KAISER ALUMINUM CORP
Form 10-Q
October 25, 2018

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

FORM 10-Q

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

For the quarterly period ended September 30, 2018

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

For the transition period from ______________________________
to____

Commission File Number: 1-09447

KAISER ALUMINUM CORPORATION

(Exact name of registrant as specified in its charter)

Delaware	**94-3030279**
(State of incorporation)	(I.R.S. Employer Identification No.)
27422 Portola Parkway, Suite 200 Foothill Ranch, California	**92610-2831**
(Address of principal executive offices)	(Zip Code)

(949) 614-1740

(Registrant's telephone number, including area code)

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, and (2) has been subject to such filing requirements for the past 90 days. Yes þ No o

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

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

Large accelerated filer þ	Accelerated filer o
Non-accelerated filer o (Do not check if a smaller reporting company)	Smaller reporting company o
	Emerging growth company o

If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the Exchange Act. o

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

As of October 22, 2018, there were 16,501,758 shares of common stock of the registrant outstanding.

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KAISER ALUMINUM CORPORATION AND SUBSIDIARY COMPANIES
PART I – FINANCIAL INFORMATION

Item 1. ***Financial Statements***
CONSOLIDATED BALANCE SHEETS (UNAUDITED)

	September 30, 2018	December 31, 2017
	(In millions of dollars, except share and per share amounts)	
ASSETS		
Current assets:		
Cash and cash equivalents	$94.3	$51.1
Short-term investments	88.4	183.7
Receivables:		
Trade receivables, net	194.5	165.0
Other	24.4	15.5
Contract assets	51.0	—
Inventories	196.2	207.9
Prepaid expenses and other current assets	24.2	33.4
Total current assets	673.0	656.6
Property, plant and equipment, net	595.4	571.4
Deferred tax assets, net	42.2	72.0
Intangible assets, net	33.0	25.0
Goodwill	43.4	18.8
Other assets	39.0	41.4
Total	$1,426.0	$1,385.2
LIABILITIES AND STOCKHOLDERS' EQUITY		
Current liabilities:		
Accounts payable	$120.4	$90.0
Accrued salaries, wages and related expenses	35.1	42.6
Other accrued liabilities	37.0	40.5
Total current liabilities	192.5	173.1
Net liabilities of Salaried VEBA	31.8	31.9
Deferred tax liabilities	4.3	4.3
Long-term liabilities	64.7	60.0
Long-term debt	370.2	369.6
Total liabilities	663.5	638.9
Commitments and contingencies – Note 7		
Stockholders' equity:		
Preferred stock, 5,000,000 shares authorized at both September 30, 2018 and December 31, 2017; no shares were issued and outstanding at September 30, 2018 and December 31, 2017	—	—
Common stock, par value $0.01, 90,000,000 shares authorized at both September 30, 2018 and at December 31, 2017; 22,471,628 shares issued and 16,547,237 shares outstanding at September 30, 2018; 22,393,537 shares issued and 16,773,586 shares outstanding at December 31, 2017	0.2	0.2
Additional paid in capital	1,057.4	1,055.9
Retained earnings	135.6	85.5
Treasury stock, at cost, 5,924,391 shares at September 30, 2018 and 5,619,951 shares at December 31, 2017, respectively	(390.9)	(358.6)

Accumulated other comprehensive loss	(39.8)	(36.7)
Total stockholders' equity	762.5	746.3
Total	$1,426.0	$1,385.2

The accompanying notes to interim consolidated financial statements are an integral part of these statements.

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KAISER ALUMINUM CORPORATION AND SUBSIDIARY COMPANIES
STATEMENTS OF CONSOLIDATED INCOME (UNAUDITED)

	Quarter Ended September 30,		Nine Months Ended September 30,	
	2018	2017	2018	2017
	(In millions of dollars, except share and per share amounts)			
Net sales	$393.1	$332.8	$1,196.5	$1,044.4
Costs and expenses:				
Cost of products sold, excluding depreciation and amortization and other items[1]	323.3	256.4	983.4	808.7
Depreciation and amortization	11.0	10.2	32.4	29.3
Selling, general, administrative, research and development[2]	23.9	24.7	73.9	74.7
Goodwill impairment	—	—	—	18.4
Other operating charges, net	—	—	0.1	—
Total costs and expenses	358.2	291.3	1,089.8	931.1
Operating income	34.9	41.5	106.7	113.3
Other income (expense):				
Interest expense	(5.7)	(5.3)	(17.0)	(16.4)
Other income (expense), net – Note 10	0.7	(0.2)	0.3	0.5
Income before income taxes	29.9	36.0	90.0	97.4
Income tax provision	(8.2)	(16.1)	(21.9)	(36.8)
Net income	$21.7	$19.9	$68.1	$60.6
Net income per common share:				
Basic	$1.31	$1.18	$4.09	$3.55
Diluted	$1.29	$1.16	$4.03	$3.49
Weighted-average number of common shares outstanding (in thousands):				
Basic	16,573	16,834	16,654	17,072
Diluted	16,783	17,160	16,882	17,363
Dividends declared per common share	$0.55	$0.50	$1.65	$1.50

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1. See Note 5 for discussion of our adoption of ASU 2017-12 (as defined in Note 1) and the related reclassification of amounts previously presented in the Statements of Consolidated Income within Unrealized (gain) loss on derivative instruments and now included within Cost of products sold, excluding depreciation and amortization and other items.
2. See Note 1 for discussion of our adoption of ASU 2017-07 (as defined in Note 1) and the related reclassification of amounts previously presented in the Statements of Consolidated Income within Selling, general, administrative, research and development and now included within Other income (expense).

The accompanying notes to interim consolidated financial statements are an integral part of these statements.

KAISER ALUMINUM CORPORATION AND SUBSIDIARY COMPANIES
STATEMENTS OF CONSOLIDATED COMPREHENSIVE INCOME (UNAUDITED)

	Quarter Ended		Nine Months Ended	
	September 30,		September 30,	
	2018	2017	2018	2017
	(In millions of dollars)			
Net income	$21.7	$19.9	$68.1	$60.6
Other comprehensive (loss) income, net of tax – Note 8:				
Defined benefit pension plan and Salaried VEBA	1.1	0.8	3.5	2.5
Available for sale securities	(0.2)	0.3	(0.5)	0.6
Cash flow hedges	(1.7)	0.4	(5.7)	0.7
Foreign currency translation	—	0.1	—	0.2
Other comprehensive (loss) income, net of tax	(0.8)	1.6	(2.7)	4.0
Comprehensive income	$20.9	$21.5	$65.4	$64.6

The accompanying notes to interim consolidated financial statements are an integral part of these statements.

KAISER ALUMINUM CORPORATION AND SUBSIDIARY COMPANIES
STATEMENT OF CONSOLIDATED STOCKHOLDERS' EQUITY (UNAUDITED)

	Common Shares Outstanding	Common Stock	Additional Paid in Capital	Retained Earnings	Treasury Stock	Accumulated Other Comprehensive Loss	Total
	(In millions of dollars, except share and per share amounts)						
BALANCE, December 31, 2017	16,773,586	$ 0.2	$1,055.9	$85.5	$(358.6)	$ (36.7)	$746.3
Cumulative-effect adjustment[1]	—	—	—	10.5	—	(0.4)	10.1
BALANCE, January 1, 2018	16,773,586	$ 0.2	$1,055.9	$96.0	$(358.6)	$ (37.1)	$756.4
Net income	—	—	—	68.1	—	—	68.1
Other comprehensive loss, net of tax	—	—	—	—	—	(2.7)	(2.7)
Issuance of non-vested shares to non-employee directors	9,009	—	—	—	—	—	—
Issuance of common shares to non-employee directors	1,954	—	0.2	—	—	—	0.2
Issuance of common shares to employees upon vesting of restricted stock units and performance shares	135,294	—	—	—	—	—	—
Cancellation of shares to cover employees' tax withholdings upon vesting of non-vested shares	(68,166)	—	(6.9)	—	—	—	(6.9)
Repurchase of common stock	(304,440)	—	—	—	(32.3)	—	(32.3)
Cash dividends on common stock and restricted shares and dividend equivalents on restricted stock units and performance shares	—	—	—	(28.5)	—	—	(28.5)
Amortization of unearned equity compensation	—	—	8.2	—	—	—	8.2
BALANCE, September 30, 2018	16,547,237	$ 0.2	$1,057.4	$135.6	$(390.9)	$ (39.8)	$762.5

[1] See Note 1 for discussion of our adoption of ASC 606 and ASU 2016-01 (as defined in Note 1).

The accompanying notes to interim consolidated financial statements are an integral part of these statements.

KAISER ALUMINUM CORPORATION AND SUBSIDIARY COMPANIES
STATEMENTS OF CONSOLIDATED CASH FLOWS (UNAUDITED)

	Nine Months Ended September 30,	
	2018	2017
	(In millions of dollars)	
Cash flows from operating activities:		
Net income	$68.1	$60.6
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation of property, plant and equipment	31.3	28.3
Amortization of definite-lived intangible assets	1.1	1.0
Amortization of debt discount and debt issuance costs	0.8	0.9
Deferred income taxes	27.4	38.6
Non-cash equity compensation	8.4	10.1
Gain on disposition of available for sale securities	(2.4)	(1.8)
Non-cash asset impairment charge	0.1	18.4
Gain on disposition of property, plant and equipment	(0.2)	(0.4)
Non-cash net periodic postretirement benefit cost relating to Salaried VEBA	4.6	3.4
Other non-cash changes in assets and liabilities	15.6	(14.8)
Changes in operating assets and liabilities:		
Trade and other receivables	(35.7)	(4.0)
Contract assets	4.6	—
Inventories	(25.6)	(10.6)
Prepaid expenses and other current assets	(1.6)	(1.8)
Accounts payable	31.1	21.6
Accrued liabilities	(1.0)	0.9
Annual variable cash contributions to VEBAs	(15.7)	(20.0)
Long-term assets and liabilities, net	1.6	1.1
Net cash provided by operating activities[1]	112.5	131.5
Cash flows from investing activities[2]:		
Capital expenditures	(53.1)	(56.1)
Purchase of available for sale securities	(111.9)	(196.0)
Purchase of equity securities	(0.9)	—
Proceeds from disposition of available for sale securities	208.7	237.2
Cash payment for acquisition of Imperial Machine & Tool Co., net of cash received	(43.3)	—
Proceeds from disposal of property, plant and equipment	0.6	0.6
Net cash provided by (used in) investing activities	0.1	(14.3)
Cash flows from financing activities[2]:		
Repayment of capital lease	(0.5)	(0.2)
Cancellation of shares to cover employees' tax withholdings upon vesting of non-vested shares	(6.9)	(4.5)
Repurchase of common stock	(31.9)	(66.7)
Cash dividends and dividend equivalents paid	(28.5)	(26.4)
Net cash used in financing activities	(67.8)	(97.8)
Net increase in cash, cash equivalents and restricted cash during the period	44.8	19.4
Cash, cash equivalents and restricted cash at beginning of period	64.3	67.7
Cash, cash equivalents and restricted cash at end of period	$109.1	$87.1

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KAISER ALUMINUM CORPORATION AND SUBSIDIARY COMPANIES
STATEMENTS OF CONSOLIDATED CASH FLOWS (UNAUDITED) (CONTINUED)

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[1] See Note 9 for adjustments made to arrive at our Consolidated Balance Sheet as of January 1, 2018 upon adopting ASC 606 (as defined in Note 1).
[2] See Note 13 for the supplemental disclosure on non-cash transactions.

The accompanying notes to interim consolidated financial statements are an integral part of these statements.

KAISER ALUMINUM CORPORATION AND SUBSIDIARY COMPANIES
NOTES TO INTERIM CONSOLIDATED FINANCIAL STATEMENTS - UNAUDITED

1. Summary of Significant Accounting Policies

This Quarterly Report on Form 10-Q (this "Report") should be read in conjunction with the Company's Annual Report on Form 10-K for the year ended December 31, 2017. Unless the context otherwise requires, references in these notes to interim consolidated financial statements - unaudited to "Kaiser Aluminum Corporation," "we," "us," "our," "the Company" and "our Company" refer collectively to Kaiser Aluminum Corporation and its subsidiaries.

Organization and Nature of Operations. Kaiser Aluminum Corporation specializes in the production of semi-fabricated specialty aluminum mill products, such as aluminum plate and sheet and extruded and drawn products, for the following end market applications: aerospace and high strength ("Aero/HS products"), automotive applications ("Automotive Extrusions"), general engineering ("GE products") and other industrial ("Other products"). Our business is organized into one operating segment. See Note 14 for additional information regarding our business, product and geographical area information and concentration of risk.

Principles of Consolidation and Basis of Presentation. The accompanying unaudited consolidated financial statements include the accounts of our wholly owned subsidiaries and are prepared in accordance with United States generally accepted accounting principles ("GAAP") and the rules and regulations of the Securities and Exchange Commission ("SEC") applicable for interim periods and, therefore, do not include all information and footnotes required by GAAP for complete financial statements. In management's opinion, all adjustments (which include normal recurring adjustments) considered necessary for a fair presentation have been included. The results of operations for our interim periods are not necessarily indicative of the results of operations that may be achieved for the entire 2018 fiscal year. The financial information as of December 31, 2017 is derived from our audited consolidated financial statements and footnotes included in our Annual Report on Form 10-K for the year ended December 31, 2017. We have reclassified certain amounts in prior-period financial statements to conform to the current period’s presentation. On the Statements of Consolidated Income, prior period presentation of Unrealized (gain) loss on derivative instruments is now contained within "Cost of products sold, excluding depreciation and amortization and other items." See Note 5 for additional details. See Note 14 for changes relating to the consolidation of the All Other business unit into the Fabricated Products reporting segment.

Use of Estimates in the Preparation of Financial Statements. The preparation of financial statements in accordance with GAAP requires the use of estimates and assumptions that affect the reported amounts of assets and liabilities, disclosure of contingent assets and liabilities known to exist as of the date the financial statements are published and the reported amounts of revenues and expenses during the reporting period. Uncertainties with respect to such estimates and assumptions are inherent in the preparation of our consolidated financial statements; accordingly, it is possible that the actual results could differ from these estimates and assumptions, which could have a material effect on the reported amounts of our consolidated financial position and results of operations.

Fair Value Measurements. We apply the fair value hierarchy established by GAAP for the recognition and measurement of certain financial assets and liabilities. An asset or liability's fair value classification within the hierarchy is determined based on the lowest level input that is significant to the fair value measurement. In determining fair value, we utilize valuation techniques that maximize the use of observable inputs and minimize the use of unobservable inputs to the extent possible and consider counterparty risk in our assessment of fair value. We also review the underlying inputs that are significant to the fair value measurement of financial instruments to determine if a transfer among hierarchy levels is appropriate. We historically have not had significant transfers into or out of each hierarchy level.

Financial assets and liabilities that we measure at fair value each period include our derivative instruments, equity investments related to our deferred compensation plan and debt investment securities classified as available for sale securities (see Note 4). Additionally, we measure at fair value once each year at December 31 the plan assets of the Salaried VEBA (defined in Note 4) and our Canadian defined benefit pension plan. We record our remaining financial assets and liabilities at carrying value.

For a majority of our non-financial assets and liabilities, which include goodwill, intangible assets, inventories and property, plant and equipment, we are not required to measure their fair value on a recurring basis. However, if certain triggering events occur (or at least annually for goodwill), an evaluation of the affected non-financial asset or liability will be required, which could result in a reduction to the carrying amount of such asset or liability. See Note 3 for a discussion of our business

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acquisition during the quarter ended September 30, 2018, as well as the goodwill impairment charge recorded during the quarter ended June 30, 2017 related to the operations at our Chandler, Arizona (Extrusion) facility.

None of our non-financial assets and liabilities subject to fair value assessments on a non-recurring basis required a material adjustment to the carrying amount of such assets and liabilities for the quarter and nine months ended September 30, 2018.

Inventories. Inventories are stated at the lower of cost or market value. Finished products, work-in-process and raw material inventories are stated on the last-in, first-out ("LIFO") basis. At September 30, 2018 and December 31, 2017, the current cost of our inventory exceeded its stated LIFO value by $42.9 million and $24.3 million, respectively. Other inventories are stated on the first-in, first-out basis and consist of operating supplies, which are materials and supplies to be consumed during the production process. Inventory costs consist of material, labor and manufacturing overhead, including depreciation. Abnormal costs, such as idle facility expenses, freight, handling costs and spoilage, are accounted for as current period charges (see Note 2 for the components of inventories).

Replacement Parts. Replacement parts consist of preventative maintenance and capital spare parts, which are stated on the first-in, first-out basis. Replacement parts are recorded within Prepaid expenses and other current assets or Other assets depending on whether or not the expected utilization of the replacement parts is to occur within the current operating cycle.

Property, Plant and Equipment, Net. Property, plant and equipment, net is recorded at cost and includes construction in progress (see Note 2). Interest related to the construction of qualifying assets is capitalized as part of the construction costs. The amount of interest expense capitalized as construction in progress was $0.4 million and $0.7 million during the quarters ended September 30, 2018 and September 30, 2017, respectively. The amount of interest expense capitalized as construction in progress was $1.3 million and $1.9 million during the nine months ended September 30, 2018 and September 30, 2017, respectively.

Depreciation is computed using the straight-line method at rates based on the estimated useful lives of the various classes of assets. Capital lease assets and leasehold improvements are depreciated on a straight-line basis over the shorter of the estimated useful lives of the assets or the lease term.

We classify assets as held for sale only when an asset is being actively marketed and expected to sell within 12 months. Assets held for sale are initially measured at the lesser of the assets' carrying amount and the fair value less costs to sell.

Derivative Financial Instruments. Consistent with guidelines established by management and approved by our Board of Directors, we use derivative financial instruments to mitigate our exposure to changes in the market price of aluminum, alloying metals, energy, and, to a lesser extent, foreign currency exchange rates. We do not use derivative financial instruments for trading or other speculative purposes. Hedging transactions are executed centrally on behalf of all of our operations to minimize transaction costs, monitor consolidated net exposures and allow for increased responsiveness to changes in market factors.

We reflect the fair value of all of our derivative instruments on our Consolidated Balance Sheets (see Note 5). The fair value of hedges settling within one year is included in Prepaid expenses and other current assets or Other accrued liabilities. The fair value of hedges settling beyond one year is included in Other assets or Long-term liabilities.

Prior to our adoption of ASU 2017-12 (as defined below under "*Adoption of New Accounting Standards")*, we did not meet the documentation requirements for hedge (deferral) accounting related to our aluminum and energy derivatives. Accordingly, we recorded unrealized gain or loss associated with these hedges in the Statements of Consolidated Income. Subsequent to our adoption of ASU 2017-12 on January 1, 2018, our aluminum and energy derivatives qualified for hedge (deferral) accounting and, as such, we designated such hedges as cash flow hedges. Forward swap contracts for zinc and copper ("Alloying Metals") used in our fabrication operations are also designated as cash flow hedges. Unrealized gains and losses associated with our cash flow hedges are deferred in Other comprehensive income, net of tax and reclassified to Cost of products sold, excluding depreciation and amortization and other items when such hedges settle (see Note 5).

From time to time, we enter into foreign currency forward contracts to protect the value of anticipated foreign currency expenses associated with cash commitments for equipment purchases. We do not meet the documentation requirements for hedge (deferral) accounting related to foreign currency derivatives and, as such, gains and losses (both unrealized and realized) related to our foreign currency forward contracts are reflected as an increase or reduction in Other income, net.

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Self Insurance of Workers' Compensation and Employee Healthcare Liabilities. We self-insure the majority of the costs of workers' compensation benefits and employee healthcare benefits and rely on insurance coverage to protect us from large losses on individual claims. Workers' compensation liabilities are based on a combination of estimates for: (i) incurred-but-not-reported claims and (ii) the ultimate expense of incurred claims. Such estimates are based on judgment, using our historical claims data and information and analysis provided by actuarial and claims advisors, our insurance carriers and other professionals. Our undiscounted workers' compensation liabilities were estimated at $27.9 million and $24.8 million as of September 30, 2018 and December 31, 2017, respectively. However, we account for our workers' compensation accrued liability on a discounted basis, using a discount rate of 3.00% and 2.25% at September 30, 2018 and December 31, 2017, respectively. Accrued liabilities for employee healthcare benefits, which are estimates of unpaid incurred medical and prescription drug costs as provided by our healthcare administrators, were $3.1 million and $3.5 million as of September 30, 2018 and December 31, 2017, respectively.
Short-Term Incentive Plans ("STI Plans"). We have annual short-term incentive compensation plans for senior management and certain other employees payable at our election in cash, shares of common stock, or a combination of cash and shares of common stock. Amounts earned under STI Plans are based on our adjusted earnings before interest, taxes, depreciation and amortization ("Adjusted EBITDA"), modified for certain safety, quality, delivery, cost and individual performance factors. The Adjusted EBITDA targets are determined based on the return on adjusted net assets. Most of our production facilities have similar programs for both hourly and salaried employees. As of September 30, 2018, we had a liability of $10.6 million recorded within Accrued salaries, wages and related expenses for estimated probable future payments relating to the nine month performance period of our 2018 STI Plan.
Long-Term Incentive Programs ("LTI Programs"). Executive officers and other key employees of the Company, as well as non-employee directors of the Company, are eligible to participate in the Kaiser Aluminum Corporation 2016 Equity and Incentive Compensation Plan approved by stockholders on May 26, 2016 ("2016 Plan"). At September 30, 2018, 577,300 shares were available for awards under the 2016 Plan. We issue new shares of our common stock upon vesting under the 2016 Plan.

Adoption of New Accounting Pronouncements

Accounting Standards Update ("ASU") No. 2014-09, *Revenue from Contracts with Customers (Topic 606)* ("ASU 2014-09") was issued in May 2014 and requires an entity to recognize revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. We adopted ASU 2014-09, including its subsequent amendments as codified under Accounting Standards Codification Topic 606 ("ASC 606"), during the quarter ended March 31, 2018. Upon adoption under the modified retrospective method, we elected to apply the guidance only to contracts that were not completed at the date of initial application, which resulted in a cumulative-effect increase of $10.1 million (see Note 9) to our Retained earnings (net of a $3.3 million tax impact) on January 1, 2018. Comparative information in this report has not been adjusted and continues to be reported under previous revenue recognition guidance within Accounting Standards Codification Topic 605 ("ASC 605"). See Statement of Consolidated Stockholders' Equity and Note 9 for details of the significant changes and quantitative impacts of the changes, as well as our policy on revenue recognition.
ASU No. 2016-01, *Financial Instruments - Overall (Subtopic 825-10): Recognition and Measurement of Financial Assets and Financial Liabilities* ("ASU 2016-01"), was issued in January 2016. The amendments in ASU 2016-01 require equity investments to be measured at fair value with changes in fair value recognized in net income. Equity investments related to our deferred compensation plan that had previously been accounted for as available for sale securities are now accounted for as equity investments with changes in fair value recorded within net income. As such, we recorded a cumulative-effect increase of $0.4 million to our Retained earnings (net of a $0.2 million tax impact) on January 1, 2018 to remove the balance of mark-to-market adjustments recorded within Accumulated other comprehensive income at December 31, 2017. See Note 4 for additional details on our deferred compensation plan, including the fair value of related equity investments.

ASU No. 2017-07, *Compensation - Retirement Benefits (Topic 715): Improving the Presentation of Net Periodic Pension Cost and Net Periodic Postretirement Benefit Cost* ("ASU 2017-07"), was issued in March 2017. ASU 2017-07 amends the requirements related to the income statement presentation of the components of net periodic benefit cost for our defined benefit pension and other postretirement plans. Specifically, ASU 2017-07 requires us to: (i) disaggregate the current-service-cost component from the "other components" of net benefit cost and present it with other current compensation costs for related employees in the income statement and (ii) present the other components elsewhere in the income statement and outside of

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income from operations. As a result of our retrospective adoption of ASU 2017-07, we reclassified amounts that had previously been presented within Selling, general, administrative, research and development to Other income (expense), net in the Statements of Consolidated Income. See Note 4 for further discussion of our defined benefit pension and other postretirement plans.

ASU No. 2017-12, *Derivatives and Hedging (Topic 815): Targeted Improvements to Accounting for Hedging Activities* ("ASU 2017-12"), was issued in August 2017. The amendments under ASU 2017-12 refine and expand hedge accounting requirements for both financial (e.g., interest rate) and commodity risks. Its provisions create more transparency around how economic results are presented, both on the face of the financial statements and in the related notes. It also makes certain targeted improvements to simplify the application of hedge accounting guidance. There was no cumulative effect adjustment to record as a result of early adopting ASU 2017-12 in the quarter ended March 31, 2018; however, we designated all of our outstanding commodity hedges as cash flow hedges beginning January 1, 2018. We therefore have significantly reduced the mark-to-market adjustments that have historically been recorded within the Statements of Consolidated Income. These adjustments have instead been recorded within Other comprehensive income, net of tax beginning in the quarter ended March 31, 2018. See Note 5 for further discussion of our derivatives and hedging programs.

There were no material impacts on our consolidated financial statements resulting from our adoption in the quarter ended March 31, 2018 of ASU No. 2017-09, *Compensation - Stock Compensation (Topic 718): Scope of Modification Accounting.*

Accounting Pronouncements Issued But Not Yet Adopted

ASU No. 2016-02, *Leases (Topic 842): Amendments to the Financial Accounting Standards Board Accounting Standards Codification* ("ASU 2016-02"), was issued in February 2016. Under ASU 2016-02, lessees will need to recognize a right-of-use asset and a lease liability for virtually all of their leases (other than leases that meet the definition of a short-term lease). For income statement purposes, a dual model was retained, requiring leases to be classified as either operating or finance. Operating leases will result in straight-line expense (similar to current operating leases) while finance leases will result in a front-loaded expense pattern (similar to current capital leases). ASU 2016-02 was subsequently amended by three additional pronouncements: (i) ASU No. 2018-01, *Leases (Topic 842): Land Easement Practical Expedient for Transition to Topic 842*; (ii) ASU No. 2018-10, *Codification Improvements to Topic 842, Leases*; and (iii) ASU No. 2018-11, *Leases (Topic 842): Targeted Improvements*. ASU 2016-02 and its subsequent amendments (together "ASC 842") become effective for us in the first quarter of 2019. We are currently assessing the impact and expect the adoption of ASC 842 in 2019 to have a material impact on our consolidated financial statements. We plan to apply the optional transition method allowed by ASU 2018-11 upon adoption of ASC 842 in the first quarter of 2019.

ASU No. 2016-13, *Financial Instruments - Credit Losses (Topic 326): Measurement of Credit Losses on Financial Instruments* ("ASU 2016-13"), was issued in June 2016. Under ASU 2016-13, existing guidance on reporting credit losses for trade and other receivables and available for sale debt securities will be replaced with a new forward-looking "expected loss" model that generally will result in the earlier recognition of allowances for losses. We are currently in the process of evaluating the impact of adopting ASU 2016-13 in 2020, but do not expect it to have a material impact on our consolidated financial statements.

ASU No. 2018-15, *Intangibles - Goodwill and Other - Internal-Use Software (Subtopic 350-40): Customer's Accounting for Implementation Costs Incurred in a Cloud Computing Arrangement that is a Service Contract* ("ASU 2018-15"), was issued in August 2018. Under ASU 2018-15, requirements for capitalizing implementation costs incurred in a hosting arrangement (cloud computing) that is a service contract, are to be aligned with the requirements for capitalizing implementation costs incurred to develop or obtain internal-use software. We are currently in the process of evaluating the impact of adopting ASU 2018-15 in 2020, but do not expect it to have a material impact on our consolidated financial statements.

We do not anticipate any material impact on our consolidated financial statements upon the adoption of the following accounting pronouncements: (i) ASU No. 2018-07, *Compensation-Stock Compensation (Topic 718): Improvements to*

Nonemployee Share-Based Payment Accounting; (ii) ASU No. 2018-08, *Not-for-Profit Entities (Topic 958): Clarifying the Scope and the Accounting Guidance for Contributions Received and Contributions Made*; (iii) ASU 2018-13*, Fair Value Measurement (Topic 820): Disclosure Framework - Changes to the Disclosure Requirements for Fair Value Measurement*; and (iv) ASU 2018-14, *Compensation - Retirement Benefits - Defined Benefit Plans - General (Subtopic 715-20): Disclosure Framework - Changes to the Disclosure Requirements for Defined Benefit Plans*.

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2. Supplemental Balance Sheet Information

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	September 30, 2018	December 31, 2017
	(In millions of dollars)	
Cash and Cash Equivalents		
Cash and money market funds	$23.2	$ 23.5
Commercial paper	71.1	27.6
Total	$94.3	$ 51.1
Trade Receivables, Net		
Billed trade receivables	$194.2	$ 165.9
Unbilled trade receivables	1.5	0.3
Trade receivables, gross	195.7	166.2
Allowance for doubtful receivables	(1.2)	(1.2)
Trade receivables, net	$194.5	$ 165.0
Inventories		
Finished products	$41.4	$ 63.8
Work-in-process	73.3	78.3
Raw materials	76.2	61.3
Operating supplies	5.3	4.5
Total	$196.2	$ 207.9
Property, Plant and Equipment, Net		
Land and improvements	$21.4	$ 21.1
Buildings and leasehold improvements	96.4	92.1
Machinery and equipment	736.3	689.1
Construction in progress	38.1	35.1
Property, plant and equipment, gross	892.2	837.4
Accumulated depreciation	(298.4)	(267.9)
Assets held for sale	1.6	1.9
Property, plant and equipment, net	$595.4	$ 571.4
Other Accrued Liabilities		
Uncleared cash disbursements	$5.6	$ 7.3
Accrued income taxes and taxes payable	8.2	6.8
Accrued annual contribution to VEBAs – Note 4	—	15.7
Accrued interest	8.4	2.9
Other	14.8	7.8
Total	$37.0	$ 40.5

	September 30, 2018	December 31, 2017
	(In millions of dollars)	
Long-Term Liabilities		
Workers' compensation accruals	$24.5	$ 22.6
Long-term environmental accrual – Note 7	14.4	15.8
Other long-term liabilities	25.8	21.6
Total	$64.7	$ 60.0

3. Business Combinations and Goodwill

Business Combinations. On September 19, 2018, we acquired Imperial Machine and Tool Co. ("IMT"), located in Columbia, New Jersey, for $43.3 million in cash, net of cash received. IMT specializes in multi-material additive manufacturing and machining technologies for demanding aerospace and defense, automotive, high-tech and general industrial applications. The acquisition allows us to gain further insights into the potentially disruptive additive manufacturing technology and enhances our ability to address customer needs by broadening our capability to provide innovative solutions for demanding applications. IMT has approximately 25 employees.

The following table summarizes recognized amounts of identifiable assets acquired and liabilities assumed at the acquisition date (in millions of dollars):

Accounts receivable	$2.7
Inventory	3.4
Property, plant and equipment	4.1
Identifiable intangible assets with definite lives	9.1
Goodwill	24.6
Accounts payable and other current liabilities	(0.6)
Consideration paid, net of cash received	$43.3

Total acquisition-related costs were approximately $0.3 million, all of which were expensed during the nine months ended September 30, 2018 and were included in Selling, general, administrative, research and development in the Statements of Consolidated Income.

Goodwill. The following table presents the changes to goodwill during the nine months ended September 30, 2018 (in millions of dollars):

	December 31, 2017	Increases to Goodwill[1]	September 30, 2018
Goodwill	$ 37.2	$ 24.6	$ 61.8
Accumulated impairment loss	(18.4)	—	(18.4)
Carrying value	$ 18.8	$ 24.6	$ 43.4

1 The goodwill of $24.6 million arising from the acquisition of IMT after allocating the consideration paid, net of cash received, to all other identifiable assets is expected to be deductible for income tax purposes over the next 15 years.

Due to a reduction in our long-term demand assumption for hard alloy extruded shapes, we recorded an impairment charge of $18.4 million with respect to our Chandler, Arizona (Extrusion) facility for the quarter ended June 30, 2017 within Operating income in the Statements of Consolidated Income.

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4. Employee Benefits

Pension and Similar Benefit Plans. We provide contributions to: (i) defined contribution 401(k) savings plans for salaried employees and certain hourly employees; (ii) a non-qualified, unfunded, unsecured plan of deferred compensation (see "*Deferred Compensation Plan*" below); (iii) multi-employer pension plans sponsored by the United Steel, Paper and Forestry, Rubber, Manufacturing, Energy, Allied Industrial and Service Workers International Union AFL-CIO, CLC ("USW"), the International Association of Machinists and certain other unions at certain of our production facilities; and (iv) a defined benefit plan for salaried employees at our London, Ontario (Canada) facility.
Deferred Compensation Plan. We have a non-qualified, unsecured plan of deferred compensation for key employees who would otherwise suffer a loss of benefits under our defined contribution plan as a result of the limitations imposed by the Internal Revenue Code of 1986. Despite the plan being an unfunded plan, we make an annual contribution to a rabbi trust to fulfill future funding obligations as contemplated by the terms of the plan. These assets are held in various investment funds at certain registered investment companies. Upon adoption of ASU 2016-01 on January 1, 2018 (see Note 1), these investments are now accounted for as equity investments with changes in fair value recorded within Other income (expense), net. During the quarter and nine months ended September 30, 2018, we recognized a $0.1 million loss and a $0.3 million gain, respectively, on equity securities still held at each respective reporting date related to the deferred compensation plan. Assets of our deferred compensation plan are classified within Level 2 of the fair value hierarchy and are measured and recorded at fair value based on their quoted market prices. The fair value of these assets at September 30, 2018 and December 31, 2017 was $10.9 million and $9.8 million, respectively, and are included in Other assets. Offsetting liabilities relating to the deferred compensation plan are included in Long-term liabilities.
Salaried VEBA Postretirement Obligation. Certain retirees who retired prior to 2004 and certain employees who were hired prior to February 2002 and have subsequently retired or will retire with the requisite age and service, along with their surviving spouses and eligible dependents, are eligible to participate in a voluntary employees' beneficiary association ("VEBA") that provides healthcare cost, medical cost and long-term care insurance cost reimbursement benefits ("Salaried VEBA"). We have an ongoing obligation with no express termination date to make variable cash contributions up to a maximum of $2.9 million each year to the Salaried VEBA. We paid the maximum of $2.9 million with respect to 2017 during the quarter ended March 31, 2018. We account for the Salaried VEBA as a defined benefit plan in our financial statements.
Union VEBA Postretirement Obligation. Certain other eligible retirees represented by certain unions along with their surviving spouses and eligible dependents participate in a separate VEBA ("Union VEBA"). During the quarter ended March 31, 2018, we made a $12.8 million cash contribution to the Union VEBA with respect to the nine months ended September 30, 2017. This was our final contribution. We have no ongoing obligation to make further contributions to the Union VEBA.
Fair Value of Plan Assets. The plan assets of the Salaried VEBA and our Canadian pension plan are measured annually on December 31 and reflected in our Consolidated Balance Sheets at fair value. In determining the fair value of the plan assets at an annual period end, we utilize primarily the results of valuations supplied by the investment advisors responsible for managing the assets of each plan, which we independently review for reasonableness.
The following tables present the total expense (income) related to all benefit plans for the periods presented (in millions of dollars):

	Quarter Ended		**Nine Months Ended**	
	September 30,		**September 30,**	
	2018	**2017**	**2018**	**2017**
Defined contribution plans[1]	$ 1.7	$ 1.4	$ 7.3	$ 7.5
Deferred compensation plan[1]	0.2	0.5	1.2	1.4
Multiemployer pension plans[1]	1.2	1.1	3.5	3.4

Net periodic postretirement benefit cost relating to Salaried VEBA[2]	1.4	1.2	4.5	3.4
Loss (gain) on removal of Union VEBA net assets[2]	—	0.5	—	(0.8)
Total	$4.5	$4.7	$16.5	$14.9

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[1] Substantially all of the employee benefits related charges are in Cost of products sold, excluding depreciation and amortization and other items with the remaining balance in Selling, general, administrative, research and development ("SG&A and R&D").

[2] On January 1, 2018, we retrospectively adopted ASU 2017-07 (see Note 1). As such, the current service cost component of Net periodic postretirement benefit cost relating to Salaried VEBA is included within the Statements of Consolidated Income in SG&A and R&D for all periods presented. We reclassified all other components of Net periodic postretirement benefit cost relating to Salaried VEBA, as well as Loss (gain) on removal of Union VEBA net assets that had previously been presented within SG&A and R&D, to Other income (expense), net in the Statements of Consolidated Income.

Components of Net Periodic Benefit Cost. Our results of operations included the following impacts associated with the Canadian defined benefit plan and the Salaried VEBA: (i) charges for service rendered by employees; (ii) a charge for accretion of interest; (iii) a benefit for the return on plan assets; and (iv) amortization of net gains or losses on assets, prior service costs associated with plan amendments and actuarial differences. Net periodic benefit cost related to the Canadian defined benefit plan was not material for the quarters and nine months ended September 30, 2018 and September 30, 2017.

The following table presents the components of Net periodic postretirement benefit cost relating to Salaried VEBA for the periods presented (in millions of dollars):

	Quarter Ended		**Nine Months Ended**	
	September 30,		**September 30,**	
	2018	**2017**	**2018**	**2017**
Salaried VEBA[1]:				
Interest cost	$0.7	$0.8	$2.1	$2.3
Expected return on plan assets	(0.8)	(1.0)	(2.2)	(3.1)
Amortization of prior service cost[2]	1.3	1.2	4.0	3.6
Amortization of net actuarial loss	0.2	0.2	0.6	0.6
Total net periodic postretirement benefit cost relating to Salaried VEBA	$1.4	$1.2	$4.5	$3.4

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[1] The service cost was insignificant for all periods presented.

[2] We amortize prior service cost on a straight-line basis over the average remaining years of service to full eligibility for benefits of the active plan participants.

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5. Derivatives, Hedging Programs and Other Financial Instruments

Overview

In conducting our business, we enter into derivative transactions, including forward contracts and options, to limit our exposure to: (i) metal price risk related to our sale of fabricated aluminum products and the purchase of metal used as raw material for our fabrication operations; (ii) energy price risk relating to fluctuating prices of natural gas and electricity used in our production processes; and (iii) foreign currency requirements with respect to our foreign subsidiaries and cash commitments for equipment purchases denominated in foreign currency.

Our derivative activities are overseen by a committee ("Hedging Committee"), which is composed of our chief executive officer, chief operating officer, chief financial officer, chief accounting officer, vice president of metal management, treasurer and other officers and employees selected by the chief executive officer. The Hedging Committee meets regularly to review commodity price exposure, derivative positions and strategy. Management reviews the scope of the Hedging Committee's activities with our Board of Directors.

We are exposed to counterparty credit risk on all of our derivative instruments, which we manage by monitoring the credit quality of our counterparties and allocating our hedging positions among multiple counterparties to limit exposure to any single entity. Our counterparties are major, investment grade financial institutions or trading companies. Hedging transactions are governed by negotiated reciprocal credit lines, which generally require collateral to be posted above specified credit thresholds. We believe the risk of loss is remote and contained due to counterparty credit quality, our diversification practice and collateral requirements.

In a majority of our hedging counterparty agreements, our counterparty offers us a credit line that adjusts up or down, depending on our liquidity. Below specified liquidity thresholds, we may have to post collateral if the fair value of our net liability with such counterparty exceeds our reduced credit line. We manage this risk by allocating hedging transactions among multiple counterparties, using options as part of our hedging activities, or both. The aggregate fair value of our derivative instruments that were in a net liability position was $3.1 million and $0.1 million at September 30, 2018 and December 31, 2017, respectively, and we had no collateral posted as of those dates.

Additionally, our firm-price customer sales commitments create incremental customer credit risk related to metal price movements. Under certain circumstances, we mitigate this risk by periodically requiring cash collateral from them, which we classify as deferred revenue and include as a component of Other accrued liabilities. At both September 30, 2018 and December 31, 2017, we had no cash collateral posted from any of our customers. For more information about concentration risks concerning customers and suppliers, see Note 14.

Aluminum Hedges. Our pricing of fabricated aluminum products is generally intended to lock in a conversion margin (representing the value added from the fabrication process(es)) and to pass through metal price fluctuations to our customers. For some of our higher value added products sold on a spot basis, the pass through of metal price movements can sometimes lag by as much as several months, with a favorable impact to us when metal prices decline and an adverse impact to us when metal prices increase. Additionally, in certain instances, we enter into firm-price arrangements with our customers for stipulated volumes to be delivered in the future. Because we generally purchase primary and secondary aluminum on a floating price basis, the lag in passing through metal price movements to customers on some of our higher value added products sold on a spot basis and the volume that we have committed to sell to our customers under a firm-price arrangement create metal price risk for us. We use third-party hedging instruments to limit exposure to metal price risk related to the metal pass through lag on some of our products and firm-price customer sales contracts.

Alloying Metals Hedges. We are exposed to risk of fluctuating prices for Alloying Metals used as raw materials in our fabrication operations. We, from time to time, in the ordinary course of business, use third-party hedging instruments to mitigate our risk from price fluctuations in Alloying Metals.

Energy Hedges. We are exposed to risk of fluctuating prices for natural gas and electricity. We, from time to time, in the ordinary course of business, enter into hedging transactions and/or physical delivery commitments with third parties to mitigate our risk from fluctuations in natural gas and electricity prices.

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KAISER ALUMINUM CORPORATION AND SUBSIDIARY COMPANIES
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Notional Amount of Derivative Contracts

The following table summarizes our derivative positions at September 30, 2018:

Aluminum	**Maturity Period (month/year)**	**Notional Amount of Contracts (mmlbs)**
Fixed price purchase contracts	10/18 through 12/21	138.3
Fixed price sales contracts	10/18 through 11/19	2.1
Midwest premium swap contracts[1]	10/18 through 12/21	105.9

Alloying Metals	**Maturity Period (month/year)**	**Notional Amount of Contracts (mmlbs)**
Fixed price purchase contracts	10/18 through 12/19	9.9

Natural Gas[2]	**Maturity Period (month/year)**	**Notional Amount of Contracts (mmbtu)**
Fixed price purchase contracts	10/18 through 12/21	4,130,000

Electricity[3]	**Maturity Period (month/year)**	**Notional Amount of Contracts (Mwh)**
Fixed price purchase contracts	1/20 through 12/21	219,600

Euro[4]	**Maturity Period (month/year)**	**Notional Amount of Contracts (euro)**
Fixed price purchase contracts	11/18	33,064

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1 Regional premiums represent the premium over the London Metal Exchange price for primary aluminum which is incurred on our purchases of primary aluminum.

2 As of September 30, 2018, we had derivative and/or physical delivery commitments with energy companies for approximately 70% of the expected natural gas purchases for the remainder of 2018, 68% of the expected natural gas purchases for 2019, 67% of the expected natural gas purchases for 2020 and 63% of the expected natural gas purchases for 2021.

3 As of September 30, 2018, we had derivative and/or physical delivery commitments with energy companies for approximately 53% of our expected electricity purchases for the remainder of 2018, 54% of our expected electricity purchases for both 2019 and 2020 and 9% of our expected electricity purchases for 2021.

4 We use non-designated foreign currency forward contracts designed to line up with the timing and amounts of scheduled payments to foreign equipment manufacturers to mitigate our exposure to currency exchange rate fluctuations on these purchases.

Adoption of ASU 2017-12

Prior to our adoption of ASU 2017-12 on January 1, 2018, changes in the fair value of non-designated hedges (aluminum and energy) were recorded within Unrealized (gain) loss on derivative instruments in the Statements of Consolidated Income. Upon settlement, realized gain or loss was recorded within Cost of products sold, excluding depreciation and amortization and other items, with an offsetting reversal of previously recognized unrealized amounts recorded within Unrealized (gain) loss on derivative instruments.

Beginning with our adoption of ASU 2017-12 (see Note 1), aluminum and energy hedges that were non-designated prior to 2018 are now designated as cash flow hedges. As these previously non-designated hedges are settled, unrealized gains and losses recognized subsequent to December 31, 2017 are reclassified from Accumulated other comprehensive loss to Cost of products sold, excluding depreciation and amortization.

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(Gain) Loss

See Note 8 for the total amount of gain or loss on derivative instruments designated and qualifying as cash flow hedging instruments that was reported in Accumulated other comprehensive income (loss) ("AOCI"), as well as the related reclassifications into earnings and tax effects. Cumulative gains and losses related to cash flow hedges are reclassified out of AOCI when the associated hedged commodity purchases impact earnings.

The location and amount of (gain) loss included on the Statements of Consolidated Income associated with all derivative contracts consisted of the following for each period presented (in millions of dollars):

	Quarter Ended September 30,			Nine Months Ended September 30,		
	2018	2017		2018	2017	
	Cost of products sold, excluding depreciation and amortization and other items[1]	Cost of products sold, excluding depreciation and amortization and other items[1]	Unrealized gain on derivative instruments	Cost of products sold, excluding depreciation and amortization and other items[1]	Cost of products sold, excluding depreciation and amortization and other items[1]	Unrealized (gain) loss on derivative instruments
Total amounts of income and expense line items presented in the statements of consolidated income in which the effects of hedges are recorded	$323.3	$267.2	$(10.8)	$983.4	$822.7	$(14.0)
Loss (gain) recognized in income related to cash flow hedges:						
Aluminum	$2.1	$—	$—	$(1.2)	$—	$—
Alloying Metals	1.0	(0.3)	—	0.4	(0.2)	—
Natural gas	—	—	—	(0.1)	—	—
Total loss (gain) recognized in income	$3.1	$(0.3)	$—	$(0.9)	$(0.2)	$—
(Gain) loss recognized in income related to non-designated hedges:						
Aluminum	$—	$(4.0)	$(10.6)	$—	$(13.8)	$(15.3)
Natural gas	—	0.2	(0.2)	—	0.3	1.3
Foreign exchange	—	(0.1)	—	—	(0.1)	—
Total gain recognized in income	$—	$(3.9)	$(10.8)	$—	$(13.6)	$(14.0)

1 Beginning with our adoption of ASU 2017-12 effective January 1, 2018, we no longer have Unrealized (gain) loss on derivative instruments on the Statements of Consolidated Income as all of our commodity hedges are designated as cash flow hedges. As such, all Unrealized (gain) loss on derivative instruments is reported in AOCI. For the quarter and nine months ended September 30, 2017, Unrealized (gain) loss on derivative instruments was reclassified to Cost of products sold, excluding depreciation and amortization and other items in the Statements of Consolidated Income to conform to the current period's presentation, for a combined total of $256.4 million and $808.7 million, respectively. The amounts comprising both line items are presented separately here for comparative purposes.

KAISER ALUMINUM CORPORATION AND SUBSIDIARY COMPANIES
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Fair Values of Derivative Contracts

The fair values of our derivative contracts are based upon trades in liquid markets. Valuation model inputs can be verified, and valuation techniques do not involve significant judgment. The fair values of such financial instruments are classified within Level 2 of the fair value hierarchy.

All of our derivative contracts with counterparties are subject to enforceable master netting arrangements. We reflect the fair value of our derivative contracts on a gross basis on the Consolidated Balance Sheets. The following table presents the fair value of our derivative financial instruments as of the periods presented (in millions of dollars):

	September 30, 2018			December 31, 2017		
	Derivative Assets	Derivative Liabilities	Net Amount	Derivative Assets	Derivative Liabilities	Net Amount
Cash Flow Hedges:						
Aluminum –						
Fixed price purchase contracts	$ 3.0					