MILLENNIUM CHEMICALS INC
Form 10-Q
May 04, 2006

# 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 March 31, 2006**

**OR**

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

**For the transition period from _____ to _____**

**Commission file number 1-12091**

# MILLENNIUM CHEMICALS INC.

**(Exact name of registrant as specified in its charter)**

| | |
|---|---|
| **Delaware** | **22-3436215** |
| **(State or other jurisdiction of incorporation or organization)** | **(I.R.S. Employer Identification No.)** |
| **Two Greenville Crossing, 4001 Kennett Pike Suite 238, Greenville, Delaware** | **19807** |
| **(Address of principal executive offices)** | **(Zip Code)** |

**Registrant s telephone number, including area code: (713) 652-7200**

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

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, or a non-accelerated filer. See definition of accelerated filer and large accelerated filer in Rule 12b-2 of the Exchange Act.

(Check one):  Large accelerated filer ¨  Accelerated filer ¨  Non-accelerated filer x

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

Number of shares of common stock outstanding as of March 31, 2006: 61,336,122. There is no established public trading market for the registrant s common stock.

**The Registrant meets the conditions set forth in General Instructions H(1)(a) and (b) of Form 10-Q and, therefore, is filing this form with a reduced disclosure format.**

**PART I. FINANCIAL INFORMATION**

**ITEM 1. CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)**

**MILLENNIUM CHEMICALS INC.**

**CONSOLIDATED STATEMENTS OF INCOME**

| Millions of dollars | For the three months ended March 31, 2006 | 2005 |
|---|---|---|
| **Sales and other operating revenues** | | |
| Trade | $ 467 | $ 440 |
| Related parties | 17 | 13 |
| | 484 | 453 |
| **Operating costs and expenses** | | |
| Cost of sales | 438 | 365 |
| Selling, general and administrative expenses | 36 | 43 |
| Research and development expenses | 6 | 6 |
| Asset impairments | 2 | 2 |
| | 482 | 416 |
| Operating income | 2 | 37 |
| Interest expense | (34) | (28) |
| Interest income | 2 | 4 |
| Other expense, net | (9) | (9) |
| Income (loss) before equity investment, minority interest and income taxes | (39) | 4 |
| Income from equity investment in Equistar | 75 | 98 |
| Income before income taxes and minority interest | 36 | 102 |
| Provision for income taxes | 2 | 37 |
| Income before minority interest | 34 | 65 |
| Minority interest | (1) | (1) |
| **Net income** | $ 33 | $ 64 |

See Notes to the Consolidated Financial Statements.

**MILLENNIUM CHEMICALS INC.**

**CONSOLIDATED BALANCE SHEETS**

| Millions of dollars | March 31, 2006 | December 31, 2005 |
|---|---|---|
| **ASSETS** | | |
| Current assets: | | |
| Cash and cash equivalents | $ 99 | $ 279 |
| Accounts receivable: | | |
| Trade, net | 338 | 331 |
| Related parties | 28 | 30 |
| Inventories | 427 | 429 |
| Prepaid expenses and other current assets | 107 | 79 |
| Total current assets | 999 | 1,148 |
| Property, plant and equipment, net | 649 | 647 |
| Investments in Equistar Chemicals, LP | 480 | 464 |
| Goodwill, net | 104 | 104 |
| Other assets, net | 105 | 110 |
| Total assets | $ 2,337 | $ 2,473 |
| **LIABILITIES AND STOCKHOLDER S DEFICIT** | | |
| Current liabilities: | | |
| Current maturities of long-term debt | $ 21 | $ 169 |
| Accounts payable: | | |
| Trade | 272 | 305 |
| Related parties | 70 | 62 |
| Accrued liabilities | 169 | 156 |
| Total current liabilities | 532 | 692 |
| Long-term debt | 873 | 966 |
| Other liabilities | 647 | 644 |
| Deferred income taxes | 229 | 167 |
| Commitments and contingencies | | |
| Minority interests | 46 | 42 |
| Stockholder s equity (deficit) | | |
| Common stock, $0.01 par value, 100,000,000 shares authorized, 66,135,816 shares issued | 1 | 1 |
| Additional paid-in capital | 1,175 | 1,175 |
| Retained deficit | (966) | (999) |
| Accumulated other comprehensive loss | (110) | (125) |
| Treasury stock, at cost, (4,799,694 shares issued) | (90) | (90) |
| Total stockholder s equity (deficit) | 10 | (38) |
| Total liabilities and stockholder s equity (deficit) | $ 2,337 | $ 2,473 |

See Notes to the Consolidated Financial Statements.

**MILLENNIUM CHEMICALS INC.**

**CONSOLIDATED STATEMENTS OF CASH FLOWS**

| | For the three months ended March 31, | |
|---|---|---|
| **Millions of dollars** | **2006** | **2005** |
| **Cash flows from operating activities** | | |
| Net income | $ 33 | $ 64 |
| Adjustments to reconcile net income to cash provided by (used in) operating activities: | | |
| Depreciation and amortization | 27 | 26 |
| Asset impairments | 2 | 2 |
| Equity investment in Equistar - | | |
| Amount included in net income | (75) | (98) |
| Distribution of earnings | 59 | |
| Deferred income taxes | | 9 |
| Debt prepayment premiums and charges | 7 | |
| Changes in assets and liabilities that provided (used) cash: | | |
| Accounts receivable | (2) | (14) |
| Inventories | 7 | (64) |
| Accounts payable | (30) | 24 |
| Other, net | 44 | 21 |
| Net cash provided by (used in) operating activities | 72 | (30) |
| **Cash flows from investing activities** | | |
| Expenditures for property, plant and equipment | (11) | (9) |
| Net cash used in investing activities | (11) | (9) |
| **Cash flows from financing activities** | | |
| Repayment of long-term debt | (244) | |
| Contribution from affiliate | | 6 |
| Other, net | 2 | |
| Net cash provided by (used in) financing activities | (242) | 6 |
| Effect of exchange rate changes on cash | 1 | (2) |
| **Decrease in cash and cash equivalents** | (180) | (35) |
| Cash and cash equivalents at beginning of period | 279 | 344 |
| Cash and cash equivalents at end of period | $ 99 | $ 309 |

See Notes to the Consolidated Financial Statements.

**MILLENNIUM CHEMICALS INC.**

**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS**

**TABLE OF CONTENTS**

**MILLENNIUM CHEMICALS INC.**

**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

**1. Basis of Preparation**

The accompanying consolidated financial statements are unaudited and have been prepared from the books and records of Millennium Chemicals Inc. and its subsidiaries (collectively Millennium ) in accordance with the instructions to Form 10-Q and Rule 10-01 of Regulation S-X for interim financial information. Accordingly, they do not include all of the information and notes required by generally accepted accounting principles for complete financial statements. In the opinion of management, all adjustments, consisting only of normal recurring adjustments, considered necessary for a fair presentation have been included. For further information, refer to the audited consolidated financial statements and notes thereto included in the Millennium Annual Report on Form 10-K for the year ended December 31, 2005. Certain previously reported amounts have been reclassified to conform to current period presentation.

**2. Company Ownership**

On November 30, 2004, Lyondell Chemical Company ( Lyondell ) acquired Millennium in a stock-for-stock business combination. As a result of the business combination, Millennium is a wholly-owned subsidiary of Lyondell. The consolidated financial statements of Millennium reflect its historical cost basis and, accordingly, do not reflect any purchase accounting adjustments related to the acquisition by Lyondell.

**3. Accounting and Reporting Changes**

Effective January 1, 2006, Millennium adopted the provisions of Statement of Financial Accounting Standards ( SFAS ) No. 123 (revised 2004), *Share-Based Payment* using the modified prospective method and, consequently, has not adjusted results of prior periods. Millennium previously accounted for these plans using the intrinsic value method prescribed in Accounting Principles Board ( APB ) Opinion No. 25 and related interpretations. As a result of its acquisition by Lyondell, Millennium s use of share-based payment arrangements is minimal, and, consequently, the application of SFAS No. 123 (revised 2004) had no material effect on its consolidated financial statements.

In September 2005, the Emerging Issues Task Force ( EITF ) of the Financial Accounting Standards Board reached consensus on one issue of EITF Issue No. 04-13, *Accounting for Purchases and Sales of Inventory with the Same Counterparty,* that inventory purchase and sales transactions with the same counterparty that are entered into in contemplation of one another should be combined for purposes of applying APB Opinion No. 29, *Accounting for Nonmonetary Transactions.* The effect would be to reduce reported revenues and cost of sales for affected transactions. The consensus on this issue would apply to transactions entered into beginning in the second quarter 2006. Millennium does not expect the application of EITF 04-13 to have a material effect on its consolidated financial statements.

**4. Asset Impairments**

In 2003, Millennium recognized the impairment of the entire book value of property, plant and equipment at Millennium s Le Havre, France titanium dioxide ( $TiO_2$ ) manufacturing plant. Capital expenditures at this plant of $2 million for each of the three months ended March 31, 2006 and 2005 were reflected in asset impairments. At March 31, 2006 and December 31, 2005, the carrying value of the property, plant and equipment at the Le Havre manufacturing plant was zero.

**MILLENNIUM CHEMICALS INC.**

**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

**5. Investment in Equistar Chemicals, LP**

Equistar Chemicals, LP ( Equistar ) is owned 70.5% by Lyondell and 29.5% by Millennium. As a result of Lyondell s acquisition of Millennium in 2004, Millennium and Equistar are wholly-owned subsidiaries of Lyondell. Millennium accounts for its investment in Equistar using the equity method. As a partnership, Equistar is not subject to federal income taxes.

The consolidated financial statements of Equistar reflect its historical cost basis and, accordingly, do not reflect any purchase accounting adjustments related to the acquisition by Lyondell. Summarized financial information for Equistar follows:

| Millions of dollars | March 31, 2006 | December 31, 2005 |
|---|---|---|
| **BALANCE SHEETS** | | |
| Total current assets | $ 1,769 | $ 1,849 |
| Property, plant and equipment, net | 3,022 | 3,063 |
| Investments and other assets, net | 391 | 408 |
| Total assets | $ 5,182 | $ 5,320 |
| Current maturities of long-term debt | $ | $ 150 |
| Other current liabilities | 964 | 1,010 |
| Long-term debt | 2,160 | 2,161 |
| Other liabilities and deferred revenues | 419 | 416 |
| Partners capital | 1,639 | 1,583 |
| Total liabilities and partners capital | $ 5,182 | $ 5,320 |

| Millions of dollars | For the three months ended March 31, 2006 | 2005 |
|---|---|---|
| **STATEMENTS OF INCOME** | | |
| Sales and other operating revenues | $ 3,036 | $ 2,861 |
| Cost of sales | 2,670 | 2,417 |
| Selling, general and administrative expenses | 48 | 50 |
| Research and development expenses | 8 | 8 |
| Operating income | 310 | 386 |
| Interest expense, net | (53) | (54) |
| Other expense, net | (1) | |
| Net income | $ 256 | $ 332 |
| **OTHER INFORMATION** | | |
| Depreciation and amortization | $ 82 | $ 79 |
| Expenditures for property, plant and equipment | 22 | 35 |

**MILLENNIUM CHEMICALS INC.**

**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

**6. Inventories**

Inventories consisted of the following:

| Millions of dollars | March 31, 2006 | December 31, 2005 |
|---|---|---|
| Finished goods | $ 225 | $ 223 |
| Work-in-process | 40 | 40 |
| Raw materials | 100 | 106 |
| Materials and supplies | 62 | 60 |
| Total inventories | $ 427 | $ 429 |

**7. Property, Plant and Equipment**

The components of property, plant and equipment, at cost, and the related accumulated depreciation were as follows:

| Millions of dollars | March 31, 2006 | December 31, 2005 |
|---|---|---|
| Land | $ 19 | $ 20 |
| Manufacturing facilities and equipment | 1,564 | 1,531 |
| Construction in progress | 75 | 77 |
| Total property, plant and equipment | 1,658 | 1,628 |
| Less accumulated depreciation | (1,009) | (981) |
| Property, plant and equipment, net | $ 649 | $ 647 |

Depreciation and amortization is summarized as follows:

| | For the three months ended March 31, | |
|---|---|---|
| Millions of dollars | 2006 | 2005 |
| Property, plant and equipment | $ 20 | $ 21 |
| Turnaround costs | 2 | 1 |
| Software costs | 3 | 3 |
| Other | 2 | 1 |
| Total depreciation and amortization | $ 27 | $ 26 |

**8. Accounts Payable**

Accounts payable at March 31, 2006 and December 31, 2005 included liabilities in the amounts of $7 million and $5 million, respectively, for checks issued in excess of associated bank balances but not yet presented for collection.

**MILLENNIUM CHEMICALS INC.**

**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

**9. Long-Term Debt**

Long-term debt consisted of the following:

| Millions of dollars | March 31 2006 | December 31, 2005 |
|---|---|---|
| Bank Credit Facilities: | | |
| $150 million senior secured revolving credit facility | $ | $ |
| $100 million Australian senior secured term loan due 2010 | 98 | 99 |
| 60 million U.K. asset-based revolving credit facility | | |
| Other debt obligations: | | |
| Senior Notes due 2006, 7% | 9 | 158 |
| Senior Notes due 2008, 9.25% ($4 million of premium) | 377 | 463 |
| Senior Debentures due 2026, 7.625% ($1 million of discount) | 248 | 248 |
| Convertible Senior Debentures due 2023, 4% | 150 | 150 |
| Debt payable through 2011 at interest rates ranging from 0% to 9.5% | 17 | 19 |
| Other | (5) | (2) |
| Total | 894 | 1,135 |
| Less current maturities | (21) | (169) |
| Total long-term debt, net | $ 873 | $ 966 |

In January 2006, a U.K. subsidiary of Millennium entered into a new 60 million, five-year, revolving credit facility, which, subject to permitted liens, is generally secured by the subsidiary s inventory, accounts receivable and certain other assets. Availability under the U.K. facility, which was 49 million, or approximately $60 million, at March 31, 2006, gave effect to the borrowing base as determined using a formula applied to accounts receivable and inventory balances and was reduced to the extent of borrowing and outstanding letters of credit provided under the facility. At March 31, 2006, there were no outstanding letters of credit under the facility. The U.K. facility bears interest between LIBOR plus 1.25% and LIBOR plus 1.75%.

In February 2006, Millennium completed a cash tender offer for its 7% Senior Notes due 2006, purchasing $149 million principal amount of the notes and paying a premium of $2 million. In addition, during the first three months of 2006, Millennium purchased $85 million principal amount of the 9.25% Senior Notes due 2008, paying a premium of $5 million.

As of March 31, 2006, based on a quarterly test related to the price of Lyondell common stock, Millennium s 4% Convertible Senior Debentures were convertible into Lyondell common stock at a conversion rate of 72.0183 Lyondell shares per one thousand dollar principal amount of the Debentures. The principal amount of Debentures converted into shares of Lyondell common stock as of March 31, 2006 was not significant.

Current maturities of long-term debt were $21 million at March 31, 2006. At December 31, 2005, current maturities of long-term debt included $158 million of Millennium s 7% Senior Notes due 2006 and other debt of $11 million.

Amortization of debt issuance costs of less than $1 million for each of the three-month periods ended March 31, 2006 and 2005 is included in interest expense in the Consolidated Statements of Income.

**MILLENNIUM CHEMICALS INC.**

**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

**10. Pension and Other Postretirement Benefits**

Net periodic pension costs included the following components for the three months ended March 31:

| | 2006 | | 2005 | |
|---|---|---|---|---|
| **Millions of dollars** | **U.S.** | **Non-U.S.** | **U.S.** | **Non-U.S.** |
| Service cost | $ 2 | $ 2 | $ 2 | $ 2 |
| Interest cost | 10 | 3 | 10 | 3 |
| Recognized return on plan assets | (11) | (2) | (12) | (2) |
| Amortization | 5 | 1 | 4 | 1 |
| Net periodic pension benefit cost | $ 6 | $ 4 | $ 4 | $ 4 |

Net periodic other postretirement benefits, which are provided to U.S. employees, were a net credit of $1 million in each of the three month periods ended March 31, 2006 and 2005 as a result of a reduction of benefits and related prior service cost in 2004, which resulted in a net amortization credit of $4 million annually.

**11. Income Taxes**

The effective tax rate for the first quarter 2006 was 6% compared to the 37% estimated annual effective rate in the first quarter 2005. The effective tax rate for the first quarter 2006 was lower than the statutory rate due to changes in estimates for prior year items that reduced the tax provision, partly offset by the effect of losses at Millennium s French subsidiaries with no related tax benefit. The estimated annual effective tax rate for 2006 is 43% as the full-year effect of the French subsidiary losses is only partly offset by the first quarter 2006 change in estimate of prior year items.

**12. Commitments and Contingencies**

*Asset Retirement Obligation* Certain manufacturing facilities are held under land lease arrangements that require the lessee to return the land to substantially the same condition as at the inception of the lease. Generally, these leases would terminate if Millennium discontinued use of the land. It is not possible at this time to estimate the costs that could be incurred upon termination of these leases, nor to reasonably estimate the likely timing of such costs.

*Environmental Remediation* Millennium s accrued liability for future environmental remediation costs at current and former plant sites and other remediation sites totaled $170 million as of March 31, 2006. The remediation expenditures are expected to occur over a number of years, and not to be concentrated in any single year. In the opinion of management, there is no material estimable range of reasonably possible loss in excess of the liabilities recorded for environmental remediation. However, it is possible that new information about the sites for which the accrual has been established, new technology or future developments such as involvement in investigations by regulatory agencies, could require Millennium to reassess its potential exposure related to environmental matters.

**MILLENNIUM CHEMICALS INC.**

**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

**12. Commitments and Contingencies (Continued)**

The following table summarizes the activity in Millennium s accrued environmental liability for the three-month periods ended March 31:

| Millions of dollars | 2006 | 2005 |
|---|---|---|
| Balance at January 1 | $ 168 | $ 122 |
| Additional accruals | 4 | |
| Amounts paid | (2) | (1) |
| Balance at March 31 | $ 170 | $ 121 |

The liabilities for individual sites range from less than $1 million to $104 million. The $104 million liability relates to the Kalamazoo River Superfund Site.

A Millennium subsidiary has been identified as a Potential Responsible Party ( PRP ) with respect to the Kalamazoo River Superfund Site. The site involves cleanup of river sediments and floodplain soils contaminated with polychlorinated biphenyls, cleanup of former paper mill operations, and cleanup and closure of landfills associated with the former paper mill operations. In 2000, the Kalamazoo River Study Group (the KRSG ), of which the Millennium subsidiary and other PRPs are members, submitted to the State of Michigan a Draft Remedial Investigation and Draft Feasibility Study, which evaluated a number of remedial options for the river. The estimated costs for these remedial options ranged from $0 to $2.5 billion.

At the end of 2001, the U.S. Environmental Protection Agency ( EPA ) took lead responsibility for the river portion of the site at the request of the State of Michigan. In 2004, the EPA initiated a confidential process to facilitate discussions among the agency, the Millennium subsidiary, other PRPs, the Michigan Departments of Environmental Quality and Natural Resources, and certain federal natural resource trustees about the need for additional investigation activities and different possible approaches for addressing the contamination in and along the Kalamazoo River. These discussions are continuing.

As of March 31, 2006, the probable future remediation spending associated with the river cannot be determined with certainty. Although the KRSG study identified a broad range of remedial options, not all of those options would represent reasonably possible outcomes. Management does not believe that it can identify a single remedy among those options that would represent the highest-cost reasonably possible outcome. However, in 2004, Millennium recognized a liability representing Millennium s interim allocation of 55% of the $73 million total of estimated cost of bank stabilization, recommended as the preferred remedy in 2000 by the KRSG study, and of certain other costs. At both March 31, 2006 and December 31, 2005, the balance of this liability, net of related spending, was $57 million.

In addition, in 2004, Millennium recognized a liability primarily related to Millennium s estimated share of remediation costs for two former paper mill sites and associated landfills, which are also part of the Kalamazoo River Superfund Site. The liability was increased in the first three months of 2006 by $2 million to reflect new information obtained during the period regarding the probable costs associated with the remediation activity. At March 31, 2006 and December 31, 2005, the balance of the liability, net of related spending, was $47 million and $46 million, respectively. Although no final agreement has been reached as to the ultimate remedy for these locations, Millennium has begun remediation activity related to these sites.

Millennium s ultimate liability for the Kalamazoo River Superfund Site will depend on many factors that have not yet been determined, including the ultimate remedy selected, the determination of natural resource damages, the number and financial viability of the other PRPs, and the determination of the final allocation among the PRPs.

**MILLENNIUM CHEMICALS INC.**

**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

**12. Commitments and Contingencies (Continued)**

Also, based on additional information obtained during the first three months of 2006 regarding remediation liabilities related to Millennium sites other than the Kalamazoo River Superfund Site, Millennium increased the estimated remediation liabilities for those sites by $2 million. The balance of these liabilities at March 31, 2006 and December 31, 2005 was $66 million and $65 million, respectively.

Millennium currently estimates that environmentally related capital expenditures at its facilities will be approximately $11 million in 2006 and $6 million in 2007. These amounts include estimated expenditures related to air emission reductions.

*Litigation* Together with alleged past manufacturers of lead-based paint and lead pigments for use in paint, Millennium has been named as a defendant in various legal proceedings alleging personal injury, property damage, and remediation costs allegedly associated with the use of these products. The majority of these legal proceedings assert unspecified monetary damages in excess of the statutory minimum and, in certain cases, equitable relief such as abatement of lead-based paint in buildings. Legal proceedings relating to lead pigment or paint are in various trial stages and post-dismissal settings, some of which are on appeal.

One legal proceeding relating to lead pigment or paint was tried in 2002. On October 29, 2002, the judge in that case declared a mistrial after the jury declared itself deadlocked. The sole issue before the jury was whether lead pigment in paint in and on Rhode Island buildings constituted a public nuisance. The re-trial of this case began on November 1, 2005. On February 22, 2006, a jury returned a verdict in favor of the State of Rhode Island finding that the cumulative presence of lead pigments in paints and coatings on buildings in the state constitutes a public nuisance; that a Millennium subsidiary and other defendants either caused or substantially contributed to the creation of the public nuisance; and that those defendants, including the Millennium subsidiary, should be ordered to abate the public nuisance. On February 28, 2006, the judge held that the state could not proceed with its claim for punitive damages. As a result, the jury was discharged. There will be further proceedings by the judge to determine the scope of any abatement. Millennium is considering its options, including all appropriate appeals.

Millennium s defense costs to date for lead-based paint and lead pigment litigation largely have been covered by insurance. Millennium has insurance policies that potentially provide approximately $1 billion in indemnity coverage for lead-based paint and lead pigment litigation. Millennium s ability to collect under the indemnity coverage would depend upon, among other things, the resolution of certain potential coverage defenses that the insurers have asserted or are likely to assert and the solvency of the various insurance carriers that are part of the coverage block at the time of such a request.

While Millennium believes that it has valid defenses to all the lead-based paint and lead pigment proceedings and is vigorously defending them, litigation is inherently subject to many uncertainties. Any liability that Millennium may ultimately incur, net of any insurance or other recoveries, cannot be estimated at this time.

*Other Contingencies* Millennium is organized under the laws of Delaware and is subject to United States Federal income taxation of corporations. However, in 1996, in order to obtain clearance from the United Kingdom Inland Revenue as to the tax-free treatment of the demerger stock dividend for United Kingdom tax purposes for Hanson plc ( Hanson ) and Hanson s shareholders, Hanson agreed with the United Kingdom Inland Revenue that Millennium would continue to be centrally managed and controlled in the United Kingdom at least until September 30, 2001. Millennium agreed with Hanson not to take, or fail to take, during such five-year period, any action that would result in a breach of, or constitute non-compliance with, any of the representations and undertakings made by Hanson in its agreement with the United Kingdom Inland Revenue. Effective February 4, 2002, Millennium ceased being centrally managed and controlled in the United Kingdom. Millennium believes that it has satisfied all obligations that it be managed and controlled in the United Kingdom for the requisite five-year period.

**MILLENNIUM CHEMICALS INC.**

**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

**12. Commitments and Contingencies (Continued)**

*Indemnification* Millennium and its joint ventures are parties to various indemnification arrangements, including arrangements entered into in connection with acquisitions, divestitures and the formation of joint ventures. For example, Millennium entered into indemnification arrangements in connection with its demerger from Hanson, and Equistar and its owner companies (including Millennium) entered into indemnification arrangements in connection with the formation of Equistar. Pursuant to these arrangements, Millennium and its joint ventures provide indemnification to and/or receive indemnification from other parties in connection with liabilities that may arise in connection with the transactions and in connection with activities prior to completion of the transactions. These indemnification arrangements typically include provisions pertaining to third party claims relating to environmental and tax matters and various types of litigation. As of March 31, 2006, Millennium has not accrued any significant amounts for such indemnification obligations, other than amounts under tax sharing agreements that have been reflected in the provision for income taxes, and is not aware of other circumstances that would be likely to lead to significant future indemnification claims against Millennium. Millennium cannot determine with certainty the potential amount of future payments under the indemnification arrangements until events arise that would trigger a liability under the arrangements.

*Other* Millennium and its joint ventures are, from time to time, defendants in lawsuits and other commercial disputes, some of which are not covered by insurance. Many of these suits make no specific claim for relief. Although final determination of any liability and resulting financial impact with respect to any such matters cannot be ascertained with any degree of certainty, management does not believe that any ultimate uninsured liability resulting from these matters in which it, its subsidiaries or its joint ventures currently are involved (directly or indirectly) will individually, or in the aggregate, have a material adverse effect on the financial position, liquidity or results of operations of Millennium.

*General* In the opinion of management, the matters discussed in this note are not expected to have a material adverse effect on the financial position or liquidity of Millennium. However, the adverse resolution in any reporting period of one or more of these matters could have a material impact on Millennium s results of operations for that period, which may be mitigated by contribution or indemnification obligations of others, or by any insurance coverage that may be available.

**13. Comprehensive Income**

The components of comprehensive income (loss) were as follows:

| | For the three months ended March 31, | |
|---|---|---|
| **Millions of dollars** | **2006** | **2005** |
| Net income | $ 33 | $ 64 |
| Other comprehensive income (loss): | | |
| Foreign currency translation income (loss) | 15 | (11) |
| Derivative instruments | | (1) |
| Total other comprehensive income (loss) | 15 | (12) |
| Comprehensive income | $ 48 | $ 52 |

**MILLENNIUM CHEMICALS INC.**

**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

**14. Segment and Related Information**

Millennium, a wholly-owned subsidiary of Lyondell, sells its products on a global basis primarily to other industrial concerns in the coatings and petrochemicals industries. Millennium operates in two reportable segments:

Inorganic chemicals, primarily manufacturing and marketing of $TiO_2$ and related products, and

Ethylene, co-products and derivatives ( EC&D ), including Millennium s acetyls business, which produces vinyl acetate monomer ( VAM ), acetic acid and methanol; and Millennium s equity investment in Equistar, which produces primarily ethylene, co-products such as propylene, butadiene and aromatics, and derivatives such as ethylene oxide, ethylene glycol and polyethylene.

Summarized financial information concerning reportable segments is shown in the following table for the three months ended:

| Millions of dollars | Inorganic Chemicals | EC&D | Other | Total |
|---|---|---|---|---|
| **March 31, 2006** | | | | |
| Sales and other operating revenues | $ 342 | $ 116 | $ 26 | $ 484 |
| Operating income (loss) | 15 | (8) | (5) | 2 |
| Income from equity investment | | 75 | | 75 |
| **March 31, 2005** | | | | |
| Sales and other operating revenues | $ 318 | $ 113 | $ 22 | $ 453 |
| Operating income (loss) | 24 | 20 | (7) | 37 |
| Income from equity investment | | 98 | | 98 |

Operating income (loss) in the Other column above includes businesses that are not reportable segments and costs not allocated to Millennium s business segments, including costs from predecessor businesses.

**MILLENNIUM CHEMICALS INC.**

**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

**15. Supplemental Guarantor Information**

Millennium America Inc., a 100% owned indirect subsidiary of Millennium ( Millennium America ), is a holding company that owns Millennium s operating subsidiaries other than its operations in the United Kingdom, France, Brazil and Australia. Millennium America is the issuer of the 7% Senior Notes, the 7.625% Senior Debentures, and the 9.25% Senior Notes. Millennium is the issuer of the 4% Convertible Senior Debentures. Millennium America fully and unconditionally guarantees the 4% Convertible Senior Debentures. The 7% Senior Notes, the 7.625% Senior Debentures and the 9.25% Senior Notes are fully and unconditionally guaranteed by Millennium. The following condensed consolidating financial information present supplemental information for Millennium Chemicals Inc., the parent, and Millennium America as of March 31, 2006 and December 31, 2005 and for the three-month periods ended March 31, 2006 and 2005.

**CONDENSED CONSOLIDATING FINANCIAL INFORMATION**

**BALANCE SHEET**

**As of March 31, 2006**

| Millions of dollars | Millennium Chemicals Inc. | Millennium America Inc. | Non-Guarantor Subsidiaries | Eliminations | Millennium Chemicals Inc. and Subsidiaries |
|---|---|---|---|---|---|
| Inventories | $ | $ | $ 427 | $ | $ 427 |
| Other current assets | | 39 | 533 | | 572 |
| Property, plant and equipment, net | | | 649 | | 649 |
| Investment in Equistar Chemicals, LP | | | 480 | | 480 |
| Investment in subsidiaries | 173 | 418 | | (591) | |
| Goodwill, net | | | 104 | | 104 |
| Other assets, net | (3) | (3) | 111 | | 105 |
| Due from parent and affiliates, net | | 252 | | (252) | |
| Total assets | $ 170 | $ 706 | $ 2,304 | $ (843) | $ 2,337 |
| Current maturities of long-term debt | $ | $ 10 | $ 11 | $ | $ 21 |
| Other current liabilities | 2 | 15 | 494 | | 511 |
| Long-term debt | 150 | 620 | 103 | | 873 |
| Other liabilities | | 5 | 642 | | 647 |
| Deferred income taxes | | | 229 | | 229 |
| Due to parent and affiliates, net | 8 | | 244 | (252) | |
| Total liabilities | 160 | 650 | 1,723 | (252) | 2,281 |
| Minority interest | | | 46 | | 46 |
| Stockholder s equity | 10 | | | | |