicals are used decreases, and our business, results of operations, cash flow and financial condition may be adversely affected.

Our wood treating products are sold into relatively stable markets. However, demand for treated wood generally increases or decreases with the financial strength and maintenance budgets of electric utilities, and demand can vary with damage levels suffered from severe storms. A significant decline in utility pole sales could have a material adverse effect on our business, financial condition and results of operations.

The implementation of a new enterprise resource planning system could cause a financial statement error not to be detected, and could take longer and be more costly than anticipated.

We are in the process of implementing a new enterprise resource planning (“ERP”) system to replace our current system. This is a complex process, and the new system will result in changes to our internal controls over financial reporting, including disclosure controls and procedures. The possibility exists that the migration to a new ERP system could adversely affect the effectiveness of our internal controls over financial reporting. Furthermore, no assurance can be given that the effort will not take longer or be more costly than currently believed.

If we are unable to identify, fund and execute new acquisitions, we will not be able to execute a key element of our business strategy.

Our strategy is to grow primarily by acquiring additional businesses and product lines. We cannot give any assurance that we will be able to identify, acquire or profitably manage additional businesses and product lines, or successfully integrate any acquired business or product line without substantial expenses, delays or other operational or financial difficulties. Financing for acquisitions may not be available, or may be available only at a cost or on terms and conditions that are unacceptable to us. Further, acquisitions may involve a number of special risks or effects, including diversion of management’s attention, failure to retain key acquired personnel, unanticipated events or circumstances, legal liabilities, impairment of acquired intangible assets and other one-time or ongoing acquisition-related expenses. Some or all of these special risks or effects could have a material adverse effect on our financial and operating results. In addition, we cannot assure you that acquired businesses or product lines, if any, will achieve anticipated revenues and earnings.

The consideration we pay in connection with an acquisition also may affect our financial results. If we were to proceed with one or more significant acquisitions in which the consideration included cash, we could be required to use a substantial portion of our available cash or obtain debt or equity financing. To the extent that we issue shares of our capital stock or other rights to purchase shares of our common stock as consideration for an acquisition or in connection with the financing of an acquisition, including options or other rights, our existing common shareholders may be diluted, and our earnings per share may decrease.

We may experience increased costs and production delays if suppliers fail to deliver materials or if prices increase for raw materials and other goods and services that we purchase from third parties.

We purchase raw materials for our electronic chemicals business from a number of domestic and foreign suppliers. Although we believe that the raw materials we require in our electronic chemicals business will be available in sufficient supply on a competitive basis for the foreseeable future, increases in the cost of raw materials, including energy and other inputs used to make our products, could affect future sales volumes, prices and margins for our products. If a supplier should cease to deliver goods or services to us, we would in most cases find other sources. However, such a disruption could result in added cost and manufacturing delays. In addition, political instability, war,

terrorism and other disruptions to international transit routes could adversely impact our ability to obtain key raw materials in a timely fashion, or at all.

Increases in the price of our primary raw materials may decrease our profitability and adversely affect our liquidity, cash flow, financial condition and results of operations.

The prices we pay for raw materials in our businesses may increase significantly, and we may not always be able to pass those increases through to our customers fully and timely. In the future, we may be unable to pass on increases in our raw material costs, and raw material price increases may erode the profitability of our products by reducing our gross profit. Price increases for raw materials may also increase our working capital needs, which could adversely affect our liquidity and cash flow. For these reasons, we cannot assure you that raw material cost increases in our businesses would not have a material adverse effect on our financial condition and results of operations.

Our ability to make payments on our debt will be contingent on our future operating performance, which will depend on a number of factors that are outside of our control.

Our ability to make principal and interest payments on our debt is contingent on our future operating performance, which will depend on a number of factors, many of which are outside of our control. The degree to which we are leveraged could have other important negative consequences, including the following:

- we must dedicate a substantial portion of our cash flows from operations to the payment of our indebtedness, reducing the funds available for future working capital requirements, capital expenditures, acquisitions or other general corporate requirements;
- a significant portion of our borrowings are, and will continue to be, at variable rates of interest, which may result in higher interest expense in the event of increases in interest rates;
- we may be more vulnerable to a downturn in the segments in which we operate or a downturn in the economy in general;
- we may be limited in our flexibility to plan for, or react to, changes in our businesses and the segments in which we operate;
- we may be placed at a competitive disadvantage compared to our competitors that have less debt;
- we may be limited in our ability to react to unforeseen increases in certain costs and obligations arising in our businesses, including environmental liabilities;
- we may determine it to be necessary to dispose of certain assets or one or more of our businesses to reduce our debt; and
- our ability to borrow additional funds may be limited.

If we are unable to make scheduled debt payments or comply with the other provisions of our debt instruments, our lenders may be permitted under certain circumstances to accelerate the maturity of the indebtedness owed to them and exercise other remedies provided for in those instruments and under applicable law.

Restrictions in our debt agreements could limit our growth and our ability to respond to changing conditions.

Our debt agreements contain a number of covenants which affect our ability to take certain actions and restrict our ability to incur additional debt. These include covenants that prohibit certain acquisitions that are not approved by our lenders. In addition, our debt agreements require us to maintain certain financial ratios and satisfy certain financial condition tests, which may require us to take action to reduce our debt or take some other action to comply with them.

These restrictions could limit our ability to obtain future financings, make needed capital expenditures, withstand a future downturn in our business or the economy in general or otherwise conduct necessary corporate activities. We may also be prevented from taking advantage of business opportunities that arise because of the limitations that these restrictive covenants impose on us.

A breach of any of these covenants would result in a default under the applicable debt agreement. A default, if not waived, could result in acceleration of the debt outstanding under the agreement and in a default with respect to certain of our other agreements. The accelerated debt would become immediately due and payable. If that should occur, we may not be able to pay all such debt or to borrow sufficient funds to refinance it. Even if new financing were then available, it may not be on terms that are acceptable to us.

We are subject to extensive environmental laws and regulations and may incur costs that have a material adverse effect on our financial condition as a result of violations of or liabilities under environmental laws and regulations.

Like other companies involved in environmentally sensitive businesses, our operations and properties are subject to extensive and stringent federal, state, local and foreign environmental laws and regulations, including those concerning, among other things:

- the treatment, storage and disposal of wastes;
- the investigation and remediation of contaminated soil and groundwater;
- the discharge of effluents into waterways;
- the emission of substances into the air; and
- other matters relating to environmental protection and various health and safety matters.

The EPA and other federal and state agencies in the United States, as well as comparable agencies in other countries where we have facilities or sell our products, have the authority to promulgate regulations that could have a material adverse impact on our operations. These environmental laws and regulations may require permits for certain types of operations, require the installation of

expensive pollution control equipment, place restrictions upon operations or impose substantial liability for pollution resulting from our operations. We expend substantial funds to minimize the discharge of hazardous materials in the environment and to comply with governmental regulations relating to protection of the environment. Compliance with environmental and health and safety laws and regulations has resulted in ongoing costs for us, and could restrict our ability to modify or expand our facilities or continue production, or require us to install costly pollution control equipment or incur significant expenses, including remediation costs. We have incurred, and expect to continue to incur, significant costs to comply with environmental and health and safety laws or to address liabilities for contaminated facilities. Federal, state and foreign governmental authorities may seek fines and penalties, as well as injunctive relief, for violation of the various laws and governmental regulations, and could, among other things, impose liability on us for cleaning up the damage resulting from a release of pesticides, hazardous materials or other chemicals into the environment.

If our products are not re-registered by the EPA or are re-registered subject to new restrictions, our ability to sell our products may be curtailed or significantly limited.

Our penta product registrations are under continuous review by the EPA under FIFRA. We have submitted and will submit a wide range of scientific data to support our U.S. registrations. To satisfy the registration review, we are required to demonstrate, among other things, that our products will not cause unreasonable adverse effects on human health or the environment when used according to approved label directions. In September 2008, the EPA announced that it had determined that penta was eligible for re-registration, but the EPA proposed new restrictions on the use of penta that have required our customers to incur substantial additional costs and to revise certain operating procedures. The EPA also required that penta registrants provide additional research and testing data respecting certain potential risks to human health or the environment as a further condition to continued re-registration. The cancer risk profile of penta was recently reviewed under the National Toxicology Program, and the EPA will reconsider its risk assessment of penta and may subject penta to a greater degree of regulatory or commercial scrutiny. We cannot tell you when or if the EPA will issue a final decision concluding that the conditions of re-registration for our penta products have been satisfied, and that all additional testing requirements have been satisfied. Even though EPA concluded that our wood treating chemicals were eligible for re-registration in 2008, our products are subject to further review and data submission requirements, and we cannot assure you that our products will not be subject to use or labeling restrictions that may have an adverse effect on our financial position and results of operations. The failure of our current or future-acquired products to be re-registered or to satisfy the registration review by the EPA, or the imposition of new use, labeling or other restrictions in connection with re-registration could have a material adverse effect on our financial condition and results of operations.

Our use of hazardous materials exposes us to potential liabilities.

Our manufacturing and distribution of chemical products involves the controlled use of hazardous materials. Our operations, therefore, are subject to various associated risks, including chemical spills, discharges or releases of toxic or hazardous substances or gases, fires, mechanical failure, storage facility leaks and similar events. Our suppliers are subject to similar risks that may adversely impact the availability of raw materials. While we adapt our manufacturing and distribution processes to the environmental control standards of regulatory authorities, we cannot completely eliminate the risk of accidental contamination or injury from hazardous or regulated materials, including injury of our employees, individuals who handle our products or goods treated with our products, or others who claim to have been exposed to our products, nor can we completely eliminate the unanticipated interruption or suspension of operations at our facilities due to such events. We may be held liable for significant damages or fines in the event of contamination or injury, and such assessed damages or fines could have a material adverse effect on our financial performance and results of operations.

The distribution and sale of our products is subject to prior governmental approvals and thereafter ongoing governmental regulation.

Our products are subject to laws administered by federal, state and foreign governments, including regulations requiring registration, approval and labeling of our products. The labeling requirements restrict the use and type of application for our products. More stringent restrictions could make our products less desirable which would adversely affect our sales and profitability. All states where our products are used also require registration before they can be marketed or used in that state.

Governmental regulatory authorities have required, and may require in the future, that certain scientific testing and data production be provided on our products. Under FIFRA, the federal government requires registrants to submit a wide range of scientific data to support U.S. registrations. This requirement significantly increases our operating expenses, and we expect those expenses will continue in the future. Because scientific analyses are constantly improving, we cannot determine with certainty whether or not new or additional tests may be required by regulatory authorities. While Good Laboratory Practice standards specify the minimum practices and procedures that must be followed in order to ensure the quality and integrity of data related to these tests submitted to the EPA, there can be no assurance that the EPA will not request certain tests or studies be repeated. In addition, more stringent legislation or requirements may be imposed in the future. We can provide no assurance that our resources will be adequate to meet the costs of regulatory compliance or that the cost of such compliance will not adversely affect our profitability.

The Registration Evaluation and Authorization of Chemicals (“REACH”) legislation may affect our ability to manufacture and sell certain products in the European Union.

REACH, which was effective on June 1, 2007, requires chemical manufacturers and importers in the European Union to prove the safety of their products. As a result, we were required to pre-register certain products and file comprehensive reports, including testing data, on each chemical substance, and perform chemical safety assessments. Additionally, substances of high concern are subject to an authorization process. Authorization may result in restrictions on certain uses of products or even prohibitions on the manufacture or importation of products. The full registration requirements of REACH will be phased in over several years. We will incur additional expense to cause the registration of our products under these regulations. REACH may also affect our ability to manufacture and sell certain products in the European Union.

Our products may be rendered obsolete or less attractive by changes in industry requirements or by supply-chain driven pressures to shift to environmentally preferable alternatives.

Changes in regulatory, legislative and industry requirements, or changes driven by supply-chain pressures, may shift current customers away from products using penta or certain of our other products and toward alternative products that are believed to have fewer environmental effects. The EPA, foreign and state regulators, local governments, private environmental advocacy organizations and a number of large industrial companies have proposed or adopted policies designed to decrease the use of a variety of chemicals, including penta and others included in certain of our products. Our ability to anticipate changes in regulatory, legislative, and industry requirements, or changes driven by supply-chain pressures, will be a significant factor in our ability to remain competitive. Further, we may not be able to comply with changed or new regulatory or industrial standards that may be necessary for us to remain competitive.

We cannot assure you that the EPA, foreign and state regulators and local governments will not restrict the uses of penta or certain of our other products or ban the use of one or more of these products, or that the companies who use our products may decide to reduce significantly or cease the use of our products voluntarily. As a result, our products may become obsolete or less attractive to our customers.

Volatility of oil and natural gas prices can adversely affect demand for our products and services.

Volatility in oil and natural gas prices may impact our customers’ activity levels and spending for our products and services. Expectations about future prices and price volatility are important for determining future spending levels for customers of our industrial valve lubricants and sealants products.

Historically, world-wide oil and natural gas prices and markets have been volatile, and may continue to be volatile in the future. In particular, the prices of oil and natural gas were highly volatile in 2014 and 2015 and declined dramatically. Prices for oil and natural gas are subject to wide fluctuations in response to relatively minor changes in the supply of and demand for oil and natural gas, market uncertainty and a variety of additional factors that are beyond our control. These factors include, but are not limited to, increases in supplies from US shale production, international political conditions, including recent uprisings and political unrest in the Middle East and Africa, the European sovereign debt crisis, the domestic and foreign supply of oil and natural gas, the level of consumer demand due to slowing economic growth in China and continued weak economic growth in Europe, weather conditions, domestic and foreign governmental regulations and taxes, the price and availability of alternative fuels, the health of international economic and credit markets, the ability of the members of the Organization of Petroleum Exporting Countries and other state-controlled oil companies to agree upon and maintain oil price and production controls, and general economic conditions.

Lower oil and natural gas prices generally lead to decreased spending by customers of our industrial valve lubricants and sealants. While higher oil and natural gas prices generally lead to increased spending by our customers in that business, sustained high energy prices can be an impediment to economic growth and to other segments of our

business as described below, and can therefore negatively impact spending by some of our customers. Our customers also take into account the volatility of energy prices and other risk factors by requiring higher returns for individual projects if there is higher perceived risk. Any of these factors could affect the demand for oil and natural gas for our customers in the industrial lubricants and sealants business and could have a material adverse effect on our results of operations.

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The profitability of our electronic chemicals and some of our other chemicals could also be adversely affected by high petroleum prices.

The profitability of our business depends, to a degree, upon the price of petroleum products, both as a component of transportation costs for delivery of products to our customers and as a raw material used to make our products, including penta solutions. High petroleum prices also affect the businesses of our customers. Our penta customers dissolve our product in petroleum based materials to make a treating solution for utility poles. Unfavorable changes in petroleum prices or in other business and economic conditions affecting our customers could reduce purchases of our products, and impose practical limits on our pricing. Any of these factors could lower our profit margins, and have a material adverse effect on our results of operations. We are unable to predict what the price of crude oil and petroleum-based products will be in the future. We may be unable to pass along to our customers the increased costs that result from higher petroleum prices.

We may be unable to identify liabilities associated with the properties and businesses that may be acquired or obtain protection from sellers against them.

The acquisition of properties and businesses requires assessment of a number of factors, including physical condition and potential environmental and other liabilities. Such assessments are inexact and inherently uncertain. The assessments made result from a due diligence review of the subject properties and businesses, but such a review may not reveal all existing or potential problems. We may not be able to obtain comprehensive contractual indemnities from the seller for liabilities that it created or that were created by any predecessor of the seller. We may be required to assume the risk of the physical or environmental condition of the properties and businesses in addition to the risk that the properties and businesses may not perform in accordance with expectations.

We are dependent upon many critical systems and processes, many of which are dependent upon hardware that is concentrated in a limited number of locations. If a catastrophe or cyber security event were to occur at one or more of those locations or with our data, it could have a material adverse effect on our business.

Our business is dependent on certain critical systems, which support various aspects of our operations, from our computer network to our billing and customer service systems. The hardware supporting a large number of such systems is housed in a small number of locations. If one or more of these locations were to be subject to fire, natural disaster, terrorism, power loss, or other catastrophe, it could have a material adverse effect on our business. While we believe that we maintain reasonable disaster recovery programs, there can be no assurance that, despite these efforts, any disaster recovery, security and service continuity protection measures we may have or may take in the future will be sufficient.

In addition, we may be susceptible to acts of aggression on our critical operating system. Cyber security events such as computer viruses, electronic break-ins or other similar disruptive technological problems could also adversely affect our operations. Should such an event occur in the future, our insurance policies may not adequately compensate us for any losses that may occur due to any failures or interruptions in our computer systems and could affect our financial and operating results, causing disruptions in operations, damage of reputation, litigation, increased costs, or inaccurate information reported by our manufacturing facilities.

Weather may adversely impact our ability to conduct business.

Our penta facility in Matamoros, Mexico, and several suppliers of raw materials for our electronic chemicals business are located on or near the Gulf of Mexico. Thus, we are dependent on terminals and facilities located in coastal areas for a substantial portion of certain of the raw materials we use, the penta we make and for our electronic chemicals products. These terminals and facilities are vulnerable to hurricanes, rising water and other adverse weather conditions that have the potential to cause substantial damage and to interrupt operations. For example, in 2005 Hurricane Katrina temporarily closed a terminal in New Orleans, Louisiana that we used for creosote distribution (a business we

have since divested) and forced us to locate an interim substitute terminal. There can be no assurance that adverse weather conditions will not affect the availability of penta and certain other raw materials in the future, the occurrence of which could have a material adverse effect on our financial condition and results of operations. More generally, severe weather conditions have the potential to adversely affect our operations, damage facilities and increase our costs, and those conditions may also have an indirect effect on our financing and operations by disrupting services provided by service companies or suppliers with whom we have a business relationship. We may not be able to recover through insurance some or any of the damages, losses or costs that may result from potential physical effects of climate.

Our business success depends significantly on the reliability and sufficiency of our manufacturing facilities.

Our revenues depend significantly on the continued operation of our manufacturing facilities. The operation of our facilities involves risks, including the breakdown, failure, or substandard operation or performance of equipment, power outages, explosions, fires, earthquakes, other natural disasters, terrorism and other unscheduled downtime. The occurrence of material operational problems, the loss or shutdown of our facilities over an extended period of time due to these or other events could have a material adverse effect on our financial performance and operating results.

Our business is subject to many operational risks for which we may not be adequately insured.

We cannot assure you that we will not incur losses beyond the limits of, or outside the coverage of, our insurance policies. From time to time, various types of insurance for companies in the chemical industry have not been available on commercially acceptable terms or, in some cases, have been unavailable. In addition, we cannot assure you that in the future we will be able to maintain existing coverage or that our insurance premiums will not increase substantially.

We maintain limited insurance coverage for sudden and accidental environmental damages. We do not believe that insurance coverage for environmental damages that occur over time is available at a reasonable cost. Also, we do not believe that insurance coverage for the full potential liability that could be caused by sudden and accidental incidences is available at a reasonable cost. Accordingly, we may be subject to an uninsured or under-insured loss in such cases.

Our business may be adversely affected by cyclical and seasonal effects.

In general, the chemical industry is cyclical and demand for our wood treating products and lubricants is somewhat seasonal. There is greater demand for our wood treating chemicals in the summer than in the winter because of the effects of weather on timber harvest, and the pipeline customers of our lubricants business tend to prefer doing maintenance on their systems from the spring through the fall seasons. Our electronic chemical products are often used to produce semiconductors for industries and applications that are cyclical in nature, as well as subject to customer marketing programs and requirements. There can be no assurance that our business, resources and margins will not be adversely affected by seasonal or cyclical effects.

We depend on our senior management team and the loss of any member could adversely affect our operations.

Our success is dependent on the management and leadership skills of our senior management team, including Christopher T. Fraser, our President and Chief Executive Officer, Malinda G. Passmore, our Chief Financial Officer, Ernest C. Kremling, our Vice President of Operations, Andrew Lau, our Vice President of Electronic Chemicals, Michael A. Hoffman, our Vice President and General Manager of Wood Treating Chemicals, Jason Councill, our Vice President and General Manager of Industrial Valve Lubricants and Sealants, Christopher W. Gonser, our Vice President of Human Resources, and Roger C. Jackson, our General Counsel. While we have succession plans for key positions, the loss of any member of our senior management team or an inability to attract, retain and maintain additional qualified personnel could prevent us from implementing our business strategy. We cannot assure you that we will be able to retain our existing senior management personnel or attract additional qualified personnel when needed.

If we are unable to successfully negotiate with the labor unions representing our employees, we may experience a material work stoppage.

About 19.3% of our full-time employees are represented by labor unions, workers councils or comparable organizations, particularly in Mexico and Europe. As our current agreements expire, we cannot assure you that new agreements will be reached at the end of each period without union action, or that a new agreement will be reached on terms satisfactory to us. An extended work stoppage, slowdown or other action by our employees could significantly disrupt our business. Future labor contracts may be on terms that result in higher labor costs to us, which also could adversely affect our results of operations.

Our financial performance is subject to risks associated with changes in the value of the U.S. dollar versus local currencies.

Our primary exposure to movements in foreign currency exchange rates relates to non-U.S. dollar denominated sales and operating expenses worldwide. Weakening of foreign currencies relative to the U.S. dollar adversely affects the U.S. dollar value of our foreign currency-denominated sales and earnings, and generally leads us to raise international pricing, potentially reducing demand for our products. Margins on sales of our products in foreign countries and on sales of products that include components obtained from foreign suppliers, could be materially adversely affected by foreign currency exchange rate fluctuations. In some circumstances, for competitive or other reasons, we may decide not to raise local prices to fully offset the dollar's strengthening, or at all, which would adversely affect the U.S. dollar value of our foreign currency denominated sales and earnings. Conversely, a strengthening of foreign currencies relative to the U.S. dollar, while generally beneficial to our foreign currency-denominated sales and earnings, could cause us to reduce international pricing. Additionally, strengthening of foreign currencies may also increase our cost of product components denominated in those currencies, thus adversely affecting gross margins.

Additionally, because our consolidated financial statements are presented in U.S. dollars, we must translate revenues, income and expenses, as well as assets and liabilities, into U.S. dollars at exchange rates in effect during or at the end of each reporting period. Therefore, increases or decreases in the value of the U.S. dollar against other major currencies affect our net operating revenues, operating income and the value of balance sheet items denominated in foreign currencies. We do not use derivative financial instruments to reduce our net exposure to currency exchange rate fluctuations. We cannot assure you that fluctuations in foreign currency exchange rates, particularly the strengthening of the U.S. dollar against major currencies or the currencies of large developing countries, would not materially affect our financial results.

We are subject to narcotics gang disruption in Mexico and to possible risk of terrorist attacks, each of which could adversely affect our business.

Our penta manufacturing facility is located in Matamoros, Mexico, an area where there has been violent crime involving narcotics gang warfare. Our penta operations could be disrupted or otherwise affected by narcotics gang activities in the Mexico border area where our facility is located. We are not insured against terrorist or narcotics gang attacks, and there can be no assurance that losses that could result from an attack on our facilities or personnel, railcars or tank trucks would not have a material adverse effect on our business, results of operations and financial condition. Since September 11, 2001, there has been concern that chemical manufacturing facilities and railcars carrying hazardous chemicals may be at an increased risk of terrorist attacks. Federal, state and local governments have begun a regulatory process that could lead to new regulations impacting the security of chemical industry facilities and the transportation of hazardous chemicals. Our business could be adversely impacted if a terrorist incident were to occur at any chemical facility or while a railcar or tank truck was transporting chemicals.

We are subject to risks inherent in foreign operations, including changes in social, political and economic conditions.

We have facilities in the United States, Mexico, Europe and Singapore, and generate a significant portion of our sales in foreign countries. Like other companies with foreign operations and sales, we are exposed to market risks relating to fluctuations in foreign currency exchange rates. At this time, the Euro and the Great Britain Pound are the functional currencies of our operations in Europe. We are also exposed to risks associated with changes in the laws and policies governing foreign investments in Mexico, Europe and Asia, and to a lesser extent, changes in United States laws and regulations relating to foreign trade and investment. While such changes in laws, regulations and conditions have not had a material adverse effect on our business or financial condition, we cannot assure you as to the future effect of any such changes.

ITEM 1B. UNRESOLVED STAFF COMMENTS

None.

ITEM 2. PROPERTIES

As of July 31, 2015, we own or lease the following properties.

| Location | Primary Use | Approximate Size | Owned/ Lease Expiration | |
|-----------------------|---|--------------------|-------------------------|---------------------------------|
| | | | Leased | Date |
| Houston, Texas | Corporate Office | 17,527 square feet | Leased | January 2017 |
| Tuscaloosa, Alabama | Formulation and Distribution: Penta | 2.0 acres | Owned | N/A |
| Hollister, California | Manufacture and Warehouse: Electronic Chemicals | 4.4 acres | Owned | N/A |
| Pueblo, Colorado | Manufacture and Warehouse: Electronic Chemicals | 37.4 acres | Owned | N/A |
| Houston, Texas | Formulation and Distribution: Lubricants | 1.15 acres | Leased | June 2016 |
| Rousset, France | Warehouse and adjacent land: Electronic Chemicals | 1.2 acres | Leased | December 2023 and December 2024 |
| St. Cheron, France | Manufacture and Warehouse: Electronic Chemicals | 4.0 acres | Owned | N/A |
| St. Fromond, France | Manufacture and Warehouse: Electronic Chemicals | 71.6 acres | Owned | N/A |
| Milan, Italy | Warehouse: Electronic Chemicals | 4.9 acres | Owned | N/A |
| Milan, Italy | Manufacture: Electronic Chemicals | 2.5 acres | Owned | N/A |
| Johor Bahru, Malaysia | Sales office: Electronic Chemicals | 1,360 square feet | Leased | March 2016 |
| Johor Bahru, Malaysia | Warehouse: Electronic Chemicals | 750 square feet | Leased | May 2016 |
| Matamoros, Mexico | Manufacture and Warehouse: Penta | 13.0 acres | Owned | N/A |
| Singapore | Warehouses (2): Electronic Chemicals | 3.0 acres | Leased | August 2016 and March 2017 |
| Riddings, UK | Manufacture and Warehouse: Electronic Chemicals | 4.2 acres | Leased | August 2025 |

We believe that all of these properties are adequately insured, in good condition and suitable for their anticipated future use. We believe that if the leases for our offices and facilities in Malaysia and France are not renewed or are terminated, we can obtain other suitable facilities. If our warehouses and facilities in Singapore and the United Kingdom, respectively, were not renewed or terminated, no assurance can be given that we could obtain suitable

substitutes without incurring substantial expense. We believe, however, that we will be able to renew our leases on acceptable terms and conditions at the end of their respective terms.

In August 2015 we entered into a lease for corporate offices in Fort Worth, Texas. We intend to relocate our corporate offices from Houston to Fort Worth in December 2015. The new offices consist of 27,778 square feet of space, and the lease extends to December 2028.

We also have several storage agreements with commercial warehouses from which we distribute our electronic chemicals.

ITEM 3. LEGAL PROCEEDINGS

The information set forth in Note 8 to the consolidated financial statements included in Item 8 of Part II of this report is incorporated herein by reference.

ITEM 4. MINE SAFETY DISCLOSURES

None.

PART II

ITEM 5. MARKET FOR REGISTRANT'S COMMON EQUITY, RELATED STOCKHOLDER MATTERS AND ISSUER PURCHASES OF EQUITY SECURITIES

Our common stock, par value \$.01 per share, is traded on The New York Stock Exchange (trading symbol KMG). As of November 23, 2015, there were 11,715,586 shares of common stock issued and outstanding held by approximately 430 shareholders of record, and more than 300 round lot holders. The following table represents the high and low sale prices for our common stock as reported by the New York Stock Exchange for fiscal year 2015 and fiscal year 2014. The table also shows quarterly dividends we declared and paid during fiscal years 2015 and 2014.

| | Common Stock Prices | | Dividends Declared and Paid | |
|----------------|------------------------|----------|-----------------------------|------------|
| | High | Low | Per Share | Amount |
| Fiscal 2015 | | | | |
| First Quarter | \$ 18.00 | \$ 14.04 | \$ 0.03 | \$ 350,000 |
| Second Quarter | 21.14 | 17.20 | 0.03 | 350,000 |
| Third Quarter | 30.97 | 21.79 | 0.03 | 350,000 |
| Fourth Quarter | 31.90 | 21.68 | 0.03 | 351,000 |
| Fiscal 2014 | | | | |
| First Quarter | \$ 24.17 | \$ 19.20 | \$ 0.03 | \$ 347,000 |
| Second Quarter | 20.27 | 14.79 | 0.03 | 348,000 |
| Third Quarter | 17.18 | 14.47 | 0.03 | 349,000 |
| Fourth Quarter | 18.50 | 14.99 | 0.03 | 349,000 |

We intend to pay out a reasonable share of cash from operations as dividends, consistent on average with the payout record of past years. We declared and paid a dividend in the first quarter of fiscal year 2016 of \$0.03 per share, or approximately \$350,000. The current quarterly dividend rate represents an annualized dividend of \$0.12 per share. The future payment of dividends, however, will be within the discretion of the Board of Directors and depends on our profitability, capital requirements, financial condition, growth, business opportunities and other factors which our Board of Directors may deem relevant. We repurchased no shares in fiscal years 2015 or 2014.

Our 2009 Long-Term Incentive Plan was submitted to the shareholders and approved at our annual meeting of shareholders on December 8, 2009.

The following information respecting our outstanding options, warrants and rights is provided as of July 31, 2015:

| | | |
|--------------|-----------|---------------|
| Number of | Weighted- | Number of |
| securities | average | securities |
| to be issued | | available for |

| | upon exercise of outstanding options, warrants and rights | exercise price of outstanding options, warrants and rights | future issuance under equity compensation plans (excluding securities reflected in column (a) (c) |
|---|---|--|---|
| | (a) | (b) | (c) |
| Plan Category Equity compensation plans | | | |
| approved by security holders | — | \$ — | — 124,575 |
| Equity compensation plans not approved by | | | |
| security holders | — | — | — |
| Total | — | \$ — | — 124,575 |

ITEM 6. SELECTED FINANCIAL DATA

The following table shows selected historical consolidated financial data for the five fiscal years ended July 31, 2015. The consolidated statements of income and cash flow data for each of the three fiscal years ended July 31, 2015, and the balance sheet data as of July 31, 2015 and 2014, have been derived from our audited consolidated financial statements included elsewhere in this report. The consolidated statements of income and cash flow data for the fiscal years ended July 31, 2012 and 2011, and the balance sheet data as of July 31, 2013, 2012 and 2011 have been derived from our previously issued audited consolidated financial statements. The data should be read in conjunction with our consolidated financial statements and notes to consolidated financial statements.

| | Year Ended July 31, | | | | |
|---|---------------------|-----------|-----------|-----------|-----------|
| | 2015 | 2014 | 2013 | 2012 | 2011 |
| Statement of Income Data⁽¹⁾ | | | | | |
| Net sales | \$320,498 | \$353,406 | \$263,311 | \$272,700 | \$255,596 |
| Operating income | 16,589 | 3,951 | 17,180 | 25,437 | 17,022 |
| Income/(loss) from continuing operations | 12,138 | (988) | 9,486 | 14,315 | 9,418 |
| Net income/(loss) | 12,138 | (988) | 9,348 | 13,825 | 9,729 |
| Income/(loss) per share from continuing operations- | | | | | |
| basic | \$1.04 | \$(0.09) | \$0.82 | \$1.26 | \$0.83 |
| Income/(loss) per share from discontinued | | | | | |
| operations-basic | — | — | (0.01) | (0.04) | 0.03 |
| Income/(loss) per share-basic | \$1.04 | \$(0.09) | \$0.81 | \$1.22 | \$0.86 |
| Income/(loss) per share from continuing operations- | | | | | |
| diluted | \$1.03 | \$(0.09) | \$0.82 | \$1.24 | \$0.82 |
| Income/(loss) per share from discontinued | | | | | |
| operations-diluted | — | — | (0.01) | (0.04) | 0.03 |
| Income/(loss) per share-diluted | \$1.03 | \$(0.09) | \$0.81 | \$1.20 | \$0.85 |
| Cash Flow Data⁽¹⁾ | | | | | |
| Net cash provided by operating activities | \$17,568 | \$40,358 | \$20,272 | \$25,249 | \$12,713 |
| Net cash provided by (used in) investing activities | (18,288) | (9,274) | (68,113) | 4,043 | (8,007) |
| Net cash provided by (used in) financing activities | (9,091) | (26,065) | 59,992 | (29,275) | (7,823) |
| Payment of dividends | (1,402) | (1,393) | (1,378) | (1,249) | (1,017) |
| Balance Sheet Data⁽¹⁾ | | | | | |
| Total assets | \$242,359 | \$250,858 | \$262,015 | \$167,690 | \$185,378 |
| Long-term debt | 53,000 | 60,000 | 85,000 | 24,000 | 41,279 |
| Total stockholders' equity | 123,421 | 120,206 | 117,240 | 106,767 | 96,530 |

(1) Our historical results are not necessarily indicative of results to be expected for any future period. The comparability of the data is affected by our acquisitions during the fiscal years 2015 and 2013; the disposition of our creosote distribution business during the fiscal year 2015; and our restructuring and realignment of operations during the fiscal years 2015 and 2014 as described in Item 7, Management's Discussion and Analysis of Financial Condition and Results of Operations.

ITEM 7. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

The following discussion and analysis of our financial condition and results of operations should be read in conjunction with the "Selected Financial Data" section of this report and our consolidated financial statements and the related notes and other financial information included elsewhere in this report. In addition to historical financial information, the following discussion and analysis contains forward-looking statements that involve risks, uncertainties and assumptions. Our actual results and timing of selected events may differ materially from those anticipated in these forward-looking statements as a result of many factors, including those discussed under the section entitled "Risk Factors" and elsewhere in this report.

Introduction

We manufacture, formulate and globally distribute specialty chemicals. We operate businesses selling electronic chemicals, industrial wood treating chemicals and industrial valve lubricants and sealants. Our electronic chemicals are sold to the semiconductor industry where they are used primarily to clean and etch silicon wafers in the production of semiconductors. Our wood treating chemicals, based on penta, are used by industrial customers primarily to extend the useful life of utility poles and cross-arms. Our valve lubricants and sealants enable optimal valve operation and help prevent costly downtime at oil and gas storage facilities and pipelines. In addition, our lubricants and sealants provide important safety benefits along with preventing fugitive valve emissions.

In fiscal year 2015, approximately 82.9% of our revenues were from our electronic chemicals segment, and 17.1% were from our other chemicals segment, which includes our wood treating chemicals and our industrial valve lubricants and sealants.

Our results of operations are impacted by various competitive and other factors including:

- fluctuations in sales volumes;
- raw material pricing and availability;
- our ability to acquire and integrate new products and businesses; and
- the difference between prices received by us for our specialty chemical products and the costs to produce those products.

Acquisition of Valves Incorporation of Texas

On May 1, 2015, we completed the acquisition of Valves Incorporated of Texas, a privately held Texas corporation, pursuant to the terms of a previously announced agreement and plan of merger. The acquired company manufactures and distributes industrial sealants and lubricants, primarily to the oil and gas storage, pipeline and gas distribution markets, as well as related products, such as lubrication equipment and fittings. In addition to the lubricants business, Valves Incorporated of Texas also owned 606,875 shares of our common stock. The aggregate merger consideration to the former shareholders of Valves Incorporated of Texas was 606,875 shares of our common stock plus \$23.7 million in cash. The 606,875 shares previously owned by Valves Incorporated of Texas were cancelled as of the time of the merger, and no additional net shares were issued as a result of the merger. At the closing of the merger, Valves Incorporated of Texas merged into Val-Tex, our wholly owned subsidiary. See Note 2 to the consolidated financial statements included in this report.

Acquisition of Ultra Pure Chemicals Business

On May 31, 2013, we completed our acquisition of the ultra pure chemicals ("UPC") business subsidiaries of OM Group, with facilities located in the United States, the United Kingdom, France and Singapore. The final purchase price for the acquisition was \$63.2 million. The subsidiaries sell high purity and ultra purity, wet process chemicals to the semiconductor industry. See Note 2 to the consolidated financial statements included in this report.

Sale of Creosote Distribution Business

On January 16, 2015, we sold our creosote distribution business, part of our previous wood treating chemicals segment, to Koppers Inc. pursuant to an asset purchase agreement. Creosote is a wood preservative used to treat utility poles and railroad crossties. The transaction closed concurrently with the signing of the asset purchase agreement. Assets that were sold in the transaction included our EPA registrations for creosote, creosote inventory, railcar and tank terminal leases and various customer agreements. The sale price for the assets was approximately \$14.9 million. The gain on the sale was \$5.4 million.

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Sale of Elwood Facility

We had retained the real estate and building of our facility in Elwood, Kansas when we sold our animal health business in 2012 and had been leasing the facility to a third party since that time. The tenant, Ritepack, Inc., exercised its option to purchase the facility. The sale price was \$2.5 million, payable in cash on the closing date. The sale of the facility closed on February 26, 2015. We recognized a loss on the sale of approximately \$29,000.

Restructuring and Realignment of Operations

In October 2013, we announced that, as part of a global restructuring of our electronic chemicals operations, we would close our Fremont, California manufacturing site acquired in the UPC acquisition, and shift production primarily to our Hollister, California and Pueblo, Colorado facilities. We ceased production at the Fremont facility, and completed site decommissioning by the end of fiscal year 2014. In November 2013, we announced that we would close a facility in Milan, Italy, and shift some production to our facilities in France and the United Kingdom. We are decommissioning certain manufacturing equipment in Milan, and transitioning products from there to other sites in Europe. That effort will be completed in calendar year 2015.

Total costs related to restructuring incurred for fiscal year 2015 was \$1.3 million, including \$0.9 million related to accelerated depreciation. Restructuring charges, including accelerated depreciation, have been \$7.6 million in the aggregate in fiscal years 2015 and 2014. Accelerated depreciation with respect to the Fremont and Milan facilities was approximately \$3.3 million over those two fiscal years. See Note 14 to the financial statements included in this report.

On October 13, 2014, we announced a realignment of our hydrofluoric acid business, and subsequently exited the facility operated for us by Chemtrade Logistics (“Chemtrade”) in Bay Point, California. Under the toll manufacturing agreement with Chemtrade, we are to pay or reimburse Chemtrade for certain costs associated with the cessation of operations at Bay Point, including certain employee costs and the decommissioning, dismantling and removal of our manufacturing equipment at the site. In fiscal year 2014, we established an asset retirement obligation of \$3.7 million for decontamination, decommissioning and dismantling at Bay Point. Operations ceased in the third quarter of fiscal year 2015. In fiscal year 2015, we incurred realignment charges of \$4.8 million for accelerated depreciation. Additionally, we incurred certain employee costs of \$0.8 million. In fiscal year 2014 we recorded accelerated depreciation expense of \$1.8 million against our assets and retirement obligation. In addition, we recognized an impairment charge of \$2.7 million in fiscal year 2014 with respect to certain manufacturing equipment at Bay Point that were no longer in service. See Note 14 to the financial statements included in this report.

Results of Operations

Segment Data

Segment data is presented for our two reportable segments for the three fiscal years ended July 31, 2015, 2014 and 2013. The segment data should be read in conjunction with our consolidated financial statements and related notes included elsewhere in this report. The information presented for the other chemicals segment for fiscal years 2014 and 2013 represents information that was previously reported in our wood treating chemicals operations. Following the sale of our creosote distribution business in January 2015 and the acquisition of our industrial valve lubricants and sealants business on May 1, 2015, our wood treating chemicals operations were combined with the newly acquired industrial valve lubricants and sealants business to form the other chemicals segment, as discussed in Note 13 to our consolidated financial statements.

| Year Ended July 31, | | |
|---------------------|------|------|
| 2015 | 2014 | 2013 |

(Amounts in thousands)

| | | | |
|-------------------------------------|-----------|-----------|-----------|
| Sales: | | | |
| Electronic chemicals | \$265,608 | \$253,754 | \$165,755 |
| Other chemicals | 54,820 | 99,514 | 97,185 |
| Total sales for reportable segments | \$320,428 | \$353,268 | \$262,940 |

Segment Sales

In fiscal year 2015, net sales in the electronic chemicals segment were \$265.6 million, an increase of \$11.8 million, or 4.6% over net sales of \$253.8 million in fiscal year 2014. In fiscal year 2014, net sales in the electronic chemicals segment increased \$88.0 million, or 53.1%, over net sales of \$165.8 million in fiscal year 2013. In fiscal year 2015, the increase in net sales from the prior year came primarily from increased sales volume and pricing in North America and Asia, offset to a degree by weaker sales in Europe, primarily due to the stronger U.S. dollar. In fiscal year 2014, the increase in net sales from the prior year came primarily from the acquisition of the UPC business subsidiaries of OM Group on May 31, 2013.

Net sales of other chemicals decreased by \$44.7 million, or 44.9%, to \$54.8 million in fiscal year 2015 from \$99.5 million in fiscal year 2014. Net sales of other chemicals in fiscal year 2014 increased by \$2.3 million, or 2.4%, from \$97.2 million in fiscal year 2013. The decrease in other chemicals net sales in fiscal year 2015 was due to lower creosote sales. Creosote sales ceased upon the divestiture of the creosote business in January 2015. The lower creosote sales were partially offset by sales in the industrial valve lubricants and sealants business acquired in May 2015. The increase in fiscal year 2014 in other chemicals net sales came mostly from an increase in penta block sales to customers, offset by lower creosote volume.

Segment Income from Operations

Income from operations of the electronic chemicals segment was \$21.8 million in fiscal year 2015, as compared to \$14.1 million in fiscal year 2014 and \$14.0 million in fiscal year 2013. Income from operations of electronic chemicals increased by \$7.7 million, or 54.6%, in fiscal year 2015 as compared to the prior year period, and increased by \$0.1 million, or 0.01%, in fiscal year 2014 as compared to the prior year period.

The fiscal year 2015 improvement in income from operations in electronic chemicals was primarily due to increased sales in North America and Asia, partially offset by weaker sales in Europe. The fiscal year 2014 improvement in income from operations in electronic chemicals was primarily due to the effect of our acquisition of the UPC business net of integration expense of approximately \$1.2 million and additional depreciation and amortization of \$5.4 million. Integration expenses in fiscal years 2015 and 2014 were primarily for consulting, professional services and travel expenses, including Sarbanes-Oxley implementation and testing at the acquired UPC subsidiaries.

Depreciation expense for the electronic chemicals segment for fiscal year 2015 includes accelerated depreciation of assets of \$4.8 million at the Bay Point, California facility, and \$0.9 million at our Milan, Italy facility, including accelerated depreciation related to asset retirement obligations at Bay Point. We ceased operations at Fremont in fiscal year 2014, and exited from our toll manufacturing arrangement and ceased operations at the Bay Point facility in the third fiscal quarter of 2015. We have also closed a portion of our Milan facility. These decisions resulted in a reassessment of the useful lives of certain equipment at each facility and in accelerated depreciation. In addition, we recognized an impairment loss in fiscal year 2014 of \$2.7 million on certain long-lived assets at the Bay Point facility that are no longer in service and management has concluded will be disposed of.

In fiscal year 2015, income from operations of the other chemicals segment was \$8.7 million as compared to \$8.4 million in fiscal year 2014 and \$10.5 million in fiscal year 2013. Income from operations for the other chemicals segment increased by \$0.3 million, or 3.6%, in fiscal year 2015 and decreased by \$2.1 million, or 20.0%, in fiscal year 2014 as compared to the respective prior year period.

Income from operations of the other chemicals segment improved in fiscal year 2015 over the prior year because of the acquisition of our industrial valve lubricants and sealants business and due to improved sales of penta products and lower raw material costs. In fiscal year 2014, creosote and penta volume improved approximately 3.6% and 9.4%, respectively, but operating income in other chemicals was down due to lower pricing of the hydrochloric acid that is a byproduct of penta production, higher raw material costs for penta and creosote and lower creosote pricing.

Net Sales and Gross Profit

Net Sales and Gross Profit for Fiscal Year 2015 vs. Fiscal Year 2014

Net sales decreased \$32.9 million, or 9.3% in fiscal year 2015 to \$320.5 million from \$353.4 million in fiscal year 2014. Net sales for fiscal year 2015 decreased compared to the prior year period primarily because creosote sales ceased upon the divestiture of the creosote business in January 2015. The decrease was partially offset by increased sales in the electronic chemicals segment and the acquisition of the industrial valve lubricants and sealants business acquired in May 2015.

Gross profits increased by \$6.0 million, or 5.8%, to \$109.5 million compared to \$103.5 million in fiscal year 2014. The increase in gross profit was the result of increased sales in our electronic chemicals business and the acquisition of our industrial valve lubricants and sealants business. Gross profit as a percent of sales increased in fiscal 2015 to 34.2% from 29.3% in fiscal 2014. The improvements in gross profits as a percentage of sales in fiscal year 2015 as compared to 2014 was due to the sale of our creosote distribution business, which included products with lower profit margins. In addition, gross profit margins increased in electronic chemicals due to synergies realized from our manufacturing consolidation in North America.

Because other companies may include certain of the costs that we record in cost of sales in distribution expenses or selling, general and administrative expenses, and may include certain of the costs that we record in distribution expenses or selling, general and administrative expenses as cost of sales, our gross profit may not be comparable to that reported by other companies.

Net Sales and Gross Profit for Fiscal Year 2014 vs. Fiscal Year 2013

Net sales increased \$90.1 million, or 34.2% in fiscal year 2014 to \$353.4 million from \$263.3 million in fiscal year 2013. Net sales for fiscal year 2014 increased over the prior year period primarily because of the UPC acquisition. That acquisition has allowed us to expand our global presence, and expand our ability to serve a broader spectrum of our semiconductor customers' requirements.

Gross profits increased by \$27.0 million, or 35.3%, to \$103.5 million compared to \$76.5 million in fiscal year 2013. The increase in gross profit was the result of sales attributable to the UPC acquisition. Gross profit as a percent of sales increased in fiscal 2014 to 29.3% from 29.0% in fiscal 2013.

Distribution and Selling, General and Administrative Expenses

Distribution and Selling, General and Administrative Expenses for Fiscal Year 2015 vs. Fiscal Year 2014

Distribution expenses decreased to approximately \$48.5 million in fiscal year 2015 from \$50.3 million in fiscal year 2014, a decrease of \$1.8 million, or 2.9%. Distribution expense is heavily concentrated in our electronic chemicals business. The electronic chemicals segment incurred approximately 94%, 89% and 82% of our distribution expense in fiscal years 2015, 2014 and 2013, respectively. Distribution expense decreased in fiscal year 2015, despite greater volume shipments in North America, because of lower volume shipments in the segment in Europe, improved cost control in Asia and the sale of the creosote business. Distribution expense was 15.1% of consolidated net sales in fiscal year 2015 and 14.2% in fiscal year 2014. The increase in distribution expense as a percent of net sales in fiscal year 2015 was predominantly due to increased deliveries of inventory to expand a customer's safety stock in local third party warehouses and the sale of the creosote business, which had relatively low distribution expenses.

Selling, general and administrative expenses decreased to \$37.5 million in fiscal year 2015 from \$38.4 million in fiscal year 2014, a decrease of \$0.9 million, or 2.3%. As a percentage of net sales, those expenses were 11.7% and 10.9% in fiscal years 2015 and 2014, respectively. The decrease in fiscal year 2015 over the prior year was primarily because we incurred \$1.3 million of CEO transition costs in the first quarter of fiscal year 2014. Stock-based compensation expenses increased by \$1.6 million during fiscal year 2015 as compared to 2014 (excluding \$1.0 million related to CEO transition costs incurred in fiscal year 2014), but the increase was largely offset by lower professional service fees.

Distribution and Selling, General and Administrative Expenses for Fiscal Year 2014 vs. Fiscal Year 2013

Distribution expenses increased to approximately \$50.3 million in fiscal year 2014 from \$30.3 million in fiscal year 2013, an increase of \$20.0 million, or 66.0%. Distribution expense is heavily concentrated in our electronic chemicals business. The electronic chemicals segment incurred approximately 89 and 82% of our distribution expense in fiscal years 2014 and 2013, respectively. The increase in distribution expense in fiscal year 2014 reflected a greater volume of shipments from UPC-related sales. Distribution expense was 14.2% of consolidated net sales in fiscal year 2014 and 11.5% in fiscal year 2013. The increase in distribution expense as a percent of net sales in fiscal year 2014 was predominantly due to the effect of our Total Chemical Management personnel costs included in distribution expense from the Singapore UPC business acquired in May 2013.

Selling, general and administrative expenses increased to \$38.4 million in fiscal year 2014 from \$29.0 million in fiscal year 2013, an increase of \$9.4 million, or 32.4%. As a percentage of net sales, those expenses were 10.9% and 11.0% in fiscal years 2014 and 2013, respectively. The increase in fiscal year 2014 over the prior year was primarily because of the UPC acquisition in May 2013 and employee-related costs, including stock-based compensation, and professional services.

Adjusted EBITDA, Adjusted Net Income and Adjusted Earnings Per Share

Adjusted EBITDA excludes the effect of acquisition-related restructuring, the realignment of the hydrofluoric acid business, integration and CEO transition expenses. In fiscal year 2015, adjusted EBITDA was \$37.1 million, an increase of \$6.5 million, or 21.2%, as compared to \$30.6 million in fiscal year 2014. The improvement in fiscal 2015 adjusted EBITDA reflects increased sales of electronic chemicals in North America and Asia and the acquisition of our industrial valve lubricants and sealants business, partially offset by weaker sales in Europe, and by approximately \$1.6 million greater expense for stock based compensation.

In fiscal year 2015 adjusted earnings per share was \$1.21, compared to \$0.81 in fiscal year 2014. The increase in fiscal year 2015 in adjusted earnings per share primarily reflects increased sales in our electronic chemicals segment and the acquisition of our industrial valve lubricants and sealants business, partially offset by weakness in Europe.

We provide non-GAAP financial information to complement reported GAAP results with adjusted EBITDA, adjusted net income and adjusted diluted earnings per share. We believe that analysis of our financial performance is enhanced by an understanding of these non-GAAP financial measures. We believe that they aid in evaluating the underlying operational performance of our business, and facilitate comparisons between periods. Non-GAAP financial information, such as adjusted EBITDA, is used

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externally by users of our consolidated financial statements, such as analysts and investors. A similar calculation of adjusted EBITDA is utilized internally for executives' compensation and by our lenders for a key debt compliance ratio.

We define adjusted EBITDA as earnings from continuing operations before interest, taxes, depreciation, amortization, acquisition and integration expenses, restructuring and realignment charges and other designated items. Adjusted EBITDA is a primary measurement of cash flows from operations and a measure of our ability to invest in our operations and provide shareholder returns. Adjusted EBITDA is not intended to represent United States GAAP definitions of cash flow from operations or net income/(loss). Adjusted net income adjusts net income for acquisition and integration expenses, restructuring and realignment charges and other designated items, while diluted adjusted earnings per share is adjusted net income divided by diluted shares outstanding.

Adjusted EBITDA, adjusted net income and diluted adjusted earnings per share should be viewed as supplements to, and not substitutes for, United States GAAP measures of performance.

The table below provides a reconciliation of operating income to adjusted EBITDA.

| | Year Ended July 31, | | |
|---|------------------------|----------|----------|
| | 2015 | 2014 | 2013 |
| | (Amounts in thousands) | | |
| Operating income | \$16,589 | \$3,951 | \$17,180 |
| Other income/(expense) | (496) | (831) | (208) |
| Depreciation and amortization | 19,171 | 18,327 | 8,295 |
| EBITDA | 35,264 | 21,447 | 25,267 |
| Acquisition and integration expenses | 530 | 1,249 | 2,637 |
| CEO transition costs | — | 1,280 | 1,516 |
| Restructuring and realignment charges, excluding accelerated depreciation | 1,264 | 3,925 | — |
| Impairment charges | — | 2,741 | — |
| Adjusted EBITDA | \$37,058 | \$30,642 | \$29,420 |

The table below provides a reconciliation of net income/(loss) to adjusted net income and diluted adjusted earnings per share.

| | Year Ended July 31, | | |
|---|--|---------------------|---------|
| | 2015 | 2014 ⁽¹⁾ | 2013 |
| | (Amounts in thousands, except per share) | | |
| Net income/(loss) | \$12,138 | \$(988) | \$9,348 |
| Items impacting pre-tax income, net of tax: | | | |
| Restructuring and realignment charges | 4,488 | 7,069 | — |
| Acquisition and integration expenses | 344 | 812 | 2,446 |
| CEO transition costs | — | 832 | 1,014 |
| Restructuring income tax expense | — | 1,725 | — |
| Gain on sale of creosote business | (3,541) | — | — |

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| | | | |
|---|----------|---------|----------|
| Environmental site cleanup reserve | 812 | — | — |
| Adjusted net income including discontinued operations | \$14,241 | \$9,450 | \$12,808 |
| Diluted adjusted earnings per share | \$1.21 | \$0.81 | \$1.11 |
| Weighted average diluted shares outstanding | 11,779 | 11,644 | 11,578 |

- (1) Potentially dilutive shares are included in the weighted average diluted shares outstanding for the computation of diluted adjusted earnings per share for fiscal year 2014.

Interest Expense

Interest expense was \$1.4 million in fiscal year 2015, \$2.9 million in fiscal year 2014, and \$1.8 million in fiscal year 2013. In fiscal year 2015, we paid \$30.5 million towards our revolving loan facility, borrowed \$23.5 million on our revolving loan facility for the acquisition of our industrial valve lubricants and sealants business, and reduced the debt from \$60.0 million at the beginning of the fiscal year to \$53.0 million at July 31, 2015.

Income Taxes

We had income tax expense from continuing operations of \$6.7 million, \$1.3 million and \$5.7 million in fiscal years 2015, 2014 and 2013, respectively. Our effective tax rate was 35.7% in fiscal 2015, 471.4% in fiscal 2014 and 37.6% in fiscal year 2013. For fiscal year 2015, the difference between the effective tax rate and the United States statutory rate of 35.0% is primarily due to state income taxes, adjustments of foreign operations, valuation allowances recorded against our current and prior year period operating losses for our Italian subsidiary as a result of restructuring of those operations, offset by the tax benefits from tax credits available to us and effects of foreign currency fluctuations in the U.S. dollar and the revaluation of certain transactions.

Discontinued Operations

Discontinued operations reflected a loss before income taxes of \$203,000 for fiscal year 2013.

In fiscal year 2008, we discontinued operations of our herbicide product line that had comprised the agricultural chemical segment. We incurred costs of \$121,000 in fiscal year 2013 for dismantling the herbicide facility and for medical and other expenses associated with an accident that occurred while the facility was being dismantled.

On March 1, 2012, we sold the business that had comprised our animal health segment to Bayer Healthcare LLC. For fiscal year 2013, \$82,000 was reported as a loss from discontinued operations before income taxes. In fiscal year 2013 the loss included \$57,000 for a post-closing inventory adjustment that was recognized as loss on sale of the business in the first fiscal quarter.

Liquidity and Capital Resources

Our principal requirements for capital funds are for our day-to-day operations, manufacturing and integration activities, and to satisfy our contractual obligations, including for the payment of interest on our indebtedness.

Capital expenditures for fiscal year 2015 were approximately \$13.8 million. Currently we plan to spend a total of approximately \$15.0 million of capital expenses during fiscal year 2016. Capital expenses in fiscal year 2015 were primarily for ERP system implementation in the United States, UPC integration costs and asset investments to support increased electronic chemicals volumes, and normal maintenance and improvements of our facilities. For fiscal year 2016, we expect to continue expending capital for ERP system implementation, including for our Val-Tex subsidiary, and for several production expansions, and normal maintenance and improvements.

We expect to fund our 2016 capital budget predominantly with cash flows from operations, supplemented by borrowings under our credit facility. As of July 31, 2015, our cash and cash equivalents totaled \$7.5 million. Cash and cash equivalents are held for working capital purposes. We do not enter into investments for trading or speculative purposes.

We believe that our existing cash and cash equivalents, cash flows from our operating activities and available borrowing amounts under our credit facility, will be sufficient to meet our anticipated cash needs for the next twelve months. Our future capital requirements will depend on many factors including our growth rate, the expansion of our sales and marketing activities, the introduction of new and enhanced products, the expansion of our manufacturing capacity and the continuing market acceptance of our products. In the event that additional financing is required from outside sources, we may not be able to raise it on terms acceptable to us, if at all. If we are unable to raise additional capital when desired, our business, operating results and financial condition would be adversely affected.

Cash Flows

Net cash provided by operating activities was \$17.6 million in fiscal year 2015, \$40.4 million in fiscal year 2014 and \$20.3 million in fiscal year 2013.

In fiscal year 2015, operating cash flows were favorably impacted by higher sales in our electronic chemicals business resulting in adjusted EBITDA of \$37.1 million. However, we made restructuring and realignment payments of \$5.3 million and paid \$11.2 million more for income taxes during the year ended July 31, 2015 (including taxes relating to the sale of the creosote business). In addition, there was a decrease in accounts payable and accrued liabilities of \$6.6 million, primarily due to the sale of the creosote distribution business and payments for professional fees that were accrued at prior year end. Additionally, the decrease in our cash conversion cycle made in the prior year was not repeated.

In fiscal year 2014, operating cash flows increased significantly due to improvements in KMG's cash conversion cycle. Trade accounts receivable decreased \$2.1 million primarily in our electronic chemicals business in North America, and inventories decreased \$7.9 million primarily in other chemicals due to lower creosote volumes. Accrued liabilities increased by \$7.8 million in part due to restructuring and realignment accruals. Overall, fiscal year 2014 cash flows increased due to the UPC acquisition.

In fiscal year 2013, operating cash flows were favorably impacted by a \$5.3 million increase in accounts payable, primarily from the timing of creosote inventory purchases and by a \$1.8 million decrease in trade accounts receivable. Trade accounts receivable decreased because of lower electronic chemical sales in the fourth quarter of fiscal year 2013 as compared to the same period in the prior year. Operating cash flow was unfavorably impacted by an increase in accounts receivable-other of \$2.6 million, primarily from payments of estimated income taxes for the current period.

In fiscal year 2015, cash used in investing activities was \$18.3 million, compared to cash used in investing activities of \$9.3 million in fiscal year 2014. We paid \$21.9 million for the acquisition of our industrial valve lubricants and sealants business, which was partially offset by \$14.9 million from the sale of our creosote business and \$2.6 million from the sale of our Elwood, Kansas facility. In addition, we spent \$13.8 million for the additions to property, plant and equipment, of which \$10.0 million was for electronic chemicals and \$3.3 million related to our global project to implement a comprehensive financial/enterprise management software solution with SAP.

In fiscal year 2014, cash used in investing activities was \$9.3 million, compared to cash used in investing activities of \$68.1 million in fiscal year 2013. The fiscal year 2014 investing activities were for the additions to property, plant and equipment, of which \$7.0 million was for electronic chemicals and \$2.0 million related to our global project to implement a comprehensive financial/enterprise management software solution with SAP.

In fiscal year 2013, cash used in investing activities was \$68.1 million compared to cash provided by investing activities of \$4.0 million in fiscal year 2012. In fiscal year 2013, \$62.6 million was used to acquire the UPC business of the OM Group, which was net of cash acquired, and \$5.5 million was invested in property, plant and equipment, about \$4.2 million of which was invested in our legacy electronic chemicals business. The rest of the capital expenditure was primarily for various equipment and additions across our other facilities.

In fiscal year 2015, net cash used in financing activities was \$9.1 million. Including the refinancing of our debt, we paid down \$30.5 million on our revolving credit facility and borrowed \$23.5 million on our revolving credit facility to finance the acquisition of our industrial valve lubricants and sealants business.

In fiscal year 2014, net cash used in financing activities was \$26.1 million, out of which \$25.0 million was used to pay down debt on our revolving credit facility.

In fiscal year 2013, net cash provided by financing activities was \$60.0 million including \$61.0 million of net borrowings on our revolving credit facility to finance the purchase of the UPC business.

We paid dividends of \$1.4 million in each of fiscal years 2015, 2014 and 2013.

Working Capital

On October 9, 2014, we refinanced our revolving loan facility and entered into a new credit facility. At July 31, 2015, we had \$53.0 million outstanding under our revolving line of credit of \$150.0 million. The maximum borrowing capacity under the revolving loan was \$94.2 million, after giving effect to a reduction of \$2.8 million for unused letters of credit. The amount available under that revolving facility at July 31, 2015 was limited, however, to approximately \$76.8 million, because of a loan covenant restriction respecting funded debt to pro-forma earnings before interest, taxes and depreciation.

Long Term Obligations

Our long-term debt and current maturities as of July 31, 2015 and July 31, 2014 consisted of the following (in thousands):

| | July 31, | July 31, |
|---|-----------------|-----------------|
| | 2015 | 2014 |
| Senior secured debt: | | |
| Note purchase agreement, maturing on | | |
| December 31, 2015, interest rate of 7.43% | \$— | \$20,000 |
| Revolving loan facility, maturing on April 30, 2018, | | |
| variable interest rates based on LIBOR plus 2.0% | | |
| at July 31, 2014 | — | 40,000 |
| Revolving loan facility, maturing on October 9, 2019, | | |
| variable interest rates based on LIBOR plus 1.0% | | |
| at July 31, 2015 | 53,000 | — |
| Total debt | 53,000 | 60,000 |
| Current maturities of long-term debt | — | — |
| Long-term debt, net of current maturities | \$53,000 | \$60,000 |

In December 2007, we entered into an amended and restated credit agreement and a note purchase agreement, which was subsequently amended. Advances under the revolving loan, as amended, bore interest at 2.155% as of July 31, 2014. The amount outstanding on the revolving loan facility was \$40.0 million at July 31, 2014. The note purchase agreement was for \$20.0 million. Advances under the note purchase agreement bore interest at 7.43% per annum.

We refinanced our then existing revolving loan facility and entered into the Second Amended and Restated Credit Agreement on October 9, 2014 (the “Second Restated Credit Facility”) with Wells Fargo Bank, National Association, Bank of America, N.A., HSBC Bank USA, National Association, and JPMorgan Chase Bank, N.A. The initial advance under the Second Restated Credit Facility was used to repay in full the \$20.0 million outstanding indebtedness under our note purchase agreement with The Prudential Insurance Company of America and Pruco Life Insurance Company, and to pay the \$38.0 million then outstanding on our existing revolving loan facility.

The Second Restated Credit Facility provides for a revolving loan up to \$150 million, including an accordion feature that allows for an additional revolving loan increase of up to \$100 million with approval from our lenders. The amount available under the Second Restated Credit Facility at July 31, 2015 was limited, however, to approximately \$76.8 million, because of a loan covenant restriction respecting funded debt to EBITDA. The maturity date for Second Restated Credit Facility is October 9, 2019.

The revolving loan under the Second Restated Credit Facility bears interest at varying rate of LIBOR plus a margin based on funded debt to earnings before interest, taxes, depreciation and amortization (“EBITDA”), as described in the table.

| Ratio of Funded Debt to EBITDA | Margin |
|---|---------|
| Equal to or greater than 3.0 to 1.0 | 1.875 % |
| Equal to or greater than 2.75 to 1.0, but less than 3.0 to 1.0 | 1.625 % |
| Equal to or greater than 2.50 to 1.0, but less than 2.75 to 1.0 | 1.500 % |
| Equal to or greater than 2.25 to 1.0, but less than 2.50 to 1.0 | 1.375 % |
| Equal to or greater than 2.00 to 1.0, but less than 2.25 to 1.0 | 1.250 % |
| Equal to or greater than 1.50 to 1.0, but less than 2.00 to 1.0 | 1.125 % |
| Less than 1.50 to 1.0 | 1.000 % |

Advances under the revolving loan bore interest at 1.189% as of July 31, 2015. We also incur an unused commitment fee on the unused amount of commitments under the revolving loan facility from 0.30% to 0.15% based on ratio of funded debt to EBITDA.

Advances under the Second Restated Credit Facility are secured by our assets, including stock in subsidiaries, inventory, accounts receivable, equipment, intangible assets, and real property. The Second Restated Credit Facility has restrictive covenants, including requirements that we must maintain a fixed charge coverage ratio of 1.5 to 1.0, a ratio of funded debt to EBITDA (as adjusted for non-cash and unusual, non-recurring, and certain acquisition and integration costs) of 3.25 to 1.0 (with a step-up to 3.5 to 1.0 during an acquisition period with lender consent) and a current ratio of at least 1.5 to 1.0. As of July 31, 2015, we were in compliance with all covenants of the Second Restated Credit Facility.

Attributable only to the Second Restated Credit Facility, at July 31, 2015, principal payments due under our long-term debt agreements as of July 31, 2015 were as follows (in thousands):

| | Total | 2016 | 2017 | 2018 | 2019 | 2020 | Thereafter |
|----------------|----------|------|------|------|------|----------|------------|
| Long-term debt | \$53,000 | \$ — | \$ — | \$ — | \$ — | \$53,000 | \$ — |

Environmental Expenditures

Our capital expenditures and operating expenses for environmental matters, excluding testing, data submission and other costs associated with our product task force participation, were approximately \$2.5 million in fiscal year 2015, \$2.7 million in fiscal year 2014 and \$1.3 million in fiscal year 2013.

We expensed approximately \$977,000 for testing, data submission and other costs associated with our participation in product task forces in fiscal year 2015, and approximately \$667,000 and \$522,000 in fiscal years 2014 and 2013, respectively. We estimate that we will continue to incur additional testing, data submission and other costs of approximately \$1.2 million in fiscal year 2016. Since environmental laws have traditionally become increasingly stringent, costs and expenses relating to environmental control and compliance may increase in the future. While we do not believe that the incremental cost of compliance with existing or future environmental laws and regulations will have a material adverse effect on our business, financial condition or results of operations, we cannot assure that costs of compliance will not exceed current estimates.

Contractual Obligations

Our obligations to make future payments under contracts as of July 31, 2015 are summarized in the following table (in thousands):

| | Payments Due by Period (in thousands) | | | |
|--|---------------------------------------|----------|-----------|-------------------|
| | Total | 1 Year | 2-5 Years | More than 5 Years |
| Long-term debt | \$53,000 | \$— | \$53,000 | \$— |
| Estimated interest payments on debt ⁽¹⁾ | 1,795 | 595 | 1,200 | — |
| Operating leases | 10,811 | 2,772 | 3,801 | 4,238 |
| Other long-term liabilities ⁽²⁾ | 2,384 | 161 | 998 | 1,225 |
| Purchase obligations ⁽³⁾ | 78,296 | 45,790 | 32,506 | — |
| Total | \$146,286 | \$49,318 | \$91,505 | \$5,463 |

(1) Estimated payments are based on interest rates in effect and the amount of outstanding borrowings on our revolving credit facility as of the end of July 2015.

(2) Includes postretirement benefit obligations for a supplemental executive retirement plan for one of our former United States executives and in connection with benefit obligations of our foreign subsidiary; and estimated unused commitment fees on our revolving credit facility.

(3) Consists primarily of raw materials purchase contracts. These are typically not fixed prices arrangements. The prices are based on the prevailing prices.

Outlook for Fiscal Year 2016

Our electronic chemicals business is closely tied to global semiconductor production. In calendar year 2015, the global semiconductor market is expected to show growth of approximately 3%, aided by gains in the data center, automotive and smartphone markets, partially offset by softness in the personal computer market. According to industry forecasts, the global semiconductor market is anticipated to grow less than 3% in calendar 2016, benefiting from relative strength in the automotive and wireless communications markets.

Our other chemicals segment is comprised of our penta business and a lubricants, sealants and related equipment business. We expect continued strong demand for utility poles treated with penta, as utilities in the Western United States upgrade their distribution infrastructure and other pole purchasers throughout North America continue their normal pole maintenance and replacement programs.

We believe that we will experience steady demand for our lubricants, sealants and related equipment, which are used primarily for the maintenance and service of existing energy-related infrastructure. However, the prospect for continued low energy prices is likely to limit drilling and well services while also slowing pipeline infrastructure development, limiting near-term sales growth opportunities in lubricants.

Overall, fiscal 2016 consolidated net sales are forecast to be approximately \$300 million, compared to \$320.5 million in fiscal 2015. The projected decline reflects lower sales in the other chemicals segment due to the divestiture of the creosote distribution business, partially offset by moderate growth in the electronic chemicals segment and a full year contribution from our lubricants business.

Off-Balance Sheet Arrangements

We do not have any off-balance sheet arrangements, such as financing or unconsolidated variable interest entities, other than operating leases.

Recent Accounting Standards

We have considered all recently issued accounting standards updates and SEC rules and interpretive releases, and none of them are expected to have a material impact on our financial statements. See Note 1 to the financial statements included in this report.

Critical Accounting Policies

Our consolidated financial statements are prepared in conformity with accounting principles generally accepted in the United States of America. The preparation of these consolidated financial statements requires the use of estimates, judgments, and assumptions that affect the reported amounts of assets and liabilities at the date of the consolidated financial statements and the reported amounts of revenues and expenses during the periods presented. The significant accounting principles that we believe are the most important to aid in fully understanding our financial results are the following:

Revenue Recognition — Our chemical products are sold in the open market and revenue is recognized when risk of loss and title to the products transfers to customers. In general, risk of loss transfers upon shipment to customers. We also recognize service revenue in connection with technical support services and chemicals delivery and handling at customer facilities. Revenue is recognized as those services are provided.

Allowance for Doubtful Accounts — We record an allowance for doubtful accounts to reduce accounts receivable where we believe accounts receivable may not be collected. A provision for bad debt expense recorded to selling, general and administrative expenses increases the allowance. Accounts receivable that are written off decrease the allowance.

The amount of bad debt expense recorded each period and the resulting adequacy of the allowance at the end of each period are determined using a customer-by-customer analyses of accounts receivable balances each period and subjective assessments of future bad debt exposure. Historically, write offs of accounts receivable balances have been insignificant. The allowance was \$144,000 and \$272,000 at July 31, 2015 and 2014, respectively.

Goodwill — Goodwill represents the excess of the purchase price paid for acquired businesses over the allocated fair value of the related net assets after impairments, if applicable.

We evaluate goodwill for impairment annually, and when an event occurs or circumstances change to suggest that the carrying amount may not be recoverable. We have goodwill of \$14.5 million and \$7.9 million associated with our other chemicals and electronic chemicals segments, respectively, as of July 31, 2015. As part of the goodwill impairment analysis, current accounting standards give us the option to first perform a qualitative assessment to determine whether it is more likely than not that the fair value of a reporting unit is less than its carrying amount, including goodwill. If it is determined that it is more likely than not that the fair value of a reporting unit is greater than its carrying amount, then performing the currently prescribed two-step impairment test is unnecessary. In developing a qualitative assessment to meet the “more-likely-than-not” threshold, each reporting unit with goodwill on its balance sheet is assessed separately and different relevant events and circumstances are evaluated for each unit. If it is determined that it is more likely than not that the fair value of a reporting unit is less than its carrying amount, then the prescribed two-step impairment test is performed. Current accounting standards also give us the option to bypass the qualitative assessment for any reporting unit in any period, and proceed directly to performing the first step of the two-step goodwill impairment test. We conduct our annual impairment test as of July of each year. In 2013, 2014 and 2015, our goodwill impairment tests indicated that the fair value of each of our reporting units is greater than its carrying amount. In conjunction with the sale of our creosote distribution business on January 16, 2015, we wrote off goodwill in the amount of approximately \$662,000 that was previously a part of the wood treating chemicals reporting unit.

Impairment of Long-Lived Assets — Long-lived assets, including property, plant and equipment, and intangible assets, with defined lives, are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount of such assets may not be recoverable. Determination of recoverability is based on an estimate of undiscounted future cash flows resulting from the use of the asset or its disposition. The measurement of an impairment loss for long-lived assets, where management expects to hold and use the asset, are based on the asset’s estimated fair value. Long-lived assets to be disposed of are reported at the lower of carrying amount or fair value. In conjunction with its decision to cease operations at its Bay Point, California facility, we recognized an impairment loss in fiscal year 2014 of \$2.7 million on certain long-lived assets at that facility.

Asset Retirement Obligations — We measure asset retirement obligations based upon the applicable accounting guidance, using certain assumptions including estimates for decommissioning, dismantling and disposal costs. In the event that operational or regulatory issues vary from our estimates, we could incur additional significant charges to income and increases in cash expenditures related to those costs. Certain conditional asset retirement obligations related to facilities have not been recorded in the consolidated financial statements due to uncertainties surrounding the ultimate settlement date and estimate of fair value related to a legal obligation to perform an asset retirement activity. When a reasonable estimate of the ultimate settlement can be made, an asset retirement obligation is recorded and such amounts may be material to the consolidated financial statements in the period in which they are recorded. In conjunction with our decision to exit the Bay Point facility, in fiscal year 2014 we recognized \$3.7 million in asset retirement obligations related to the estimated decommissioning, decontamination, and dismantling costs. See Note 14 to the consolidated financial statements included in item 8 of Part II of this report.

Income Taxes — We follow the liability method of accounting for income taxes in accordance with current accounting standards regarding the accounting for income taxes. Under this method, deferred income taxes are recorded based upon the differences between the financial reporting and tax bases of assets and liabilities and are measured using the enacted tax rates and laws in effect at the time the underlying assets or liabilities are recovered or settled.

When our earnings from foreign subsidiaries are considered to be indefinitely reinvested, no provision for United States income taxes is made for these earnings. If any of the subsidiaries have a distribution of earnings in the form of dividends or otherwise, we would be subject to both United States income taxes (subject to an adjustment for foreign tax credits) and withholding taxes payable to the various foreign countries.

We record a valuation allowance in the reporting period when management believes that it is more likely than not that any deferred tax asset created will not be realized. Management will continue to evaluate the appropriateness of the valuation allowance in the future based upon our operating results.

The calculation of our tax liabilities involves assessing the uncertainties regarding the application of complex tax regulations. We recognize liabilities for tax expenses based on our estimate of whether, and the extent to which, additional taxes will be due. If we determine that payment of these amounts is unnecessary, we reverse the liability and recognize a tax benefit when the determination is made. We record an additional charge in our provision for taxes in the period in which we determine that the recorded tax liability is less than we expect the ultimate assessment to be.

Inventory— Inventories are valued at the lower of cost or market. For certain products, cost is generally determined using the first-in, first-out (“FIFO”) method. For certain other products we utilize a weighted-average cost. We record inventory obsolescence as a reduction in inventory when considered unsellable. We review inventories periodically to ensure the valuation of these assets is recorded at the lower of cost or market and to record an obsolescence reserve when inventory is considered unsellable. During the fiscal years ended July 31, 2015 and 2014, we recognized inventory valuation loss of \$941,000 and \$634,000, respectively. As of July 31, 2015 and 2014, we had \$481,000 and \$290,000, respectively, of reserves for inventory obsolescence.

Disclosure Regarding Forward Looking Statements

This report includes “forward-looking statements” within the meaning of Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities Exchange Act of 1934, as amended. These forward-looking statements include information about possible or assumed future results of our operations. All statements, other than statements of historical facts, included or incorporated by reference in this report that address activities, events or developments that we expect or anticipate may occur in the future, including such things as future capital expenditures, business strategy, competitive strengths, goals, growth of our business and operations, plans and references to future successes may be considered forward-looking statements. Also, when we use words such as “anticipate,” “believe,” “estimate,” “intend,” “plan,” “project,” “forecast,” “may,” “should,” “budget,” “goal,” “expect,” “probably” or similar expressions, we are making forward-looking statements. Many risks and uncertainties may impact the matters addressed in these forward-looking statements. Our forward-looking statements speak only as of the date made and we will not update forward-looking statements unless the securities laws require us to do so.

Some of the key factors which could cause our future financial results and performance to vary from those expected include:

- the loss or significant reduction in business from primary customers;
- the loss of key suppliers;
- the integration of our UPC acquisition taking longer or being more costly than currently believed, or the failure to achieve all the planned benefits of that integration;
- the impact of penta being banned or restricted as a persistent organic pollutant under the Stockholm Convention Treaty;
- the implementation of a new enterprise resource planning system taking longer or being more costly than currently believed;
- our ability to implement productivity improvements, cost reduction initiatives or facilities expansions;
- market developments affecting, and other changes in, the demand for our products and the entry of new competitors or the introduction of new competing products;
- availability or increases in the price of energy, affecting our primary raw materials and active ingredients;
- depressed oil and gas prices and price volatility affecting demand for our industrial lubricants products by the energy exploration and production and gas transmission industries;
- the timing of planned capital expenditures;
- our ability to identify, develop or acquire, and market additional product lines and businesses necessary to implement our business strategy and our ability to finance such acquisitions and development;
- our ability to realize the anticipated benefits of business acquisitions and to successfully integrate previous or future business acquisitions;
- the condition of the capital markets generally, which will be affected by interest rates, foreign currency fluctuations and general economic conditions;
- cost and other effects of legal and administrative proceedings, settlements, investigations and claims, including environmental liabilities which may not be covered by indemnity or insurance;
- the effects of weather, earthquakes, other natural disasters and terrorist attacks;
- the ability to obtain registration and re-registration of our products under applicable law;
- exposure to movements in foreign currency exchange rates as a result of the geographic diversity of our operations;
- the political and economic climate in the foreign or domestic jurisdictions in which we conduct business; and
- other United States or foreign regulatory or legislative developments which affect the demand for our products generally or increase the environmental compliance cost for our products or impose liabilities on the manufacturers and distributors of such products.

The information contained in this report, including the information set forth under the heading “Risk Factors”, identifies additional factors that could cause our results or performance to differ materially from those we express in our forward-looking statements. Although we believe that the assumptions underlying our forward-looking statements are reasonable, any of these assumptions and, therefore, the forward-looking statements based on these assumptions,

could themselves prove to be inaccurate. In light of the significant uncertainties inherent in the forward-looking statements which are included in this report and the exhibits and

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other documents incorporated herein by reference, our inclusion of this information is not a representation by us or any other person that our objectives and plans will be achieved.

ITEM 7A. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

We are exposed to certain market risks in the ordinary course of our business, arising primarily from changes in interest rates and to a lesser extent foreign currency exchange rate fluctuations. Currently, we do not utilize derivative financial instruments or hedging transactions to manage that risk.

Interest Rate Sensitivity

As of July 31, 2015, we had no fixed rate debt.

Our variable rate debt as of July 31, 2015 consisted of a revolving loan advanced under the Second Restated Credit Facility with an interest rate of 1.190% (1.0% plus LIBOR), maturing on October 9, 2019. On July 31, 2015, we had \$53.0 million borrowed on the revolving loan under that facility. Currently advances bear interest at LIBOR plus 1.0%.

Based on the outstanding balance of our variable rate debt under the Second Restated Credit Facility at July 31, 2015, a 1.0% change in the interest rate as of July 31, 2015 would result in an additional charge of approximately \$500,000 in annual interest expense.

Foreign Currency Exchange Rate Sensitivity

We are exposed to fluctuations in foreign currency exchange rates from international operations in the electronic chemicals segment. Our international operations in Europe and Singapore use different functional currencies, including the Euro, Great Britain Pound and Singapore Dollar. The U.S. dollar is our consolidated reporting currency. Currency translation gains and losses result from the process of translating those operations from the functional currency into our reporting currency. Currency translation gains and losses have no impact on the consolidated statements of income and are recorded as accumulated other comprehensive income or loss within stockholders' equity in our consolidated balance sheets. Assets and liabilities have been translated using exchange rates in effect at the balance sheet dates. Revenues and expenses have been translated using the average exchange rates during the period.

We recognized a foreign currency translation loss of \$10.2 million in fiscal year 2015, and gains of \$3.1 million and \$1.8 million in fiscal years 2014 and 2013, respectively, each of which were included in accumulated other comprehensive income/(loss) in the consolidated balance sheets. At July 31, 2015, the cumulative foreign currency translation loss reflected in accumulated other comprehensive income/(loss) was \$9.5 million.

Additionally we have limited exposure to certain transactions denominated in a currency other than the functional currency in our European and Singapore operations. Accordingly, we recognize exchange gains or losses in our consolidated statement of income from these transactions. Foreign currency exchange gains during fiscal year 2015 were \$62,000.

ITEM 8. FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA

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REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

The Board of Directors and Stockholders

KMG Chemicals, Inc.:

We have audited the accompanying consolidated balance sheets of KMG Chemicals, Inc. and subsidiaries (the “Company”) as of July 31, 2015 and 2014, and the related consolidated statements of income, comprehensive income, stockholders’ equity, and cash flows for each of the years in the three-year period ended July 31, 2015. In connection with our audits of the consolidated financial statements, we also have audited the related financial statement Schedule II. These consolidated financial statements and the related financial statement Schedule II are the responsibility of the Company’s management. Our responsibility is to express an opinion on these consolidated financial statements and financial statement schedule based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of KMG Chemicals, Inc. and subsidiaries as of July 31, 2015 and 2014, and the results of their operations and their cash flows for each of the years in the three-year period ended July 31, 2015, in conformity with U.S. generally accepted accounting principles. Also in our opinion, the related financial statement Schedule II, when considered in relation to the basic consolidated financial statements taken as a whole, presents fairly, in all material respects, the information set forth therein.

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), KMG Chemicals, Inc.’s internal control over financial reporting as of July 31, 2015, based on criteria established in Internal Control—Integrated Framework (2013) issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO), and our report dated November 27, 2015 expressed an adverse opinion on the effectiveness of KMG Chemicals, Inc.’s internal control over financial reporting.

/s/ KPMG LLP
Houston, Texas
November 27, 2015

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

The Board of Directors and Stockholders

KMG Chemicals, Inc.:

We have audited KMG Chemicals, Inc.'s ("the Company") internal control over financial reporting as of July 31, 2015, based on criteria established in Internal Control—Integrated Framework (2013) issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO). KMG Chemicals, Inc.'s management is responsible for maintaining effective internal control over financial reporting and for its assessment of the effectiveness of internal control over financial reporting, included in the accompanying Management's Report on Internal Control over Financial Reporting. Our responsibility is to express an opinion on KMG Chemicals, Inc.'s internal control over financial reporting based on our audit.

We conducted our audit in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether effective internal control over financial reporting was maintained in all material respects. Our audit included obtaining an understanding of internal control over financial reporting, assessing the risk that a material weakness exists, and testing and evaluating the design and operating effectiveness of internal control based on the assessed risk. Our audit also included performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion.

A company's internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. A company's internal control over financial reporting includes those policies and procedures that (1) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; (2) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and (3) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the company's assets that could have a material effect on the financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

A material weakness is a deficiency, or a combination of deficiencies, in internal control over financial reporting, such that there is a reasonable possibility that a material misstatement of the company's annual or interim financial statements will not be prevented or detected on a timely basis. Material weaknesses have been identified and included in management's assessment in Item 9A related to the Company's control environment (sufficient personnel with appropriate knowledge, skills and experience), risk assessment processes (identification and mitigation of financial reporting risks associated with an ERP system implementation) and monitoring activities (review and supervision of internal controls compliance by subsidiaries).

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the consolidated balance sheets of the Company as of July 31, 2015 and 2014 and the related consolidated statements of income, comprehensive income, stockholders' equity, cash flows, and related financial statement Schedule II for each of the fiscal years in the three-year period then ended. These material weaknesses were considered in determining the nature, timing, and extent of audit tests applied in our audit of the fiscal year 2015

consolidated financial statements, and this report does not affect our report dated November 27, 2015, which expressed an unqualified opinion on those consolidated financial statements.

In our opinion, because of the effect of the aforementioned material weaknesses on the achievement of the objectives of the control criteria, KMG Chemicals, Inc. has not maintained effective internal control over financial reporting as of July 31, 2015, based on criteria established in Internal Control—Integrated Framework (2013) issued by the Committee of Sponsoring Organizations of the Treadway Commission.

We do not express an opinion or any other form of assurance on management's statements referring to corrective actions taken after July 31, 2015, relative to the aforementioned material weaknesses in internal control over financial reporting.

/s/ KPMG LLP
Houston, Texas
November 27, 2015

KMG CHEMICALS, INC. AND SUBSIDIARIES

CONSOLIDATED BALANCE SHEETS

AS OF JULY 31, 2015 AND 2014

(In thousands, except for share and per share amounts)

| | 2015 | 2014 |
|--|-----------|-----------|
| Assets | | |
| Current assets | | |
| Cash and cash equivalents | \$7,517 | \$19,252 |
| Accounts receivable | | |
| Trade, net of allowances of \$144 at July 31, 2015 and \$272 at July 31, 2014 | 36,887 | 40,176 |
| Other | 3,668 | 1,904 |
| Inventories, net | 42,082 | 45,268 |
| Current deferred tax assets | 2,953 | 1,577 |
| Prepaid expenses and other | 3,738 | 3,476 |
| Total current assets | 96,845 | 111,653 |
| Property, plant and equipment, net | 80,589 | 92,450 |
| Deferred tax assets | 131 | 442 |
| Goodwill | 22,408 | 12,595 |
| Intangible assets, net | 36,560 | 28,353 |
| Restricted cash | 1,000 | 1,000 |
| Other assets, net | 4,826 | 4,365 |
| Total assets | \$242,359 | \$250,858 |
| Liabilities & stockholders' equity | | |
| Current liabilities | | |
| Accounts payable | \$35,980 | \$36,690 |
| Accrued liabilities | 9,602 | 16,986 |
| Employee incentive accrual | 4,852 | 4,575 |
| Total current liabilities | 50,434 | 58,251 |
| Long-term debt | 53,000 | 60,000 |
| Deferred tax liabilities | 13,075 | 9,881 |
| Other long-term liabilities | 2,429 | 2,520 |
| Total liabilities | 118,938 | 130,652 |
| Commitments and contingencies | | |
| Stockholders' equity | | |
| Preferred stock, \$.01 par value, 10,000,000 shares authorized, none issued | — | — |
| Common stock, \$.01 par value, 40,000,000 shares authorized, 11,690,439 shares issued and outstanding at July 31, 2015 and 11,649,001 shares issued and outstanding at July 31, 2014 | 117 | 116 |
| Additional paid-in capital | 31,676 | 28,886 |
| Accumulated other comprehensive income/(loss) | (9,667) | 645 |
| Retained earnings | 101,295 | 90,559 |
| Total stockholders' equity | 123,421 | 120,206 |
| Total liabilities and stockholders' equity | \$242,359 | \$250,858 |

See accompanying notes to consolidated financial statements.

KMG CHEMICALS, INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF INCOME

FOR THE YEARS ENDED JULY 31, 2015, 2014 AND 2013

(In thousands, except per share amounts)

| | 2015 | 2014 | 2013 |
|--|-----------|-----------|-----------|
| Net sales | \$320,498 | \$353,406 | \$263,311 |
| Cost of sales | 211,021 | 249,907 | 186,841 |
| Gross profit | 109,477 | 103,499 | 76,470 |
| Distribution expenses | 48,523 | 50,251 | 30,312 |
| Selling, general and administrative expenses | 37,461 | 38,421 | 28,978 |
| Restructuring charges | 1,279 | 6,359 | — |
| Realignment charges | 5,625 | 4,517 | — |
| Operating income | 16,589 | 3,951 | 17,180 |
| Other income/(expense) | | | |
| Interest expense, net | (1,407) | (2,854) | (1,771) |
| Gain on sale of creosote distribution business, net | 5,448 | — | — |
| Other non-operating expense | (1,250) | — | — |
| Other, net | (496) | (831) | (208) |
| Total other income/(expense), net | 2,295 | (3,685) | (1,979) |
| Income from continuing operations before income taxes | 18,884 | 266 | 15,201 |
| Provision for income taxes | (6,746) | (1,254) | (5,715) |
| Income/(loss) from continuing operations | 12,138 | (988) | 9,486 |
| Discontinued operations | | | |
| Loss from discontinued operations, before income taxes | — | — | (203) |
| Income tax benefit | — | — | 65 |
| Loss from discontinued operations | — | — | (138) |
| Net income/(loss) | \$12,138 | \$(988) | \$9,348 |
| Earnings/(loss) per share | | | |
| Basic | | | |
| Income/(loss) from continuing operations | \$1.04 | \$(0.09) | \$0.82 |
| Loss from discontinued operations | — | — | (0.01) |
| Net income/(loss) | \$1.04 | \$(0.09) | \$0.81 |
| Diluted | | | |
| Income/(loss) from continuing operations | \$1.03 | \$(0.09) | \$0.82 |
| Loss from discontinued operations | — | — | (0.01) |
| Net income/(loss) | \$1.03 | \$(0.09) | \$0.81 |
| Weighted average shares outstanding | | | |
| Basic | 11,673 | 11,615 | 11,487 |
| Diluted | 11,779 | 11,615 | 11,578 |

See accompanying notes to consolidated financial statements.

KMG CHEMICALS, INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME

FOR THE YEARS ENDED JULY 31, 2015, 2014 AND 2013

(In thousands)

| | 2015 | 2014 | 2013 |
|---|----------|----------|----------|
| Net income/(loss) | \$12,138 | \$(988) | \$9,348 |
| Other comprehensive income/(loss) | | | |
| Foreign currency translation gain/(loss) | (10,202) | 3,149 | 1,835 |
| Pension and other post-retirement benefit liability adjustments | (110) | — | — |
| Total other comprehensive income/(loss) | (10,312) | 3,149 | 1,835 |
| Total comprehensive income | \$1,826 | \$2,161 | \$11,183 |

See accompanying notes to consolidated financial statements.

KMG CHEMICALS, INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF STOCKHOLDERS' EQUITY

FOR THE YEARS ENDED JULY 31, 2015, 2014 AND 2013

(In thousands)

| | Common Stock Shares | Par Value | Additional Paid- In Capital | Accumulated Other Comprehensive Income (Loss) | Retained Earnings | Total Stockholders' Equity |
|---|------------------------|--------------|-----------------------------------|--|----------------------|----------------------------------|
| BALANCE AT JULY 31, 2012 | 11,406 | \$ 114 | \$ 26,022 | \$ (4,339) | \$ 84,970 | \$ 106,767 |
| Cash dividends (\$0.12 per share) | | | | | (1,378) | (1,378) |
| Stock options/warrants exercised | 70 | | 70 | | | 70 |
| Restricted stock issued | 46 | 1 | (1) | | | — |
| Stock-based compensation expense | | | 446 | | | 446 |
| Tax benefit from stock-based awards | | | 529 | | | 529 |
| Other | | | (377) | | | (377) |
| Net income | | | | | 9,348 | 9,348 |
| Gain on foreign currency translation | | | | 1,835 | | 1,835 |
| BALANCE AT JULY 31, 2013 | 11,522 | \$ 115 | \$ 26,689 | \$ (2,504) | \$ 92,940 | \$ 117,240 |
| Cash dividends (\$0.12 per share) | | | | | (1,393) | (1,393) |
| Stock options/warrants exercised | 47 | | | | | — |
| Restricted stock issued | 80 | 1 | (1) | | | — |
| Stock-based compensation expense | | | 2,231 | | | 2,231 |
| Tax benefit from stock-based awards | | | 328 | | | 328 |
| Other | | | (361) | | | (361) |
| Net loss | | | | | (988) | (988) |
| Gain on foreign currency translation | | | | 3,149 | | 3,149 |
| BALANCE AT JULY 31, 2014 | 11,649 | \$ 116 | \$ 28,886 | \$ 645 | \$ 90,559 | \$ 120,206 |
| Cash dividends (\$0.12 per share) | | | | | (1,402) | (1,402) |
| Restricted stock issued | 41 | 1 | | | | 1 |
| Stock-based compensation expense | | | 2,766 | | | 2,766 |
| Tax benefit from stock-based awards | | | 24 | | | 24 |
| Net income | | | | | 12,138 | 12,138 |
| Gain/(loss) on foreign currency translation | | | | (10,202) | | (10,202) |
| Pension liability adjustment | | | | (110) | | (110) |
| BALANCE AT JULY 31, 2015 | 11,690 | \$ 117 | \$ 31,676 | \$ (9,667) | \$ 101,295 | \$ 123,421 |

See accompanying notes to consolidated financial statements.

KMG CHEMICALS, INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF CASH FLOWS

FOR THE YEARS ENDED JULY 31, 2015, 2014 AND 2013

(In thousands)

| | 2015 | 2014 | 2013 |
|---|----------|----------|----------|
| Cash flows from operating activities | | | |
| Net income /(loss) | \$12,138 | \$(988) | \$9,348 |
| Adjustments to reconcile net income/(loss) to net cash provided by operating activities | | | |
| Depreciation and amortization | 13,531 | 14,117 | 8,295 |
| Depreciation related to restructuring and realignment | 5,640 | 4,210 | — |
| Non-cash Impairment charges | — | 2,741 | — |
| Amortization of loan costs included in interest expense | 153 | 60 | 41 |
| Stock-based compensation expense | 2,766 | 2,231 | 446 |
| Bad debt expense | — | 128 | 208 |
| Allowance for excess and obsolete inventory | 941 | 634 | (355) |
| Gain on sale of creosote business | (5,448) | — | — |
| Loss on sale of animal health business | — | — | 57 |
| (Gain) loss on disposal of property | — | (28) | 59 |
| Deferred income tax expense/(benefit) | (3,532) | (2,227) | 1,247 |
| Tax benefit from stock-based awards | 23 | (328) | (529) |
| Changes in operating assets and liabilities, net of effects of acquisition | | | |
| Accounts receivable — trade | 1,265 | 2,137 | 1,813 |
| Accounts receivable — other | (1,884) | 746 | (2,593) |
| Inventories | (740) | 7,861 | (1,018) |
| Other current and non-current assets | (633) | 822 | (654) |
| Accounts payable | 1,234 | 398 | 5,301 |
| Accrued liabilities and other | (7,886) | 7,844 | (1,394) |
| Net cash provided by operating activities | 17,568 | 40,358 | 20,272 |
| Cash flows from investing activities | | | |
| Additions to property, plant and equipment | (13,821) | (9,497) | (5,505) |
| Disposals of property, plant and equipment | 2,572 | 74 | — |
| Acquisition of Ultra Pure Chemicals, net of cash acquired | — | 149 | (62,608) |
| Acquisition of industrial lubricants business | (21,938) | — | — |
| Proceeds from sale of creosote business | 14,899 | — | — |
| Net cash used in investing activities | (18,288) | (9,274) | (68,113) |
| Cash flows from financing activities | | | |
| Net borrowings/(payments) under revolving loan facility | (40,000) | (25,000) | 61,000 |
| Deferred financing costs | (666) | — | (229) |
| Proceeds from borrowing under New Credit Facility | 59,100 | — | — |
| Net payments under New Credit Facility | (6,100) | — | — |
| Principal payments on borrowings on term loan | (20,000) | — | — |
| Proceeds from exercise of stock options and warrants | — | — | 70 |
| Tax benefit from stock-based awards | (23) | 328 | 529 |
| Payment of dividends | (1,402) | (1,393) | (1,378) |
| Net cash provided by/(used in) financing activities | (9,091) | (26,065) | 59,992 |
| Effect of exchange rate changes on cash | (1,924) | 284 | 165 |

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| | | | |
|--|----------|----------|----------|
| Net increase (decrease) in cash and cash equivalents | (11,735) | 5,303 | 12,316 |
| Cash and cash equivalents at the beginning of year | 19,252 | 13,949 | 1,633 |
| Cash and cash equivalents at end of year | \$7,517 | \$19,252 | \$13,949 |
| Supplemental disclosures of cash flow information | | | |
| Cash paid for interest | \$1,321 | \$2,562 | \$1,709 |
| Cash paid for income taxes | \$12,182 | \$865 | \$5,854 |
| Supplemental disclosure of non-cash investing activities | | | |
| Purchase of property, plant and equipment through accounts payable | \$882 | \$1,135 | \$649 |
| Accrued liabilities under industrial lubricants business acquisition | \$1,798 | \$— | \$— |
| See accompanying notes to consolidated financial statements. | | | |

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

General — KMG Chemicals, Inc. (the “Company”) is involved principally in the manufacture, formulation and distribution of specialty chemicals in carefully focused markets through its three wholly-owned subsidiaries, KMG Electronic Chemicals, Inc. (“KMG EC”), KMG-Bernuth, Inc. (“KMG Bernuth”) and KMG Val-Tex, LLC (“Val-Tex”).

In its electronic chemicals business, the Company sells high purity wet process chemicals to the semiconductor industry. In the wood treating chemicals business, the Company sells industrial wood treating chemicals based on pentachlorophenol (“penta”). In its industrial valve lubricants and sealants business, the Company sells industrial lubricants and sealants, primarily to the oil and gas storage, pipeline and gas distribution markets, as well as related products, such as lubrication equipment and fittings. The Company operates its electronic chemicals business through KMG EC in North America and through KMG Italia, S.r.l. (“KMG Italia”) and KMG Electronic Chemicals Holdings S.a.r.l (“KMG Lux”) (and its subsidiaries) in Europe and Asia. That business has facilities in the United States, the United Kingdom, France, Italy and Singapore. In the wood treating business the Company manufactures penta at its plant in Matamoros, Mexico through KMG de Mexico (“KMEX”), a Mexican corporation which is a wholly-owned subsidiary of KMG Bernuth. The Company sells its wood treating chemicals in the United States, Mexico and Canada. The Company operates its industrial valve lubricants and sealants business through Val-Tex, a Texas limited liability company. That business has one facility in the United States. The Company has two reportable segments, electronic chemicals and other chemicals. The other chemicals segment includes the Company’s wood treating chemicals business and its industrial valve lubricants and sealants business. See Note 13.

Principles of Consolidation — The consolidated financial statements include the accounts of KMG Chemicals, Inc. and its subsidiaries. All significant intercompany accounts and transactions have been eliminated in consolidation.

Use of Estimates — The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America (“GAAP”) requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from these estimates.

Reclassifications — Certain reclassifications of prior year amounts have been made to conform to current year presentation. These reclassifications had no impact on net income (loss) or total stockholders’ equity as previously reported.

Cash and Cash Equivalents — The Company considers all investments with original maturities of three months or less when purchased to be cash equivalents.

Restricted Cash — Restricted cash includes cash balances which are legally or contractually restricted to use. The Company’s restricted cash as of July 31, 2015 and 2014 includes proceeds that were placed in escrow in connection with the sale of the animal health business. See Note 12.

Fair Value of Financial Instruments — The carrying value of financial instruments, including cash and cash equivalents, accounts receivable, and accounts payable approximate fair value because of the relatively short maturity of these instruments. The fair value of the Company’s debt at July 31, 2015 and 2014 approximated its carrying value since the debt obligations bear interest at a rate consistent with market rates.

Accounts Receivable — The Company's trade accounts receivables are primarily from sales of products worldwide. The Company extends credit based on an evaluation of the customer's financial condition, generally without requiring collateral. Exposure to losses on receivables is dependent on each customer's financial condition. At July 31, 2015 there was one customer that represented approximately 9.1% of the Company's accounts receivable. At July 31, 2014 there was one customer that represented approximately 15% of the Company's accounts receivable.

The Company records an allowance for doubtful accounts to reduce accounts receivable when the Company believes an account may not be collected. A provision for bad debt expense is recorded to selling, general and administrative expenses. The amount of bad debt expense recorded each period and the resulting adequacy of the allowance at the end of each period are determined using a customer-by-customer analyses of accounts receivable balances each period and the Company's assessment of future bad debt exposure. Historically, write offs of accounts receivable balances have been insignificant. The allowance was \$144,000 and \$272,000 at July 31, 2015 and 2014, respectively.

Inventories — Inventories are valued at the lower of cost or market. For certain products, cost is generally determined using the first-in, first-out ("FIFO") method. For certain other products the Company utilizes a weighted-average cost. The Company records a reserve for inventory obsolescence as a reduction in its inventory when considered not salable.

Property, Plant, and Equipment — Property, plant, and equipment are stated at cost less accumulated depreciation and amortization. Major renewals and betterments are capitalized. Repairs and maintenance costs are expensed as incurred.

Depreciation for equipment commences once placed in service, and depreciation for buildings and leasehold improvements commences once they are ready for their intended use. Depreciable life is determined through economic analysis. Depreciation for financial statement purposes is provided on the straight-line method.

The estimated useful lives of classes of assets are as follows:

| Asset Class | Life (Years) |
|------------------------|-----------------------------|
| Building | 15 to 30 |
| Plant | 10 to 18 |
| Equipment | 3 to 15 |
| Leasehold improvements | Remaining life of the lease |

Depreciation expense was approximately \$17.5 million and \$16.5 million (including accelerated depreciation of \$5.6 million and \$4.2 million) in fiscal years 2015 and 2014, respectively. See Notes 4 and 14.

Intangible Assets — Identifiable intangible assets with a defined life are amortized using a straight-line or accelerated method over the useful lives of the assets. Identifiable intangible assets of an indefinite life are not amortized. These assets are required to be tested for impairment at least annually. If this review indicates that impairment has occurred, the carrying value of the intangible assets will be adjusted to fair value. Based on an assessment of qualitative factors, in accordance with GAAP, it was determined that there were no events or circumstances that would lead the Company to a determination that is more likely than not that the fair value of the applicable assets was less than its carrying value as of July 31, 2015 and 2014. The Company therefore concluded that its indefinite lived intangible assets were not impaired as of July 31, 2015 and 2014. It is the Company's policy to expense costs as incurred in connection with the renewal or extension of its intangible assets.

Goodwill — Goodwill represents the excess of the purchase price paid for acquired businesses over the allocated fair value of the related net assets after impairments, if applicable.

The Company evaluates goodwill for impairment annually, and when an event occurs or circumstances change to suggest that the carrying amount may not be recoverable. The Company has goodwill of \$14.5 million and \$7.9 million associated with its other chemicals and electronic chemicals segments, respectively, as of July 31, 2015. As part of the goodwill impairment analysis, current accounting standards give us the option to first perform a qualitative assessment to determine whether it is more likely than not that the fair value of a reporting unit is less than its carrying amount, including goodwill. If it is determined that it is more likely than not that the fair value of a reporting unit is greater than its carrying amount, then performing the currently prescribed two-step impairment test is unnecessary. In developing a qualitative assessment to meet the "more-likely-than-not" threshold, each reporting unit with goodwill on its balance sheet is assessed separately, and different relevant events and circumstances are evaluated for each unit. If it is determined that it is more likely than not that the fair value of a reporting unit is less than its carrying amount, then the prescribed two-step impairment test is performed. Current accounting standards also give us the option to bypass the qualitative assessment for any reporting unit in any period, and proceed directly to performing the first step of the two-step goodwill impairment test. The Company conducts its annual impairment test as of July of each year. In 2015, 2014 and 2013, the Company's goodwill impairment tests indicated that the fair value of each of its reporting units is greater than its carrying amount. In conjunction with the sale of the creosote business on January 16, 2015, the Company wrote off goodwill in the amount of approximately \$662,000 that was previously a part of the wood treating

chemicals reporting unit.

Asset retirement obligation — The Company measures asset retirement obligations based upon the applicable accounting guidance, using certain assumptions including estimates for decommissioning, dismantling and disposal costs. In the event that operational or regulatory issues vary from management's estimates, the Company could incur additional significant charges to income and increases in cash expenditures related to those costs. Certain conditional asset retirement obligations related to facilities have not been recorded in the consolidated financial statements due to uncertainties surrounding the ultimate settlement date and estimate of fair value related to a legal obligation to perform an asset retirement activity. When a reasonable estimate of the ultimate settlement can be made, an asset retirement obligation is recorded and such amounts may be material to the consolidated financial statements in the period in which they are recorded. In conjunction with its decision to exit the Bay Point facility, in fiscal year 2014 the Company recognized \$3.7 million in asset retirement obligations related to the decommissioning, decontamination, and dismantling costs for which it is obligated under its manufacturing agreement. See Note 14.

Impairment of Long-Lived Assets — Long-lived assets, including property, plant and equipment, and intangible assets with defined lives, are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount of such assets may not be recoverable. The determination of recoverability is based on an estimate of undiscounted future cash flows resulting

from the use of the asset and its disposition. The measurement of an impairment loss for long-lived assets, where management expects to hold and use the asset, are based on the asset's estimated fair value. Long-lived assets to be disposed of are reported at the lower of carrying amount or fair value. The Company recognized an impairment loss in fiscal year 2014 of \$2.7 million on certain long-lived assets at the Bay Point, California facility where Chemtrade toll manufactures for the Company.

Revenue Recognition — The Company's chemical products are sold in the open market and revenue is recognized when risk of loss and title to the products transfers to customers. In general, risk of loss transfers upon shipment to customers. The Company also recognizes service revenue in connection with technical support services and chemicals delivery and handling at customer facilities. Revenue is recognized as those services are provided.

Cost of Sales — Cost of sales includes inbound freight charges, purchasing and receiving costs, depreciation, inspection costs and internal transfer costs. In the case of products manufactured by the Company, direct and indirect manufacturing costs and associated plant administrative expenses are included as well as laid-in cost of raw materials consumed in the manufacturing process.

Distribution Expenses — These expenses include outbound freight, depreciation, storage and handling expenses and other miscellaneous costs (including depreciation and amortization) associated with product storage, handling and distribution.

Selling, General and Administrative Expenses — These expenses include selling expenses, corporate headquarters' expenses, amortization of intangible assets and environmental regulatory support expenses.

Shipping and Handling Costs — Shipping and handling costs are included in cost of sales and distribution expenses. Inbound freight charges and internal transfer costs are included in cost of sales. Product storage and handling costs and the cost of distributing products to the Company's customers are included in distribution expenses.

Income Taxes — The Company follows the liability method of accounting for income taxes in accordance with current accounting standards regarding the accounting for income taxes. Under this method, deferred income taxes are recorded based upon the differences between the financial reporting and tax bases of assets and liabilities and are measured using the enacted tax rates and laws in effect at the time the underlying assets or liabilities are recovered or settled.

When the Company's earnings from foreign subsidiaries are considered to be indefinitely reinvested, no provision for United States income taxes is made for these earnings. If any of the subsidiaries have a distribution of earnings in the form of dividends or otherwise, the Company would be subject to both United States income taxes (subject to an adjustment for foreign tax credits) and withholding taxes payable to the various foreign countries.

The Company records a valuation allowance in the reporting period when management believes that it is more likely than not that any deferred tax asset created will not be realized. Management will continue to evaluate the appropriateness of the valuation allowance in the future based upon the operating results of the Company.

The calculation of the Company's tax liabilities involves assessing the uncertainties regarding the application of complex tax regulations. The Company recognizes liabilities for tax expenses based on its estimate of whether, and the extent to which, additional taxes will be due. If the Company determines that payment of these amounts is

unnecessary, the Company reverses the liability and recognizes a tax benefit during the period in which it determines that the liability is no longer necessary. The Company records an additional charge in its provision for taxes when the determination is made. See Note 5.

Earnings Per Share — Basic earnings per common share amounts are calculated using the average number of common shares outstanding during each period. Diluted earnings per share assumes the issuance of restricted stock under time-based and performance-based awards, and the exercise of stock options having exercise prices less than the average market price during the applicable period, using the treasury stock method. Time-based and performance-based awards have no liquidation or dividend rights and are thus are not considered participating securities.

Foreign Currency Translation — The functional currency of the Company's Mexico operations is the U.S. Dollar. As a result, monetary assets and liabilities for KMEX are re-measured to U.S. dollars at current rates at the balance sheet dates, income statement items are re-measured at the average monthly exchange rates for the dates those items were recognized, and certain assets (including plant and production equipment) are re-measured at historical exchange rates. Foreign currency transaction gains and losses are included in the statement of operations as incurred along with gains and losses from currency re-measurement. These gains and losses were nominal in fiscal years 2015, 2014 and 2013.

The Company's international operations in the electronic chemicals business are in Europe and Singapore, and use local currencies as the functional currency, including the GB Pound, Euro and Singapore Dollar. The translation adjustment resulting from currency translation of the local currency into the reporting currency (U.S. Dollar) is included as a separate component of stockholders' equity. The assets and liabilities have been translated from local currencies into U.S. Dollars using exchange rates in

effect at the balance sheet dates. Results of operations have been translated using the average exchange rates during the period. Foreign currency translation resulted in a translation adjustment gains/(losses) of \$(10.2) million, \$3.1 million and \$1.8 million in fiscal years 2015, 2014 and 2013, respectively, each of which are included in accumulated other comprehensive income/(loss) in the consolidated balance sheets.

Stock-Based Compensation — The Company's stock-based compensation expense is based on the fair value of the award measured on the date of grant. For stock option awards, the grant date fair value is measured using a Black-Scholes option valuation model. For stock awards, the Company's stock price on the date of the grant is used to measure the grant date fair value. For awards of stock which are based on a fixed monetary value the grant date fair value is based on the monetary value. Stock-based compensation costs are recognized as an expense over the requisite service period of the award using the straight-line method.

Recent Accounting Standards

The Company has considered all recently issued accounting standards updates and SEC rules and interpretive releases.

In April 2014, the Financial Accounting Standards Board (FASB) issued ASU No. 2014-08, Presentation of Financial Statements (Topic 205) and Property, Plant, and Equipment (Topic 360): Reporting Discontinued Operations and Disclosures of Disposals of Components of an Entity ("ASU No. 2014-08"). ASU No. 2014-08 limits discontinued operations reporting to disposals of components of an entity that represent a strategic shift that has (or will have) a major effect on an entity's operations and financial results when any of the following occurs: a) the component of an entity or group of components of an entity meets the criteria to be classified as held for sale; b) the component of an entity or group of components of an entity is disposed of by sale; or c) the component of an entity or group of components of an entity is disposed of other than by sale. ASU No. 2014-08 also requires additional disclosures about discontinued operations. ASU No. 2014-08 is effective for reporting periods beginning after December 15, 2014. Early adoption is permitted, but only for disposals (or classifications as held for sale) that have not been reported in financial statements previously issued or available for issuance. The Company early adopted ASU No. 2014-08 for the reporting period beginning November 1, 2014. As a result of the adoption of ASU No. 2014-08, results of operations for disposals in the ordinary course of business on or subsequent to November 1, 2014 would generally be included in continuing operations on the Company's consolidated statements of operations, to the extent such disposals did not meet the criteria for classification as a discontinued operation. Additionally, any gain or loss on disposals that do not meet the criteria for classification as a discontinued operation would be included in income from continuing operations on the consolidated statements of operations.

In May 2014, the FASB issued Accounting Standards Update ("ASU") No. 2014-09, "Revenue from Contracts with Customers," which provides guidance for revenue recognition. The standard's core principle is that a company will recognize revenue when it transfers promised goods or services to customers in an amount that reflects the consideration to which the company expects to be entitled in exchange for those goods or services. The new guidance is effective for annual reporting periods beginning after December 15, 2016, including interim periods within that reporting period. Early application is not permitted. The Company is currently assessing the potential impact of ASU No. 2014-09 on its financial statements.

2. ACQUISITIONS

On May 1, 2015, the Company completed the acquisition of Valves Incorporated of Texas, a privately held Texas corporation, pursuant to the terms of a previously announced Agreement and Plan of Merger. That acquired company manufactures and distributes industrial sealants and lubricants, primarily to the oil and gas storage, pipeline and gas

distribution markets, as well as related products, such as lubrication equipment and fittings. In addition to the lubricants business, it also owned 606,875 shares of the Company's common stock. Fred C. Leonard III, a director of the Company, was the majority shareholder, president and chief executive officer of Valves Incorporated of Texas.

The aggregate merger consideration paid to the former shareholders of Valves Incorporated of Texas was 606,875 shares of the Company's common stock plus \$23.7 million in cash. The 606,875 shares of the Company previously owned by Valves Incorporated of Texas were cancelled as of the time of the merger, and no additional net shares of the Company were issued as a result of the merger. Of the \$23.7 million cash consideration, \$1.0 million of the purchase price was retained as a holdback to satisfy post-closing inventory adjustments and potential indemnity claims. \$500,000 of the holdback related to inventory adjustments was released in August 2015. The remaining \$500,000 of the holdback for potential indemnity claims will be released eighteen months after the closing. The Company completed the acquisition by borrowing \$23.5 million on the revolving loan under its revolving credit facility. At the closing of the merger, Valves Incorporated of Texas merged into Val-Tex. See Note 7 for further discussion of the Company's revolving credit facility.

The Company accounted for the acquisition under the acquisition method of accounting in accordance with GAAP. The Company expensed transaction and acquisition-related costs of approximately \$0.5 million in fiscal year 2015, which is included in selling, general and administrative expenses on the Company's consolidated statement of income.

The following table summarizes preliminary acquired assets and liability and the acquisition accounting for the fair value of the assets and liability recognized in the consolidated balance sheets at the acquisition date of the industrial lubricants and sealants business (in thousands):

| | |
|-------------------------------------|----------|
| Inventory | \$ 1,900 |
| Other current assets | 15 |
| Property, plant and equipment | 482 |
| Intangible assets: | |
| Customer relationships | 10,291 |
| Trade name and trademark | 2,885 |
| Proprietary manufacturing process | 2,808 |
| Other | 152 |
| Total intangible assets | 16,136 |
| Deferred tax liability - noncurrent | (6,178) |
| Net assets acquired | 12,355 |
| Goodwill | 11,352 |
| Total purchase consideration | \$23,707 |

The Company recognized \$2.1 million in net sales and net income of \$0.5 million related to the acquired business, in its consolidated statements of income for the fiscal year ended July 31, 2015. The pro forma impact on consolidated results had the acquisition of Valves Incorporated of Texas occurred as of the beginning of fiscal year 2015 is immaterial.

On May 31, 2013, the Company completed its acquisition of the ultra pure chemicals (“UPC”) business subsidiaries of OM Group, Inc. (“OM Group”) located in the United States, Europe and Singapore. The subsidiaries sell high purity and ultra pure, wet process chemicals to the semiconductor industry. The Company completed the acquisition by borrowing \$65.0 million on the revolving loan under its revolving credit facility on May 31, 2013. See Note 7 for further discussion of the Company’s revolving credit facility. During 2014, the Company entered into a settlement agreement with OM Group to finalize working capital adjustments related to the purchase price. The final purchase price of the UPC acquisition totaled \$63.2 million. The Company received a net payment of \$149,000 as part of the settlement of working capital adjustments.

The Company accounted for the UPC acquisition under the acquisition method of accounting in accordance with GAAP. The Company expensed transaction and acquisition-related costs of approximately \$2.1 million in fiscal year 2013, which is included in selling, general and administrative expenses on the Company’s consolidated statement of income.

The following table summarizes final acquired assets and assumed liabilities and the acquisition accounting for the fair value of the assets and liabilities recognized in the consolidated balance sheets at the UPC acquisition date (in thousands):

| | |
|---------------------------------|--------|
| Cash | \$689 |
| Accounts receivable | 14,698 |
| Inventory | 11,047 |
| Other current assets | 1,963 |
| Property, plant and equipment | 28,939 |
| Intangible assets: | |
| Value of product qualifications | 12,800 |

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| | |
|-----------------------------|----------|
| Non-compete agreement | 1,900 |
| Transition services | 154 |
| Total intangible assets | 14,854 |
| Total assets acquired | \$72,190 |
| Current liabilities | 11,401 |
| Other long-term liabilities | 6,206 |
| Total liabilities assumed | 17,607 |
| Net assets acquired | \$54,583 |

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The following table sets forth pro forma results for the fiscal year ended July 31, 2013 had the UPC acquisition occurred as of the beginning of fiscal year 2013. The unaudited pro forma financial information is not necessarily indicative of what our consolidated results of operations would have been had we completed the UPC acquisition as of the dates indicated.

| | |
|----------------------------|-------------|
| | (Unaudited) |
| | (in |
| | thousands, |
| | except per |
| | share data) |
| | 2013 |
| Revenues | \$ 340,427 |
| Operating income | 15,955 |
| Net income | 9,123 |
| Earnings per share — basic | \$ 0.79 |

The Company recognized \$16.0 million of net sales and net income of \$979,000, and integration costs of \$577,000 related to the acquired UPC business, in its consolidated statements of income for the fiscal year ended July 31, 2013.

The supplemental pro forma information for the UPC acquisition includes incremental interest expense from the Company's revised credit facility of \$1.0 million for the year ended July 31, 2013, excludes \$2.1 million of acquisition-related costs incurred in fiscal year 2013, and includes incremental depreciation and amortization expense of approximately \$3.1 million for the year ended July 31, 2013.

3. INVENTORIES

Inventories are summarized as follows at July 31, 2015 and 2014 (in thousands):

| | | |
|---|----------|----------|
| | 2015 | 2014 |
| Raw materials and supplies | \$8,723 | \$7,914 |
| Work in process | 780 | 1,508 |
| Supplies | 525 | 1,793 |
| Finished products | 32,535 | 34,343 |
| Less reserve for inventory obsolescence | (481) | (290) |
| Inventories, net | \$42,082 | \$45,268 |

4. PROPERTY, PLANT AND EQUIPMENT

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Property, plant, and equipment and related accumulated depreciation and amortization are summarized as follows at July 31, 2015 and 2014 (in thousands):

| | 2015 | 2014 |
|--|-----------|-----------|
| Land | \$13,257 | \$15,763 |
| Buildings and improvements | 38,036 | 42,664 |
| Equipment | 84,273 | 77,557 |
| Leasehold improvements | 193 | 143 |
| | 135,759 | 136,127 |
| Less accumulated depreciation and amortization | (61,936) | (52,972) |
| | 73,823 | 83,155 |
| Construction-in-progress | 6,766 | 9,295 |
| Property, plant and equipment, net | \$80,589 | \$92,450 |

5. INCOME TAXES

The Company is subject to United States federal, state and foreign taxes on its operations. The geographical sources of income from continuing operations before income taxes for each of the three years ended July 31 are as follows (in thousands):

| | 2015 | 2014 | 2013 |
|---|----------|---------|----------|
| United States | \$20,442 | \$1,923 | \$12,033 |
| Foreign | (1,558) | (1,657) | 3,168 |
| Income from continuing operations before income taxes | \$18,884 | \$266 | \$15,201 |

The components of income tax expense/(benefit) from continuing operations for the years ended July 31 consisted of the following (in thousands):

| | 2015 | 2014 | 2013 |
|-----------|----------|---------|---------|
| Current: | | | |
| Federal | \$9,176 | \$2,582 | \$2,833 |
| Foreign | (127) | 1,071 | 1,437 |
| State | 1,214 | 603 | 197 |
| | 10,263 | 4,256 | 4,467 |
| Deferred: | | | |
| Federal | (3,660) | (1,978) | 1,426 |
| Foreign | 293 | (897) | (282) |
| State | (150) | (127) | 104 |
| | (3,517) | (3,002) | 1,248 |
| Total | \$6,746 | \$1,254 | \$5,715 |

The Company allocated income tax benefit of \$65,000 to discontinued operations for the fiscal year ended July 31, 2013.

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Deferred income taxes are provided on all temporary differences between financial and taxable income. The following table presents the components of the Company's deferred tax assets and liabilities at July 31, 2015 and 2014 (in thousands):

| | 2015 | 2014 |
|---|------------|------------|
| Deferred tax assets: | | |
| Current deferred tax assets: | | |
| Bad debt expense | \$238 | \$326 |
| Inventory | 675 | 787 |
| Accrued liabilities | 227 | 1,545 |
| Employee benefits | 2,025 | 1,879 |
| Other | 972 | 102 |
| Less valuation allowance | (34) | (636) |
| Total current deferred tax assets | \$4,103 | \$4,003 |
| Non-current deferred tax assets | | |
| Net operating loss | \$1,629 | \$839 |
| Deferred compensation | 1,490 | 616 |
| Other | 295 | — |
| Less valuation allowance | (1,982) | (1,090) |
| Total non-current deferred tax assets | \$1,432 | \$365 |
| Deferred tax liabilities: | | |
| Current deferred tax liabilities: | | |
| Other | \$— | \$(128) |
| Prepaid assets | (341) | (398) |
| Total current deferred tax liabilities: | \$(341) | \$(526) |
| Non-current deferred tax liabilities: | | |
| Difference in amortization basis of intangibles | \$(11,131) | \$(7,129) |
| Difference in depreciable basis of property | (4,182) | (4,575) |
| Total non-current deferred tax liabilities | (15,313) | (11,704) |
| Net non-current deferred tax liability | \$(10,119) | \$(7,862) |

As of July 31, 2015, the Company has \$5.5 million of foreign net operating losses carry forwards, which do not expire.

The Company records provisions for uncertain tax provisions in accordance with GAAP, which prescribes the minimum recognition threshold that a tax position is required to meet before being recognized in the financial statements. The Company recognizes interest and penalties related to uncertain tax positions in income tax expense. The statute of limitations remain open for fiscal year ended July 31, 2012 and forward for United States federal income taxes and fiscal year ended July 31, 2010 and forward for state tax jurisdictions. On August 28, 2014, the Company was notified by the Internal Revenue Service that the federal income tax return for the July 31, 2013 fiscal year-end had been selected for examination. The audit is ongoing at this time.

The Company's subsidiary in Italy is contesting income tax assessments for the three year period ended July 31, 2011 and a registration tax assessment for the December 2007 purchase of the electronic chemicals business in Italy. Adjustments were proposed by the taxing authorities that would result in approximately \$2.8 million (including interest and penalties) of additional liability, if all the adjustments are sustained. In October 2014, the Italian tax court

ruled in favor of the Company's positions related to the income tax assessments. In April 2015, the taxing authority appealed the ruling. The Company does not expect all of this amount to result in cash payments in the event of an unfavorable resolution, as the Company would be able to utilize available net operating losses. The Company intends to vigorously defend its tax position. The ultimate outcome of this examination is subject to uncertainty, and the Company had a liability for its uncertain tax position in Italy as of July 31, 2015, 2014 and 2013 of \$57,000, \$326,000 and \$437,000, respectively, which includes penalties and interest offset by net operating losses. These uncertain tax positions primarily relate to transfer pricing. See Note 8 to the consolidated financial statements.

The Company has reviewed its Mexican operations and concluded that they do not have the same level of immediate capital needs as previously expected. Therefore, the Company no longer intends for previously unremitted foreign earnings associated with its Mexico operations to be permanently reinvested outside the United States. The Company maintains its foreign earnings from the remaining foreign subsidiaries to be permanently reinvested.

The following table accounts for the differences between the actual tax provision, and the amounts obtained by applying the applicable statutory United States federal income tax rate of 35% to income from continuing operations before income taxes for each of the years ended July 31, 2015, 2014, and 2013, respectively (in thousands):

| | 2015 | 2014 | 2013 |
|--|---------|---------|---------|
| Income taxes at the federal statutory rate | \$6,610 | \$93 | \$5,320 |
| Effect of foreign operations | 182 | 329 | (65) |
| Change in valuation allowance | 648 | 1,725 | — |
| Adjustments to foreign operations | 1,148 | (916) | — |
| Effects of foreign currency fluctuations | (953) | — | — |
| State income taxes, net of federal income tax effect | 639 | 269 | 232 |
| Production deduction and tax credits | (1,182) | — | — |
| Acquisition related cost | 125 | — | 714 |
| Other | (471) | (246) | (486) |
| Total | \$6,746 | \$1,254 | \$5,715 |

Uncertain Tax Positions

The Company accounts for uncertain tax positions in accordance with FASB ASC 740, which prescribes the minimum recognition threshold a tax position taken or expected to be taken in a tax return is required to meet before being recognized in the financial statements.

The following table summarizes the activity related to our gross unrecognized tax benefits (in thousands):

| | |
|--|-------|
| Balance at July 31, 2014 | \$461 |
| Increases related to prior years positions | 619 |
| Decreases related to prior years positions | (362) |
| Balance at July 31, 2015 | \$718 |

The Company does not anticipate any significant changes to the unrecognized tax benefits within the next twelve months. The Company recognizes interest and penalties related to uncertain tax positions within the provision for income taxes in the consolidated statements of income. During the year ended July 31, 2014, the Company had accrued \$221,000 of interest and penalties related to its unrecognized tax benefits. The amount of interest and penalties recognized in our tax provision for the year ended July 31, 2015 was a decrease of accrued interest and penalties of \$163,000.

6. INTANGIBLE ASSETS

Intangible assets are summarized as follows (in thousands):

| | Number of Years Weighted Average | July 31, 2015 | | | Carrying |
|--|---|------------------|-----------------------------|------------------------------------|----------|
| | Amortization Period | Original Cost | Accumulated Amortization | Foreign Currency Translation | Amount |
| Intangible assets subject to amortization | | | | | |
| (range of useful life): | | | | | |
| Electronic chemicals-related contracts (5-8 years) | 6.6 | \$2,204 | \$(839) | \$ (87) | \$1,278 |
| Electronic chemicals-related trademarks | | | | | |
| and patents (10-15 years) | 12.0 | 117 | (77) | — | 40 |
| Electronic chemicals-value of product | | | | | |
| qualifications (5-15 years) | 14.1 | 14,100 | (3,649) | 70 | 10,521 |
| Other chemicals-customer relationships (15 years) | 15.0 | 10,291 | (172) | — | 10,119 |
| Other chemicals-other related contracts (5 years) | 5.0 | 152 | (8) | — | 144 |
| Total intangible assets subject to amortization | 13.8 | \$26,864 | \$(4,745) | \$ (17) | \$22,102 |
| Intangible assets not subject to amortization: | | | | | |
| Other chemicals-penta product registrations | | | | | 8,765 |
| Other chemicals-related trade name and trademark | | | | | 2,885 |
| Other chemicals-proprietary manufacturing process | | | | | 2,808 |
| Total intangible assets not subject to | | | | | |
| amortization | | | | | 14,458 |
| Total intangible assets, net | | | | | \$36,560 |

| | Number of Years Weighted Average | July 31, 2014 | | | Carrying |
|--|---|------------------|-----------------------------|------------------------------------|----------|
| | Amortization Period | Original Cost | Accumulated Amortization | Foreign Currency Translation | Amount |
| Intangible assets subject to amortization | | | | | |
| (range of useful life): | | | | | |
| Electronic chemicals-related contracts (5-8 years) | 6.6 | \$2,204 | \$(559) | \$ 79 | \$1,724 |
| Electronic chemicals-related trademarks | 12.0 | 117 | (67) | — | 50 |

| | | | | | |
|---|------|-----------|-----------|--------|-----------|
| and patents (10-15 years) | | | | | |
| Electronic chemicals-value of product | | | | | |
| qualifications (5-15 years) | 14.1 | 14,100 | (2,426) | 801 | 12,475 |
| Total intangible assets subject to amortization | 13.1 | \$ 16,421 | \$(3,052) | \$ 880 | \$ 14,249 |
| Intangible assets not subject to amortization: | | | | | |
| Creosote product registrations | | | | | 5,339 |
| Penta product registrations | | | | | 8,765 |
| Total intangible assets not subject to | | | | | |
| amortization | | | | | 14,104 |
| Total intangible assets, net | | | | | \$ 28,353 |

Assets acquired in the acquisition of the industrial valve lubricants and sealants business in May 2015 included \$10.3 million of customer relationships and \$0.2 million of non-compete agreements, which are being amortized over fifteen and five years, respectively. Additionally, in connection with the acquisition, the Company recorded \$11.4 million of goodwill (non-deductible for tax). Assets acquired in the acquisition of the UPC subsidiaries in May 2013 included \$12.8 million of product qualifications and \$1.9 million of non-compete agreements, which are being amortized over 15 and seven years, respectively. Intangible assets subject to amortization are amortized over their estimated useful lives which are between five and 15 years. Total amortization expense related to intangible assets was approximately \$1.7 million, \$1.8 million and \$573,000 for the fiscal years ended July 31, 2015, 2014 and 2013, respectively. The estimated amortization expense is projected to be approximately \$2.1 million, \$2.1 million, \$2.0 million and \$2.0 million and \$1.8 million for fiscal years 2016 through 2020, respectively.

The following table presents carrying value of goodwill by operating segment as of July 31, 2015, 2014 and 2013 (in thousands):

| | Other | Electronic | |
|--|-----------|------------|-----------|
| | Chemicals | Chemicals | Total |
| Balance as of July 31, 2013 | 3,779 | 7,150 | 10,929 |
| Working capital adjustment from the UPC | | | |
| acquisition | — | 535 | 535 |
| Finalization of purchase price allocation | — | 880 | 880 |
| Foreign currency translation adjustment | — | 251 | 251 |
| Balance as of July 31, 2014 | 3,779 | 8,816 | 12,595 |
| Industrial lubricants business acquisition | 11,352 | — | 11,352 |
| Foreign currency translation adjustment | — | (877) | (877) |
| Sale of creosote business | (662) | — | (662) |
| Balance as of July 31, 2015 | \$ 14,469 | \$ 7,939 | \$ 22,408 |

7. LONG-TERM OBLIGATIONS

Working Capital

On October 9, 2014, the Company refinanced and amended its existing loan facility and entered into a new credit facility as reported on Form 8-K filed on October 10, 2014 (the “Second Restated Credit Facility”). At July 31, 2015 the Company had \$53 million outstanding under the Second Restated Credit Facility of \$150.0 million. The maximum borrowing capacity under that revolving loan facility was \$94.2 million, after giving effect to a reduction of \$2.8 million for unused letters of credit. The actual amount available under the revolving facility at July 31, 2015 was limited, however, to approximately \$76.8 million, because of a loan covenant restriction respecting funded debt to pro-forma earnings before interest, taxes and depreciation.

Long Term Obligations

The Company’s long-term debt and current maturities as of July 31, 2015 and 2014 consisted of the following (in thousands):

| | July 31, | July 31, |
|----------------------|----------|----------|
| | 2015 | 2014 |
| Senior secured debt: | \$— | \$20,000 |

Note purchase agreement, maturing on

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| | | |
|---|----------|----------|
| December 31, 2015, interest rate of 7.43% | | |
| Revolving loan facility, maturing on April 30, 2018, | | |
| variable interest rates based on LIBOR plus 2.0% | | |
| at July 31, 2014 | — | 40,000 |
| Revolving loan facility, maturing on October 9, 2019, | | |
| variable interest rates based on LIBOR plus 1.0% | | |
| at July 31, 2015 | 53,000 | — |
| Total debt | 53,000 | 60,000 |
| Current maturities of long-term debt | — | — |
| Long-term debt, net of current maturities | \$53,000 | \$60,000 |

The Company entered into an amended and restated credit agreement and a note purchase agreement in December 2007, which were subsequently amended. Advances under the revolving loan, as amended, bore interest at 2.155% as of July 31, 2014. The amount outstanding on the revolving loan facility was \$40.0 million at July 31, 2014. The note purchase agreement was for \$20.0 million. Advances under the note purchase agreement bore interest at 7.43% per annum.

On October 9, 2014, the Company refinanced its then existing revolving loan facility and entered into the Second Restated Credit Facility. The Second Restated Credit Facility is now with Wells Fargo Bank, National Association, Bank of America, N.A., HSBC Bank USA, National Association, and JPMorgan Chase Bank, N.A. The initial advance under the Second Restated Credit Facility was used to repay in full the \$20.0 million outstanding indebtedness under the Company's note purchase agreement with The Prudential Insurance Company of America and Pruco Life Insurance Company, and the Company refinanced \$38.0 million then outstanding under its existing revolving loan facility. As a result, the note purchase agreement was classified as a long-term obligation as of July 31, 2014.

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The Second Restated Credit Facility provides for a revolving loan up to \$150.0 million, including an accordion feature that allows for an additional revolving loan increase of up to an additional \$100.0 million with approval from the lenders. The amount available under the Second Restated Credit Facility at July 31, 2015 was limited, however, by a loan covenant restriction related to the ratio of funded debt to earnings before interest, taxes, depreciation and amortization (“EBITDA”). Taking that restriction into account, at July 31, 2015, the Company could draw approximately an additional \$76.8 million on its revolving loan. The maturity date for the Second Restated Credit Facility is October 9, 2019.

The revolving loan under the Second Restated Credit Facility bears interest at varying rate of LIBOR plus a margin based on funded debt to EBITDA, as described in the table.

| Ratio of Funded Debt to EBITDA | Margin |
|---|---------|
| Equal to or greater than 3.0 to 1.0 | 1.875 % |
| Equal to or greater than 2.75 to 1.0, but less than 3.0 to 1.0 | 1.625 % |
| Equal to or greater than 2.50 to 1.0, but less than 2.75 to 1.0 | 1.500 % |
| Equal to or greater than 2.25 to 1.0, but less than 2.50 to 1.0 | 1.375 % |
| Equal to or greater than 2.00 to 1.0, but less than 2.25 to 1.0 | 1.250 % |
| Equal to or greater than 1.50 to 1.0, but less than 2.00 to 1.0 | 1.125 % |
| Less than 1.50 to 1.0 | 1.000 % |

Advances under the revolving loan bore interest at 1.189% as of July 31, 2015. The Company also incurs an unused commitment fee on the unused amount of commitments under the Second Restated Credit Facility from 0.30% to 0.15%, based on the ratio of funded debt to EBITDA.

Loans under the Second Restated Credit Facility are secured by the Company’s assets, including stock in subsidiaries, inventory, accounts receivable, equipment, intangible assets, and real property. The Second Restated Credit Facility has restrictive covenants, including requirements that the Company must maintain a fixed charge coverage ratio of 1.5 to 1.0, a ratio of funded debt to EBITDA (as adjusted for non-cash and unusual, non-recurring, and certain acquisition and integration costs) of 3.25 to 1.0 (with a step-up to 3.5 to 1.0 during an acquisition period with lender consent) and a current ratio of at least 1.5 to 1.0. As of July 31, 2015, the Company was in compliance with all covenants of the Second Restated Credit Facility.

After considering the Second Restated Credit Facility, principal payments due under long-term debt agreements as of July 31, 2015 for the fiscal years ended July 31 are as follows (in thousands):

| | Total | 2016 | 2017 | 2018 | 2019 | 2020 | Thereafter |
|----------------|----------|------|------|------|------|----------|------------|
| Long-term debt | \$53,000 | \$ — | \$ — | \$ — | \$ — | \$53,000 | \$ — |

8. COMMITMENTS AND CONTINGENCIES

Contractual Obligations — The Company has non-cancelable operating leases for its office and warehouse facilities and certain transportation equipment and purchase obligations. Our obligations to make future payments under certain contractual obligations as of July 31, 2015 are summarized in the following table (in thousands):

| | Total | 2016 | 2017 | 2018 | 2019 | 2020 | Thereafter |
|-------------------------------------|----------|----------|----------|---------|-------|-------|------------|
| Operating leases | \$10,811 | \$2,772 | \$1,722 | \$849 | \$693 | \$537 | \$ 4,238 |
| Purchase obligations ⁽¹⁾ | 78,296 | 45,790 | 28,419 | 4,087 | — | — | — |
| Total | \$89,107 | \$48,562 | \$30,141 | \$4,936 | \$693 | \$537 | \$ 4,238 |

(1) Consists primarily of raw materials purchase contracts. These are typically not fixed price arrangements. The prices are based on the prevailing market prices.

Rent expense relating to the operating leases was approximately \$3.4 million, \$3.8 million and \$2.7 million in fiscal years 2015, 2014 and 2013, respectively.

Environmental — The Company's operations are subject to extensive federal, state and local laws, regulations and ordinances in the United States and abroad relating to the generation, storage, handling, emission, transportation and discharge of certain

materials, substances and waste into the environment, and various other health and safety matters. Governmental authorities have the power to enforce compliance with their regulations, and violators may be subject to fines, injunctions or both. The Company must devote substantial financial resources to ensure compliance, and it believes that it is in substantial compliance with all of the applicable laws and regulations.

Certain licenses, permits and product registrations are required for the Company's products and operations in the United States, Mexico and other countries in which it does business. The licenses, permits and product registrations are subject to revocation, modification and renewal by governmental authorities. In the United States in particular, producers and distributors of chemicals such as penta and creosote are subject to registration and notification requirements under federal law (including under the Federal Insecticide Fungicide and Rodenticide Act ("FIFRA"), and comparable state law) in order to sell those products in the United States. Compliance with these requirements has had, and in the future will continue to have, a material effect on our business, financial condition and results of operations.

The Company incurred expenses in connection with FIFRA research and testing programs of approximately \$ 977,000, \$667,000, and \$522,000, in fiscal years 2015, 2014 and 2013, respectively. These costs are included in selling, general, and administrative expenses.

Litigation and Other Contingencies — The Company is subject to contingencies, including litigation relating to environmental laws and regulations, commercial disputes and other matters. Certain of these contingencies are discussed below. The ultimate resolution of these contingencies is subject to significant uncertainty, and should the Company fail to prevail in any of them or should several of them be resolved against the Company in the same reporting period, these matters could, individually or in the aggregate, be material to the consolidated financial statements. The ultimate outcome of these matters, however, cannot be determined at this time, nor can the amount of any potential loss be reasonably estimated, and as a result except where indicated no amounts have been recorded in the Company's consolidated financial statements.

The Company records legal costs associated with loss contingencies as expenses in the period in which they are incurred.

The Company's subsidiary in Italy is contesting two cases in the Provincial Tax Court in Milan, Italy. In the first case the Company disputes income tax assessments by the taxing authority for the three year period ended July 31, 2011. In the aggregate, the amount of the assessments, including interest and penalties, is €1.8 million. If all the adjustments are sustained, the additional liability for the years 2009 through 2011 would total approximately \$2.0 million, including interest and penalties through July 31, 2015 (at an exchange rate of 1.103 \$/€). The Company had a liability for an uncertain tax position for items in the amount of \$57,000, \$326,000 and \$437,000 as of July 31, 2015, 2014 and 2013, respectively. In the second case, the Company's subsidiary is contesting the assessment of additional registration tax. The taxing authority is asserting an increased valuation of assets purchased from Air Products and Chemicals, Inc. in December 2007 on which registration tax is payable. The amount of this assessment, including interest and penalties through July 31, 2015, is €802,000 (or approximately \$885,000, at an exchange rate of 1.103 \$/€). The Provincial Tax Court issued a ruling in October 2014 agreeing with the Company's position in the income tax assessment case. In April 2015, the taxing authority appealed that ruling. The hearing date has not been set. The Company intends to vigorously pursue its position before the court in both cases, but the ultimate outcome of this litigation is subject to uncertainty.

The EPA has listed the Star Lake Canal Superfund Site near Beaumont, Texas on the National Priorities List. In December 2002, the Company received a letter from the EPA addressed to Idacon, Inc. (f/k/a Sonford Chemical Company) notifying Idacon of potential liability under CERCLA in connection with this site. The letter requested reimbursement from Idacon for costs incurred by the EPA in responding to releases at the sites, equal to approximately \$500,000 as of July 31, 2002. Idacon sold substantially all of its assets to one of our subsidiaries in 1988. The Company responded to a request for information from the EPA on the corporate history and relationship

between the Company and its subsidiaries and Sonford Chemical Company in April 2003. On December 22, 2005, the EPA and certain potentially responsible parties entered an administrative order on consent which required the implementation of a remedial investigation and feasibility study. We understand that these studies were completed by mid-2012. EPA prepared a Record of Decision, selecting a remedy of excavation and disposal or soil and/or sediment, containment with soil, clay and/or armor caps and monitored natural recovery. The EPA has estimated that the remediation will cost approximately \$22.0 million. In October 2014, the Company's subsidiary, KMG-Bernuth, received a letter from EPA notifying it of potential liability under CERCLA, and inviting it to enter into negotiations to pay for or perform the selected remedy. The Company is engaged in discussions with EPA and approximately seven other parties to assess their respective potential liability. No assurance can be given that the EPA will not designate the Company's subsidiary as a potentially responsible party. The Company established a liability of \$1.3 million in the third quarter of fiscal year 2015 in connection with this matter.

The Company is subject to federal, state, local and foreign laws and regulations and potential liabilities relating to the protection of the environment and human health and safety including, among other things, the cleanup of contaminated sites, the treatment, storage and disposal of wastes, the emission of substances into the air or waterways, and various health and safety matters. The Company expects to incur substantial costs for ongoing compliance with such laws and regulations. The Company may also face governmental or third-party claims, or otherwise incur costs, relating to cleanup of, or for injuries resulting from, contamination at

sites associated with past and present operations. The Company accrues for environmental liabilities when a determination can be made that they are probable and reasonably estimable.

9. EMPLOYEE BENEFIT PLANS

The Company has a defined contribution 401(k) plan in which all regular U.S. employees are eligible to participate. The Company makes matching contributions under this plan of up to 4% of a participant's compensation up to the annual regulated maximum amounts. The first 3% of the employee contribution is matched at 100%. The next 2% of the employee contribution is matched at 50%. Company contributions to the plan totaled approximately \$573,000, \$608,000 and \$457,000 in fiscal years 2015, 2014, and 2013, respectively.

The locations in the United Kingdom and Singapore, acquired as part of the UPC acquisition from OM Group, make contributions to retirement plans that function as defined contribution retirement plans. The Company's contributions to those plans were approximately \$1.3 million and \$1.5 million in fiscal years 2015 and 2014, respectively. The Company's contributions to those plans were not significant in fiscal year 2013.

The Company's other long-term liabilities included approximately \$1.2 million and \$1.1 million as of July 31, 2015 and 2014, respectively, related to benefit obligations in connection with the France location included in the acquisition of the UPC business. This payable is an unfunded benefit obligation of the Company.

The Company has an employee benefit arrangement for one of its former U.S. employees. As of July 31, 2015 and 2014, the associated liability was approximately \$490,000 and \$553,000, respectively. The amount payable is a general obligation of the Company. Benefit payments under this arrangement, which the Company began paying in April 2013, will be paid for 10 years.

10. EARNINGS PER SHARE

Basic earnings per share have been computed by dividing net income by the weighted average shares outstanding. Diluted earnings per share have been computed by dividing net income by the weighted average shares outstanding plus potentially dilutive common shares. The following table presents information necessary to calculate basic and diluted earnings per share for periods indicated:

| | Year Ended | | |
|--|---|-----------|---------|
| | 2015 | 2014 | 2013 |
| | (Amounts in thousands, except per share data) | | |
| Income/(loss) from continuing operations | \$12,138 | \$ (988) | \$9,486 |
| Income/(loss) from discontinued operations | — | — | (138) |
| Net income (loss) | \$12,138 | \$ (988) | \$9,348 |
| Weighted average shares outstanding — basic | 11,673 | 11,615 | 11,487 |
| Dilutive effect of options/warrants and stock awards | 106 | — | 91 |

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| | | | |
|--|--------|----------|--------|
| Weighted average shares outstanding — diluted | 11,779 | 11,615 | 11,578 |
| Basic earnings/(loss) per share | | | |
| Basic earnings/(loss) per share from continuing operations | \$1.04 | \$(0.09) | \$0.82 |
| Basic earnings per share on income/(loss) from | | | |
| discontinued operations | — | — | (0.01) |
| Basic earnings/(loss) per share | \$1.04 | \$(0.09) | \$0.81 |
| Diluted earnings per share | | | |
| Diluted earnings/(loss) per share from continuing operations | \$1.03 | \$(0.09) | \$0.82 |
| Diluted earnings per share on income/(loss) from | | | |
| discontinued operations | — | — | (0.01) |
| Diluted earnings/(loss) per share | \$1.03 | \$(0.09) | \$0.81 |

Outstanding stock-based awards are not included in the computation of diluted earnings per share under the treasury stock method, if including them would be anti-dilutive. There was an average of 136 shares, 21,033 shares and 6,222 shares for the fiscal years ended 2015, 2014 and 2013, respectively, not included in the computation of diluted earnings per share. Potentially dilutive shares are not included in the computation of diluted weighted average shares outstanding for the fiscal year ended July 31, 2014 due to a loss from continuing operations for the year.

11. STOCK-BASED COMPENSATION

Stock-Based Incentive Plans

The Company adopted a 2009 Long-Term Incentive Plan (“LTI Plan”) in October 2009, and it was approved by the shareholders at the annual meeting in December 2009. The Company adopted a 2004 Long-Term Incentive Plan (“2004 LTI Plan”) in October 2004, and it was approved by the shareholders at the annual meeting in November 2005, which expired and terminated on October 14, 2014. The Company adopted the 1996 Stock Option Plan (the “1996 Stock Plan”) in October, 1996, which expired and terminated on July 31, 2007. There are no options outstanding under the 1996 Stock Plan or the 2004 LTI Plan as of July 31, 2015.

The LTI Plan permits the granting of incentive stock options, non-qualified stock options, stock appreciation rights, restricted stock, restricted stock units, performance awards, dividend equivalent rights, and other awards. They are administered by the Board of Directors or a committee appointed by the Board of Directors. The Board has designated the Compensation and Development Committee as the administrator of the LTI Plan. Subject to the terms of the LTI Plan, the committee has the sole discretion to select the persons eligible to receive awards, the type and amount of incentives to be awarded, and the terms and conditions of awards. The committee also has the authority to interpret the LTI Plan, and establish and amend regulations necessary or appropriate for their administration. Any employee of the Company or a subsidiary of the Company or a director of the Company whose judgment, initiative, and efforts contributed or may be expected to contribute to the successful performance of the Company is eligible to participate. The maximum number of shares of the Company’s common stock that may be delivered pursuant to awards granted is 750,000 shares under the LTI Plan. Under the LTI Plan, no executive officer may receive in any calendar year stock options or stock appreciation rights, or awards that are subject to the attainment of performance goals relating to more than 200,000 shares of common stock. At July 31, 2015 there were approximately 124,575 shares available for future grants under the LTI Plan.

Accounting for Stock-Based Compensation

The Company recognized stock-based compensation costs of approximately \$2.8 million, \$2.2 million and \$446,000, respectively, for the fiscal years ended July 31, 2015, 2014 and 2013, and the related tax benefits of \$887,000, \$825,000 and \$168,000, respectively, for the fiscal years ended July 31, 2015, 2014 and 2013. Stock-based compensation costs are recorded as selling, general and administrative expenses in the consolidated statements of income. The Company accounts for stock-based compensation costs at fair value measured on the date of grant of the award using a Black-Scholes option valuation model for stock option awards. Grant date fair value for stock awards is measured using the Company’s closing stock price on the date of grant of the stock awards where the award is based on a specific number of shares. Stock-based compensation costs are recognized as an expense over the requisite service period, generally the vesting period of the award, using the straight-line method.

As of July 31, 2015, there was approximately \$4.2 million of unrecognized compensation costs that are related to outstanding stock awards expected to be recognized over a weighted-average period of 1.8 years.

In connection with the election of Christopher T. Fraser as the Company’s President and Chief Executive Officer on September 24, 2013, the Company granted Mr. Fraser (i) 50,000 shares of common stock and (ii) time-based restricted stock awards for 30,000 shares of common stock (vesting over five years). The Company also agreed to grant performance-based restricted stock awards for an aggregate of 70,000 shares of common stock in five equal installments beginning in fiscal year 2014. The Company recorded an expense of approximately \$1.1 million in the first quarter of fiscal year 2014 for the grant date fair value of the 50,000 shares of common stock.

A summary of activity for stock option and stock-awards is presented below.

Stock Options

There were no stock options granted in fiscal years 2015, 2014 and 2013 and no stock options outstanding at July 31, 2015 and 2014.

There were no options exercised in fiscal year 2015. The total intrinsic value of options exercised in fiscal years 2014 and 2013 was approximately \$952,000 and \$1.6 million, respectively. The total fair value of shares vested was \$0, and \$39,000 for the fiscal years ended July 31, 2014 and 2013, respectively.

Performance Shares

The Company grants performance-based Series 1 and Series 2 awards for shares to certain executives and employees. Stock-based compensation for the awards is recognized on a straight-line basis over the requisite service period beginning on the date of

grant through the end of the measurement period based on the number of shares expected to vest under the awards at the end of the measurement period. The expected percent of vesting is determined using certain performance measures described below and is re-evaluated at the end of each reporting period through the end of the measurement period.

At August 1, 2014 there were non-vested performance share awards outstanding for 185,915 shares, which reflected the target number of shares under the awards. During fiscal year 2015 there were Series 1 awards granted for 124,672 shares and awards for 12,147 shares were forfeited. These shares represented the target award subject to certain performance measures. No Series 1 awards for shares vested during fiscal year 2015. Total performance share awards for 53,650 shares granted in fiscal year 2013 did not vest at July 31, 2015, the end of the measurement period for such awards. At July 31, 2015, there were non-vested performance share awards outstanding for 244,790 shares reflecting the target number of shares issuable under outstanding awards for fiscal years 2014 and 2015.

The fair value of the key personnel fiscal year 2015 award granted on March 26, 2015 was measured using the Company's closing stock price on the grant date of \$25.85. The fair value of the executive fiscal year 2015 award granted on December 9, 2014 was measured using the Company's closing stock price on the grant date of \$17.81. Stock-based compensation on the awards is recognized on a straight-line basis over the requisite service period beginning on the date of grant through the end of the measurement period ending on July 31, 2017, based on the number of shares expected to vest under the award at the end of the measurement period.

A summary of the performance-based stock awards granted to certain employees and executives as Series 1 awards in fiscal years 2015, 2014 and 2013 is detailed below.

| Date of Grant | Series Award | Target Award (Shares) | Grant Date Fair Value | Measurement Period Ending | Actual or Expected Percentage of Vesting ⁽¹⁾ | Shares Projected to Vest or Vested |
|-------------------------------|----------------------------|-----------------------|-----------------------|---------------------------|---|------------------------------------|
| Fiscal Year 2015 Award | | | | | | |
| 03/26/2015 | Series 1 | 21,173 | \$25.85 | 07/31/2017 | | |
| 12/09/2014 | Series 1 | 103,499 | \$17.81 | 07/31/2017 | | |
| | Forfeitures ⁽²⁾ | (562) | | | | |
| Total | | 124,110 | | | 135 % | 168,042 |
| Fiscal Year 2014 Award | | | | | | |
| 02/25/2014 | Series 1 | 127,315 | \$14.88 | 07/31/2016 | | |
| | Forfeitures ⁽²⁾ | (6,635) | | | | |
| Total | | 120,680 | | | 100 % | 120,680 |
| Fiscal Year 2013 Award | | | | | | |
| 12/4/2012 | Series 1 | 141,059 | \$18.75 | 07/31/2015 | | |
| | Forfeitures ⁽²⁾ | (87,409) | | | | |
| Total | | 53,650 | | | 0 % | — |

(1) The percentage vesting for performance share awards is currently estimated at 135%, 100% and 0% of the target awards for the fiscal year 2015, 2014 and 2013 awards, respectively.

(2) Forfeitures include Series 1 awards that were granted in fiscal years 2015, 2014 and 2013 to certain employees that were forfeited at the termination of their employment.

Series 1: For the fiscal year 2015, 2014 and 2013 awards, vesting is subject to performance requirements composed of certain objectives including average annual return on invested capital and annual compound growth rate in the Company's diluted earnings per share. These objectives are measured quarterly using the Company's budget, actual results and long-term projections. For each of the Series 1 awards, the expected percentage of vesting is evaluated through July 31, 2015, and reflects the percentage of shares projected to vest for the respective awards at the end of their measurement periods. For the fiscal year 2015 and 2014 awards, shares vested under the awards may increase to a maximum of 167% and 150%, respectively, of the target award on achievement of maximum performance objectives. For the fiscal year 2013 awards, the target award is equal to the maximum award.

Series 2: None outstanding.

Series 3: The table does not include certain performance-based awards to be granted to Christopher T. Fraser according to his employment agreement as of September 24, 2013. Awards to Mr. Fraser for fiscal year 2015 included (i) a performance-based Series 3 award for 10,000 shares of common stock (at maximum) having a performance requirement related to debt payments during fiscal year 2015, and (ii) a performance-based Series 3 award for 4,000 shares of common stock having certain organizational objectives as a performance requirement, and in each case such awards vest and are measured over a one year period beginning August 1, 2014 and ending July 31, 2015. As of July 31, 2015, the Series 3 awards to Mr. Fraser have fully vested.

The weighted-average grant-date fair value of performance share awards forfeited during the fiscal year 2015 was \$15.74. The weighted-average grant-date fair value of performance share awards outstanding at August 1, 2014 and July 31, 2015 was \$14.88 and \$17.36, respectively.

The total fair value of performance share awards vested during fiscal years 2015, 2014 and 2013 was approximately \$233,000, \$45,000, and \$118,000, respectively.

Time-Based Shares

A summary of activity for time-based stock awards for the fiscal year ended July 31, 2015 is presented below:

| | Weighted-Average | |
|------------------------------|------------------|------------|
| | Grant-Date | |
| | Shares | Fair Value |
| Non-vested on August 1, 2014 | 50,100 | \$ 19.19 |
| Granted ⁽¹⁾ | 68,774 | 20.00 |
| Vested ⁽²⁾ | (36,186) | 19.65 |
| Forfeited | — | — |
| Non-vested on July 31, 2015 | 82,688 | 19.66 |

(1)Includes 19,386 share awards granted to non-employee directors during fiscal year 2015. The director awards were granted for a three month service period. The director awards were granted at the end of each quarter and vested once the service period was complete. Includes 8,000 share awards granted to certain employees vesting over one or two years from the date of grant. Includes 41,388 share awards granted to certain employees and executives during fiscal year 2015 which are expected to vest on July 31, 2017. The Company recognizes compensation expense related to the awards over the respective service period.

(2)Includes 19,386 share awards granted to non-employee directors indicated above and 16,800 share awards granted to employees.

The total fair value of share awards vested during the fiscal years ended 2015, 2014 and 2013 was approximately \$944,000, \$1,822,000, and \$542,000, respectively.

12. DISCONTINUED OPERATIONS

Discontinued operations reflected a loss before income taxes of \$203,000 for fiscal year 2013.

On March 1, 2012, the Company sold the business that had comprised the animal health segment to Bayer Healthcare LLC. For the fiscal year ended July 31, 2013, \$82,000 was reported as a loss from discontinued operations before income taxes. In fiscal year 2013 the loss included \$57,000 for a post-closing inventory adjustment that was recognized as loss on sale of the business in the first fiscal quarter.

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In the sale of the animal health business, \$1.0 million of the price is restricted cash held in escrow. The escrowed amount is to be held pending the final acceptance by the EPA of certain studies being performed at the request of the EPA on tetrachlorvinphos, the active ingredient used in Rabon products. The escrowed funds are to be released to the Company once the EPA has finally accepted the studies, the buyer has voluntarily canceled the products, or after five years. The escrowed funds are to be released to the buyer if the EPA cancels the products to which the studies pertain before the funds are distributed to the Company.

Animal health net sales and income before income tax reported in discontinued operations were as follows for the fiscal year ended July 31. There were no such amounts for fiscal year 2015 or 2014:

| | 2013 (Amounts in thousands) |
|-----------------------------------|--------------------------------------|
| Revenue | \$ 57 |
| Income (loss) before income taxes | (25) |

13. SEGMENT INFORMATION

The Company has two reportable segments—electronic chemicals and other chemicals. In conjunction with the acquisition of the industrial valve lubricants and sealants business, the Company’s management, including the chief executive officer, who is the chief operating decision maker, determined that the Company’s operations should be reported as the electronic chemicals and other chemicals business segments. Previously the Company had two reportable segments – electronic chemicals and wood treating chemicals. The electronic chemicals segment includes the ultra pure chemicals business acquired from OM Group on May 31, 2013 and represents the substantial majority of the Company’s on-going operations. During the second quarter ended January 31, 2015, the Company sold the creosote business which, along with the Company’s penta business, comprised the previous wood treating chemicals segment. The remaining piece of the wood treating chemicals segment was combined with the recently acquired industrial lubricants business and are presented as the other chemicals segment. Therefore, as of May 1, 2015 our other chemicals segment includes the Company’s penta business and the recently acquired industrial valve lubricants and sealants business.

| | 2015 | 2014 | 2013 |
|---|------------------------|-----------|-----------|
| | (Amounts in thousands) | | |
| Sales | | | |
| Electronic chemicals | \$265,608 | \$253,754 | \$165,755 |
| Other chemicals | 54,820 | 99,514 | 97,185 |
| Total sales for reportable segments | \$320,428 | \$353,268 | \$262,940 |
| Depreciation and amortization⁽¹⁾ | | | |
| Electronic chemicals | \$12,257 | \$13,240 | \$7,416 |
| Other chemicals | 626 | 400 | 418 |
| Other — general corporate | 648 | 477 | 461 |
| Total consolidated depreciation and amortization | \$13,531 | \$14,117 | \$8,295 |
| Segment income from operations⁽²⁾ | | | |
| Electronic chemicals | \$21,787 | \$14,089 | \$13,992 |
| Other chemicals | 8,735 | 8,390 | 10,522 |
| Total segment income from operations | \$30,522 | \$22,479 | \$24,514 |

(1) Segment depreciation excludes depreciation for restructuring and realignment.

(2) Segment income from operations includes allocated corporate overhead expenses, but excludes restructuring and realignment charges.

For fiscal years 2015, 2014 and 2013 sales to one customer represented approximately 23%, 15% and 20%, respectively, of the Company’s net sales. In fiscal years 2014 and 2013, sales to another customer represented approximately 13% and 16% of the Company’s net sales. No other customers accounted for 10% or more of the Company’s net sales.

Corporate overhead expenses allocated to segment income for the fiscal years ended July 31, 2015, 2014 and 2013 were as follows:

| | 2015 | 2014 | 2013 |
|----------------------|------------------------|---------|---------|
| | (Amounts in thousands) | | |
| Electronic chemicals | \$10,780 | \$8,751 | \$5,218 |
| Other chemicals | 4,071 | 4,458 | 4,461 |

Total corporate overhead expense allocation \$14,851 \$13,209 \$9,679

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A reconciliation of total segment to consolidated amounts as of July 31, 2015 and 2014, and for fiscal years 2015, 2014 and 2013 is set forth in the table below.

| | 2015 | 2014 | 2013 |
|---|------------------------|-----------|-----------|
| | (Amounts in thousands) | | |
| Assets: | | | |
| Total assets for reportable segments | \$228,233 | \$233,580 | \$244,015 |
| Total assets for discontinued operations ⁽¹⁾ | — | — | 467 |
| Other current assets | 8,440 | 7,690 | 9,120 |
| Other assets | 5,686 | 9,588 | 8,413 |
| Total assets | \$242,359 | \$250,858 | \$262,015 |
| Sales: | | | |
| Total sales for reportable segments | \$320,428 | \$353,268 | \$262,940 |
| Other ⁽²⁾ | 70 | 138 | 371 |
| Net sales | \$320,498 | \$353,406 | \$263,311 |
| Segment income from operations: | | | |
| Total segment income from operations ⁽³⁾ | \$30,522 | \$22,479 | \$24,514 |
| Other corporate expense ⁽³⁾ | (7,029) | (7,652) | (7,334) |
| Restructuring and realignment charges | (6,904) | (10,876) | - |
| Operating income | 16,589 | 3,951 | 17,180 |
| Interest expense, net | (1,407) | (2,854) | (1,771) |
| Other income/(expense), net | 3,702 | (831) | (208) |
| Income from continuing operations before income taxes | \$18,884 | \$266 | \$15,201 |

Geographic Data:

| | 2015 | 2014 | 2013 |
|--|------------------------|-----------|-----------|
| | (Amounts in thousands) | | |
| Net sales: | | | |
| United States | \$183,384 | \$212,903 | \$200,184 |
| International | 137,114 | 140,503 | 63,127 |
| Net sales | \$320,498 | \$353,406 | \$263,311 |
| Property, plant and equipment, net: | | | |
| United States | \$45,257 | \$49,776 | |
| International | 35,332 | 42,674 | |
| Property, plant and equipment, net | \$80,589 | \$92,450 | |

(1) Reflects deferred tax assets as of July 31, 2013.

(2) Primarily reflects income in connection with the sale of the animal health business. See Note 12.

(3) Other corporate expense primarily represents employee stock-based compensation expenses and those expenses associated with the Company's operation as a public entity such as board compensation, audit expense, fees related to the listing of our stock and expenses incurred to pursue acquisition opportunities.

14. RESTRUCTURING AND REALIGNMENT EVENTS

In October 2013, the Company announced that as part of global restructuring of its electronic chemicals operations, the Fremont, California manufacturing site acquired in the acquisition from OM Group will be closed, and production shifted primarily to the Company's Hollister, California and Pueblo, Colorado facilities. The Company ceased production at the Fremont facility and completed site decommissioning prior to the end of fiscal year 2014. In November 2013, the Company also announced that it will close a facility in Milan, Italy, and shift production to facilities in France and the United Kingdom. Restructuring charges, exclusive of accelerated depreciation, have been \$4.3 million in the aggregate in fiscal years 2015 and 2014, and accelerated depreciation with respect to the closed facilities was approximately \$3.3 million over those two fiscal years.

At July 31, 2015, the accrued liability associated with restructuring and other related charges consisted of the following:

| | Decommissioning | | | |
|------------------------------------|-----------------|---------------|-------|----------|
| | and | | | |
| | Employee Costs | Environmental | Other | Total |
| Accrued liability at July 31, 2013 | \$ — | \$ — | \$ — | \$ — |
| Charges | 2,631 | 1,260 | 34 | 3,925 |
| Payments | (698) | (438) | 0 | (1,136) |
| Adjustment | (45) | (12) | (7) | (64) |
| Accrued liability at July 31, 2014 | \$ 1,888 | \$ 810 | \$ 27 | \$ 2,725 |
| Charges | — | 90 | 11 | 101 |
| Payments | (882) | (654) | (12) | (1,548) |
| Adjustment | (290) | (77) | (9) | (376) |
| Accrued liability at July 31, 2015 | \$ 716 | \$ 169 | \$ 17 | \$ 902 |

Total accelerated depreciation for the fiscal years ended July 31, 2015 and 2014 was \$900,000 and \$2.4 million, respectively.

In October 2014, the Company announced a realignment of its hydrofluoric acid business and subsequently exited the facility operated for the Company by Chemtrade Logistics (“Chemtrade”) in Bay Point, California. Under the manufacturing agreement, the Company is obligated to pay or reimburse Chemtrade for certain costs associated with the cessation of operations at Bay Point, including certain employee costs and the decommissioning, dismantling and removal of the Company’s manufacturing equipment at the site. Operations ceased in the third quarter of fiscal year 2015. The Company incurred total charges of \$4.8 million for accelerated depreciation during fiscal year 2015. Additionally, the Company incurred certain employee costs of \$0.8 million. All assets have been fully depreciated as of July 31, 2015.

The changes to the asset retirement obligation associated with realignment are as follows:

| | |
|--|---------|
| Asset retirement obligation at July 31, 2014 | \$3,870 |
| Charges | 671 |
| Payments | (3,721) |
| Adjustment | (9) |
| Asset retirement obligation at July 31, 2015 | \$811 |

In fiscal year 2014, the Company established an asset retirement obligation of \$3.7 million for decontamination, decommissioning and dismantling at Bay Point, and recorded \$1.0 million depreciation expense against that obligation, and the Company recognized \$0.8 million of additional accelerated depreciation. In addition, the Company recognized an impairment charge of \$2.7 million in fiscal year 2014 with respect to certain manufacturing equipment at Bay Point that is unrelated to hydrofluoric acid production.

15. SELECTED QUARTERLY FINANCIAL DATA (UNAUDITED)

Quarterly results for the fiscal years ended July 31, 2015 and 2014 exclude the effect of discontinued operations, except for net income amounts. See note 12 for further detail on discontinued operations.

| | First | Second | Third | Fourth |
|-----------------------------------|---|-----------|----------|-----------|
| | Quarter | Quarter | Quarter | Quarter |
| | (Amounts in thousands, except per share data) | | | |
| Year Ended July 31, 2015 | | | | |
| Net sales | \$90,779 | \$79,762 | \$73,964 | \$75,993 |
| Gross profit | 27,591 | 28,555 | 26,815 | 26,516 |
| Operating income | 2,819 | 3,167 | 4,761 | 5,842 |
| Income before income taxes | 1,988 | 8,534 | 2,827 | 5,535 |
| Net income | 1,185 | 5,490 | 2,135 | 3,328 |
| Earnings per share: | | | | |
| Net income per share | | | | |
| - basic | \$0.10 | \$0.47 | \$0.18 | \$0.29 |
| - diluted | 0.10 | 0.47 | 0.18 | 0.28 |
| Year Ended July 31, 2014 | | | | |
| Net sales | \$93,560 | \$84,253 | \$84,437 | \$91,156 |
| Gross profit | 25,567 | 25,190 | 24,765 | 27,977 |
| Operating income/(loss) | 3,055 | (1,603) | 2,914 | (415) |
| Income/(loss) before income taxes | 2,077 | (2,384) | 1,883 | (1,310) |
| Net income /(loss) | 1,352 | (2,744) | 1,226 | (822) |
| Earnings/(loss) per share: | | | | |
| Income/(loss) per share | | | | |
| - basic | \$0.12 | \$(0.24) | \$0.11 | \$(0.07) |
| - diluted | 0.12 | (0.24) | 0.11 | (0.07) |

Earnings per share amounts are computed independently for each quarter presented. Therefore, the sum of the quarterly earnings per share may not equal annual earnings per share.

ITEM 9. CHANGES IN AND DISAGREEMENTS WITH ACCOUNTANTS ON ACCOUNTING AND FINANCIAL DISCLOSURE

None.

ITEM 9A. CONTROLS AND PROCEDURES

Disclosure Controls and Procedures

The term “disclosure controls and procedures” is defined in Rules 13a-15(e) and 15d-15(e) of the Securities Exchange Act of 1934. This term refers to the controls and procedures of a company that are designed to ensure that information required to be disclosed by a company in the reports that it files or submits under the Exchange Act is recorded, processed, summarized and reported within the time periods specified by the Securities and Exchange Commission. Our management, including our Chief Executive Officer and Chief Financial Officer, has evaluated the effectiveness of our disclosure controls and procedures as of the end of the period covered by this annual report. Based upon that evaluation, our Chief Executive Officer and Chief Financial Officer have concluded that our disclosure controls and procedures were not effective as of the end of the period covered by this annual report, because of material weaknesses in internal control over financial reporting described below.

Management’s Report on Internal Control over Financial Reporting

Our management is responsible for establishing and maintaining adequate internal control over financial reporting, as such term is defined in Rules 13a-15(f) and 15d-15(f) under the Exchange Act. Because of inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluations of effectiveness to future periods is subject to the risk that controls may become inadequate in the future period because of changes in conditions, in the degree of compliance with the policies, or because procedures may deteriorate.

Under the supervision and with the participation of our management, including our principal executive and principal financial officers, we conducted an assessment as of July 31, 2015 of the effectiveness of our internal control over financial reporting based on the framework in Internal Control—Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission (2013 Framework) (the “COSO Framework”). In this assessment, management identified material weaknesses in financial controls, and concluded that internal control over financial reporting was not effective as of July 31, 2015. A material weakness is a deficiency, or combination of deficiencies, in internal control over financial reporting such that there is reasonable possibility that a material misstatement of the interim and annual consolidated financial statements could occur and not be prevented or detected.

Although we determined in our assessment that internal control over financial reporting was not effective as of July 31, 2015, in connection with the fourth quarter financial close of fiscal year 2015 and the implementation of the new ERP system in that quarter, we delayed the quarter close and performed additional analyses and procedures, including among other things, additional transaction reviews, control activities, account reconciliations and physical inventories. As a result of these and other expanded procedures, and taking into account the material weaknesses in internal control over financial reporting described below, we have concluded that the consolidated financial statements included in Item 8 of Part II of this report present fairly, in all material respects, our financial position, results of operations and cash flows for the periods presented in conformity with GAAP.

In our assessment of the effectiveness of our internal control over financial reporting as of July 31, 2015, the material weaknesses that were identified result from our personnel not having sufficient knowledge, experience and skills to handle both the demands of financial reporting and the added burden of the implementation and stabilization of our new ERP system at the same time, and also result from failures in the control environment and monitoring activities

over our operations in France.

The following are the material weaknesses within our financial reporting process arising in connection with the implementation of the new ERP system:

- With respect to the control environment, we did not provide sufficient personnel with an appropriate level of knowledge, experience and skills commensurate with the requirements of our business environment and our financial reporting, including the ability to complete the financial reporting process timely in the same quarter as the ERP implementation.
- With respect to risk assessment, we did not adequately identify and mitigate risks associated with implementing the new ERP system used for financial reporting purposes, including a failure to adequately assess and implement (i) the staffing level and training needs of our business and our accounting and financial reporting staff, and (ii) effective protocols for information systems access and segregation of duty conflicts.

Additionally, the following control deficiencies were noted in the control environment and monitoring activities in connection with our operations in France:

- We did not design and maintain effective controls for the review, supervision and monitoring of our internal control processes in France, particularly related to the detailed performance and documentation of controls.
- We did not have sufficient accounting professionals for operations in France with an appropriate level of commitment to the importance of internal controls over financial reporting and the knowledge, experience and skills to perform and monitor those controls.

The material weaknesses that we identified above were related to the implementation of our new ERP system for operations in the United States and for the corporate function. We initially planned for a “go live” date of February 1, 2015. The initial “go live” date was selected to allow sufficient time to address issues normally expected to be encountered in a major system implementation. The “go live” date was ultimately postponed to May 1, 2015, however, in order to be assured that order processing and shipping, operations and invoicing and collection would function properly for our customers. Although those business processes did function successfully, the postponement meant that “go live” occurred in our fourth quarter of fiscal year 2015, and due to the delay in the implementation, additional stress was placed on our personnel, organization and maintenance of internal controls over financial reporting. The new ERP system required implementation of internal controls under a new system environment, and placed additional demands on our personnel in the businesses and in accounting and financial reporting. The new implementation also meant that data from the prior system in the United States, and the several ERP systems run globally, had to be merged with the new ERP system.

KPMG LLP, our independent registered public accounting firm, has audited the effectiveness of our internal control over financial reporting as of July 31, 2015, and has issued an adverse opinion, which appears herein.

Management’s Remediation Plans. To correct these material weaknesses in internal control over financial reporting, we plan on taking appropriate actions over the next year including:

- Senior leadership will reemphasize the importance of having effective controls over financial reporting. That effort will include face-to-face meetings during the year, the creation of a formalized role for someone to have primary oversight responsibility for the Company’s controls compliance, training, and the implementation of other regular, periodic interactions with employees who are involved in the financial reporting process and related internal controls to ensure that these personnel have the necessary skill, training, and time to carry out the Company’s internal control over financial reporting.
- We will hire personnel with enhanced qualifications, implement reorganized reporting and supervision of financial controls, and improve training with respect to the controls.
- We will continue our risk assessment process by formally considering staffing and training needs as they relate to the financial reporting process, including enhanced mitigation in order to assure that we have sufficient personnel with an appropriate level of knowledge, experience and skills to successfully accomplish the requirements of the financial reporting process, including in connection with any ERP system.
- To assist in the completion of the financial reporting process timely, we will further automate the consolidation process.
- We will reconsider the design of selected controls over financial reporting to improve their clarity and effectiveness, add additional controls where advisable, and analyze selected business processes and more effectively align appropriate and effective controls over those processes.
- We will address failures in information systems access and segregation of duties controls by reconsidering how user authorization is implemented, and make modifications where advisable to enhance their effectiveness, including by evaluating and acquiring additional monitoring and assessment tools.

Changes in Internal Control over Financial Reporting

There were no changes to our internal control over financial reporting identified in conjunction with our management’s evaluation of such control that occurred during our fiscal quarter ended July 31, 2015 that materially affected, or are reasonably likely to materially affect, our internal control over financial reporting, except that various manual and automated controls changed or were put in place in connection with the implementation of our new ERP system for our U.S. business, including our corporate function.

PART III

Pursuant to instruction G(3) to Form 10-K, the information required by Part III is incorporated by reference from our definitive proxy statement relating to our annual meeting of shareholders, which will be filed with the Securities and Exchange Commission within 120 days of the end of fiscal year 2015.

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PART IV

ITEM 15. EXHIBITS, FINANCIAL STATEMENT SCHEDULES, AND REPORTS ON FORM 10-K

- (a) The financial statements and financial statement schedules filed as part of this report in Item 8 are listed in the Index to Financial Statements contained in that item.
- (b) The following documents are filed as exhibits. Documents marked with an asterisk (*) are management contracts or compensatory plans, and portions of documents marked with a dagger (†) have been granted confidential treatment.
- 3.1 Restated and Amended Articles of Incorporation filed as Exhibit 3(i) to the Company's Form 10-QSB12G filed December 6, 1996, and incorporated herein by reference.
- 3.2 Amended and Restated Bylaws, amended and restated as of October 23, 2014, filed as Exhibit 3.2 to the Company's report on Form 10-K filed October 28, 2014, and incorporated herein by reference.
- 3.3 Articles of Amendment to Restated and Amended Articles of Incorporation, filed December 11, 1997 filed as Exhibit 3 to the Company's second quarter 1998 report on Form 10-QSB filed December 12, 1997, and incorporated herein by reference.
- 4.1 Form of Common Stock Certificate filed as Exhibit 4.1 to the Company's Form 10-QSB12G filed December 6, 1996, and incorporated herein by reference.
- 10.4* Employment Agreement with Roger C. Jackson dated August 1, 2002 filed as Exhibit 10.31 to the Company's 2003 report on Form 10-K filed October 23, 2003, and incorporated herein by reference.
- 10.6* Supplemental Executive Retirement Plan dated effective August 1, 2001 filed as Exhibit 10.27 to the Company's 2001 report on Form 10-K filed October 24, 2001, and incorporated herein by reference.
- 10.8* Performance-Based Restricted Stock Agreement, Series 1 dated September 2, 2005 filed as Exhibit 10.28 to the Company's report on Form 8-K filed September 7, 2005, and incorporated herein by reference.
- 10.9* Performance-Based Restricted Stock Agreement, Series 2 dated September 2, 2005 filed as Exhibit 10.29 to the Company's report on Form 8-K filed September 7, 2005, and incorporated herein by reference.
- 10.13† Agreement with Acme Chemical Marketing, LLC dated February 14, 2008 filed as Exhibit 10.41, to the Company's report on Form 10-Q filed March 17, 2008, and incorporated herein by reference.
- 10.14* Executive Severance Plan dated October 10, 2008, by and between the Company and its Eligible Employees filed as Exhibit 10.42, to the Company's report on Form 8-K filed October 13, 2008, and incorporated herein by reference.
- 10.17† Purchase Agreement dated December 31, 2007 with Intel Corporation filed as Exhibit 10.45 to the Company's report on Form 8-K filed May 13, 2009, and incorporated herein by reference.
- 10.18*

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2009 Long Term Incentive Plan of the Company, filed as Exhibit 10.46 to the Company's report on Form 10-K filed October 14, 2009, and incorporated herein by reference.

- 10.19 Second Amendment to Amended and Restated Credit Agreement with Wachovia Bank, National Association dated March 18, 2010 filed as Exhibit 10.47, to the Company's report on Form 8-K filed on March 30, 2010, and incorporated herein by reference.
- 10.27 Purchase Agreement between OM Group, Inc., OMG Kokkola Chemicals Holding (Two) BV, OMG Harjavalta Chemicals Holding BV, KMG Electronic Chemicals Ltd, KMG Electronic Chemicals, Ltd, KMG Electronic Chemicals Pte. LTD., KMG Electronic Chemicals, Inc. and KMG Chemicals. Inc. dated April 28, 2013 filed as Exhibit 10.27 to the Company's report on Form 10-Q filed on June 10, 2013, and incorporated herein by reference.
- 10.28 Share Purchase Agreement between OM Group, Inc., OMG Harjavalta Chemicals Holding BV, KMG Electronic Chemicals SAS and KMG Chemicals, Inc. dated April 28, 2013 filed as Exhibit 10.28 to the Company's report on Form 10-Q filed on June 10, 2013, and incorporated herein by reference.
- 10.29* Interim CEO Agreement with Mr. Fraser filed as Exhibit 10.29 to the Company's report on Form 8-K filed on July 2, 2013, and incorporated herein by reference.
- 10.31* Employment Agreement with Mr. Fraser dated September 24, 2013 filed as Exhibit 10.31 to the Company's report on Form 8-K filed on September 26, 2013, and incorporated herein by reference.
- 10.32 Form of the Indemnification Agreement filed as Exhibit 10.32 to the Company's report on Form 8-K filed on March 3, 2014, and incorporated herein by reference.
- 10.33 Second Amended and Restated Credit Agreement with Wells Fargo Bank, National Association Bank of America, N.A., HSBC Bank USA, National Association, and JPMorgan Chase Bank, N.A. dated October 9, 2014 initially filed as Exhibit 10.33 to the Company's report on Form 8-K filed October 10, 2014, and incorporated herein by reference.

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- 10.34 Asset Purchase Agreement dated as of January 16, 2015 between the Company, KMG-Bernuth, Inc. and Koppers Inc., filed as Exhibit 10.34 to the Company's report on Form 8-K filed on January 20, 2015, and incorporated herein by reference.
- 10.35 Agreement and Plan of Merger dated as of April 1, 2015, among KMG Chemicals, Inc., Valves Incorporated of Texas, KMG Victoria I, LLC, KMG Victoria II, LLC and the Principal Shareholders and the Shareholders' Representative named therein, filed as Exhibit 10.35 to the Company's report on Form 8-K filed on April 2, 2015, and incorporated herein by reference.
- 21.1 Subsidiaries of the Company.
- 23.1 Consent of KPMG LLP.
- 31 Certificates under Section 302 the Sarbanes-Oxley Act of 2002 of the Chief Executive Officer and the Chief Financial Officer.
- 32 Certificates under Section 906 of the Sarbanes-Oxley Act of 2002 of the Chief Executive Officer and the Chief Financial Officer.
- 101.INS^ XBRL Instance Document
- 101.SCH^ XBRL Schema Document
- 101.CAL^ XBRL Calculation Linkbase Document
- 101.DEF^ XBRL Definition Linkbase Document
- 101.LAB^ XBRL Label Linkbase Document
- 101.PRE^ XBRL Presentation Linkbase Document

(c) Schedule II-Valuation and Qualifying Accounts and Reserves. All other schedules are omitted because they are not applicable or the required information is contained in the applicable financial statements of notes thereto.

KMG Chemicals, Inc.

Schedule II — Valuation and Qualifying Accounts

Fiscal years ended July 31, 2015, 2014 and 2013

(in thousands)

| Description | Balance at beginning of period | Charged to costs and expenses | Additions/ Deductions | Balance at end of period |
|--|--------------------------------|-------------------------------|-----------------------|--------------------------|
| Year ended July 31, 2015: | | | | |
| Allowance for doubtful accounts | \$ 272 | \$ — | \$ (128) | \$ 144 |
| Inventory obsolescence | 290 | 941 | (750) | 481 |
| Valuation allowance on deferred tax assets | 1,725 | 291 | — | 2,016 |
| Year ended July 31, 2014: | | | | |
| Allowance for doubtful accounts | \$ 224 | \$ 108 | \$ (60) | \$ 272 |
| Inventory obsolescence | 180 | 221 | (111) | 290 |
| Valuation allowance on deferred tax assets | — | 1,725 | — | 1,725 |
| Year ended July 31, 2013: | | | | |
| Allowance for doubtful accounts | \$ 16 | \$ 208 | \$ — | \$ 224 |
| Inventory obsolescence | 493 | 107 | (420) | 180 |
| Valuation allowance on deferred tax assets | — | — | — | — |

SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

KMG CHEMICALS, INC.

By: /s/ Christopher T. Fraser
Christopher T. Fraser

Date: November 27, 2015

President, Chief Executive Officer and Director

Pursuant to the Securities Exchange Act of 1934, this report has been signed below by the following persons on behalf of the registrant and in the capacities and on the dates indicated.

By: /s/ Malinda G. Passmore
Malinda G. Passmore, Vice President and Chief
Financial Officer

Date: November 27, 2015

By: /s/ Marcelino Rodriguez
Marcelino Rodriguez, Controller and
Chief Accounting Officer

Date: November 27, 2015

By: /s/ James F. Gentilcore
James F. Gentilcore, Director

Date: November 27, 2015

By: /s/ Gerald G. Ermentrout
Gerald G. Ermentrout, Director

Date: November 27, 2015

By: /s/ George W. Gilman
George W. Gilman, Director

Date: November 27, 2015

By: /s/ Robert Harrer
Robert Harrer, Director

Date: November 27, 2015

By: /s/ John C. Hunter, III
John C. Hunter, III, Director

Date: November 27, 2015

By: /s/ Fred C. Leonard
Fred C. Leonard III, Director

Date: November 27, 2015

By: /s/ Karen A. Twitchell
Karen A. Twitchell, Director

Date: November 27, 2015

