

W R GRACE & CO
Form 10-Q
August 08, 2008

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**UNITED STATES
SECURITIES AND EXCHANGE COMMISSION**

WASHINGTON, D.C. 20549

FORM 10-Q

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

For the Quarterly Period Ended June 30, 2008

OR

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

Commission File Number 1-13953

W. R. GRACE & CO.

Delaware
(State of Incorporation)

65-0773649
(I.R.S. Employer
Identification No.)

**7500 Grace Drive
Columbia, Maryland 21044
(410) 531-4000**

(Address and phone number of
principal executive offices)

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 is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See the definitions of "large accelerated filer," "accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act.

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

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

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

Class	Outstanding at July 31, 2008
Common Stock, \$0.01 par value per share	72,151,518 shares

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PART I. FINANCIAL INFORMATION

Item 1. Financial Statements

Review by Independent Registered Public Accounting Firm

With respect to the interim consolidated financial statements included in this Quarterly Report on Form 10-Q for the three months and six months ended June 30, 2008 and 2007, PricewaterhouseCoopers LLP, the company's independent registered public accounting firm, has applied limited procedures in accordance with professional standards for a review of such information. Their report on the interim consolidated financial statements, which follows, states that they did not audit and they do not express an opinion on the unaudited interim financial statements. Accordingly, the degree of reliance on their report on the unaudited interim financial statements should be restricted in light of the limited nature of the review procedures applied. This report is not considered a "report" within the meaning of Sections 7 and 11 of the Securities Act of 1933, and, therefore, the independent accountants' liability under Section 11 does not extend to it.

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Report of Independent Registered Public Accounting Firm

To the Shareholders and Board of Directors of W. R. Grace & Co.:

We have reviewed the accompanying consolidated balance sheet of W. R. Grace & Co. and its subsidiaries as of June 30, 2008, and the related consolidated statements of operations, shareholders' equity (deficit), and comprehensive income (loss) for each of the three-month and six-month periods ended June 30, 2008 and June 30, 2007 and the consolidated statements of cash flows for the six-month periods ended June 30, 2008 and June 30, 2007. These interim financial statements are the responsibility of the Company's management.

We conducted our review in accordance with the standards of the Public Company Accounting Oversight Board (United States). A review of interim financial information consists principally of applying analytical procedures and making inquiries of persons responsible for financial and accounting matters. It is substantially less in scope than an audit conducted in accordance with the standards of the Public Company Accounting Oversight Board (United States), the objective of which is the expression of an opinion regarding the financial statements taken as a whole. Accordingly, we do not express such an opinion.

Based on our review, we are not aware of any material modifications that should be made to the accompanying interim consolidated financial statements for them to be in conformity with accounting principles generally accepted in the United States of America.

The accompanying interim consolidated financial statements have been prepared assuming that the Company will continue as a going concern. As discussed in Notes 1 and 2 to the interim consolidated financial statements, on April 2, 2001, the Company and substantially all of its domestic subsidiaries voluntarily filed for protection under Chapter 11 of the United States Bankruptcy Code, which raises substantial doubt about the Company's ability to continue as a going concern in its present form. Management's intentions with respect to this matter are also described in Notes 1 and 2. The accompanying interim consolidated financial statements do not include any adjustments that might result from the outcome of this uncertainty.

We have previously audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the consolidated balance sheet as of December 31, 2007, and the related consolidated statements of operations, shareholders' equity (deficit) and comprehensive income (loss) for the year then ended, and of cash flows for the year then ended December 31, 2007 (not presented herein), and in our report dated February 29, 2008, we expressed an unqualified opinion on those consolidated financial statements with an explanatory paragraph relating to the Company's ability to continue as a going concern. In our opinion, the information set forth in the accompanying consolidated balance sheet as of December 31, 2007, is fairly stated in all material respects in relation to the consolidated balance sheet from which it has been derived.

/s/ PricewaterhouseCoopers LLP
McLean, Virginia
August 8, 2008

Table of Contents**W. R. Grace & Co. and Subsidiaries****Consolidated Statements of Operations (Unaudited)****(In millions, except per share amounts)**

	Three Months Ended June 30,		Six Months Ended June 30,	
	2008	2007	2008	2007
Net sales	\$ 900.0	\$ 812.8	\$ 1,659.2	\$ 1,528.4
Cost of goods sold	635.3	552.9	1,162.5	1,050.6
Selling, general and administrative expenses	153.6	146.0	296.4	281.2
Research and development expenses	21.2	18.7	42.9	37.4
Defined benefit pension expense	14.0	13.1	28.3	25.8
Interest expense and related financing costs	14.5	20.3	29.6	39.7
Provision for environmental remediation		12.0	5.9	12.0
Chapter 11 expenses, net of interest income	18.0	23.6	36.4	41.4
Other (income) expense, net	(7.2)	(7.7)	(24.5)	(15.7)
	849.4	778.9	1,577.5	1,472.4
Income before income taxes and minority interest	50.6	33.9	81.7	56.0
Provision for income taxes	(21.5)	(9.3)	(37.1)	(24.2)
Minority interest in consolidated entities	(4.1)	(4.1)	(6.0)	(6.5)
Net income	\$ 25.0	\$ 20.5	\$ 38.6	\$ 25.3
Basic earnings per share:				
Net income	\$ 0.35	\$ 0.29	\$ 0.54	\$ 0.36
Weighted average number of basic shares	72.1	70.1	71.9	69.8
Diluted earnings per share:				
Net income	\$ 0.34	\$ 0.29	\$ 0.53	\$ 0.35
Weighted average number of diluted shares	72.9	71.8	72.6	71.4

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

Table of Contents**W. R. Grace & Co. and Subsidiaries****Consolidated Statements of Cash Flows (Unaudited)**

(In millions)

	Six Months Ended June 30,	
	2008	2007
OPERATING ACTIVITIES		
Net income	\$ 38.6	\$ 25.3
Reconciliation to net cash provided by (used for) operating activities:		
Depreciation and amortization	60.9	55.2
Chapter 11 expenses, net of interest income	36.4	41.4
Provision for income taxes	37.1	24.2
Income taxes paid, net of refunds	(32.4)	(18.5)
Minority interest in consolidated entities	6.0	6.5
Dividends paid to minority interests in consolidated entities	(13.3)	(11.8)
Interest accrued on pre-petition liabilities subject to compromise	26.8	38.8
Net (gain) loss on sales of investments and disposals of assets	(0.6)	(3.6)
Defined benefit pension expense	28.3	25.8
Payments under defined benefit pension arrangements	(42.5)	(57.0)
Net payments under postretirement benefit plans	(3.3)	(3.1)
Net income from life insurance policies	(1.8)	(2.5)
Provision for uncollectible receivables	0.3	1.4
Provision for environmental remediation	5.9	12.0
Expenditures for environmental remediation	(1.2)	(4.8)
Expenditures for retained obligations of divested businesses	(0.1)	(0.8)
Changes in assets and liabilities, excluding effect of foreign currency translation:		
Working capital items (trade accounts receivable, inventories and accounts payable)	(40.4)	(34.2)
Other accruals and non-cash items	(65.6)	(43.3)
Net cash provided by operating activities before Chapter 11 expenses and settlements	39.1	51.0
Cash paid to resolve contingencies subject to Chapter 11	(101.6)	(10.3)
Chapter 11 expenses paid	(36.7)	(35.5)
Net cash provided by (used for) operating activities	(99.2)	5.2
INVESTING ACTIVITIES		
Capital expenditures	(58.7)	(52.3)
Investments in short-term debt securities		(25.0)
Proceeds from sales of investment securities	46.7	
Purchase of equity investment	(3.0)	(6.3)
Proceeds from termination of life insurance policies	8.1	
Net investment in life insurance policies	0.1	0.2
Proceeds from disposals of assets	2.6	3.0
Net cash used for investing activities	(4.2)	(80.4)
FINANCING ACTIVITIES		
Net (repayments) borrowings under credit arrangements	(0.9)	9.6
Fees paid under debtor-in-possession credit facility	(1.3)	(1.3)
Proceeds from exercise of stock options	9.6	19.4

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Net cash provided by financing activities	7.4	27.7
Effect of currency exchange rate changes on cash and cash equivalents	10.9	5.5
Decrease in cash and cash equivalents	(85.1)	(42.0)
Cash and cash equivalents, beginning of period	480.5	536.3
Cash and cash equivalents, end of period	\$ 395.4	\$494.3

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

Table of Contents**W. R. Grace & Co. and Subsidiaries****Consolidated Balance Sheets****(In millions, except par value and shares)**

	June 30, 2008	December 31, 2007
	(unaudited)	
ASSETS		
Current Assets		
Cash and cash equivalents	\$ 395.4	\$ 480.5
Investment securities	50.5	98.3
Cash value of life insurance policies, net of policy loans	70.7	77.1
Trade accounts receivable, less allowance of \$5.1 (2007-\$5.2)	534.9	500.6
Inventories	368.7	303.5
Deferred income taxes	97.0	37.7
Other current assets	85.9	80.8
Total Current Assets	1,603.1	1,578.5
Properties and equipment, net of accumulated depreciation and amortization of \$1,625.5 (2007-\$1,545.0)	724.4	706.1
Goodwill	126.7	122.3
Cash value of life insurance policies, net of policy loans	3.9	3.9
Deferred income taxes	707.2	767.5
Asbestos-related insurance	500.0	500.0
Overfunded defined benefit pension plans	58.0	54.1
Other assets	135.5	136.6
Total Assets	\$ 3,858.8	\$ 3,869.0
LIABILITIES AND SHAREHOLDERS' EQUITY (DEFICIT)		
Liabilities Not Subject to Compromise		
Current Liabilities		
Debt payable within one year	\$ 3.8	\$ 4.7
Accounts payable	228.9	191.3
Other current liabilities	436.9	325.1
Total Current Liabilities	669.6	521.1
Debt payable after one year	0.3	0.3
Deferred income taxes	35.0	32.7
Minority interest in consolidated entities	62.7	70.8
Underfunded defined benefit pension plans	173.8	169.1
Unfunded pay-as-you-go defined benefit pension plans	138.4	137.9
Other liabilities	51.6	46.2
Total Liabilities Not Subject to Compromise	1,131.4	978.1
Liabilities Subject to Compromise Note 2		
Pre-petition bank debt plus accrued interest	805.1	783.0
Drawn letters of credit plus accrued interest	29.5	26.9
Income tax contingencies	100.8	89.3
Asbestos-related contingencies	1,700.0	1,700.0
Environmental contingencies	147.7	368.6
Postretirement benefits	165.3	172.7
Other liabilities and accrued interest	115.1	137.0
Total Liabilities Subject to Compromise	3,063.5	3,277.5
Total Liabilities	4,194.9	4,255.6
Commitments and Contingencies		

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Shareholders' Equity (Deficit)

Common stock issued, par value \$0.01; 300,000,000 shares authorized; outstanding: 2008-72,151,518 (2007-71,627,901)	0.8	0.8
Paid-in capital	434.9	431.5
Accumulated deficit	(366.5)	(405.1)
Treasury stock, at cost: shares: 2008-4,828,242; (2007-5,351,859)	(57.5)	(63.7)
Accumulated other comprehensive income (loss)	(347.8)	(350.1)
Total Shareholders' Equity (Deficit)	(336.1)	(386.6)
Total Liabilities and Shareholders' Equity (Deficit)	\$ 3,858.8	\$ 3,869.0

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

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W. R. Grace & Co. and Subsidiaries

Consolidated Statements of Shareholders' Equity (Deficit) (Unaudited)

(In millions)

	Common Stock and Paid-in Capital	Accumulated Deficit	Treasury Stock	Accumulated Other Comprehensive Income (Loss)	Total Shareholders' Equity (Deficit)
Balance, March 31, 2008	\$ 435.7	\$ (391.5)	\$ (58.2)	\$ (342.7)	\$ (356.7)
Net income		25.0			25.0
Stock plan activity			0.7		0.7
Other comprehensive income (loss)				(5.1)	(5.1)
Balance, June 30, 2008	\$ 435.7	\$ (366.5)	\$ (57.5)	\$ (347.8)	\$ (336.1)
Balance, December 31, 2007	\$ 432.3	\$ (405.1)	\$ (63.7)	\$ (350.1)	\$ (386.6)
Net income		38.6			38.6
Stock plan activity	3.4		6.2		9.6
Other comprehensive income (loss)				2.3	2.3
Balance, June 30, 2008	\$ 435.7	\$ (366.5)	\$ (57.5)	\$ (347.8)	\$ (336.1)

W. R. Grace & Co. and Subsidiaries

Consolidated Statements of Comprehensive Income (Loss) (Unaudited)

(In millions)

	Three Months Ended June 30,		Six Months Ended June 30,	
	2008	2007	2008	2007
Net income	\$25.0	\$20.5	\$38.6	\$25.3
Other comprehensive income (loss):				
Foreign currency translation adjustments	(4.5)	8.9	(2.6)	14.6
Gain (loss) from hedging activities, net of income taxes	1.8	(1.2)	4.0	(0.1)
Defined benefit pension and other postretirement plans, net of income taxes (see Note 12)	(2.4)	39.4	0.9	39.0
Total other comprehensive income (loss)	(5.1)	47.1	2.3	53.5
Comprehensive income (loss)	\$19.9	\$67.6	\$40.9	\$78.8

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

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W. R. Grace & Co. and Subsidiaries

Notes to Consolidated Financial Statements (Unaudited)

1. Basis of Presentation and Summary of Significant Accounting and Financial Reporting Policies

W. R. Grace & Co., through its subsidiaries, is engaged in specialty chemicals and specialty materials businesses on a worldwide basis through two operating segments: "Grace Davison," which includes specialty catalysts and materials used in a wide range of energy, refining, consumer, industrial, packaging and life sciences applications; and "Grace Construction Products," which includes specialty chemicals and materials used in commercial, infrastructure and residential construction.

W. R. Grace & Co. conducts substantially all of its business through a direct, wholly-owned subsidiary, W. R. Grace & Co.-Conn. ("Grace-Conn."). Grace-Conn. owns substantially all of the assets, properties and rights of W. R. Grace & Co. on a consolidated basis, either directly or through subsidiaries.

As used in these notes, the term "Company" refers to W. R. Grace & Co. The term "Grace" refers to the Company and/or one or more of its subsidiaries and, in certain cases, their respective predecessors.

Voluntary Bankruptcy Filing During 2000 and the first quarter of 2001, Grace experienced several adverse developments in its asbestos-related litigation, including: a significant increase in personal injury claims, higher than expected costs to resolve personal injury and certain property damage claims, and class action lawsuits alleging damages from Zonolite Attic Insulation ("ZAI"), a former Grace attic insulation product.

After a thorough review of these developments, Grace's Board of Directors concluded that a federal court-supervised bankruptcy process provided the best forum available to achieve fairness in resolving these claims and on April 2, 2001 (the "Filing Date"), Grace and 61 of its United States subsidiaries and affiliates, including Grace-Conn. (collectively, the "Debtors"), filed voluntary petitions for reorganization (the "Filing") under Chapter 11 of the United States Bankruptcy Code in the United States Bankruptcy Court for the District of Delaware (the "Bankruptcy Court"). The cases were consolidated and are being jointly administered under case number 01-01139 (the "Chapter 11 Cases"). Grace's non-U.S. subsidiaries and certain of its U.S. subsidiaries were not included in the Filing.

Under Chapter 11, the Debtors have continued to operate their businesses as debtors-in-possession under court protection from creditors and claimants, while using the Chapter 11 process to develop and implement a plan for addressing the asbestos-related claims. Since the Filing, all motions necessary to conduct normal business activities have been approved by the Bankruptcy Court. (See Note 2 for Chapter 11-Related Information.)

Basis of Presentation The interim Consolidated Financial Statements presented herein are unaudited and should be read in conjunction with the Consolidated Financial Statements presented in the Company's 2007 Annual Report on Form 10-K. Such interim Consolidated Financial Statements reflect all adjustments that, in the opinion of management, are necessary for a fair presentation of the results of the interim periods presented; all such adjustments are of a normal recurring nature. Potential accounting adjustments discovered during normal reporting and accounting processes are evaluated on the basis of materiality, both individually and in the aggregate, and are recorded in the accounting period discovered, unless a restatement of a prior period is necessary. All significant intercompany accounts and transactions have been eliminated.

The results of operations for the six-month interim period ended June 30, 2008 are not necessarily indicative of the results of operations for the year ending December 31, 2008.

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W. R. Grace & Co. and Subsidiaries

Notes to Consolidated Financial Statements (Unaudited) (Continued)

1. Basis of Presentation and Summary of Significant Accounting and Financial Reporting Policies (Continued)

Reclassifications Certain amounts in prior years' Consolidated Financial Statements have been reclassified to conform to the 2008 presentation. In the fourth quarter of 2007, Grace completed the transfer of its packaging technologies product group to the Grace Davison segment in an effort better to capture operating synergies. All 2007 segment information herein has been retrospectively restated to reflect this realignment of the packaging technologies product group. The former Grace Performance Chemicals segment has been renamed "Grace Construction Products" as a result of the transfer. Other than the realignment of operating segments, reclassifications have not materially affected previously reported amounts in the Consolidated Financial Statements.

Use of Estimates The preparation of financial statements in conformity with U.S. generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amount of assets and liabilities and disclosure of contingent assets and liabilities at the date of the Consolidated Financial Statements, and the reported amounts of revenues and expenses for the periods presented. Actual amounts could differ from those estimates, and the differences could be material. Changes in estimates are recorded in the period identified. Grace's accounting measurements that are most affected by management's estimates of future events are:

Contingent liabilities, which depend on an assessment of the probability of loss and an estimate of ultimate resolution cost, such as asbestos-related matters (see Notes 2 and 3), environmental remediation (see Note 13), income taxes (see Note 4), and litigation (see Note 13); and

Pension and postretirement liabilities that depend on assumptions regarding participant life spans, future inflation, discount rates and total returns on invested funds (see Note 14); and

Realization values of net deferred tax assets and insurance receivables, which depend on projections of future income and cash flows and assessments of insurance coverage and insurer solvency.

The accuracy of management's estimates may be materially affected by the uncertainties arising under Grace's Chapter 11 proceeding.

Effect of New Accounting Standards In May 2008, the Financial Accounting Standards Board ("FASB") issued Statement of Financial Accounting Standards ("SFAS") No. 162, "The Hierarchy of Generally Accepted Accounting Principles." SFAS No. 162 identifies the sources of accounting principles and the framework for selecting the principles to be used in the preparation of financial statements of nongovernmental entities that are presented in conformity with generally accepted accounting principles. This statement is effective 60 days following the SEC's approval of the Public Company Accounting Oversight Board amendments to AU section 411, *The Meaning of Present Fairly in Conformity With Generally Accepted Accounting Principles*.

In April 2008, the FASB issued FSP No. FAS 142-3, "Determination of the Useful Life of Intangible Assets." FSP 142-3 will improve the consistency between the useful life of a recognized intangible asset under Statement 142 and the period of expected cash flows used to measure the fair value of the asset under FASB Statement No. 141 (revised 2007), *Business Combinations*, and other U.S. generally accepted accounting principles (GAAP). This FSP is effective for financial statements issued for fiscal years beginning after December 15, 2008, and interim periods within those fiscal years.

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W. R. Grace & Co. and Subsidiaries

Notes to Consolidated Financial Statements (Unaudited) (Continued)

1. Basis of Presentation and Summary of Significant Accounting and Financial Reporting Policies (Continued)

In April 2008, the FASB issued FSP No. SOP 90-7-1, "An Amendment of AICPA Statement of Position 90-7." FSP No. SOP 90-7-1 resolves the conflict between the guidance requiring early adoption of new accounting standards for entities required to follow fresh-start reporting under AICPA Statement of Position 90-7, *Financial Reporting by Entities in Reorganization Under the Bankruptcy Code*, and other authoritative accounting standards that expressly prohibit early adoption. This FSP is effective for financial statements issued after April 24, 2008, and is not expected to impact Grace's Consolidated Financial Statements.

In March 2008, the FASB issued SFAS No. 161, "Disclosures about Derivative Instruments and Hedging Activities" an amendment of FASB Statement No. 133." SFAS No. 161 expands the current disclosure framework by requiring entities to provide qualitative disclosures about the objectives and strategies for using derivatives, quantitative data about the fair value of and gains and losses on derivative contracts, and details of credit-risk-related contingent features in their hedged positions. SFAS No. 161 is effective for fiscal years beginning after November 15, 2008.

In December 2007, the FASB issued SFAS No. 141(R), "Business Combinations." SFAS No. 141(R) will require the acquirer in a business combination to recognize the assets acquired, the liabilities assumed, and any noncontrolling interest in the acquiree at the acquisition date, measured at their fair values as of that date, with acquisition-related costs recognized separately from the acquisition. SFAS No. 141(R) applies prospectively to business combinations occurring on or after the beginning of the first annual reporting period beginning on or after December 15, 2008.

In December 2007, the FASB issued SFAS No. 160, "Noncontrolling Interests in Consolidated Financial Statements." SFAS No. 160 establishes new accounting and reporting standards for the noncontrolling interest in a subsidiary and for the deconsolidation of a subsidiary. SFAS No. 160 is effective for fiscal years beginning on or after December 15, 2008.

In September 2006, the FASB issued SFAS No. 157, "Fair Value Measurements." SFAS No. 157 defines fair value, establishes a framework for measuring fair value, and expands disclosures about fair value measurements. In February 2008, the FASB issued FASB Staff Position ("FSP") 157-1, "Application of FASB Statement No. 157 to FASB Statement No. 13 and Other Accounting Pronouncements That Address Fair Value Measurements for Purposes of Lease Classification or Measurement under Statement 13", and FSP 157-2, "Effective Date of FASB Statement No. 157". FSP 157-1 amends SFAS No. 157 to remove certain leasing transactions from its scope. FSP 157-2 delays the effective date of SFAS No. 157 for all non-financial assets and non-financial liabilities, except for items that are recognized or disclosed at fair value in the financial statements on a recurring basis (at least annually), until fiscal years beginning after November 15, 2008. Grace adopted SFAS No. 157 and the related FSPs in the first quarter of 2008, and the adoption for Grace's financial assets and liabilities did not have a material impact on its Consolidated Financial Statements. Grace does not believe the adoption of SFAS No. 157 for its non-financial assets and liabilities, effective January 1, 2009, will have a material impact on its Consolidated Financial Statements. See Note 6 for further discussion of SFAS No. 157.

2. Chapter 11 Related Information

Official Parties to Grace's Chapter 11 Proceedings Three creditors' committees, two representing asbestos claimants, the Official Committee of Asbestos Personal Injury Claimants (the

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W. R. Grace & Co. and Subsidiaries

Notes to Consolidated Financial Statements (Unaudited) (Continued)

2. Chapter 11 Related Information (Continued)

"PI Committee") and the Official Committee of Asbestos Property Damage Claimants (the "PD Committee"), and the third representing other unsecured creditors, and the Official Committee of Equity Security Holders (the "Equity Committee"), have been appointed in the Chapter 11 Cases. These committees, and a legal representative of future asbestos claimants, have the right to be heard on all matters that come before the Bankruptcy Court and have important roles in the Chapter 11 Cases. The Debtors are required to bear certain costs and expenses of the committees and of the representative of future asbestos claimants, including those of their counsel and financial advisors.

As discussed below, the Debtors, supported by the committee representing general unsecured creditors and the Equity Committee, as co-proponents, have filed a plan of reorganization with the Bankruptcy Court. The PI Committee and the FCR, as co-proponents, also have filed a separate plan of reorganization with the Bankruptcy Court. Each of these plans of reorganization is designed to address all pending and future asbestos-related claims and all other pre-petition claims as outlined therein. Subsequent to these filings, on April 6, 2008, the Debtors, the Equity Committee, the PI Committee and the FCR entered into an agreement in principle that would settle all present and future asbestos-related personal injury claims. The committee representing general unsecured creditors and the PD Committee are not parties to this agreement in principle. The Debtors, Equity Committee, PI Committee and FCR contemplate that a joint plan of reorganization reflecting the terms of the agreement in principle would be filed with the Bankruptcy Court and would supersede the existing plans on file.

Plans of Reorganization On November 13, 2004, Grace filed a plan of reorganization, as well as several associated documents, including a disclosure statement, trust distribution procedures, exhibits and other supporting documents, with the Bankruptcy Court. On January 13, 2005, Grace filed an amended plan of reorganization (the "Debtors Plan") and related documents to address certain objections of creditors and other interested parties. At the time it was filed, the Debtors Plan was supported by the committee representing general unsecured creditors and the Equity Committee, but was not supported by the PI Committee, the PD Committee or the FCR.

On July 26, 2007, the Bankruptcy Court terminated Grace's exclusive rights to propose a plan of reorganization and solicit votes thereon. As a result of the termination of these rights, any party-in-interest may propose a competing plan of reorganization.

On November 5, 2007, the PI Committee and the FCR filed a proposed plan of reorganization (the "PI Plan", and with the Debtors Plan, the "Plans") with the Bankruptcy Court. Copies of the Plans are available from the Bankruptcy Court. The filing did not include a disclosure statement, trust distribution procedures, exhibits, or other supporting documents.

On April 6, 2008, the Debtors reached an agreement in principle with the PI Committee, the FCR, and the Equity Committee that would settle all present and future asbestos-related personal injury claims, as further described below (the "PI Settlement"). The PI Settlement contemplates that the Debtors, the PI Committee, the FCR and the Equity Committee would file a new joint plan of reorganization with the Bankruptcy Court reflecting the terms and conditions of the PI Settlement. The drafting and negotiation of the joint plan and related documentation is in progress. The committee representing general unsecured creditors and the PD Committee are not parties to the PI Settlement. Neither the PI Settlement nor a joint plan of reorganization reflecting its terms has been filed with the Bankruptcy Court.

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W. R. Grace & Co. and Subsidiaries

Notes to Consolidated Financial Statements (Unaudited) (Continued)

2. Chapter 11 Related Information (Continued)

The Bankruptcy Court had previously entered a case management order for estimating liability for pending and future asbestos personal injury claims. A trial for estimating liability for such claims began in January 2008 but was suspended in April 2008 as a result of the PI Settlement.

Any plan of reorganization, including either of the Plans, a plan reflecting the PI Settlement and any plan of reorganization that may be filed in the future by a party-in-interest, will become effective only after a vote of eligible creditors and with the approval of the Bankruptcy Court and the U.S. District Court for the District of Delaware. Votes on a plan of reorganization may not be solicited until the Bankruptcy Court approves a related disclosure statement.

Each of the Plans and the PI Settlement assumes that Cryovac, Inc. ("Cryovac"), a wholly-owned subsidiary of Sealed Air Corporation ("Sealed Air"), will pay \$512.5 million in cash (plus interest at 5.5% compounded annually from December 21, 2002) and will issue 18 million shares (reflecting a two-for-one stock split) of common stock of Sealed Air to an asbestos trust pursuant to the terms of a settlement agreement resolving asbestos-related, successor liability and fraudulent transfer claims against Sealed Air and Cryovac, as further described below (the "Sealed Air Settlement"). The value of the Sealed Air Settlement changes daily with the accrual of interest and the trading value of Sealed Air common stock. The Sealed Air Settlement has been approved by the Bankruptcy Court, but remains subject to the fulfillment of specified conditions.

Each of the Plans and the PI Settlement contemplate that a trust would be established under Section 524(g) of the Bankruptcy Code (the "Asbestos Trust") to which asbestos-related personal injury claims would be channeled for resolution.

The Debtors Plan and the PI Plan are designed to address all pending and future asbestos-related claims and all other pre-petition claims as outlined respectively, therein. However, it is possible that neither of the Plans, nor any plan that may be filed as contemplated by the PI Settlement, will be approved by the Bankruptcy Court. If a new joint plan of reorganization reflecting the PI Settlement is not filed with the Bankruptcy Court, the Debtors would expect to resume the estimation trial, which was suspended in April due to the PI Settlement, to determine the amount of its asbestos-related liabilities. Therefore, until an ultimate plan of reorganization is confirmed, the interests of the holders of Company common stock remain subject to substantial dilution or cancellation, and the value of asbestos claims and non-asbestos claims could be materially different from that reflected in Grace's balance sheet. The value of Company common stock and the extent of any recovery by non-asbestos-related creditors will depend principally on the amount of Grace's asbestos-related liability under a confirmed plan of reorganization.

Debtors Plan of Reorganization Under the terms of the Debtors Plan, claims will be satisfied under the Chapter 11 Cases as follows:

Asbestos-Related Claims and Costs

All pending and future asbestos-related claims would be channeled to the Asbestos Trust for resolution. The Debtors Plan contemplates that the Bankruptcy Court will conduct hearings to determine, among other things, the amount that would need to be paid into the Asbestos Trust on the effective date of the Debtors Plan to satisfy Grace's asbestos-related liabilities and trust administration

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W. R. Grace & Co. and Subsidiaries

Notes to Consolidated Financial Statements (Unaudited) (Continued)

2. Chapter 11 Related Information (Continued)

costs and expenses over time. The Asbestos Trust would utilize specified trust distribution procedures to satisfy the following allowed asbestos-related claims and costs:

"PI-SE Claims" Personal Injury Symptomatic Eligible claims In order to qualify for this class, claims would have to meet specified exposure and medical criteria and claimants would have to prove that their health is impaired due to meaningful exposure to asbestos-containing products formerly manufactured by Grace; and

"PI-AO Claims" Personal Injury Asymptomatic and Other claims This class would contain all asbestos-related personal injury claims against Grace that did not meet the specific requirements to be PI-SE Claims, but did meet certain other specified exposure and medical criteria; and

"PD Claims" Property Damage, including ZAI, claims In order to qualify for this class, claimants would have to prove Grace liability for loss of property value or remediation costs related to products formerly manufactured by Grace that claimants allege contained asbestos; and

Trust administration costs and legal expenses.

The claims arising from such proceedings would be subject to this classification process.

Asbestos personal injury claimants, including holders of both PI-SE Claims and PI-AO Claims, would have the option either to litigate their claims against the Asbestos Trust in federal court in Delaware or, if they meet specified eligibility criteria, accept a settlement amount based on the severity of their condition. Holders of PD Claims would be required to present allowed claims to the Asbestos Trust or litigate their claims against the Asbestos Trust in federal court in Delaware. The Debtors Plan provides that, as a condition precedent to confirmation, the maximum estimated aggregate funding amount for all asbestos-related liabilities (PI-SE Claims, PI-AO Claims and PD Claims) and trust administration costs and expenses as determined by the Bankruptcy Court cannot exceed \$1,613 million, which Grace believes would fund over \$2 billion in claims, costs and expenses over time.

PI-SE Claims, PD Claims and related trust administration costs and expenses would be funded with (1) cash and shares of Sealed Air common stock pursuant to the Sealed Air Settlement; and (2) Company common stock. The number of shares of Company common stock required to satisfy these claims will depend on the price of Company common stock on the effective date of the Debtors Plan, liability measures approved by the Bankruptcy Court, and the value of the Sealed Air Settlement.

PI-AO Claims would be funded with warrants exercisable for that number of shares of Company common stock which, when added to the shares issued directly to the Asbestos Trust on the effective date of the Debtors Plan, would represent 50.1% of Grace's voting securities. If the common stock issuable upon exercise of the warrants is insufficient to pay all PI-AO Claims (the liability for which is uncapped under the Debtors Plan), then Grace would pay any additional liabilities in cash.

The amounts to fund PI-SE Claims, PD Claims and trust administration costs and expenses would be capped at the amount determined by the Bankruptcy Court. Amounts required to fund PI-AO Claims would not be capped, so if the amount funded in respect thereof later proved to be inadequate, Grace would be responsible for contributing additional funds into the Asbestos Trust to satisfy PI-AO Claims. Because of the number and nature of the uncertainties involved, Grace is unable to determine

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W. R. Grace & Co. and Subsidiaries

Notes to Consolidated Financial Statements (Unaudited) (Continued)

2. Chapter 11 Related Information (Continued)

the extent to which, if any, the liability for PI-AO Claims may exceed the amount funded into the Asbestos Trust in respect thereof.

Other Claims

All allowed administrative or priority claims would be paid 100% in cash and all general unsecured claims, other than those covered by the Asbestos Trust, would be paid 85% in cash and 15% in Company common stock. Grace would finance these payments with cash on hand, cash from Fresenius Medical Care Holdings, Inc. ("Fresenius") paid in settlement of asbestos and other Grace-related claims as described below (the "Fresenius Settlement"), new Grace debt, and Company common stock. Grace would satisfy other non-asbestos related liabilities and claims (primarily certain environmental, tax, pension and retirement medical obligations) as they become due and payable over time using cash flow from operations, insurance proceeds from policies and settlements covering asbestos-related liabilities, and new credit facilities. Proceeds from available product liability insurance applicable to asbestos-related claims would supplement operating cash flow to service new debt and liabilities not paid on the effective date of the Debtors Plan.

Effect on Company Common Stock

The Debtors Plan provides that Company common stock will remain outstanding at the effective date of the Debtors Plan, but that the interests of existing shareholders would be subject to dilution by additional shares of common stock issued under the Debtors Plan.

The PI and PD Committees and the FCR have challenged the confirmability of the Debtors Plan, arguing that the Debtors Plan impairs the rights of asbestos creditors and impermissibly denies them voting rights, and have asserted that Grace's asbestos-related liabilities exceed the fair value of Grace's assets.

PI Committee and FCR Plan of Reorganization Under the terms of the PI Plan, all pending and future asbestos-related personal injury claims and demands ("PI Claims") would be channeled to the Asbestos Trust for resolution. The PI Plan contemplates that the Bankruptcy Court would determine, among other things, an estimate of the value of all PI Claims. The PI Plan assumes that: cash would be available from insurers; cash would be available from Fresenius pursuant to the Fresenius Settlement; and cash and shares of Sealed Air common stock would be available from Cryovac pursuant to the Sealed Air Settlement. As a condition precedent to the PI Plan, the Bankruptcy Court must determine that the estimated value of all PI Claims, excluding to the extent applicable, post-petition interest, is not less than \$4 billion. If the amount available for distribution pursuant to the PI Plan is more than the principal amount of creditors' claims, creditors entitled to post-petition interest would be paid such interest in the form of Company equity securities and any remaining value would be available to current Company shareholders in the form of new Company equity securities.

Under the terms of the PI Plan, claims would be satisfied under the Chapter 11 Cases as follows:

Asbestos-Related Personal Injury Claims and Costs (PI Claims)

All pending and future PI Claims would be channeled to the Asbestos Trust for resolution. The PI Plan provides that claims arising from such proceedings would be subject to specified trust distribution procedures, which have not been filed with the Bankruptcy Court.

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W. R. Grace & Co. and Subsidiaries

Notes to Consolidated Financial Statements (Unaudited) (Continued)

2. Chapter 11 Related Information (Continued)

In order to satisfy allowed PI Claims and the related trust administration costs and expenses, on the effective date of the PI Plan, the Asbestos Trust would be funded with: (1) cash; (2) cash and shares of Sealed Air common stock pursuant to the Sealed Air Settlement; (3) personal injury liability insurance, unless it is valued at more than \$500 million, in which case it would remain with Grace; and (4) Company equity securities. The value of Company equity securities contributed to the Asbestos Trust would depend on the enterprise value of Grace, the value of Grace's personal injury liability insurance and the value of the Sealed Air Settlement.

Asbestos-Related Property Damage Claims excluding ZAI (non-ZAI PD Claims)

Settled asbestos-related property damage claims excluding ZAI ("non-ZAI PD Claims") would be paid in a combination of cash and Company equity securities on the effective date of the PI Plan. On the effective date of the PI Plan, Grace would establish a reserve consisting of cash and Company equity securities with a value equal to the estimated amount of unresolved non-ZAI PD Claims. Unresolved non-ZAI PD Claims would remain in the mediation and litigation process and would be paid in cash and Company equity securities from the reserve. If the reserve did not have sufficient assets to pay all unresolved non-ZAI PD Claims once the amounts were determined, Grace would be liable to pay any amounts not funded from the reserve.

ZAI Claims

ZAI claims would remain in the litigation process and would be paid by Grace, if required.

Certain Environmental Claims

Certain allowed environmental claims would be paid in cash and Company equity securities on the effective date of the PI Plan. On the effective date of the PI Plan, Grace would establish a reserve consisting of cash and Company equity securities with a value equal to the estimated amount of unresolved environmental claims. Unresolved environmental claims would be determined by the Bankruptcy Court and would be paid in cash and Company equity securities from the reserve. If the reserve did not have sufficient assets to pay all unresolved environmental claims once the amounts were determined, Grace would be liable to pay any amounts not funded from the reserve.

Other Claims

All allowed administrative or priority claims would be paid in cash (either on the effective date of the PI Plan or as they become due and payable over time). General unsecured claims, other than those covered by the Asbestos Trust, would be paid in cash (either on the effective date of the PI Plan or as they become due and payable over time) and Company equity securities. Certain environmental and general unsecured claims would be reinstated and the holders of such claims would retain all legal and other rights to which they are entitled under such claims. Other non-asbestos-related liabilities and claims (primarily certain tax claims and employee-related claims such as pension and retirement medical obligations) would be paid in cash as they become due and payable over time.

Effect on Company Common Stock

Outstanding Company common stock would be cancelled at the effective date of the PI Plan.

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W. R. Grace & Co. and Subsidiaries

Notes to Consolidated Financial Statements (Unaudited) (Continued)

2. Chapter 11 Related Information (Continued)

PI Settlement Under the terms of the PI Settlement, the Debtors, the PI Committee, the FCR, and the Equity Committee would file a joint plan of reorganization. Under this plan, all present and future PI Claims would be channeled to the Asbestos Trust for resolution.

The Asbestos Trust would be funded with:

\$250 million in cash; and

A warrant to acquire 10 million shares of Company common stock at an exercise price of \$17.00 per share, expiring one year from the effective date of a plan of reorganization; and

All of the Debtors' insurance policies and proceeds, including interest, received after the date of the PI Settlement, that are available for payment of PI Claims; and

Cash and shares of Sealed Air common stock to be paid to the Asbestos Trust by Cryovac, Inc. pursuant to the Sealed Air Settlement; and

The proceeds of the payment received by Grace pursuant to the Fresenius Settlement; and

Deferred payments by Grace-Conn. of \$110 million per year for five years beginning in 2019, and \$100 million per year for 10 years beginning in 2024, that would be subordinate to any bank debt or bonds outstanding, guaranteed by the Company and secured by the Company's obligation to issue 50.1% of its outstanding common stock to the Asbestos Trust in the event of default.

Under the terms of the PI Settlement, claims would be satisfied under the Chapter 11 Cases as follows:

Asbestos-Related Personal Injury Claims (PI Claims)

All pending and future PI Claims would be channeled to the Asbestos Trust for resolution. The Asbestos Trust would pay claims from trust assets in accordance with a trust agreement and trust distribution procedures established by the PI Committee and the FCR, subject to the approval of the Bankruptcy Court.

Asbestos-Related Property Damage Claims, excluding ZAI (non-ZAI PD Claims)

Settled non-ZAI PD Claims would be paid in cash on the effective date of a plan of reorganization. A plan of reorganization would set forth procedures for the allowance or disallowance of all non-ZAI PD Claims that are disputed as of the effective date of the plan.

ZAI Claims

The PI Settlement contemplates that the Bankruptcy Court would estimate the value of all ZAI claims prior to or in connection with the confirmation of a plan of reorganization. ZAI claims would be paid up to the amount of the estimate in cash.

Other Claims

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All allowed administrative or priority claims would be paid in cash. Secured claims would be paid in cash or by reinstatement. Allowed general unsecured claims would be paid in cash, including any

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W. R. Grace & Co. and Subsidiaries

Notes to Consolidated Financial Statements (Unaudited) (Continued)

2. Chapter 11 Related Information (Continued)

post-petition interest as follows: (i) for holders of pre-petition bank credit facilities, post-petition interest at the rate of 6.09% from the Filing Date through December 31, 2005 and thereafter at floating prime, in each case compounded quarterly; and (ii) for all other unsecured claims that are not subject to a settlement agreement providing otherwise, interest at 4.19%, compounded annually, or if pursuant to an existing contract, interest at the non-default contract rate. The general unsecured creditors that hold pre-petition bank credit facilities have asserted that they are entitled to post-petition interest at the default rate specified under the terms of the underlying credit agreements which, if paid, would be materially greater than that reflected above. Grace has asserted that such creditors are not entitled to interest at the default rate and has requested the Bankruptcy Court to determine the appropriate rate at which interest would be payable. Unsecured employee-related claims such as pension, retirement medical obligations and workers compensation claims, would be reinstated.

Effect on Company Common Stock

The PI Settlement assumes that Company common stock will remain outstanding at the effective date of a plan of reorganization, but that the interests of existing shareholders would be subject to dilution by additional shares of Company common stock issued under the warrant or in the event of default in respect of the deferred payments by Grace-Conn. under the Company's security obligation.

Claims Filings The Bankruptcy Court established a bar date of March 31, 2003 for claims of general unsecured creditors, asbestos-related property damage claims (other than ZAI claims) and medical monitoring claims related to asbestos. The bar date did not apply to asbestos-related personal injury claims or claims related to ZAI.

Approximately 14,900 proofs of claim were filed by the March 31, 2003 bar date. Of these claims, approximately 9,400 were non-asbestos related, approximately 4,300 were for asbestos-related property damage, and approximately 1,000 were for medical monitoring. The medical monitoring claims were made by individuals who allege exposure to asbestos through Grace's products or operations. These claims, if sustained, would require Grace to fund ongoing health monitoring costs for qualified claimants. In addition, approximately 800 proofs of claim were filed after the bar date.

Approximately 7,000 of the non-asbestos related claims involve claims by employees or former employees for future retirement benefits such as pension and retiree medical coverage. Grace views most of these claims as contingent and has proposed a plan of reorganization that would retain such benefits. The remaining non-asbestos claims include claims for payment of goods and services, taxes, product warranties, principal and interest under pre-petition credit facilities, amounts due under leases and other contracts, leases and other executory contracts rejected in the Bankruptcy Court, environmental remediation, pending non-asbestos-related litigation, and non-asbestos-related personal injury. Claims for indemnification or contribution to actual or potential codefendants in asbestos-related and other litigation were also filed.

The Debtors analyzed the claims filed pursuant to the March 31, 2003 bar date and found that many are duplicates, represent the same claim filed against more than one of the Debtors, lack any supporting documentation, or provide insufficient supporting documentation. As of June 30, 2008, of the approximately 4,035 asbestos property damage claims filed, 275 claims have been resolved, approximately 3,570 claims have been expunged or withdrawn by claimants, leaving approximately 190 claims to be addressed through the property damage case management order approved by the Bankruptcy Court. As of June 30, 2008, of the approximately 3,265 non-asbestos claims filed,

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Notes to Consolidated Financial Statements (Unaudited) (Continued)

2. Chapter 11 Related Information (Continued)

approximately 1,855 have been expunged or withdrawn by claimants, approximately 1,140 have been resolved, and an additional approximately 270 claims are to be addressed through the claim objection process and the dispute resolution procedures approved by the Bankruptcy Court.

Grace believes that its recorded liabilities for claims subject to the March 31, 2003 bar date represent a reasonable estimate of the ultimate allowable amount for claims that are not in dispute or have been submitted with sufficient information to both evaluate the merit and estimate the value of the claim. The asbestos-related claims are considered as part of Grace's overall asbestos liability and are being accounted for in accordance with the conditions precedent under the Debtors Plan, as described in "Accounting Impact" below. Grace expects to adjust its recorded asbestos-related liability as necessary: to reflect rulings made by the Bankruptcy Court; when a new joint plan of reorganization is filed to reflect the terms of the PI Settlement; and when significant uncertainties have been resolved. Such adjustments may be material to Grace's consolidated financial position and results of operations.

Litigation Proceedings in Bankruptcy Court In September 2000, Grace was named in a purported class action lawsuit filed in California Superior Court for the County of San Francisco, alleging that the 1996 reorganization involving a predecessor of Grace and Fresenius AG and the 1998 reorganization involving a predecessor of Grace and Sealed Air were fraudulent transfers (*Abner, et al., v. W.R. Grace & Co., et al.*). The Bankruptcy Court authorized the PI and PD Committees to proceed with claims against Fresenius and Sealed Air and Cryovac on behalf of the Debtors' bankruptcy estate.

On November 29, 2002, Sealed Air (and Cryovac) and Fresenius each announced that they had reached agreements in principle with the PI and PD Committees to settle asbestos, successor liability and fraudulent transfer claims related to such transactions (the "litigation settlement agreements"). Under the terms of the Fresenius Settlement, subject to the fulfillment of certain conditions, Fresenius would pay \$115.0 million to the Debtors' estate as directed by the Bankruptcy Court upon confirmation of the Debtors' plan of reorganization. In July 2003, the Fresenius Settlement was approved by the Bankruptcy Court. Under the terms of the Sealed Air Settlement, subject to the fulfillment of certain conditions, Cryovac would make a payment of \$512.5 million (plus interest at 5.5% compounded annually, commencing on December 21, 2002) and nine million shares (now 18 million shares to reflect a two-for-one stock split) of Sealed Air common stock (collectively valued at \$1,031.2 million as of June 30, 2008), as directed by the Bankruptcy Court upon confirmation of a plan of reorganization. In June 2005, the Sealed Air Settlement was approved by the Bankruptcy Court.

Accounting Impact The accompanying Consolidated Financial Statements have been prepared in accordance with Statement of Position 90-7 ("SOP 90-7"), "Financial Reporting by Entities in Reorganization Under the Bankruptcy Code," promulgated by the American Institute of Certified Public Accountants. SOP 90-7 requires that financial statements of debtors-in-possession be prepared on a going concern basis, which contemplates continuity of operations, realization of assets and liquidation of liabilities in the ordinary course of business. However, as a result of the Filing, the realization of certain of the Debtors' assets and the liquidation of certain of the Debtors' liabilities are subject to significant uncertainty. While operating as debtors-in-possession, the Debtors may sell or otherwise dispose of assets and liquidate or settle liabilities for amounts other than those reflected in the Consolidated Financial Statements. Further, the ultimate plan of reorganization could materially change the amounts and classifications reported in the Consolidated Financial Statements.

Pursuant to SOP 90-7, Grace's pre-petition and future liabilities that are subject to compromise are required to be reported separately on the balance sheet at an estimate of the amount that will

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Notes to Consolidated Financial Statements (Unaudited) (Continued)

2. Chapter 11 Related Information (Continued)

ultimately be allowed by the Bankruptcy Court. As of June 30, 2008, such pre-petition liabilities include fixed obligations (such as debt and contractual commitments), as well as estimates of costs related to contingent liabilities (such as asbestos-related litigation, environmental remediation, and other claims). Obligations of Grace subsidiaries not covered by the Filing continue to be classified on the Consolidated Balance Sheets based upon maturity dates or the expected dates of payment. SOP 90-7 also requires separate reporting of certain expenses, realized gains and losses, and provisions for losses related to the Filing as reorganization items. Grace presents reorganization items as "Chapter 11 expenses, net of interest income," a separate caption in its Consolidated Statements of Operations.

Grace has not recorded the benefit of any assets that may be available to fund asbestos-related and other liabilities under the litigation settlements with Sealed Air and Fresenius, as such agreements are subject to conditions, which, although expected to be met, have not been satisfied and confirmed by the Bankruptcy Court. The value available under these litigation settlement agreements as measured at June 30, 2008, was \$1,146.2 million comprised of \$115.0 million in cash from Fresenius and \$1,031.2 million in cash and stock from Cryovac. Payments under the Sealed Air Settlement will be made directly to the Asbestos Trust by Cryovac.

Grace's Consolidated Balance Sheets separately identify the liabilities that are "subject to compromise" as a result of the Chapter 11 proceedings. In Grace's case, "liabilities subject to compromise" represent both pre-petition and future liabilities as determined under U.S. generally accepted accounting principles. The bases for the asbestos-related liability component of "liabilities subject to compromise" are described in Note 3. Changes to the recorded amount of such liabilities will be based on developments in the Chapter 11 Cases and management's assessment of the claim amounts that will ultimately be allowed by the Bankruptcy Court. Changes to pre-petition liabilities subsequent to the Filing Date reflect: 1) cash payments under approved court orders; 2) the terms of Grace's proposed plan of reorganization, as discussed above, including the accrual of interest on pre-petition debt and other fixed obligations; 3) accruals for employee-related programs; and 4) changes in estimates related to other pre-petition contingent liabilities.

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Components of liabilities subject to compromise are as follows:

(In millions)	June 30, 2008	December 31, 2007
Pre-petition bank debt plus accrued interest	\$ 805.1	\$ 783.0
Drawn letters of credit plus accrued interest	29.5	26.9
Asbestos-related contingencies	1,700.0	1,700.0
Income taxes(1)	100.8	89.3
Environmental contingencies(2)	147.7	368.6
Postretirement benefits other than pension	77.8	84.0
Unfunded special pension arrangements	99.6	100.8
Retained obligations of divested businesses	30.8	30.9
Accounts payable	31.2	31.7
Other accrued liabilities(2)	53.1	74.4
Reclassification to current liabilities(3)	(12.1)	(12.1)
Total Liabilities Subject to Compromise	\$3,063.5	\$ 3,277.5

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- (1) Amounts as of June 30, 2008 and December 31, 2007 are net of expected refunds of \$79.0 million and \$76.4 million, respectively.
- (2) In June 2008, Grace reclassified approximately \$26.1 million of accrued interest from "Other accrued liabilities" to "Environmental contingencies" related to the settlement of environmental contingencies in Libby, Montana. See Note 13 for discussion.
- (3) As of June 30, 2008 and December 31, 2007, approximately \$12.1 million of certain pension and postretirement benefit obligations subject to compromise have been presented in other current liabilities in the Consolidated Balance Sheet in accordance with SFAS No. 158.

Note that the unfunded special pension arrangements reflected above exclude non-U.S. pension plans and qualified U.S. pension plans that became underfunded subsequent to the Filing. Contributions to qualified U.S. pension plans are subject to Bankruptcy Court approval.

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Notes to Consolidated Financial Statements (Unaudited) (Continued)

2. Chapter 11 Related Information (Continued)

Change in Liabilities Subject to Compromise

The following table is a reconciliation of the changes in pre-filing date liability balances for the period from the Filing Date through June 30, 2008:

(In millions)	Cumulative Since Filing
Balance, Filing Date April 2, 2001	\$ 2,366.0
Cash disbursements and/or reclassifications under Bankruptcy Court orders:	
Payment of environmental settlement liability Libby (see Note 13)	