

EBIX INC  
Form 10-Q  
May 10, 2012  
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UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION  
Washington, D.C. 20549  
FORM 10-Q

R QUARTERLY REPORT UNDER SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE  
ACT OF 1934  
For the quarterly period ended March 31, 2012

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

Commission file number 0-15946  
Ebix, Inc.  
(Exact name of registrant as specified in its charter)

DELAWARE 77-0021975  
(State or other jurisdiction of incorporation or (I.R.S. Employer Identification No.)  
organization)

5 CONCOURSE PARKWAY, SUITE 3200  
ATLANTA, GEORGIA 30328  
(Address of principal executive offices) (Zip Code)

Registrant's telephone number, including area code: 678-281-2020  
Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes R No o  
Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes R No o N/A o

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, or a non-accelerated filer.  
Large accelerated filer o Accelerated filer R Non-accelerated filer o Smaller reporting company  
(Do not check if a smaller reporting company) o

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

As of May 10, 2012, the number of shares of common stock outstanding was 36,471,081.

FORM 10-Q  
FOR THE QUARTER ENDED MARCH 31, 2012  
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## PART I — FINANCIAL INFORMATION

## Item 1: CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

Ebix, Inc. and Subsidiaries

Condensed Consolidated Statements of Income

(In thousands, except per share data)

(Unaudited)

	Three Months Ended March 31,	
	2012	2011
Operating revenue	\$43,827	\$40,050
Operating expenses:		
Cost of services provided	9,029	7,307
Product development	4,272	4,619
Sales and marketing	3,812	2,852
General and administrative	6,444	7,761
Amortization and depreciation	1,941	1,877
Total operating expenses	25,498	24,416
Operating income	18,329	15,634
Interest income	167	200
Interest expense	(253)	(215)
Other non-operating income (loss)	—	(354)
Foreign currency exchange gain (loss)	(296)	1,468
Income before income taxes	17,947	16,733
Income tax expense	(2,262)	(1,569)
Net income	\$15,685	\$15,164
Basic earnings per common share	\$0.43	\$0.40
Diluted earnings per common share	\$0.40	\$0.37
Basic weighted average shares outstanding	36,450	38,151
Diluted weighted average shares outstanding	39,523	38,154

See accompanying notes to the condensed consolidated financial statements.

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Ebix, Inc. and Subsidiaries  
 Condensed Consolidated Statements of Comprehensive Income  
 (In thousands)  
 (Unaudited)

	Three Months Ended March 31,	
	2012	2011
Net income	\$ 15,685	\$ 15,164
Other comprehensive income (loss):		
Foreign currency translation adjustments	4,327	2,053
Total other comprehensive income	4,327	2,053
Comprehensive income	\$ 20,012	\$ 17,217

See accompanying notes to the condensed consolidated financial statements.

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## Ebix, Inc. and Subsidiaries

## Condensed Consolidated Balance Sheets

(In thousands, except share amounts)

	March 31, 2012 (Unaudited)	December 31, 2011
<b>ASSETS</b>		
Current assets:		
Cash and cash equivalents	\$37,140	\$23,696
Short-term investments	730	1,505
Trade accounts receivable, less allowances of \$1,221 and \$1,719, respectively	29,351	31,133
Deferred tax asset, net	2,817	2,981
Other current assets	4,747	4,502
Total current assets	74,785	63,817
Property and equipment, net	9,399	8,834
Goodwill	264,504	259,218
Intangibles, net	37,763	38,386
Indefinite-lived intangibles	30,990	30,453
Deferred tax asset, net	10,970	9,412
Other assets	1,053	1,062
Total assets	\$429,464	\$411,182
<b>LIABILITIES AND STOCKHOLDERS' EQUITY</b>		
Current liabilities:		
Accounts payable and accrued liabilities	\$19,075	\$18,719
Accrued payroll and related benefits	3,518	5,034
Short term debt	8,333	6,667
Current portion of long term debt and capital lease obligations, net of discount of \$64 and \$0, respectively	852	165
Deferred revenue	16,211	16,460
Current deferred rent	279	266
Other current liabilities	119	2,468
Total current liabilities	48,387	49,779
Revolving line of credit	31,750	31,750
Long term debt and capital lease obligations, less current portion, net of discount of \$128 and \$0, respectively	9,367	8,468
Other liabilities	3,775	3,803
Deferred revenue	69	328
Long term deferred rent	864	939
Total liabilities	94,212	95,067
Commitments and Contingencies, Note 5		
Stockholders' equity:		
Preferred stock, \$0.10 par value, 500,000 shares authorized, no shares issued and outstanding at March 31, 2012 and December 31, 2011	—	—
Common stock, \$0.10 par value, 60,000,000 shares authorized, 36,495,652 issued and 36,455,143 outstanding at March 31, 2012 and 36,418,385 issued and 36,377,876	3,646	3,638

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outstanding at December 31, 2011		
Additional paid-in capital	180,099	179,518
Treasury stock (40,509 shares as of March 31, 2012 and December 31, 2011)	(76	) (76 )
Retained earnings	151,780	137,559
Accumulated other comprehensive income	(197	) (4,524 )
Total stockholders' equity	335,252	316,115
Total liabilities and stockholders' equity	\$429,464	\$411,182
See accompanying notes to the condensed consolidated financial statements.		

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Ebix, Inc. and Subsidiaries  
Condensed Consolidated Statements Stockholders' Equity  
(unaudited)  
(In thousands, except share amounts)

	Common Stock					Retained Earnings	Accumulated Other Comprehensive Income	Total
	Issued Shares	Amount	Treasury Stock Shares	Treasury Stock Amount	Additional Paid-in Capital			
Balance, December 31, 2011	36,418,385	\$3,638	(40,509)	\$(76 )	\$179,518	\$137,559	\$ (4,524 )	\$316,115
Net income	—	—	—	—	—	15,685	—	15,685
Cumulative translation adjustment	—	—	—	—	—	—	4,327	4,327
Vesting of restricted stock	44,267	4	—	—	(4 )	—	—	—
Exercise of stock options	33,000	4	—	—	10	—	—	14
Deferred compensation and amortization related to options and restricted stock	—	—	—	—	548	—	—	548
APIC adjustment for stock options	—	—	—	—	27	—	—	27
Dividends paid	—	—	—	—	—	(1,464 )	—	(1,464 )
Balance, March 31, 2012	36,495,652	\$3,646	(40,509)	\$(76 )	\$180,099	\$151,780	\$ (197 )	\$335,252

See accompanying notes to the condensed consolidated financial statements.



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## Ebix, Inc. and Subsidiaries

## Condensed Consolidated Statements of Cash Flows

(In thousands)

(Unaudited)

	Three Months Ended March 31,	
	2012	2011
Cash flows from operating activities:		
Net income	\$15,685	\$15,164
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	1,941	1,877
Share based compensation	548	556
Provision for doubtful accounts	266	11
Benefit (provision) for deferred taxes	(1,401)	2,198
Debt discount amortization on convertible debt	—	21
Unrealized foreign exchange (gain) loss on forward contracts	—	(152)
Unrealized foreign exchange (gain) loss	661	(1,890)
(Gain) loss on put option	—	354
Changes in assets and liabilities, net of effects from acquisitions:		
Accounts receivable	1,771	(5,987)
Other assets	(302)	1,278
Accounts payable and accrued expenses	(861)	(2,357)
Accrued payroll and related benefits	(1,575)	(1,463)
Deferred revenue	(560)	689
Deferred rent	(75)	(55)
Other current liabilities	(2,336)	69
Net cash provided by operating activities	13,762	10,313
Cash flows from investing activities:		
Acquisition of ADAM, net of cash acquired	—	3,529
Maturities of marketable securities	979	7,960
Purchases of marketable securities	—	(5,384)
Capital expenditures	(673)	(524)
Net cash provided by investing activities	306	5,581
Cash flows from financing activities:		
Principal payments of term loan obligation	—	(1,407)
Repurchases of common stock	—	(2,395)
Proceeds from the exercise of stock options	14	1
Dividend payments	(1,464)	—
Payments of capital lease obligations	(45)	(102)
Net cash used in financing activities	(1,495)	(3,903)
Effect of foreign exchange rates on cash	871	201
Net change in cash and cash equivalents	13,444	12,192
Cash and cash equivalents at the beginning of the period	23,696	23,397
Cash and cash equivalents at the end of the period	\$37,140	\$35,589
Supplemental disclosures of cash flow information:		
Interest paid	\$312	\$204
Income taxes paid	\$3,030	\$558

See accompanying notes to the condensed consolidated financial statements.

Supplemental schedule of noncash financing activities:

Effective February 7, 2011, Ebix acquired ADAM for aggregate consideration in the approximate amount of \$88.4 million. Under the terms of the merger agreement, ADAM shareholders received, at a fixed exchange ratio, 0.3122 shares of Ebix common stock for every share of ADAM common stock. Ebix issued approximately 3.65 million shares of Ebix common stock with a fair value of \$87.5 million as part of the purchase consideration.

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Ebix, Inc. and Subsidiaries

Notes to Condensed Consolidated Financial Statements

## Note 1: Description of Business and Summary of Significant Accounting Policies

Description of Business—Ebix, Inc. and subsidiaries (“Ebix” or the “Company”) is an international supplier of on-demand software and e-commerce solutions to the insurance industry. Ebix provides various application software products for the insurance industry ranging from data exchanges, carrier systems, and agency systems, to custom software development for business entities across the insurance and financial industries. The Company's products feature fully customizable and scalable on-demand software designed to streamline the way insurance professionals manage distribution, marketing, sales, customer service, and accounting activities. The Company has its headquarters in Atlanta, Georgia and also conducts operating activities Australia, Canada, China, India, Japan, New Zealand, Singapore, and Brazil. International revenue accounted for 30.4% and 30.3% of the Company’s total revenue for the three months ended March 31, 2012 and 2011, respectively.

The Company’s revenues are derived from four product/service groups. Presented in the table below is the breakout of our revenue streams for each of those product/service groups for the three months ended March 31, 2012 and 2011.

(dollar amounts in thousands)	Three Months Ended	
	March 31,	
	2012	2011
Exchanges	\$34,646	\$31,065
Broker Systems	4,754	3,842
Business Process Outsourcing (“BPO”)	3,571	3,619
Carrier Systems	856	1,524
Totals	\$43,827	\$40,050

## Summary of Significant Accounting Policies

Basis of Presentation—The accompanying unaudited condensed consolidated financial statements and these notes have been prepared pursuant to the rules and regulations of the Securities and Exchange Commission (the "SEC") and in accordance with U.S. generally accepted accounting principles with the effect of inter-company balances and transactions eliminated. Certain information and note disclosures normally included in annual financial statements prepared in accordance with generally accepted accounting principles (“GAAP”) have been condensed or omitted pursuant to the SEC’s rules and regulations, although the Company believes that the disclosures made are adequate to make the information not misleading. In the opinion of management these unaudited condensed consolidated financial statements contain adjustments (consisting only of normal recurring items) necessary to fairly present the consolidated financial position of the Company and its consolidated results of operations and cash flows. Operating results for the three months ended March 31, 2012 are not necessarily indicative of the results that may be expected for the full year. The condensed consolidated December 31, 2011 balance sheet included in this interim period filing has been derived from the audited financial statements at that date but does not include all of the information and related notes required by GAAP for complete financial statements. These condensed interim financial statements should be read in conjunction with the financial statements and notes thereto included in the Company’s Annual Report on Form 10-K for the year ended December 31, 2011.

Fair Value of Financial Instruments—The Company believes the carrying amount of cash and cash equivalents, short-term investments, accounts receivable, accounts payable, accrued expenses, accrued payroll and related benefits, line of credit, long-term debt obligations, and capital lease obligations is a reasonable estimate of their fair value due to the short remaining maturity of these items and/or their fluctuating interest rates.

Revenue Recognition—The Company derives its revenues primarily from subscription and transaction fees pertaining to services delivered over our exchanges or from our ASP platforms, fees for business process outsourcing services, and fees for software development projects including associated fees for consulting, implementation, training, and project

management provided to customers with installed systems. Sales and value-added taxes are not included in revenues, but rather are recorded as a liability until the taxes assessed are remitted to the respective taxing authorities. In accordance with Financial Accounting Standard Board (“FASB”) and the SEC's accounting guidance on revenue recognition, the Company considers revenue earned and realizable when: (a) persuasive evidence of the sales arrangement exists, provided that the arrangement fee is fixed or determinable, (b) delivery or performance has occurred, (c) customer acceptance has been received, if contractually required, and (d) collectability of the arrangement fee is probable. The Company uses signed contractual agreements as persuasive evidence of a sales arrangement. We apply the provisions of the relevant generally accepted

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accounting principles related to all transactions involving the license of software where the software deliverables are considered more than inconsequential to the other elements in the arrangement.

For contracts that contain multiple deliverables, we analyze the revenue arrangements in accordance with the relevant technical accounting guidance, which provides criteria governing how to determine whether goods or services that are delivered separately in a bundled sales arrangement should be considered separate units of accounting for the purpose of revenue recognition. Generally these types of arrangements include deliverables pertaining to software licenses, system set-up, and professional services associated with product customization or modification. Delivery of the various contractual elements typically occurs over periods of less than eighteen months. These arrangements generally do not have refund provisions or have very limited refund terms.

Software development arrangements involving significant customization, modification or production are accounted for in accordance with the appropriate technical accounting guidance issued by FASB using the percentage-of-completion method. The Company recognizes revenue using periodic reported actual hours worked as a percentage of total expected hours required to complete the project arrangement and applies the percentage to the total arrangement fee.

Accounts Receivable and the Allowance for Doubtful Accounts Receivable—Reported accounts receivable as of March 31, 2012 include \$23.3 million of trade receivables stated at invoice billed amounts net of the estimated allowance for doubtful accounts receivable, and \$6.1 million of unbilled receivables. Approximately \$7.5 million of deferred revenue is included in accounts receivable at March 31, 2012. Bad debt expense incurred during the three month periods ended March 31, 2012 and March 31, 2011 was approximately \$266 thousand, and \$11 thousand, respectively. Accounts receivable are written off against the allowance account when the Company has exhausted all reasonable collection efforts.

Goodwill and Other Indefinite-Lived Intangible Assets—Goodwill represents the cost in excess of the fair value of the net assets of acquired businesses. Indefinite-lived intangible assets represent the fair value of acquired contractual customer relationships for which future cash flows are expected to continue indefinitely. In accordance with the relevant FASB accounting guidance, goodwill and indefinite-lived intangible assets are not amortized but are tested for impairment at the reporting unit level on an annual basis or on an interim basis if an event occurs or circumstances change that would likely have reduced the fair value of a reporting unit below its carrying value. Potential impairment indicators include a significant change in the business climate, legal factors, operating performance indicators, competition, and the sale or disposition of a significant portion of the business. The impairment evaluation process involves an assessment of certain qualitative factors to determine whether the existence of events or circumstances would indicate that it is more likely than not that the fair value of any of our reporting units was less than their than its carrying amount. If after assessing the totality of events or circumstances, we were to determine that it is not more likely than not that the fair value of a reporting unit is less than its carrying amount, then we would not perform the two-step quantitative impairment testing described further below.

The aforementioned two-step quantitative testing process involves comparing the reporting unit carrying values to their respective fair values; we determine fair value of our reporting units by applying the discounted cash flow method using the present value of future estimated net cash flows. If the fair value of a reporting unit exceeds its carrying value, then no further testing is required. However, if a reporting unit's fair value were to be less than its carrying value, we would then determine the amount of the impairment charge, if any, which would be the amount that the carrying value of the reporting unit's goodwill exceeded its implied value. Projections of cash flows are based on our views of growth rates, operating costs, anticipated future economic conditions and the appropriate discount rates relative to risk and estimates of residual values. We believe that our estimates are consistent with assumptions that marketplace participants would use in their estimates of fair value. The use of different estimates or assumptions for our projected discounted cash flows (e.g., growth rates, future economic conditions, discount rates and estimates of terminal values) when determining the fair value of our reporting units could result in different values and may result in a goodwill impairment charge. We perform our annual goodwill impairment evaluation and testing as of September 30th of each year. During the year ended December 31, 2011 we had no impairment of our reporting unit goodwill balances.

Changes in the carrying amount of goodwill for the three months ended March 31, 2012 are as follows:

	(In thousands)
Beginning Balance (December 31, 2011)	\$259,218
Additions, net (see Note 3)	3,486
Foreign currency translation adjustments	1,800
Ending Balance (March 31, 2012)	\$264,504
Finite-lived Intangible Assets—Purchased intangible assets represent the estimated acquisition date fair value of customer	

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relationships, developed technology, trademarks and non-compete agreements obtained in connection with the businesses we acquire. We amortize these intangible assets on a straight-line basis over their estimated useful lives, as follows:

Category	Life (yrs)
Customer relationships	7-15
Developed technology	3-20
Trademarks	3-15
Non-compete agreements	5
Database	10

The carrying value of finite-lived and indefinite-lived intangible assets at March 31, 2012 and December 31, 2011 are as follows:

	March 31, 2012	December 31, 2011
	(In thousands)	
Finite-lived intangible assets:		
Customer relationships	\$40,739	\$40,289
Developed technology	11,836	11,640
Trademarks	2,188	2,188
Non-compete agreements	418	418
Backlog	140	140
Database	213	207
Total intangibles	55,534	54,882
Accumulated amortization	(17,771)	(16,496)
Finite-lived intangibles, net	\$37,763	\$38,386
Indefinite-lived intangibles:		
Customer/territorial relationships	\$30,990	\$30,453

## Indefinite-lived intangibles:

Customer/territorial relationships

\$30,990      \$30,453

Amortization expense recognized in connection with acquired intangible assets was \$1.2 million and \$1.2 million for the three months ended March 31, 2012 and March 31, 2011, respectively.

**Income Taxes—Deferred income taxes** are recorded to reflect the estimated future tax effects of differences between the financial statement and tax basis of assets, liabilities, operating loss and tax credit carry forwards using the tax rates expected to be in effect when the temporary differences reverse. Valuation allowances, if any, are recorded to reduce deferred tax assets to the amount management considers more likely than not to be realized. Such valuation allowances are recorded for the portion of the deferred tax assets that are not expected to be realized based on the levels of historical taxable income and projections for future taxable income over the periods in which the temporary differences will be deductible.

The Company also applies FASB accounting guidance on accounting for uncertainty in income taxes positions. This guidance clarifies the accounting for uncertainty in income taxes by prescribing the minimum recognition threshold a tax position is required to meet before being recognized in the financial statements. In this regard we recognize the tax benefit from uncertain tax positions only if it is more likely than not that the tax position will be sustained on examination by the taxing authorities, based on the technical merits of the position.

**Recent Relevant Accounting Pronouncements—**The following is a brief discussion of recently released accounting pronouncements that are pertinent to the Company's business:

In June 2011, the Financial Accounting Standards Board ("FASB") issued new financial reporting guidance regarding the reporting of "other comprehensive income, or (OCI)". This guidance revises the manner in which entities present comprehensive income in their financial statements. The new guidance requires entities to report components of

comprehensive income in either (1) a continuous statement of comprehensive income, or (2) two separate but consecutive statements. Under the two-statement approach, the first statement would include components of net income, which is consistent with the income statement format used



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currently, and the second statement would include components of OCI. Under either method, entities must display adjustments for items that are reclassified from OCI to net income in both net income and OCI. The new reporting guidance does not change the items that must be reported in OCI. This new reporting standard is effective for interim and annual periods beginning after December 15, 2011. After adoption, the guidance must be applied retrospectively for all periods presented in the financial statements. The Company adopted this new guidance during the first quarter of 2012.

In September 2011, the FASB issued new technical guidance regarding an entity's evaluation of goodwill for possible impairment. Under this new guidance an entity has the option to first assess qualitative factors to determine whether the existence of events or circumstances leads to a determination that it is more likely than not that the fair value of a reporting unit is less than its carrying amount. If after assessing the totality of events or circumstances, an entity determines that it is not more likely than not that the fair value of a reporting unit is less than its carrying amount, then performing the two-step quantitative impairment test is unnecessary. This new technical guidance was effective for fiscal years beginning after December 15, 2011. Early adoption was permitted for annual and interim goodwill impairment evaluations performed as of a date before September 2011, if an entity's financial statements for the most recent annual or interim period have not yet been issued. The Company elected to adopt this technical guidance early and accordingly applied it to the 2011 annual impairment evaluation of goodwill.

In December 2010, the Emerging Issues Task Force of the FASB reached consensus regarding the disclosure of pro forma information for business combinations. This new guidance addressed the diversity in practice concerning the interpretation of the pro forma revenue and earnings disclosure requirements for business combinations. The guidance specifies that if a public entity presents comparative financial statements, the entity should disclose revenue and earnings of the combined entity as though the business combination had occurred as of the beginning of the comparable prior annual reporting period only. The amendments also expand the supplemental pro forma disclosures to include a description of the nature and amount of material, nonrecurring pro forma adjustments directly attributable to the business combination included in the reported pro forma revenue and earnings. The amendments affect any public entity that enters into business combinations that are material on an individual or aggregate basis. The new guidance was applicable to business combinations for which the acquisition date is on or after the first annual reporting period beginning on or after December 15, 2010. The Company adopted this new guidance in 2011.

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## Note 2: Earnings per Share

A reconciliation between basic and diluted earnings per share is as follows (in thousands, except per share data):

	Three Months Ended	
	March 31,	
	2012	2011
	(In thousands, except per share data)	
Net income for basic and diluted earnings per share	\$15,685	\$15,164
Basic weighted average shares outstanding	36,450	38,151
Dilutive effect of stock options and restricted stock awards	3,073	3,366
Diluted weighted average shares outstanding	39,523	41,517
Basic earnings per common share	\$0.43	\$0.40
Diluted earnings per common share	\$0.40	\$0.37

## Note 3: Business Combinations

The Company executes accretive business acquisitions in combination with organic growth initiatives as part of its comprehensive business growth and expansion strategy. The Company' looks to acquire businesses that are complementary to Ebix's existing products and services. During the first quarter of 2012 the Company did not execute any material business acquisitions.

Consideration paid by the Company for the businesses it purchases is allocated to the assets and liabilities acquired based upon their estimated fair values as of the date of the acquisition. The excess of the purchase price over the estimated fair values of assets acquired and liabilities assumed is recorded as goodwill. Recognized goodwill pertains to the value of the expected synergies to be derived from combining the operations of the businesses we acquire including the value of the acquired workforce.

During the first quarter of 2012 the Company received a termination fee in connection with a failed business acquisition. In this regard the Company recorded a reduction to general and administrative expense in the approximate amount of \$971 thousand (net of significant directly related internal operating costs incurred by the Company and a portion of the fee that had to be paid to our investment banker).

## Note 4: Debt with Commercial Bank

On April 20, 2011 the Company entered into a seventh amendment to a credit agreement (the "Seventh Amendment") with Bank of America, N.A. ("BOA"), as administrative agent, which materially amended the initial credit agreement dated February 12, 2010. The Seventh Amendment increased the existing revolving credit facility from \$25 million to \$35 million with its term ending on April 20, 2014, and the \$10 million secured term loan was increased to \$20 million and amortizes over a three year period with quarterly principal and interest payments that commenced on June 30, 2011. The entire credit facility has a variable interest rate currently set at LIBOR plus 1.50%. The Company deferred the origination costs in connection with this expanded and amended credit facility, and amortizes these costs into interest expense over the three-year life of the credit agreement. As of March 31, 2012 the Company's Condensed Consolidated Balance Sheet includes \$143 thousand of remaining deferred financing costs. The revolving credit facility is used by the Company to fund working capital requirements primarily in support of current operations, organic growth, and accretive business acquisitions. The underlying financing agreement contains financial covenants regarding the Company's annualized EBITDA, fixed charge coverage ratio, and leverage ratio, as well as certain restrictive covenants pertaining to such matters as the incurrence of new debt, the aggregate amount of repurchases of the Company's equity shares, and the consummation of new business acquisitions. The Company currently is in compliance with all such financial and restrictive covenants, and there have been no violations thereof or in the event

of noncompliance, appropriate waivers having been obtained.

At March 31, 2012, the outstanding balance on the revolving line of credit was \$31.8 million and the facility carried an

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interest rate of 1.75%. This balance is included in the long-term liabilities section of the Condensed Consolidated Balance Sheets. During the three month period ending March 31, 2012, both the average and maximum outstanding balances on the revolving line of credit was \$31.8 million.

At March 31, 2012, the outstanding balance on the term loan was \$15 million of which \$8.3 million is due within the next twelve months. This term loan also carried an interest rate of 1.75%. During the three months ended March 31, 2012, no payments were made against the term loan. The current and long-term portions of the term loan are included in the respective current and long-term sections of the Condensed Consolidated Balance Sheets.

Refer to Note 9 "Subsequent Events" in regards the termination of this credit facility with BOA, and the entering into of a new secured syndicated credit facility with Citibank N.A..

#### Note 5: Commitments and Contingencies

Contingencies—Between July 14, 2011 and July 21, 2011, securities class action complaints were filed against the Company and certain of its officers in the United States District Court for the Southern District of New York and in the United States District Court for the Northern District of Georgia. The complaints assert claims against (i) the Company and the Company's CEO and CFO for alleged violations of Section 10(b) of the Securities Exchange Act of 1934 (the "Exchange Act") and Rule 10b-5 promulgated thereunder and (ii) the Company's CEO and CFO as alleged controlling persons. The complaints generally allege false statements in earnings reports, SEC filings, press releases, and other public statements that allegedly caused the Company's stock to trade at artificially inflated prices. Plaintiff seeks an unspecified amount of damages. The New York action has been transferred to Georgia and has been consolidated with the Georgia action, now styled In re: Ebix, Inc. Securities Litigation, Civil Action No.

1:11-CV-02400-RSW (N.D. Ga.). In September 2011, a related derivative complaint was filed against the Company and each of its Directors in the Superior Court of Fulton County, Georgia, styled Nauman v. Raina, et al., Civil Action File No. 2011-cv-205276. The derivative action has been stayed pending resolution of the Defendants' Motion to Dismiss in the federal action. A Consolidated Amended Complaint ("CAC") was filed by Plaintiffs on November 28, 2011, in the federal action. On January 12, 2012, the Company filed a Motion to Dismiss the CAC, which raises various defenses that the CAC fails to state a claim. Plaintiffs filed their Response on February 23, 2012. On March 26, 2012 the Company filed a Reply Memorandum in Further Support of the Motion to Dismiss. The Company believes that the complaints are legally insufficient, and we intend to seek dismissal.

In the normal course of business, the Company is involved in various other claims and legal actions arising in the ordinary course of business. In the opinion of management, the ultimate likely disposition of these matters will not have a material adverse effect on the Company's business, consolidated financial position, results of operations or liquidity.

Lease Commitments—The Company leases office space under non-cancelable operating leases with expiration dates ranging through 2019, with various renewal options. Capital leases range from three to five years and are primarily for computer equipment. There were multiple assets under various individual capital leases at March 31, 2012 and 2011. Rental expense for office facilities and certain equipment subject to operating leases for the three months ended March 31, 2012 and 2011 was \$1.3 million and \$963 thousand, respectively.

Self Insurance—For most of the Company's U.S. employees the Company is currently self-insured for its health insurance program and has a stop loss policy that limits the individual liability to \$100 thousand per person and the aggregate liability to 125% of the expected claims based upon the number of participants and historical claims. As of March 31, 2012, the amount accrued on the Company's Condensed Consolidated Balance Sheet for the self-insured component of the Company's employee health insurance was \$384 thousand. The maximum potential estimated cumulative liability for the annual contract period, which ends in September 2012, is \$2.5 million.

#### Note 6: Income Taxes

The Company's consolidated world-wide effective tax rate reflects the tax benefits of conducting operating activities in certain foreign jurisdictions where earnings are taxed at rates lower than U.S. statutory rates and where certain components of the Company's income are exempt from taxation. Furthermore, the Company's world-wide product development operations and intellectual property ownership has been centralized into our India and Singapore

subsidiaries, respectively. Our operations in India benefit from a tax holiday which will continue through 2015; as such local India taxable income, other than passive interest and rental income, is not taxed. After the tax holiday expires taxable income generated by our India operations will be taxed at 50% of the normal 33.99% corporate tax rate for a period of five years. The Company also has a relatively low income tax rate in Singapore in which our operations are taxed at a 10% marginal tax rate as a result of concessions granted by the local Singapore Economic Development Board for the benefit of in-country intellectual property owners. The concessionary 10% income tax rate will expire after 2015, at which time our Singapore operations will be subject to the prevailing corporate tax rate in Singapore,

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which is currently 17%, unless the Company reaches a subsequent agreement to extend the incentive period and the then applicable concessionary rate.

The Company recognized income tax expense of \$2.3 million for the three months ended March 31, 2012. The Company's interim period income tax provisions are based on an estimate of the effective income tax rate expected to be applicable to the corresponding annual period, after eliminating discrete items unique to the respective interim period being reported. The calculated estimated annual effective tax rate used by the Company to determine the interim income tax provision for the first quarter of 2012 was 12.52% as compared to 9.38% for the same period in 2011. The effective rate increased primarily due to increased taxable income from jurisdictions with higher tax rates. At March 31, 2012, the Company had remaining available domestic net operating loss ("NOL") carry-forwards of approximately \$56.0 million which are available to offset future federal and certain state income taxes. The Company expects to fully utilize these NOLs before they begin to expire in 2020.

Accounting for Uncertainty in Income Taxes—The Company has applied the FASB's accounting guidance on accounting for uncertain income tax positions. As of March 31, 2012 the Company's Condensed Consolidated Balance Sheet includes a liability of \$3.18 million for unrecognized tax benefits which is included in other long-term liabilities. During the three months ended March 31, 2012 there were no changes to this liability. A reconciliation of the beginning and ending amount of the Company's liability reserves for unrecognized tax benefits is as follows:

	(in thousands)
Balance at January 1, 2012	\$3,180
Additions for tax positions related to current year	\$—
Additions for tax positions of prior years	\$—
Reductions for tax position of prior years	\$—
Balance at March 31, 2012	\$3,180

The Company recognizes interest accrued and penalties related to unrecognized tax benefits as part of income tax expense. As of March 31, 2012 approximately \$754 thousand of estimated interest and penalties is included in other long-term liabilities in the accompanying Condensed Consolidated Balance Sheet.

Based on its current knowledge and the probability assessment of potential outcomes, the Company believes that recorded tax reserves, as determined in accordance with the requisite income tax guidance, are adequate.

#### Note 7: Derivative Instruments

The Company uses derivative instruments that are not designated as hedges under FASB accounting guidance related to the accounting for derivative instruments and hedging activity, to hedge the fluctuations in foreign exchange rates for recognized balance sheet items, primarily intercompany receivables. As of March 31, 2012, all of the Company's pre-existing foreign currency hedge contracts have matured. The inputs used in the valuation of the hedge contracts included the USD/INR foreign currency exchange spot rates in effect at the inception date of the contract, forward premiums, forward foreign currency exchange rates, term, and contract maturity date.

The intended purpose of these hedging instruments was to offset the income statement impact of recorded foreign exchange transaction gains and losses resulting from U.S. dollar denominated intercompany invoices issued by our Indian subsidiary whose functional currency is the Indian rupee. The change in the fair value of these derivatives was recorded in foreign currency exchange gains (losses) in the Condensed Consolidated Statements of Income and was \$1.2 million and \$25 thousand for the three months ended March 31, 2012 and 2011, respectively. These reported gains are in addition to the consolidated foreign exchange gains (losses) equivalent to \$(1.5) million and \$1.5 million recorded during the three months ended March 31, 2012 and 2011, respectively, incurred by our subsidiaries for settlement of transactions denominated in other than their functional currency. The Company classifies its foreign currency hedges, for which the fair value is remeasured on a recurring basis at each reporting date, as a Level 2 instrument (i.e. wherein fair value is determined and based on observable inputs other than quoted market prices), which we believe is the most appropriate level within the fair value hierarchy based on the inputs used to determine its the fair value at the measurement date.



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## Note 8: Geographic Information

The Company operates with one reportable segment whose results are regularly reviewed by the Company's chief operating decision maker as to performance and allocation of resources. The following enterprise wide information is provided. The following information relates to primary geographic locations in which the Company conducts its operations (all amounts in thousands):

## Three Months Ended March 31, 2012

	United States	Canada	Latin America	Australia	Singapore	New Zealand	India	Total
External Revenues	\$ 30,490	\$ 382	\$ 2,422	\$ 9,167	\$ 795	\$ 571	\$ —	\$ 43,827
Long-lived assets	\$ 261,713	\$ —	\$ 14,452	\$ 1,441	\$ 65,749	\$ 260	\$ 11,064	\$ 354,679

## Three Months Ended March 31, 2011

	United States	Canada	Latin America	Australia	Singapore	New Zealand	India	Total
External Revenues	\$ 27,898	\$ 182	\$ 2,563	\$ 8,322	\$ 724	\$ 361	\$ —	\$ 40,050
Long-lived assets	\$ 237,464	\$ —	\$ 18,180	\$ 1,506	\$ 70,922	\$ 36	\$ 3,674	\$ 331,782

## Note 9: Subsequent Events

## Entry into a Material Definitive Agreement the Creation of a Direct Financial Obligation

On April 26, 2012 Ebix entered into a credit agreement providing for a \$100 million secured syndicated credit facility (the "Secured Syndicated Credit Facility") with Citi Bank, N.A. as administrative agent and Citibank, N.A., Wells Fargo Capital Finance, LLC, and RBS Citizens, N.A. as joint lenders. The financing is comprised of a four-year, \$45 million secured revolving credit facility, a \$45 million secured term loan which amortizes over a four year period with quarterly principal and interest payments commencing on June 30, 2012 and a final payment of all remaining outstanding principal and accrued interest due on April 26, 2016, and an accordion feature that provides for the expansion of the credit facility by an additional \$10 million. This new \$100 million credit facility with Citibank, N.A., as administrative agent, replaces the former \$55 million facility that the Company had in place with Bank of America, N.A. The initial interest rate applicable to the Secured Syndicated Credit Facility is LIBOR plus 1.50% or currently 1.74%. Under the Secured Syndicated Credit Facility the maximum interest rate that could be charged depending upon the Company's leverage ratio is LIBOR plus 2.00%.

## Termination of a Material Definitive Agreement

On April 26, 2012, Ebix fully paid all of its obligations and related fees then outstanding to Bank of America N.A. ("BOA") and as pertaining to the Credit Agreement dated February 12, 2010 (as amended). The aggregate amount of the payment was \$45.14 million and was funded from a portion of the proceeds of the Citi Bank led Secured Syndicated Credit Facility discussed immediately above. Upon the effective date this payoff, BOA's commitment to extend further credit to the Company terminated.

## Completion of Business Acquisition

Effective April 1, 2012 Ebix acquired Canadian based Taimma Communications, Inc., ("Taimma"). Taimma provides innovative e-learning medical education solutions to the pharmaceutical, biotechnology, and healthcare industries. Ebix acquired all of the outstanding stock and the business operations of Taimma for a cash purchase price of \$5.2 million and funded the transaction using existing available internal cash resources. The former shareholders of Taimma retain the right to earn up to an additional \$4.5 million if certain incremental revenue targets are achieved over the two-year anniversary date subsequent to the effective date of the acquisition.



Appointment of New Named Executive Officers

Effective May 1, 2012 the Company appointed the following three additional individuals as new executives.

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Mr. Graham Prior, as Corporate Senior Vice President International Business & Intellectual Property. Mr. Prior, age 55, has been employed by Ebix since 1996 when the Company acquired Complete Broking Systems Ltd for which Mr. Prior was a part owner. Mr. Prior has been working within the insurance technology industry since 1990 and is currently responsible for the Company's international operations in Singapore, New Zealand, Australia, Europe, Africa and Asia. Mr. Prior is also responsible for the company's worldwide product development initiatives.

Mr. Leon d'Apice, as Managing Director - Ebix Australia Group Head. Mr. d'Apice, age 56, has been employed with Ebix since 1996 when the Company acquired Complete Broking Systems Ltd for which Mr. d'Apice was also a part owner in. Mr. d'Apice has been in the information technology field since 1977 and is currently responsible for all of the operations of the Ebix's Australia's business units.

Mr. James Senge Sr., as Senior Vice President EbixHealth. Mr. Senge, age 51, has been employed with Ebix, (as a result of the business acquisition of Acclamation Systems, Inc. in 2008), since 1979. During his over 32 plus years with the Acclamation/Ebix Mr. Senge has been involved with all facets of the EbixHealth division, including being responsible for the strategic direction and day to day operations of the division. Mr. Senge's focus is on expanding the Company's reach into the on-demand, end to end technology solutions for the health insurance and healthcare markets. Mr. Senge works from Ebix's Pittsburgh, Pennsylvania office. Ebix also employs a related party of Mr. Senge, namely James Senge Jr. who is the son of Mr. James Senge Sr. James Senge Jr. also works in the product development function within our EbixHealth division and is located in the Company's Atlanta, GA office.

**Item 2: MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS**

As used herein, the terms "Ebix," "the Company," "we," "our" and "us" refer to Ebix, Inc., a Delaware corporation, and its consolidated subsidiaries as a combined entity, except where it is clear that the terms mean only Ebix, Inc.

Safe Harbor for Forward-Looking Statements—This Form 10-Q and certain information incorporated herein by reference contains forward-looking statements and information within the "safe harbor" provisions of the Private Securities Litigation Reform Act of 1995, Section 27A of the Securities Act of 1933, and Section 21E of the Securities Exchange Act of 1934. This information includes assumptions made by, and information currently available to management, including statements regarding future economic performance and financial condition, liquidity and capital resources, acceptance of the Company's products by the market, and management's plans and objectives. In addition, certain statements included in this and our future filings with the Securities and Exchange Commission ("SEC"), in press releases, and in oral and written statements made by us or with our approval, which are not statements of historical fact, are forward-looking statements. Words such as "may," "could," "should," "would," "believe," "expect," "anticipate," "estimate," "intend," "seeks," "plan," "project," "continue," "predict," "will," "should," and other words or expressions of similar meaning are intended by the Company to identify forward-looking statements, although not all forward-looking statements contain these identifying words. These forward-looking statements are found at various places throughout this report and in the documents incorporated herein by reference. These statements are based on our current expectations about future events or results and information that is currently available to us, involve assumptions, risks, and uncertainties, and speak only as of the date on which such statements are made.

Our actual results may differ materially from those expressed or implied in these forward-looking statements. Factors that may cause such a difference, include, but are not limited to those discussed and identified in Part I, Item 1A, "Risk Factors" in our 2011 Form 10-K which is incorporated by reference herein, as well as: the willingness of independent insurance agencies to outsource their computer and other processing needs to third parties; pricing and other competitive pressures and the company's ability to gain or maintain share of sales as a result of actions by competitors and others; changes in estimates in critical accounting judgments; changes in or failure to comply with laws and regulations, including accounting standards, taxation requirements (including tax rate changes, new tax laws and revised tax interpretations) in domestic or foreign jurisdictions; exchange rate fluctuations and other risks associated with investments and operations in foreign countries (particularly in Australia, Singapore, Brazil, and India wherein we have significant operations); equity markets, including market disruptions and significant interest rate fluctuations, which may impede our access to, or increase the cost of, external financing; and international conflict, including terrorist acts. Except as expressly required by the federal securities laws, the Company undertakes no obligation to update any such factors, or to publicly announce the results of, or changes to any of the forward-looking statements contained herein to reflect future events, developments, changed circumstances, or for any other reason. The important risk factors that could cause actual results to differ materially from those in our specific forward-looking statements included in this Form 10-Q include, but are not limited to, the following:

Regarding Note 4 of the Notes to the Condensed Consolidated Financial Statements, and our future liquidity needs discussed under "Liquidity and Financial Condition," as pertaining to our ability to generate cash from operating activities and any declines in our credit ratings or financial condition which could restrict our access to the capital markets or materially increase our financing costs;

With respect to Note 5 of the Notes to the Condensed Consolidated Financial Statements, "Commitments and Contingencies", and "Contractual Obligations and Commercial Commitments" in MD&A, as regarding changes in the market value of our assets or the ultimate actual cost of our commitments and contingencies;

With respect Note 3 of the Condensed Notes to the Condensed Consolidated Financial Statements as pertaining to the business acquisitions we have made and our ability to efficiently and effectively integrate acquired business operations, and our ability to accurately estimate the fair value of tangible and intangible assets; and,

With respect this Management Discussion & Analysis of Financial Condition and Results of Operation and the analysis of the three revenue trends including the actual realized level of demand for our products during the immediately foreseeable future.

Readers should carefully review the disclosures and the risk factors described in this and other documents we file from time to time with the SEC, including future reports on Forms 10-Q and 8-K, and any amendments thereto. You may obtain our SEC filings at our website, [www.ebix.com](http://www.ebix.com) under the "Investor Information" section, or over the Internet at the SEC's web site, [www.sec.gov](http://www.sec.gov).

The following information should be read in conjunction with the unaudited condensed consolidated financial statements and the notes thereto included in Part 1. Item 1 of this Quarterly Report, and the audited consolidated financial statements and

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notes thereto and Management's Discussion and Analysis of Financial Condition and Results of Operations contained in the Company's Annual Report on Form 10-K for the year ended December 31, 2011.

## Company Overview

Ebix, Inc. is a leading international supplier of software and e-commerce solutions to the insurance and financial industries. Ebix provides a variety of application software products for the insurance and financial industries ranging from data exchanges, carrier systems, and agency systems, to custom software development for all entities involved in insurance and financial services. Our goal is to be the leading powerhouse of backend insurance transactions in the world. The Company's vision is to focus on the convergence of technology platforms for all insurance channels, processes and entities in a manner such that data can seamlessly flow once a data entry has been made. Our customers include many of the top insurance and financial sector companies in the world.

The insurance and financial service industries continue to undergo significant consolidation as driven by the need for, and benefits from, economies of scale and scope in providing insurance and financial services in a competitive environment. The insurance markets have particularly experienced a steady increase in the desire to reduce paper-based processes and improve efficiency at the back-end side and consumer end side. Such consolidation has involved both insurance carriers and insurance brokers and is directly impacting the manner in which insurance products are distributed. Management believes the insurance industry will continue to experience significant change and increased efficiencies through online exchanges, as the transition from paper-based processes are increasingly becoming the norm across world insurance markets. Changes in the insurance industry are likely to create new opportunities for the Company.

Ebix strives to work collaboratively with clients to develop innovative technology strategies and solutions that address their specific business challenges. Ebix combines the newest technologies with its capabilities in consulting, systems design and integration, information technology, business process outsourcing, applications software, and Web and application hosting to meet the individual needs of insurance and financial service organizations. We continue to expand both through business acquisitions and organically.

## Offices and Geographic Information

The Company has its worldwide headquarters in Atlanta, Georgia with its international operations being managed from its Singapore offices, and it also has domestic operations throughout the United States including California, Florida, Pennsylvania, Utah, Virginia, Texas, Ohio, and Connecticut; and international operations in Australia, Brazil, China, Japan, New Zealand, the United Kingdom, Canada and India. In these offices, Ebix employs insurance and technology professionals who provide products, services, support and consultancy to thousands of customers across six continents. The Company's product development unit in India has been awarded Level 5 status of the Carnegie Mellon Software Engineering Institute's Capability Maturity Model Integrated (CMMI), ISO 9001:2000 certification, and ISO 2700 security certification.

## Results of Operations — Three Months Ended March 31, 2012 and 2011

## Operating Revenue

The Company derives its revenues primarily from subscription and transaction fees pertaining to services delivered over our exchanges or from our ASP platforms, fees for business process outsourcing services, and fees for software development projects including associated fees for consulting, implementation, training, and project management provided to customers with installed systems.

Ebix's revenue streams come from four product channels. Presented in the table below is the breakout of our revenues for each of those product channels for the three months ended March 31, 2012 and 2011.

(dollar amounts in thousands)	Three Months Ended	
	March 31, 2012	2011
Exchanges	\$34,646	\$31,065
Broker Systems	4,754	3,842
Business Process Outsourcing ("BPO")	3,571	3,619

Carrier Systems	856	1,524
Totals	\$43,827	\$40,050

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During the three months ended March 31, 2012 our total operating revenues increased \$3.8 million or 9%, to \$43.8 million as compared to \$40.1 million during the first quarter of 2011. This increase is the result of growth in our Exchange channel. The Company continues to effectively leverage product cross-selling opportunities across all channels, as facilitated by our business acquisitions. Also partially effecting reported revenues was the impact from fluctuations in the exchange rates of the foreign currencies in the countries in which we conduct operations. During the three months ended March 31, 2012 and 2011 the change in foreign currency exchange rates increased reported consolidated operating revenues by \$332 thousand and \$1.1 million, respectfully.

**Cost of Services Provided**

Costs of services provided, which includes costs associated with maintenance, support, call center, consulting, implementation and training services, increased \$1.7 million or 24%, from \$7.3 million in the first quarter of 2011 to \$9.0 million in the first quarter of 2012. This increase is primarily due to additional customer support costs, personnel expenses, and facilities related costs in support of increased revenue streams associated with business acquisitions completed during 2011, and in support of the growth in our Exchange channel.

**Product Development expenses**

The Company's product development efforts are focused on the development of new operating technologies and services for use by insurance carriers, brokers and agents, and the development of new data exchanges for use in both the domestic and international insurance and financial services industries. Product development expenses decreased \$0.3 million or 8% from \$4.6 million during the first quarter of 2011 to \$4.3 million during the first quarter of 2012. This modest decrease is primarily due to less spending on product development personnel in support of the Carrier Systems and BPO channels.

**Sales and Marketing Expenses**

Sales and marketing expenses increased \$1.0 million or 34%, from \$2.9 million in the first quarter of 2011 to \$3.8 million in the first quarter of 2012. This increase is primarily attributable to personnel and facility costs associated with additional sales personnel in support of our Exchange channels.

**General and Administrative Expenses**

General and administrative expenses ("G&A") decreased by 1.3 million or 17% from \$7.8 million in the first quarter of 2011 to \$6.4 million in the first quarter of 2012. Included in this quarter's G&A costs is the net benefit in the approximate amount of \$971 thousand related to a termination fee received by the Company in connection with a failed business acquisition (net of significant directly related internal operating costs incurred by the Company and a portion of the fee that had to be paid to our investment banker). Partially offsetting the net benefit from the acquisition termination fee was a \$255 thousand bad debt expense charge necessary to adequately increase the Company's allowance for doubtful accounts receivable.

**Amortization and Depreciation Expenses**

Amortization and depreciation expenses increased \$64 thousand or 3%, from \$1.88 million in the first quarter of 2011 to \$1.94 million in the first quarter of 2012. This increase is primarily due to \$71 thousand of depreciation expenses in connection with equipment costs associated with the expansion of our data exchange networks and facilities.

**Income Taxes**

The Company recognized income tax expense of \$2.3 million for the three months ended March 31, 2012. The Company's interim period income tax provisions are based on an estimate of the effective income tax rate expected to be applicable to the corresponding annual period, after eliminating discrete items unique to the respective interim period being reported. The calculated estimated annual effective tax rate used by the Company to determine the interim income tax provision for the first quarter of 2012 was 12.52% as compared to 9.38% for the same period in 2011. The effective rate increased primarily due to increased taxable income from jurisdictions with higher tax rates.



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## Dividends, Liquidity and Capital Resources

The Company's ability to generate significant cash flows from its ongoing operating activities is one of our fundamental financial strengths. Our principal sources of liquidity are the cash flows provided by the Company's operating activities, our commercial banking credit facility, and cash and cash equivalents on hand. Due to the effect of temporary or timing differences resulting from the differing treatment of items for tax and accounting purposes (including the treatment of net operating loss carryforwards and minimum alternative tax obligations in the U.S. and India), future income tax expense is expected to exceed cash outlays for income taxes. We intend to utilize cash flows generated by our operations, in combination with our bank credit facility, and the possible issuance of additional equity or debt securities, to fund capital expenditures and organic growth initiatives, to make strategic business acquisitions in the insurance and financial services sector, and to repurchase shares of our common stock as market conditions warrant.

We intend to utilize cash flows generated by our ongoing operating activities, in combination with our commercial lending facility, and the possible issuance of additional equity or debt securities to fund capital expenditures and organic growth initiatives, to make strategic business acquisitions, to retire outstanding indebtedness, and to possibly repurchase shares of our common stock as market and operating conditions warrant.

In the 4th quarter of 2011 the Company paid its first quarterly dividend in the amount of \$0.04 per common share, paying \$1.5 million in the aggregate in regards to this dividend issuance. This same quarterly dividend per share was paid in February 2012. The dividend rate was increased to \$0.05 effective with dividend payment to be made in May 2012. The Company intends to use a portion of its operating cash flows to continue issuing dividends to its shareholders in the foreseeable future, while remaining dedicated to using most of its cash to generate improvement in future earnings by funding organic growth initiatives and accretive business acquisitions.

We believe that anticipated cash flows provided by our operating activities, together with current cash and cash equivalent balances and access to our credit facilities and the capital markets, if required and available, will be sufficient to meet our projected cash requirements for the next twelve months, and the foreseeable future thereafter, although any projections of future cash needs, cash flows, and the condition of the capital markets in general, as to the availability of debt and equity financing, are subject to substantial uncertainty. In the event additional liquidity needs arise, we may raise funds from a combination of sources, including the potential issuance of debt or equity securities. However, there are no assurances that such financing facilities or the equity capital markets will be available in amounts or on terms acceptable to us, if at all.

We continue to strategically evaluate our ability to sell additional equity or debt securities, to expand existing or obtain new credit facilities from lenders in order to strengthen our financial position. We regularly evaluate our liquidity requirements, including the need for additional debt or equity offerings, when considering potential business acquisitions, development of new products or services, or repurchases of our common stock.

Our cash and cash equivalents were \$37.1 million and \$23.7 million at March 31, 2012 and December 31, 2011, respectively. As of March 31, 2012, the Company held an additional amount of \$730 thousand in fixed bank deposits of more than 90 days, which is not included in the reported cash and cash equivalents amount of \$37.1 million. Our cash and cash equivalents balance has increased by \$13.4 million since year end 2011, as a direct result of cash generated by our ongoing operating activities. The Company holds material cash and cash equivalent balances overseas in foreign jurisdictions. The free flow of cash from certain countries where we hold such balances may be subject to repatriation tax effects and other restrictions. Furthermore, the repatriation of earnings from some of our foreign subsidiaries would result in the application of withholding taxes at source as well as a tax at the U.S. parent level upon receipt of the repatriation amounts. The approximate cash, cash equivalents, and short-term investments balances held in our domestic U.S. operations and each of our foreign subsidiaries as of May 7, 2012 is presented in table below (figures denominated in thousands):

	United States	Canada	Latin America	Australia	Singapore	New Zealand	India	Sweden	Total
Cash and ST investments	\$ 7,489	\$ 979	\$ 1,508	\$ 3,123	\$ 871	\$ 467	\$ 15,875	\$ 16	\$ 30,328



Our current ratio increased to 1.55 at March 31, 2012 as compared to 1.28 at December 31, 2011 and our working capital position improved to \$26.4 million million at March 31, 2012 as compared to \$14.0 million at the end of the 2011. The increase in our short-term liquidity position is primarily the result of the additional available cash balances and the reduction in trade payables and accrued liabilities. We believe that our ability to generate sustainable and robust cash flows from operations will enable the Company to continue to fund its current liabilities from current assets including available cash balances for the foreseeable future.

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### Business Combinations

The Company executes accretive business acquisitions in combination with organic growth initiatives as part of its comprehensive business growth and expansion strategy. The Company' looks to acquire businesses that are complementary to Ebix's existing products and services. During the first quarter of 2012 the Company did not execute any material business acquisitions.

### Operating Activities

Net cash provided by our operating activities was \$13.8 million for the three month period ended March 31, 2012. The primary components of the cash provided by operations during this three month interim period consisted of net income of \$15.7 million, net of \$661 thousand of non-cash unrealized foreign currency exchange losses, \$1.9 million of depreciation and amortization, \$(5.1) million of working capital requirements primarily associated with reductions to trade payables and accrued liabilities, and \$548 thousand of non-cash share-based compensation.

During the three months ended March 31, 2011 the Company generated \$10.3 million of net cash flow from operating activities. The primary components of the cash provided by operations during this three-month interim period consisted of net income of \$15.2 million, net of \$(1.7) million of net non-cash gains recognized on derivative instruments and foreign currency exchange, \$1.9 million of depreciation and amortization, \$(5.6) million of working capital requirements primarily associated with payments of trade payables and accrued liabilities, and increased outstanding trade receivables, and \$556 thousand of non-cash compensation.

### Investing Activities

Net cash provided from investing activities during the three months ended March 31, 2012 totaled \$306 thousand which primarily consisted of \$979 thousand from maturities of marketable securities (specifically bank certificates of deposit), net of purchases, less \$673 thousand used for capital expenditures pertaining to the enhancement of our technology platforms and the purchases of operating equipment to support our expanding operations.

Net cash provided from investing activities during the three months ended March 31, 2011 totaled \$5.6 million and was primarily related to the \$3.5 million of net cash obtained from the acquisition of ADAM in February 2011 (net of \$944 thousand used to settle outstanding ADAM stock options). Also \$524 thousand was used for capital expenditures and \$2.6 million was provided from the net maturities of marketable securities (specifically bank certificates of deposit).

### Financing Activities

During the three months ended March 31, 2012 net cash used in financing activities was \$1.5 million. This net financing cash outflow primarily consisted of the \$1.46 million used to remit the dividend paid to common stock holders in February.

During the three months ended March 31, 2011 net cash used in financing activities was \$3.9 million. During that interim period the Company remitted \$1.3 million to make principal repayments on existing term loan obligations (net of proceeds received), \$2.4 million was used to complete open market repurchases of our common stock, and \$258 thousand was used to service then existing debt and capital lease obligations.

### Commercial Bank Financing Facility

On April 26, 2012 Ebix entered into a credit agreement providing for a \$100 million secured syndicated credit facility (the "Secured Syndicated Credit Facility") with Citi Bank, N.A. as administrative agent and Citibank, N.A., Wells Fargo Capital Finance, LLC, and RBS Citizens, N.A. as joint lenders. The financing is comprised of a four-year, \$45 million secured revolving credit facility, a \$45 million secured term loan which amortizes over a four year period with quarterly principal and interest payments commencing on June 30, 2012 and a final payment of all remaining outstanding principal and accrued interest due on April 26, 2016, and an accordion feature that provides for the expansion of the credit facility by an additional \$10 million. This new \$100 million credit facility with Citibank, N.A., as administrative agent, replaces the former \$55 million facility that the Company had in place with Bank of America, N.A. The initial interest rate applicable to the Secured Syndicated Credit Facility is LIBOR plus 1.50% or currently

1.74%. Under the Secured Syndicated Credit Facility the maximum interest rate that could be charged depending upon the Company's leverage ratio is LIBOR plus 2.00%.

On April 26, 2012, Ebix fully paid all of its obligations and related fees then outstanding to Bank of America N.A. ("BOA") and as pertaining to the Credit Agreement dated February 12, 2010 (as amended). The aggregate amount of the payment

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was \$45.14 million and was funded from a portion of the proceeds of the Citi Bank led Secured Syndicated Credit Facility discussed immediately above. Upon the effective date this payoff, BOA's commitment to extend further credit to the Company terminated.

Previously on April 20, 2011 the Company entered into a seventh amendment to a credit agreement (the "Seventh Amendment") with Bank of America, N.A. ("BOA"), as administrative agent, which materially amended the initial credit agreement dated February 12, 2010. The Seventh Amendment increased the existing revolving credit facility from \$25 million to \$35 million with its term ending on April 20, 2014, and the \$10 million secured term loan was increased to \$20 million and amortizes over a three year period with quarterly principal and interest payments that commenced on June 30, 2011. The entire credit facility had a variable interest rate currently set at LIBOR plus 1.50%.

The revolving credit facility is used by the Company to fund working capital requirements primarily in support of current operations, organic growth, and accretive business acquisitions. The underlying financing agreement contains financial covenants regarding the Company's annualized EBITDA, fixed charge coverage ratio, and leverage ratio, as well as certain restrictive covenants pertaining to such matters as the incurrence of new debt, the aggregate amount of repurchases of the Company's equity shares, and the consummation of new business acquisitions. The Company currently is in compliance with all such financial and restrictive covenants, and there have been no violations thereof or in the event of noncompliance, appropriate waivers having been obtained.

At March 31, 2012, the outstanding balance on the revolving line of credit was \$31.8 million and the facility carried an interest rate of 1.75%. This balance is included in the long-term liabilities section of the Condensed Consolidated Balance Sheets. During the three month period ending March 31, 2012, both the average and maximum outstanding balances on the revolving line of credit was \$31.8 million.

At March 31, 2012, the outstanding balance on the term loan was \$15 million of which \$8.3 million is due within the next twelve months. This term loan also carried an interest rate of 1.75%. During the three months ended March 31, 2012, no payments were made against the term loan. The current and long-term portions of the term loan are included in the respective current and long-term sections of the Condensed Consolidated Balance Sheets.

**Convertible Debt**

On August 25, 2009, the Company entered into a Convertible Note Purchase Agreement with the Rennes Foundation in an original amount of \$5.0 million, which amount is convertible into shares of common stock at a conversion price of \$16.66 per share (the "Note"). The Note had a 0.0% stated interest rate and no warrants were issued. The Note was payable in full at its maturity date of August 25, 2011. The Company applied imputed interest on these convertible notes using an interest rate of 1.75% and discounted their carrying value accordingly. With respect to this convertible note, and in accordance with the terms of the notes, as understood between the Company and the holder, upon a conversion election by the holder the Company had to satisfy the related original principal balance in cash and could have satisfied the conversion spread (that being the excess of the conversion value over the related original principal component) in either cash or stock at option of the Company. On April 18, 2011, the Rennes Foundation elected to fully convert the Note. The Company settled this conversion election by paying \$5.0 million in cash with respect to the principal component, and paying \$1.8 million in cash with respect to the conversion spread. The Company also recognized a pre-tax gain in the amount of \$108 thousand with respect the settlement of this convertible debt.

As of March 31, 2012 and December 31, 2011 the Company has no remaining convertible debt obligations.

**Off-Balance Sheet Arrangements**

We do not engage in off -balance sheet financing arrangements.

**Contractual Obligations and Commercial Commitments**

The following table summarizes our significant contractual purchase obligations and other long-term commercial commitments as of March 31, 2012. The table excludes obligations or commitments that are contingent based on events or factors uncertain at this time.

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	Payment Due by Period				
	Total	Less Than 1 Year	1-3 Years	3-5 Years	More than 5 years
			(in thousands)		
Revolving line of credit	\$31,750	\$—	\$31,750	\$—	\$—
Long-term debt	\$18,000	\$8,934	\$9,066	\$—	\$—
Operating leases	\$15,910	\$4,256	\$5,868	\$2,867	\$2,919
Capital leases	\$825	\$363	\$462	\$—	\$—
Total	\$66,485	\$13,553	\$47,146	\$2,867	\$2,919

## Recent Accounting Pronouncements

For information about new accounting pronouncements and the potential impact on our Consolidated Financial Statements, see Note 1 of the condensed notes to the condensed consolidated financial statements in this Form 10-Q and Note 1 of the notes to consolidated financial statements in our 2011 Form 10-K.

## Application of Critical Accounting Policies

The preparation of financial statements in conformity with generally accepted accounting principles (“GAAP”), as promulgated in the United States, requires our management to make estimates and assumptions that affect the reported amounts of assets and liabilities, revenues and expenses and related disclosures of contingent assets and liabilities in our Condensed Consolidated Financial Statements and accompanying notes. We believe the most complex and sensitive judgments, because of their significance to the Condensed Consolidated Financial Statements, result primarily from the need to make estimates and assumptions about the effects of matters that are inherently uncertain. The following accounting policies involve the use of “critical accounting estimates” because they are particularly dependent on estimates and assumptions made by management about matters that are uncertain at the time the accounting estimates are made. In addition, while we have used our best estimates based on facts and circumstances available to us at the time, different estimates reasonably could have been used in the current period, or changes in the accounting estimates that we used are reasonably likely to occur from period to period which may have a material impact on our financial condition and results of operations. For additional information about these policies, see Note 1 of the Condensed Notes to the Condensed Consolidated Financial Statements in this Form 10-Q. Although we believe that our estimates, assumptions and judgments are reasonable, they are limited based upon information presently available. Actual results may differ significantly from these estimates under different assumptions, judgments or conditions.

## Revenue Recognition

The Company derives its revenues from professional and support services, which include: (a) subscription and transaction fees related to services delivered over our exchanges or on an application service provider (“ASP”) basis; (b) subscription and transaction fees related to services delivered over our exchanges or on an application service provider (“ASP”) basis; (c) implementation, training, and project management provided to customers with installed systems; (d) revenue generated from software development projects and associated fees for consulting; and, (e) the licensing of proprietary and third-party software. Sales and value-added taxes are not included in revenues, but rather are recorded as a liability until the taxes assessed are remitted to the respective taxing authorities.

In accordance with Financial Accounting Standard Board (“FASB”) and Securities and Exchange Commission Staff Accounting (the “SEC”) accounting guidance on revenue recognition the Company considers revenue earned and realizable when: (a) persuasive evidence of the sales arrangement exists, provided that the arrangement fee is fixed or determinable, (b) delivery or performance has occurred, (c) customer acceptance has been received, if contractually required, and (d) collectability of the arrangement fee is probable. The Company generally uses signed contractual agreements as persuasive evidence of a sales arrangement. We apply the provisions of the relevant generally accepted accounting principles related to all transactions involving the license of software where the software deliverables are considered more than inconsequential to the other elements in the arrangement.

For contracts that contain multiple deliverables, we analyze the revenue arrangements in accordance with the relevant technical accounting guidance, which provides criteria governing how to determine whether goods or services that are

delivered separately in a bundled sales arrangement should be considered as separate units of accounting for the purpose of revenue recognition. Generally these types of arrangements include deliverables pertaining to software licenses, system set-up, and professional services associated with product customization or modification. Delivery of the various contractual elements typically

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occurs over periods of less than eighteen months. These arrangements generally do not have refund provisions or have very limited refund terms.

Software development arrangements involving significant customization, modification or production are accounted for in accordance with the appropriate technical accounting guidance issued by FASB using the percentage-of-completion method. The Company recognizes revenue using periodic reported actual hours worked as a percentage of total expected hours required to complete the project arrangement and applies the percentage to the total arrangement fee.

### Allowance for Doubtful Accounts Receivable

Management specifically analyzes accounts receivable and historical bad debts, write-offs, customer concentrations, customer credit-worthiness, current economic trends and changes in our customer payment terms when evaluating the adequacy of the allowance for doubtful accounts.

### Valuation of Goodwill

Goodwill represents the cost in excess of the fair value of the net assets of acquired businesses. Indefinite-lived intangible assets represent the fair value of acquired contractual customer relationships for which future cash flows are expected to continue indefinitely. In accordance with the relevant FASB accounting guidance, goodwill and indefinite-lived intangible assets are not amortized but are tested for impairment at the reporting unit level on an annual basis or on an interim basis if an event occurs or circumstances change that would likely have reduced the fair value of a reporting unit below its carrying value. Potential impairment indicators include a significant change in the business climate, legal factors, operating performance indicators, competition, and the sale or disposition of a significant portion of the business. The impairment evaluation process involves an assessment of certain qualitative factors to determine whether the existence of events or circumstances would indicate that it is more likely than not that the fair value of any of our reporting units was less than their than its carrying amount. If after assessing the totality of events or circumstances, we were to determine that it is not more likely than not that the fair value of a reporting unit is less than its carrying amount, then we would not perform the two-step quantitative impairment testing described further below.

The aforementioned two-step quantitative testing process involves comparing the reporting unit carrying values to their respective fair values; we determine fair value of our reporting units by applying the discounted cash flow method using the present value of future estimated net cash flows. If the fair value of a reporting unit exceeds its carrying value, then no further testing is required. However, if a reporting unit's fair value were to be less than its carrying value, we would then determine the amount of the impairment charge, if any, which would be the amount that the carrying value of the reporting unit's goodwill exceeded its implied value. Projections of cash flows are based on our views of growth rates, operating costs, anticipated future economic conditions and the appropriate discount rates relative to risk and estimates of residual values. We believe that our estimates are consistent with assumptions that marketplace participants would use in their estimates of fair value. The use of different estimates or assumptions for our projected discounted cash flows (e.g., growth rates, future economic conditions, discount rates and estimates of terminal values) when determining the fair value of our reporting units could result in different values and may result in a goodwill impairment charge. We perform our annual goodwill impairment evaluation and testing as of September 30th of each year. During the year ended December 31, 2011 we had no impairment of our reporting unit goodwill balances.

### Income Taxes

Deferred income taxes are recorded to reflect the estimated future tax effects of differences between financial statement and tax basis of assets, liabilities, operating losses, and tax credit carry forwards using the tax rates expected to be in effect when the temporary differences reverse. Valuation allowances, if any, are recorded to reduce deferred tax assets to the amount management considers more likely than not to be realized. Such valuation allowances are recorded for the portion of the deferred tax assets that are not expected to be realized based on the levels of historical taxable income and projections for future taxable income over the periods in which the temporary differences will be deductible.

The Company also applies FASB accounting guidance on accounting for uncertainty in income taxes positions. This guidance clarifies the accounting for uncertainty in income taxes by prescribing the minimum recognition threshold a

tax position is required to meet before being recognized in the financial statements.

Foreign Currency Matters

Our reporting currency is the U.S. dollar. The functional currency of the Company's foreign subsidiaries is the local currency of the country in which the subsidiary operates. The assets and liabilities of foreign subsidiaries are translated into U.S. Dollars at the rates of exchange at the balance sheet dates. Income and expense accounts are translated at the average exchange rates in effect during the period. Gains and losses resulting from translation adjustments are included as a component of other



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comprehensive income in the accompanying consolidated financial statements. Foreign exchange transaction gains and losses that are derived from transactions denominated in other than the subsidiary's functional currency is included in the determination of net income.

**Item 3: QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK**

The Company is exposed to foreign currency exchange rate risk related to our foreign-based operations where certain transactions are denominated in other than our entity's functional currency and are subject to market risk with respect to fluctuations in the relative value of those currencies. Most of the Company's transactions are denominated in U.S. dollars, however, the Company has significant and expanding operations in Australia, Singapore, Brazil and India, and we conduct transactions in the local currencies of each of those locations. There can be no assurance that fluctuations in the value of foreign currencies will not have a material adverse effect on the Company's business, operating results, revenues or financial condition. During the three months ended March 31, 2012 and 2011 the net change in the cumulative foreign currency translation account, which is a component of stockholders' equity, were unrealized gains of \$4.3 million and \$2.1 million, respectively. The Company considered the historical trends in currency exchange rates and determined that it was reasonably possible that adverse changes in our respective foreign currency exchange rates of 20% could be experienced in the near term. Such an adverse change in currency exchange rates would have resulted in reduction to pre-tax income of approximately \$1.1 million and \$1.4 million for the three months ended March 31, 2012 and 2011, respectively.

The Company had entered into a series of six-month and one-year forward foreign exchange contracts to hedge the intercompany receivables originated by our Indian subsidiary that are denominated in United States dollars. These U.S. dollars/Indian rupee hedges are intended to partially offset the impact of movement in exchange rates on future operating costs, and to reduce the risk that our earnings and cash flows will be adversely affected by changes in foreign currency exchange rates. As of March 31, 2012, these contracts have matured. Changes in the fair value of these derivative instruments are recognized in our Condensed Consolidated Statements of Income as part of reported foreign currency exchange gains or losses. We use these instruments as economic hedges intended to mitigate the effects of changes in foreign exchange rates, and not for speculative purposes. These derivative instruments do not subject us to material balance sheet risk due to exchange rate movements because gains and losses on these derivatives partially offset the gains and losses on the intercompany receivables being hedged. As related to these hedging instruments, during the three months ended March 31, 2012, we recognized a gain of \$1.2 million included in "Foreign exchange gain (loss)" in the Condensed Consolidated Statements of Income. We regularly review our hedging strategies and may in the future, as a part of this review, determine the need to change our hedging activities.

The Company's exposure to interest rate risk relates to its interest expense on outstanding debt obligations and to its interest income on existing cash balances. As of March 31, 2012 the Company had \$49.8 million of outstanding debt obligations which consisted of a \$31.8 million balance on our commercial banking revolving line of credit, a \$15.0 million secured term loan, and a \$3.0 million secured promissory note payable. The Company's revolving line of credit bears interest at the rate of LIBOR + 1.50%, and stood at 1.75% at March 31, 2012. The Company is exposed to market risk in relation to this line of credit in regards to the potential increase to interest expense arising from adverse changes in interest rates. This interest rate risk is estimated as the potential decrease in earnings resulting from a hypothetical 30% increase in the LIBOR rate. Such an adverse change in the LIBOR rate would have resulted in a reduction to pre-tax income of approximately \$10 thousand and \$8 thousand for the three months ending March 31, 2012 and 2011, respectively. The Company's average cash balances during the first quarter of 2012 was \$30.4 million and its existing cash balances as of March 31, 2012 was \$37.1 million. The Company is exposed to market risk in relation to these cash balances in regards to the potential loss of interest income arising from adverse changes in interest rates. This interest rate risk is estimated as the potential decrease in earnings resulting from a hypothetical 20% decrease in interest rates earned on deposited funds. Such an adverse change in these interest rates would have resulted in a reduction to pre-tax income of approximately \$33 thousand and \$40 thousand for the three months ended March 31, 2012 and 2011, respectively.

There were no other material changes to our market risk exposure during the three months ended March 31, 2012. For additional information regarding our exposure to certain market risks, see “Quantitative and Qualitative Disclosures about Market Risk,” in Part II, Item 7A of our 2011 Form 10-K.

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Item 4: CONTROLS AND PROCEDURES

Evaluation of Disclosure Controls and Procedures: The Company's management evaluated, with the participation of the Chief Executive Officer and Chief Financial Officer, the effectiveness of the company's disclosure controls and procedures as of the end of the period covered by this report. Based on that evaluation, the Chief Executive Officer and Chief Financial Officer have concluded that the Company's disclosure controls and procedures were effective as of the end of the period covered by this report.

Internal Control over Financial Reporting: There were no changes in our internal control over financial reporting during the three months ended March 31, 2012, that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

Part II — OTHER INFORMATION

Items required under Part II not specifically shown below are not applicable.

Item 1: LEGAL PROCEEDINGS

Contingencies-Between July 14, 2011 and July 21, 2011, securities class action complaints were filed against the Company and certain of its officers in the United States District Court for the Southern District of New York and in the United States District Court for the Northern District of Georgia. The complaints assert claims against (i) the Company and the Company's CEO and CFO for alleged violations of Section 10(b) of the Securities Exchange Act of 1934 (the "Exchange Act") and Rule 10b-5 promulgated thereunder and (ii) the Company's CEO and CFO as alleged controlling persons. The complaints generally allege false statements in earnings reports, SEC filings, press releases, and other public statements allegedly caused the Company's stock to trade at artificially inflated prices. Plaintiff seeks an unspecified amount of damages. The New York action has been transferred to Georgia and has been consolidated with the Georgia action, now styled In re: Ebix, Inc. Securities Litigation, Civil Action No. 1:11-CV-02400-RSW (N.D. Ga.). A consolidated amended complaint will be filed by Lead Plaintiff on or about November 28, 2011. In September 2011, a related derivative complaint was filed against the Company and each of its Directors in the Superior Court of Fulton County, Georgia, styled Nauman v. Raina, et al., Civil Action File No. 2011-cv-205276. The derivative action has been stayed pending resolution of the Defendants' Motion to Dismiss the Amended Consolidated Complaint in the federal action. The Company believes that the complaints are legally insufficient and we intend to seek dismissal.

The Company is involved in various other claims and legal actions arising in the ordinary course of business. In the opinion of management, the ultimate likely disposition of these matters will not have a material adverse effect on the Company's consolidated financial position, results of operations or liquidity.

Item 1A: RISK FACTORS

We believe there have been no material changes from the risk factors previously disclosed in our Annual Report on Form 10-K for the year ended December 31, 2011. Readers of this interim report on Form 10-Q should carefully consider, in addition to the other information set forth in this report, the risk factors discussed in our Annual Report on Form 10-K, which could materially affect our business, financial condition, or future results. Such risk factors are expressly incorporated herein by reference. The risks described in our Annual Report are not the only risks facing our Company. In addition to risks and uncertainties inherent in forward looking statements contained in this Report on Form 10-Q, additional risks and uncertainties not currently known to us or that we currently deem to be immaterial also could materially adversely affect our business, financial condition, and/or operating results.

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## Item 2: REPURCHASES OF EQUITY SECURITIES

The following table contains information with respect to purchases of our common stock made by or on behalf of Ebix during the three months ended March 31, 2012, as part of our publicly-announced share repurchase plan:

Period	Total Number of Shares (Units) Purchased	Total Number of Shares Purchased as Part of Publicly-Announced Plans or Programs	Average Price Paid Per Share (1)	Maximum Number (or Approximate Dollar Value) of Shares that May Yet Be Purchased Under the Plans or Programs (2)
As of December 31, 2011	4,472,308	4,472,308	\$—	\$23,751,000
January 1, 2012 to January 31, 2012	—	—	\$—	\$23,751,000
February 1, 2012 to February 29, 2012	—	—	\$—	\$23,751,000
March 1, 2012 to March 31, 2012	—	—	\$—	\$23,751,000
Total	4,472,308	4,472,308		\$23,751,000

(1) Average price paid per share for shares purchased as part of our publicly-announced plan.

Effective June 30, 2011 the Company's Board of Directors unanimously approved an increase in the size of the

(2) Company's authorized share repurchase plan from \$45.0 million to \$100.0 million. The Board directed that the repurchases be funded with available cash balances and cash generated by the Company's operating activities, and be completed in the subsequent twelve months if possible.

## Item 3: DEFAULTS UPON SENIOR SECURITIES

None.

## Item 6: EXHIBITS

The exhibits filed herewith or incorporated by reference herein are listed in the Exhibit Index attached hereto.

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SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

Ebix, Inc.

Date: May 10, 2012

By: /s/ Robin Raina  
Robin Raina  
Chief Executive Officer  
(Principal Executive Officer)

Date: May 10, 2012

By: /s/ Robert F. Kerris  
Robert F. Kerris  
Chief Financial Officer  
(Principal Financial and Accounting Officer)

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EXHIBIT INDEX

Exhibits

- 2.1 Stock Purchase Agreement dated February 23, 2004 by and among the Company and the shareholders of LifeLink Corporation (incorporated herein by reference to Exhibit 2.1 to the Company's Current Report of Form 8-K dated February 23, 2004 (the "February 2004 8-K")) and incorporated herein by reference.
- 2.2 Secured Promissory Note, dated February 23, 2004, issued by the Company (incorporated herein by reference to Exhibit 2.2 of the February 2004 8-K) and incorporated herein by reference.
- 2.3 Purchase Agreement, dated June 28, 2004, by and between Heart Consulting Pty Ltd. And Ebix Australia Pty Ltd. (incorporated by reference to Exhibit 2.1 to the Company's Current Report of Form 8-K dated July 14, 2004 (the "July 14, 2004 8-K")) and incorporated herein by reference.
- 2.4 Agreement, dated July 1, 2004, by and between Heart Consulting Pty Ltd. and Ebix, Inc. (incorporated by reference to Exhibit 2.2 to the Company's Current Report of Form 8-K dated July 14, 2004 (the "July 14, 2004 8-K")) and incorporated herein by reference.
- 2.5 Agreement Plan of Merger by and among Ebix, Finetre and Steven F. Piaker, as shareholders' Representative dated September 22, 2006 (incorporated by reference to Exhibit 2.1 to the Company's Current Report on 8-K/A dated October 2, 2006) and incorporated herein by reference.
- 2.6 Asset Purchase Agreement dated May 9, 2006, by and among Ebix, Inc., Infinity Systems Consulting, Inc. and the Shareholders of Infinity Systems Consulting, Inc. (incorporated here by reference to

Exhibit 2.1 to the Company's Current Report on Form 8-K/A dated May 9, 2006) and incorporated herein by reference.

Agreement and Plan of Merger dated October 31, 2007 by and among Ebix, Inc., Jenquest, Inc. IDS Acquisition Sub. and Robert M.

2.7

Ward as Shareholder Representative (incorporated here by reference to Exhibit 2.1 to the Company's Current Report on Form 8-K/A dated November 7, 2007) and incorporated herein by reference.

Stock Purchase Agreement by and among Ebix, Inc., Acclamation Systems, Inc., and Joseph Ott

2.8

(incorporated here by reference to Exhibit 2.1 to the Company's Current Report on Form 8-K dated August 5, 2008) and incorporated herein by reference.

Stock Purchase Agreement by and amongst Ebix, Inc., ConfirmNet Corporation, Ebix Software India Private Limited, ConfirmNet Acquisition Sub, Inc., and Craig

2.9

Irving, as Shareholders' Representative (incorporated here by reference to Exhibit 2.1 to the Company's Current Report on Form 8-K dated November 12, 2008) and incorporated herein by reference.

2.10

	Common stock (unaudited)	Additional paid-in capital	Retained earnings	Accumulated other comprehensive income (loss)	Noncontrolling interest in subsidiary	Total equity
Balance at December 31, 2017	\$ 6,089	\$ 300,866	\$ 220,104	\$ (191,737 )	\$ 17,756	\$ 353,078
Change in accounting principle - ASU 2016-01	—	—	46,069	(46,069 )	—	—
Balance at January 1, 2018, as adjusted	6,089	300,866	266,173	(237,806 )	17,756	353,078

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Net income (loss)	—	—	(43,752 )	—	1,654	(42,098 )
Other comprehensive income, net of tax	—	—	—	299	—	299
Issuance of NL common stock	1	119	—	—	—	120
Dividends	—	—	—	—	(251 )	(251 )
Other, net	—	154	—	—	18	172
Balance at September 30, 2018	\$ 6,090	\$301,139	\$222,421	\$ (237,507 )	\$ 19,177	\$311,320

See accompanying notes to Condensed Consolidated Financial Statements.



## NL INDUSTRIES, INC. AND SUBSIDIARIES

## CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

(In thousands)

	Nine months ended September 30,	
	2017	2018
	(unaudited)	
<b>Cash flows from operating activities:</b>		
Net income (loss)	\$68,160	\$(42,098 )
Depreciation and amortization	2,794	2,609
Deferred income taxes	27,924	(16,624 )
Equity in earnings of Kronos Worldwide, Inc.	(93,357 )	(55,029 )
Dividends received from Kronos Worldwide, Inc.	15,849	17,961
Cash funding of benefit plans in excess of net benefit plan expense	(689 )	(2,074 )
Marketable equity securities	-	55,911
Other, net	348	426
<b>Change in assets and liabilities:</b>		
Accounts and other receivables, net	(1,436 )	(18,203 )
Inventories, net	(475 )	(1,935 )
Prepaid expenses and other	70	110
Accounts payable and accrued liabilities	(466 )	62,025
Income taxes	2	11
Accounts with affiliates	(2,062 )	2,939
Accrued environmental remediation and related costs	(1,392 )	(428 )
Other noncurrent assets and liabilities, net	(54 )	16,698
<b>Net cash provided by operating activities</b>	<b>15,216</b>	<b>22,299</b>
<b>Cash flows from investing activities:</b>		
Capital expenditures	(2,152 )	(2,043 )
Promissory notes receivable from affiliate:		
Loans	(49,700 )	(39,000 )
Collections	40,400	44,200
Other, net	4	225
<b>Net cash provided by (used in) investing activities</b>	<b>(11,448 )</b>	<b>3,382</b>
<b>Cash flows from financing activities -</b>		
Distributions to noncontrolling interests in subsidiary	(250 )	(251 )
<b>Cash and cash equivalents and restricted cash and cash equivalents - net</b>		
change from:		
<b>Operating, investing and financing activities</b>	<b>3,518</b>	<b>25,430</b>

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Balance at beginning of period	98,242	102,941
Balance at end of period	\$101,760	\$128,371
Supplemental disclosure - cash paid (received) for:		
Interest	\$22	\$25
Income taxes, net	\$3,085	\$(1,740 )

See accompanying notes to Condensed Consolidated Financial Statements.

NL INDUSTRIES, INC. AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

September 30, 2018

(unaudited)

Note 1 – Organization and basis of presentation:

Organization – At September 30, 2018, Valhi, Inc. (NYSE: VHI) held approximately 83% of our outstanding common stock and a wholly-owned subsidiary of Contran Corporation held approximately 92% of Valhi's outstanding common stock. All of Contran's outstanding voting stock is held by a family trust established for the benefit of Lisa K. Simmons and Serena Simmons Connelly and their children for which Ms. Simmons and Ms. Connelly are co-trustees, or is held directly by Ms. Simmons and Ms. Connelly or entities related to them. Consequently, Ms. Simmons and Ms. Connelly may be deemed to control Contran, Valhi and us.

Basis of presentation – Consolidated in this Quarterly Report are the results of our majority-owned subsidiary, CompX International Inc. We also own 30% of Kronos Worldwide, Inc. (Kronos). CompX (NYSE American: CIX) and Kronos (NYSE: KRO); each file periodic reports with the Securities and Exchange Commission (SEC).

The unaudited Condensed Consolidated Financial Statements contained in this Quarterly Report have been prepared on the same basis as the audited Consolidated Financial Statements in our Annual Report on Form 10-K for the year ended December 31, 2017 that we filed with the SEC on March 12, 2018 (the 2017 Annual Report). In our opinion, we have made all necessary adjustments (which include only normal recurring adjustments) in order to state fairly, in all material respects, our consolidated financial position, results of operations and cash flows as of the dates and for the periods presented. We have condensed the Consolidated Balance Sheet at December 31, 2017 contained in this Quarterly Report as compared to our audited Consolidated Financial Statements at that date, and we have omitted certain information and footnote disclosures (including those related to the Consolidated Balance Sheet at December 31, 2017) normally included in financial statements prepared in accordance with accounting principles generally accepted in the United States of America (GAAP). Our results of operations for the interim periods ended September 30, 2018 may not be indicative of our operating results for the full year. The Condensed Consolidated Financial Statements contained in this Quarterly Report should be read in conjunction with our 2017 Consolidated Financial Statements contained in our 2017 Annual Report.

Unless otherwise indicated, references in this report to “NL,” “we,” “us” or “our” refer to NL Industries, Inc. and its subsidiaries and affiliate, Kronos, taken as a whole.

Note 2 – Accounts and other receivables, net:

December	September
31,	30,
2017	2018

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	(In thousands)	
Trade receivables - CompX	\$10,516	\$ 13,416
Accrued insurance recoveries	145	15,427
Other receivables	79	96
Allowance for doubtful accounts	(70 )	(70 )
Total	\$10,670	\$ 28,869

Accrued insurance recoveries are discussed in Note 14.

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## Note 3 – Inventories, net:

	December 31, 2017	September 30, 2018
	(In thousands)	
Raw materials	\$2,730	\$ 3,001
Work in process	9,836	10,864
Finished products	2,816	3,294
<b>Total</b>	<b>\$ 15,382</b>	<b>\$ 17,159</b>

## Note 4 – Marketable securities:

Our marketable securities consist of investments in the publicly-traded shares of our immediate parent company Valhi, Inc. Prior to 2018, any unrealized gains or losses on the securities were recognized through other comprehensive income, net of deferred income taxes. Beginning on January 1, 2018 with the adoption of Accounting Standards Update (“ASU”) 2016-01, our marketable equity securities will continue to be carried at fair value as noted below, but any unrealized gains or losses on the securities are now recognized as a component of other income included in Marketable equity securities on our Condensed Consolidated Statements of Operations. See Note 16.

	Fair value measurement level	Market value	Cost basis	Unrealized gain
	(In thousands)			
<b>December 31, 2017</b>				
Valhi common stock 1		\$88,681	\$24,347	\$ 64,334
<b>September 30, 2018</b>				
Valhi common stock 1		\$32,770	\$24,347	\$ 8,423

At December 31, 2017 and September 30, 2018, we held approximately 14.4 million shares of common stock of Valhi. See Note 1. Our shares of Valhi common stock are carried at fair value based on quoted market prices, representing a Level 1 input within the fair value hierarchy. At December 31, 2017 and September 30, 2018, the quoted per share market price of Valhi common stock was \$6.17 and \$2.28, respectively. During the first nine months of 2018 we recognized a pre-tax loss of \$55.9 million related to the aggregate net change in market value of our marketable equity securities during such period.

The Valhi common stock we own is subject to the restrictions on resale pursuant to certain provisions of the SEC Rule 144. In addition, as a majority-owned subsidiary of Valhi, we cannot vote our shares of Valhi common stock under Delaware General Corporation Law, but we do receive dividends from Valhi on these shares, when declared and paid.

Note 5 – Investment in Kronos Worldwide, Inc.:

At December 31, 2017 and September 30, 2018, we owned approximately 35.2 million shares of Kronos common stock. At September 30, 2018, the quoted market price of Kronos' common stock was \$16.25 per share, or an aggregate market value of \$572.3 million. At December 31, 2017, the quoted market price was \$25.77 per share, or an aggregate market value of \$907.6 million.

The change in the carrying value of our investment in Kronos during the first nine months of 2018 is summarized below.

	Amount (In millions)
Balance at the beginning of the period	\$ 229.5
Equity in earnings of Kronos	55.0
Dividends received from Kronos	(17.9 )
Equity in Kronos' other comprehensive income:	
Currency translation	(3.0 )
Defined benefit pension plans	2.2
Balance at the end of the period	\$ 265.8

Selected financial information of Kronos is summarized below:

	December 31, 2017	September 30, 2018
	(In millions)	
Current assets	\$ 1,062.5	\$ 1,238.4
Property and equipment, net	506.4	491.9
Investment in TiO <sub>2</sub> joint venture	86.5	79.7
Other noncurrent assets	169.0	124.9
Total assets	\$ 1,824.4	\$ 1,934.9
Current liabilities	\$ 231.5	\$ 249.6
Long-term debt	473.8	465.2
Accrued pension and postretirement benefits	261.9	255.0
Other noncurrent liabilities	102.9	91.7
Stockholders' equity	754.3	873.4
Total liabilities and stockholders' equity	\$ 1,824.4	\$ 1,934.9

	Three months ended September 30, 2017		Nine months ended September 30, 2018	
	2017	2018	2017	2018
	(In millions)			
Net sales	\$464.5	\$410.3	\$1,275.7	\$1,312.5
Cost of sales	309.5	291.2	882.3	846.8

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Income from operations	96.1	58.1	226.8	285.5
Income tax expense (benefit)	6.1	14.1	(114.0 )	75.5
Net income	73.8	32.6	307.1	181.0

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## Note 6 – Other noncurrent assets, net:

	December 31, 2017	September 30, 2018
	(In thousands)	
Restricted cash	\$ 1,255	\$ 1,089
Pension asset	2,593	2,847
Other	995	1,201
<b>Total</b>	<b>\$4,843</b>	<b>\$ 5,137</b>

## Note 7 – Accrued and other current liabilities:

	December 31, 2017	September 30, 2018
	(In thousands)	
Employee benefits	\$8,269	\$ 7,955
Litigation settlement	-	60,000
Other	1,438	2,095
<b>Total</b>	<b>\$9,707</b>	<b>\$ 70,050</b>

See Note 14 for a discussion of the accrued litigation settlement.

## Note 8 – Long-term debt:

During the first nine months of 2018, our wholly owned subsidiary, NLKW Holding, LLC had no borrowings or repayments under its \$50 million secured revolving credit facility with Valhi. At September 30, 2018, we had outstanding borrowings of \$0.5 million under such facility, and the remaining \$49.5 million was available for future borrowing under this facility. Outstanding borrowings under such credit facility bear interest at the prime rate plus 1.875% per annum, and the average interest rate as of and for the nine months ended September 30, 2018 was 7.125% and 6.64%, respectively. We are in compliance with all of the covenants contained in such facility at September 30, 2018.

## Note 9 – Employee benefit plans:

The components of net periodic defined benefit pension cost are presented in the table below.

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	Three months ended September 30, 2017 2018		Nine months ended September 30, 2017 2018	
	(In thousands)			
Interest cost	\$506	\$372	\$1,518	\$1,116
Expected return on plan assets	(689)	(590)	(2,067)	(1,770)
Recognized actuarial losses	394	365	1,182	1,095
<b>Total</b>	<b>\$211</b>	<b>\$147</b>	<b>\$633</b>	<b>\$441</b>

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The components of net periodic postretirement benefits other than pension (OPEB) income are presented in the table below.

	Three months ended September 30, 2017		Nine months ended September 30, 2018	
	2017	2018	2017	2018
	(In thousands)			
Interest cost	\$20	\$15	\$60	\$45
Recognized actuarial gains	(54)	(63)	(162)	(189)
Total	\$(34)	\$(48)	\$(102)	\$(144)

Upon the adoption of ASU 2017-07, Compensation - Retirement Benefits (Topic 715) Improving the Presentation of Net Periodic Pension Cost and Net Periodic Postretirement Benefit Cost, our net periodic defined benefit pension cost and other postretirement benefit cost is presented as a separate line item (“Other components of net periodic pension and OPEB cost”) in our Condensed Consolidated Statements of Operations for all periods presented. See Note 16.

We currently expect our 2018 contributions to our defined benefit pension plans and other postretirement plans to be approximately \$3.4 million.

Note 10 – Other noncurrent liabilities:

	December 31, 2017	September 30, 2018
	(In thousands)	
Reserve for uncertain tax positions	\$7,312	\$7,312
Insurance claims and expenses	620	674
Litigation settlement	-	17,000
Other	560	410
Total	\$8,492	\$25,396

See Note 14 for a discussion of the accrued litigation settlement.

Note 11 – Revenue Recognition

Our sales are conducted through our majority-owned subsidiary CompX and involve single performance obligations to ship our products pursuant to customer purchase orders. In some cases, the purchase order is supported by an underlying master sales agreement, but the purchase order acceptance generally evidences the contract with our customer by specifying the key terms of product and quantity ordered, price and delivery and payment terms. Effective January 1, 2018 with the adoption of ASU No. 2014-09, Revenue from Contracts with Customers (Topic 606), see Note 16, we record revenue when we satisfy our performance obligations to our customers by transferring control of our products to them, which generally occurs at point of shipment or upon delivery. Such transfer of control is also evidenced by transfer of legal title and other risks and rewards of ownership (giving the customer the ability to direct the use of, and obtain substantially all of the benefits of, the product), and our customers becoming obligated to pay us and such payment being probable of occurring. In certain arrangements we provide shipping and handling activities after the transfer of control to our customer (e.g. when control transfers prior to delivery). In such arrangements shipping and handling are considered fulfillment activities, and accordingly, such costs are accrued when the related revenue is recognized.

Revenue is recorded in an amount that reflects the net consideration we expect to receive in exchange for our products. Prices for our products are based on terms specified in published list prices and purchase orders,

which generally do not include financing components, noncash consideration or consideration paid to our customers. As our standard payment terms are less than one year, we have elected the practical expedient under ASC 606 and we have not assessed whether a contract has a significant financing component. We state sales net of price, early payment and distributor discounts as well as volume rebates (collectively, variable consideration). Variable consideration, to the extent present, is not material and is recognized as the amount to which we are most-likely to be entitled, using all information (historical, current and forecasted) that is reasonably available to us, and only to the extent that a significant reversal in the amount of the cumulative revenue recognized is not probable of occurring in a future period. Differences, if any, between estimates of the amount of variable consideration to which we will be entitled and the actual amount of such variable consideration have not been material in the past. We report any tax assessed by a governmental authority that we collect from our customers that is both imposed on and concurrent with our revenue-producing activities (such as sales, use, value added and excise taxes) on a net basis (meaning we do not recognize these taxes either in our revenues or in our costs and expenses).

Frequently, we receive orders for products to be delivered over dates that may extend across reporting periods. We invoice for each delivery upon shipment and recognize revenue for each distinct shipment when all sales recognition criteria for that shipment have been satisfied. As scheduled delivery dates for these orders are within a one year period, under the optional exemption provided by ASC 606, we do not disclose sales allocated to future shipments of partially completed contracts.

The following table disaggregates our net sales by reporting unit, which are the categories that depict how the nature, amount, timing and uncertainty of revenue and cash flows are affected by economic factors (as required by ASC 606).

	Three months ended September 30, 2017		2018		Nine months ended September 30, 2017		2018	
	(In thousands)							
Net Sales:								
Security Products	\$22,854	\$24,541	\$74,903	\$75,845				
Marine Components	4,139	5,488	12,040	14,982				
Total	\$26,993	\$30,029	\$86,943	\$90,827				

## Note 12 – Income taxes:

	Three months ended September 30,		Nine months ended September 30,	
	2017	2018	2017	2018
Expected tax expense (benefit), at U.S. federal statutory income tax rate of 35% in 2017 and 21% in 2018	\$8.5	\$(4.4)	\$34.0	\$(12.1)
Rate differences on equity in earnings of Kronos	(2.1)	(1.9)	(5.0)	(4.3)
Nontaxable income	(.1)	-	(.3)	(.2)
U.S. state income taxes and other, net	.2	.2	.2	1.2
<b>Income tax expense (benefit)</b>	<b>\$6.5</b>	<b>\$(6.1)</b>	<b>\$28.9</b>	<b>\$(15.4)</b>
<b>Comprehensive provision for income taxes</b>				
<b>(benefit) allocable to:</b>				
Net income (loss)	\$6.5	\$(6.1)	\$28.9	\$(15.4)
<b>Other comprehensive income (loss):</b>				
Marketable securities	(2.8)	-	(5.3)	-
Currency translation	3.1	.3	5.7	(.6)
Interest rate swap	.2	-	.2	-
Pension plans	.4	.3	1.1	.8
OPEB plans	(.1)	(.1)	(.1)	(.1)
<b>Total</b>	<b>\$7.3</b>	<b>\$(5.6)</b>	<b>\$30.5</b>	<b>\$(15.3)</b>

In accordance with GAAP, we recognize deferred income taxes on our undistributed equity in earnings (losses) of Kronos. Because we and Kronos are part of the same U.S. federal income tax group, any dividends we receive from Kronos are nontaxable to us. Accordingly, we do not recognize and we are not required to pay income taxes on dividends from Kronos. We received aggregate dividends from Kronos of \$15.8 million in the first nine months of 2017 and \$18.0 million in the first nine months of 2018. The amounts shown in the above table of our income tax rate reconciliation for rate differences on equity in earnings of Kronos represents the net tax (benefit) associated with such non-taxability of the dividends we receive from Kronos, as it relates to the amount of deferred income taxes we recognize on our undistributed equity in earnings (losses) of Kronos and the result determined by multiplying the pre-tax earnings or losses of each of our non-U.S. subsidiaries by the difference between the applicable statutory income tax rate for each non-U.S. jurisdiction.

As discussed in the 2017 Annual Report, on December 22, 2017, H.R.1, formally known as the “Tax Cuts and Jobs Act” (“2017 Tax Act”) was enacted into law. This new tax legislation among other changes, (i) reduced the U.S. Federal corporate income tax rate from 35% to 21% effective January 1, 2018; (ii) eliminated the domestic production activities deduction beginning in 2018; and (iii) allows for the expensing of certain capital expenditures. Following the enactment of the 2017 Tax Act, the Securities and Exchange Commission issued Staff Accounting Bulletin (SAB) 118 to provide guidance on the accounting and reporting impacts of the 2017 Tax Act. SAB 118 states that companies should account for changes related to the 2017 Tax Act in the period of enactment if all information is available and the accounting can be completed. In situations where companies do not have enough information to complete the accounting in the period of enactment, a company must either 1) record an estimated provisional amount if the impact of the change can be reasonably estimated; or 2) continue to apply the accounting guidance that was in effect immediately prior to the 2017 Tax Act if the impact of the change cannot be reasonably estimated. If estimated provisional amounts are recorded, SAB 118 provides a measurement period of no longer than one year during which companies should adjust those amounts as additional information becomes available in the reporting period within the measurement period in which such adjustment is determined.

Under GAAP, we are required to revalue our net deferred tax liability associated with our U.S. net taxable temporary differences in the period in which the new tax legislation is enacted based on deferred tax balances as of the enactment date, to reflect the effect of such reduction in the corporate income tax rate. Other than with respect to temporary differences related to our marketable securities, and certain year-end actuarial valuations associated with our defined benefit pension and OPEB plans, our temporary differences as of December 31, 2017 were not materially different from our temporary differences as of the enactment date, accordingly revaluation of our net taxable temporary differences was based on our net deferred tax liability as of December 31, 2017 (except for our temporary differences related to our marketable securities, and certain year-end actuarial valuations associated with our defined benefit pension and OPEB plans, for which such revaluation was based on the deferred income tax asset/liability as of enactment date). Such revaluation resulted in a non-cash deferred income tax benefit of \$37.5 million recognized as of December 31, 2017 in continuing operations, reducing our net deferred income tax liability. The amounts recorded as of December 31, 2017 as a result of the 2017 Tax Act represent estimates based on information currently available. We did not make any additional measurement-period adjustments to the provisional amounts recorded for this item during the first six months of 2018, as we were still waiting on additional guidance that might impact the income tax effects of the new legislation recognized at December 31, 2017. During the third quarter of 2018, in conjunction with finalizing our federal income tax return, we were able to obtain, prepare and analyze the necessary information to complete the accounting under ASC 740 related to the revaluation of our net deferred tax liability associated with our U.S. net taxable temporary differences as of December 31, 2017, which resulted in the recognition of an immaterial adjustment to the provisional amount recognized at December 31, 2017. Accordingly, we have completed our analysis related to such revaluation as of September 30, 2018.

#### Income tax matters related to Kronos

Kronos has substantial net operating loss (NOL) carryforwards in Germany (the equivalent of \$652 million for Kronos' German corporate purposes and \$.5 million for German trade tax purposes at December 31, 2017) and in Belgium (the equivalent of \$50 million for Kronos' Belgian corporate tax purposes at December 31, 2017), all of which have an indefinite carryforward period. As a result, Kronos has net deferred income tax assets with respect to these two jurisdictions, primarily related to these NOL carryforwards. The German corporate tax is similar to the U.S. federal income tax, and the German trade tax is similar to the U.S. state income tax. As discussed in the 2017 Annual Report, commencing June 30, 2015, Kronos concluded that it was required to recognize a non-cash deferred income tax asset valuation allowance under the more-likely-than-not recognition criteria with respect to its German and Belgian net deferred income tax assets at such date. During the first six months of 2017, Kronos recognized an aggregate non-cash deferred income tax benefit of \$12.7 million as a result of a net decrease in such deferred income tax asset valuation allowance, due to utilizing a portion of both the German and Belgian NOL during the period, including \$7.7 million in the second quarter of 2017. As also discussed in the 2017 Annual Report, at June 30, 2017, Kronos concluded it had sufficient positive evidence under the more-likely-than-not recognition criteria to support reversal of the entire valuation allowance related to its German and Belgian operations. In accordance with the ASC 740-270 guidance regarding accounting for income taxes at interim dates, the amount of the valuation allowance reversed at June 30, 2017 (\$149.9 million, of which \$141.9 million related to Germany and \$8.0 million related to Belgium) relates to Kronos' change in judgment at that date regarding the realizability of the related deferred income tax asset as it relates to future years (i.e., 2018 and after). A change in judgment regarding the realizability of deferred tax assets as it relates to the current year is considered in determining the estimated annual effective tax rate for the year and is recognized throughout the year, including interim periods subsequent to the date of the change in judgment. Accordingly, Kronos' income tax benefit in calendar 2017 includes an aggregate non-cash deferred income tax benefit of \$186.7 million related to the reversal of the German and Belgian valuation allowance, comprised of



\$12.7 million recognized in the first half of 2017 (noted above) related to the utilization of a portion of both the German and Belgian NOLs during such period, \$149.9 million related to the portion of the valuation allowance reversed as of June 30, 2017 and \$24.1 million recognized in the second half of 2017 (including \$7.8 million reversed in the third quarter) related to the utilization of a portion of both the German and Belgian NOLs during such period. Kronos' deferred income tax asset valuation allowance increased \$13.7 million in 2017 as a result of changes in currency exchange rates, which increase was recognized as part of other comprehensive income (loss).

Prior to the enactment of the 2017 Tax Act, the undistributed earnings of Kronos' European subsidiaries were deemed to be permanently reinvested (Kronos had not made a similar determination with respect to the undistributed

earnings of its Canadian subsidiary). Pursuant to the Transition Tax provisions imposing a one-time repatriation tax on post-1986 undistributed earnings, Kronos recognized a provisional current income tax expense of \$76.2 million in the fourth quarter of 2017. The amounts recorded as of December 31, 2017 as a result of the 2017 Tax Act represent estimates based on information currently available. Kronos elected to pay such tax over an eight year period beginning in 2018, including approximately \$6.1 million which was paid in April 2018 (for the 2017 tax year) and \$4.6 million which was paid in the second and third quarters of 2018 (for the 2018 tax year). Kronos did not make any measurement-period adjustments to the provisional amounts recorded for this item during the first six months of 2018 because no new information became available during the period that required an adjustment. During the third quarter of 2018, in conjunction with finalizing Kronos' federal income tax return and based on additional information that became available (including proposed regulations issued by the IRS in August 2018 with respect to the Transition Tax), Kronos recognized a provisional income tax benefit of \$1.7 million which amount is recorded as a measurement-period adjustment, reducing the provisional income tax expense of \$76.2 million recognized in the fourth quarter of 2017. As a result, at September 30, 2018, taking into account the prior Transition Tax installments payments of \$10.7 million (noted above), the balance of Kronos' unpaid Transition Tax aggregates \$63.8 million, which will be paid in quarterly installments over the remainder of the eight year period. Of the \$63.8 million, \$58.1 million is recorded as a noncurrent payable to affiliate (income taxes payable to Valhi) and \$5.7 million is included with Kronos' current payable to affiliate (income taxes payable to Valhi) classified as a current liability. The issuance of final regulations and/or additional guidance with respect to the Transition Tax may impact the amount of the Transition Tax recognized in the fourth quarter of 2017, as adjusted in the third quarter of 2018. Kronos continues to gather information and is awaiting further guidance from the state jurisdictions in which Kronos operates with respect to the Transition Tax. Kronos will complete its accounting for this item within the prescribed measurement period ending December 22, 2018, pursuant to the guidance under SAB 118, and if Kronos determines an adjustment to the provisional amount recognized at December 31, 2017 is required, Kronos will recognize such adjustment in the reporting period within the SAB 118 measurement period in which such adjustment is determined.

Prior to the enactment of the 2017 Tax Act the undistributed earnings of Kronos' European subsidiaries were deemed to be permanently reinvested (Kronos had not made a similar determination with respect to the undistributed earnings of its Canadian subsidiary). As a result of the implementation of a territorial tax system under the 2017 Tax Act, effective January 1, 2018, and the Transition Tax which in effect taxes the post-1986 undistributed earnings of Kronos' non-U.S. subsidiaries accumulated up through December 31, 2017, Kronos determined effective December 31, 2017 that all of the post-1986 undistributed earnings of its European subsidiaries are not permanently reinvested. Accordingly, in the fourth quarter of 2017 Kronos recognized an aggregate provisional non-cash deferred income tax expense of \$4.5 million based on its reasonable estimates of the U.S. state and non-U.S. income tax and withholding tax liability attributable to all of such previously-considered permanently reinvested undistributed earnings through December 31, 2017. The amounts recorded as of December 31, 2017 as a result of the 2017 Tax Act represent estimates based on information currently available. Kronos has not made any measurement-period adjustments to the provisional amounts recorded at December 31, 2017 for this item during the first nine months of 2018. However, Kronos recorded a provisional non-cash deferred income tax expense of \$2.5 million for the estimated U.S. state and non-U.S. income tax and withholding tax liability attributable to the 2018 undistributed earnings of its non-U.S. subsidiaries in the first nine months of 2018, including withholding taxes related to the undistributed earnings of Kronos's Canadian subsidiary. Kronos is continuing its review of certain other provisions under the 2017 Tax Act and waiting on further guidance, primarily from the state jurisdictions in which it operates, that may impact its determination of the aggregate temporary differences attributable to its investments in its non-U.S. subsidiaries. Kronos will complete its accounting for this item within the prescribed measurement period ending December 22, 2018, pursuant to the guidance under SAB 118, and if Kronos determines an adjustment to the provisional amount recognized at December 31, 2017 and September 30, 2018 are required, Kronos will recognize such adjustment in the reporting period within the SAB 118 measurement period in which such adjustment is determined.

Under U.S. GAAP, as it relates to the new GILTI tax rules, Kronos is allowed to make an accounting policy choice of either (1) treating taxes due on future U.S. inclusions in taxable income related to GILTI as a current-period expense when incurred (the “period cost method”) or (2) factoring such amounts into the measurement of our deferred taxes (the “deferred method”). Kronos’ selection of an accounting policy related to the GILTI tax provisions will depend, in part, on analyzing our global income to determine whether it expects to have future U.S. inclusions in taxable income related to GILTI and, if so, what the impact is expected to be. While Kronos’ future global operations depend on a number of different factors, Kronos does expect to have future U.S. inclusions in

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taxable income related to GILTI. As such, Kronos has performed an analysis of GILTI's impact on its provision and determined the impact is not material. Because the impact is not material to its tax provision, Kronos has not recorded any adjustments related to potential GILTI tax in its financial statements in the first nine months of 2018. Further, Kronos has not made a policy decision regarding whether to record deferred taxes on GILTI or record GILTI tax as a current-period expense when incurred. Kronos will complete its policy election for this item within the prescribed measurement period ending December 22, 2018, pursuant to the guidance under SAB 118 and if Kronos determines such policy election impacts its provision, it will recognize an adjustment in the reporting period within the SAB 118 measurement period in which such adjustment is determined. Similarly, Kronos has evaluated the tax impact of BEAT on its tax provision in the first nine months of 2018 and determined that the tax law has no material impact on its tax provision as it has historically not entered into international payments between related parties that are unrelated to cost of goods sold.

None of Kronos U.S. and non-U.S. tax returns are currently under examination. As a result of prior audits in certain jurisdictions, which are now settled, in 2008 Kronos filed Advance Pricing Agreement Requests with the tax authorities in the U.S., Canada and Germany. These requests have been under review with the respective tax authorities since 2008 and prior to 2016, it was uncertain whether an agreement would be reached between the tax authorities and whether Kronos would agree to execute and finalize such agreements.

During the third quarter of 2017, Kronos' Canadian subsidiary executed and finalized an Advance Pricing Agreement with the Competent Authority for Canada (the "Canada-Germany APA") effective for tax years 2005 - 2017. Pursuant to the terms of the Canada-Germany APA, the Canadian and German tax authorities agreed to certain prior year changes to taxable income of our Canadian and German subsidiaries. As a result of such agreed-upon changes, Kronos reversed a significant portion of its reserve for uncertain tax positions and recognized a non-cash income tax benefit of \$8.1 million related to such reversal in the third quarter of 2017. In addition, Kronos recognized a \$2.6 million non-cash income tax benefit related to an increase in its German NOLs and a \$.6 million German cash tax refund related to the Canada-Germany APA in the third quarter of 2017.

During the first quarter of 2018, Kronos' German subsidiary executed and finalized the related Advance Pricing Agreement with the Competent Authority for Germany (the "Germany- Canada APA") effective for tax years 2005 - 2017. In the first quarter of 2018, Kronos recognized a net \$1.4 million non-cash income tax benefit related to an APA tax settlement payment between its German and Canadian subsidiaries.

Note 13 – Accumulated other comprehensive income (loss):

Changes in accumulated other comprehensive income (loss) attributable to NL stockholders, including amounts resulting from our investment in Kronos Worldwide (see Note 5), are presented in the table below.

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	Three months ended		Nine months ended	
	September 30,		September 30,	
	2017	2018	2017	2018
	(In thousands)			
Accumulated other comprehensive loss, net of tax:				
Marketable securities:				
Balance at beginning of period	\$ 15,882	\$-	\$ 20,473	\$ 46,069
Change in accounting principle	-	-	-	(46,069 )
Balance at beginning of period, as adjusted	\$ 15,882	\$-	\$ 20,473	\$-
Other comprehensive loss -				
unrealized losses arising				
during the year	(5,260 )	-	(9,851 )	-
Balance at end of period	\$ 10,622	\$-	\$ 10,622	\$-
Currency translation:				
Balance at beginning of period	\$(171,163)	\$(167,984)	\$(175,859)	\$(164,467)
Other comprehensive income (loss)	5,908	1,103	10,604	(2,414 )
Balance at end of period	\$(165,255)	\$(166,881)	\$(165,255)	\$(166,881)
Interest rate swap:				
Balance at beginning of period	\$(362 )	\$-	\$(390 )	\$-
Other comprehensive income (loss):				
Unrealized losses arising				
during the year	(119 )	-	(296 )	-
Less reclassification adjustment for				
amounts included in interest expense	481	-	686	-
Balance at end of period	\$-	\$-	\$-	\$-
Defined benefit pension plans:				
Balance at beginning of period	\$(75,450 )	\$(70,994 )	\$(76,710 )	\$(72,951 )
Other comprehensive income -				
amortization of net losses included				
in net periodic pension cost	738	959	1,998	2,916
Balance at end of period	\$(74,712 )	\$(70,035 )	\$(74,712 )	\$(70,035 )
OPEB plans:				
Balance at beginning of period	\$(456 )	\$(526 )	\$(360 )	\$(388 )
Other comprehensive loss -	(49 )	(65 )	(145 )	(203 )

amortization of net gains included in net periodic OPEB cost

Balance at end of period	\$ (505 )	\$ (591 )	\$ (505 )	\$ (591 )
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Total accumulated other comprehensive loss:

Balance at beginning of period	\$ (231,549)	\$ (239,504)	\$ (232,846)	\$ (191,737)
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Change in accounting principle	-	-	-	(46,069 )
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Balance at beginning of period, as adjusted	\$ (231,549)	\$ (239,504)	\$ (232,846)	\$ (237,806)
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Other comprehensive income	1,699	1,997	2,996	299
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Balance at end of period	\$ (229,850)	\$ (237,507)	\$ (229,850)	\$ (237,507)
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See Note 9 for amounts related to our defined benefit pension plans and OPEB plans.

Note 14 – Commitments and contingencies:

General

We are involved in various environmental, contractual, product liability, patent (or intellectual property), employment and other claims and disputes incidental to our current and former businesses. At least quarterly our management discusses and evaluates the status of any pending litigation or claim to which we are a party or which has been asserted against us. The factors considered in such evaluation include, among other things, the nature of such pending cases and claims, the status of such pending cases and claims, the advice of legal counsel and our experience in similar cases and claims (if any). Based on such evaluation, we make a determination as to whether we believe (i) it is probable a loss has been incurred, and if so if the amount of such loss (or a range of loss) is reasonably estimable, or (ii) it is reasonably possible but not probable a loss has been incurred, and if so if the amount of such loss (or a range of loss) is reasonably estimable, or (iii) the probability a loss has been incurred is remote.

Lead pigment litigation

Our former operations included the manufacture of lead pigments for use in paint and lead-based paint. We, other former manufacturers of lead pigments for use in paint and lead-based paint (together, the “former pigment manufacturers”), and the Lead Industries Association (LIA), which discontinued business operations in 2002, have been named as defendants in various legal proceedings seeking damages for personal injury, property damage and governmental expenditures allegedly caused by the use of lead-based paints. Certain of these actions have been filed by or on behalf of states, counties, cities or their public housing authorities and school districts, and certain others have been asserted as class actions. These lawsuits seek recovery under a variety of theories, including public and private nuisance, negligent product design, negligent failure to warn, strict liability, breach of warranty, conspiracy/concert of action, aiding and abetting, enterprise liability, market share or risk contribution liability, intentional tort, fraud and misrepresentation, violations of state consumer protection statutes, supplier negligence and similar claims.

The plaintiffs in these actions generally seek to impose on the defendants responsibility for lead paint abatement and health concerns associated with the use of lead-based paints, including damages for personal injury, contribution and/or indemnification for medical expenses, medical monitoring expenses and costs for educational programs. To the extent the plaintiffs seek compensatory or punitive damages in these actions, such damages are generally unspecified. In some cases, the damages are unspecified pursuant to the requirements of applicable state law. A number of cases are inactive or have been dismissed or withdrawn. Most of the remaining cases are in various pre-trial stages. Some are on appeal following dismissal or summary judgment rulings or a trial verdict in favor of either the defendants or the plaintiffs.

We believe that these actions are without merit, and we intend to continue to deny all allegations of wrongdoing and liability and to defend against all actions vigorously. Other than with respect to the Santa Clara case discussed below, we do not believe it is probable that we have incurred any liability with respect to all of the lead pigment litigation cases to which we are a party, and with respect to all such lead pigment litigation cases to which we are a party, other than with respect to the Santa Clara case discussed below, we believe liability to us that may result, if any, in this regard cannot be reasonably estimated, because:

- we have never settled any of the market share, intentional tort, fraud, nuisance, supplier negligence, breach of warranty, conspiracy, misrepresentation, aiding and abetting, enterprise liability, or statutory cases (subject to the final outcome of the Santa Clara case discussed below),
- no final, non-appealable adverse verdicts have ever been entered against NL (subject to the final outcome of the Santa Clara case discussed below), and

•we have never ultimately been found liable with respect to any such litigation matters, including over 100 cases over a twenty-year period for which we were previously a party and for which we have been dismissed without any finding of liability (subject to the final outcome of the Santa Clara case discussed below).



Accordingly, other than with respect to the Santa Clara case discussed below, we have not accrued any amounts for any of the pending lead pigment and lead-based paint litigation cases filed by or on behalf of states, counties, cities or their public housing authorities and school districts, or those asserted as class actions other than the Santa Clara case noted below. In addition, we have determined that liability to us which may result, if any, cannot be reasonably estimated at this time because there is no prior history of a loss of this nature on which an estimate could be made and there is no substantive information available upon which an estimate could be based.

In one of these lead pigment cases, in April 2000 we were served with a complaint in County of Santa Clara v. Atlantic Richfield Company, et al. (Superior Court of the State of California, County of Santa Clara, Case No. 1-00-CV-788657) brought by a number of California government entities against the former pigment manufacturers, the LIA and certain paint manufacturers. The County of Santa Clara sought to recover compensatory damages for funds the plaintiffs have expended or would in the future expend for medical treatment, educational expenses, abatement or other costs due to exposure to, or potential exposure to, lead paint, disgorgement of profit, and punitive damages. In July 2003, the trial judge granted defendants' motion to dismiss all remaining claims. Plaintiffs appealed and the intermediate appellate court reinstated public nuisance, negligence, strict liability, and fraud claims in March 2006. A fourth amended complaint was filed in March 2011 on behalf of The People of California by the County Attorneys of Alameda, Ventura, Solano, San Mateo, Los Angeles and Santa Clara, and the City Attorneys of San Francisco, San Diego and Oakland. That complaint alleged that the presence of lead paint created a public nuisance in each of the prosecuting jurisdictions and sought its abatement. In July and August 2013, the case was tried. In January 2014, the Judge issued a judgment finding us, The Sherwin Williams Company and ConAgra Grocery Products Company jointly and severally liable for the abatement of lead paint in pre-1980 homes, and ordered the defendants to pay an aggregate \$1.15 billion to the people of the State of California to fund such abatement. The trial court's judgment also found that to the extent any abatement funds remained unspent after four years, such funds were to be returned to the defendants. In February 2014, we filed a motion for a new trial, and in March 2014 the trial court denied the motion. Subsequently in March 2014, we filed a notice of appeal with the Sixth District Court of Appeal for the State of California. On November 14, 2017, the Sixth District Court of Appeal issued its opinion, upholding the trial court's judgment, except that it reversed the portion of the judgment requiring abatement of homes built between 1951 and 1980 which significantly reduced the number of homes subject to the abatement order. In addition, the appellate court ordered the case be remanded to the trial court to recalculate the amount of the abatement fund, to limit it to the amount necessary to cover the cost of investigating and remediating pre-1951 homes, and to hold an evidentiary hearing to appoint a suitable receiver. In addition, the appellate court found that we and the other defendants had the right to seek recovery from liable parties that contributed to a hazardous condition at a particular property. Subsequently, we and the other defendants filed a Petition with the California Supreme Court seeking its review of a number of issues. On February 14, 2018, the California Supreme Court denied such petition. In July 2018, we and the other defendants filed appeals with the U.S. Supreme Court, seeking its review of two federal issues in the trial court's original judgment. Review by the U.S. Supreme Court is discretionary, and in October 2018 the U.S. Supreme Court denied the petitions for the Court to hear such appeals.

Under such remand ordered by the appellate court, the trial court would, among other things, (i) recalculate the amount of the abatement fund, excluding remediation of homes built between 1951 and 1980, (ii) hold an evidentiary hearing to appoint a suitable receiver for the abatement fund and (iii) enter an order setting forth its rulings on these issues. We believe any party will have a right to appeal any of these new decisions to be made by the trial court from the remand of the case. Several uncertainties exist with respect to the new decisions to be made by the trial court from the remand of the case, including the following:

•The appellate court remanded the case back to the trial court to recalculate the total amount of the abatement, limiting the abatement to pre-1951 homes. In this regard, NL and the other defendants filed a brief with the trial court proposing a recalculated maximum abatement fund amount of no more than \$409 million and plaintiffs filed a brief proposing an abatement fund amount of \$730 million. In September 2018, following a case-management hearing regarding the recalculated abatement fund amount held in August 2018, the trial court issued an order setting the recalculated amount of the abatement fund at \$409 million;

•The appellate court upheld NL's and the other defendants' right to seek contribution from other liable parties (e.g. property owners who have violated the applicable housing code) on a house-by-house basis.

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The method by which the trial court would undertake to determine such house-by-house responsibility, and the outcome of such a house-by-house determination, is not presently known;

• Participation in any abatement program by each homeowner is voluntary, and each homeowner would need to consent to allowing someone to come into the home to undertake any inspection and abatement, as well as consent to the nature, timing and extent of any abatement. The original trial court's judgment unrealistically assumed 100% participation by the affected homeowners. Actual participation rates are likely to be less than 100% (the ultimate extent of participation is not presently known);

• The remedy ordered by the trial court is an abatement fund. The trial court ordered that any funds unspent after four years are to be returned to the defendants (this provision of the trial court's original judgment was not overturned by the appellate court). As noted above, the actual number of homes which would participate in any abatement, and the nature, timing and extent of any such abatement, is not presently known; and

• We and the other two defendants are jointly and severally liable for the abatement, we do not believe any individual defendant would be 100% responsible for the cost of any abatement, and the allocation of the recalculated amount of the abatement fund (\$409 million) among the three defendants has not yet been determined.

In May 2018, we and the plaintiffs entered into a settlement agreement pursuant to which, as supplemented, the plaintiffs would be paid an aggregate of \$80 million, in return for which we would be dismissed from the case with prejudice and all pending and future claims, causes of action, cross-complaints, actions or proceedings against us and our affiliates for indemnity, contribution, reimbursement or declaratory relief in respect to the case would be barred, discharged and enjoined as a matter of applicable law. Of such \$80 million, \$65 million would be paid by us and \$15 million would be provided by one of our former insurance carriers that has previously placed such amount on deposit with the trial court in satisfaction of potential liability such former carrier might have with respect to the case under certain insurance policies we had with such former carrier. Of such \$65 million which would be paid by us, \$45 million would be paid upon approval of the terms of the settlement, and the remaining \$20 million would be paid in five annual installments beginning four years from such approval (\$6 million for the first installment, \$5 million for the second installment and \$3 million for each of the third, fourth and fifth installments). The settlement agreement is subject to a number of conditions including the trial court's approval of the terms of the settlement (which trial court approval includes a determination that such settlement agreement meets the standards for a "good faith" settlement under applicable California law). The other defendants filed motions with the trial court objecting to the terms of the settlement. In September 2018, the trial court denied approval of the settlement agreement, finding among other things that the settlement agreement did not meet the standards for a "good faith" settlement under applicable California law. Subsequently in October 2018, we filed an appeal of the trial court's denial of approval of the settlement agreement with the Sixth District Court of Appeal for the State of California, asserting among other things that in denying such approval the trial court made several legal errors in applying applicable California law to the terms of the settlement. The appellate court has discretion whether to hear such appeal, and the time for the appellate court to determine if it will hear such appeal has not yet run. There can be no assurance that the appellate court will agree to hear such appeal, or if it agrees to hear such appeal, that it would rule in favor of us and approve the settlement agreement. We continue to believe the settlement agreement satisfies the standards for a "good faith" settlement under applicable California law.

The Santa Clara case is unusual in that this is the second time that an adverse verdict in the lead pigment litigation has been entered against us (the first adverse verdict against us was ultimately overturned on appeal). Given the appellate court's November 2017 ruling, and the denial of an appeal by the California Supreme Court, we have concluded that the likelihood of a loss in this case has reached a standard of "probable" as contemplated by ASC 450. With all of the uncertainties that exist with respect to the new decisions to be made by the trial court from the remand of the case, as noted above, we had previously concluded that the amount of such loss could not be reasonably estimated (nor could a range of loss be reasonably estimated). However, the terms of the settlement agreement entered into by us and the plaintiffs in May 2018, as supplemented, provides evidence that the amount of the loss to us could be reasonably estimated (and provides evidence of the low end of a range of loss to us). For financial reporting purposes, we discounted the five payments aggregating \$20 million to be paid in installments to their estimated net present value,

using a discount rate of 3.0% per annum. Such net present value is \$17 million, and we would begin to accrete such present value amount upon approval of the settlement agreement. Accordingly, in the second quarter of 2018 we recognized a net \$62 million pre-tax charge with respect to this matter (\$45 million for the amount to be paid by us upon approval of the terms of the settlement and \$17 million for the net present

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value of the five payments aggregating \$20 million to be paid by us in installments beginning four years from such approval), representing the net amount we would pay in full settlement of our liability under the terms of the proposed settlement agreement. For purposes of our condensed consolidated balance sheet, we have presented the aggregate \$45 million that would be paid to the plaintiffs upon approval of the terms of the settlement and the \$15 million that would be paid to the plaintiffs from the amount placed as deposit with the trial court by one of our former insurance carriers as a current liability, \$17 million for the net present value of the five payments aggregating \$20 million to be paid by us in installments beginning four years from such approval as a noncurrent liability and the \$15 million portion of such aggregate \$80 million undiscounted amount which would be funded from the amount placed on deposit with the trial court by one of our former insurance carriers as a current insurance recovery receivable. See Notes 2, 7 and 10.

Although, we and the plaintiffs believed the settlement met all requirements of applicable California law, the trial court denied our motion for approval of a good faith settlement, and there can be no assurance that appellate court will reverse that decision and approve the terms of this or any other settlement agreement between us and the plaintiffs. If the appellate court does not reverse the trial court decision and approve the terms of this or any other settlement agreement between us and the plaintiffs, the proceedings in the trial court under the remand, as discussed above, would continue. In such event, NL's share of the recalculated amount of the abatement fund is not presently known, and other uncertainties exist with respect to the new decisions to be made by the trial court from the remand of the case, as discussed above. As with any legal proceeding, there is no assurance that any appeal would be successful, and it is reasonably possible, based on the outcome of the appeals process and the remand proceedings in the trial court, that NL may in the future incur some liability resulting in the recognition of an additional loss contingency accrual that could have a material adverse impact on our results of operations, financial position and liquidity.

New cases may continue to be filed against us. We cannot assure you that we will not incur liability in the future in respect of any of the pending or possible litigation in view of the inherent uncertainties involved in court and jury rulings. In the future, if new information regarding such matters becomes available to us (such as a final, non-appealable adverse verdict against us or otherwise ultimately being found liable with respect to such matters), at that time we would consider such information in evaluating any remaining cases then-pending against us as to whether it might then have become probable we have incurred liability with respect to these matters, and whether such liability, if any, could have become reasonably estimable. The resolution of any of these cases could result in the recognition of a loss contingency accrual that could have a material adverse impact on our net income for the interim or annual period during which such liability is recognized and a material adverse impact on our consolidated financial condition and liquidity.

#### Environmental matters and litigation

Our operations are governed by various environmental laws and regulations. Certain of our businesses are and have been engaged in the handling, manufacture or use of substances or compounds that may be considered toxic or hazardous within the meaning of applicable environmental laws and regulations. As with other companies engaged in similar businesses, certain of our past and current operations and products have the potential to cause environmental or other damage. We have implemented and continue to implement various policies and programs in an effort to minimize these risks. Our policy is to maintain compliance with applicable environmental laws and regulations at all of our plants and to strive to improve environmental performance. From time to time, we may be subject to environmental regulatory enforcement under U.S. and non-U.S. statutes, the resolution of which typically involves the establishment of compliance programs. It is possible that future developments, such as stricter requirements of environmental laws and enforcement policies, could adversely affect our production, handling, use, storage, transportation, sale or disposal of such substances. We believe that all of our facilities are in substantial compliance with applicable environmental laws.

Certain properties and facilities used in our former operations, including divested primary and secondary lead smelters and former mining locations, are the subject of civil litigation, administrative proceedings or investigations arising under federal and state environmental laws and common law. Additionally, in connection with past operating practices, we are currently involved as a defendant, potentially responsible party (PRP) or both, pursuant to the Comprehensive Environmental Response, Compensation and Liability Act, as amended by the Superfund Amendments and Reauthorization Act (CERCLA), and similar state laws in various governmental and

private actions associated with waste disposal sites, mining locations, and facilities that we or our predecessors, our subsidiaries or their predecessors currently or previously owned, operated or used, certain of which are on the United States Environmental Protection Agency's (EPA) Superfund National Priorities List or similar state lists. These proceedings seek cleanup costs, damages for personal injury or property damage and/or damages for injury to natural resources. Certain of these proceedings involve claims for substantial amounts. Although we may be jointly and severally liable for these costs, in most cases we are only one of a number of PRPs who may also be jointly and severally liable, and among whom costs may be shared or allocated. In addition, we are occasionally named as a party in a number of personal injury lawsuits filed in various jurisdictions alleging claims related to environmental conditions alleged to have resulted from our operations.

Obligations associated with environmental remediation and related matters are difficult to assess and estimate for numerous reasons including the:

- complexity and differing interpretations of governmental regulations,
- number of PRPs and their ability or willingness to fund such allocation of costs,
- financial capabilities of the PRPs and the allocation of costs among them,
- solvency of other PRPs,
- multiplicity of possible solutions,
  - number of years of investigatory, remedial and monitoring activity required,
- uncertainty over the extent, if any, to which our former operations might have contributed to the conditions allegedly giving rise to such personal injury, property damage, natural resource and related claims and
- number of years between former operations and notice of claims and lack of information and documents about the former operations.

In addition, the imposition of more stringent standards or requirements under environmental laws or regulations, new developments or changes regarding site cleanup costs or the allocation of costs among PRPs, solvency of other PRPs, the results of future testing and analysis undertaken with respect to certain sites or a determination that we are potentially responsible for the release of hazardous substances at other sites, could cause our expenditures to exceed our current estimates. We cannot assure you that actual costs will not exceed accrued amounts or the upper end of the range for sites for which estimates have been made, and we cannot assure you that costs will not be incurred for sites where no estimates presently can be made. Further, additional environmental and related matters may arise in the future. If we were to incur any future liability, this could have a material adverse effect on our consolidated financial statements, results of operations and liquidity.

We record liabilities related to environmental remediation and related matters (including costs associated with damages for personal injury or property damage and/or damages for injury to natural resources) when estimated future expenditures are probable and reasonably estimable. We adjust such accruals as further information becomes available to us or as circumstances change. Unless the amounts and timing of such estimated future expenditures are fixed and reasonably determinable, we generally do not discount estimated future expenditures to their present value due to the uncertainty of the timing of the payout. We recognize recoveries of costs from other parties, if any, as assets when their receipt is deemed probable. We recognize recoveries of costs from other parties, if any, as assets when their receipt is deemed probable. At December 31, 2017 we had not recognized any receivables for recoveries and at September 30, 2018, we have recognized \$15.0 million of receivables for recoveries related to the lead pigment litigation in California discussed above.

We do not know and cannot estimate the exact time frame over which we will make payments for our accrued environmental and related costs. The timing of payments depends upon a number of factors, including but not limited to the timing of the actual remediation process; which in turn depends on factors outside of our control. At each balance sheet date, we estimate the amount of our accrued environmental and related costs which we expect to pay

within the next twelve months, and we classify this estimate as a current liability. We classify the remaining accrued environmental costs as a noncurrent liability.

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Changes in the accrued environmental remediation and related costs during the first nine months of 2018 are as follows:

	Amount (In thousands)
Balance at the beginning of the period	\$ 111,909
Additions charged to expense, net	2,671
Payments, net	(3,098 )
<b>Balance at the end of the period</b>	<b>\$ 111,482</b>
<b>Amounts recognized in the Condensed Consolidated</b>	
<b>Balance Sheet at the end of the period:</b>	
Current liability	\$ 17,762
Noncurrent liability	93,720
<b>Balance at the end of the period</b>	<b>\$ 111,482</b>

On a quarterly basis, we evaluate the potential range of our liability for environmental remediation and related costs at sites where we have been named as a PRP or defendant, including sites for which our wholly-owned environmental management subsidiary, NL Environmental Management Services, Inc. (EMS), has contractually assumed our obligations. At September 30, 2018, we had accrued approximately \$111 million related to approximately 37 sites associated with remediation and related matters that we believe are at the present time and/or in their current phase reasonably estimable. The upper end of the range of reasonably possible costs to us for remediation and related matters for which we believe it is possible to estimate costs is approximately \$130 million, including the amount currently accrued. These accruals have not been discounted to present value.

We believe that it is not reasonably possible to estimate the range of costs for certain sites. At September 30, 2018, there were approximately 5 sites for which we are not currently able to reasonably estimate a range of costs. For these sites, generally the investigation is in the early stages, and we are unable to determine whether or not we actually had any association with the site, the nature of our responsibility for the contamination at the site, if any, and the extent of contamination at and cost to remediate the site. The timing and availability of information on these sites is dependent on events outside of our control, such as when the party alleging liability provides information to us. At certain of these previously inactive sites, we have received general and special notices of liability from the EPA and/or state agencies alleging that we, sometimes with other PRPs, are liable for past and future costs of remediating environmental contamination allegedly caused by former operations. These notifications may assert that we, along with any other alleged PRPs, are liable for past and/or future clean-up costs. As further information becomes available to us for any of these sites, which would allow us to estimate a range of costs, we would at that time adjust our accruals. Any such adjustment could result in the recognition of an accrual that would have a material effect on our consolidated financial statements, results of operations and liquidity.

#### Insurance coverage claims

We are involved in certain legal proceedings with a number of our former insurance carriers regarding the nature and extent of the carriers' obligations to us under insurance policies with respect to certain lead pigment and asbestos lawsuits. The issue of whether insurance coverage for defense costs or indemnity or both will be found to exist for our lead pigment and asbestos litigation depends upon a variety of factors and we cannot assure you that such insurance coverage will be available.



We have agreements with certain of our former insurance carriers pursuant to which the carriers reimburse us for a portion of our future lead pigment litigation defense costs, and one such carrier reimburses us for a portion of our future asbestos litigation defense costs. We are not able to determine how much we will ultimately recover from these carriers for defense costs incurred by us because of certain issues that arise regarding which defense costs qualify for reimbursement. While we continue to seek additional insurance recoveries, we do not know if we will be successful in obtaining reimbursement for either defense costs or indemnity. Accordingly, we recognize insurance recoveries in income only when receipt of the recovery is probable and we are able to reasonably estimate the amount of the recovery.

For a complete discussion of certain litigation involving us and certain of our former insurance carriers, refer to our 2017 Annual Report.

#### Other litigation

We have been named as a defendant in various lawsuits in several jurisdictions, alleging personal injuries as a result of occupational exposure primarily to products manufactured by our former operations containing asbestos, silica and/or mixed dust. In addition, some plaintiffs allege exposure to asbestos from working in various facilities previously owned and/or operated by us. There are 109 of these types of cases pending, involving a total of approximately 582 plaintiffs. In addition, the claims of approximately 8,676 plaintiffs have been administratively dismissed or placed on the inactive docket in Ohio state court. We do not expect these claims will be re-opened unless the plaintiffs meet the courts' medical criteria for asbestos-related claims. We have not accrued any amounts for this litigation because of the uncertainty of liability and inability to reasonably estimate the liability, if any. To date, we have not been adjudicated liable in any of these matters.

Based on information available to us, including:

- facts concerning historical operations,
- the rate of new claims,
- the number of claims from which we have been dismissed, and
- our prior experience in the defense of these matters,

we believe that the range of reasonably possible outcomes of these matters will be consistent with our historical costs (which are not material). Furthermore, we do not expect any reasonably possible outcome would involve amounts material to our consolidated financial position, results of operations or liquidity. We have sought and will continue to vigorously seek dismissal and/or a finding of no liability from each claim. In addition, from time to time, we have received notices regarding asbestos or silica claims purporting to be brought against former subsidiaries, including notices provided to insurers with which we have entered into settlements extinguishing certain insurance policies. These insurers may seek indemnification from us. For a discussion of other legal proceedings to which we are a party, refer to our 2017 Annual Report.

In addition to the litigation described above, we and our affiliates are also involved in various other environmental, contractual, product liability, patent (or intellectual property), employment and other claims and disputes incidental to present and former businesses. In certain cases, we have insurance coverage for these items, although we do not expect additional material insurance coverage for environmental matters.

We currently believe the disposition of all of these various other claims and disputes, individually and in the aggregate, should not have a material adverse effect on our consolidated financial position, results of operations or liquidity beyond the accruals already provided.

Note 15 – Financial instruments and fair value measurements:

See Note 4 for information on how we determine fair value of our marketable securities.

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The following table presents the financial instruments that are not carried at fair value but which require fair value disclosure:

	December 31, 2017		September 30, 2018	
	Carrying amount	Fair value	Carrying amount	Fair value
	(In thousands)			
Cash, cash equivalents and restricted cash	\$102,941	\$102,941	\$128,371	\$128,371
Noncontrolling interest in CompX common stock	17,756	22,224	19,177	22,854

The fair value of our noncontrolling interest in CompX stockholders' equity is based upon its quoted market price at each balance sheet date, which represents a Level 1 input. Due to their near-term maturities, the carrying amounts of accounts receivable and accounts payable are considered equivalent to fair value.

Note 16 – Recent accounting pronouncements:

Adopted

On January 1, 2018, we adopted ASU No. 2014-09, Revenue from Contracts with Customers (Topic 606) for all contracts which were not completed as of January 1, 2018 using the modified retrospective method. Prior to adoption of this standard, we recorded sales when our products were shipped and title and other risks and rewards of ownership had passed to our customer, which was generally at the time of shipment (although in some instances shipping terms were FOB destination point, for which we did not recognize revenue until the product was received by our customer). Following adoption of this standard, we record sales when we satisfy our performance obligations to our customers by transferring control of our products to them, which we have determined is at the same point in time that we recognized revenue prior to adoption of this new standard. Accordingly, the adoption of Topic 606 as of January 1, 2018 did not have a material impact on our consolidated financial statements, and we believe adoption of this standard will have a minimal effect on our revenues on an ongoing basis. See Note 11.

On January 1, 2018, we adopted ASU 2016-01, Financial Instruments-Overall (Subtopic 825-10): Recognition and Measurement of Financial Assets and Financial Liabilities, which addresses certain aspects related to the recognition, measurement, presentation and disclosure of financial instruments. The ASU requires equity investments (except for those accounted for under the equity method of accounting or those that result in the consolidation of the investee) to generally be measured at fair value with changes in fair value recognized in net income (previously, changes in fair value of such securities were recognized in other comprehensive income). The amendment also requires a number of other changes, including among others: simplifying the impairment assessment for equity instruments without readily determinable fair values; eliminating the requirement for public business entities to disclose methods and assumptions used to determine fair value for financial instruments measured at amortized cost; requiring an exit price notion when measuring the fair value of financial instruments for disclosure purposes; and requiring separate presentation of financial assets and liabilities by measurement category and form of asset. We adopted the new standard prospectively. The most significant aspect of adopting this ASU is the requirement to recognize changes in fair value of our available-for-sale marketable equity securities in net income. At December 31, 2017, our entire portfolio of marketable securities consisted of marketable equity securities. Upon adoption of the ASU on January 1, 2018, the entire balance of our accumulated other comprehensive income related to marketable securities of \$46.1 million was

reclassified to our beginning retained earnings pursuant to the transition requirements of the ASU.

In March 2017, the FASB issued ASU 2017-07, Compensation— Retirement Benefits (Topic 715) Improving the Presentation of Net Periodic Pension Cost and Net Periodic Postretirement Benefit Cost, which requires that the service cost component of net periodic defined benefit pension and OPEB cost be reported in the same line item as other compensation costs for applicable employees incurred during the period. Other components of such net benefit cost are required to be presented in the income statement separately from the service cost component, and below income from operations (if such a subtotal is presented). These other net benefit cost components must be disclosed either on the face of the financial statements or in the notes to the financial statements. In addition only the service cost component is eligible for capitalization in assets where applicable (inventory or internally

constructed fixed assets for example). We adopted the amendments in ASU 2017-07 beginning in the first quarter of 2018, with retrospective presentation in our Condensed Consolidated Statements of Operations. We began applying ASU 2017-07 prospectively beginning on January 1, 2018 as it relates to the capitalization of the service cost component of net benefit cost into assets (primarily inventory). We are availing ourselves of the practical expedient that permits us to use amounts we previously disclosed as components of our net periodic defined benefit pension and OPEB cost for periods prior to the adoption of this ASU as the estimation basis for applying the retrospective presentation requirements. As a result we have reclassified \$.2 million and \$.5 million previously classified as part of corporate expense for the third quarter and first nine months of September 30, 2017, respectively, to “Other components of net periodic pension and OPEB cost” in our Condensed Consolidated Statement of Income.

#### Pending adoption

In February 2016, the FASB issued ASU 2016-02, Leases (Topic 842), which is a comprehensive rewriting of the lease accounting guidance which aims to increase comparability and transparency with regard to lease transactions. The primary change will be the recognition of lease assets for the right-of-use of the underlying asset and lease liabilities for the obligation to make payments by lessees on the balance sheet for leases currently classified as operating leases. The ASU also requires increased qualitative disclosure about leases in addition to quantitative disclosures currently required. Companies are currently required to use a modified retrospective approach to adoption with a practical expedient which will allow companies to continue to account for existing leases under the prior guidance unless a lease is modified, other than the requirement to recognize the right-of-use asset and lease liability for all operating leases. The changes indicated above will be effective for us beginning in the first quarter of 2019, with early adoption permitted. We are in the process of assessing all of our current leases. We are in the process of completing our evaluation of the effect this ASU will have on our Consolidated Financial Statements, and we do not expect the adoption of this standard to have a material effect on our Consolidated Balance Sheet.

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

Business overview

We are primarily a holding company. We operate in the component products industry through our majority-owned subsidiary, CompX International Inc. We also own a non-controlling interest in Kronos Worldwide, Inc. Both CompX (NYSE American: CIX) and Kronos (NYSE: KRO) file periodic reports with the Securities and Exchange Commission (SEC).

CompX is a leading manufacturer of engineered components utilized in a variety of applications and industries. Through its Security Products operations, CompX manufactures mechanical and electronic cabinet locks and other locking mechanisms used in recreational transportation, postal, office and institutional furniture, cabinetry, tool storage and healthcare applications. CompX also manufactures stainless steel exhaust systems, gauges, throttle controls and trim tabs for the recreational marine and other non-marine industries through its Marine Components operations.

We account for our 30% non-controlling interest in Kronos by the equity method. Kronos is a leading global producer and marketer of value-added titanium dioxide pigments (TiO<sub>2</sub>). TiO<sub>2</sub> is used for a variety of manufacturing applications including paints, plastics, paper and other industrial and specialty products.

Forward-looking information

This report contains forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995, as amended. Statements in this Quarterly Report on Form 10-Q that are not historical facts are forward-looking in nature and represent management's beliefs and assumptions based on currently available information. Statements in this report including, but not limited to, statements found in Item 2 — "Management's Discussion and Analysis of Financial Condition and Results of Operations," are forward-looking statements that represent our management's beliefs and assumptions based on currently available information. In some cases you can identify forward-looking statements by the use of words such as "believes," "intends," "may," "should," "could," "anticipates," "expects" or comparable terminology by discussions of strategies or trends. Although we believe the expectations reflected in forward-looking statements are reasonable, we do not know if these expectations will be correct. Such statements by their nature involve substantial risks and uncertainties that could significantly impact expected results. Actual future results could differ materially from those predicted. The factors that could cause our actual future results to differ materially from those described herein are the risks and uncertainties discussed in this Quarterly Report and those described from time to time in our other filings with the SEC including, but are not limited to, the following:

- Future supply and demand for our products
- The extent of the dependence of certain of our businesses on certain market sectors
- The cyclicity of our businesses (such as Kronos' TiO<sub>2</sub> operations)
- Customer and producer inventory levels
- Unexpected or earlier-than-expected industry capacity expansion (such as the TiO<sub>2</sub> industry)
- Changes in raw material and other operating costs (such as energy, ore, zinc and brass costs) and our ability to pass those costs on to our customers or offset them with reductions in other operating costs
- Changes in the availability of raw material (such as ore)
- General global economic and political conditions (such as changes in the level of gross domestic product in various regions of the world and the impact of such changes on demand for, among other things, TiO<sub>2</sub> and component products)



- Competitive products and substitute products
- Price and product competition from low-cost manufacturing sources (such as China)
- Customer and competitor strategies
- Potential consolidation of Kronos' competitors
- Potential consolidation of Kronos' customers
- The impact of pricing and production decisions

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- Competitive technology positions
- Potential difficulties in integrating future acquisitions
- Potential difficulties in upgrading or implementing new accounting and manufacturing software systems (such as Kronos' enterprise resource planning system)
- The introduction of trade barriers
- Possible disruption of Kronos' or CompX's business, or increases in our cost of doing business resulting from terrorist activities or global conflicts
- The impact of current or future government regulations (including employee healthcare benefit related regulations)
- Fluctuations in currency exchange rates (such as changes in the exchange rate between the U.S. dollar and each of the euro, the Norwegian krone and the Canadian dollar), or possible disruptions to our business resulting from potential instability resulting from uncertainties associated with the euro or other currencies
- Operating interruptions (including, but not limited to, labor disputes, leaks, natural disasters, fires, explosions, unscheduled or unplanned downtime, transportation interruptions and cyber attacks)
- Decisions to sell operating assets other than in the ordinary course of business
- Kronos' ability to renew or refinance credit facilities
- Our ability to maintain sufficient liquidity
- The timing and amounts of insurance recoveries
  - The extent to which our subsidiaries or affiliates were to become unable to pay us dividends
- Uncertainties associated with CompX's development of new product features
- The ultimate outcome of income tax audits, tax settlement initiatives or other tax matters, including future tax reform
- Our ability to utilize income tax attributes or changes in income tax rates related to such attributes, the benefits of which may or may not have been recognized under the more-likely-than-not recognition criteria
- Environmental matters (such as those requiring compliance with emission and discharge standards for existing and new facilities or new developments regarding environmental remediation at sites related to our former operations)
- Government laws and regulations and possible changes therein (such as changes in government regulations which might impose various obligations on former manufacturers of lead pigment and lead-based paint, including us, with respect to asserted health concerns associated with the use of such products)
- The ultimate resolution of pending litigation (such as our lead pigment and environmental matters)
- Possible future litigation.

Should one or more of these risks materialize (or if the consequences of such a development worsen), or should the underlying assumptions prove incorrect, actual results could differ materially from those currently forecasted or expected. We disclaim any intention or obligation to update or revise any forward-looking statement whether as a result of changes in information, future events or otherwise.

## Results of operations

### Net income overview

Quarter ended September 30, 2018 compared to the quarter ended September 30, 2017

We had a net loss attributable to NL stockholders of \$15.4 million or \$.32 per share in the third quarter of 2018 compared to net income attributable to NL stockholders of \$17.5 million, or \$.36 per share, in the third quarter of 2017. As more fully described below, the decrease in our earnings per share from 2017 to 2018 is primarily due to the net effects of:

- a pre-tax marketable equity securities expense of \$35.6 million recognized in the third quarter of 2018 as a result of adopting ASU 2016-01 in 2018;
- equity in earnings of Kronos in 2018 of \$9.9 million compared to \$22.4 million in 2017; and

higher income from operations attributable to CompX of \$1.1 million in 2018.

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Our 2017 net income attributable to NL stockholders includes:

- income of \$.03 per share, net of income taxes, included in our equity in earnings of Kronos related to Kronos' non-cash deferred income tax benefit recognized as a result of a net decrease in Kronos' deferred income tax asset valuation allowance related to its German and Belgian operations;
- income of \$.05 per share, net of income taxes, included in our equity in earnings of Kronos related to Kronos' income tax benefit related to the execution and finalization of an Advance Pricing Agreement between Canada and Germany; and
- loss of \$.02 per share, net of income taxes, included in our equity in earnings of Kronos related to Kronos' loss on prepayment of debt.

Nine months ended September 30, 2018 compared to nine months ended September 30, 2017

We had a net loss attributable to NL stockholders of \$43.8 million or \$.90 per share in the first nine months of 2018 compared to net income attributable to NL stockholders of \$67.0 million, or \$1.38 per share, in the first nine months of 2017. As more fully described below, the decrease in our earnings per share from 2017 to 2018 is primarily due to the net effects of:

- a pre-tax litigation settlement expense of \$62 million recognized in the second quarter of 2018;
- a pre-tax marketable equity securities expense of \$55.9 million recognized in the first nine months of 2018 as a result of adopting ASU 2016-01 in 2018;
- equity in earnings of Kronos in 2018 of \$55.0 million compared to \$93.4 million in 2017;
- higher income from operations attributable to CompX of \$2.4 million in 2018; and
- higher litigation fees and litigation related costs of \$2.3 million in 2018.

Our 2018 net loss attributable to NL stockholders includes a loss of \$1.01 per share related to the litigation settlement expense recognized in the second quarter.

Our 2017 net income attributable to NL stockholders includes:

- income of \$.69 per share, net of income taxes, included in our equity in losses of Kronos related to Kronos' non-cash deferred income tax benefit recognized as a result of a net decrease in Kronos' deferred income tax asset valuation allowance related to its German and Belgian operations;
- income of \$.05 per share, net of income taxes, included in our equity in earnings of Kronos related to Kronos' income tax benefit related to the execution and finalization of an Advance Pricing Agreement between Canada and Germany; and
- loss of \$.02 per share, net of income taxes, included in our equity in earnings of Kronos related to Kronos' loss on prepayment of debt.

Income (loss) from operations

The following table shows the components of our income (loss) from operations.

	Three months ended			Nine months ended			
	September 30, 2017 (In millions)	2018	% Change	September 30, 2017	2018	% Change	
CompX	\$ 3.4	\$ 4.5	34	% \$ 12.5	\$ 14.9	19	%
Insurance recoveries	0.1	0.5	411	0.2	0.9	306	

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Other income, net	0.1	-	n/m	0.1	0.6	n/m
Litigation settlement expense	-	-	n/m	-	(62.0 )	n/m
Corporate expense	(2.6 )	(1.6 )	(38 )	(11.1 )	(14.4 )	29
Income (loss) from operations	\$ 1.0	\$ 3.4	n/m	\$ 1.7	\$ (60.0 )	n/m

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Amounts attributable to CompX relate primarily to its components products business, while the other amounts generally relate to NL. Each of these items is further discussed below.

The following table shows the components of our income before income taxes exclusive of our income (loss) from operations.

	Three months ended			Nine months ended		
	September 30,		% Change	September 30,		% Change
	2017	2018		2017	2018	
Equity in earnings of Kronos	\$ 22.4	\$ 9.9	(56 )%	\$ 93.4	\$ 55.0	(41 )%
Marketable equity securities	-	(35.6 )	n/m	-	(55.9 )	n/m
Other components of net periodic pension and OPEB	(.2 )	(.1 )	(44 )	(.5 )	(.3 )	(44 )
Interest and dividend income	1.0	1.3	37	2.6	3.6	42

CompX International Inc.

	Three months ended			Nine months ended		
	September 30,		% Change	September 30,		% Change
	2017	2018		2017	2018	
	(In thousands)			(In thousands)		
Net sales	\$ 27.0	\$ 30.0	11 %	\$ 86.9	\$ 90.8	4 %
Cost of sales	18.8	20.4	9	59.5	60.4	2
Gross margin	8.2	9.6	17	27.4	30.4	11
Operating costs and expenses	4.8	5.1	5	14.9	15.5	4
Income from operations	\$ 3.4	\$ 4.5	34	\$ 12.5	\$ 14.9	19
Percentage of net sales:						
Cost of sales	70 %	68 %		69 %	67 %	
Gross margin	30	32		32	33	
Operating costs						
and expenses	18	17		17	17	
Income from operations	13	15		14	16	

Net sales – Net sales increased \$3.0 million in the third quarter of 2018 compared to the same period in 2017 due to higher sales of security products across the majority of our markets including transportation, government security, office furniture and distribution as well as continued strong growth in sales of marine components to various marine and industrial markets. Net sales increased \$3.9 million in the first nine months of 2018 compared to the same period in 2017 due to the higher Marine Components sales volumes, and to a lesser extent Security Products sales across the majority of our markets, particularly transportation, office furniture and distribution. Relative changes in selling prices did not have a material impact on net sales comparisons.

Cost of sales and gross margin – Cost of goods sold as a percentage of sales decreased 1.5% in the third quarter of 2018 compared to the same period in 2017 primarily due to improved coverage of fixed costs over increased production volumes. As a result, gross profit increased over the same period. As a percentage of net sales, cost of goods sold for the first nine months of 2018 decreased 1.9% compared to the same period in 2017 due to favorable changes in customer and product mix in Security Products as well as improved manufacturing efficiencies and fixed cost leverage facilitated by higher production volumes for each of our business segments. Gross profit for the third quarter and first nine months of 2018 increased over the same periods in the prior year due to the aforementioned factors.

Operating costs and expenses – Operating costs and expenses consist primarily of sales and administrative-related personnel costs, sales commissions and advertising expenses, as well as gains and losses on plant, property and equipment. Operating costs and expenses for the third quarter and first nine months of 2018 were comparable to the same periods in 2017.

Income from operations – As a percentage of net sales, income from operations for the third quarter and first nine months of 2018 increased compared to the same periods of 2017 and was primarily impacted by the factors impacting cost of goods sold, gross margin and operating costs discussed above.

#### Results by reporting unit

The key performance indicator for CompX's reporting units is the level of their income from operations (see discussion below).

	Three months ended			Nine months ended			
	September 30, 2017 (In thousands)	2018	% Change	September 30, 2017 (In thousands)	2018	% Change	
Net sales:							
Security Products	\$ 22.9	\$ 24.5	7	\$ 74.9	\$ 75.8	1	%
Marine Components	4.1	5.5	33	12.0	15.0	24	
Total net sales	\$ 27.0	\$ 30.0	11	\$ 86.9	\$ 90.8	4	
Gross margin:							
Security Products	\$ 7.2	\$ 8.1	12	\$ 24.4	\$ 26.1	7	
Marine Components	1.0	1.5	51	3.0	4.3	41	
Total gross margin	\$ 8.2	\$ 9.6	17	\$ 27.4	\$ 30.4	11	
Income from operations:							
Security Products	\$ 4.3	\$ 5.3	26	\$ 15.3	\$ 17.8	16	
Marine Components	.4	.8	95	1.3	2.3	82	
Corporate operating expenses	(1.3 )	(1.6 )	25	(4.1 )	(5.2 )	28	
Total income from							
operations	\$ 3.4	\$ 4.5	34	\$ 12.5	\$ 14.9	19	
Gross margin:							
Security Products	32	% 33	%	33	% 34	%	
Marine Components	24	27		25	28		
Total gross margin	30	32		32	33		
Income from operations margin:							
Security Products	19	% 22	%	20	% 23	%	
Marine Components	10	15		11	16		
Total income from	13	15		14	16		



operations margin

Security Products — Security Products net sales in the third quarter of 2018 increased 7% compared to the same period in 2017 on improved sales across the majority of our markets including transportation, government security, office furniture and distribution. Gross profit margin and operating income as a percentage of sales for the third quarter increased compared to the same period in 2017 primarily due to improved coverage of fixed cost over increased production volumes.

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#### Marine Components –

Marine Components net sales increased 33% and 24% in the third quarter and first nine months of 2018, respectively, as compared to the same periods last year. The increase in sales reflects improved demand for products sold to original equipment manufacturers of recreational towboats and to a lesser extent sales to manufacturers of larger center-console boats and industrial customers. Gross profit margin and operating income as a percentage of net sales increased in the third quarter and first nine months of 2018 compared to the same periods last year due to improved fixed cost leverage facilitated by the higher production volumes.

Outlook – Due to the strong third quarter, year-to-date sales of security products now exceed the comparable year-to-date period, while sales of marine components continue to significantly outpace year-to-date 2017 due to the significant traction achieved through new product offerings, primarily to the recreational boat markets. We believe full year sales of our security products and marine components, as well as the related operating earnings, will also surpass prior year. We monitor changes in economic conditions and sales order rates and will respond to fluctuations in customer demand through continuous evaluation of staffing levels and consistent execution of our lean manufacturing and cost improvement initiatives. Additionally, we continue to seek opportunities to gain market share in markets we currently serve, to expand into new markets and to develop new product features in order to mitigate the impact of changes in demand as well as broaden our sales base.

#### General corporate and other items

Insurance recoveries – We have agreements with certain insurance carriers pursuant to which the carriers reimburse us for a portion of our past lead pigment and asbestos litigation defense costs. Insurance recoveries include amounts we received from these insurance carriers.

The agreements with certain of our insurance carriers also include reimbursement for a portion of our future litigation defense costs. We are not able to determine how much we will ultimately recover from these carriers for defense costs incurred by us because of certain issues that arise regarding which defense costs qualify for reimbursement. Accordingly, these insurance recoveries are recognized when the receipt is probable and the amount is determinable. See Note 14 to our Condensed Consolidated Financial Statements.

Litigation settlement expense – We recognized a pre-tax \$62.0 million litigation settlement expense charge in the second quarter of 2018 related to the lead pigment litigation in California. See Note 14 to our Condensed Consolidated Financial Statements.

Corporate expense – Corporate expenses were \$1.6 million in the third quarter of 2018, \$1.0 million lower than in the third quarter of 2017 primarily due to lower environmental remediation and related costs in 2018. Included in corporate expense in the third quarter of 2017 and 2018 are:

- litigation fees and related costs of \$1.1 million in 2018 compared to \$.9 million in 2017, and
- environmental remediation and related credit of \$1.6 million in 2018 compared to costs of \$.1 million in 2017.

Corporate expenses were \$14.4 million in the first nine months of 2018, \$3.2 million higher than in the first nine months of 2017 primarily due to higher litigation and related costs in 2018. Included in corporate expense in the first nine months of 2017 and 2018 are:

- litigation fees and related costs of \$5.1 million in 2018 compared to \$2.8 million in 2017, and
- environmental remediation and related costs of \$2.7 million in 2018 compared to \$3.2 million in 2017.

The level of our litigation fees and related costs varies from period to period depending upon, among other things, the number of cases in which we are currently involved, the nature of such cases and the current stage of such cases (e.g. discovery, pre-trial motions, trial or appeal, if applicable). See Note 14 to our Condensed Consolidated Financial

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Statements. If our current expectations regarding the number of cases in which we expect to be involved during 2018 or the nature of such cases were to change, our corporate expenses could be higher than we currently estimate.

Obligations for environmental remediation costs are difficult to assess and estimate and it is possible that actual costs for environmental remediation will exceed accrued amounts or that costs will be incurred in the future for sites in which we cannot currently estimate our liability. If these events were to occur in 2018, our corporate expenses would be higher than we currently estimate. In addition, we adjust our environmental accruals as further information becomes available to us or as circumstances change. Such further information or changed circumstances could result in an increase in our accrued environmental costs. See Note 14 to our Condensed Consolidated Financial Statements.

Overall, we currently expect that our net general corporate expenses in 2018 will be higher than in 2017 primarily due to higher expected litigation and related costs.

Interest and dividend income – Interest and dividend income increased \$.4 million in the third quarter and \$1.1 million in the first nine months of 2018 primarily due to interest income earned on CompX's revolving promissory note receivable from Valhi, which CompX entered into in August 2016. Interest income on such note receivable from Valhi was \$.5 million in each of the third quarters of 2017 and 2018, respectively and \$1.3 million and \$1.6 million in the first nine months of 2017 and 2018, respectively.

Marketable equity securities – Beginning on January 1, 2018 with the adoption of ASU 2016-01, any unrealized gains or losses on our marketable equity securities are now recognized as a component of other income included in Marketable equity securities on our Condensed Consolidated Statements of Operations. See Note 4 to our Condensed Consolidated Financial Statements.

Income tax expense (benefit) – We recognized income tax benefit of \$6.2 million in the third quarter of 2018 compared to income tax expense of \$6.5 million in the third quarter of 2017 and an income tax benefit of \$15.4 million in the first nine months of 2018 compared to income tax expense of \$28.9 million in the first nine months of 2017. In accordance with GAAP, we recognize deferred income taxes on our undistributed equity in earnings of Kronos. Because we and Kronos are part of the same U.S. federal income tax group, any dividends we receive from Kronos are nontaxable to us. Accordingly, we do not recognize and we are not required to pay income taxes on dividends from Kronos. Therefore, our full-year effective income tax rate will generally be lower than the U.S. federal statutory income tax rate in years during which we receive dividends from Kronos and recognize equity in earnings of Kronos. Conversely, our effective income tax rate will generally be higher than the U.S. federal statutory income tax rate in years during which we receive dividends from Kronos and recognize equity in losses of Kronos. During interim periods, our effective income tax rate may not necessarily correspond to the foregoing due to the application of accounting for income taxes in interim periods which requires us to base our effective rate on full year projections. We received dividends from Kronos of \$15.8 million in the first nine months of 2017 and \$18.0 million in the first nine months of 2018.

Our effective tax rate attributable to our equity in earnings of Kronos, including the effect of the non-taxable dividends we received from Kronos was 13.3% in the first nine months of 2018 and 29.6% in the first nine months of 2017. See Note 12 to our Condensed Consolidated Financial Statements for more information about our 2018 income tax items, including a tabular reconciliation of our statutory tax expense (benefit) to our actual expense (benefit).

Noncontrolling interest – Noncontrolling interest in net income of CompX is consistent in the first nine months of 2017 and 2018. The noncontrolling interest we recognize in each period is directly related to the level of earnings at CompX for the period.



## Equity in earnings of Kronos Worldwide, Inc.

	Three months ended			Nine months ended		
	September 30, 2017 (In millions)	2018	% Change	September 30, 2017 (In millions)	2018	% Change
Net sales	\$ 464.5	\$ 410.3	(12)%	\$ 1,275.7	\$ 1,312.5	4 %
Cost of sales	309.5	291.2	(6 )	882.3	846.8	(4 )%
Gross margin	\$ 155.0	\$ 119.1		\$ 393.4	\$ 465.7	
Income from operations	\$ 96.1	\$ 58.1	(40)	\$ 226.8	\$ 285.5	26 %
Marketable equity securities	-	(4.3 )		-	(6.7 )	
Other components of net periodic pension and OPEB cost	(4.5 )	(3.7 )		(12.8 )	(11.3 )	
Interest and dividend income	.4	1.5		.7	3.7	
Loss on prepayment of debt, net	(7.1 )	-		(7.1 )	-	
Interest expense	(5.0 )	(4.9 )		(14.5 )	(14.7 )	
Income before income taxes	79.9	46.7		193.1	256.5	
Income tax expense (benefit)	6.1	14.1		(114.0 )	75.5	
Net income	\$ 73.8	\$ 32.6		\$ 307.1	\$ 181.0	
Percentage of net sales:						
Cost of sales	67	% 71	%	69	% 65	%
Income from operations	21	14		18	22	
Equity in earnings of Kronos Worldwide, Inc.	\$ 22.4	\$ 9.9		\$ 93.4	\$ 55.0	
TiO <sub>2</sub> operating statistics:						
Sales volumes*	150	123	(19)%	450	385	(15)%
Production volumes*	141	131	(7 )	427	400	(6 )%
Change in TiO <sub>2</sub> net sales:						
TiO <sub>2</sub> product pricing			9 %			18 %
TiO <sub>2</sub> sales volumes			(19)			(15)
TiO <sub>2</sub> product mix/other			(2 )			(4 )
Changes in currency exchange rates			-			4
Total			(12)%			3 %

\* Thousands of metric tons  
Current industry conditions

Due to the successful implementation of previously-announced price increases, average selling prices rose throughout 2017 and the first six months of 2018. Kronos' average TiO<sub>2</sub> selling prices at the end of 2017 were 27% higher than at the end of 2016, and Kronos' average selling prices at the end of the second quarter of 2018 were 3% higher than at the end of 2017, with most of the increase occurring during the first quarter. Kronos' average selling prices declined during the third quarter of 2018. Kronos' average selling prices at the end of the third quarter of 2018 were 2% lower

than at the end of the second quarter of 2018, and were 1% higher than at the end of 2017. Higher prices in the European and North American markets were partially offset by lower prices in the Latin American and export markets (attributable to changes in customer mix) at the end of the third quarter of 2018 as compared to the end of 2017. We experienced lower sales volumes in all major markets in the first nine months of 2018 as compared to the record sales volumes achieved in the same period of 2017.

Kronos operated its production facilities at overall average capacity utilization rates of 95% in the first nine months of 2018 compared to full practical capacity utilization rates in the first nine months of 2017. Kronos'

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production rates in the third quarter of 2018 were impacted by maintenance activities at certain facilities. The table below lists our comparative quarterly capacity utilization rates.

	Production Capacity Utilization Rates	
	2017	2018
First quarter	100%	95%
Second quarter	100%	97%
Third quarter	100%	92%

Due to a moderate rise in the cost of third-party feedstock ore Kronos procured in 2017 and the first nine months of 2018, Kronos' cost of sales per metric ton of TiO<sub>2</sub> sold in the first nine months of 2018 was higher as compared to the first nine months of 2017 (excluding the effect of changes in currency exchange rates).

Net sales - Net sales in the third quarter of 2018 decreased 12%, or \$54.2 million, compared to the third quarter of 2017 primarily due to the net effect of a 9% increase in average TiO<sub>2</sub> selling prices (which increased net sales by approximately \$42 million) and a 19% decrease in sales volumes (which decreased net sales by approximately \$88 million). TiO<sub>2</sub> selling prices will increase or decrease generally as a result of competitive market pressures, changes in the relative level of supply and demand as well as changes in raw material and other manufacturing costs.

Kronos' sales volumes decreased 19% in the third quarter of 2018 as compared to the record third quarter sales volumes of 2017 primarily due to lower sales in the European and export markets reflecting the effects of reduced shipments as customer inventory levels returned to more normal levels. In addition to the impact of changes in average TiO<sub>2</sub> selling prices and sales volumes, Kronos estimates that changes in currency exchange rates (primarily the euro) had a nominal effect on Kronos' net sales as compared to the third quarter of 2017.

Net sales in the first nine months of 2018 increased 3%, or \$36.8 million, compared to the first nine months of 2017 primarily due to the net effect of an 18% increase in average TiO<sub>2</sub> selling prices (which increased net sales by approximately \$230 million) and a 15% decrease in sales volumes (which decreased net sales by approximately \$191 million). TiO<sub>2</sub> selling prices will increase or decrease generally as a result of competitive market pressures, changes in the relative level of supply and demand as well as changes in raw material and other manufacturing costs.

Kronos' sales volumes decreased 15% in the first nine months of 2018 as compared to the record first nine months of 2017 primarily due to a combination of factors including (i) lower sales in all major markets resulting from a controlled ramp-up in January 2018 as Kronos brought the second phase of its new global enterprise resource planning system online; (ii) inventory management to assure adequate supply to its customers during the spring and summer necessitated by the lower production volumes in the first three months of the year (as discussed below); (iii) product availability in the second quarter; and (iv) customer inventory level changes in the second and third quarters as discussed above. In addition to the impact of changes in average TiO<sub>2</sub> selling prices and sales volumes, Kronos estimate that changes in currency exchange rates increased its net sales by approximately \$53 million as compared to the first nine months of 2017.

Cost of sales and gross margin - Cost of sales decreased \$18.3 million or 6% in the third quarter of 2018 compared to the third quarter of 2017 due to the net effect of a 19% decrease in sales volumes, a 7% decrease in TiO<sub>2</sub> production volumes, higher raw materials and other production costs of approximately \$40 million and currency fluctuations (primarily the euro). The decrease in TiO<sub>2</sub> production volumes in the third quarter of 2018 compared to the production volumes in the third quarter of 2017 was primarily due to maintenance activities at certain facilities in 2018. Kronos' cost of sales as a percentage of net sales increased to 71% in the third quarter of 2018 compared to 67%



in the same period of 2017 as the unfavorable effects related to lower production volumes and higher raw materials and other production costs more than offset the favorable impact of higher average selling prices, as discussed above.

Gross margin as a percentage of net sales decreased to 29% in the third quarter of 2018 compared to 33% in the third quarter of 2017. As discussed and quantified above, Kronos' gross margin decreased primarily due to the net effect of higher average selling prices, lower sales and production volumes and higher raw materials and other production costs.

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Cost of sales decreased \$35.5 million in the first nine months of 2018 compared to the same period in 2017 primarily due to the net impact of a 15% decrease in sales volumes, 6% decrease in TiO<sub>2</sub> production volumes, higher raw materials and other production costs of approximately \$75 million (primarily caused by higher third-party feedstock ore costs) and currency fluctuations (primarily the euro). The decrease in TiO<sub>2</sub> production volumes in the first nine months of 2018 compared to the production volumes in the first nine months of 2017 was primarily due to maintenance activities at certain facilities in 2018, and the implementation of a productivity-enhancing improvement project at Kronos' Belgian facility in the first quarter of 2018. Kronos' cost of sales as a percentage of net sales decreased to 65% in the first nine months of 2018 compared to 69% in the same period of 2017 as the favorable impact of higher average selling prices more than offset the unfavorable effects related to lower production volumes and higher raw materials and other production costs, as discussed above.

Gross margin as a percentage of net sales increased to 35% in the first nine months of 2018 compared to 31% in the first nine months of 2017. As discussed and quantified above, Kronos' gross margin increased primarily due to the net effect of higher average selling prices, lower sales and production volumes and higher raw materials and other production costs.

Selling, general and administrative expense - Selling, general and administrative expense in the third quarter of 2018 was \$57.3 million, an increase of \$6.0 million compared to the third quarter of 2017 in part due to higher general and administrative costs related to the implementation of a new accounting and manufacturing software system and higher sales support costs.

Selling, general and administrative expense in the first nine months of 2018 was \$173.7 million, an increase of \$26.1 million compared to the first nine months of 2017 in part due to higher general and administrative costs related to the implementation of a new accounting and manufacturing software system and higher sales support costs.

Income from operations - Income from operations decreased by \$38.0 million, or 40%, in the third quarter of 2018 compared to the third quarter of 2017. Income from operations as a percentage of net sales decreased to 14% in the third quarter of 2018 from 21% in the same period of 2017. This decrease was driven by the decrease in gross margin, discussed above. Kronos estimates that changes in currency exchange rates increased income from operations by approximately \$7 million in the third quarter of 2018 as compared to the same period in 2017, as discussed below.

Income from operations increased by \$58.7 million, or 26%, in the first nine months of 2018 compared to the first nine months of 2017. Income from operations as a percentage of net sales increased to 22% in the first nine months of 2018 from 18% in the same period of 2017. This increase was driven by the increase in gross margin, discussed above. Kronos estimates that changes in currency exchange rates increased income from operations by approximately \$26 million in the first nine months of 2018 as compared to the same period in 2017.

Other non-operating income (expense) - Beginning on January 1, 2018 with the adoption of Accounting Standards Update ("ASU") 2016-01, all of Kronos' marketable equity securities will continue to be carried at fair value, but any unrealized gains or losses on the securities are now recognized in Marketable equity securities. Other components of net periodic pension and OPEB cost in the third quarter of 2018 was comparable to the third quarter of 2017. Interest expense in the third quarter and first nine months of 2018 was comparable to the same periods of 2017. Kronos currently expect its interest expense for all of 2018 will be comparable to 2017, as higher average debt levels in 2018 resulting from the September 2017 issuance of its Senior Secured Notes would be offset by lower average interest rates on outstanding indebtedness. Kronos also recognized a loss on prepayment of debt in the third quarter of 2017 aggregating \$7.1 million, associated with the prepayment and termination of its term loan indebtedness.

Income tax expense (benefit) - Kronos recognized income tax expense of \$14.1 million in the third quarter of 2018 compared to income tax expense of \$6.1 million in the third quarter of 2017. The difference is primarily due to the

net effect of higher earnings in the third quarter of 2017, the reversal of Kronos' deferred income tax asset valuation allowance associated with its German and Belgian operations in 2017 and the reversal of a significant portion of its reserve for uncertain tax positions in 2017. Kronos recognized income tax expense of \$75.5 million in the first nine months of 2018 compared to an income tax benefit of \$114.0 million in the first nine months of 2017.

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The difference is primarily due to the effect of the reversal of Kronos' deferred income tax asset valuation allowance associated with its German and Belgium operations in 2017. Kronos' earnings are subject to income tax in various U.S. and non-U.S. jurisdictions, and effective in 2018 the income tax rates applicable to its pre-tax earnings (losses) of its non-U.S. operations are generally higher than the income tax rates applicable to its U.S. operations. Excluding the effect of any increase or decrease in Kronos' deferred income tax asset valuation allowance or changes in its reserve for uncertain tax positions, Kronos would generally expect its overall effective tax rate to be higher than the U.S. federal statutory tax rate of 21% primarily because of Kronos' non-U.S. operations. Prior to 2018, the income tax rates applicable to Kronos' pre-tax earnings (losses) of its non-U.S. operations were generally lower than the U.S. federal statutory tax rate of 35%.

Kronos has substantial net operating loss ("NOL") carryforwards in Germany (the equivalent of \$652 million for German corporate purposes and \$.5 million for German trade tax purposes at December 31, 2017) and in Belgium (the equivalent of \$50 million for Belgian corporate tax purposes at December 31, 2017), all of which have an indefinite carryforward period. As a result, Kronos has net deferred income tax assets with respect to these two jurisdictions, primarily related to these NOL carryforwards. The German corporate tax is similar to the U.S. federal income tax, and the German trade tax is similar to the U.S. state income tax. As discussed in the 2017 Annual Report, commencing June 30, 2015, Kronos concluded that it was required to recognize a non-cash deferred income tax asset valuation allowance under the more-likely-than-not recognition criteria with respect to its German and Belgian net deferred income tax assets at such date. During the first six months of 2017, Kronos recognized an aggregate non-cash deferred income tax benefit of \$12.7 million as a result of a net decrease in such deferred income tax asset valuation allowance, due to utilizing a portion of both the German and Belgian NOL during the period, including \$7.7 million in the second quarter of 2017. As also discussed in the 2017 Annual Report, at June 30, 2017, Kronos concluded it had sufficient positive evidence under the more-likely-than-not recognition criteria to support reversal of the entire valuation allowance related to its German and Belgian operations. In accordance with the ASC 740-270 guidance regarding accounting for income taxes at interim dates, the amount of the valuation allowance reversed at June 30, 2017 (\$149.9 million, of which \$141.9 million related to Germany and \$8.0 million related to Belgium) relates to Kronos' change in judgment at that date regarding the realizability of the related deferred income tax asset as it relates to future years (i.e. 2018 and after). A change in judgment regarding the realizability of deferred tax assets as it relates to the current year is considered in determining the estimated annual effective tax rate for the year and is recognized throughout the year, including interim periods subsequent to the date of the change in judgment. Accordingly, Kronos' income tax benefit in calendar 2017 includes an aggregate non-cash deferred income tax benefit of \$186.7 million related to the reversal of the German and Belgian valuation allowance, comprised of \$12.7 million recognized in the first half of 2017 (noted above) related to the utilization of a portion of both the German and Belgian NOLs during such period, \$149.9 million related to the portion of the valuation allowance reversed as of June 30, 2017 and \$24.1 million recognized in the second half of 2017 (including \$7.8 million reversed in the third quarter) related to the utilization of a portion of both the German and Belgian NOLs during such period. Kronos' deferred income tax asset valuation allowance increased \$13.7 million in 2017 as a result of changes in currency exchange rates, which increase was recognized as part of other comprehensive income (loss).

As discussed in the 2017 Annual Report, on December 22, 2017, the 2017 Tax Act was enacted into law. This new tax legislation, among other changes, (i) reduced the U.S. Federal corporate income tax rate from 35% to 21% effective January 1, 2018; (ii) implemented a territorial tax system and imposed a one-time repatriation tax ("Transition Tax") on the deemed repatriation of the post-1986 undistributed earnings of non-U.S. subsidiaries accumulated up through December 31, 2017, regardless of whether such earnings are repatriated; (iii) eliminated U.S. tax on future non-U.S. earnings (subject to certain exceptions); (iv) eliminated the domestic production activities deduction beginning in 2018; (v) eliminated the net operating loss carryback and provides for an indefinite carryforward period subject to an 80% annual usage limitation; (vi) allows for the expensing of certain capital expenditures; (vii) imposed a tax on global intangible low-tax income ("GILTI") beginning in 2018; (viii) imposed a base erosion anti-abuse tax ("BEAT") beginning in 2018; and (ix) amended the rules limiting the deduction for business interest expense beginning

in 2018. Following the enactment of the 2017 Tax Act, the Securities and Exchange Commission issued Staff Accounting Bulletin (“SAB”) 118 to provide guidance on the accounting and reporting impacts of the 2017 Tax Act. SAB 118 states that companies should account for changes related to the 2017 Tax Act in the period of enactment if all information is available and the accounting can be completed. In situations where companies do not have enough information to complete the accounting in the period of enactment, a company must either 1) record an estimated provisional amount if the impact of the change can be reasonably

estimated; or 2) continue to apply the accounting guidance that was in effect immediately prior to the 2017 Tax Act if the impact of the change cannot be reasonably estimated. If estimated provisional amounts are recorded, SAB 118 provides a measurement period of no longer than one year during which companies should adjust those amounts as additional information becomes available in the reporting period within the measurement period in which such adjustment is determined.

Under GAAP, Kronos is required to revalue its net deferred tax asset associated with its U.S. net deductible temporary differences in the period in which the new tax legislation is enacted based on deferred tax balances as of the enactment date, to reflect the effect of such reduction in the corporate income tax rate. Kronos' temporary differences as of December 31, 2017 were not materially different from its temporary differences as of the enactment date, accordingly revaluation of its net deductible temporary differences was based on its net deferred tax asset as of December 31, 2017. Such revaluation was recognized in continuing operations and was not material to us.

Prior to the enactment of the 2017 Tax Act, the undistributed earnings of Kronos' European subsidiaries were deemed to be permanently reinvested (Kronos had not made a similar determination with respect to the undistributed earnings of its Canadian subsidiary). Pursuant to the Transition Tax provisions imposing a one-time repatriation tax on post-1986 undistributed earnings, Kronos recognized a provisional current income tax expense of \$76.2 million in the fourth quarter of 2017. The amounts recorded as of December 31, 2017 as a result of the 2017 Tax Act represented estimates based on information currently available. Kronos elected to pay such tax over an eight year period beginning in 2018, including approximately \$6.1 million which was paid in April 2018 (for the 2017 tax year) and \$4.6 million which was paid in the second and third quarters of 2018 (for the 2018 tax year). Kronos did not make any measurement-period adjustments to the provisional amounts recorded for this item during the first six months of 2018 because no new information became available during the period that required an adjustment. During the third quarter of 2018, in conjunction with finalizing our federal income tax return and based on additional information that became available (including proposed regulations issued by the IRS in August 2018 with respect to the Transition Tax), Kronos recognized a provisional income tax benefit of \$1.7 million which amount is recorded as a measurement-period adjustment, reducing the provisional income tax expense of \$76.2 million recognized in the fourth quarter of 2017. As a result, at September 30, 2018, taking into account the prior Transition Tax installments payments of \$10.7 million (noted above), the balance of Kronos' unpaid Transition Tax aggregates \$63.8 million, which will be paid in quarterly installments over the remainder of the eight year period. Of such \$63.8 million, \$58.1 million is recorded as a noncurrent payable to affiliate (income taxes payable to Valhi) classified as a noncurrent liability at September 30, 2018, and \$5.7 million is classified as a current liability. The issuance of final regulations and/or additional guidance with respect to the Transition Tax may impact the amount of the Transition Tax recognized in the fourth quarter of 2017, as adjusted in the third quarter of 2018. Kronos is also continuing to gather information and await further guidance from the state jurisdictions in which Kronos operates with respect to the Transition Tax. Kronos will complete its accounting for this item within the prescribed measurement period ending December 22, 2018, pursuant to the guidance under SAB 118, and if Kronos determines an adjustment to the provisional amounts recognized at December 31, 2017 and September 30, 2018 is required, Kronos will recognize such adjustment in the reporting period within the SAB 118 measurement period in which such adjustment is determined.

Prior to the enactment of the 2017 Tax Act the undistributed earnings of Kronos' European subsidiaries were deemed to be permanently reinvested (Kronos had not made a similar determination with respect to the undistributed earnings of its Canadian subsidiary). As a result of the implementation of a territorial tax system under the 2017 Tax Act, effective January 1, 2018, and the Transition Tax which in effect taxes the post-1986 undistributed earnings of Kronos' non-U.S. subsidiaries accumulated up through December 31, 2017, Kronos determined effective December 31, 2017 that all of the post-1986 undistributed earnings of its European subsidiaries are not permanently reinvested. Accordingly, in the fourth quarter of 2017 Kronos recognized an aggregate provisional non-cash deferred income tax expense of \$4.5 million based on its reasonable estimates of the U.S. state and non-U.S. income tax and withholding tax liability attributable to all of such previously-considered permanently reinvested undistributed

earnings through December 31, 2017. The amounts recorded as of December 31, 2017 as a result of the 2017 Tax Act represented estimates based on information currently available. Kronos has not made any measurement-period adjustments to the provisional amounts recorded at December 31, 2017 for this item during the first nine months of 2018. However, Kronos recorded a provisional non-cash deferred income tax expense of \$2.5 million for the estimated U.S. state and non-U.S. income tax and withholding tax liability attributable to the 2018

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undistributed earnings of its non-U.S. subsidiaries in the first nine months of 2018, including withholding taxes related to the undistributed earnings of its Canadian subsidiary. Kronos is continuing its review of certain other provisions under the 2017 Tax Act and waiting on further guidance primarily from the state jurisdictions in which it operates that may impact its determination of the aggregate temporary differences attributable to its investments in its non-U.S. subsidiaries. Kronos will complete Kronos' accounting for this item within the prescribed measurement period ending December 22, 2018, pursuant to the guidance under SAB 118, and if it determines an adjustment to the provisional amounts recognized at December 31, 2017 and September 30, 2018 are required, Kronos will recognize such adjustment in the reporting period within the SAB 118 measurement period in which such adjustment is determined.

Under U.S. GAAP, as it relates to the new GILTI tax rules, Kronos is allowed to make an accounting policy choice of either (1) treating taxes due on future U.S. inclusions in taxable income related to GILTI as a current-period expense when incurred (the "period cost method") or (2) factoring such amounts into the measurement of Kronos' deferred taxes (the "deferred method"). Kronos' selection of an accounting policy related to the GILTI tax provisions will depend, in part, on analyzing its global income to determine whether it expects to have future U.S. inclusions in taxable income related to GILTI and, if so, what the impact is expected to be. While Kronos' future global operations depend on a number of different factors, Kronos do expect to have future U.S. inclusions in taxable income related to GILTI. As such, Kronos performed an analysis of GILTI's impact on its provision and determined the impact is not material. Because the impact is not material to its tax provision, Kronos has not recorded any adjustments related to potential GILTI tax in its financial statements in the first nine months of 2018. Further, Kronos has not made a policy decision regarding whether to record deferred taxes on GILTI or record GILTI tax as a current-period expense when incurred. Kronos will complete its policy election for this item within the prescribed measurement period ending December 22, 2018, pursuant to the guidance under SAB 118 and if Kronos determines such policy election impacts its provision, Kronos will recognize an adjustment in the reporting period within the SAB 118 measurement period in which such adjustment is determined. Similarly, Kronos has evaluated the tax impact of BEAT on its tax provision in the first nine months of 2018 and determined that the tax law has no material impact on its tax provision as Kronos has historically not entered into international payments between related parties that are unrelated to cost of goods sold.

#### Effects of Currency Exchange Rates

Kronos has substantial operations and assets located outside the United States (primarily in Germany, Belgium, Norway and Canada). The majority of Kronos' sales from non-U.S. operations are denominated in currencies other than the U.S. dollar, principally the euro, other major European currencies and the Canadian dollar. A portion of Kronos' sales generated from its non-U.S. operations is denominated in the U.S. dollar (and consequently its non-U.S. operations will generally hold U.S. dollars from time to time). Certain raw materials used in all Kronos' production facilities, primarily titanium-containing feedstocks, are purchased in U.S. dollars, while labor and other production and administrative costs are incurred primarily in local currencies. Consequently, the translated U.S. dollar value of Kronos' non-U.S. sales and operating results are subject to currency exchange rate fluctuations which may favorably or unfavorably impact reported earnings and may affect the comparability of period-to-period operating results. In addition to the impact of the translation of sales and expenses over time, Kronos' non-U.S. operations also generate currency transaction gains and losses which primarily relate to (i) the difference between the currency exchange rates in effect when non-local currency sales or operating costs (primarily U.S. dollar denominated) are initially accrued and when such amounts are settled with the non-local currency, (ii) changes in currency exchange rates during time periods when Kronos' non-U.S. operations are holding non-local currency (primarily U.S. dollars), and (iii) relative changes in the aggregate fair value of currency forward contracts held from time to time. As discussed in Note 14 to Kronos' Condensed Consolidated Financial Statements, Kronos periodically use currency forward contracts to manage a portion of Kronos' currency exchange risk, and relative changes in the aggregate fair value of any currency forward



contracts it holds from time to time serves in part to mitigate the currency transaction gains or losses its would otherwise recognize from the first two items described above.

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Overall, Kronos estimates that fluctuations in currency exchange rates had the following effects on the reported amounts of its sales and income from operations for the periods indicated.

Impact of changes in currency exchange rates

three months ended September 30, 2018 vs September 30, 2017

	Transaction gains/(losses)		Change	rate changes	Total currency
	recognized	gains –			
	2017	2018	Change	rate changes	2018 vs 2017
	(In millions)				
<b>Impact on:</b>					
Net sales	\$-	\$-	\$ -	\$ -	\$ -
Income from operations	(4)	(1)	3	4	7

Changes in currency exchange rates (primarily the euro) had a nominal effect on Kronos' net sales as compared to the third quarter of 2017.

The \$7 million increase in income from operations was comprised of the following:

- Approximately \$3 million from net currency transaction gains primarily caused by relative changes in currency exchange rates at each applicable balance sheet date between the U.S. dollar and the euro, Canadian dollar and the Norwegian krone, which causes increases or decreases, as applicable, in U.S. dollar-denominated receivables and payables and U.S. dollar currency held by Kronos' non-U.S. operations, and
- Approximately \$4 million from net currency translation gains primarily caused by the strengthening of the U.S. dollar relative to the Canadian dollar, as its local currency-denominated operating costs were translated into less U.S. dollars in 2018 as compared to 2017 and such translation, as it related to the U.S. dollar relative to the euro, had a nominal effect on income from operations in 2018 as compared to 2017.

Impact of changes in currency exchange rates

nine months ended September 30, 2018 vs September 30 2017

	Transaction gains/(losses)		Change	rate changes	Total currency
	recognized	gains –			
	2017	2018	Change	rate changes	2018 vs 2017
	(In millions)				
<b>Impact on:</b>					
Net sales	\$-	\$ -	\$ -	\$ 53	\$ 53
Income from operations	(8)	4	12	14	26

The \$53 million increase in net sales (translation gain) was caused primarily by a weakening of the U.S. dollar relative to the euro, as Kronos' euro-denominated sales were translated into more U.S. dollars in 2018 as compared to 2017. The weakening of the U.S. dollar relative to the Canadian dollar and the Norwegian krone in 2018 did not have a significant effect on the reported amount of Kronos' net sales, as a substantial portion of the sales generated by Kronos' Canadian and Norwegian operations are denominated in the U.S. dollar.



The \$26 million increase in income from operations was comprised of the following:

- Approximately \$12 million from net currency transaction gains primarily caused by relative changes in currency exchange rates at each applicable balance sheet date between the U.S. dollar and the euro, Canadian dollar and the Norwegian krone, which causes increases or decreases, as applicable, in U.S. dollar-denominated receivables and payables and U.S. dollar currency held by Kronos' non-U.S. operations, and

- Approximately \$14 million from net currency translation gains primarily caused by a weakening of the U.S. dollar relative to the euro as the positive effects of the weaker U.S. dollar on euro-denominated sales more than offset the unfavorable effects of euro-denominated operating costs being translated into more U.S. dollars in 2018 as compared to 2017, partially offset by the weakening of the U.S. dollar relative to the Canadian dollar, as its local currency-denominated operating costs were translated into more U.S. dollars in 2018 as compared to 2017.

#### Outlook

Kronos expects its production volumes in 2018 to be lower as compared to the record 2017 production volumes. Assuming current global economic conditions continue and based on anticipated production levels, Kronos expects its 2018 sales volumes to be lower as compared to record 2017 sales volumes. As expected, customer inventory level changes Kronos experienced in the second quarter of 2018 continued into the third quarter. However, Kronos believes customer inventory level changes were short term and worldwide demand remains solid. Kronos will continue to monitor current and anticipated near-term customer demand levels and align its production and inventories accordingly.

The cost of third-party feedstock ore Kronos purchased in the first nine months of 2018 was higher as compared to the fourth quarter of 2017, and such higher cost feedstock ore was reflected in Kronos' results of operations beginning in the second quarter of 2018. Kronos expects its cost of sales per metric ton of TiO<sub>2</sub> sold in 2018 will be moderately higher than its per-metric ton cost in 2017 primarily due to higher third-party feedstock ore costs along with the unfavorable effects of lower production volumes.

Kronos started 2018 with average selling prices 27% higher than the beginning of 2017, and average selling prices increased by an additional 3% in the first six months of 2018 (most of which occurred in the first quarter). Average selling prices declined by 2% during the third quarter of 2018. Industry data indicates that overall TiO<sub>2</sub> inventory held by producers stood at adequate-to-low levels in the third quarter of 2018. Kronos expects changes in customer inventory levels to continue to decrease through the fourth quarter of 2018 which could lead to some selling price decreases during the fourth quarter of 2018.

Overall, Kronos expects its sales in 2018 will be comparable to 2017, as the favorable impact of expected higher average selling prices in 2018 would be offset by the unfavorable impact of expected lower sales volumes. In addition, Kronos expects its income from operations in 2018 will be comparable to 2017, as the favorable impact of expected higher average selling prices in 2018 would be offset by the unfavorable impact of expected lower sales and production volumes and higher raw material and other production costs (principally feedstock ore). However, Kronos expects its net income in 2018 will be lower as compared to 2017 due to the favorable impact of the aggregate net income tax benefit of \$136.5 million Kronos recognized in 2017.

Due to the constraints of high capital costs and extended lead time associated with adding significant new TiO<sub>2</sub> production capacity, especially for premium grades of TiO<sub>2</sub> products produced from the chloride process, Kronos believes increased and sustained profit margins will be necessary to financially justify major expansions of western producers' TiO<sub>2</sub> production capacity required to meet expected future growth in demand. Any such major expansion of TiO<sub>2</sub> production capacity, if announced, would take a number of years before such production would become available to meet future growth in demand. Certain Chinese producers have recently announced expansion plans, but the extent to which such expansion plans will be implemented, or if implemented the resulting additional capacity and

the timing thereof is uncertain.

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Kronos' expectations for its future operating results are based upon a number of factors beyond its control, including worldwide growth of gross domestic product, competition in the marketplace, continued operation of competitors, unexpected or earlier-than-expected capacity additions or reductions and technological advances. If actual developments differ from Kronos' expectations, its results of operations could be unfavorably affected.

## Liquidity and Capital Resources

### Consolidated cash flows

#### Operating activities

Trends in cash flows from operating activities, excluding the impact of deferred taxes and relative changes in assets and liabilities, are generally similar to trends in our income from operations.

Net cash provided by operating activities was \$22.3 million in the first nine months of 2018 compared to \$15.2 million in the first nine months of 2017. The \$7.1 million net increase in cash provided by operating activities includes the net effects of:

- higher income from operations from CompX in 2018 of \$2.4 million;
- lower net cash used for relative changes in receivables, inventories, payables and accrued liabilities in 2018 of \$2.7 million;
- lower cash required for income taxes of \$4.8 million in 2018 primarily as a result of the timing of tax payments;
- higher interest and dividend income in 2018 of \$1.1 million; and
- higher dividends received from Kronos in 2018 of \$2.1 million.

We do not have complete access to CompX's cash flows in part because we do not own 100% of CompX. A detail of our consolidated cash flows from operating activities is presented in the table below. Intercompany dividends have been eliminated. The reference to NL Parent in the table below is a reference to NL Industries, Inc., as the parent company of CompX and our wholly-owned subsidiaries.

	Nine months ended	
	September 30, 2017	2018
	(In millions)	
Net cash provided by operating activities:		
CompX	\$8.9	\$12.8
NL Parent and wholly-owned subsidiaries	7.9	11.1
Eliminations	(1.6)	(1.6)
Total	\$15.2	\$22.3

Changes in working capital can have a significant effect on cash flows from operating activities. Our September 30, 2018 days sales outstanding was consistent with recent trends and in line with our expectations. As expected, our total average number of days in inventory decreased from December 31, 2017 to September 30, 2018 primarily as a result of the seasonal increase in sales during the third quarter 2018 as compared to the fourth quarter of 2017. The variability in days in inventory among our segments primarily relates to the differences in the complexity of the production processes and therefore the length of time it takes to produce and sell end-products. For comparative

purposes, we have provided December 31, 2016 and September 30, 2017 numbers below.

	December 31, 2016	September 30, 2017	December 31, 2017	September 30, 2018
Days sales outstanding	36 days	40 days	38 days	40 days
Days in inventory	79 days	74 days	79 days	76 days

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### Investing activities

Our capital expenditures were \$2.0 million in the first nine months of 2018 compared to \$2.2 million in the first nine months of 2017. During the first nine months of 2018, Valhi repaid a net \$5.2 million under the promissory note (\$39.0 million of gross borrowings and \$44.2 million of gross repayments). During the first nine months of 2017, Valhi borrowed a net \$9.3 million under the promissory note (\$49.7 million of gross borrowings and \$40.4 million of gross repayments).

### Financing activities

Cash flows from financing activities in the first nine months of each of 2017 and 2018 consist of CompX dividends paid to its stockholders other than us.

### Outstanding debt obligations

At September 30, 2018, NLKW had outstanding debt obligations of \$.5 million under its secured revolving credit facility with Valhi, and CompX did not have any outstanding debt obligations. We are in compliance with all of the covenants contained in our secured revolving credit facility with Valhi at September 30, 2018. See Note 8 to our Condensed Consolidated Financial Statements.

Kronos' North American and European revolvers and its senior secured notes contain a number of covenants and restrictions which, among other things, restrict its ability to incur additional debt, incur liens, pay dividends or make other restricted payments, or merge or consolidate with, or sell or transfer substantially all of our assets to, another entity, and contains other provisions and restrictive covenants customary in lending transactions of this type. Certain of Kronos' credit agreements contain provisions which could result in the acceleration of indebtedness prior to their stated maturity for reasons other than defaults for failure to comply with typical financial or payment covenants. For example, certain credit agreements allow the lender to accelerate the maturity of the indebtedness upon a change of control (as defined in the agreement) of the borrower. In addition, certain credit agreements could result in the acceleration of all or a portion of the indebtedness following a sale of assets outside the ordinary course of business. Kronos' European revolving credit facility also requires the maintenance of certain financial ratios, and one of such requirements is based on the ratio of net debt to the last twelve months EBITDA of the borrowers. Kronos is in compliance with all of its debt covenants at September 30, 2018. Kronos believes that it will be able to continue to comply with the financial covenants contained in its credit facilities through their maturity.

### Future cash requirements

### Liquidity

Our primary source of liquidity on an ongoing basis is our cash flow from operating activities and credit facilities with affiliates as further discussed below. We generally use these amounts to fund capital expenditures (substantially all of which relate to CompX), pay ongoing environmental remediation and litigation costs and provide for the payment of dividends (if declared).

At September 30, 2018, we had aggregate cash, cash equivalents and restricted cash of \$128.4 million, substantially all of which was held in the U.S. A detail by entity is presented in the table below.



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	Amount (In millions)
CompX	\$ 43.8
NL Parent and wholly-owned subsidiaries	84.6
Total	\$ 128.4

In addition, at September 30, 2018 we owned 14.4 million shares of Valhi common stock with an aggregate market value of \$32.8 million. See Note 4 to our Condensed Consolidated Financial Statements. We also owned 35.2 million shares of Kronos common stock at September 30, 2018 with an aggregate market value of \$572.3 million. See Note 5 to our Condensed Consolidated Financial Statements.

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We routinely compare our liquidity requirements and alternative uses of capital against the estimated future cash flows we expect to receive from our subsidiaries and affiliates. As a result of this process, we have in the past and may in the future seek to raise additional capital, incur debt, repurchase indebtedness in the market or otherwise, modify our dividend policies, consider the sale of our interests in our subsidiaries, affiliates, business, marketable securities or other assets, or take a combination of these and other steps, to increase liquidity, reduce indebtedness and fund future activities. Such activities have in the past and may in the future involve related companies.

We periodically evaluate acquisitions of interests in or combinations with companies (including related companies) perceived by management to be undervalued in the marketplace. These companies may or may not be engaged in businesses related to our current businesses. We intend to consider such acquisition activities in the future and, in connection with this activity, may consider issuing additional equity securities and increasing indebtedness. From time to time, we also evaluate the restructuring of ownership interests among our respective subsidiaries and related companies.

Based upon our expectations of our operating performance, and the anticipated demands on our cash resources we expect to have sufficient liquidity to meet our short-term obligations (defined as the twelve-month period ending September 30, 2019) including any amounts CompX might loan from time to time under the terms of its new revolving loan to Valhi (which loans would be solely at CompX's discretion). If actual developments differ materially from our expectations, our liquidity could be adversely affected. In this regard, Valhi has agreed to loan us up to \$50 million on a revolving basis. At September 30, 2018, we had \$.5 million in outstanding borrowings under this facility, and we had \$49.5 million available for future borrowing. See Note 8 to our Condensed Consolidated Financial Statements.

#### Capital Expenditures

Firm purchase commitments for capital projects in process at September 30, 2018 totaled \$0.6 million. CompX's 2018 capital investments are limited to those expenditures required to meet our expected customer demand and those required to properly maintain our facilities and technology infrastructure.

#### Dividends

Because our operations are conducted primarily through subsidiaries and affiliates, our long-term ability to meet parent company-level corporate obligations is largely dependent on the receipt of dividends or other distributions from our subsidiaries and affiliates. A detail of annual dividends we expect to receive from our subsidiaries and affiliates in 2018, based on the number of shares of common stock of these affiliates we own as of September 30, 2018 and their current regular quarterly dividend rate, is presented in the table below.

	Shares held (In millions)	Current Quarterly Dividend Rate	Annual Expected Dividend (In millions)
Kronos	35.2	\$ .17	\$ 23.9
CompX	10.8	.05	2.2
Valhi	14.4	.02	1.1
Total expected annual dividends			\$ 27.2

Investments in our subsidiaries and affiliates and other acquisitions

We have in the past and may in the future, purchase the securities of our subsidiaries and affiliates or third-parties in market or privately-negotiated transactions. We base our purchase decisions on a variety of factors, including an analysis of the optimal use of our capital, taking into account the market value of the securities and the relative value of expected returns on alternative investments. In connection with these activities, we may consider issuing additional equity securities or increasing our indebtedness. We may also evaluate the restructuring of ownership interests of our businesses among our subsidiaries and related companies.

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#### Off-balance sheet financing arrangements

Other than operating lease commitments discussed in our 2017 Annual Report, we are not party to any material off-balance sheet financing arrangements.

#### Commitments and contingencies

There have been no material changes in our contractual obligations since we filed our 2017 Annual Report and we refer you to that report for a complete description of these commitments.

We are subject to certain commitments and contingencies, as more fully described in our 2017 Annual Report, or in Note 14 to our Condensed Consolidated Financial Statements or in Part II, Item 1 of this report, including certain legal proceedings. In addition to such legal proceedings, various legislation and administrative regulations have, from time to time, been proposed that seek to (i) impose various obligations on present and former manufacturers of lead pigment and lead-based paint (including us) with respect to asserted health concerns associated with the use of such products and (ii) effectively overturn court decisions in which we and other pigment manufacturers have been successful. Examples of such proposed legislation include bills which would permit civil liability for damages on the basis of market share, rather than requiring plaintiffs to prove that the defendant's product caused the alleged damage and bills which would revive actions barred by the statute of limitations. While no legislation or regulations have been enacted to date that are expected to have a material adverse effect on our consolidated financial position, results of operations or liquidity, enactment of such legislation could have such an effect.

#### Recent accounting pronouncements

See Note 16 to our Condensed Consolidated Financial Statements.

#### Critical accounting policies and estimates

For a discussion of our critical accounting policies, refer to Part I, — “Management’s Discussion and Analysis of Financial Condition and Results of Operations” in our 2017 Annual Report. There have been no changes in our critical accounting policies during the first nine months of 2018.

#### ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURE ABOUT MARKET RISK

We are exposed to market risk, including currency exchange rates, interest rates and security prices. There have been no material changes in these market risks since we filed our 2017 Annual Report, and we refer you to Part I, Item 7A. — “Quantitative and Qualitative Disclosure about Market Risk” in our 2017 Annual Report. See also Note 14 to our Condensed Consolidated Financial Statements.

#### ITEM 4. CONTROLS AND PROCEDURES

Evaluation of disclosure controls and procedures – We maintain disclosure controls and procedures which, as defined in Exchange Act Rule 13a-15(e), means controls and other procedures that are designed to ensure that information required to be disclosed in the reports that we file or submit to the SEC under the Securities Exchange Act of 1934, as amended (the Act), is recorded, processed, summarized and reported, within the time periods specified in the SEC’s rules and forms. Disclosure controls and procedures include, without limitation, controls and procedures designed to ensure that information we are required to disclose in the reports we file or submit to the SEC under the Act is accumulated and communicated to our management, including our principal executive officer and our principal financial officer, or persons performing similar functions, as appropriate to allow timely decisions to be made regarding required disclosure. Each of Robert D. Graham, our Vice Chairman of the Board and Chief Executive Officer and Gregory M. Swalwell, our Executive Vice President and Chief Financial Officer, have evaluated the

design and effectiveness of our disclosure controls and procedures as of September 30, 2018. Based upon their evaluation, these executive officers have concluded that our disclosure controls and procedures are effective as of the date of this evaluation.

Internal control over financial reporting – Our management is responsible for establishing and maintaining adequate internal control over financial reporting which, as defined by Exchange Act Rule 13a-15(f) means a

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process designed by, or under the supervision of, our principal executive and principal financial officers, or persons performing similar functions, and effected by the board of directors, management and other personnel, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles, and includes those policies and procedures that:

- Pertain to the maintenance of records that in reasonable detail accurately and fairly reflect transactions and dispositions of our assets,

- Provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with GAAP, and that receipts and expenditures are made only in accordance with authorizations of our management and directors, and

- Provide reasonable assurance regarding prevention or timely detection of an unauthorized acquisition, use or disposition of assets that could have a material effect on our Condensed Consolidated Financial Statements.

Other – As permitted by the SEC, our assessment of internal control over financial reporting excludes (i) internal control over financial reporting of equity method investees and (ii) internal control over the preparation of any financial statement schedules which would be required by Article 12 of Regulation S-X. However, our assessment of internal control over financial reporting with respect to equity method investees did include controls over the recording of amounts related to our investment that are recorded in the consolidated financial statements, including controls over the selection of accounting methods for our investments, the recognition of equity method earnings and losses and the determination, valuation and recording of our investment account balances.

Changes in internal control over financial reporting – There have been no changes to our internal control over financial reporting during the quarter ended September 30, 2018 that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

## PART II. OTHER INFORMATION

### Item 1. Legal Proceedings

In addition to the matters discussed below, refer to Note 14 to our Condensed Consolidated Financial Statements and our 2017 Annual Report.

**Big River Mine Tailings Superfund Site.** In October 2018, NL and the United States entered into a consent decree for Operable Unit 1 (OU1). The consent decree was filed with the court and released for public comment in October 2018. After it has responded to any comments, the United States will file a motion seeking judicial approval of the settlement. If approved, the consent decree will resolve NL's liability for OU1.

**Refined Metals Corporation v. NL Industries, Inc.** (United States District Court for the Southern District of Indiana, Case 1:17-cv-2565). In September 2018, the court dismissed the case, holding that all federal claims brought against NL were barred by the statute of limitations and finding that the court lacked jurisdiction to consider the state law claims. In October 2018, Refined Metals filed an appeal with the federal court of appeals. NL will continue to deny liability and will vigorously defend against all claims in the court of appeals.

In November 2018, NL was served with two complaints filed by county governments in Pennsylvania. Each county alleges that NL and several other defendants created a public nuisance by selling and promoting lead-containing paints and pigments in the counties. The plaintiffs seek abatement and declaratory relief. We believe these lawsuits are inconsistent with Pennsylvania law and without merit, and we intend to defend ourselves vigorously.

### Item 1A. Risk Factors

For a discussion of the risk factors related to our businesses, refer to Part I, Item 1A., "Risk Factors," in our 2017 Annual Report.

### Item 6. Exhibits

31.1 [Certification](#)

31.2 [Certification](#)

32.1 [Certification](#)

101.INS XBRL Instance Document

101.SCHXBRL Taxonomy Extension Schema

101.CALXBRL Taxonomy Extension Calculation Linkbase

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101.DEF XBRL Taxonomy Extension Definition Linkbase

101.LABXBRL Taxonomy Extension Label Linkbase

101.PRE XBRL Taxonomy Extension Presentation Linkbase



SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the Registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

NL INDUSTRIES, INC.  
(Registrant)

Date: November 7, 2018 /s/ Gregory M. Swalwell  
Gregory M. Swalwell  
(Executive Vice President and  
Chief Financial Officer,  
Principal Financial Officer)

Date: November 7, 2018 /s/ Amy Allbach Samford  
Amy Allbach Samford  
(Vice President and Controller,  
Principal Accounting Officer)