## Item 7A. – Quantitative and Qualitative Disclosures About Market Risk

In the normal course of business, we are exposed to various market risks. We continually monitor these risks and regularly develop appropriate strategies to manage them. Accordingly, from time to time, we may enter into certain financial and commodity-based derivative instruments. These instruments are used solely to mitigate market exposure and are not used for trading or speculative purposes. Refer to “Item 8. – Financial Statements and Supplementary Data – Notes to Consolidated Financial Statements – Note P – Derivative Instruments and Hedging Activities” of this Annual Report on Form 10-K for additional information.

### Interest Rate Risk

We are exposed to changes in interest rates primarily as a result of our borrowing and investing activities to maintain liquidity and fund operations. The nature and amount of our long-term and short-term debt can be expected to fluctuate as a result of business requirements, market conditions and other factors. We manage exposures to interest rates using a mix of fixed and variable rate debt. We use interest rate swap instruments to manage our exposure to interest rate movements.

We entered into an interest rate swap in October 2014 to hedge changes in cash flows attributable to changes in EURIBOR associated with a five-year, euro denominated term loan entered into by our

55

consolidated joint venture in Turkey. Under the terms of the swap, we receive interest at a variable rate equal to the three-month EURIBOR plus 1.5% and pay interest at a fixed rate of 2.015%. The interest rate swap has a notional amount equal to 60% of the borrowings outstanding under the facility. Borrowings outstanding under the facility totaled $28.4 million at May 31, 2016.

We entered into an interest rate swap in March 2014, in anticipation of the issuance of $250.0 million principal amount of our 2026 Notes. Refer to “Item 8. – Financial Statements and Supplementary Data – Notes to Consolidated Financial Statements – Note G – Debt and Receivables Securitization” of this Annual Report on Form 10-K for additional information regarding the 2026 Notes. The interest rate swap had a notional amount of $150.0 million to hedge the risk of changes in the semi-annual interest payments attributable to changes in the benchmark interest rate during the several days leading up to the issuance of the 12-year fixed-rate debt. Upon pricing of the 2026 Notes, the derivative was settled and resulted in a loss of approximately $3.1 million, a significant portion of which was reflected within accumulated other comprehensive income in our consolidated statement of equity and will be recognized in earnings, as an increase to interest expense, over the life of the related 2026 Notes.

We entered into a U.S. Treasury Rate-based treasury lock in April 2010, in anticipation of the issuance of

$150.0 million principal amount of our 2020 Notes. Refer to “Item 8. – Financial Statements and Supplementary Data – Notes to Consolidated Financial Statements – Note G – Debt and Receivables Securitization” of this Annual Report on Form 10-K for additional information regarding the 2020 Notes. The treasury lock had a notional amount of $150.0 million to hedge the risk of changes in the semi-annual interest payments attributable to changes in the benchmark interest rate during the several days leading up to the issuance of the 10-year fixed-rate debt. Upon pricing of the 2020 Notes, the derivative was settled and resulted in a loss of approximately $1.4 million, which has been reflected within accumulated other comprehensive income in our consolidated statements of equity. That balance is being recognized in earnings, as an increase to interest expense, over the life of the related 2020 Notes.

### Foreign Currency Risk

The translation of foreign currencies into United States dollars subjects us to exposure related to fluctuating exchange rates. Derivative instruments are not used to manage this risk; however, we do make use of forward contracts to manage exposure to certain intercompany loans with our foreign affiliates as well as exposure to transactions denominated in a currency other than the related foreign affiliate’s local currency. Such contracts limit exposure to both favorable and unfavorable currency fluctuations. At May 31, 2016, the difference between the contract and book value of these instruments was not material to our consolidated financial position, results of operations or cash flows. A 10% change in the exchange rate to the U.S. dollar forward rate is not expected to materially impact our consolidated financial position, results of operations or cash flows. A sensitivity analysis of changes in the U.S. dollar on these foreign currency-denominated contracts indicates that if the U.S. dollar uniformly weakened by 10% against all of these currency exposures, the fair value of these instruments would not be materially impacted. Any resulting changes in fair value would be offset by changes in the underlying hedged balance sheet position. A sensitivity analysis of changes in the currency exchange rates of our foreign locations indicates that a 10% increase in those rates would not have materially impacted our net results. The sensitivity analysis assumes a uniform shift in all foreign currency exchange rates. The assumption that exchange rates change in uniformity may overstate the impact of changing exchange rates on assets and liabilities denominated in a foreign currency.

### Commodity Price Risk

We are exposed to market risk for price fluctuations on purchases of steel, natural gas, zinc and other raw materials as well as our utility requirements. We attempt to negotiate the best prices for commodities and to competitively price products and services to reflect the fluctuations in market prices. Derivative financial instruments have been used to manage a portion of our exposure to fluctuations in the cost of certain

commodities, including steel, natural gas, zinc and other raw materials. These contracts covered periods commensurate with known or expected exposures throughout fiscal 2016. The derivative instruments were executed with highly rated financial institutions. No credit loss is anticipated. No derivatives are held for trading purposes.

A sensitivity analysis of changes in the price of hedged commodities indicates that a 10% decline in the market prices of steel, zinc, natural gas or any combination of these would not have a material impact to the value of our hedges or our reported results.

The fair values of our outstanding derivative positions as of May 31, 2016 and 2015 are summarized below. Fair values of these derivatives do not consider the offsetting impact of the underlying hedged item.

## Fair Value At May 31,

|  |  |  |  |  |
| --- | --- | --- | --- | --- |
|  | **(in millions)** | **2016** |  | **2015** |
| Interest rate |  | $ (0.5) |  | $ (0.2) |
| Foreign currency |  | - |  | 0.1 |
| Commodity |  | 20.3 |  | (21.9) |
|  |  | $19.8 |  | $(22.0) |

### Safe Harbor

Quantitative and qualitative disclosures about market risk include forward-looking statements with respect to management’s opinion about risks associated with the use of derivative instruments. These statements are based on certain assumptions with respect to market prices and industry supply of, and demand for, steel products and certain raw materials. To the extent these assumptions prove to be inaccurate, future outcomes with respect to hedging programs may differ materially from those discussed in the forward- looking statements.

## Item 8. – Financial Statements and Supplementary Data

**Report of Independent Registered Public Accounting Firm**

The Board of Directors and Shareholders Worthington Industries, Inc.:

We have audited the accompanying consolidated balance sheets of Worthington Industries, Inc. and subsidiaries as of May 31, 2016 and 2015, and the related consolidated statements of earnings, comprehensive income, equity, and cash flows for each of the years in the three-year period ended May 31, 2016. In connection with our audits of the consolidated financial statements, we also have audited the financial statement schedule of valuation and qualifying accounts. These consolidated financial statements and financial statement schedule are the responsibility of the Company’s management. Our responsibility is to express an opinion on these consolidated financial statements and financial statement schedule based on our audits.

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

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of Worthington Industries, Inc. and subsidiaries as of May 31, 2016 and 2015, and the results of their operations and their cash flows for each of the years in the three-year period ended May 31, 2016, in conformity with U.S. generally accepted accounting principles. Also in our opinion, the related financial statement schedule, when considered in relation to the basic consolidated financial statements taken as a whole, presents fairly, in all material respects, the information set forth therein.

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), Worthington Industries, Inc.’s internal control over financial reporting as of May 31, 2016, based on criteria established in *Internal Control – Integrated Framework (2013)* issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO), and our report dated August 1, 2016 expressed an unqualified opinion on the effectiveness of the Company’s internal control over financial reporting.

 /s/ KPMG LLP

Columbus, Ohio August 1, 2016

## WORTHINGTON INDUSTRIES, INC. CONSOLIDATED BALANCE SHEETS

**(In thousands)**

**ASSETS**

Current assets:

## May 31,

**2016 2015**

|  |  |  |
| --- | --- | --- |
| Cash and cash equivalentsReceivables, less allowances of $4,579 and $3,085 at May 31, 2016 and 2015, respectivelyInventories: | $ 84,188439,688 | $ 31,067474,292 |
| Raw materials | 162,427 |  | 181,975 |
| Work in process | 86,892 |  | 107,069 |
| Finished products | 70,016 |  | 85,931 |
| Total inventories | 319,335 |  | 374,975 |
| Income taxes receivable | 10,535 |  | 12,119 |
| Assets held for sale | 10,079 |  | 23,412 |
| Deferred income taxes | - |  | 22,034 |
| Prepaid expenses and other current assets | 51,635 |  | 54,294 |
| Total current assets | 915,460 |  | 992,193 |
| Investments in unconsolidated affiliates | 191,826 |  | 196,776 |
| Goodwill | 246,067 |  | 238,999 |
| Other intangible assets, net of accumulated amortization of $49,532 and $47,547 at |  |  |  |
| May 31, 2016 and 2015, respectively | 96,164 |  | 119,117 |
| Other assets | 31,400 |  | 24,867 |
| Property, plant and equipment: |  |  |  |
| Land | 18,537 |  | 16,017 |
| Buildings and improvements | 256,973 |  | 218,182 |
| Machinery and equipment | 945,951 |  | 872,986 |
| Construction in progress | 48,156 |  | 40,753 |
| Total property, plant and equipment | 1,269,617 |  | 1,147,938 |
| Less: accumulated depreciation | 686,779 |  | 634,748 |
| Total property, plant and equipment, net | 582,838 |  | 513,190 |
| **Total assets** | $2,063,755 |  | $2,085,142 |

See notes to consolidated financial statements.

## WORTHINGTON INDUSTRIES, INC. CONSOLIDATED BALANCE SHEETS

**(In thousands)**

**LIABILITIES AND EQUITY**

Current liabilities:

## May 31,

**2016 2015**

|  |  |  |  |
| --- | --- | --- | --- |
| Accounts payable | $ 290,432 |  | $ 294,129 |
| Short-term borrowingsAccrued compensation, contributions to employee benefit plans and related taxes | 2,65175,105 |  | 90,55066,252 |
| Dividends payable | 13,471 |  | 12,862 |
| Other accrued items | 45,056 |  | 56,913 |
| Income taxes payable | 2,501 |  | 2,845 |
| Current maturities of long-term debt | 862 |  | 841 |
| Total current liabilities | 430,078 |  | 524,392 |
| Other liabilities | 63,487 |  | 58,269 |
| Distributions in excess of investment in unconsolidated affiliate | 52,983 |  | 61,585 |
| Long-term debt | 579,982 |  | 579,352 |
| Deferred income taxes | 17,379 |  | 21,495 |
| Total liabilities | 1,143,909 |  | 1,245,093 |

Shareholders’ equity – controlling interest:

Preferred shares, without par value; authorized – 1,000,000 shares; issued and

outstanding – none - -

Common shares, without par value; authorized – 150,000,000 shares; issued and

|  |  |  |  |
| --- | --- | --- | --- |
| outstanding, 2016 – 61,533,668 shares, 2015 – 64,141,478 sharesAdditional paid-in capitalAccumulated other comprehensive loss, net of taxes of $4,768 and $16,909 at | -298,984 |  | -289,078 |
| May 31, 2016 and 2015, respectively | (28,565) |  | (50,704) |
| Retained earnings | 522,952 |  | 510,738 |
| Total shareholders’ equity – controlling interest | 793,371 |  | 749,112 |
| Noncontrolling interests | 126,475 |  | 90,937 |
| Total equity | 919,846 |  | 840,049 |
| **Total liabilities and equity** | $2,063,755 |  | $2,085,142 |

See notes to consolidated financial statements.

## WORTHINGTON INDUSTRIES, INC. CONSOLIDATED STATEMENTS OF EARNINGS

**(In thousands, except per share amounts)**

**Fiscal Years Ended May 31,**

|  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- |
|  | **2016** |  | **2015** |  | **2014** |
| Net sales | $2,819,714 |  | $3,384,234 |  | $3,126,426 |
| Cost of goods sold | 2,367,121 |  | 2,920,701 |  | 2,633,907 |
| Gross margin | 452,593 |  | 463,533 |  | 492,519 |
| Selling, general and administrative expense | 297,402 |  | 295,920 |  | 300,396 |
| Impairment of goodwill and long-lived assets | 25,962 |  | 100,129 |  | 58,246 |
| Restructuring and other expense (income) | 7,177 |  | 6,927 |  | (1,876) |
| Operating income Other income (expense):Miscellaneous income, net | 122,05211,267 |  | 60,557795 |  | 135,75316,963 |
| Interest expense | (31,670) |  | (35,800) |  | (26,671) |
| Equity in net income of unconsolidated affiliates | 114,966 |  | 87,476 |  | 91,456 |
| Earnings before income taxes | 216,615 |  | 113,028 |  | 217,501 |
| Income tax expense | 58,987 |  | 25,772 |  | 57,349 |
| Net earnings | 157,628 |  | 87,256 |  | 160,152 |
| Net earnings attributable to noncontrolling interests | 13,913 |  | 10,471 |  | 8,852 |
| **Net earnings attributable to controlling interest** | $ 143,715 |  | $ 76,785 |  | $ 151,300 |
| **Basic** |  |  |  |  |  |
| Average common shares outstanding | 62,469 |  | 66,309 |  | 68,944 |
| **Earnings per share attributable to controlling interest** | $ 2.30 |  | $ 1.16 |  | $ 2.19 |
| **Diluted** |  |  |  |  |  |
| Average common shares outstanding | 64,755 |  | 68,483 |  | 71,664 |
| **Earnings per share attributable to controlling interest** | $ 2.22 |  | $ 1.12 |  | $ 2.11 |

See notes to consolidated financial statements.

## WORTHINGTON INDUSTRIES, INC. CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME

**(In thousands)**

|  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- |
|  | **2016** |  | **2015** |  | **2014** |
| Net earningsOther comprehensive income (loss): Foreign currency translation | $157,6284,716 |  | $ 87,256(34,229) |  | $160,1527,618 |
| Pension liability adjustment, net of tax | (2,058) |  | (3,738) |  | (1,044) |
| Cash flow hedges, net of tax | 22,208 |  | (11,653) |  | 2,509 |
| Other comprehensive income (loss) | 24,866 |  | (49,620) |  | 9,083 |
| **Comprehensive income** | 182,494 |  | 37,636 |  | 169,235 |
| Comprehensive income attributable to noncontrolling interests | 16,640 |  | 7,974 |  | 9,480 |
| **Comprehensive income attributable to controlling interest** | $165,854 |  | $ 29,662 |  | $159,755 |

See notes to consolidated financial statements.

## WORTHINGTON INDUSTRIES, INC. CONSOLIDATED STATEMENTS OF EQUITY

**(Dollars in thousands, except per share amounts)**

**Controlling Interest**

**Accumulated Other**

**Common Shares Additional Comprehensive**

 **Paid-in**

**Loss,**

**Retained**

**Noncontrolling**

**(in thousands) Shares Amount**

**Capital**

**Net of Tax**

**Earnings Total**

**Interests Total**

**Balance at May 31, 2013** 69,752,411 $ - $244,864 $(12,036) $ 597,994 $ 830,822 $ 41,415 $ 872,237

Net earnings

|  |  |  |  |  |  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- |
| - |  | - - |  | - |  | 151,300 151,300 |  | 8,852 |  | 160,152 |
| - |  | - - |  | 8,455 |  | - 8,455 |  | 628 |  | 9,083 |
| - |  | - - |  | - |  | - - |  | 84,144 |  | 84,144 |
| 1,036,573 |  | - 4,618 |  | - |  | - 4,618 |  | - |  | 4,618 |
| - |  | - 25,651 |  | - |  | - 25,651 |  | - |  | 25,651 |
| (3,380,500) |  | - (12,523) |  | - |  | (115,695) (128,218) |  | - |  | (128,218) |
| - |  | - - |  | - |  | - - |  | (40,969) |  | (40,969) |
| - |  | - - |  | - |  | (41,816) (41,816) |  | - |  | (41,816) |
| 67,408,484 |  | $ - $262,610 |  | $ (3,581) |  | $ 591,783 $ 850,812 |  | $ 94,070 |  | $ 944,882 |
| - |  | - - |  | - |  | 76,785 76,785 |  | 10,471 |  | 87,256 |
| - |  | - - |  | (47,123) |  | - (47,123) |  | (2,497) |  | (49,620) |
| - |  | - - |  | - |  | - - |  | 4,082 |  | 4,082 |
| 909,181 |  | - 2,910 |  | - |  | - 2,910 |  | - |  | 2,910 |
| - |  | - 14,560 |  | - |  | - 14,560 |  | - |  | 14,560 |
| - |  | - 26,837 |  | - |  | - 26,837 |  | - |  | 26,837 |
| (4,176,187) |  | - (17,839) |  | - |  | (109,521) (127,360) |  | - |  | (127,360) |
| - |  | - - |  | - |  | - - |  | (15,189) |  | (15,189) |
| - |  | - - |  | - |  | (48,309) (48,309) |  | - |  | (48,309) |
| 64,141,478 |  | $ - $289,078 |  | $(50,704) |  | $ 510,738 $ 749,112 |  | $ 90,937 |  | $ 840,049 |
| - |  | - - |  | - |  | 143,715 143,715 |  | 13,913 |  | 157,628 |
| - |  | - - |  | 22,139 |  | - 22,139 |  | 2,727 |  | 24,866 |
| - |  | - - |  | - |  | - - |  | 28,004 |  | 28,004 |
| 892,190 |  | - 8,707 |  | - |  | - 8,707 |  | - |  | 8,707 |
| - |  | - 960 |  | - |  | - 960 |  | - |  | 960 |
| - |  | - 16,534 |  | - |  | - 16,534 |  | - |  | 16,534 |
| (3,500,000) |  | - (16,295) |  | - |  | (83,552) (99,847) |  | - |  | (99,847) |
| - |  | - - |  | - |  | - - |  | (9,106) |  | (9,106) |
| - |  | - - |  | - |  | (47,949) (47,949) |  | - |  | (47,949) |

Other comprehensive income Acquisition of PSI Energy

Solutions, LLC

Common shares issued, net of withholding tax

Stock-based compensation Purchases and retirement of

common shares Payments to noncontrolling

interests

Cash dividends declared ($0.60 per share)

**Balance at May 31, 2014**

Net earnings

Other comprehensive loss Acquisition of dHybrid Systems,

LLC

Common shares issued, net of withholding tax

Theoretical common shares in NQ plans

Stock-based compensation Purchases and retirement of

common shares Payments to noncontrolling

interests

Cash dividends declared ($0.72 per share)

**Balance at May 31, 2015**

Net earnings

Other comprehensive income Acquisition of Worthington

Specialty Processing Common shares issued, net of

withholding tax

Theoretical common shares in NQ plans

Stock-based compensation Purchases and retirement of

common shares Payments to noncontrolling

interests

Cash dividends declared ($0.76 per share)

**Balance at May 31, 2016** 61,533,668 $ - $298,984 $(28,565) $ 522,952 $ 793,371 $126,475 $ 919,846

See notes to consolidated financial statements.

## WORTHINGTON INDUSTRIES, INC. CONSOLIDATED STATEMENTS OF CASH FLOWS

**(In thousands)**

**Fiscal Years Ended May 31,**

|  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- |
|  | **2016** |  | **2015** |  | **2014** |
| **Operating activities:** |  |  |  |  |  |
| Net earnings | $ 157,628 |  | $ 87,256 |  | $ 160,152 |
| Adjustments to reconcile net earnings to net cash provided by operating |  |  |  |  |  |
| activities: |  |  |  |  |  |
| Depreciation and amortization | 84,699 |  | 85,089 |  | 79,730 |
| Impairment of goodwill and long-lived assets | 25,962 |  | 100,129 |  | 58,246 |
| Provision for (benefit from) deferred income taxes | 7,354 |  | (39,960) |  | (25,916) |
| Bad debt expense | 346 |  | 259 |  | 32 |
| Equity in net income of unconsolidated affiliates, net of distributions | (29,473) |  | (12,299) |  | (15,333) |
| Net (gain) loss on sale of assets | (12,996) |  | 3,277 |  | (11,212) |
| Stock-based compensation | 15,836 |  | 17,916 |  | 22,017 |
| Excess tax benefits – stock-based compensation | - |  | (7,178) |  | (8,880) |
| Gain on previously held equity interests | (6,877) |  | - |  | (11,000) |
| Changes in assets and liabilities, net of impact of acquisitions: |  |  |  |  |  |
| Receivables | 66,117 |  | 32,011 |  | (49,206) |
| Inventories | 66,351 |  | 54,108 |  | (38,010) |
| Prepaid expenses and other current assets | 18,327 |  | (15,295) |  | (2,921) |
| Other assets | (4,530) |  | 1,617 |  | (5,278) |
| Accounts payable and accrued expenses | 20,180 |  | (83,190) |  | 69,682 |
| Other liabilities | 4,460 |  | (9,365) |  | 6,943 |
| **Net cash provided by operating activities** | 413,384 |  | 214,375 |  | 229,046 |
| **Investing activities:** |  |  |  |  |  |
| Investment in property, plant and equipment | (97,036) |  | (96,255) |  | (71,338) |
| Investment in notes receivable | - |  | (7,300) |  | - |
| Acquisitions, net of cash acquired | (34,206) |  | (105,291) |  | (11,517) |
| Distributions from (investments in) unconsolidated affiliates | (5,595) |  | (8,230) |  | 9,223 |
| Proceeds from sale of assets and insurance | 9,797 |  | 14,007 |  | 27,438 |
| **Net cash used by investing activities** | (127,040) |  | (203,069) |  | (46,194) |
| **Financing activities:** |  |  |  |  |  |
| Net proceeds from (repayments of) short-term borrowings, net of |  |  |  |  |  |
| issuance costs | (85,843) |  | 79,047 |  | (103,618) |
| Proceeds from long-term debt, net of issuance costs | 921 |  | 30,572 |  | 247,566 |
| Principal payments on long-term debt | (862) |  | (102,852) |  | (1,219) |
| Proceeds from issuance of common shares | 8,707 |  | 2,910 |  | 4,618 |
| Excess tax benefits – stock-based compensation | - |  | 7,178 |  | 8,880 |
| Payments to noncontrolling interests | (9,106) |  | (13,379) |  | (40,969) |
| Repurchase of common shares | (99,847) |  | (127,360) |  | (128,218) |
| Dividends paid | (47,193) |  | (46,434) |  | (31,198) |
| **Net cash used by financing activities** | (233,223) |  | (170,318) |  | (44,158) |
| Increase (decrease) in cash and cash equivalents | 53,121 |  | (159,012) |  | 138,694 |
| Cash and cash equivalents at beginning of year | 31,067 |  | 190,079 |  | 51,385 |
| **Cash and cash equivalents at end of year** | $ 84,188 |  | $ 31,067 |  | $ 190,079 |

See notes to consolidated financial statements.

## WORTHINGTON INDUSTRIES, INC.

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**Fiscal Years Ended May 31, 2016, 2015 and 2014**

**Note A – Summary of Significant Accounting Policies**

*Consolidation:* The consolidated financial statements include the accounts of Worthington Industries, Inc. and consolidated subsidiaries (collectively, “we,” “our,” “Worthington,” or the “Company”). Investments in unconsolidated affiliates are accounted for using the equity method. Significant intercompany accounts and transactions are eliminated.

dHybrid Systems, LLC (“dHybrid”), Spartan Steel Coating, LLC (“Spartan”), TWB Company, L.L.C. (“TWB”), Worthington Arıtas¸ Basınc¸lı Kaplar Sanayi (“Worthington Aritas”), Worthington Energy Innovations, LLC (“WEI”), and Worthington Specialty Processing (“WSP”) in which we own controlling interests of 79.59%, 52%, 55%, 75%, 75%, and 51%, respectively, are consolidated with the equity owned by the other joint venture members shown as noncontrolling interests in our consolidated balance sheets, and the other joint venture members’ portions of net earnings and other comprehensive income or loss (“OCI”) shown as net earnings or comprehensive income attributable to noncontrolling interests in our consolidated statements of earnings and consolidated statements of comprehensive income, respectively.

*Use of Estimates:* The preparation of consolidated financial statements in conformity with accounting principles generally accepted in the United States (“U.S. GAAP”) requires management to make estimates and assumptions that affect the amounts reported in the consolidated financial statements and accompanying notes. Actual results could differ from those estimates.

*Cash and Cash Equivalents:* We consider all highly liquid investments purchased with an original maturity of three months or less to be cash equivalents.

*Inventories:* Inventories are valued at the lower of cost or market. Cost is determined using the first-in, first-out method for all inventories. This assessment requires the use of significant estimates to determine replacement cost, cost to complete, normal profit margin and the ultimate selling price of the inventory. No lower of cost or market adjustment was recorded in fiscal 2016. Due to a decline in steel prices in fiscal 2015, the replacement cost of our inventory was lower than what was reflected in our records at May 31, 2015. Accordingly, we recorded a lower of cost or market adjustment of $1,716,000 at May 31, 2015 to reflect this lower value. The entire amount related to our Steel Processing operating segment and was recorded in cost of goods sold. We believe our inventories were valued appropriately as of May 31, 2016 and May 31, 2015.

*Derivative Financial Instruments:* We utilize derivative financial instruments to manage exposure to certain risks related to our ongoing operations. The primary risks managed through the use of derivative instruments include interest rate risk, currency exchange risk and commodity price risk. All derivative instruments are accounted for using mark-to-market accounting. The accounting for changes in the fair value of a derivative instrument depends on whether it has been designated and qualifies as part of a hedging relationship and, if so, the reason for holding it. Gains and losses on fair value hedges are recognized in current period earnings in the same line as the underlying hedged item. The effective portion of gains and losses on cash flow hedges is deferred as a component of accumulated other comprehensive income or loss (“AOCI”) and recognized in earnings at the time the hedged item affects earnings, in the same financial statement caption as the underlying hedged item. Ineffectiveness of the hedges during the fiscal year ended May 31, 2016 (“fiscal 2016”), the fiscal year ended May 31, 2015 (“fiscal 2015”) and the fiscal year ended May 31, 2014 (“fiscal 2014”) was immaterial. Classification in the consolidated statements of earnings of gains and losses related to derivative instruments that do not qualify for hedge accounting is determined based on the underlying intent of the instruments. Cash flows related to derivative instruments are generally classified as operating activities in our consolidated statements of cash flows.

In order for hedging relationships to qualify for hedge accounting under current accounting guidance, we formally document each hedging relationship and its risk management objective. This documentation includes the hedge strategy, the hedging instrument, the hedged item, the nature of the risk being hedged, how hedge effectiveness will be assessed prospectively and retrospectively as well as a description of the method used to measure hedge ineffectiveness.

Derivative instruments are executed only with highly-rated counterparties. No credit loss is anticipated on existing instruments, and no material credit losses have been experienced to date. We monitor our positions, as well as the credit ratings of counterparties to those positions.

We discontinue hedge accounting when it is determined that the derivative instrument is no longer effective in offsetting the hedged risk, expires or is sold, is terminated or is no longer designated as a hedging instrument because it is unlikely that a forecasted transaction will occur or we determine that designation of the hedging instrument is no longer appropriate. In all situations in which hedge accounting is discontinued and the derivative instrument is retained, we continue to carry the derivative instrument at its fair value on the consolidated balance sheet and recognize any subsequent changes in its fair value in net earnings immediately. When it is probable that a forecasted transaction will not occur, we discontinue hedge accounting and immediately recognize the gains and losses that were accumulated in AOCI.

Refer to “Note P – Derivative Instruments and Hedging Activities” for additional information regarding the consolidated balance sheet location and the risk classification of our derivative instruments.

*Risks and Uncertainties*: As of May 31, 2016, we, together with our unconsolidated affiliates, operated 82 manufacturing facilities in 24 states and 11 countries. A total of 31 of these facilities are operated by wholly- owned, consolidated subsidiaries of the Company. The remaining facilities are operated by our consolidated and unconsolidated joint ventures. As of May 31, 2016, we held equity positions in 12 active joint ventures, of which six are consolidated. Our largest market is the automotive market, which comprised 43%, 38%, and 36% of consolidated net sales in fiscal 2016, fiscal 2015, and fiscal 2014, respectively. Our foreign operations represented 8%, 6%, and 7% of consolidated net sales and 10%, (2)%, and (2)% of net earnings attributable to controlling interest in fiscal 2016, fiscal 2015, and fiscal 2014, respectively, and 14% and 14% of consolidated net assets as of May 31, 2016 and 2015, respectively. As of May 31, 2016, approximately 8% of our consolidated labor force was represented by collective bargaining agreements. The concentration of credit risks from financial instruments related to the markets we serve is not expected to have a material adverse effect on our consolidated financial position, cash flows or future results of operations.

In fiscal 2016, our largest customer accounted for approximately 8% of our consolidated net sales, and our ten largest customers accounted for approximately 34% of our consolidated net sales. A significant loss of, or decrease in, business from any of these customers could have an adverse effect on our sales and financial results if we cannot obtain replacement business. Also, due to consolidation within the industries we serve, including the construction, automotive and retail industries, our sales may be increasingly sensitive to deterioration in the financial condition of, or other adverse developments with respect to, one or more of our largest customers.

Our principal raw material is flat-rolled steel, which we purchase from multiple primary steel producers. The steel industry as a whole has been cyclical, and at times availability and pricing can be volatile due to a number of factors beyond our control. This volatility can significantly affect our steel costs. In an environment of increasing prices for steel and other raw materials, in general, competitive conditions may impact how much of the price increases we can pass on to our customers. To the extent we are unable to pass on future price increases in our raw materials to our customers, our financial results could be adversely affected. Also, if steel prices decrease, in general, competitive conditions may impact how quickly we must reduce our prices to our customers and we could be forced to use higher-priced raw materials to complete orders for which the selling prices have decreased. Declining steel prices could also require us to write-down

66

the value of our inventories to reflect current market pricing. Further, the number of suppliers has decreased in recent years due to industry consolidation and the financial difficulties of certain suppliers, and consolidation may continue. Accordingly, if delivery from a major steel supplier is disrupted, it may be more difficult to obtain an alternative supply than in the past.

*Receivables:* We review our receivables on an ongoing basis to ensure that they are properly valued and collectible. This is accomplished through two contra-receivable accounts: returns and allowances and allowance for doubtful accounts. Returns and allowances are used to record estimates of returns or other allowances resulting from quality, delivery, discounts or other issues affecting the value of receivables. This account is estimated based on historical trends and current market conditions, with the offset to net sales. The returns and allowances account decreased approximately $341,000 during fiscal 2016 to

$6,052,000.

The allowance for doubtful accounts is used to record the estimated risk of loss related to the customers’ inability to pay. This allowance is maintained at a level that we consider appropriate based on factors that affect collectability, such as the financial health of our customers, historical trends of charge-offs and recoveries and current economic and market conditions. As we monitor our receivables, we identify customers that may have payment problems, and we adjust the allowance accordingly, with the offset to selling, general and administrative (“SG&A”) expense. Account balances are charged off against the allowance when recovery is considered remote. The allowance for doubtful accounts increased approximately

$1,494,000 during fiscal 2016 to $4,579,000.

While we believe our allowances are adequate, changes in economic conditions, the financial health of customers and bankruptcy settlements could impact our future earnings. If the economic environment and market conditions deteriorate, particularly in the automotive and construction end markets where our exposure is greatest, additional reserves may be required.

*Property and Depreciation:* Property, plant and equipment are carried at cost and depreciated using the straight-line method. Buildings and improvements are depreciated over 10 to 40 years and machinery and equipment over 3 to 20 years. Depreciation expense was $68,886,000, $64,666,000, and $62,344,000 during fiscal 2016, fiscal 2015 and fiscal 2014, respectively. Accelerated depreciation methods are used for income tax purposes.

*Goodwill and Other Long-Lived Assets:* We use the purchase method of accounting for all business combinations and recognize amortizable and indefinite-lived intangible assets separately from goodwill. The acquired assets and assumed liabilities in an acquisition are measured and recognized based on their estimated fair values at the date of acquisition, with goodwill representing the excess of the purchase price over the fair value of the identifiable net assets. A bargain purchase may occur, wherein the fair value of identifiable net assets exceeds the purchase price, and a gain is then recognized in the amount of that excess. Goodwill and intangible assets with indefinite lives are not amortized, but instead are tested for impairment annually, during the fourth quarter, or more frequently if events or changes in circumstances indicate that impairment may be present. Application of goodwill impairment testing involves judgment, including but not limited to, the identification of reporting units and estimation of the fair value of each reporting unit. A reporting unit is defined as an operating segment or one level below an operating segment. With the exception of Pressure Cylinders, we test goodwill at the operating segment level as we have determined that the characteristics of the reporting units within each operating segment are similar and allow for their aggregation in accordance with the applicable accounting guidance. For our Pressure Cylinders operating segment, the Oil & Gas Equipment business has been treated as a separate reporting unit since the second quarter of fiscal 2016.

The goodwill impairment test consists of comparing the fair value of each reporting unit, determined using discounted cash flows, to each reporting unit’s respective carrying value. If the estimated fair value of a reporting unit exceeds its carrying value, there is no impairment. If the carrying amount of the reporting unit

67

exceeds its estimated fair value, goodwill impairment is indicated. The amount of the impairment is determined by comparing the fair value of the net assets of the reporting unit, excluding goodwill, to its estimated fair value, with the difference representing the implied fair value of the goodwill. If the implied fair value of the goodwill is lower than its carrying value, the difference is recorded as an impairment charge in our consolidated statements of earnings. The impairment test for indefinite-lived intangible assets consists of a comparison of the fair value of the intangible asset to its carrying value. If the carrying value of the intangible asset exceeds its fair value, the difference is recorded as an impairment charge in our consolidated statements of earnings.

We review the carrying value of our long-lived assets, including intangible assets with finite useful lives, for impairment whenever events or changes in circumstances indicate that the carrying value of an asset or asset group may not be recoverable. Impairment testing involves a comparison of the sum of the undiscounted future cash flows of the asset or asset group to its respective carrying amount. If the sum of the undiscounted future cash flows exceeds the carrying amount, then no impairment exists. If the carrying amount exceeds the sum of the undiscounted future cash flows, then a second step is performed to determine the amount of impairment, if any, to be recognized. The loss recognized is equal to the amount that the carrying value of the asset or asset group exceeds fair value.

Our impairment testing for both goodwill and other long-lived assets, including intangible assets with finite useful lives, is largely based on cash flow models that require significant judgment and require assumptions about future volume trends, revenue and expense growth rates; and, in addition, external factors such as changes in economic trends and cost of capital. Significant changes in any of these assumptions could impact the outcomes of the tests performed. See “Note C – Goodwill and Other Long-Lived Assets” for additional details regarding these assets and related impairment testing.

*Leases:* Certain lease agreements contain fluctuating or escalating payments and rent holiday periods. The related rent expense is recorded on a straight-line basis over the lease term. Leasehold improvements made by the lessee, whether funded by the lessee or by landlord allowances or incentives, are recorded as leasehold improvement assets and will be amortized over the shorter of the economic life or the lease term. These incentives are also recorded as deferred rent and amortized as reductions in rent expense over the lease term.

*Stock-Based Compensation:* At May 31, 2016, we had stock-based compensation plans for our employees as well as our non-employee directors as described more fully in “Note J – Stock-Based Compensation.” All share-based awards, including grants of stock options and restricted common shares, are recorded as expense in the consolidated statements of earnings based on their grant-date fair values.

*Revenue Recognition*: We recognize revenue upon transfer of title and risk of loss, or in the case of toll processing revenue, upon delivery of the goods, provided evidence of an arrangement exists, pricing is fixed and determinable and the ability to collect is probable. We provide, through charges to net sales, for returns and allowances based on experience and current customer activities. We also provide, through charges to net sales, for customer rebates and sales discounts based on specific agreements and recent and anticipated levels of customer activity. In circumstances where the collection of payment is not probable at the time of shipment, we defer recognition of revenue until payment is collected.

*Advertising Expense:* We expense advertising costs as incurred. Advertising expense was $13,970,000,

$11,153,000, and $6,788,000 for fiscal 2016, fiscal 2015 and fiscal 2014, respectively.

*Shipping and Handling Fees and Costs:* Shipping and handling fees billed to customers are included in net sales, and shipping and handling costs incurred are included in cost of goods sold.

*Environmental Costs:* Environmental costs are capitalized if the costs extend the life of the property, increase its capacity, and/or mitigate or prevent contamination from future operations. Costs related to environmental contamination treatment and clean up are charged to expense as incurred.

68

*Statements of Cash Flows:* Supplemental cash flow information was as follows for the fiscal years ended May 31:

|  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- |
| **(in thousands)** | **2016** |  | **2015** |  | **2014** |
| Interest paid, net of amount capitalized | $30,431 |  | $36,190 |  | $24,199 |
| Income taxes paid, net of refunds | 50,750 |  | 67,825 |  | 81,997 |

We use the “cumulative earnings” approach for determining cash flow presentation of distributions from our unconsolidated joint ventures. Distributions received are included in our consolidated statements of cash flows as operating activities, unless the cumulative distributions exceed our portion of the cumulative equity in the net earnings of the joint venture, in which case the excess distributions are deemed to be returns of the investment and are classified as investing activities in our consolidated statements of cash flows.

*Income Taxes:* We account for income taxes using the asset and liability method. The asset and liability method requires the recognition of deferred tax assets and liabilities for expected future tax consequences of temporary differences that currently exist between the tax basis and the financial reporting basis of our assets and liabilities. In assessing the realizability of deferred tax assets, we consider whether it is more likely than not that all, or a portion, of the deferred tax assets will not be realized. We provide a valuation allowance for deferred income tax assets when it is more likely than not that a portion of such deferred income tax assets will not be realized.

Tax benefits from uncertain tax positions that are recognized in the consolidated financial statements are measured based on the largest benefit that has a greater than fifty percent likelihood of being realized upon ultimate settlement.

We have reserves for taxes and associated interest and penalties that may become payable in future years as a result of audits by taxing authorities. It is our policy to record these in income tax expense. While we believe the positions taken on previously filed tax returns are appropriate, we have established the tax and interest reserves in recognition that various taxing authorities may challenge our positions. The tax reserves are analyzed periodically, and adjustments are made as events occur to warrant adjustment to the reserves, such as lapsing of applicable statutes of limitations, conclusion of tax audits, additional exposure based on current calculations, identification of new issues and release of administrative guidance or court decisions affecting a particular tax issue.

*Self-Insurance Reserves:* We are largely self-insured with respect to workers’ compensation, general and automobile liability, property damage, employee medical claims and other potential losses. In order to reduce risk and better manage our overall loss exposure, we purchase stop-loss insurance that covers individual claims in excess of the deductible amounts. We maintain reserves for the estimated cost to settle open claims, which includes estimates of legal costs expected to be incurred, as well as an estimate of the cost of claims that have been incurred but not reported. These estimates are based on actuarial valuations that take into consideration the historical average claim volume, the average cost for settled claims, current trends in claim costs, changes in our business and workforce, general economic factors and other assumptions believed to be reasonable under the circumstances. The estimated reserves for these liabilities could be affected if future occurrences and claims differ from the assumptions used and historical trends.

*Recently Issued Accounting Standards*: In May 2014, amended accounting guidance was issued that replaces most existing revenue recognition guidance under U.S. GAAP. The amended guidance requires an entity to recognize the amount of revenue to which it expects to be entitled for the transfer of promised goods or services to customers. Subsequently, additional guidance was issued on several areas including guidance intended to improve the operability and understandability of the implementation of principal versus agent considerations and clarifications on the identification of performance obligations and

69

implementation of guidance related to licensing. The amended guidance is effective for annual reporting periods beginning after December 15, 2017, including interim periods within that reporting period. We are in the process of evaluating the effect this guidance will have on our consolidated financial position and results of operations. The amended guidance permits the use of either the retrospective or cumulative effect transition method. We have not selected a transition method nor have we determined the effect of the amended guidance on our ongoing financial reporting.

In February 2015, amended accounting guidance was issued that revised consolidation requirements in order to provide financial statement users with a more useful presentation of an entity’s economic and operational results. The amended guidance is effective for fiscal years beginning after December 15, 2015, including interim periods within those fiscal years. Early adoption is permitted, and the amendments may be applied using either a retrospective or modified retrospective approach. We do not expect the adoption of this amended accounting guidance to have a material impact on our financial position or results of operations.

In April 2015, amended accounting guidance was issued to simplify the presentation of debt issuance costs by requiring that such costs be presented in the balance sheet as a direct deduction from the carrying amount of the corresponding debt liability itself. The amended guidance is effective for financial statements issued for fiscal years beginning after December 15, 2015, including interim periods within those fiscal years. Early adoption is permitted for financial statements that have not been issued. Retrospective application to prior periods is required. The adoption of this guidance will not have a significant impact on our consolidated financial position and results of operations.

In July 2015, amended accounting guidance was issued regarding the measurement of inventory. The amended guidance requires that inventory accounted for under the first-in, first-out (FIFO) or average cost methods be measured at the lower of cost and net realizable value, where net realizable value represents the estimated selling price of inventory in the ordinary course of business, less reasonably predictable costs of completion, disposal, and transportation. The amended guidance has no impact on inventory accounted for under the last-in, first-out (LIFO) or retail inventory methods. The amended guidance is effective prospectively for fiscal years beginning after December 15, 2016, including interim periods within those fiscal years. Early adoption is permitted as of the beginning of an interim or annual reporting period. We do not expect the adoption of this amended accounting guidance to have a material impact on our financial position or results of operations.

In September 2015, amended accounting guidance was issued regarding adjustments to provisional amounts reported in conjunction with a business combination. The amended guidance requires that an acquirer in a business combination recognize adjustments to provisional amounts identified during the measurement period in the reporting period in which the adjustment amounts are determined. The amendment also requires that the acquirer record, in the same period’s financial statements, the effect on earnings of changes in depreciation, amortization, or other income effects, if any, as a result of the change, calculated as if the accounting had been completed at the acquisition date. Additionally, the amendment requires the acquirer to present separately on the face of the income statement or disclose in the notes the portion of the amount recorded in current-period earnings by line item that would have been recorded in previous reporting periods if the adjustment to the provisional amounts had been recognized as of the acquisition date. The amended guidance is effective prospectively for fiscal years beginning after December 15, 2015, including interim periods within those fiscal years. Early adoption is permitted for financial statements that have not been issued. We do not expect the adoption of this amended accounting guidance to have a material impact on our financial position or results of operations.

In November 2015, amended accounting guidance was issued that simplifies the presentation of deferred income taxes. The amended guidance requires entities with a classified balance sheet to present all deferred income tax assets and liabilities as noncurrent. The amended guidance is effective for financial

70

statements issued for annual periods beginning after December 15, 2016, including interim periods within those annual periods. Early adoption is permitted as of the beginning of an interim or annual reporting period, and the change may be applied either prospectively or retrospectively. The Company elected to early adopt this amended accounting guidance during the fourth quarter of fiscal 2016. The adoption was on a prospective basis and therefore prior periods have not been restated.

In February 2016, amended accounting guidance was issued that replaces most existing lease accounting guidance under U.S. GAAP. Among other changes, the amended guidance requires that lease assets and liabilities be recognized on the balance sheet by lessees for those leases classified as operating leases under previous guidance. The amended guidance is effective for fiscal years beginning after December 15, 2018, including interim periods within those fiscal years. Early adoption is permitted, and the change is to be applied using a modified retrospective approach as of the beginning of the earliest period presented. We are in the process of evaluating the effect this guidance will have on our consolidated financial position and results of operations, and we have not determined the effect of the amended guidance on our ongoing financial reporting.

In March 2016, amended accounting guidance was issued regarding derivatives instruments designated as hedging instruments. The amended guidance clarifies that a change in the counterparty to such a hedging instrument does not, in and of itself, require dedesignation of that hedging relationship provided that all other hedge accounting criteria continue to be met. The amended guidance is effective for fiscal years beginning after December 15, 2016, including interim periods within those fiscal years. Early adoption is permitted, and the change may be applied either prospectively or retrospectively. We do not expect the adoption of this amended accounting guidance to have a material impact on our financial position or results of operations.

In March 2016, amended accounting guidance was issued that simplifies the accounting for share-based payments. The amended guidance impacts several aspects of the accounting for share-based payment transactions, including the income tax consequences, forfeitures, statutory withholding requirements, and classification in the statement of cash flows. The amended guidance is effective for fiscal years beginning after December 15, 2016, including interim periods within those fiscal years. Early adoption is permitted. The Company elected to early adopt this amended accounting guidance during the fourth quarter of fiscal 2016. The impact resulting from the adoption of this amended guidance is summarized below.

* *Income Tax Accounting* – The amended accounting guidance requires all excess tax benefits and tax deficiencies to be recognized as an income tax benefit or expense on a prospective basis in the period of adoption. The adoption of this provision of the amended accounting guidance resulted in the recognition of excess tax benefits of $3,178,000 in income tax expense, rather than in paid-in capital, during fiscal 2016. As the adoption was on a prospective basis, prior periods have not been restated.
* *Forfeitures* – The Company has elected to continue to estimate the number of awards expected to vest, as permitted by the amended accounting guidance, rather than electing to account for forfeitures as they occur.
* *Statement of Cash Flows Presentation* – The amended accounting guidance requires excess tax benefits to be classified as an operating activity in the statement of cash flows. Previously, excess tax benefits were presented as a cash inflow from financing activities and cash outflow from operating activities. The Company has elected to present these changes on a prospective basis and therefore prior periods have not been adjusted to conform with the current presentation.

In June 2016, amended accounting guidance was issued related to the measurement of credit losses on financial instruments. The amended guidance changes the impairment model for most financial assets to require measurement and recognition of expected credit losses for financial assets held. The amended guidance is effective for fiscal years beginning after December 15, 2019, including interim periods within

71

those fiscal years. We are in the process of evaluating the effect this guidance will have on our consolidated financial position and results of operations, and we have not determined the effect of the amended guidance on our ongoing financial reporting.

## Note B – Investments in Unconsolidated Affiliates

At May 31, 2016, equity investments and the percentage interests owned consisted of the following (in alphabetic order): ArtiFlex Manufacturing, LLC (“ArtiFlex”) (50%), Clarkwestern Dietrich Building Systems LLC (“ClarkDietrich”) (25%), Samuel Steel Pickling Company (31.25%), Serviacero Planos, S. de R. L. de C.V. (“Serviacero”) (50%), Worthington Armstrong Venture (“WAVE”) (50%), and Zhejiang Nisshin Worthington Precision Specialty Steel Co., Ltd. (10%).

Effective March 1, 2016, the Company reached an agreement with United States Steel Corporation (“U.S. Steel”), its partner in the WSP joint venture, whereby the Company appoints a majority of the WSP Board of Directors, giving the Company effective control over the operations of WSP. Since that date, WSP’s results have been consolidated within the financial results of Steel Processing versus being reported in equity in net income of unconsolidated affiliates. For additional information, refer to “Note O – Acquisitions.”

On October 18, 2013, we finalized an agreement with Nisshin Steel Co., Ltd. and Marubeni-Itochu Steel Inc. to form Zhejiang Nisshin Worthington Precision Specialty Steel Co., Ltd. We own a 10% interest in the joint venture with the option to increase our ownership interest to 34%. The joint venture is constructing a facility to produce cold-rolled strip steel, primarily for the automotive industry, which is scheduled to start production in the first quarter of fiscal 2017.

During the second quarter of fiscal 2014, we dissolved our wind tower joint venture, Gestamp Worthington Wind Steel, LLC, due to the volatile political environment in the United States, particularly in regards to the Federal Production Tax Credit. This event did not have a material impact on our financial position or results of operations.

On July 31, 2013, we acquired an additional 10% interest in our laser welded blank joint venture, TWB, increasing our ownership to a 55% controlling interest. Since that date, TWB’s results have been consolidated within the financial results of Steel Processing versus being reported in equity in net income of unconsolidated affiliates. For additional information, refer to “Note O – Acquisitions.”

We received distributions from unconsolidated affiliates totaling $86,513,000, $78,297,000, and

$85,346,000 in fiscal 2016, fiscal 2015 and fiscal 2014, respectively. We have received cumulative distributions from WAVE in excess of our investment balance, which resulted in an amount recorded within other liabilities on our consolidated balance sheets of $52,983,000 and $61,585,000 at May 31, 2016 and 2015, respectively. In accordance with the applicable accounting guidance, we reclassified the negative balance to the liability section of our consolidated balance sheet. We will continue to record our equity in the net income of WAVE as a debit to the investment account, and if it becomes positive, it will again be shown as an asset on our consolidated balance sheet. If it becomes probable that any excess distribution may not be returned (upon joint venture liquidation or otherwise), we will recognize any balance classified as a liability as income immediately.

We use the “cumulative earnings” approach for determining cash flow presentation of distributions from our unconsolidated joint ventures. Distributions received are included in our consolidated statements of cash flows as operating activities, unless the cumulative distributions exceed our portion of the cumulative equity in the net earnings of the joint venture, in which case the excess distributions are deemed to be returns of the investment and are classified as investing activities in our consolidated statements of cash flows. During fiscal 2015, we received excess distributions from ClarkDietrich of $570,000.

The following table presents combined information of the financial position of our unconsolidated affiliates accounted for using the equity method as of May 31, 2016 and 2015:

|  |  |  |  |
| --- | --- | --- | --- |
| **(in thousands)** | **2016** |  | **2015** |
| Cash | $112,122 |  | $101,011 |
| Receivable from member (1) | - |  | 11,092 |
| Other current assets | 446,796 |  | 491,507 |
| Noncurrent assets | 352,370 |  | 318,939 |
| Total assets | $911,288 |  | $922,549 |
| Current liabilities | $112,491 |  | $184,028 |
| Short-term borrowings | 11,398 |  | - |
| Current maturities of long-term debt | 3,297 |  | 4,489 |
| Long-term debt | 266,942 |  | 272,861 |
| Other noncurrent liabilities | 21,034 |  | 20,471 |
| Equity | 496,126 |  | 440,700 |
| Total liabilities and equity | $911,288 |  | $922,549 |
|  |  |  |  |

(1) Represents cash owed from a third-party joint venture partner as a result of centralized cash management. The decrease in fiscal 2016 is due to the consolidation of the WSP joint venture.

The following table presents financial results of our four largest unconsolidated affiliates for fiscal 2016, fiscal 2015 and fiscal 2014. All other unconsolidated affiliates are combined and presented in the Other category.

|  |  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- | --- |
|  | **(in thousands)** | **2016** |  | **2015** |  | **2014** |
| **Net sales** |  |  |  |  |  |  |
| WAVE |  | $ 393,718 |  | $ 382,451 |  | $ 382,821 |
| ClarkDietrich |  | 615,609 |  | 576,171 |  | 549,267 |
| Serviacero |  | 260,337 |  | 277,385 |  | 249,661 |
| ArtiFlex |  | 219,510 |  | 183,029 |  | 170,531 |
| Other |  | 74,214 |  | 91,144 |  | 140,522 |
| Total net sales |  | $1,563,388 |  | $1,510,180 |  | $1,492,802 |
| **Gross margin** |  |  |  |  |  |  |
| WAVE | $ 207,143 |  | $ 181,102 |  | $ 177,935 |
| ClarkDietrich | 95,427 |  | 65,530 |  | 73,803 |
| Serviacero | 15,328 |  | 17,028 |  | 22,268 |
| ArtiFlex | 30,181 |  | 24,145 |  | 16,839 |
| Other | 13,142 |  | 14,201 |  | 21,775 |
| Total gross margin | $ 361,221 |  | $ 302,006 |  | $ 312,620 |
| **Operating income** |  |  |  |  |  |  |
| WAVE | $ 172,721 |  | $ 147,603 |  | $ 144,167 |
| ClarkDietrich | 33,897 |  | 10,436 |  | 27,918 |
| Serviacero | 11,110 |  | 14,036 |  | 19,413 |
| ArtiFlex | 22,612 |  | 16,476 |  | 9,785 |
| Other | 6,910 |  | 4,980 |  | 12,649 |
| Total operating income | $ 247,250 |  | $ 193,531 |  | $ 213,932 |
| **Depreciation and amortization** |  |  |  |  |  |
| WAVE | $ 4,120 |  | $ 4,150 |  | $ 4,916 |
| ClarkDietrich | 14,289 |  | 16,638 |  | 16,523 |
| Serviacero | 3,508 |  | 3,462 |  | 3,533 |
| ArtiFlex | 6,105 |  | 7,258 |  | 7,129 |
| Other | 3,081 |  | 4,154 |  | 4,857 |
| Total depreciation and amortization | $ 31,103 |  | $ 35,662 |  | $ 36,958 |
| **Interest expense (income)** |
| WAVE | $ 6,635 |  | $ 6,412 |  | $ 6,464 |
| ClarkDietrich | 80 |  | 138 |  | 103 |
| Serviacero | 114 |  | 201 |  | 474 |
| ArtiFlex | 1,650 |  | 1,973 |  | 2,183 |
| Other | (10) | (29) | (2) |
| Total interest expense | $ 8,469 |  | $ 8,695 |  | $ 9,222 |
| **Income tax expense** |  |  |  |  |  |  |
| WAVE | $ 2,449 |  | $ 2,539 |  | $ 3,606 |
| ClarkDietrich | - |  | - |  | - |
| Serviacero | 6,249 |  | 7,844 |  | 5,689 |
| ArtiFlex | 289 |  | 105 |  | 82 |
| Other | 53 |  | - |  | 477 |
| Total income tax expense | $ 9,040 |  | $ 10,488 |  | $ 9,854 |
| **Net earnings** |  |  |  |  |  |  |
| WAVE | $ 164,132 |  | $ 138,670 |  | $ 134,019 |
| ClarkDietrich | 58,539 |  | 11,799 |  | 27,837 |
| Serviacero | 6,246 |  | 8,429 |  | 14,530 |
| ArtiFlex | 20,673 |  | 14,398 |  | 7,539 |
| Other | 8,516 |  | 4,806 |  | 12,206 |
| Total net earnings | $ 258,106 |  | $ 178,102 |  | $ 196,131 |

The financial results of WSP have been included in the amounts presented in the tables above through March 1, 2016. Effective March 1, 2016, the Company obtained effective control over the operations of WSP. As a result, WSP’s results have been consolidated within the financial results of Steel Processing since that date with the minority member’s portion of earnings eliminated within earnings attributable to noncontrolling interest.

The financial results of TWB have been included in the amounts presented in the tables above through July 31, 2013. On July 31, 2013, we completed the acquisition of an additional 10% interest in TWB. As a result, TWB’s results have been consolidated within the financial results of Steel Processing since that date with the minority member’s portion of earnings eliminated within earnings attributable to noncontrolling interest.

At May 31, 2016, $23,283,000 of our consolidated retained earnings represented undistributed earnings, net of tax, of our unconsolidated affiliates.

## Note C – Goodwill and Other Long-Lived Assets

Fiscal 2016: Due to the decline in oil prices and resulting reduced demand for products, management determined that an impairment indicator was present for the long-lived assets in the Oil & Gas Equipment business within Pressure Cylinders. The Company had tested the five asset groups in its Oil & Gas Equipment business for impairment during the fourth quarter of fiscal 2015 and again in the first quarter of fiscal 2016. In each of these tests, the Company’s estimate of the undiscounted future cash flows for each asset group indicated that the carrying amounts were expected to be recovered as of those measurement dates.

During the second quarter of fiscal 2016, the continued decline of oil prices further reduced the demand for Oil & Gas Equipment products, causing a significant decrease in the long-term cash flow projections of that business. Based on these revised cash flow projections, the Company determined that long-lived assets of two of the facilities with a combined carrying amount of $59,895,000 were impaired and wrote them down to their estimated fair value of $36,933,000, resulting in an impairment charge of $22,962,000. Fair value was based on expected future cash flows using Level 3 inputs under Accounting Standard Codification (“ASC”) 820. The cash flows are those expected to be generated by market participants, discounted at an appropriate rate for the risks inherent in those cash flow projections, or 13%. Because of deteriorating market conditions (i.e., rising interest rates and declining marketplace demand), it is possible that our estimate of discounted cash flows may change resulting in the need to adjust our determination of fair value.

As a result of the impairment of the Oil & Gas Equipment assets noted above, the Company also performed an impairment review of the goodwill of the Pressure Cylinders reporting unit during the second quarter of fiscal 2016. The Company first assessed the reporting unit structure and determined that it was no longer appropriate to aggregate the Oil & Gas Equipment component with the rest of Pressure Cylinders for purposes of goodwill impairment testing. This determination was driven by changes in the economic characteristics of the Oil & Gas Equipment business as a result of sustained low oil prices, which now indicate that the risk profile and prospects for growth and profitability of the Oil & Gas Equipment component are no longer similar to the other components of our Pressure Cylinders businesses. In accordance with the applicable accounting guidance, the Company allocated a portion of Pressure Cylinders goodwill totaling

$25,982,000 to the Oil & Gas Equipment reporting unit using a relative fair value approach. A subsequent comparison of the fair values of the Oil & Gas Equipment and the Pressure Cylinders reporting units, determined using discounted cash flows, to their respective carrying values indicated that a step 2 calculation to quantify a potential impairment was not required. The key assumptions that drive the fair value calculations are projected cash flows and the discount rate. Prior to the allocation of goodwill, the Company tested the goodwill of the old Pressure Cylinders reporting unit for impairment and determined that fair value exceeded carrying value by a significant amount.

During the first quarter of fiscal 2016, management finalized its plan to close the Engineered Cabs facility in Florence, South Carolina and transfer the majority of the business to the Engineered Cabs facility in

Greeneville, Tennessee. Under the plan, certain machinery and equipment was transferred to the Greeneville facility to support higher volume requirements. Management reevaluated the recoverability of the remaining assets and determined that long-lived assets with a carrying value of $4,059,000 were impaired. As a result, these long-lived assets were written down to their estimated fair value of $1,059,000 resulting in an impairment charge of $3,000,000 during the first quarter of fiscal 2016. The Company ceased production at the Florence facility on September 30, 2015.

Fiscal 2015: During the fourth quarter of fiscal 2015, we determined that indicators of impairment were present with regard to intangible assets related to our compressed natural gas (“CNG”) fuel systems joint venture, dHybrid. Recoverability of the identified asset group was tested using future cash flow projections based on management’s long-range estimates of market conditions. The sum of these undiscounted future cash flows was less than the net book value of the asset group. In accordance with the applicable accounting guidance, the intangible assets were written down to their fair value, resulting in an impairment charge of

$2,344,000.

During the third quarter of fiscal 2015, the Company concluded that an interim impairment test of the goodwill of its Engineered Cabs reporting unit was necessary. This conclusion was based on certain indicators of impairment, including the decision to close the Company’s Engineered Cabs’ facility in Florence, South Carolina and significant downward revisions to forecasted cash flows as a result of continued weakness in the mining and agricultural end markets and higher than expected manufacturing costs.

Prior to conducting the goodwill impairment test, the Company first evaluated the other long-lived assets of the Engineered Cabs reporting unit for recoverability. Recoverability was tested using future cash flow projections based on management’s long-range estimates of market conditions. The sums of the undiscounted future cash flows for the customer relationship intangible asset and the property, plant and equipment of the Florence, South Carolina facility were less than their respective carrying values. As a result, these assets were written down to their respective fair values, resulting in impairment charges of $22,356,000 for the customer relationship intangible asset and $14,311,000 for the property, plant and equipment of the Florence asset group during the third quarter of fiscal 2015. As noted above, an additional impairment charge related to the Florence asset group was later recognized during the first quarter of fiscal 2016.

As noted above, the Company determined that indicators of potential impairment existed to require an interim goodwill analysis of the Engineered Cabs reporting unit. A comparison of the fair value of the Engineered Cabs reporting unit, determined using discounted cash flows, to its carrying value indicated that a step 2 calculation to quantify the potential impairment was required. After a subsequent review of the fair value of the net assets of Engineered Cabs, it was determined that the implied fair value of goodwill was $0 and, accordingly, the entire $44,933,000 goodwill balance was written-off during the third quarter of fiscal 2015. The key assumptions used in the fair value calculations were projected cash flows and the discount rate.

During the second quarter of fiscal 2015, management committed to a plan to sell the assets of the Advanced Component Technologies, Inc. (“ACT”) business within Engineered Cabs. In accordance with the applicable accounting guidance, the net assets were recorded at the lower of net book value or fair value less costs to sell, resulting in an impairment charge of $2,389,000. During the third quarter of fiscal 2015, the Company completed the sale of these assets and recognized a gain of $332,000.

Also during the second quarter of fiscal 2015, we determined that indicators of impairment were present at the Company’s aluminum high-pressure cylinder business in New Albany, Mississippi, and at the Company’s military construction business due to current and projected operating losses. Recoverability of the identified asset groups was tested using future cash flow projections based on management’s long-range estimates of market conditions. The sum of the undiscounted future cash flows was less than the net book value of the asset groups. In accordance with the applicable accounting guidance, the net assets were written down to their fair values, resulting in impairment charges of $3,221,000 and $1,179,000, respectively.

During the fourth quarter of fiscal 2014, the Company committed to a plan to sell its 60% ownership interest in Worthington Nitin Cylinders, a consolidated joint venture in India, and Precision Specialty Metals (“PSM”), a stainless steel business. Accordingly, at May 31, 2014, the net assets of these businesses were recorded as assets held for sale at the lower of their fair values or net book values, less selling costs. During the first half of fiscal 2015, changes in facts and circumstances related to these businesses indicated that the Company needed to reassess the fair value of these assets. As a result, additional impairment charges of

$6,346,000 and $3,050,000, respectively, were recorded. The Company completed the sale of Worthington Nitin Cylinders during the second quarter of fiscal 2016.

Fiscal 2014: As noted above, during the fourth quarter of fiscal 2014, management committed to a plan to sell Worthington Nitin Cylinders and PSM. In accordance with the applicable accounting guidance, the net assets were recorded at the lower of net book value or fair value less costs to sell resulting in impairment charges of $18,959,000 and $7,141,000, respectively. The portion of the Worthington Nitin Cylinders impairment charge attributable to the noncontrolling interest was $7,583,000 and was recorded within net earnings attributable to noncontrolling interest.

During the fourth quarter of fiscal 2014, we determined that indicators of impairment were present at the Company’s aluminum high-pressure cylinder business in New Albany, Mississippi, due to current and projected operating losses. Recoverability of the identified asset group was tested using future cash flow projections based on management’s long-range estimates of market conditions. The sum of these undiscounted future cash flows was less than the net book value of the asset group. In accordance with the applicable accounting guidance, the net assets were written down to their fair value of $7,034,000, resulting in an impairment charge of $1,412,000.

During the second quarter of fiscal 2014, we committed to a re-branding initiative. Under the re- branding initiative, we re-branded substantially all of our businesses under the Worthington Industries name. In connection with the change in branding strategy, we discontinued the use of all non-Worthington trade names except those related to consumer products such as BernzOmatic® and Balloon Time® and those related to our joint ventures. As a result, we determined an impairment indicator was present for the trade names that have been or will be discontinued. As no future cash flows will be attributed to the impacted trade names, the entire book value was written off, resulting in an impairment charge of $30,734,000.

## Goodwill

The following table summarizes the changes in the carrying amount of goodwill during fiscal 2016 and fiscal 2015 by reportable business segment:

## (in thousands) Balance at May 31, 2014

**Steel Processing**

**Pressure Cylinders**

**Engineered**

**Cabs Other Total**

|  |  |  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- | --- | --- |
| Goodwill | $ - |  | $200,509 |  | $ 44,933 |  | $ 127,245 $ 372,687 |
| Accumulated impairment losses | - |  | - |  | - |  | (121,594) (121,594) |
|  | - |  | 200,509 |  | 44,933 |  | 5,651 251,093 |
| Acquisitions and purchase accounting adjustments | 6,587 |  | 41,421 |  | - |  | - 48,008 |
| Divestitures | - |  | (1,891) |  | - |  | - (1,891) |
| Translation adjustments | - |  | (13,278) |  | - |  | - (13,278) |
| Impairment losses | - |  | - |  | (44,933) |  | - (44,933) |
|  | 6,587 |  | 26,252 |  | (44,933) |  | - (12,094) |
| **Balance at May 31, 2015**Goodwill | 6,587 |  | 226,761 |  | 44,933 |  | 127,245 405,526 |
| Accumulated impairment losses | - |  | - |  | (44,933) |  | (121,594) (166,527) |
|  | 6,587 |  | 226,761 |  | - |  | 5,651 238,999 |
| Acquisitions and purchase accounting adjustments | 458 |  | 6,713 |  | - |  | - 7,171 |
| Translation adjustments | - |  | (103) |  | - |  | - (103) |
|  | 458 |  | 6,610 |  | - |  | - 7,068 |
| **Balance at May 31, 2016**Goodwill | 7,045 |  | 233,371 |  | 44,933 |  | 127,245 412,594 |
| Accumulated impairment losses | - |  | - |  | (44,933) |  | (121,594) (166,527) |
|  | $7,045 |  | $233,371 |  | $ - |  | $ 5,651 $ 246,067 |

For additional information regarding the Company’s acquisitions, refer to “Note O – Acquisitions.”

## Other Intangible Assets

Intangible assets with definite lives are amortized on a straight-line basis over their estimated useful lives, which range from one to 20 years. The following table summarizes other intangible assets by class as of May 31, 2016 and 2015:

## 2016 2015

**(in thousands) Cost**

Indefinite-lived intangible assets:

## Accumulated Amortization Cost

**Accumulated Amortization**

|  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- |
| Trademarks | $ 14,501 |  | $ - $ 12,601 |  | $ - |
| Total indefinite-lived intangible assets | 14,501 |  | - 12,601 |  | - |
| Definite-lived intangible assets: |  |  |  |  |  |
| Customer relationships | $ 96,072 |  | $35,561 |  | $119,871 |  | $34,421 |
| Non-compete agreements | 9,422 |  | 6,237 |  | 14,221 |  | 6,897 |
| Technology / know-how | 21,689 |  | 3,865 |  | 15,633 |  | 2,350 |
| Other | 4,012 |  | 3,869 |  | 4,338 |  | 3,879 |
| Total definite-lived intangible assets | 131,195 |  | 49,532 |  | 154,063 |  | 47,547 |
| Total intangible assets | $145,696 |  | $49,532 |  | $166,664 |  | $47,547 |

Amortization expense of $15,813,000, $20,422,000, and $17,386,000 was recognized during fiscal 2016, fiscal 2015 and fiscal 2014, respectively.

Amortization expense for each of the next five fiscal years is estimated to be:

## (in thousands)

|  |  |
| --- | --- |
| 2017 | $13,664 |
| 2018 | $13,225 |
| 2019 | $10,772 |
| 2020 | $ 8,385 |
| 2021 | $ 7,813 |

**Note D – Restructuring and Other Expense**

We consider restructuring activities to be programs whereby we fundamentally change our operations such as closing and consolidating manufacturing facilities, moving manufacturing of a product to another location, and employee severance (including rationalizing headcount or other significant changes in personnel).

A progression of the liabilities associated with our restructuring activities, combined with a reconciliation to the restructuring and other expense (income) financial statement caption in our consolidated statement of earnings for fiscal 2016, is summarized below:

|  |  |  |  |  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- | --- | --- | --- | --- |
| **(in thousands)** | **Beginning Balance** |  | **Expense** |  | **Payments** |  | **Adjustments** |  | **Ending Balance** |
| Early retirement and severance | $2,170 |  | $ 6,137 |  | $ (5,746) |  | $(730) |  | $1,831 |
| Facility exit and other costs | 371 |  | 7,967 |  | (7,482) |  | (203) |  | 653 |
|  | $2,541 |  | 14,104 |  | $(13,228) |  | $(933) |  | $2,484 |
| Net gain on sale of assets |  |  | (6,927) |  |  |  |  |  |  |
| Restructuring and other expense |  |  | $ 7,177 |  |  |  |  |  |  |

During fiscal 2016, the following actions were taken related to the Company’s restructuring activities:

* In connection with the closure of the Engineered Cabs facility in Florence, South Carolina the Company recognized severance expense of $1,929,000 and facility exit costs of $1,283,000. The Company also recognized a net loss of $207,000 related to the disposal of assets.
* The Company recognized severance expense of $1,803,000 related to workforce reductions in our Oil & Gas Equipment business within Pressure Cylinders.
* In connection with the closure of the Company’s stainless steel business, PSM, the Company recognized $5,863,000 of facility exit costs and severance expense of $1,122,000. The Company also recognized a net gain of $670,000 related to the disposal of assets.
* In connection with the pending closure of the steel packaging facility in York, Pennsylvania, the Company recognized severance expense of $589,000.
* The Company recognized a gain of $2,978,000 in connection with the sale of the remaining fixed assets of its legacy Baltimore steel processing facility. The Company also recorded a $240,000 credit to severance expense and recognized facility exit costs of $130,000 during fiscal 2016 related to this matter.
* The Company recognized a gain of $1,484,000 in connection with the sale of the remaining land and building of its legacy metal framing business.
* The Company recognized a gain of $1,928,000 in connection with the sale of its interest in Worthington Nitin Cylinders, the Company’s alternative fuels joint venture in India. The sale was completed on January 28, 2016.
* In connection with the consolidation of the cryogenics trailer business in Boston, Massachusetts, to the recently acquired facility in Theodore, Alabama, the Company recognized severance expense of

$550,000.

* The Company incurred severance expense and facility costs totaling $384,000 and $691,000, respectively, related to other non-significant restructuring activities.

The total liability as of May 31, 2016 is expected to be paid in the next twelve months.

A progression of the liabilities associated with our restructuring activities, combined with a reconciliation to the restructuring and other expense (income) financial statement caption in our consolidated statement of earnings for fiscal 2015, is summarized as follows:

|  |  |  |  |  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- | --- | --- | --- | --- |
| **(in thousands)** | **Beginning Balance** |  | **Expense** |  | **Payments** |  | **Adjustments** |  | **Ending Balance** |
| Early retirement and severance | $6,495 |  | $3,323 |  | $(7,694) |  | $ 46 |  | $2,170 |
| Facility exit and other costs | 534 |  | 1,266 |  | (1,568) |  | 139 |  | 371 |
|  | $7,029 |  | 4,589 |  | $(9,262) |  | $185 |  | $2,541 |
| Net loss on sale of assets |  |  | 2,338 |  |  |  |  |  |  |
| Restructuring and other expense |  |  | $6,927 |  |  |  |  |  |  |

During fiscal 2015, the following actions were taken related to the Company’s restructuring activities:

* In connection with the wind-down of our former Metal Framing operating segment, we recognized

$413,000 of facility exit and other costs.

* The Company completed the sale of its aluminum high-pressure cylinder business in New Albany, Mississippi, for cash proceeds of $8,415,000. A loss of $2,670,000 was recognized as a result of the transaction, which included $1,891,000 of allocated goodwill. The Company also recognized an accrual of $664,000 for expected severance costs associated with the transaction.
* The Company completed the sale of the ACT business within Engineered Cabs for cash proceeds of

$2,622,000, resulting in a gain of $332,000.

* On March 24, 2015, the Company announced a workforce reduction in several Oil & Gas Equipment locations due to slowing demand. The Company recognized an accrual of $2,221,000 for expected severance costs covering those affected by the workforce reductions.
* In connection with the consolidation of the BernzOmatic hand torch manufacturing operation in Medina, New York into the existing Pressure Cylinders’ facility in Chilton, Wisconsin, we incurred

$853,000 of facility exit costs.

* In connection with the wind down of the Military Construction business, the Company recognized an accrual of $366,000 for expected severance costs.

## Note E – Contingent Liabilities and Commitments Legal Proceedings

We are defendants in certain legal actions. In the opinion of management, the outcome of these actions, which is not clearly determinable at the present time, would not significantly affect our consolidated financial position or future results of operations. We also believe that environmental issues will not have a material effect on our capital expenditures, consolidated financial position or future results of operations.

## Insurance Recoveries

On August 19, 2013, a fire occurred at our Pressure Cylinders facility in Kienberg, Austria, in the building that houses the massing process in the production of acetylene cylinders. The other portions of the Austrian facility were not damaged; however, the massing process building sustained extensive damage and was rendered inoperable. Additionally, we incurred incremental business interruption costs. The Company had business interruption and property damage insurance and, as a result, the fire did not have a material adverse impact on the Company’s consolidated financial results.

During fiscal 2015, the Company received proceeds of $1,248,000 representing advance payments for the replacement value of damaged equipment. These proceeds were in excess of the $243,000 remaining book value of the assets, resulting in a gain of $1,005,000 within miscellaneous income.

Total proceeds received related to insurance claims since the date of loss have been as follows:

## (in thousands)

|  |  |
| --- | --- |
| Property and equipment | $ 6,892 |
| Business interruption | 5,521 |
| Other expenses | 1,001 |
| Total insurance proceeds | $13,414 |

Proceeds for business interruption related to the loss of profits since the date of the fire and have been recorded as a reduction of manufacturing expense, including $2,653,000 during fiscal 2015. Proceeds for other expenses represent reimbursement for incremental expenses related to the fire and were recorded as an offset to manufacturing expense, including $256,000 during fiscal 2015. This claim was settled during the third quarter of fiscal 2015.

## Note F – Guarantees

We do not have guarantees that we believe are reasonably likely to have a material current or future effect on our financial condition, changes in financial condition, revenues or expenses, results of operations, liquidity, capital expenditures or capital resources. However, as of May 31, 2016, we were party to an operating lease for an aircraft in which we have guaranteed a residual value at the termination of the lease. The maximum obligation under the terms of this guarantee was approximately $10,510,000 at May 31, 2016. Based on current facts and circumstances, we have estimated the likelihood of payment pursuant to this guarantee, and determined that the fair value of our obligation based on the likely outcome is not material.

## Note G – Debt and Receivables Securitization

The following table summarizes our long-term debt and short-term borrowings outstanding at May 31, 2016 and 2015:

|  |  |  |  |
| --- | --- | --- | --- |
| **(in thousands)** | **2016** |  | **2015** |
| Short-term borrowings | $ 2,651 |  | $ 90,550 |
| 4.55% senior notes due April 15, 2026 | 249,567 |  | 249,524 |
| 4.60% senior notes due August 10, 2024 | 150,000 |  | 150,000 |
| 6.50% senior notes due April 15, 2020 | 149,937 |  | 149,920 |
| Term loans | 31,020 |  | 30,429 |
| Other | 320 |  | 320 |
| Total debt | 583,495 |  | 670,743 |
| Less: current maturities and short-term borrowings | 3,513 |  | 91,391 |
| Total long-term debt | $579,982 |  | $579,352 |

Short-term borrowings at May 31, 2016, consisted of an aggregate of $2,651,000 outstanding under various credit facilities maintained by our consolidated affiliate, Worthington Aritas.

We maintain a $100,000,000 revolving trade accounts receivable securitization facility (the “AR Facility”) that expires in January 2018 and was available throughout fiscal 2016 and fiscal 2015. Pursuant to the terms of the AR Facility, certain of our subsidiaries sell their accounts receivable without recourse, on a revolving basis, to Worthington Receivables Corporation (“WRC”), a wholly-owned, consolidated, bankruptcy-remote subsidiary. In turn, WRC may sell without recourse, on a revolving basis, up to $100,000,000 of undivided ownership interests in this pool of accounts receivable to a multi-seller, asset-backed commercial paper conduit (the “Conduit”). Purchases by the Conduit are financed with the sale of A1/P1 commercial paper. We retain an undivided interest in this pool and are subject to risk of loss based on the collectability of the receivables from this retained interest. Because the amount eligible to be sold excludes receivables more than 90 days past due, receivables offset by an allowance for doubtful accounts due to bankruptcy or other cause, concentrations over certain limits with specific customers and certain reserve amounts, we believe additional risk of loss is minimal. The book value of the retained portion of the pool of accounts receivable approximates fair value. As of May 31, 2016, no undivided ownership interests in this pool of accounts receivable had been sold. Facility fees of $540,000, $723,000, and $652,000 were recognized within interest expense during fiscal 2016, fiscal 2015 and fiscal 2014, respectively.

We maintain a $500,000,000 multi-year revolving credit facility (the “Credit Facility”) with a group of lenders that matures in April 2020. Borrowings under the Credit Facility typically have maturities of less than one year and given that our intention has been to repay them within a year, they have been classified as short-term borrowings within current liabilities on our consolidated balance sheets. However, we can also extend the term of amounts borrowed by renewing these borrowings for the term of the Credit Facility. We have the option to borrow at rates equal to an applicable margin over the LIBOR, Prime or Fed Funds rates. The applicable margin is determined by our credit rating. There were no borrowings outstanding under the Credit Facility at May 31, 2016.

We also had letters of credit totaling $16,428,000 outstanding as of May 31, 2016. These letters of credit have been issued to third-party service providers and had no amounts drawn against them at May 31, 2016.

On September 26, 2014, our consolidated joint venture in Turkey, Worthington Aritas, executed a five- year term loan denominated in Euros. As of May 31, 2016, we had borrowed $28,445,000 against the facility. The facility bears interest at a variable rate based on EURIBOR. The applicable variable rate was 1.500% at May 31, 2016. On October 15, 2014, we entered into an interest rate swap to fix the interest rate on 60% of the borrowings outstanding under this facility at 2.015% starting on December 26, 2014 through September 26, 2019. Borrowings against the facility are being used for the construction of a new cryogenics manufacturing facility in Turkey.

On April 15, 2014, we issued $250,000,000 aggregate principal amount of unsecured senior notes due on April 15, 2026 (the “2026 Notes”). The 2026 Notes bear interest at a rate of 4.55%. The 2026 Notes were sold to the public at 99.789% of the principal amount thereof, to yield 4.573% to maturity. We used a portion of the net proceeds from the offering to repay borrowings then outstanding under our revolving credit facilities. Approximately $3,081,000, $2,256,000 and $528,000 of the aggregate proceeds were allocated to the settlement of a derivative contract entered into in anticipation of the issuance of the 2026 Notes, debt issuance costs, and the debt discount, respectively. The debt discount, debt issuance costs and the loss on the derivative contract were recorded on the consolidated balance sheet as of May 31, 2016, within long-term debt as a contra-liability, short- and long-term other assets and AOCI, respectively. Each will be recognized, through interest expense, in our consolidated statements of earnings over the term of the 2026 Notes. The unamortized portion of the debt issuance costs and debt discount was $1,867,000 and $433,000, respectively, at May 31, 2016.

On August 10, 2012, we issued $150,000,000 aggregate principal amount of unsecured senior notes due August 10, 2024 (the “2024 Notes”). The 2024 Notes bear interest at a rate of 4.60%. The net proceeds from this issuance were used to repay a portion of the then outstanding borrowings under our revolving credit facilities.

On April 27, 2012, we executed a $5,880,000 seven-year term loan that matures on May 1, 2019 and requires monthly payments of $76,350. The loan bears interest at a rate of 2.49% and is secured by an aircraft that was purchased with its proceeds. Borrowings outstanding totaled $2,575,000 as of May 31, 2016.

On April 13, 2010, we issued $150,000,000 aggregate principal amount of unsecured senior notes due on April 15, 2020 (the “2020 Notes”). The 2020 Notes bear interest at a rate of 6.50%. The 2020 Notes were sold to the public at 99.890% of the principal amount thereof, to yield 6.515% to maturity. We used the net proceeds from the offering to repay a portion of the then outstanding borrowings under our revolving credit facilities. Approximately $165,000, $1,535,000 and $1,358,000 of the aggregate proceeds were allocated to the debt discount, debt issuance costs, and the settlement of a derivative contract entered into in anticipation of the issuance of the 2020 Notes. The debt discount, debt issuance costs and the loss on the derivative contract were recorded on the consolidated balance sheets within long-term debt as a contra-liability, short- and long- term other assets and AOCI, respectively. Each will continue to be recognized, through interest expense, in our consolidated statements of earnings over the remaining term of the 2020 Notes. The unamortized portion of the debt issuance costs and debt discount was $569,000 and $63,000, respectively, at May 31, 2016.

Maturities on long-term debt and short-term borrowings in the next five fiscal years, and the remaining years thereafter, are as follows:

|  |  |  |
| --- | --- | --- |
|  | **(in thousands)** |  |
| 2017 |  | $ 3,513 |
| 2018 |  | 6,573 |
| 2019 |  | 6,518 |
| 2020 |  | 167,067 |
| 2021 |  | - |
| Thereafter |  | 400,320 |
| Total |  | $583,991 |

## Note H – Comprehensive Income (Loss)

*Other Comprehensive Income (Loss):* The following table summarizes the tax effects of each component of other comprehensive income (loss) for the fiscal years ended May 31:

## 2016 2015 2014

**(in thousands)**

**Before-**

**Tax Tax**

**Net-of- Tax**

**Before-**

**Tax Tax**

**Net-of- Tax**

**Before-**

**Tax Tax**

**Net-of- Tax**

Foreign currency translation $ 4,716 $ - $ 4,716 $(34,229) $ - $(34,229) $ 7,618 $ - $ 7,618 Pension liability adjustment (3,233) 1,175 (2,058) (5,652) 1,914 (3,738) (1,555) 511 (1,044)

Cash flow hedges 35,524 (13,316) 22,208 (18,605) 6,952 (11,653) 3,548 (1,039) 2,509

## Other comprehensive

**income (loss)** $37,007 $(12,141) $24,866 $(58,486) $8,866 $(49,620) $ 9,611 $ (528) $ 9,083

*Accumulated Other Comprehensive Loss:* The components of the changes in accumulated other comprehensive loss for the fiscal year ended May 31, 2016 were as follows:

## Foreign Currency

**Pension Liability**

**Accumulated Other**

**Cash Flow Comprehensive**

**(in thousands)**

**Translation**

**Adjustment**

**Hedges**

**Loss**

Balance as of May 31, 2015 $(20,717) $(15,003) $(14,984) $(50,704)

Other comprehensive income (loss) before

|  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- |
| reclassifications | 1,989 (3,667) |  | 7,283 |  | 5,605 |
| Reclassification adjustments to income (a) | - 434 |  | 28,241 |  | 28,675 |
| Income taxes | - 1,175 |  | (13,316) |  | (12,141) |
| Balance as of May 31, 2016 | $(18,728) $(17,061) |  | $ 7,224 |  | $(28,565) |
|  |  |  |  |  |  |

(a) The statement of earnings classification of amounts reclassified to income for cash flow hedges is disclosed in “Note P – Derivative Instruments and Hedging Activities.”

The estimated net amount of the gains in AOCI at May 31, 2016 expected to be reclassified into net earnings within the succeeding twelve months is $6,792,000 (net of tax of $4,127,000). This amount was computed using the fair value of the cash flow hedges at May 31, 2016, and will change before actual reclassification from other comprehensive income to net earnings during fiscal 2017.

## Note I – Equity

*Preferred Shares:* The Worthington Industries, Inc. Amended Articles of Incorporation authorize two classes of preferred shares and their relative voting rights. The Board of Directors of Worthington Industries, Inc. is empowered to determine the issue prices, dividend rates, amounts payable upon liquidation and other terms of the preferred shares when issued. No preferred shares are issued or outstanding.

*Common Shares*: On June 29, 2011, the Board of Worthington Industries, Inc. authorized the repurchase of up to 10,000,000 of our outstanding common shares, of which none remained available for repurchase at May 31, 2015. During fiscal 2015, 1,722,332 common shares were repurchased under this authorization.

On June 25, 2014, the Board of Worthington Industries, Inc. authorized the repurchase of up to an additional 10,000,000 of our outstanding common shares. An aggregate of 3,500,000 and 2,453,855 common shares were repurchased under this authorization during fiscal 2016 and fiscal 2015, respectively. At May 31, 2016, 4,046,145 common shares remained available for repurchase under this authorization.

During fiscal 2016 and fiscal 2015, we paid $99,847,000 and $127,360,000 to repurchase 3,500,000 and 4,176,187 of our common shares, respectively, under these authorizations.

The common shares available for repurchase under these authorizations may be purchased from time to time, with consideration given to the market price of the common shares, the nature of other investment opportunities, cash flows from operations, general economic conditions and other relevant considerations. Repurchases may be made on the open market or through privately negotiated transactions.

On October 1, 2014, the Company amended its non-qualified deferred compensation plans for employees to require that any portion of a participant’s current account credited to the theoretical common share option, which reflects the fair value of the Company’s common shares with dividends reinvested, and any new contributions credited to the theoretical common share option remain credited to the theoretical common share option until distributed. For amounts credited to the theoretical common share option, payouts are required to be made in the form of whole common shares of the Company and cash in lieu of fractional shares. As a result, we account for the deferred compensation obligation credited to the theoretical

common share option within equity, which totaled $960,000 and $14,560,000 for fiscal 2016 and fiscal 2015, respectively. Prior to October 1, 2014, participant accounts credited to the theoretical common share option were settled in cash and classified as a liability in the Company’s consolidated balance sheet.

## Note J – Stock-Based Compensation

Under our employee and non-employee director stock-based compensation plans (the “Plans”), we may grant incentive or non-qualified stock options, restricted common shares and performance shares to employees and non-qualified stock options and restricted common shares to non-employee directors. We classify share-based compensation expense within SG&A expense to correspond with the same financial statement caption as the majority of the cash compensation paid to employees. A total of 4,886,393 of our common shares were authorized and available for issuance in connection with the stock-based compensation plans in place at May 31, 2016.

We recognized pre-tax stock-based compensation expense of $15,836,000 ($10,056,000 after-tax),

$17,916,000 ($11,500,000 after-tax), and $22,017,000 ($13,778,000 after-tax) under the Plans during fiscal 2016, fiscal 2015 and fiscal 2014, respectively. At May 31, 2016, the total unrecognized compensation cost related to non-vested awards was $9,963,000, which will be expensed over the next three fiscal years.

## Non-Qualified Stock Options

Stock options may be granted to purchase common shares at not less than 100% of fair market value on the date of the grant. All outstanding stock options are non-qualified stock options. The exercise price of all stock options granted has been set at 100% of the fair market value of the underlying common shares on the date of grant. Generally, stock options granted to employees vest and become exercisable at the rate of (i) 20% per year for options issued before June 30, 2011, and (ii) 33% per year for options issued on or after June 30, 2011, in each case beginning one year from the date of grant, and expire ten years after the date of grant. Non-qualified stock options granted to non-employee directors vest and become exercisable on the earlier of (a) the first anniversary of the date of grant or (b) the date on which the next annual meeting of shareholders is held following the date of grant for any stock option granted as of the date of an annual meeting of shareholders of Worthington Industries, Inc. Stock options can be exercised through net- settlement, at the election of the option holder.

U.S. GAAP requires that all share-based awards be recorded as expense in the statement of earnings based on their grant-date fair value. We calculate the fair value of our non-qualified stock options using the Black- Scholes option pricing model and certain assumptions. The computation of fair values for all stock options incorporates the following assumptions: expected volatility (based on the historical volatility of our common shares); risk-free interest rate (based on the United States Treasury strip rate for the expected term of the stock options); expected term (based on historical exercise experience); and dividend yield (based on annualized current dividends and an average quoted price of our common shares over the preceding annual period).

The table below sets forth the non-qualified stock options granted during each of the last three fiscal years. For each grant, the exercise price was equal to the closing market price of the underlying common shares at each respective grant date. The fair values of these stock options were based on the Black-Scholes option pricing model, calculated at the respective grant dates. The calculated pre-tax stock-based compensation expense for these stock options, which is after an estimate of forfeitures, will be recognized on a straight-line basis over the respective vesting periods of the stock options.

|  |  |  |  |  |
| --- | --- | --- | --- | --- |
| **2016** |  | **2015** |  | **2014** |
| **(in thousands, except per share amounts)** |  |  |  |  |
| Granted | 154 | 97 | 130 |
| Weighted average exercise price, per share | $30.92 | $42.95 | $32.21 |
| Weighted average grant date fair value, per share | $ 9.55 | $17.96 | $12.92 |
| Pre-tax stock-based compensation | $1,305 | $1,553 | $1,539 |

The weighted average fair value of stock options granted in fiscal 2016, fiscal 2015 and fiscal 2014 was based on the Black-Scholes option pricing model with the following weighted average assumptions:

|  |  |  |  |
| --- | --- | --- | --- |
|  | **2016** | **2015** | **2014** |
| Assumptions used: |  |  |  |
| Dividend yield | 2.33% | 1.88% | 2.28% |
| Expected volatility | 38.40% | 50.92% | 52.23% |
| Risk-free interest rate | 1.98% | 1.88% | 1.69% |
| Expected life (years) | 6.0 | 6.0 | 6.0 |

The following tables summarize our stock option activity for the years ended May 31:

## 2016 2015 2014

|  |  |  |  |  |  |  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- | --- |
| **(in thousands, except per share)** | **Stock Options** |  | **Weighted Average Exercise Price** |  | **Stock Options** |  | **Weighted Average Exercise Price** |  | **Stock Options** |  | **Weighted Average Exercise Price** |
| Outstanding, beginning of year | 4,044 |  | $18.25 |  | 4,752 |  | $17.58 |  | 5,517 |  | $17.19 |
| Granted | 154 |  | 30.92 |  | 97 |  | 42.95 |  | 130 |  | 32.21 |
| Exercised | (874) |  | 17.22 |  | (758) |  | 17.24 |  | (828) |  | 17.39 |
| Forfeited | (18) |  | 32.25 |  | (47) |  | 17.00 |  | (67) |  | 16.13 |
| Outstanding, end of year | 3,306 |  | 19.01 |  | 4,044 |  | 18.25 |  | 4,752 |  | 17.58 |
| Exercisable at end of year | 3,059 |  | 17.85 |  | 3,276 |  | 17.63 |  | 2,996 |  | 17.57 |

|  |  |  |
| --- | --- | --- |
|  | **Weighted** |  |
| **Average** |
| **Remaining** |
|  | **Number of** |  | **Contractual** |  | **Aggregate** |
|  | **Stock Options** |  | **Life** |  | **Intrinsic Value** |
|  | **(in thousands)** |  | **(in years)** |  | **(in thousands)** |
| **May 31, 2016**Outstanding | 3,306 |  | 4.33 |  | $ 61,178 |
| Exercisable**May 31, 2015**Outstanding | 3,0594,044 |  | 4.014.82 |  | 60,082$ 38,277 |
| Exercisable**May 31, 2014**Outstanding | 3,2764,752 |  | 4.425.50 |  | 31,625$107,970 |
| Exercisable | 2,996 |  | 4.67 |  | 68,108 |

During fiscal 2016, the total intrinsic value of stock options exercised was $9,084,000. The total amount of cash received from the exercise of stock options during fiscal 2016 was $7,893,000, and the related excess tax benefit realized from share-based payment awards was $3,178,000.